

MERRILL LYNCH

INTERNATIONAL BANK LIMITED



2004

REPORTS AND FINANCIAL
STATEMENTS FOR THE YEAR
ENDED 31ST DECEMBER 2004



MERRILL LYNCH INTERNATIONAL BANK LIMITED

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**DIRECTORS' REPORT FOR THE YEAR ENDED 31ST DECEMBER 2004**

The directors present their annual report and the audited consolidated financial statements of Merrill Lynch International Bank Limited (the "Company" and, together with its subsidiaries, the "Group") and the audited Company balance sheet for the year ended 31st December 2004.

1. PRINCIPAL ACTIVITY

The principal activity of Merrill Lynch International Bank Limited and its subsidiaries is the provision of domestic and international banking, and global foreign exchange services.

The Group provides private banking services for high and ultra-high net worth clients. These services involve the acceptance of deposits, and the provision of standardised and tailored multi-currency financing and standby letters of credit. The Group also provides loan facilities on a selective basis to corporate clients and accepts deposits from corporate clients and other banks.

Foreign exchange services are provided for clients, both private and corporate, in all major and many minor currencies on the international foreign exchange markets.

The Group provides Swiss Banking services through its subsidiary, Merrill Lynch Bank (Suisse) SA. These include securities trading and custody, portfolio management, foreign exchange, fiduciary deposits, and lending services.

On 29th October 2004 the Company acquired Majestic Acquisitions Limited and its subsidiaries ("Majestic"), a company incorporated in the United Kingdom. Majestic is a mortgage lender, administrator, arranger and servicer in the United Kingdom's non-conforming residential mortgage market.

The Company operates seven overseas branches. The main branch operates in Singapore and provides private banking services to clients located in the Far East.

The Company is an authorised institution under the Financial Services and Markets Act 2000.

2. RESULTS

The profit for the financial year after taxation of \$102.4 million (2003: \$138.9 million) has been transferred to reserves. The balance on reserves carried forward at the year end amounts to \$1,208.0 million (2003: \$1,058.1 million). The directors do not recommend the payment of a dividend for the year on the ordinary shares or non-cumulative preference shares of the Company (2003: \$nil).

3. BOARD OF DIRECTORS

The board of directors at the year end comprised:

K.V. Watts (<i>Chairman</i>)	Appointed 19th May 2004 Served until 31st December 2004	M.J. D'Souza	
A.A. Abbas		M.J. Hale	Appointed 14th October 2004
N. Azam	Appointed 11th November 2004	H.W. Lengsfeld II	Served until 24th February 2005
A.G. Braithwaite III		R.J. Lofaso	
M. Butler	Appointed 21st April 2004	S.J. Patriarco	
I. Chivers		K. Pearson	Appointed 20th April 2004
D.C. Cochran	Appointed 18th June 2004	R.C.M. Wigley	Appointed 5th November 2004
		J.E. Wright	Served until 8th February 2005

**DIRECTORS' REPORT FOR THE YEAR ENDED 31ST DECEMBER 2004**

BOARD OF DIRECTORS (continued)

Other directors who served during the year:

D.B. Gendron	Served until 21th April 2004
R. Yu, Jr.	Served until 22nd January 2004

Changes to the board since the year end:

R.C.M. Wigley	Became Chairman with effect from 1st January 2005
O. Semerci	Appointed on 22nd February 2005

The directors had no beneficial interests in the shares of the Company or any other United Kingdom group company at any time during the year.

4. EMPLOYMENT OF DISABLED PERSONS

Applications for employment by disabled persons are fully and fairly considered having regard to the aptitudes and abilities of each applicant. Efforts are made to enable any employees who become disabled during employment to continue their careers within the Company. Training, career development and promotion of disabled persons are, as far as possible, identical to those of other employees who are not disabled.

5. EMPLOYEE INVOLVEMENT

It is Group policy that there should be effective communication with all employees who, subject to practical and commercial considerations, should be consulted on and involved in decisions which affect their current jobs or future prospects.

6. CHARITABLE AND POLITICAL DONATIONS

During the financial year the Company made donations totalling £nil to various registered United Kingdom charities (2003: £3,545). There were no political donations made during the year (2003: £nil).

7. AUDITORS

The Company has elected to dispense with the obligation to appoint auditors annually and, accordingly, Deloitte & Touche LLP shall be deemed to be re-appointed as auditors for a further term under the provisions of section 386(2) of the Companies Act 1985.

BY ORDER OF THE BOARD

For and on behalf of
Merrill Lynch Corporate Services Limited
Company Secretary
London

22nd March 2005

**STATEMENT OF DIRECTORS' RESPONSIBILITIES**

United Kingdom company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and of the profit or loss of the Group for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for the system of internal control, for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF MERRILL LYNCH INTERNATIONAL BANK LIMITED**

We have audited the financial statements of Merrill Lynch International Bank Limited (the "Company") and its subsidiaries (together the "Group") for the year ended 31st December 2004 which comprise the profit and loss account, the balance sheets, the statement of total recognised gains and losses and the related notes 1 to 25. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As described in the statement of directors' responsibilities, the Company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibility is to audit the financial statements in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We read the directors' report and the other information contained in the annual report for the above year as described in the contents section and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with United Kingdom auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31st December 2004 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
London

22nd March 2005

**CONSOLIDATED PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER 2004**

		Group	
	Notes	2004 \$ 000	2003 \$ 000
Interest receivable			
– Interest receivable and similar income arising on debt securities		62,507	43,966
– Other interest receivable and similar income	2	300,625	269,494
Interest payable	2	(248,956)	(202,273)
Net interest income		114,176	111,187
Fees and commissions receivable		150,143	122,187
Fees and commissions payable		(90,936)	(69,453)
Dealing profits		209,375	216,124
Other operating income		173,897	171,741
Operating income		556,655	551,786
– Earned from continuing operations		552,193	551,786
– Earned from acquisitions		4,462	—
Administrative expenses		(435,773)	(416,575)
Depreciation and amortisation		(4,175)	(5,260)
Provisions for bad and doubtful debts	9	(2,634)	1,994
Operating profit	3	114,073	131,945
– From continuing operations		117,836	131,945
– From acquisitions		(3,763)	—
Profit on disposal of banking business of branch	3	—	16,049
Profit on ordinary activities before taxation		114,073	147,994
Tax on profit on ordinary activities	4	(11,719)	(9,051)
Profit on ordinary activities after taxation and retained for the year	20	102,354	138,943

All results arise from continuing activities.

Other movements in shareholders' funds are set out in Note 20.

