

Memo



To SCM Approvals Committee
From Jonathan Zenios
Date 28 November 2006
Subject Project Berry II – Investment in Index Linked Gilts

1. SUMMARY

Structured Capital Markets (“**SCM**”) is seeking approval for an increase in the product limit for Project Berry (the “**Transaction**”) from £3bn to £7bn. The SCM Approvals Committee approved the original Transaction on 11 January 2006 with a product limit of £3bn and an initial transaction tenor of 12 months. The tenor was subsequently extended by an additional 36 months by way of notification to the SCM Approvals Committee on 19 October 2006 (see Annex 6).

The Transaction provides an opportunity for the Barclays Bank PLC (“**Barclays**”) group to invest in additional Index Linked Gilts (“**ILGs**”). The Transaction enables Barclays to include the investment in ILGs (i) in its’ stock of sterling liquid assets (the “**SSLA**”) that Barclays is required to maintain to comply with the FSA’s Sterling Stock Liquidity Policy and (ii) to guarantee and collateralise various obligations of Barclays.

The proposed increase in the product limit for the Transaction will involve an additional purchase of ILGs by Barclays Aldersgate Investments Limited (“**BAIL**”), an existing solo-consolidated investment company within the Barclays group which currently holds £3bn of ILGs acquired as part of the original Transaction. It is proposed that the new Transaction to purchase an additional £4bn of ILGs will be executed over multiple tranches aggregating to a total investment in ILGs equal to a cash market value of £7bn in BAIL, although the exact composition of the new portfolio of ILGs is yet to be determined.

At present, the only entities whose Eligible Securities (See Annex 2) are permitted to be included in Barclays’ SSLA (see Annex 1) are those held directly by Barclays and Barclays Private Bank Limited (“**BPBL**”), although this is because of an earlier agreement with the Bank of England / FSA rather than any specific requirement under FSA rules in IPRU Chapter LS. The original SCM Approvals Paper in respect of Project Berry referred to the possibility of adding BAIL to those entities whose assets are permitted to be included in Barclays’ SSLA. Barclays Group Treasury has expressed a preference not to alter the existing agreement with the FSA and therefore, this has not been pursued by SCM. Accordingly, the ILGs held by BAIL will be made available to Barclays in order that they may be included in Barclays’ SSLA or to support the Liquidity Requirement or other business of the Portfolio Management Desk (“**PMD**”), such as the Bank of England Repo facility.

Economic Benefit

PMD within Barclays Capital has been tasked by Barclays Group Treasury with managing Barclays’ SSLA and the clearing and payment obligations of Barclays (“**Liquidity Requirement**”). Given PMD’s existing responsibilities in this area, SCM has agreed with PMD that PMD will be responsible for managing the Barclays group market exposure arising from entering into the Transaction. The cost of managing the market exposure is expected to be between 17 and 20bps per annum. However, for the purposes of this paper, the cost is assumed to be 17.5bps per annum. Key financial data relating to the Transaction is set out below:

Proposed product limit	Original product limit £3bn	Additional £4bn proposed increase to product limit	Total £7bn cash investment proposed limit
Estimated 2007 PTE revenue based on current inflation estimate	£32.6m p.a. (Pre- Provision) £21.2m p.a. (Post- Provision) (assuming provision is 30% of the s94 adjustment deduction)	£48.7m p.a. (Pre- Provision) £32.0m p.a. (Post- Provision) (assuming provision is 30% of the s94 adjustment deduction)	£81.3m p.a. (Pre- Provision) £53.2m p.a. (Post- Provision) (assuming provision is 30% of the s94 adjustment deduction)
2007 Tax capacity <i>Return on Tax capacity for 2007</i>	£93.5.m 34.8% (Pre-Provision) 22.7% (Post-Provision)	£136.9.m 35.6% (Pre-Provision) 23.4 (Post-Provision)	£230.4.m 35.3% (Pre-Provision) 23.1% (Post-Provision)
WRAs <i>Return on WRA's</i>	£0m (subject to netting per section 8.1 below) N/A (Pre-Provision) N/A (Post-Provision)	£0m (subject to netting per section 8.1 below) N/A (Pre-Provision) N/A (Post-Provision)	£0m (subject to netting per section 8.1 below) N/A (Pre-Provision) N/A (Post-Provision)
2007 PUG	£26.5m p.a. (Including Provision)	£39.0m p.a. (Including Provision)	£65.5m p.a. (Including Provision)
Tenor	48 months (Original tenor 12 months, extension of 36 months approved)		

