

Registered Number: OC313878

Nationwide Covered Bonds LLP

Annual Report and Financial Statements for
the year ended 4 April 2014

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Nationwide Covered Bonds LLP

Annual Report and Financial Statements for
the year ended 4 April 2014

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NATIONWIDE COVERED BONDS LLP

Members and partnership information

Members

Nationwide Building Society
Moulton Capital Finance Limited

Management Board

Nationwide Building Society
Moulton Capital Finance Limited

Independent auditors

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
1 Embankment Place
London
WC2N 6RH

Registered office

Nationwide House
Pipers Way
Swindon
SN38 1NW

Registered number

OC313878
Registered in England and Wales

NATIONWIDE COVERED BONDS LLP

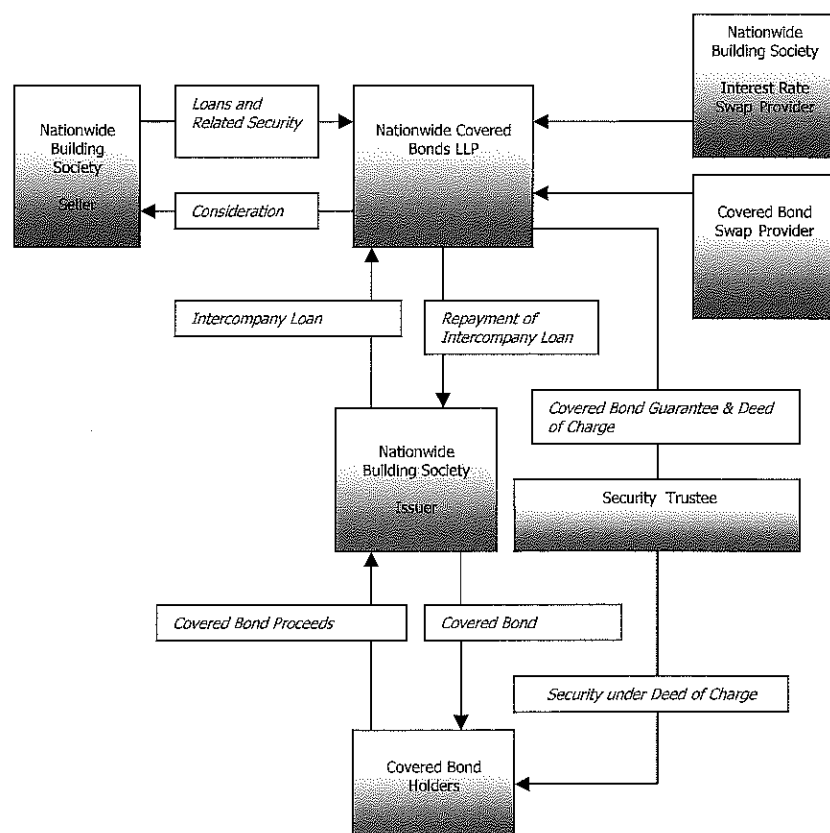
Members' report for the year ended 4 April 2014

On behalf of the members of Nationwide Covered Bonds LLP (the "LLP"), the Management Board have pleasure in presenting the member's report and the audited financial statements for the LLP for the year ended 4 April 2014. As set out in the statement of accounting policies, the annual report and financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. All financial information given in the members' report is taken solely from the statutory results prepared on the above basis. The members consider the financial statements to be fair, balanced and understandable.

Business objectives and principal activities

The LLP is a wholly owned subsidiary of Nationwide Building Society ("the Society" or "NBS") and is incorporated with limited liability. The LLP is registered, domiciled and operates solely in England and Wales. The LLP was incorporated on 25 June 2005. The LLP is a special purpose vehicle whose purpose is to guarantee the Covered Bonds issued by the Society by acquiring mortgage loans and their related security from the Society (the "Originator") pursuant to the terms of the Mortgage Sale Agreement entered into on 30 November 2005, when trading commenced. No change in principal activity is envisaged.

The LLP enters into interest rate swap agreements with the Society under which it swaps the interest cash flows of the mortgage loans for 3m Libor plus a spread. The LLP funds the purchase of the mortgage loans by loans from the Society, replicating the issue of Covered Bonds by the Society in currency. Currencies currently in use are Sterling (GBP) (the LLP's functional currency), Euros (EUR), Norwegian Krona (NOK) and Swedish Krona (SEK). The LLP enters into currency swap agreements under which it pays interest cash flows in GBP and receives EUR, NOK and SEK cash flows which are used to pay the interest on the loans to Nationwide. The Society is one of the designated members of the LLP, the Covered Bond originator and the LLP's parent undertaking. The Covered Bond structure is set out in diagrammatic form below.



NATIONWIDE COVERED BONDS LLP

Members' report for the year ended 4 April 2014 (continued)

Main accounting assumptions

The Society is considered to have retained substantially all the exposure to risks and rewards of ownership of the transferred mortgages. As a result, the acquisition of mortgage loans by the LLP is considered to fail the derecognition criteria of IAS 39, so that the assets sold are retained on the balance sheet of the Society.

As described further in note 1 to the financial statements, the LLP therefore treats the transaction as a loan from the Society (the "deemed loan"), secured on a collateral pool of assets, rather than the financial assets that it has legally purchased. The difference between the 'deemed loan' and the balance of mortgage loans is recognised as a capital contribution in the LLP. However, as the mortgage loans fail the derecognition criteria of IAS 39, the capital contribution and the associated element of the deemed loan and interest receivable (referred to as 'over-collateralisation') on it is not recognised in the LLP. The deemed loan is shown net of the over collateralisation adjustment on the face of the balance sheet. The gross amounts are disclosed in the notes.

For accounting purposes the interest rate swap between the LLP and the Society (swapping the interest cash flows of the mortgage loans for 3 month Libor + spread) is not separately recognised as a derivative. The effective interest rate accrued by the LLP on the deemed loan due to the LLP from the Society reflects the rate payable under the swap. The swap is consequentially not separately fair valued.

Creditor payment policy

The Creditor payment policy is operated at Group level, reflecting the use of the central Group accounts payable function. The Group's policy is to agree the terms of payment with suppliers at the start of trading, ensure suppliers are aware of the terms of payment and pay in accordance with its contractual and other legal obligations. The Group's policy is to settle the supplier's invoice for the complete provision of goods and services (unless there is an express provision for stage payments), when in full conformity with the terms and conditions of the purchase, within the agreed payment terms.

Employees

The LLP does not have any employees (2013: none).

Designated members

The designated members during the year were:

Nationwide Building Society
Moulton Capital Finance Limited

The designated members have remained unchanged since the date of incorporation of the LLP on 25 June 2005.

Going concern

The LLP's ultimate parent undertaking is Nationwide Building Society. The Society's Board of directors has confirmed that it will continue to fund the LLP's activities for the foreseeable future. The foreseeable future is considered for this purpose to be a period at least 12 months forward from the date of approval of the financial statements. Taking this into account, the members have a reasonable expectation that the LLP has adequate resources to continue in business for the foreseeable future and therefore continue to adopt the going concern basis in preparing the financial statements.

NATIONWIDE COVERED BONDS LLP

Members' report for the year ended 4 April 2014 (continued)

Environment

The Group recognises the importance of its environmental responsibilities, monitors its impact on the environment, and designs and implements policies to reduce any damage that might be caused by the Group's activities.

The Group has a comprehensive programme of activity on environmental issues. It runs an active carbon-saving programme and has taken action on issues such as transport, lighting, heating and recycling.

Domicile

The LLP is registered and domiciled in the United Kingdom the registered office is Nationwide House, Pipers Way, Swindon, Wiltshire, SN38 1NW.

Independent auditors

The auditors, PricewaterhouseCoopers LLP, have expressed their willingness to continue in office.

Members and members' interests

The members of the LLP who were in office during the year and up to the date of signing the financial statements are shown on page 2.

At no time during the year have the members, or their families, had any beneficial interest in the shares of the LLP. None of the members had a material interest in any contract significant to the LLP's business.

NATIONWIDE COVERED BONDS LLP

Members' report for the year ended 4 April 2014 (continued)

Statement of members' responsibilities

The members are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the members to prepare financial statements for each financial year. Under that law the members have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the members must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the LLP and of the profit or loss of the LLP for that period. In preparing these financial statements, the members are required to:

- select suitable accounting policies and then apply them consistently
- make judgements and accounting estimates that are reasonable and prudent
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the LLP will continue in business.