The notes on pages 9 to 36 form part of these financial statements.

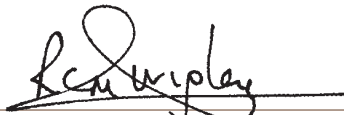
CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES FOR THE YEAR ENDED 31ST DECEMBER 2004

	Group	
	2004 \$ 000	2003 \$ 000
Profit for the financial year	102,354	138,943
Currency translation differences on foreign currency net investment	47,513	35,357
Total recognised gains and losses for the year	149,867	174,300


CONSOLIDATED BALANCE SHEET AS AT 31ST DECEMBER 2004

		Group	
		2004	2003
		\$ 000	\$ 000
ASSETS			
Cash and balances at central banks		409,029	277,179
Loans and advances to banks	10	2,908,999	1,547,771
Loans and advances to customers not subject to securitisation		9,787,822	10,432,238
Loans and advances to customers subject to securitisation	11	1,675,012	—
Less: non-recourse finance	11	(1,561,018)	—
Loans and advances to customers	10	9,901,816	10,432,238
Debt securities	12	3,307,805	2,493,343
Intangible fixed assets	13	114,006	247
Tangible fixed assets	15	8,227	7,155
Other assets		411,274	176,697
Taxation		7,590	2,603
Prepayments and accrued income		3,220,804	2,786,073
Total assets		<u>20,289,550</u>	<u>17,723,306</u>
LIABILITIES			
Deposits by banks	16	811,017	2,296,223
Customer accounts	16	11,747,953	9,712,744
Other liabilities		735,674	550,181
Taxation		10,012	-
Accruals and deferred income		4,356,542	3,056,774
Provisions for liabilities and charges			
– Deferred taxation	17	1,205	104
Subordinated liabilities including convertible debt	18	869,555	749,555
Shareholders' funds including non-equity interests			
– Called up share capital	19	549,435	299,435
– Share premium account	20	156	156
– Capital contribution	20	325,000	325,000
– Profit and loss account	20	883,001	733,134
	20	1,757,592	1,357,725
Total liabilities		<u>20,289,550</u>	<u>17,723,306</u>
MEMORANDUM ITEMS			
Contingent liabilities: Guarantees and assets pledged as collateral security	21	1,849,015	839,558
Commitments	21	16,529,347	16,809,776

The financial statements on pages 6 to 36 were approved by the Board of Directors on 22nd March 2005 and signed on their behalf by:


 Robert Wigley


 Martin Butler

The notes on pages 9 to 36 form part of these financial statements.




COMPANY BALANCE SHEET AS AT 31ST DECEMBER 2004

		Group	
		2004	2003
		\$ 000	\$ 000
ASSETS			
Cash and balances at central banks		220,324	187,647
Loans and advances to banks	10	3,341,579	1,931,003
Loans and advances to customers not subject to securitisation		8,667,085	9,420,196
Loans and advances to customers subject to securitisation		873,266	—
Less: non-recourse finance		(799,042)	—
Loans and advances to customers	10	8,741,309	9,420,196
Debt securities	12	3,295,962	2,469,441
Shares in group undertakings	24	153,531	21,561
Tangible fixed assets	15	2,283	3,398
Other assets		391,217	168,936
Taxation		8,316	—
Prepayments and accrued income		3,065,340	2,599,887
Deferred taxation	17	16,629	15,698
Total assets		<u>19,236,490</u>	<u>16,817,767</u>
LIABILITIES			
Deposits by banks	16	809,600	2,229,971
Customer accounts	16	11,306,847	9,382,860
Other liabilities		640,737	419,317
Taxation		9,761	2,564
Accruals and deferred income		4,247,223	3,005,083
Subordinated liabilities including convertible debt	18	869,555	749,555
Shareholders' funds including non-equity interests			
– Called up share capital	19	549,435	299,435
– Share premium account	20	156	156
– Capital contribution	20	325,000	325,000
– Profit and loss account	20	478,176	403,826
	20	<u>1,352,767</u>	<u>1,028,417</u>
Total liabilities		<u>19,236,490</u>	<u>16,817,767</u>
MEMORANDUM ITEMS			
Contingent liabilities: Guarantees and assets pledged as collateral security	21	1,734,600	828,623
Commitments	21	16,561,344	17,058,274

The financial statements on pages 6 to 36 were approved by the Board of Directors on 22nd March 2005 and signed on their behalf by:


Robert Wigley


Martin Butler

The notes on pages 9 to 36 form part of these financial statements.

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004****1. Accounting Policies****Basis of Accounting**

The financial statements have been prepared in accordance with applicable United Kingdom law and accounting standards, and Statements of Recommended Practice issued by the British Bankers' Association.

Accounting Period

The Group's financial year consisted of a fifty-three (2003: fifty-two) week period ending on the last Friday in December (2003: 26th December).

Accounting Convention

The financial statements have been prepared on the historical cost basis of accounting modified by the revaluation of certain assets and in accordance with the special provisions of Part VII Schedule 9 of the Companies Act 1985 relating to banks and banking companies. As permitted by section 230(3) of the Companies Act 1985, the Company does not present its profit and loss account. The Company's profit for the year was \$73.6 million (2003: \$127.1 million). Certain reclassifications and format changes have been made to prior year amounts to conform to the current year presentation.

Basis of Consolidation

The financial results of all subsidiary undertakings have been included in the consolidated financial statements. All subsidiary undertakings have been accounted for under acquisition accounting principles. Goodwill arising on consolidation of subsidiary undertakings, being the excess of the cost of the investment over the fair value of the Group's share of separable net assets at the date of acquisition, is capitalised and amortised over a twenty year period reflecting its useful economic life.

Cash Flow Statement

In accordance with FRS 1 (Revised) the Company has not prepared a cash flow statement. A consolidated cash flow statement is contained in the consolidated financial statements of the ultimate parent company Merrill Lynch & Co., Inc.

Loans

Loans are stated in the balance sheet at the principal amount outstanding net of any provisions for loan losses. Interest income on loans is accrued and credited to interest income at the actual interest rates applicable to the loan principal amounts outstanding.

The recognition of interest ceases when the payment of interest is in doubt and does so automatically if interest payments are 60 days or more overdue. At the same time, any interest previously accrued but not received on such a loan is reversed. Thereafter interest is included in income only when it is received. Loans are returned to the accruals basis only when doubt about collectibility of interest has been removed.

Fees and commissions are accrued when services for the transactions are substantially completed.

Loss Provisions

Specific provisions for loan losses are made when management considers the repayment of loan principal is in doubt and, in the case of other loss provisions, when it is determined that an asset has been impaired or a liability has been incurred.