This Approvals Paper contains a description of all significant tax, credit, market and operational risks.

2. DETAILED TRANSACTION DESCRIPTION

A structure diagram of the Transaction is attached in Annex 4 to this Approvals Paper.

2.1 Closing

- 2.1.1 Barclays will capitalise BAIL with a further £4bn non-voting preference shares (the “**Prefs**”) in addition to the £3bn currently in issue. The new Prefs will have a fixed term of 10 years but are redeemable at the option of the holder at short notice. The Prefs entitle the holder to a discretionary dividend determined by the directors.
- 2.1.2 The Prefs will be funded out of Barclays Group Treasury low-interest bearing current account (“**LIBCA**”) balances.
- 2.1.3 Barclays, acting as agent for an undisclosed principal (BAIL), will purchase the additional £4bn portfolio of ILGs. BAIL will use the proceeds from the issuance of the Prefs to fund the purchase of ILGs.
- 2.1.4 The purchase of the ILGs will probably be executed in multiple tranches over a period of several days due to availability constraints and in order to minimise the market impact of the Transaction.
- 2.1.5 As each tranche of ILGs is purchased, Barclays will enter into a short-term cash settled total rate of return swap (“**TRS**”) with a market counterparty to be determined in respect of each tranche of ILGs acquired from the market. Under each TRS, Barclays will pay away any coupons and any appreciation in respect of the ILGs and receive a LIBOR based return minus a spread, which is expected to be in the region of 30bps, and any depreciation in respect of the ILGs. It is anticipated that each TRS will have a term of anywhere between two weeks and one month, although this will depend on market conditions at the time of execution.
- 2.1.6 The choice of BAIL as the purchaser of the ILGs, rather than Barclays, allows SCM to ‘ring fence’ the economic positions in the ILGs, thereby facilitating the monitoring of their pre-tax investment performance and the calculation of the RPI uplift in the ILGs for the purposes of corporation tax.
- 2.1.7 Since only those Eligible Securities held directly by Barclays or BPBL are currently permitted to be included in Barclays’ SSLA, Barclays and BAIL will enter into an agreement at the time of closing under which BAIL will make the ILGs available to Barclays. Consequently, the ILGs purchased

under the Transaction will be available to PMD to be included in Barclays' SSLA to support the Liquidity Requirement or to be used by Barclays in the Bank of England Repo facility (see Annex 1). The ILGs will then be reported on Barclays Sterling Liquidity Return ("SLR1"). Note the SLR1 will only include those ILGs which are not used to guarantee payment obligations.

- 2.1.8 The agreement under which BAIL will transfer the ILGs to Barclays will be by way of a pledge with title transfer, a stock loan or a reverse repo (the "**Stock Loan**"), under which Barclays will post cash collateral (the "**Collateral**") to BAIL.
- 2.1.9 BAIL will deposit the Collateral with Barclays Group Treasury, thereby earning interest income. In turn, BAIL will make interest payments to Barclays in respect of the Collateral less an arm's length fee for the use of the ILGs, and Barclays will make manufactured payments to BAIL representing the coupons on the ILGs.
- 2.1.10 Once Barclays has taken title to the ILGs under the Stock Loan, PMD will utilise them for their business as described in section 2.1.7.
- 2.1.11 SCM will pay PMD a fee of approximately 17.5bps for managing the market exposure, associated with holding the ILGs, in accordance with their normal trading procedures.