The members are responsible for keeping adequate accounting records that are sufficient to show and explain the LLP's transactions and disclose with reasonable accuracy at any time the financial position of the LLP and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the LLP and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Statement of disclosure of information to auditors

In accordance with Section 418 of the Companies Act 2006, for each member in office at the date the members' report is approved:

- (a) so far as the member is aware, there is no relevant audit information of which the LLP's auditors are unaware, and
- (b) each member has taken all the steps that he/she ought to have taken as a member in order to make himself aware of any relevant audit information and to establish that the LLP's auditors are aware of that information.

By order of the management board



For and on behalf of the LLP

Date: 2 July 2014

NATIONWIDE COVERED BONDS LLP

Strategic report for the year ended 4 April 2014

All financial information given in this Strategic report is taken solely from the statutory results prepared in accordance with IFRS.

Business review

There were no issuances during the year, however the following notes matured or were repaid during the year.

| <u>Note</u> | <u>Amount</u> | <u>Date</u> |
|-------------|----------------|---------------|
| 2006-02 | €2,000 million | December 2013 |
| 2011-08 | £30 million | March 2014 |

The balance sheet on page 12 of the financial statements shows the LLP's financial position at the year end. Details of amounts owed to the Group undertakings are shown in note 13.

Future developments

The LLP will continue to guarantee Covered Bonds issued by the Society by acquiring mortgage loans and their related security from the Society.

Strategic goals

Strategic goals are set at Group level. The KPIs in relation to last year's strategic goals are set out below:

- Be the clear number 1 for customer satisfaction
- Protect and grow our market shares in: mortgages, savings and current accounts
- Grow and deepen our relationships with our members
- Engage and enable our people to deliver an exceptional member service
- Run a low risk business model
- Deliver optimal levels of profitability
- Ensure capital strength with market leading CET 1 ratio and leverage ratio above PRA requirements
- Deliver operational efficiency and prudent cost management, targeting a cost income ratio of 45-50%

Further information on the Group's performance against these, and also the strategic goals for the next five years can be found in the Overview section of the Group Annual Report and Accounts.

The programme performance is monitored monthly for financial and non-financial indicators including covenants and tests for managing risk which are published within the monthly investor report (available via Nationwide Building Society website), for example: the Asset Coverage Test (ACT); Interest Coverage Test; Servicer Trigger (which monitors the servicer's ratings to required levels); and Yield Shortfall Test (which checks that the portfolio yield does not fall below LIBOR plus 0.15%).

The level of over-collateralisation is central to the contractual mechanics and to credit ratings agency oversight. The level of over-collateralisation can be estimated using the ACT which is carried out each month and is deemed to establish the level of over-collateralisation for the LLP.

To date, all loan and note repayments have been made in accordance with the scheduled repayment dates.

NATIONWIDE COVERED BONDS LLP

Strategic report for the year ended 4 April 2014 (continued)

Results and dividends

The loss for the year was £34,453,000 (2013: £62,985,000.) This is composed primarily of net interest expense of £11,876,000 (2013: income of £14,311,000) and losses from derivatives and hedge accounting of £21,505,000 (2013: £75,933,000.)

Profits on a cash flow basis are pre-determined under the Programme Documentation. The cash flow profits before tax, which exclude gains/(losses) from derivatives and hedge accounting and foreign exchange gains/(losses), are fixed to a maximum of £1 per annum.

At 4 April 2014, the amount of beneficial interests in the mortgage loan portfolio was £20.2 billion (2013: £21.8 billion) and the amount of the deemed loan was £13.1 billion (2013: £14.9 billion). The difference of £7.1 billion (2013: £6.9 billion) represents the amount of over collateralisation in the structure. No dividends were paid during the year (2013 £ nil).

Risk management and control

Overall the outlook is encouraging, credit exposures are performing well. Market sentiment has become more positive, further increasing our confidence in the business. At a Group level this year we have also made steady improvements to our controls and our frameworks for managing risks.

Although the condition of the business has strengthened, risks remain. Current positive market conditions may reverse, driven either by UK or overseas events; or resurgent competition may put pressure on our operating margins.

It is also almost certain that regulators' and customers' expectations will increase, and their tolerance for failure will reduce. The pace of change and the standards of consistency now required present conduct and operational risks.

In common with other retail financial services organisations, our business model results in a number of inherent risks which are continuously monitored and managed. These are categorised as follows:

- Financial risk
- Operational risk
- Customer and compliance risk
- Strategic risk, and
- Model risk

The risk management objectives and policies which correspond to these risks and uncertainties are described in note 14.

By order of the management board



For and on behalf of the LLP
Date: 2 July 2014

Report on the financial statements

Our opinion

In our opinion the financial statements, defined below:

- give a true and fair view of the state of the limited liability partnership's affairs as at 4 April 2014 and of its loss and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 as applied to limited liability partnerships by the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008.

This opinion is to be read in the context of what we say in the remainder of this report.

What we have audited

The financial statements, which are prepared by Covered Bonds LLP, comprise:

- the balance sheet as at 4 April 2014;
- the statement of comprehensive income for the year then ended;
- the cash flow statement for the year then ended;
- the statement of movements in members' interests for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union.

In applying the financial reporting framework, the members have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

What an audit of financial statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the limited liability partnership's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the designated members; and
- the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report and Financial Statements for the year ended 4 April 2014 (the "Annual Report") to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

NATIONWIDE COVERED BONDS LLP

Independent auditors' report to the members of Covered Bonds LLP (continued)

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 as applicable to limited liability partnerships we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

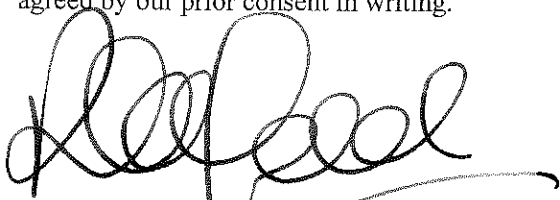
Responsibilities for the financial statements and the audit

Our responsibilities and those of the members

As explained more fully in the Members' Statement of Responsibilities, the members are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinion, has been prepared for and only for the members of the partnership as a body in accordance with the Companies Act 2006 as applied to limited liability partnerships by the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.



Richard Oldfield (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

3 July 2014

NATIONWIDE COVERED BONDS LLP**Statement of comprehensive income for the year ended 4 April 2014**

| | Note | 2014 £'000 | 2013 £'000 |
|--|------|-----------------|-----------------|
| Interest receivable and similar income | 3 | 191,979 | 301,626 |
| Interest payable and similar charges | 4 | (203,855) | (287,315) |
| Net interest (expense)/income | | (11,876) | 14,311 |
| (Losses) from derivatives and hedge accounting | 5 | (21,505) | (75,933) |
| Administrative expenses | 6 | (1,072) | (1,363) |
| (Loss) and total comprehensive (expense) for the year | | (34,453) | (62,985) |

The notes on pages 15 to 34 form part of these financial statements.

Balance sheet as at 4 April 2014

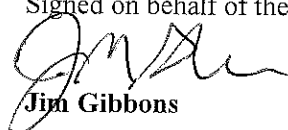
| | Note | 2014 £'000 | 2013 £'000 |
|---|------|-------------------|-------------------|
| Assets | | | |
| Cash and cash equivalents | 7 | 1,799,328 | 1,952,041 |
| Loans and other debts due from members | 8 | 13,090,718 | 14,857,842 |
| Derivative financial instruments | 9 | 1,539,010 | 2,347,832 |
| Total assets | | 16,429,056 | 19,157,715 |
| Liabilities | | | |
| Loans from LLP members | 10 | 14,923,775 | 17,179,897 |
| Other debts due to members | 11 | 348,243 | 534,383 |
| Derivative financial instruments | 9 | 202,435 | 102,392 |
| Accruals | | 48 | 31 |
| Other liabilities | 12 | 981,893 | 1,333,897 |
| Total liabilities | | 16,456,394 | 19,150,600 |
| Members' other interests | | | |
| General reserve | | (27,338) | 7,115 |
| Total members' other interests | | (27,338) | 7,115 |
| Total members' other interests and liabilities | | 16,429,056 | 19,157,715 |
| Total members' interests | | | |
| Members' interests in general reserves | | (27,338) | 7,115 |
| Loans from LLP members | | 14,923,775 | 17,179,897 |
| Other debts due to members | | 348,243 | 534,383 |
| Loans and other debts due from members | | (13,090,718) | (14,857,842) |
| Total members' interests | | 2,153,962 | 2,863,553 |

The notes on pages 15 to 34 form part of these financial statements.