Provisions made during the year are charged as a separate amount in the profit and loss account and deducted from loans and advances. Loans are written off when the extent of any loss has been confirmed.

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004** (continued)**1. Accounting Policies** (continued)**Translation of Foreign Currencies**

The financial statements are presented in US dollars, which is the Company's functional currency. Monetary assets and liabilities arising from transactions to be settled in currencies other than US dollars are translated at the market rates of exchange ruling at the balance sheet date. Transactions denominated in foreign currencies are translated into US dollars at the rates ruling at the dates of the transactions. Goodwill and tangible fixed assets denominated in foreign currencies for which there are matching foreign currency liabilities are translated into US dollars at the rates ruling at the balance sheet date. Gains and losses resulting from the translation of the opening and closing net assets of overseas subsidiaries are taken directly to reserves. All other exchange differences are included in the profit and loss account.

Depreciation

Depreciation is provided on tangible fixed assets on a straight-line basis by reference to the cost of the asset and its useful economic life at the following rates:

Motor vehicles	4 years
Computer equipment	3 years
Fixtures and fittings	3-10 years

Deferred Taxation

Deferred tax is recognised as a liability or an asset if, prior to the balance sheet date, the Company or the Group has entered into transactions or events have occurred that give rise to timing differences giving the Company or the Group an obligation to pay more tax in the future or a right to pay less tax in the future. Deferred tax assets are recognised to the extent that they are regarded as recoverable. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements.

Segmental Reporting

All of the activities of the Group arise from the provision of banking and related services. It is not possible to allocate revenues or assets to any one particular geographical source as any one trade may involve parties situated in a number of different geographical areas.

Pension Costs

The Group participates in a number of defined benefit and defined contribution pension schemes throughout Europe. The schemes are funded with the assets held in separate trustee administered funds.

The major defined benefit scheme is the Merrill Lynch (UK) Pension Plan, (the "Plan"; formerly Merrill Lynch (UK) Final Salary Plan), which was closed to new entrants with effect from 30th June 1997 and to contributions from existing members with effect from 30th June 2004. The funding cost relating to the Plan is assessed in accordance with the advice of independent qualified actuaries using the projected unit method. The Group is one of a number of Merrill Lynch employers based in the United Kingdom which participate in the Plan. The Group has been unable to identify its share of the underlying assets and liabilities of the Plan and accordingly accounts for the Plan as if it were a defined contribution scheme.

The Merrill Lynch (UK) Defined Contribution Plan is a defined contribution scheme the funding of which is set out in the rules of that plan.

The costs of defined contribution schemes are a percentage of each employee's annual salary based on their age and length of service with the Group and are charged to the profit and loss account in the period in which they fall due.


NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

1. Accounting Policies (continued)

Fiduciary Assets

Assets held in a trust or fiduciary capacity are not assets of the Group and accordingly are not included in the financial statements.

Shares in Group Undertakings

Shares in Group undertakings are stated at cost less provision for impairment.

Debt Securities

Investment securities held by the Group are stated at cost adjusted for amortisation of premiums and discounts to redemption less provisions for impairment. Other securities are held at market bid price.

Derivatives

Derivative items include forward rate agreements, interest rate swaps, currency swaps, foreign currency options, forward foreign exchange contracts and financial futures. These items are predominantly held as trading instruments and are valued on a mark-to-market basis with the differences between the fair value at the balance sheet date and the contract price being taken to the profit and loss account as operating income. Where the Group has entered into legally binding netting agreements, positive and negative values of derivatives are offset within the balance sheet totals. Hedging instruments are valued on a consistent basis with the assets, liabilities or positions, which are the subject of the hedge. Profits and losses on hedge transactions are recognised on a basis consistent with the transactions to which they apply.

Securitisations

In order to refinance existing assets the Group sells loans to special purpose securitisation companies under non-recourse finance arrangements. These companies are funded primarily through the issue of mortgage backed floating rate notes. Where the conditions for linked presentation are met, the outstanding amounts of the floating rate notes, to the extent that there is no recourse to the Group, are presented as "non-recourse finance" in the balance sheet and shown deducted from the outstanding securitised assets, which are presented as "Loans and advances to customers subject to securitisation" in the balance sheet.

2. Net Interest Income

Net interest income includes:

	2004 \$ 000	2003 \$ 000
Other interest receivable and similar income:		
Intercompany	42,696	26,937
Other	257,929	242,557
	<u>300,625</u>	<u>269,494</u>
Interest payable:		
Intercompany	(18,318)	(16,522)
Other	(205,557)	(175,068)
Interest on subordinated debt – to immediate parent company	(3,908)	(3,458)
– to ultimate parent company	(21,173)	(7,225)
	<u>(248,956)</u>	<u>(202,273)</u>



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

3. Consolidated Profit on Ordinary Activities Before Taxation

Consolidated profit on ordinary activities before taxation is stated after crediting/(charging):

	2004 \$ 000	2003 \$ 000
Intercompany service fee income	171,468	172,070
Intercompany service fee expense	(102,946)	(125,381)
Auditors' remuneration:		
– annual audit of the Company	(924)	(781)
– annual audit of subsidiaries	(289)	(270)
Profit on disposal of banking business of German branches following an agreement entered into on 28th October 2003	—	16,049

4. Tax on Profit on Ordinary Activities

(a) Analysis of charge in year

	2004 \$ 000	2003 \$ 000
Current tax		
United Kingdom corporation tax on profits of the year of 30% (2003:30%)	4,481	10,383
Double tax relief	(4,481)	(10,383)
Adjustment in respect of previous years	1,045	(4,206)
	<u>1,045</u>	<u>(4,206)</u>
Foreign tax	11,618	17,695
Total current tax (see note (b) on the following page)	<u>12,663</u>	<u>13,489</u>
Deferred tax		
Origination and reversal of timing differences	(944)	(4,438)
Tax on profit on ordinary activities	<u>11,719</u>	<u>9,051</u>


NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

4. Tax on Profit on Ordinary Activities (continued)

(b) Factors affecting tax charge for year

The tax assessed for the year is lower than the standard rate of corporation tax of 30% (2003: 30%) in the United Kingdom.