2.2 **Interim Steps**

- 2.2.1 On the date of maturity of each TRS, Barclays, through PMD, may enter into a new TRS, a reverse repo or a stock loan over similar ILGs with the market in order to effect settlement of the original TRS.
- 2.2.2 In such a scenario, the ILGs acquired under a reverse repo or stock loan by Barclays will be sold into the market by PMD and each TRS unwound at the price at which Barclays is able to effect the sale of the ILGs. As a result of entering into a reverse repo or stock loan over ILGs, Barclays will achieve a short position with respect to the ILGs whilst BAIL will maintain a long position with respect to the ILGs.
- 2.2.3 It should be noted that since SCM will be paying PMD a fee for managing the market exposure associated with holding the ILGs, PMD will be entirely responsible for determining how this risk is managed on an on-going basis.

2.3 **Maturity**

- 2.3.1 The Transaction will mature at the end of 2009, following the 36 month extension in the tenor approved in October 2006, or on the occurrence of certain specified events to be agreed by the directors of BAIL, such as a change in law. At maturity, BAIL may be invited to accept cash settlement of Barclays' obligation to return the ILGs to BAIL under the Stock Loan.

3. ECONOMICS AND ECONOMIC DRIVERS

3.1 The Barclays Inflation Research desk estimates UK RPI level to be at Dec 06: 201.3, Jan 07: 200.7 and Dec 07: 207.2. These figures are used in calculating the economic benefit below.

As mentioned above, PMD will be responsible for managing the market exposure of holding the ILGs. PMD has indicated that the cost of managing this exposure will be between 17 and 20bps per annum. The following economics assume a cost of 17.5bps per annum. Assuming the market exposure is managed by PMD, the benefit from entering into the Transaction the Barclays group will be the value of the s94 adjustment deduction less the initial cost of each TRS less the ongoing cost of managing the market exposure of holding the ILGs.

Assumptions	Original Tranche	New Tranche	Total
Cash Investment in ILGs : (a)	£3,000,000,000	£4,000,000,000	£7,000,000,000
Hedging Cost (in BPS) : (b)	17.5	17.5	
Estimated RPI at start	Dec 06: 201.3	Jan 07: 200.7	
Estimated RPI at end of 2007	Dec 07: 207.2	Dec 07: 207.2	
Applicable change in RPI	2.941%	3.249%	3.117%
s 94 Adjustment : (d)=(a * c)	£88,226,528	£129,945,192	£218,171,719
Applicable 1-Month LIBOR : (e)	5.164%	5.164%	
Blended Coupon Rate on ILGs : (f)	2.252%	2.252%	
Provision Rate : (g)	30%	30%	
UK Corporation Tax Rate : (h)	30%	30%	
TRS (in BPS) : (i)	0	30	

Illustrative Annual Benefit Calculation	Original Tranche	New Tranche	Total
PMD Hedging Cost: (j)=(a * b * 0.0001)	(£5,250,000)	(£6,057,692)	(£11,307,692)
TRS: (k) = (a * i * 0.0001 * 4/52)	£0	(£923,077)	(£923,077)
PBT: (l) = (j+k)	(£5,250,000)	(£6,980,769)	(£12,230,769)
Tax at 30% : (m) = (l*h)	£1,575,000	£2,094,231	£3,669,231
S94 Adjustment (n) = (d*h)	£26,467,958	£38,983,558	£65,451,516
Provision : (o) = (n*g)	(£7,940,387)	(£11,695,067)	(£19,635,455)
Tax : (p) = (m+n+o)	£20,102,571	£29,382,721	£49,485,292
PAT : (q) = (l+p)	£14,852,571	£22,401,952	£37,254,523
Pre Tax Equivalent (Barclays Benefit) : (r) = (q/ (1-h))	£21,217,958	£32,002,788	£53,220,747

PUG Calculations (Annual)	Stat Account	Man Acct	PUG
PBT	(£12,230,769)	£53,220,747	£65,451,516
Tax	£49,485,292	(£15,966,224)	
PAT	£37,254,523	£37,254,523	

The table below sets out the summary economics under five inflation scenarios. The first row sets out the minimum inflation rate under which the Transaction is profitable for the Barclays group. As per the Barclays Inflation Research desk, the annual UK RPI change for the year period January to December 2007 is estimated to be 3.2% whereas for the same period in 2006 it is estimated to be 4.1%.