The members acknowledge their responsibility for complying with the requirements of the Companies Act 2006 with respect to accounting records and for the preparation of financial statements.

The financial statements were approved by the members on 2 July 2014

Signed on behalf of the Members


Jim Gibbons

NATIONWIDE COVERED BONDS LLP

Statement of movements in members' interests for the year ended 4 April 2014

| | General reserve £'000 | Loans from/(to) members £'000 | Total £'000 |
|--|--------------------------------------|--|------------------------|
| General reserve at 5 April 2013 | 7,115 | - | 7,115 |
| Loss for the year | (34,453) | - | (34,453) |
| Balance carried forward at 4 April 2014 | (27,338) | - | (27,338) |
| Loans from members | - | 14,923,775 | 14,923,775 |
| Other debts due to members | - | 348,243 | 348,243 |
| Loans and other debts due from members | - | (13,090,718) | (13,090,718) |
| Members' interests as at 4 April 2014 | (27,338) | 2,181,300 | 2,153,962 |

| | General reserve £'000 | Loans from/(to) members £'000 | Total £'000 |
|--|--------------------------------------|--|------------------------|
| General reserve at 5 April 2012 | 70,100 | - | 70,100 |
| Loss for the year | (62,985) | - | (62,985) |
| Balance carried forward at 4 April 2013 | 7,115 | - | 7,115 |
| Loans from members | - | 17,179,897 | 17,179,897 |
| Other debts due to members | - | 534,383 | 534,383 |
| Loans and other debts due from members | - | (14,857,842) | (14,857,842) |
| Members' interests as at 4 April 2013 | 7,115 | 2,856,438 | 2,863,553 |

If the sale of the beneficial interest in the mortgage portfolio to the partnership had been recognised under IFRS as adopted by the European Union, the members' capital balance would have been £7.1 billion at 4 April 2014 (2013: £7.0 billion).

The notes on pages 15 to 34 form part of these financial statements.

NATIONWIDE COVERED BONDS LLP**Cash flow statement for the year ended 4 April 2014**

| | 2014 | 2013 |
|--|--------------------|--------------------|
| | £'000 | £'000 |
| (Loss) before tax | (34,453) | (62,985) |
| Adjustments for: | | |
| Other non-cash items | 99,755 | 62,985 |
| (Decrease)/increase in other creditors | (351,987) | 699,467 |
| (Decrease) in other debts due to members | (186,140) | (53,047) |
| Increase/(decrease) in interest receivable on derivative financial instruments | 8,245 | (40,427) |
| (Decrease) in interest payable on loans from members | (24,286) | (41,636) |
| Decrease in derivative financial instrument assets | 320,590 | - |
| Net cash flows generated by operating activities | (168,276) | 564,357 |
| Cash flows from investing activities: | | |
| Receipt of loans advanced to members | 1,718,153 | 3,692,839 |
| Net cashflow generated by investing activities | 1,718,153 | 3,692,839 |
| Cash flows from financing activities: | | |
| Repayment of loans from members | (1,702,590) | (3,691,841) |
| Net cash flows used in financial activities | (1,702,590) | (3,691,841) |
| Net change in cash and cash equivalents | (152,713) | 565,355 |
| Cash and cash equivalents at beginning of year | 1,952,041 | 1,386,686 |
| Cash and cash equivalents at end of year | 1,799,328 | 1,952,041 |

The notes on pages 15 to 34 form part of these financial statements.

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014

1 Accounting policies

Basis of preparation

The LLP financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU), and with those parts of the Companies Act 2006, as applied to limited liability partnerships and regulations made thereunder, applicable to partnerships reporting under IFRS.

The LLP's ultimate parent undertaking is Nationwide Building Society. The Society's Board of directors has confirmed that it will continue to fund the LLP's activities for the foreseeable future. The foreseeable future is considered for this purpose to be a period at least 12 months forward from the date of approval of the financial statements. Taking this into account, the members have a reasonable expectation that the LLP has adequate resources to continue in business for the foreseeable future and therefore continue to adopt the going concern basis in preparing the financial statements.

The principal accounting policies applied in the preparation of these financial statements are set out below.

The preparation of financial statements in conformity with general accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Further details on critical accounting estimates are given in note 2.

The financial information has been prepared under the historical cost convention as modified by revaluations of derivative financial instruments.

Changes in accounting policy

The following IFRS pronouncements, relevant to the LLP, were adopted with effect from 5 April 2013:

- IFRS 13 Fair Value Measurement: The standard has replaced guidance on fair value measurement in previous IFRS accounting publications with a single standard. The standard, which is required to be applied prospectively, provides guidance on the calculation of the fair value of financial and non-financial assets and liabilities and additionally requires enhanced disclosures. The new standard has not had a material impact for the LLP, and the new disclosure requirements have been adopted to the extent applicable to the LLP in Note 15. The disclosure requirements of IFRS 13 do not require comparative information to be provided for periods prior to initial application.
- Amendments to IFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities: The amendments require disclosure of the effect or potential effects of netting arrangements on an entity's financial position including financial instruments that are subject to an enforceable master netting arrangement or similar agreement. The amendments have been applied retrospectively with the additional disclosures provided in note 9.

Future accounting developments

The following pronouncements, relevant to the LLP, have been adopted by the European Union (EU) but were not effective at 4 April 2014 and have not therefore been applied in preparing these financial statements.

NATIONWIDE COVERED BONDS LLP**Notes to the financial statements for the year ended 4 April 2014 (continued)****1 Accounting policies (continued)**

| Pronouncement | Nature of change | Effective date |
|--|---|--|
| IFRSs 10 – 12 and amendments to IAS 27 and 28 | <p>A package of five new and revised standards addressing the accounting for consolidation, involvements in joint arrangements and disclosure of involvements with other entities.</p> <p>The new and revised standards are not expected to have an impact for the LLP.</p> | Accounting periods (AP) beginning on or after 1 January 2014 |
| IAS 32 Offsetting Financial Assets and Financial Liabilities | Clarifies existing offsetting criteria. The amendment is not expected to have an impact for the LLP. | AP beginning on or after 1 January 2014 |

The following pronouncement, relevant to the LLP, was neither adopted by the EU nor effective at 4 April 2014 and has not therefore been applied in preparing these financial statements.

| Pronouncement | Nature of change | Effective date |
|------------------------------|---|---|
| IFRS 9 Financial Instruments | <p>The new standard replaces IAS 39. Changes include classification and measurement of the LLP's financial assets and liabilities, the recognition of impairment, and hedge accounting.</p> <p>The revised classification and measurement approach will lead to the LLP's financial assets being re-classified as either amortised cost, fair value through other comprehensive income (OCI), or fair value through the income statement. Financial liabilities will in most cases be accounted for as at present. One exception is that if the LLP opts to fair value a financial liability, movement in fair value due to own credit risk would be directly recognised in OCI.</p> <p>The impairment of financial assets under IFRS9 will be based on expected credit losses rather than incurred credit losses as at present.</p> <p>Hedge accounting proposals will amend existing IAS39 approaches for micro-hedge accounting. Accounting for dynamic risk management (macro-hedge accounting) has been decoupled from IFRS9 and is now subject to separate consultation.</p> <p>A number of the proposals are not expected to be finalised until later in 2014. It is therefore not yet possible to estimate the financial effects of the new standard, although it is expected to have a significant impact for the LLP, the full extent of which is currently being considered.</p> | AP beginning on or after 1 January 2018 |

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

1 Accounting policies (continued)

Derecognition

Under IFRS, if a transferor retains substantially all the risks and rewards associated with the transferred assets, the transaction is accounted for as a financing transaction, notwithstanding that it is a sale transaction from a legal perspective. The members of the LLP have concluded that the Originator, has retained substantially all the exposure to risks and rewards of the pool of mortgage loans and as a consequence, the LLP does not recognise the mortgage loans on its balance sheet but rather a loan due from the Originator.