The differences are explained below:

	2004 \$ 000	2003 \$ 000
Profit on ordinary activities before tax	114,073	147,994
Profit on ordinary activities multiplied by standard rate of corporation tax in the United Kingdom of 30% (2003: 30%)	34,222	44,399
Effects of:		
Tax losses received by the Group for no payment	(16,899)	(35,499)
Expenses not deductible for tax purposes	1,172	761
Income not taxable	(4,151)	—
Depreciation for year in excess of capital allowances	(170)	379
Timing differences relating to compensation and social security costs	(3,806)	6,314
Impact of foreign taxes	560	1,413
Movement in other timing differences	690	(700)
Adjustment to tax charge in respect of previous years	1,045	(3,578)
Current tax charge for year (see note (a) on previous page)	<u>12,663</u>	<u>13,489</u>

5. Assets and Liabilities Denominated in US Dollars and Other Currencies

	Group 2004 \$ 000	Group 2003 \$ 000	Company 2004 \$ 000	Company 2003 \$ 000
ASSETS				
Denominated in US dollars	12,969,137	12,476,168	12,895,851	12,010,961
Denominated in other currencies	<u>7,320,413</u>	<u>5,247,138</u>	<u>6,340,639</u>	<u>4,806,806</u>
	<u>20,289,550</u>	<u>17,723,306</u>	<u>19,236,490</u>	<u>16,817,767</u>
LIABILITIES				
Denominated in US dollars	12,864,391	12,480,340	13,252,360	12,015,133
Denominated in other currencies	<u>7,425,159</u>	<u>5,242,966</u>	<u>5,984,130</u>	<u>4,802,634</u>
	<u>20,289,550</u>	<u>17,723,306</u>	<u>19,236,490</u>	<u>16,817,767</u>



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

6. Directors and Employees

Directors' and employees' costs comprise:

	2004 \$ 000	2003 \$ 000
Salaries and benefits	179,070	175,775
Social security costs	13,442	11,213
Other pension costs	8,781	9,013
	<u>201,293</u>	<u>196,001</u>

The average number of persons (including directors) employed by the Group during the year was 1,142 (2003: 1,168). All were employed in the provision of domestic and international banking and global foreign exchange services.

Of the directors that served during the year ten (2003: ten) directors were remunerated by this Company and the amounts included are those relating to their services as directors for this Company based on an estimated time allocation basis. Emoluments in relation to services performed for other group companies are not disclosed in this Company's financial statements.

Remuneration paid to directors of the Company was:

	2004 \$ 000	2003 \$ 000
Emoluments	3,063	2,959
Contributions to defined contribution pension schemes	50	20
Benefits received under long term incentive schemes	353	221

Number of directors during the year:

	2004 No.	2003 No.
Whom exercised Merrill Lynch & Co. share options	3	1
By whom Merrill Lynch & Co shares are receivable or have been received under long term incentive schemes	10	10
Whom were members of a defined benefit pension scheme	8	4
Whom were members of a defined contribution pension scheme	10	6

Highest paid director:

	2004 \$ 000	2003 \$ 000
Total emoluments	1,363	993
Benefits received under long term incentive schemes	112	43
Contributions to defined contribution pension schemes	21	4
Accrued annual pension as at year end	76	—

The highest paid director received Merrill Lynch & Co shares in the current year and did not exercise Merrill Lynch & Co share options.


NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

7. Pension Costs

The latest actuarial assessment of the Merrill Lynch (UK) Pension Plan, (the "Plan"; formerly Merrill Lynch (UK) Final Salary Plan) was as at 1st January 2003. That assessment showed that the Plan had a deficit of £25.7 million. In addition to the contributions required to meet the cost of future benefits accruing, the employing companies have decided, based on actuarial advice and after discussion with the Trustee, to make additional contributions of £2.5 million per annum (increasing in line with price inflation) over the next 13 years (2003: additional contribution of £2.5 million and a one off payment of £8.5 million).

The pension cost for the period was \$4 million (2003: \$2 million) in respect of the defined benefit schemes and \$5 million (2003: \$7 million) in respect of defined contribution schemes.

8. Related Party Transactions

At 31st December 2004, the amount outstanding in relation to transactions, arrangements and agreements entered into by the Company with directors and connected persons was \$500,000 (2003: \$378,900) in respect of a letter of credit provided to one director.

There were no other transactions requiring disclosure under the Companies Act 1985 or FRS 8. Under Paragraph 3(c) of FRS 8 - Related Party Disclosures the Company is exempt from the requirements to disclose transactions with other group companies.

9. Provisions for Bad and Doubtful Debts

	Group 2004 \$ 000	Group 2003 \$ 000	Company 2004 \$ 000	Company 2003 \$ 000
At start of year	8,496	10,490	8,496	10,490
Charged/(credited) to profit and loss account	2,634	(1,994)	2,086	(1,994)
Irrecoverable amounts written off	(234)	—	(234)	—
At end of year	<u>10,896</u>	<u>8,496</u>	<u>10,348</u>	<u>8,496</u>

The provisions above relate to loans and advances to customers.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

10. Loans and Advances

	Group 2004 \$ 000	Group 2003 \$ 000	Company 2004 \$ 000	Company 2003 \$ 000
Loans and advances to banks				
Repayable on demand	—	87,687	—	87,687
Remaining maturity:				
– over 5 years	13,525	—	13,771	—
– 5 years or less but over 1 year	—	—	40,633	26,503
– 1 year or less but over 3 months	157,421	356,265	389,689	598,419
– 3 months or less excluding on demand	<u>2,738,053</u>	<u>1,103,819</u>	<u>2,897,486</u>	<u>1,218,394</u>
	<u>2,908,999</u>	<u>1,547,771</u>	<u>3,341,579</u>	<u>1,931,003</u>
Amounts include due from subsidiary undertakings			<u>518,987</u>	<u>430,232</u>
Loans and advances to customers				
Repayable on demand	325,027	2,351,237	103,852	2,157,635
Remaining maturity:				
– over 5 years	841,204	132,609	801,934	132,609
– 5 years or less but over 1 year	239,084	393,915	198,178	367,163
– 1 year or less but over 3 months	1,581,901	1,818,051	1,237,758	1,503,239
– 3 months or less excluding on demand	6,925,497	5,744,922	6,409,935	5,268,046
Specific bad and doubtful debt provisions (see note 9)	<u>(10,897)</u>	<u>(8,496)</u>	<u>(10,348)</u>	<u>(8,496)</u>
	<u>9,901,816</u>	<u>10,432,238</u>	<u>8,741,309</u>	<u>9,420,196</u>

11. Loans and Advances to Customers Subject to Securitisation

Loans and advances to customers include mortgage loans which are subject to non-recourse finance arrangements. These loans have been sold to special purpose securitisation companies, Mortgages No 3 plc, Mortgages No 4 plc, Mortgages No 5 plc and Mortgages No 6 plc, which are ultimately beneficially owned by charitable trusts, and have been funded primarily through the issue of floating rate notes. No gain or loss has been recognised as a result of these sales. The special purpose securitisation companies are consolidated as quasi-subidiaries.