RPI Rate Δ	Post Prov PTE	Prov (PTE)	PUG	Tax Cap Utilised	ROTC
0.62%	(£0)	(£5,596,154)	£13,057,692	£56,583,332	0.00%
2.70%	£43,642,308	(£24,300,000)	£56,700,000	£202,057,692	21.60%
3.70%	£64,642,308	(£33,300,000)	£77,700,000	£272,057,692	23.76%
4.00%	£70,942,308	(£36,000,000)	£84,000,000	£293,057,692	24.21%
5.00%	£91,942,308	(£45,000,000)	£105,000,000	£363,057,692	25.32%

4. UK TAX ANALYSIS

The U.K. tax analysis is supported by an opinion issued by Slaughter & May in February 2006 for the original transaction. Confirmation will be sought that the position remains unchanged from the original opinion issued.

4.1 BAIL

- 4.1.1 Following acquisition, the ILGs will represent creditor loan relationships of BAIL. For tax purposes, fair value accounting must be used to determine the amounts to be brought into account in respect of the ILGs under the loan relationships code (s.94 FA 1996).
- 4.1.2 During the term of the Transaction, BAIL will be taxed under the loan relationships code (s.94 FA 1996) on a fair value basis on both the coupon on the ILGs and any movement in the fair value of the ILGs over the period. An adjustment is made pursuant to s.94 FA 1996 to remove from taxable income amounts corresponding to the uplift attributable to inflation on the ILGs. Over any period for which the taxation of the ILGs is considered, any movement in the fair value of the ILGs over the period will be determined as if the carrying value of the ILGs at the beginning of the period was increased or reduced by the same percentage as the percentage increase or reduction in the retail prices index between the beginning and end of the period.
- 4.1.3 If the ILGs are transferred to Barclays under the Stock Loan, any interest expense on the Collateral will be deductible for BAIL under the loan relationships provisions (s.84 FA 1996) in accordance with the interest expense recognised in its accounts. As the Collateral will constitute a connected party debt, an amortised cost basis is required to be applied. This will be consistent with the accounting treatment.

4.2 Barclays

- 4.2.1 Any hedging of the Barclays group's position will be performed by PMD in the course of its normal portfolio management activities.
- 4.2.2 If the ILGs are transferred to Barclays by BAIL under the Stock Loan, Barclays will not recognise anything in its balance sheet in respect of the Stock Loan. There will therefore be no debits and credits which can be attributed to a loan relationship in Barclays accounts in respect of the ILGs (other than the Shorts).
- 4.2.3 The Collateral provided to BAIL by Barclays will represent a connected party loan relationship of Barclays. Barclays will be taxed (under s.84 FA 1996) on any interest arising on the Collateral in accordance with the profits recognised in its accounts.

5. TAX RISK

5.1 Deductibility of Manufactured Payments

- 5.1.1 The risk that para 7A Schedule 23A ICTA 1988 could operate to deny relief for manufactured payments made by Barclays in respect of coupons paid on the ILGs under the Stock Loan is considered low because the payments are made in the context of a transaction where a manufactured payment could not be seen to secure the advantage. In addition, the manufactured payments are on a market standard repo or stock loan transaction which is on normal commercial terms.