The basis swaps between the LLP and the Originator are not recognised separately as financial derivative instruments, as the amounts payable under the swaps reflect interest flows from the mortgage loans which are not recognised by the LLP for accounting purposes. Instead, the deemed loan to the Originator is recognised with an effective interest rate which reflects the amount receivable under the swap receiving leg.

Contributions and drawings

Under the terms of the transaction documents for the sale of the mortgage loans, the Nationwide Building Society is legally treated as having made a capital contribution to the LLP in an amount equal to the difference between the current balance of the loans sold at transfer date and the cash payment made by the LLP for the loans and relevant security on that transfer date.

If so requested by the Management Board, the members may from time to time make cash contributions to the LLP which will constitute cash capital contributions. The liquidation member, Moulton Capital Finance Limited, will not make any capital contributions to the LLP. No interest is paid on the members' capital balances.

As the sale of the beneficial interest in the mortgage portfolio does not pass the derecognition criteria as described in IAS 39, capital contributions in the financial statements only consist of cash capital contributions.

Capital distributions may only be made in accordance with the LLP Deed where sufficient principal receipts are available and higher priority payments have been made.

Under the priority of payments, payment pro rata and pari passu to the members of the sum of £3,000 in aggregate (or such other sum as may be agreed by members from time to time) is allocated and paid to each member in proportion to their respective capital contribution balances as at the relevant calculation date, subject to a minimum of £1 each, as their profit for their respective interests as members in the LLP.

Deferred consideration

Under the terms of the mortgage sale agreement, the Nationwide Building Society, as the Originator of the mortgage loans, retains the right to receive excess income (deferred consideration) arising on those loans, after certain higher priority payments have been met by the LLP. On application of IFRS, deferred consideration is treated as a reduction in the interest due from the Nationwide Building Society on the loan arising from the failure to derecognise the sale of the mortgages. Deferred consideration is presented within other debts due to members.

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

1 Accounting policies (continued)

Interest receivable and interest expense

Interest income and expense are recognised in the income statement on an effective interest rate (EIR) basis. The EIR 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.

In calculating the effective interest rate, the LLP estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees received and paid and costs borne that are an integral part of the effective interest rate and all other premiums or discounts above or below market rates.

Interest income on derivatives is included in interest receivable and similar income and interest expense and similar charges in the statement of comprehensive income.

Interest receivable is presented net of amounts payable for profits in excess of the £1 per annum limit set out in the programme documents. The associated amounts payable are presented net within loans and other debts due to members.

Fees and commissions

Direct fees and costs incremental to generating a financial instrument are deferred and spread as interest receivable or expense on an effective interest basis.

Other fees and commissions are recognised on the accruals basis as services are provided, or on the performance of a significant act.

Segmental reporting

The LLP has only one business segment and operates wholly in the UK. Accordingly no segmental analysis is presented in these financial statements.

Taxation including deferred tax

Taxation on all partnership profits is solely the liability of members. Consequently, neither taxation nor related deferred taxation in the LLP are accounted for in these financial statements.

Loans and other debts due from members

The entity classifies its loans and other debts due from members as loans and receivables which are held at amortised cost. As described above the sale of the beneficial interest in the mortgage portfolio, even though legally acquired from the Nationwide Building Society, does not pass the derecognition criteria as described in IAS 39 and therefore a deemed loan is shown in the balance sheet.

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

1 Accounting policies (continued)

Impairment of financial assets

At each balance sheet date the LLP assesses whether, as a result of one or more events occurring after initial recognition, there is objective evidence that a financial asset has become impaired. Evidence of impairment may include indications that the counterparty is experiencing significant financial difficulty, default or delinquency in interest or principal payments.

The carrying amount of the asset is reduced by the amount of any impairment loss. Any losses are recognised in the statement of comprehensive income.

Derivatives and hedge accounting

Derivatives are entered into to reduce exposure to fluctuations in interest rates and exchange rates and are not used for speculative purposes.

a) Derivative financial instruments

Other than as noted in (c) below, derivatives are carried at fair value with movements in fair value recorded in the income statements. Derivative financial instruments are principally valued by discounted cashflow models using yield curves that are based on observable market data or are based on valuations obtained from counterparties. For collateralised positions the LLP uses discount curves based on overnight indexed swap rates, as detailed in note 5, and for non-collateralised positions the LLP uses discount curves based on term Libor rates.

In the first instance fair values are calculated using mid prices. An adjustment is then made to derivative assets and liabilities to value them on a bid and offer basis respectively. The bid-offer adjustment is calculated on a portfolio basis and reflects the costs that would be incurred if substantially all residual net portfolio market risks were closed out using available hedging instruments or by disposing of or unwinding actual positions. The methodology for determining the bid-offer adjustments involves netting between long and short positions and the grouping of risk by type, in accordance with hedging strategy. Bid-offer spreads are derived from market sources such as broker data and are reviewed periodically.

In measuring fair value, separate credit valuation and debit valuation adjustments are made for counterparty or own credit risk to the extent not already included in the valuation.

All derivatives are classified as assets where their fair value is positive and liabilities where their fair value is negative. Where there is a legal ability and intention to settle net, then the derivative is classified as a net asset or liability, as appropriate.

Where cash collateral is received, to mitigate the risk inherent in amounts due to the LLP, it is included as a liability. Where cash collateral is given, to mitigate the risk inherent in amounts due from the LLP, it is included as an asset.

b) Hedge accounting

When transactions meet the criteria specified in IAS 39, the LLP applies fair value hedge accounting so that changes in the fair value of the underlying asset or liability that are attributable to the hedged risk are recorded in the statement of comprehensive income to offset the fair value movement of the related derivative.

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

1 Accounting policies (continued)

To qualify for hedge accounting the hedge relationship must be clearly documented at inception and the derivative must be expected to be highly effective in offsetting the hedged risk. Effectiveness must be tested throughout the life of the hedge relationship.

The LLP discontinues hedge accounting when:

- i) it is evident from testing that a derivative is not, or has ceased to be, highly effective as a hedge;
- ii) the derivative expires, or is sold, terminated or exercised; or
- iii) the underlying item matures or is sold or repaid.

The LLP may also decide to cease hedge accounting even though the hedge relationship continues to be highly effective by ceasing to designate the financial instrument as a hedge.

If the derivative no longer meets the criteria for hedge accounting, the cumulative fair value hedging adjustment is amortised over the period to maturity of the previously designated hedge relationship. If the underlying item is sold or repaid, the unamortised fair value adjustment is immediately reflected in the statement of comprehensive income.

c) Derivatives hedging beneficial interest in the mortgage portfolio

The LLP holds derivatives to hedge interest rate risk associated with the beneficial interest on the mortgage portfolio. These derivatives are not fair valued as under IAS39 they are accounted for on an accruals basis as part of the deemed loan to originator included in loans and other debts due from members of the LLP.

Foreign currency translation

Items included in the financial statements are measured using Sterling, the currency of the primary economic environment in which the entity operates ('the functional currency').

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. 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 Statement of Comprehensive Income.

Foreign exchange gains and losses are presented in the Income Statement within 'Interest receivable and similar income'.

Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition.

2 Judgements in applying accounting policies and critical accounting estimates

No judgements, estimates or assumptions have been made that are considered critical to the preparation of these financial statements.

NATIONWIDE COVERED BONDS LLP**Notes to the financial statements for the year ended 4 April 2014 (continued)**

| 3 Interest receivable and similar income | 2014 | 2013 |
|---|----------------|----------------|
| | £'000 | £'000 |
| Interest receivable from members | 323,764 | 385,539 |
| Excess profits payable | (123,132) | (102,079) |
| Bank interest receivable | 4,295 | 5,218 |
| Foreign exchange gain/(loss) | (12,948) | 12,948 |
| | 191,979 | 301,626 |

| 4 Interest payable and similar charges | 2014 | 2013 |
|---|----------------|----------------|
| | £'000 | £'000 |
| Interest payable on loans from members | 465,820 | 557,306 |
| Interest (receivable) on derivative financial instruments | (261,965) | (269,991) |
| | 203,855 | 287,315 |

| 5 (Losses)/gains from derivatives and hedge accounting | 2014 | 2013 |
|---|-----------------|-----------------|
| | £'000 | £'000 |
| Derivatives designated as fair value hedges | (290,464) | 240,416 |
| Fair value movement attributable to hedged risk | 272,806 | (211,255) |
| (Losses)/gains from fair value hedge accounting (note i) | (17,658) | 29,161 |
| Fair value (losses) from other derivatives (note ii) | (3,847) | (105,094) |
| | (21,505) | (75,933) |

Notes

- (i) Gains or losses from fair value hedges can arise where there is an IFRS hedge accounting relationship in place and either:
- the relationship passed all the monthly effectiveness tests but the fair value of the derivative was not exactly offset by the change in fair value of the liability being hedged (sometimes referred to as hedge effectiveness) or
 - the relationship failed a monthly effectiveness test which, for that month, disallows recognition of the change in fair value of the underlying asset or liability being hedged and in following months leads to the amortisation of existing balance sheet positions.
- (ii) Other derivatives are those used for economic hedging but which are not in an IAS 39 hedge accounting relationship because hedge accounting is not currently achievable.