Holders of the floating rate notes are only entitled to obtain payment of principal and interest to the extent that the resources of the securitisation companies (as listed above) are sufficient to support such payments, and the holders of the floating rate notes have no recourse in any other form. The priority and amount of claims on the proceeds generated by the assets are determined in accordance with a strict priority of payments.


NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

11. Loans and Advances to Customers Subject to Securitisation (continued)

The Group is entitled to receive payment of deferred consideration for the sale of the mortgage loans. As part of the deferred consideration, the Group is entitled to receive any residual amounts less a predetermined amount of the principal amount outstanding of the floating rate notes on each interest determination date. The Group is also entitled to receive mortgage redemption penalty interest on the securitised loans.

The Group has no right or obligation to repurchase the benefit of any securitised loan except if certain representations and warranties given by the Group at the time of transfer are breached. The Group also has no right or obligation to financially support any of the securitisation companies and does not intend to do so.

The Group does not own directly or indirectly any of the share capital of the securitisation companies listed above or their parents.

Securitisation Company	Date of Securitisation	Gross Assets Securitised \$ 000	Non-recourse Finance \$ 000
Mortgages No 3 plc	27th November 2001/25th January 2002	109,599	98,119
Mortgages No 4 plc	28th November 2002/28th February 2003	184,777	171,950
Mortgages No 5 plc	8th July 2003/31st July 2003	259,824	244,362
Mortgages No 6 plc	7th December 2004/8th December 2004	1,120,812	1,046,587
		<u>1,675,012</u>	<u>1,561,018</u>

Summarised combined profit and loss accounts for the periods and combined balance sheets as at 31st December 2004 and 26th December 2003, for the above companies, which have been consolidated into the Group as quasi-subidiaries using linked presentation, are set out below:

	2004 \$ 000	2003 \$ 000
Profit and loss account for the period ended 31st December 2004		
Net interest income	1,958	—
Other income	5,651	—
Operating income	7,609	—
Administrative expenses	(5,214)	—
Provisions for bad and doubtful debts	(2,387)	—
Operating profit	8	—
Tax on profit on ordinary activities	(2)	—
Profit on ordinary activities after taxation	<u>6</u>	<u>—</u>



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

11. Loans and Advances to Customers Subject to Securitisation (continued)

	2004	2003
	\$ 000	\$ 000
Balance sheet as of 31st December 2004		
Cash and balances at central banks	103,683	—
Loans and advance to customers	1,675,012	—
Other assets	7,201	—
Prepayments and accrued income	481	—
Total assets	<u>1,786,377</u>	<u>—</u>
Deposits by banks	1,850	—
Other liabilities	7,156	—
Accruals and deferred income	19,815	—
Debt securities in issue	1,757,294	—
Share capital	145	—
Profit and loss account	117	—
Total liabilities	<u>1,786,377</u>	<u>—</u>

The above securitisation companies became part of the Group on the acquisition of Majestic Acquisitions Limited on 29th October 2004 (see note 14).



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

12. Debt Securities

	Book Value 2004 \$ 000	Market Value 2003 \$ 000	Book Value 2004 \$ 000	Market Value 2003 \$ 000
Group				
Listed: Government securities	1,483,212	1,487,131	570,780	571,303
Unlisted securities:				
Bank and Building Society Certificates of Deposit	1,805,018	1,805,018	1,922,563	1,922,563
Bonds	19,575	19,575	—	—
	<u>3,307,805</u>	<u>3,311,724</u>	<u>2,493,343</u>	<u>2,493,866</u>
Maturity				
Due within one year	3,288,230	3,292,149	2,474,363	2,474,886
Due one year and over	19,575	19,575	18,980	18,980
	<u>3,307,805</u>	<u>3,311,724</u>	<u>2,493,343</u>	<u>2,493,866</u>
Company				
Listed: Government securities	1,483,212	1,487,131	558,895	559,418
Unlisted securities:				
Bank and Building Society Certificates of Deposit	1,805,018	1,805,018	1,910,546	1,910,546
Bonds	7,732	7,732	—	—
	<u>3,295,962</u>	<u>3,299,881</u>	<u>2,469,441</u>	<u>2,469,964</u>
Maturity				
Due within one year	3,288,230	3,292,149	2,469,441	2,469,964
Due one year and over	7,732	7,732	—	—
	<u>3,295,962</u>	<u>3,299,881</u>	<u>2,469,441</u>	<u>2,469,964</u>

The Company does not trade in debt securities and instruments are held for investment.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

13. Intangible Fixed Assets

	\$ 000
Group	
Goodwill Cost	
At start of year	6,594
Additions	108,934
Exchange translation	6,030
At end of year	<u>121,558</u>
Amortisation	
At start of year	6,347
Charge for the year	1,205
At end of year	<u>7,552</u>
Net Book Value	
At end of year	<u>114,006</u>
At start of year	<u>247</u>

14. Summary of the Effect of Acquisitions

The following table summarises the effect of the acquisition of Majestic Acquisitions Limited and its subsidiaries on 29th October 2004:

	Book Value Before Acquisition \$ 000	Fair Value Adjustments \$ 000	Fair Value at Acquisition \$ 000
Cash and balances at central banks	33,629	—	33,629
Loans and advances to customers not subject to securitisation	1,266,139	—	1,266,139
Loans and advances to customers subject to securitisation	612,397	—	612,397
Non-recourse finance	(572,210)	—	(572,210)
Debt securities	76	—	76
Tangible fixed assets	1,993	(302)	1,691
Other assets	8,495	—	8,495
Prepayments and accrued income	22,989	—	22,989
Deposits by banks	(1,325,175)	—	(1,325,175)
Other liabilities	(5,038)	(293)	(5,331)
Taxation	(1,800)	—	(1,800)
Accruals and deferred income	(17,701)	—	(17,701)
Deferred taxation	(163)	—	(163)
Net assets acquired	<u>23,631</u>	<u>(595)</u>	<u>23,036</u>
Total fair value of the consideration and cost of acquisition			<u>131,970</u>
Goodwill on acquisition of subsidiary undertaking			<u>108,934</u>

Majestic Acquisitions Limited loss after tax for the period 1st April 2004 to 28th October 2004, and for the year ended 31st March 2004, calculated using Majestic Acquisitions Limited's accounting policies, was \$4,018,000 and \$2,830,000, respectively.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