6. UK GAAP and IAS ACCOUNTING

6.1 BAIL

- 6.1.1 BAIL prepares its accounts under UK GAAP.
- 6.1.2 The Prefs will be classified as a financial liability under FRS 25 and would be carried at amortised cost.
- 6.1.3 On initial recognition, BAIL will measure the ILGs at fair value less attributable transaction costs. The discount or premium from the redemption value as at the date of acquisition will be amortised over time to the income statement.
- 6.1.4 The interest and indexation uplift (discount or premium) will be recognised in the income statement on an accruals basis.
- 6.1.5 At the first balance sheet date, the book value will be adjusted by the amortisation of the initial discount or premium but also by the movement in the RPI since acquisition (SORP on securities 37-28).

Eg.	Acquisition value (A)	90
	Expected redemption value on acquisition (B)	100
	Maturity (C)	10 yrs
	Initial amortisation (B-A)/C	1
	Expected Redemption value on first balance sheet date (D)	110
	Movement in RPI (E) = (D-B)	10
	Amortisation adjustment at the end of year 1(E/C)	1
	Total amortisation	2

- 6.1.6 At subsequent balance sheet dates, the same adjustment will be made.
- 6.1.7 On the transfer of the ILGs to Barclays under the Stock Loan, the Collateral posted to BAIL by Barclays will be treated as a loan made by Barclays to BAIL in the books of both entities. The loan will be carried at cost with interest recognised on an accruals basis.

6.2 Barclays Solus

- 6.2.1 Barclays prepares its solus accounts under IFRS.
- 6.2.2 The Prefs will be treated as a financial asset classified as a loan and receivable carried at amortised cost under IAS 39. Any dividends will be recognised in the income statement when declared.
- 6.2.3 Each TRS will meet the definition of a derivative under IAS 39 and will be fair valued through the P&L.
- 6.2.4 If the ILGs are transferred to Barclays by BAIL under the Stock Loan, the ILGs are not derecognised by BAIL as all the risks and rewards of ownership of the asset will remain with BAIL (IAS 39.20). Accordingly, Barclays will not recognise the ILGs on its balance sheet, but will recognise the fee payable in respect of the Stock Loan in its P&L.
- 6.2.5 The cash collateral posted to BAIL by Barclays will be treated as a loan made by Barclays to BAIL. The loan will be carried at amortised cost with interest accrued on an effective yield basis.
- 6.2.6 The stock loan or reverse repo executed by PMD will be treated as secured loans carried at amortised cost. The subsequent short sale will be treated as a financial liability at fair value through profit and loss.

6.3 Barclays Consolidated

- 6.3.1 Barclays prepares its consolidated accounts under IFRS.
- 6.3.2 On initial recognition, Barclays will classify the ILGs as 'at fair value through profit or loss'. Any directly attributable transaction costs would be included in the fair value on initial recognition.
- 6.3.3 The treatment of each TRS in Barclays consolidated accounts will be identical to its treatment in the Barclays' solus accounts, i.e. marked to market through the income statement.
- 6.3.4 The Stock Loan and any payments under the Stock Loan (in respect of the Collateral and the manufactured payments representing the coupons on the ILGs) will be eliminated on consolidation as an intra-group transaction.

6.4 Barclays Consolidated US GAAP

- 6.4.1 BBPLC reports under US GAAP only on a consolidated basis.
- 6.4.2 On initial recognition, BBPLC will classify the ILGs as Trading Securities in accordance with FAS 115 and measure them at fair value with changes in fair value recorded in earnings.
- 6.4.3 Each TRS is a derivative and will be measured at fair value with changes in fair value recorded in earnings.

7. CREDIT & MARKET RISK

- 7.1 During the period of the Transaction, Barclays will have a credit exposure to the UK Government on the ILGs.
- 7.2 The market risk exposure will be managed by PMD, who will mark appropriate limits to counterparties in respect of the management of this market risk, e.g. TRS, reverse repo or stock loan.

8 REGULATORY CAPITAL

8.1 WRAs

- 8.1.1 WRAs on the investment in ILGs are ordinarily weighted at 10%.
- 8.1.2 For the purposes of the Transaction it may be possible to weight the ILG positions at nil by netting the net the long position in BAIL against the short position in Barclays. This is the case since both the long and short positions are reported in the banking book.
- 8.1.3 PMD will report any WRAs associated with managing the market risk on the ILGs.