Although the LLP uses derivatives exclusively to hedge risk exposures in interest rates or exchange rates, income statement volatility can still arise due to hedge accounting ineffectiveness or because hedge accounting is not achievable. Management recognise that this arises from the application of accounting rules which do not reflect the economic reality of the business and as such this volatility will continue period on period but will always trend back to zero over time.

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

5 (Losses)/gains from derivatives and hedge accounting (continued)

A loss of £21.5million (2013: £75.9 million loss) has been recognised in the year ended 4 April 2014 for derivatives and hedge accounting. Included within this result was the impact of the following:

- Losses of £17.7 million (2013: £29.2 million gain) on micro hedge relationships; and
- Losses of £3.8 million (2013: £105.1 million loss), principally a result of volatility in sterling:euro interest rates on cross currency interest rate swaps used to economically hedge non-sterling wholesale funding.

| 6 Administrative expenses | 2014 | 2013 |
|-----------------------------------|--------------|--------------|
| | £'000 | £'000 |
| Credit Rating Agency fees | 316 | 313 |
| Legal fees | 291 | 212 |
| Non audit fees payable to auditor | 192 | 174 |
| Audit fees payable as auditor | 24 | 24 |
| Other administrative expenses | 249 | 640 |
| | 1,072 | 1,363 |

7 Cash and cash equivalents

The LLP has placed its deposit account with the Nationwide Building Society as a provider of a Guaranteed Investment Contract. Withdrawals from this account are restricted by the detailed priority of payments set out in the transaction documents. The cash balance includes £982 million (2013: £1,334 million) collateral support to the derivatives deposited with the Covered Bond LLP as at 4 April 2014 by swap providers other than Nationwide Building Society.

8 Loans and other debts due from members

The loan to members of £13,091 million (2013: £14,858 million) represents a deemed loan to the Nationwide Building Society, generated as a result of the beneficial interest in the mortgage portfolio failing the derecognition criteria described in IAS 39. The deemed loan replaces the beneficial interest in the mortgage portfolio legally held by the LLP, and represents the substance of the transaction for accounting purposes.

If the derecognition criteria had been met the LLP would have shown a beneficial interest in a mortgage portfolio of £20,211 million as at 4 April 2014 (2013: £21,841 million). The mortgages are secured on residential property and are all designated in sterling at either fixed rates or at variable rates of interest, based on the standard variable rate of the Society. As discussed in note 1, the LLP has entered into a basis swap with the Society to swap the interest flow from these mortgages into a floating rate of return based on LIBOR. This swap is not recognised as a separate derivative financial instrument.

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

8 Loans and other debts due from members (continued)

| | 2014 | 2013 |
|--|-------------------|-------------------|
| | £'000 | £'000 |
| Loans and other debts due from members | 13,090,718 | 14,857,842 |
| Over-collateralisation | 6,832,253 | 6,991,773 |
| Deferred consideration presented in other debts due to members | (348,243) | (534,383) |
| Excess profits payable | 619,325 | 496,193 |
| Accrued interest on basis swap | 16,653 | 29,585 |
| Beneficial interest in a mortgage portfolio | 20,210,706 | 21,841,010 |

9 Derivative financial instruments

All derivative financial instruments are held for economic hedging purposes although not all derivatives are designated as hedging instruments under the terms of IAS 39. The table below analyses derivatives between those designated as hedging instruments and those which, whilst in economic hedging relationships, are not designated as hedging instruments.

| | 2014 | | | 2013 | | |
|---|--|------------------------------|----------------------------------|--|------------------------------|----------------------------------|
| | Contract/ notional amount £'000 | Fair value Asset £'000 | Fair value Liability £'000 | Contract/ notional amount £'000 | Fair value Asset £'000 | Fair value liability £'000 |
| Derivatives designed as fair value hedging instruments | | | | | | |
| Interest rate swaps | 8,449,259 | 940,095 | - | 7,883,742 | 1,271,691 | 2,390 |
| Other derivatives not designated in hedge accounting relationships | | | | | | |
| Cross currency interest rate swaps | 7,396,296 | 598,915 | 202,435 | 8,748,296 | 1,076,141 | 100,002 |
| Total | 15,845,555 | 1,539,010 | 202,435 | 16,632,038 | 2,347,832 | 102,392 |

The fair values in the above table are inclusive of accrued interest as follows:

- Cross currency interest rate swap asset includes £284,722 accrued interest (2013: £298,326 accrued interest).
- Interest rate swap asset includes £81,295,403 accrued interest (2013: £105,616,212 accrued interest).
- Cross currency interest rate swap liability includes £5,315,074 accrued interest (2013: £4,691,973 accrued interest).
- Interest rate swap liability includes £nil accrued interest (2013: £nil accrued interest).

An analysis of the maturity profiles of the derivatives can be found in note 14.

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

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

9 Derivative financial instruments (continued)

Offsetting

The LLP has financial assets and liabilities for which there is a legally enforceable right to set off the recognised amounts, and which may be settled net. However the netting arrangements do not result in an offset of balance sheet assets and liabilities for accounting purposes as the right to set off is not unconditional in all circumstances. Therefore, in accordance with IAS 32 Financial Instruments: Presentation, there are no financial assets or liabilities which are offset with the net amount presented on the balance sheet. All financial assets and liabilities are presented on a gross basis on the balance sheet.

In accordance with IFRS 7 Financial Instruments: Presentation, the following table shows the impact on derivative financial instruments, relating to transactions where:

- There is an enforceable master netting arrangement or similar agreement in place but the Offset Criteria are otherwise not satisfied, and
- Financial collateral is paid and received.

Master netting arrangements consist of agreements such as an International Swaps and Derivatives Association (ISDA) Master Agreement, whereby outstanding transactions with the same counterparty can be offset and settled net following a default or other predetermined event.

Financial collateral on derivative financial instruments consists of cash and securities settled, typically daily or weekly, to mitigate the mark to market exposures. Where cash collateral is received to mitigate the risk inherent in amounts due to the LLP, it is included as a liability. Where cash collateral is given to mitigate the risk inherent in amounts due from the LLP, it is included as an asset.

The 'Net amounts after offsetting under IFRS 7' presented below shows the exposure to counterparty credit risk for derivative contracts after netting benefits, and are not necessarily intended to represent the LLP's actual exposure to credit risk due to a variety of credit mitigation strategies which may be employed in addition to netting and collateral arrangements. Any such credit mitigation strategies are discussed further in the Credit Risk section of the note 14.

| | Gross and net amounts reported on the balance sheet £'000 | Master netting arrangements £'000 | Financial collateral £'000 | Net amounts after offsetting under IFRS 7 £'000 |
|----------------------------------|---|---|----------------------------------|--|
| 4 April 2014 | | | | |
| Financial assets | | | | |
| Derivative financial instruments | 1,539,010 | (202,435) | (869,299) | 467,276 |
| Total assets | 1,539,010 | (202,435) | (869,299) | 467,276 |
| Financial liabilities | | | | |
| Derivative financial liabilities | 202,435 | (202,435) | - | - |
| Total liabilities | 202,435 | (202,435) | - | - |
| 4 April 2013 | | | | |
| Financial assets | | | | |
| Derivative financial instruments | 2,347,832 | (102,392) | (1,323,123) | 922,317 |
| Total assets | 2,347,832 | (102,392) | (1,323,123) | 922,317 |
| Financial liabilities | | | | |
| Derivative financial liabilities | 102,392 | (102,392) | - | - |
| Total liabilities | 102,392 | (102,392) | - | - |