15. Tangible Fixed Assets

	Motor Vehicles \$ 000	Computer Equipment \$ 000	Fixtures and Fittings \$ 000	Total \$ 000
Group				
Cost				
At start of year	311	18,253	31,973	50,537
Acquisition of subsidiary	—	3,284	443	3,727
Additions	197	957	2,301	3,455
Disposals	(279)	(5,401)	(6,048)	(11,728)
Exchange translation	3	1,886	1,266	3,155
At end of year	<u>232</u>	<u>18,979</u>	<u>29,935</u>	<u>49,146</u>
Depreciation				
At start of year	216	17,397	25,769	43,382
Acquisition of subsidiary	—	2,036	—	2,036
Disposals	(247)	(4,682)	(4,503)	(9,432)
Charge for the year	68	1,250	1,652	2,970
Exchange translation	3	1,033	927	1,963
At end of year	<u>40</u>	<u>17,034</u>	<u>23,845</u>	<u>40,919</u>
Net book value				
At end of year	<u>192</u>	<u>1,945</u>	<u>6,090</u>	<u>8,227</u>
At start of year	<u>95</u>	<u>856</u>	<u>6,204</u>	<u>7,155</u>
Company				
Cost				
At start of year	288	6,478	22,595	29,361
Additions	197	34	1,420	1,651
Disposals	(279)	(4,657)	(4,039)	(8,975)
Exchange translation	—	307	163	470
At end of year	<u>206</u>	<u>2,162</u>	<u>20,139</u>	<u>22,507</u>
Depreciation				
At start of year	201	6,138	19,624	25,963
Disposals	(247)	(4,619)	(2,494)	(7,360)
Charge for the year	61	171	898	1,130
Exchange translation	—	316	175	491
At end of year	<u>15</u>	<u>2,006</u>	<u>18,203</u>	<u>20,224</u>
Net book Value				
At end of year	<u>191</u>	<u>156</u>	<u>1,936</u>	<u>2,283</u>
At start of year	<u>87</u>	<u>340</u>	<u>2,971</u>	<u>3,398</u>



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

16. Deposits and Customer Accounts

	Group 2004 \$ 000	Group 2003 \$ 000	Company 2004 \$ 000	Company 2003 \$ 000
Deposits by banks				
Repayable on demand	214,837	309,418	149,014	220,455
With agreed maturity dates or periods of notice by remaining maturity				
– 1 year or less but over 3 months	30,895	36,888	896	23,807
– 3 months or less but not repayable on demand	565,285	1,949,917	659,690	1,985,709
	<u>811,017</u>	<u>2,296,223</u>	<u>809,600</u>	<u>2,229,971</u>
Amounts include due to subsidiary undertakings			<u>119,406</u>	<u>129,139</u>
Customer accounts				
Repayable on demand	3,291,291	3,908,896	2,850,185	3,579,012
With agreed maturity dates or periods of notice by remaining maturity				
– over 5 years	—	10,110	—	10,110
– 5 years or less but over 1 year	20,311	18,663	20,311	18,663
– 1 year or less but over 3 months	340,313	386,719	340,313	386,719
– 3 months or less but not repayable on demand	8,096,038	5,388,356	8,096,038	5,388,356
	<u>11,747,953</u>	<u>9,712,744</u>	<u>11,306,847</u>	<u>9,382,860</u>



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

17. Deferred Taxation

	2004 \$ 000	2003 \$ 000
Company		
Accelerated capital allowances	1,674	2,093
Timing differences relating to compensation and social security costs	6,356	10,889
Other timing differences	8,599	2,716
	<u>16,629</u>	<u>15,698</u>
Group		
Timing differences relating to compensation and social security costs	1,235	1,222
Timing differences relating to reserves	(19,069)	(17,024)
	<u>(1,205)</u>	<u>(104)</u>
MOVEMENT ON DEFERRED TAXATION		
Company		
Balance at start of year	15,698	11,866
Deferred tax charge in profit and loss account relating to current year	(4,037)	5,283
Adjustment in respect of previous years	4,968	(1,451)
	<u>16,629</u>	<u>15,698</u>
Group		
Provision at start of year	(104)	(2,818)
Deferred tax charge in profit and loss account relating to current year	(4,023)	5,889
Adjustment in respect of previous years	4,967	(1,451)
Acquisition of subsidiary	(163)	—
Foreign exchange differences	(1,882)	(1,724)
	<u>(1,205)</u>	<u>(104)</u>

The amount of deferred tax unprovided by the Group for the year ended 31st December 2004 was \$2 million (2003: \$2 million). The amount of deferred tax unprovided by the Company for the year ended 31st December 2004 was \$2 million (2003: \$2 million).

Management is of the opinion that it is more likely than not that the Company will be able to generate future taxable income to recover the deferred tax asset recognised as at the balance sheet date, having considered historic performance.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

18. Subordinated Liabilities Including Convertible Debt**Group and Company**

		2004 \$ 000	2003 \$ 000
Dated loan capital			
2nd November 2010	Drawdown on loan facility of \$600,000,000 bearing interest at 100 basis points above LIBOR	560,000	450,000
31st December 2005	Drawdown on loan facility of \$300,000,000 bearing interest at 100 basis points above LIBOR	160,000	150,000
		<u>720,000</u>	<u>600,000</u>
Convertible dated loan capital			
31st December 2042	Drawdown on loan facility of \$150,000,000 bearing interest at LIBOR, mandatorily convertible into non-cumulative preference shares of par value \$1 each at maturity.	149,555	149,555
Maturity		<u>869,555</u>	<u>749,555</u>
Subordinated liabilities including convertible debt securities in issue are repayable:			
		2004 \$ 000	2003 \$ 000
In 1 year or less		160,000	150,000
In more than 5 years		709,555	599,555
Group and Company		<u>869,555</u>	<u>749,555</u>

The preference shares which will be created under the convertible loan facility are non-voting, except to the extent that the preferential dividend has not been paid, or a resolution is proposed varying the rights of the preference shareholders. The preference shares will pay a fixed dividend of 1 per cent above LIBOR, and are non-redeemable. In the event of a winding-up the preference shares will rank pari passu with any other shares of the Company with regard to the repayment of nominal capital. The holders of the preference shares shall not be entitled to any further participation in the assets over this amount.