8.2 Large Exposures

- 8.2.1 The ILGs are exempt.
- 8.2.2 BAIL is a solo-consolidated subsidiary and hence the Prefs will not give rise to any internal large exposure.

8.3 Basel II analysis

- 8.3.1 As under Basel I (see 8.1.1) ordinarily an unhedged ILG position would attract WRAs but the weighting would be dependent on the applicable loss given default ("LGD") and probability of counterparty default ("PD") values applicable to the ILGs. Basel II, as under Basel I, permits the netting of the long position in BAIL and the short position in Barclays (see 8.1.2) and nil WRAs will be applicable.

8.3.2 The large exposures on ILGs will remain exempt.

8.3.3 BAIL will continue to be solo consolidated subject to confirmation to the FSA stating that it will satisfy the underlying conditions required under BIPRU 2.1 (refer to the analysis attached in Annex 3).

9. PROVISION

9.1 SCM propose a provision equal to 30% of the tax deduction attributable to the RPI-linked adjustment made to the carrying value of the ILGs described in Section 4.1.2 above.

10. CLIENT ENGAGEMENT

10.1 N/A

11. MATERIALITY OF DEAL FOR COUNTERPARTY

11.1 N/A

12. Other

12.1 NPSO approval is not required for Project Berry.

Annex 1

1. The ILGs will be acquired to satisfy the "sterling stock liquidity"¹ requirements imposed upon the group by the FSA as well as to guarantee and collateralise various clearing and payment obligations of the firm ("**Liquidity Requirement**")². The responsibility for managing the Liquidity Requirement rests with the Barclays Treasury function, although the day-to-day management of this is delegated to the Portfolio Management Desk (the "**PMD**"). The ILGs would therefore be acquired and held in order to meet Barclays specific regulatory/legal and commercial requirements.
2. Liquidity management within the Barclays group involves maintaining a portfolio of highly marketable assets ("**Eligible Securities**") that can easily be liquidated as protection against any unforeseen interruption to cash flow. Eligible Securities are defined by the Bank of England on its web site and include Gilts and ILGs. A summary as at 16 May 2006 is attached at Annex 2. It is noteworthy that this list does not include Japanese or US government securities which make up a large part of the market for government securities. There are other requirements that may limit the proportion of particular securities that are held as part of the Liquidity Requirement³. These include the fact that firms are not permitted to hold more than 25% of their eligible securities from any one issuer.
3. Barclays' 2005 Accounts provide a breakdown of securities held as part of the Group's treasury management portfolio for asset and liability liquidity and regulatory purposes as at 31st December 2005. PMD currently manages some £14.9bn of bonds issued by the UK and other governments. The fact that high quality liquid assets have to be retained as part of the Liquidity Requirement necessarily means that the return on these assets is generally sub-optimal in terms of returns on balance sheet and equity when compared to other activities in which the firm engages.
4. Typically, U.K. Gilts (including the ILGs) trade more expensively than other European government bonds in part because of the structural 'demand side' requirements of the U.K. pension and life insurance industry who buy gilts to match their long term liabilities. In addition, Gilts issued by the U.K. government have a higher credit rating than bonds issued by other European governments (for example Greece is A- and Italy is A+ by S&P) which also causes them to be higher yielding but with more perceived risk of default than gilts and ILGs which are AAA rated⁴.
5. In choosing to invest in ILGs in the Transaction (as opposed to (say) other government securities including non index linked gilts), a number of factors not least the credit rating and the yield will require consideration, and the decision will to some extent be influenced by the fact that holding ILGs provides an ancillary tax benefit.
6. The Bank of England while managing its official rate may through the open market operations ("**OMOs**") enter into repo transactions ("**Bank of England Repos**") over high quality bonds such as the ILGs. The ILGs may be used by Barclays to participate in the OMOs.