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

10 Loans from LLP members

The amount owing to members represents advances equivalent to the amounts borrowed by LLP under its Secured Loan Programme, as follows:

| Coupon Rate | Maturity | Notional | 2014 £'000 | 2013 £'000 |
|---|-----------------|-----------------|-----------------------|-----------------------|
| 3.5% | due 2015 | (EUR 2bn) | 1,649,075 | 1,690,100 |
| 3.88% | due 2013 | (EUR 2bn) | - | 1,694,048 |
| 4.375% | due 2022 | (EUR 2bn) | 1,648,240 | 1,690,394 |
| LIBOR + 0.8% | due 2027 | (GBP 2.5bn) | 2,500,000 | 2,500,000 |
| LIBOR + 0.5% | due 2018 | (GBP 2bn) | 2,000,000 | 2,000,000 |
| 2.875% | due 2015 | (EUR 1.25bn) | 1,030,917 | 1,056,571 |
| 4.89% | due 2020 | (NOK 500m) | 50,304 | 56,877 |
| 5.56% | due 2021 | (NOK 500m) | 50,265 | 56,831 |
| 5.625% | due 2026 | (GBP 750m) | 743,656 | 743,289 |
| 4.625% | due 2021 | (EUR 1.25bn) | 1,025,992 | 1,051,679 |
| 4.74% | due 2031 | (EUR 30m) | 24,747 | 25,384 |
| 4.924% | due 2025 | (EUR 132m) | 108,773 | 111,564 |
| 4.699% | due 2023 | (EUR 50m) | 41,278 | 42,342 |
| 5.695% | due 2021 | (NOK 500m) | 50,309 | 56,882 |
| LIBOR + 0.75% | due 2014 | (GBP 30m) | - | 29,996 |
| 5.01% | due 2032 | (EUR 50m) | 41,268 | 42,332 |
| 5.27% | due 2018 | (NOK 400m) | 40,247 | 45,505 |
| 4.1% | due 2017 | (EUR 58m) | 47,883 | 49,115 |
| EURIBOR + 0.6% | due 2014 | (EUR 80m) | 66,066 | 67,765 |
| 4.565% | due 2026 | (EUR 100m) | 82,564 | 84,693 |
| 4.4325% | due 2029 | (EUR 40m) | 33,023 | 33,875 |
| 4.12% | due 2026 | (EUR 50m) | 41,247 | 42,308 |
| STIBOR + 0.95% | due 2014 | (SEK 450m) | 41,509 | 45,345 |
| 3.77% | due 2027 | (EUR 103m) | 85,046 | 87,239 |
| 3.75% | due 2029 | (EUR 40m) | 33,026 | 33,877 |
| 3.125% | due 2016 | (EUR 1500m) | 1,235,737 | 1,266,458 |
| LIBOR + 1.5% | due 2026 | (GBP 100m) | 99,995 | 99,994 |
| LIBOR + 1.5% | due 2028 | (GBP 100m) | 99,995 | 99,994 |
| LIBOR + 1.5% | due 2031 | (GBP 50m) | 49,997 | 49,997 |
| 3.9% | due 2032 | (EUR 77m) | 63,562 | 65,201 |
| LIBOR + 1.6% | due 2015 | (GBP 650m) | 649,708 | 649,347 |
| 3.81% | due 2027 | (EUR 116m) | 95,563 | 98,015 |
| 3.832% | due 2030 | (EUR 88m) | 72,658 | 74,531 |
| 3.555% | due 2028 | (EUR 158m) | 130,047 | 133,401 |
| | | | 13,932,697 | 15,874,949 |
| Fair value adjustment for micro hedged risk | | | 890,112 | 1,179,696 |
| Accrued interest | | | 100,966 | 125,252 |
| | | | 14,923,775 | 17,179,897 |

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

11 Other debts due to members

All of the other debts due to members fall due after a minimum of 5 years (2013: all debts fell due after a minimum of 5 years).

12 Other liabilities

The liabilities below relate to Collateral Support deposited with the Covered Bond LLP by external swap providers following credit rating downgrades of those counterparties.

| | 2014 £'000 | 2013 £'000 |
|--------------------|---------------|---------------|
| Collateral support | 981,893 | 1,333,897 |
| | 981,893 | 1,333,897 |

13 Related party transactions

Ownership Structure of Nationwide Covered Bonds LLP

The members of the LLP are Nationwide Building Society, the controlling party, and Moulton Capital Finance Limited.

Key management personnel

The LLP Management Committee (comprised of Members and/or employees of the Nationwide Building Society and the representatives of the Moulton Capital Finance Limited) manage and conduct the business of the LLP and have all the rights, power and authority to act at all times for and on behalf of the LLP.

No transactions were entered into with key management personnel (2013: none).

Transactions with related parties

A number of transactions are entered into with related parties as part of the LLP's normal business.

| | 2014 £'000 | 2013 £'000 |
|--|---------------|---------------|
| Balances | | |
| Loans and other debts due from members | 13,090,718 | 14,857,842 |
| Cash and cash equivalents with NBS | 1,799,328 | 1,952,041 |
| Loans from LLP members | (14,923,775) | (17,179,897) |
| Other debts due to members | (348,243) | (534,383) |
| Derivative assets with NBS | 459,742 | 656,836 |
| Derivative liabilities with NBS | (202,435) | (102,392) |
| Transactions | | |
| Bank interest receivable | 4,295 | 5,218 |
| Interest receivable from members | 200,631 | 283,460 |
| Interest payable on loans from members | (465,820) | (557,306) |

14 Risk management and control

The LLP's activities expose it to a number of financial risks including credit risk and liquidity risk. For this reason, Nationwide Building Society devotes considerable resource to maintaining effective controls to manage, measure and mitigate these risks. The LLP uses derivative financial instruments to hedge certain risk exposures.

Risk management is carried out by a central risk management function of the Nationwide Building Society on a group wide basis.

Control of derivatives

The LLP uses derivative financial instruments to hedge certain of its financial risks but not for any speculative purposes. The Nationwide Building Society's Asset and Liabilities Committee is responsible for setting limits and conditions over the use of derivative products. Any exchange traded instruments are subject to cash requirements under the standard margin arrangements applied by the individual exchanges. Such instruments are not subject to significant credit risk.

Credit exposures arising on derivative contracts with certain counterparties are collateralised with cash deposits to mitigate credit exposure where the credit rating of these counterparties is downgraded below a certain level. Cash collateral received on certain derivatives is disclosed in note 12. All derivatives activity is contracted with OECD financial institutions. For valuing collateralised derivatives the LLP uses discount curves based on overnight indexed swap (OIS) rates, whilst for non-collateralised derivatives the LLP continues to use discount curves based on term Libor rates.

Credit risk

Credit risk arises where there is a possibility that a counterparty may default.

The LLP assesses its counterparties for credit risk before contracting with them. Credit rating is the main method used to measure counterparty credit risk. In accordance with the criteria of the rating agencies that rate the Notes, the Programme Documentation contains various rating triggers linked to each counterparty, which require certain actions to be taken if triggers are breached, including the posting of collateral or the replacement of a counterparty.

The maximum exposure to credit risk is the carrying amount of the loans and other debts due from members of £13,091 million (2013: £14,858 million), the derivative financial instruments of £1,539 million. (2013: £2,348 million) and cash and cash equivalents with Nationwide Building Society of £1,799 million (2013: £1,952 million).

The primary credit risk of the LLP relates to the credit risk associated with the pool of mortgages originated by Nationwide Building Society.