Claims in respect of the Group's loan capital are subordinated to the claims of other creditors. None of the Group's capital is secured.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

19. Called Up Share Capital

	Authorised	Authorised	Called Up, Issued and Fully Paid	Called Up, Issued and Fully Paid
	2004	2003	2004	2003
	No.	No.	\$ 000	\$ 000
Ordinary shares of \$1 each	500,000,000	500,000,000	299,435	299,435
Non-cumulative preference shares of \$10 each	50,000,000	—	250,000	—
	<u>550,000,000</u>	<u>500,000,000</u>	<u>549,435</u>	<u>299,435</u>

On the 16th September and 29th October 2004, 10,000,000 and 15,000,000 respectively, of non-cumulative preference shares were issued at par to a fellow Merrill Lynch subsidiary. The holders of the non-cumulative preference shares are entitled to a preferential dividend at the rate of one percent over LIBOR on the nominal capital to the extent that the dividend is declared. Any accrued preferential dividend that remains undeclared or unpaid at the close of the respective calendar year shall not carry forward to the following calendar year and the holder shall have no right to demand payment for such amounts. Out of the profits available for distribution and only if resolved to be distributed, the holder shall be entitled to payment of the preferential dividend in priority to the holders of the ordinary shares.

The preference shares are non-redeemable. On a return of capital on winding-up redemption or repayment of shares or otherwise, the holders of the preference shares shall be entitled in priority to any payment to holders of any other class of shares, to the repayment of a sum equal to the nominal capital paid up or credited as paid up together with a sum equal to all declared but unpaid preferential dividends.

The holder of the non-cumulative preference shares has the right to attend, speak and vote at a general meeting of the Company only if a resolution is to be proposed abrogating, varying or modifying any of the rights or privileges of the holders of the preference shares, or for the winding up of the Company, or for sanctioning the sale of the undertaking of the Company in which case they shall only be entitled to vote on such resolution.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

20. Combined Statement of Movements in Shareholders' Funds and Statement of Movements in Reserves

	Share Capital \$ 000	Share Premium \$ 000	Capital Contribution \$ 000	Profit and Loss Account \$ 000	Total 2004 \$ 000	Total 2003 \$ 000
Group						
At start of year	299,435	156	325,000	733,134	1,357,725	1,183,425
Issue of new shares	250,000	—	—	—	250,000	—
Profit for the year	—	—	—	102,354	102,354	138,943
Translation adjustment	—	—	—	47,513	47,513	35,357
At end of year	<u>549,435</u>	<u>156</u>	<u>325,000</u>	<u>883,001</u>	<u>1,757,592</u>	<u>1,357,725</u>
Company						
At start of year	299,435	156	325,000	403,826	1,028,417	901,411
Issue of new shares	250,000	—	—	—	250,000	—
Profit for the year	—	—	—	73,643	73,643	127,072
Translation adjustment	—	—	—	707	707	(66)
At end of year	<u>549,435</u>	<u>156</u>	<u>325,000</u>	<u>478,176</u>	<u>1,352,767</u>	<u>1,028,417</u>

Profit and loss account consists of retained earnings and accumulated translation adjustments.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

21. Memorandum Items, Foreign Exchange and Interest Rate Contracts

	Contract Amount 2004 \$ 000	Risk Weighted Amount 2004 \$ 000	Contract Amount 2003 \$ 000	Risk Weighted Amount 2003 \$ 000
Group				
Contingent liabilities				
Guarantees and irrevocable letters of credit	363,436	301,873	280,663	266,621
Assets pledged as collateral security	1,485,579	148,321	558,895	55,889
Total contingent liabilities	<u>1,849,015</u>	<u>450,194</u>	<u>839,558</u>	<u>322,510</u>
Commitments				
Forward deposits placed	391,354	—	528,274	—
Undrawn formal standby facilities, credit lines and other commitments to lend:				
– 1 year and over	661,837	109,648	102,352	51,175
– less than 1 year	15,476,156	—	16,179,150	—
Total commitments	<u>16,529,347</u>	<u>109,648</u>	<u>16,809,776</u>	<u>51,175</u>
Total memorandum items	<u>18,378,362</u>	<u>559,842</u>	<u>17,649,334</u>	<u>373,685</u>
	2004		2003	
	\$ 000		\$ 000	
Exchange and interest rate contracts				
Exchange rate contracts:				
Notional value	655,089,122		539,749,407	
Risk weighted amount	2,070,525		1,741,919	
Replacement cost	12,193,485		8,410,436	
Interest rate contracts:				
Notional value	20,596,244		8,039,413	
Risk weighted amount	54,454		3,537	
Replacement cost	30,076		4,092	



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

21. Memorandum Items, Foreign Exchange and Interest Rate Contracts (continued)

	Contract Amount 2004 \$ 000	Risk Weighted Amount 2004 \$ 000	Contract Amount 2003 \$ 000	Risk Weighted Amount 2003 \$ 000
Group				
Contingent liabilities				
Guarantees and irrevocable letters of credit	251,387	251,207	269,728	264,432
Assets pledged as collateral security	1,483,213	148,321	558,895	55,889
Total contingent liabilities	<u>1,734,600</u>	<u>399,528</u>	<u>828,623</u>	<u>320,321</u>
Commitments				
Forward deposits placed	423,351	—	776,772	—
Undrawn formal standby facilities, credit lines and other commitments to lend:				
– 1 year and over	661,837	109,648	102,352	51,176
– less than 1 year	15,476,156	—	16,179,150	—
Total commitments	<u>16,561,344</u>	<u>109,648</u>	<u>17,058,274</u>	<u>51,176</u>
Total memorandum items	<u>18,295,944</u>	<u>509,176</u>	<u>17,886,897</u>	<u>371,497</u>

	2004 \$ 000	2003 \$ 000
Exchange and interest rate contracts		
Exchange rate contracts:		
Notional value	651,801,714	538,765,973
Risk weighted amount	2,036,397	1,732,092
Replacement cost	12,124,222	8,400,616
Interest rate contracts:		
Notional value	20,596,244	8,039,413
Risk weighted amount	54,454	3,537
Replacement cost	30,076	4,092

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004** (continued)**22. Derivatives and Other Financial Instruments**

Financial instruments are dealt with in both the trading book and non-trading book of the Group. Both trading book and non-trading book activities may expose the Group to various categories of risk. These risks are continually monitored through a comprehensive risk management process. The proper execution of this process leads to effective management of these risks, helping to reduce the likelihood of earnings volatility over time.

The Group, through the operation of its Risk Oversight Committee, monitors and controls all elements of risk within the Group, working in conjunction with the Merrill Lynch & Co., Inc., Corporate Risk Management Group. This Committee reviews reports from the Group's existing Credit, Asset & Liability, Process Risk and Compliance & Regulatory Committees. These Committees identify and monitor risk limits based on recommendations and analysis provided by independent risk management groups who work with the business units in establishing suitable risk profiles for each of the business units.