¹ For UK incorporated retail banks where 'sterling retail deposits at call or on short notice dominate their liabilities, not all of which in practice are withdrawn on their contractual maturity. This 'stickiness' leads to apparently large mismatches at shorter maturities. For these banks holding an appropriate stock of sterling liquidity against an unexpected loss of funding is...important' LS Section 1 Page2 Section 3 FSA IPRU (Interim Prudential Source Book) January 2005.

² (The liquidity tests refer to assets under consolidated accounting principles).

³ "In considering the adequacy of a UK incorporated bank's stock of sterling liquid assets, the FSA also has regard to the degree of diversification of those holdings and the bank's ability to mobilise them quickly and discretely when required (so as not to alert the market to a possible crisis).

⁴ By way of illustration an article on Bloomberg on 9th November 2005 reported that S&P were considering a cut in Italy's AA- credit rating. Jean Claude Trichet, the ECB President, stated that ECB policy was not to accept bonds as collateral with a rating of A-. This was expected to further increase yields on these bonds, relative to Gilts. PMD retains assets eligible for acceptance by the Bank of England (which generally has a slightly higher standard than the European Central Bank ("**ECB**")).

Annex 2

Eligible Securities

- Gilts (including gilt strips)
- Sterling Treasury bills
- Bank of England euro bills and euro notes
- HM Government non-sterling marketable debt
- Sterling-denominated securities issued by European Economic Area (EEA) central governments and central banks and major international institutions which are described in the following lists:
- List of eligible sterling-denominated international securities issued directly into CREST
- List of eligible sterling-denominated international securities issued directly into Euroclear and Clearstream, Luxembourg
- Euro-denominated securities (including strips) issued by EEA central governments and central banks and major international institutions where they are eligible for use in ESCB monetary policy operations and which are described in the following lists. These securities may either be those issued directly into Euroclear and Clearstream, Luxembourg or may be "CCBM securities" where the central bank in the country in which the relevant securities were issued has agreed to act as the Bank's custodian under the Correspondent Central Banking Model (CCBM).
 - List of eligible euro-denominated international securities issued directly into Euroclear and Clearstream, Luxembourg
 - List of eligible euro-denominated CCBM securities
- The above sovereign and supranational securities are subject to the requirement that they are issued by an issuer rated Aa3 (on Moody's scale) or higher by two or more of the ratings agencies (Moody's, Standard and Poor's, and Fitch).

Annex 3

Basel II analysis

Basel II (BIPRU 2.1) requires certain underlying conditions, listed below, to be satisfied for solo consolidation to remain applicable. BAIL will satisfy all the requisite conditions for solo consolidation (detailed below).

1. The speed with which funds can be transferred or liabilities repaid to the firm and the simplicity of the method for the transfer or repayment;

The preference share investment in BAIL will be redeemable at the option of the holder, BBPLC, on two days notice.

2. Whether there are any interests other than those of the firm in the subsidiary undertaking and what impact those other interests may have on the firm's control over the subsidiary undertaking and on the ability of the firm to require a transfer of funds or repayment of liabilities

Not applicable as BAIL is 100% owned by Barclays Group Holding Limited ("**BGHL**").

3. Whether the prompt transfer of funds or repayment of liabilities to the firm might harm the reputation of the firm or its subsidiary undertakings;

Prompt repayment will not result in any reputational risk as the only asset held, namely the ILGs, will be disposed and all capital will be held internally within BBPLC group settled. The ILGs can be disposed of to PMD. PMD will then manage the sale of the ILGs to the market.

4. Whether there are any tax disadvantages for the firm or the subsidiary undertaking as a result of the transfer of funds or repayment of liabilities;

The subsidiary would be required to dispose of its assets and incur a taxable trading profit or loss which it would have incurred irrespectively on disposal. No unfavourable tax disadvantages will be incurred in BGHL.