NATIONWIDE COVERED BONDS LLP**Notes to the financial statements for the year ended 4 April 2014 (continued)****14 Risk management and control (continued)**

The current counterparty credit ratings (short-term/long-term) are included below:

| Function | Counterparty | Rating as at 4 April 2014 S&P/Moody's/ Fitch | Rating Trigger Breached | Breach Remedy | Updated rating S&P/Moody's/ Fitch (1) |
|----------|-------------------|---|-------------------------------|-------------------|---|
| Account | Nationwide | A-1/P-1/F1 | N | - | A-1/P-1/F1 |
| Bank | Building Society | A/A2/A | | | A/A2/A |
| Swap | Barclays Bank plc | A-1/P-1/F1 | Y | Collateral Posted | A-1/P-1/F1 |
| Provider | | A/A2/A | | | A/A2/A |
| Swap | BNP Paribas | A-1/P-1/F1 | Y | Collateral Posted | A-1/P-1/F1 |
| Provider | | A+/A2/A+ | | | A+/A1/A+ |
| Swap | Deutsche Bank | A-1/P-1/F1+ | Y | Collateral Posted | A-1/P-1/F1+ |
| Provider | | A/A2/A+ | | | A/A2/A+ |
| Swap | Nationwide | A-1/P-1/F1 | N | - | A-1/P-1/F1 |
| Provider | Building Society | A/A2/A | | | A/A2/A |
| Swap | Societe General | A-1/P-1/F1 | Y | Collateral Posted | A-1/P-1/F1 |
| Provider | Paris | A/A2/A | | | A/A2/A |
| Swap | UBS | A-1/P-1/F1 | Y | Collateral Posted | A-1/P-1/F1 |
| Provider | | A/A2/A | | | A/A2/A |

Note (1) As at date of approval of the financial statements

The loans and other debts due from members are secured on residential property. At year end, there was £nil impairment provision against the loans and other debts due from members (2013: £nil). For the LLP, credit risk is additionally mitigated by the over collateralisation of the beneficial interest in mortgages (see note 8) and by eligibility criteria for selection under the secured loan covenants. Subsequent to selection, credit risk is monitored through the application of a monthly asset coverage test. For details of the eligibility criteria and asset coverage test please refer to the Nationwide Covered Bond Base Prospectus dated 28 June 2012. More information on mortgage assets is set out below.

The tables below present the characteristics of the total mortgage loans pool:

| | 2014 | 2013 |
|---------------------------------------|-----------------|----------|
| Aggregate loan balance | £20,211m | £21,856m |
| Number of loans | 246,275 | 266,821 |
| Largest loan | £971,215 | £918,807 |
| Average balance of mortgage loan | £82,066 | £81,911 |
| Longest dated mortgage legal maturity | 51 years | 46 years |

NATIONWIDE COVERED BONDS LLP**Notes to the financial statements for the year ended 4 April 2014 (continued)****14 Risk management and control (continued)**

Distribution by current loan to value ratio (indexed):

| | 2014 | 2013 |
|---|------------|------------|
| | % | % |
| <70% | 77 | 69 |
| 70% - 80% | 13 | 15 |
| 80% - 90% | 7 | 10 |
| 90% - 100% | 2 | 4 |
| >100% | 1 | 2 |
| Total book | 100 | 100 |
| Average loan to value of book (indexed) | 52 | 57 |

The value of residential property on which the mortgage loans are secured are updated quarterly to reflect changes in the house prices index.

Mortgage loans and advances by payment due status:

| | 2014 | | 2013 | |
|--|-------------------|------------|-------------------|------------|
| | £'000 | % | £'000 | % |
| Not impaired: | | | | |
| Neither past due nor impaired | 19,984,239 | 99 | 21,658,118 | 99 |
| Past due up to 3 months but not impaired | 137,441 | 1 | 105,712 | 1 |
| Impaired | 89,026 | - | 91,765 | - |
| | 20,210,706 | 100 | 21,855,595 | 100 |

A mortgage loan is classified as "impaired" if it is more than 3 months past due. Impaired mortgage loans are further analysed as follows:

| | 2014 | | 2013 | |
|-------------------------|---------------|------------|---------------|------------|
| | £'000 | % | £'000 | % |
| Impaired status: | | | | |
| Past due 3 to 6 months | 47,930 | 54 | 47,784 | 52 |
| Past due 6 to 12 months | 27,302 | 31 | 30,706 | 34 |
| Past due over 12 months | 13,794 | 15 | 13,275 | 14 |
| Possessions | - | - | - | - |
| | 89,026 | 100 | 91,765 | 100 |

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

14 Risk management and control (continued)

| Residential mortgage accounts by locations: | 2014 % | 2013 % |
|---|------------|------------|
| South-east England (excluding Greater London) | 28 | 29 |
| Central England | 19 | 19 |
| Northern England | 18 | 17 |
| Greater London | 13 | 13 |
| South-west England | 8 | 8 |
| Scotland | 6 | 8 |
| Wales and Northern Ireland | 8 | 6 |
| | 100 | 100 |

Liquidity risk

Liquidity risk is the risk that the LLP is unable to meet the payment obligations associated with its financial liabilities when they fall due.

The LLP liquidity policy is to maintain sufficient liquid resources in the Reserve Bank account to service the swap payments for the next month forward, interest on the loan and any service fees. This is reviewed by the cash manager and any shortfall is funded from the general Bank account. Liquidity risk is also mitigated through the additional income collected on the over collateralisation of the beneficial interest in mortgages. All derivatives have the same notional amount and maturity date as the corresponding loans from LLP members. The table below analyses assets and liabilities into relevant maturity ratings based on the remaining period at the balance sheet date to the contractual maturity date.

At 4 April 2014
Residual maturity

| | Due In | | | | | | | | |
|---------------------------------------|------------------------------|----------------------|----------------------|----------------------|-----------------------|---------------------|---------------------|------------------------|-------------------|
| | Less than 1 month* £000's | 1-3 months £000's | 3-6 months £000's | 6-9 months £000's | 9-12 months £000's | 1-2 years £000's | 2-5 years £000's | Over 5 years £000's | Total £000's |
| Assets | | | | | | | | | |
| Cash and cash equivalents | 1,799,328 | - | - | - | - | - | - | - | 1,799,328 |
| Loan and other debts due from members | (16,303) | 81,992 | 51,739 | - | 809,812 | 3,340,280 | 4,142,787 | 4,680,411 | 13,090,718 |
| Derivative financial instruments | - | - | - | - | - | 421,926 | 61,975 | 1,055,109 | 1,539,010 |
| Total assets | 1,783,025 | 81,992 | 51,739 | - | 809,812 | 3,762,206 | 4,204,762 | 5,735,520 | 16,429,056 |
| Liabilities | | | | | | | | | |
| Loans from LLP members | 5,583 | 71,921 | 62,466 | 44,445 | 673,700 | 2,782,489 | 3,374,571 | 7,908,600 | 14,923,775 |
| Other debts due to members | - | - | - | - | - | - | - | 348,243 | 348,243 |
| Derivative financial instruments | - | 5,915 | 1,089 | - | - | 10,955 | 86,739 | 97,737 | 202,435 |
| Other liabilities | 981,893 | - | - | - | - | - | - | - | 981,893 |
| Total liabilities | 987,476 | 77,836 | 63,555 | 44,445 | 673,700 | 2,793,444 | 3,461,310 | 8,354,580 | 16,456,346 |
| | 795,549 | 4,156 | (11,816) | (44,445) | 136,112 | 968,762 | 743,452 | (2,619,060) | (27,290) |

*Includes repayable on demand

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

14 Risk management and control (continued)

At 4 April 2013
Residual maturity

| | Due In | | | | | | | | |
|---------------------------------------|--------------------|-----------------|---------------|------------------|---------------|----------------|------------------|-------------------|-------------------|
| | Less than 1 month* | 1-3 months | 3-6 months | 6-9 months | 9-12 months | 1-2 years | 2-5 years | Over 5 years | Total |
| | £000's | £000's | £000's | £000's | £000's | £000's | £000's | £000's | £000's |
| Assets | | | | | | | | | |
| Cash and cash equivalents | 1,952,041 | - | - | - | - | - | - | - | 1,952,041 |
| Loan and other debts due from members | 1,280 | (30,865) | - | 2,067,046 | 36,605 | 930,465 | 4,956,922 | 6,896,389 | 14,857,842 |
| Derivative financial instruments | (6,565) | 1,390 | 22,553 | 452,052 | 22,030 | 2,718 | 563,488 | 1,290,166 | 2,347,832 |
| Total assets | 1,946,756 | (29,475) | 22,553 | 2,519,098 | 58,635 | 933,183 | 5,520,410 | 8,186,555 | 19,157,715 |
| Liabilities | | | | | | | | | |
| Loans from LLP members | 5,602 | 6,073 | 22,502 | 1,801,614 | 54,418 | 762,385 | 4,293,230 | 10,234,073 | 17,179,897 |
| Other debts due to members | - | - | - | - | - | - | - | 534,383 | 534,383 |
| Derivative financial instruments | (1,372) | (3,320) | - | - | - | 4,281 | 46,639 | 56,164 | 102,392 |
| Other liabilities | 1,333,897 | - | - | - | - | - | - | - | 1,333,897 |
| Total liabilities | 1,338,127 | 2,753 | 22,502 | 1,801,614 | 54,418 | 766,666 | 4,339,869 | 10,824,620 | 19,150,569 |
| | 608,629 | (32,228) | 51 | 717,484 | 4,217 | 166,517 | 1,180,541 | (2,638,065) | 7,146 |

*Includes repayable on demand

Prepayment risk

Cash flows are dependent on the underlying mortgage loans originated within Nationwide Building Society. In the normal course of business, a proportion of mortgage borrowers repay their loan in advance of contractual maturity. As a result, the weighted average life of the deemed loan is likely to be significantly less than that implied by the contractual maturity dates of the mortgage pool.