5. Whether there are any exchange controls that may have an impact on the transfer of funds or repayment of liabilities;

Not applicable as all assets and funds are denominated in sterling and located within the UK.

6. Whether there are assets in the subsidiary undertaking available either to be transferred or liquidated for the purposes of the transfer of funds or repayment of liabilities;

The ILGs which will be held by BAIL will be liquidated. The ILGs are sufficiently liquid to allow for disposal for purpose of repayment. As noted the above the ILGs can be disposed of on short notice to PMD who will then manage the sale of the ILGs to the market.

7. Whether any regulatory requirements impact on the ability of the subsidiary undertaking to transfer funds or repay liabilities promptly;

None.

8. Whether the purpose of the subsidiary undertaking prejudices the prompt transfer of funds or repayment of liabilities;

BAIL was formed with the principal objective of making investments. This will not prejudice the repayment of funds.

9. Whether the legal structure of the subsidiary undertaking prejudices the prompt transfer of funds or repayment of liabilities;

Not applicable as all capital is currently and in future will be held directly by BGHL.

10. Whether the contractual relationships of the subsidiary undertaking with the firm and other third parties prejudices the prompt transfer of funds or repayment of liabilities;

No existing contractual obligations with the BBPLC group prejudice the prompt repayment of funds. BAIL does not have any contractual commitments with external counterparties outside of the BBPLC group.

11. Whether past and proposed flows of funds between the subsidiary undertaking and the firm demonstrate the ability to make prompt transfer of funds or repayment of liabilities; and

The provision and repayment of funds has in the past taken place over a single business day.

12. Whether the degree of solo consolidation by the firm undermines the FSA's ability to assess the soundness of the firm as a legal entity (taking into account any other subsidiary undertakings to which BIPRU 2.1 is being applied).

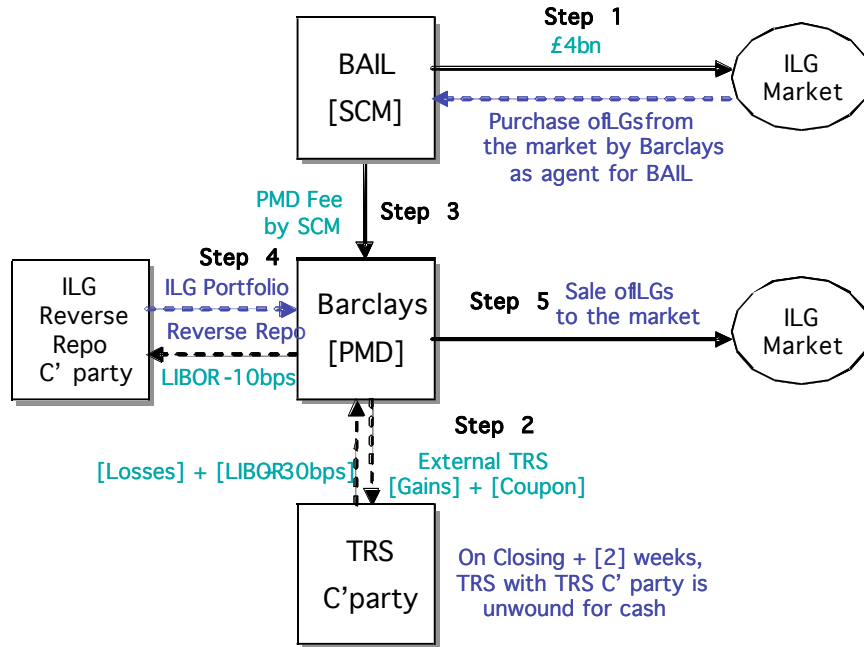
100% ownership by BBPLC and the exclusion of any third party apart from the investment in ILGs indicates a strong degree of solo consolidation.

Annex 4

Transaction Diagrams

Closing (after Pref Issuance)

Closing + 2 weeks (Ignoring Stock Loan)



Post Closing Final Structure