The terms of the loans from LLP members are that repayments of principal will only be made to the extent that sufficient cash flows have been received from the LLP's assets. In the event that prepayment rates in the mortgage pool reduce, principal repayments and the notes may be spread over a longer period.

The table below presents the cash flows payable by the LLP under financial liabilities by remaining contractual maturities at the balance sheet date. The amounts disclosed in the table are the contractual undiscounted cash flows of all financial liabilities (i.e. nominal values).

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

14 Risk management and control (continued)

At 4 April 2014
Gross contractual
cash flows

| | Due In | | | | | | | | |
|----------------------------------|------------------------------|----------------------|----------------------|----------------------|-----------------------|---------------------|---------------------|------------------------|-------------------|
| | Less than 1 month* £000's | 1-3 months £000's | 3-6 months £000's | 6-9 months £000's | 9-12 months £000's | 1-2 years £000's | 2-5 years £000's | Over 5 years £000's | Total £000's |
| Loans from LLP members | 6,728 | 82,000 | 96,775 | 132,382 | 852,534 | 3,115,197 | 4,396,369 | 9,170,220 | 17,852,205 |
| Other debts due to members** | - | - | - | - | - | - | - | 348,243 | 348,243 |
| Derivative financial instruments | 713 | 9,703 | 6,088 | 5,677 | 7,420 | 56,844 | 188,829 | 187,850 | 463,124 |
| Other liabilities | 981,893 | - | - | - | - | - | - | - | 981,893 |
| Total liabilities | 989,334 | 91,703 | 102,863 | 138,059 | 859,954 | 3,172,041 | 4,585,198 | 9,706,313 | 19,645,465 |

At 4 April 2013
Gross contractual
cash flows

| | Due In | | | | | | | | |
|----------------------------------|------------------------------|----------------------|----------------------|----------------------|-----------------------|---------------------|---------------------|------------------------|-------------------|
| | Less than 1 month* £000's | 1-3 months £000's | 3-6 months £000's | 6-9 months £000's | 9-12 months £000's | 1-2 years £000's | 2-5 years £000's | Over 5 years £000's | Total £000's |
| Loans from LLP members | 6,759 | 16,197 | 58,148 | 1,933,615 | 234,140 | 1,179,170 | 5,365,533 | 12,497,400 | 21,290,962 |
| Other debts due to members** | - | - | - | - | - | - | - | 534,383 | 534,383 |
| Derivative financial instruments | (476) | 5,014 | 4,543 | 3,882 | 3,285 | 16,315 | 60,707 | 100,564 | 193,834 |
| Other liabilities | 1,333,897 | - | - | - | - | - | - | - | 1,333,897 |
| Total liabilities | 1,340,180 | 21,211 | 62,691 | 1,937,497 | 237,425 | 1,195,485 | 5,426,240 | 13,132,347 | 23,353,076 |

*Includes repayable on demand

** Other debts due to members represents excess revenue receipts currently held by Covered Bond LLP and are repayable upon the winding up of the structure

Foreign currency risk

The current operating currencies of the LLP are in Sterling, Euros, US Dollars, Norwegian Krona and Swedish Krona. As the LLP prepares its financial statements in Sterling these will be affected by movements in the currency exchange rates. This exposure is mitigated by the use of cross currency derivatives. In particular the LLP hedges all of its exposure on its currency borrowings back to Sterling by the use of cross currency derivatives and it therefore does not have a material economic exposure to foreign exchange gains and losses. Accordingly it does not separately monitor value at risk arising from open foreign currency positions.

An accounting loss of £12.9 million is included in the statement of comprehensive income in respect of open foreign currency positions for the year ended 4 April 2014 (2013 gain: £12.9 million).

NATIONWIDE COVERED BONDS LLP

Notes to the financial statements for the year ended 4 April 2014 (continued)

14 Risk management and control (continued)

Interest rate risk

The LLP is exposed to interest rate risk in that its multiple currency interest expense is at fixed and floating rates, whilst its interest income originates from its beneficial interest in a pool of the Nationwide Building Society's mortgages at Sterling fixed and floating rates.

The LLP hedges its exposure to fixed and floating currency rate risk through entering into derivative contracts with Nationwide Building Society and external counterparties. Through a combination of basis, interest rate and cross currency swaps, the LLP is able to swap the interest receivable from its beneficial interest in the pool of the mortgages and the interest payable on its loan liabilities such that the resulting cash flows are matched. Therefore the LLP's exposure to interest rate risk is minimal. Only the interest rate swaps are utilised for hedge accounting.

15 Fair value of financial assets and liabilities

Fair value of financial assets and liabilities at amortised cost

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the balance sheet at fair value.

| At 4 April | 2014 | | 2013 | |
|--|---------------------------------|-----------------------------|---------------------------------|-----------------------------|
| | Carrying value £'000 | Fair value £'000 | Carrying value £'000 | Fair value £'000 |
| Assets | | | | |
| Loans and other debts due from members | 13,090,718 | 13,207,462 | 14,857,842 | 13,866,623 |
| Liabilities | | | | |
| Loans from LLP members | 14,923,775 | 14,919,983 | 17,179,897 | 17,050,607 |
| Other debts due to members | 348,243 | 348,243 | 534,383 | 534,383 |
| Accruals and other liabilities | 981,941 | 981,941 | 1,333,928 | 1,333,928 |

The fair value of other debts due to members and accruals and other liabilities approximates carrying value.

The estimated fair value of loans and other debts due from members represents the discounted amount of estimated future cash flows expected to be received based on the underlying mortgage pool assets. Expected cash flows are discounted at current market rates to determine fair value. These are considered to be level 3 within the fair value hierarchy.

The estimated fair value of loans from LLP members represents the discounted amount of cash flows expected to be paid. Expected cash flows are discounted at current market rates to determine fair value.

Fair value of financial assets and liabilities held at fair value

The fair value of the derivatives falls within level 2 of the fair value hierarchy. Financial instruments classified as Level 2 have been valued using models whose inputs are observable in an active market. Valuations based on observable inputs include swap derivative financial instruments which are valued using market standard pricing techniques. There are no instruments that fall within level 3 of the fair value hierarchy as at 4 April 2014 (2013: none). There have been no movements in and out of level 3 throughout the year.

16 Capital management

Capital comprises the retained earnings and share capital. Capital is managed on a Group basis.

The Group is subject to the capital requirements imposed by its regulator, the Prudential Regulation Authority (PRA), formerly the Financial Services Authority (FSA). During the year the Group complied with the capital requirements set by the PRA.

Further information on the Group's capital position can be viewed in the Business Review of the Group Annual Report and Accounts, which can be obtained from the address below or at **nationwide.co.uk**.

17 Parent undertaking and ultimate controlling entity

The member companies of the LLP are Nationwide Building Society, the controlling party, and Moulton Capital Finance Limited. Both companies are incorporated in the UK and registered in England and Wales.

The ultimate parent and controlling party is Nationwide Building Society, also registered in England and Wales.

Nationwide Building Society is registered at Nationwide House, Pipers Way, Swindon, Wiltshire, SN38 1NW. The Group Annual Report and Accounts can be obtained from this address or at **nationwide.co.uk**.

18. Post balance sheet event

In June 2014, the LLP issued notes totalling EUR 1.75 billion and received proceeds of EUR 1.74 billion.