The initial responsibility in the risk management process rests with the individual business units in managing the risks that arise on individual transactions or portfolios of similar transactions. Business units manage these risks by adhering to established risk policies and procedures.

In addition to risk management at the business unit level, the Group has developed corporate governance policies and procedures that require corporate personnel, who are independent of business units, to participate in the risk management process. The primary independent groups responsible for the maintenance of risk policies and procedures and for establishing, controlling and monitoring risk are Market Risk Management and Credit Risk Management. To ensure a proper system of checks and balances, these units are independent of business units and are accountable to senior management in the Group.

Market Risk

Market risk is the potential change in an instrument's value caused by fluctuations in interest and currency exchange rates, equity prices, credit spreads or other risks. The level of market risk is influenced by the volatility and liquidity in the markets in which financial instruments are traded. The Group seeks to mitigate market risk by employing hedging strategies that correlate rate, price and spread movements of trading inventories and related financing and hedging activities using a combination of cash instruments and derivatives.

**NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004** (continued)**22. Derivatives and Other Financial Instruments** (continued)**Interest Rate Risk**

Interest rate risk is the potential for loss due to adverse changes in interest rates. Interest rate swap agreements, futures and securities are common interest rate risk management tools.

Currency Risk

Currency risk is the potential for loss due to fluctuations in foreign exchange rates. Trading assets and liabilities include both cash instruments in and derivatives linked to over 35 currencies. Currency forwards, swaps and options are commonly used to manage currency risk associated with these instruments.

Credit Risk

Credit risk is the potential loss that may be incurred if a counterparty fails to perform its obligations under contractual terms. The Group has established policies and procedures for mitigating credit risk on principal transactions, including reviewing and establishing limits for credit exposure, maintaining collateral and continually assessing the creditworthiness of counterparties. In respect of derivative transactions, the Group enters into Master Agreements with counterparties which permit the netting of all transactional exposures on a multi-currency, multi-location basis and, in certain circumstances, across product types.

Liquidity Risk

Liquidity risk is the risk that an entity may encounter difficulty in realising assets or otherwise raising funds to meet commitments associated with financial instruments. The Group has established liquidity procedures for measuring funding requirements and identifying liquidity mismatches. The Group's funds are sourced from its own business activities and from Merrill Lynch affiliate companies.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

22. Derivatives and Other Financial Instruments (continued)**Interest Rate Sensitivity Gap**

The following tables show the contractual re-pricing terms for each category of asset and liability, together with management's estimate of the interest rate sensitivity gap for the Group's non-trading book as at 31st December 2004 and 26th December 2003. Contractual re-pricing terms do not reflect the potential impact of early repayment or withdrawal. Major changes in position can be made promptly as market outlooks change. In addition, significant variations in interest rate sensitivity may exist within the re-pricing periods presented and among the currencies in which the Group has interest rate positions.

(a) Interest rate sensitivity gap as at 31st December 2004

	Within 3 months \$ 000	After 3 months but within 6 months \$ 000	After 6 months but within 1 year \$ 000	After 1 year but within 5 years \$ 000	After 5 years \$ 000	Non-interest bearing and trading book items \$ 000	Total \$ 000
ASSETS							
Cash and balances at central banks	224,650	—	—	—	—	184,379	409,029
Loans and advances to banks	2,751,577	157,422	—	—	—	—	2,908,999
Loans and advances to customers	7,751,077	804,865	776,918	513,342	55,614	—	9,901,816
Debt securities	1,934,290	186,485	1,167,488	19,542	—	—	3,307,805
Intangible fixed assets	—	—	—	—	—	114,006	114,006
Tangible fixed assets	—	—	—	—	—	8,227	8,227
Other assets	—	—	—	—	—	411,274	411,274
Taxation	—	—	—	—	—	7,590	7,590
Prepayments and accrued income	—	—	—	—	—	3,220,804	3,220,804
Total assets	12,661,594	1,148,772	1,944,406	532,884	55,614	3,946,280	20,289,550
LIABILITIES							
Deposits by banks	780,123	20,626	10,268	—	—	—	811,017
Customer accounts	11,357,834	224,185	116,127	18,311	2,000	29,496	11,747,953
Other liabilities	—	—	—	—	—	735,674	735,674
Taxation	—	—	—	—	—	10,012	10,012
Accruals and deferred income	—	—	—	—	—	4,356,542	4,356,542
Deferred taxation	—	—	—	—	—	1,205	1,205
Subordinated liabilities including convertible debt	720,000	149,555	—	—	—	—	869,555
Equity shareholders' funds	—	—	—	—	—	1,507,592	1,507,592
Non equity shareholders' funds	—	—	—	—	—	250,000	250,000
Total liabilities	12,857,957	394,366	126,395	18,311	2,000	6,890,521	20,289,550
Derivatives affecting interest rate sensitivity	592,911	(16,743)	(47,084)	(473,470)	(55,614)	—	—
Interest rate sensitivity gap	396,548	737,663	1,770,927	41,103	(2,000)	(2,944,241)	—
Cumulative interest rate sensitivity gap	396,548	1,134,211	2,905,138	2,946,241	994,241	—	—



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

22. Derivatives and Other Financial Instruments (continued)

(b) Interest rate sensitivity gap as at 26th December 2004

	Within 3 months \$ 000	After 3 months but within 6 months \$ 000	After 6 months but within 1 year \$ 000	After 1 year but within 5 years \$ 000	After 5 years \$ 000	Non-interest bearing and trading book items \$ 000	Total \$ 000
ASSETS							
Cash and balances at central banks	185,879	—	—	—	—	91,300	277,179
Loans and advances to banks	1,191,506	356,265	—	—	—	—	1,547,771
Loans and advances to customers	8,398,191	1,018,282	762,278	226,837	35,146	(8,496)	10,432,238
Debt securities	1,344,857	189,776	939,730	18,980	—	—	2,493,343
Intangible fixed assets	—	—	—	—	—	247	247
Tangible fixed assets	—	—	—	—	—	7,155	7,155
Other assets	—	—	—	—	—	179,300	179,300
Prepayments and accrued income	—	—	—	—	—	2,786,073	2,786,073
Total assets	11,120,433	1,564,323	1,702,008	245,817	35,146	3,055,579	17,723,306
LIABILITIES							
Deposits by banks	2,197,696	74,471	93	—	—	23,963	2,296,223
Customer accounts	8,946,454	197,176	180,963	18,662	10,110	359,379	9,712,744
Other liabilities	229,918	—	—	—	—	320,263	550,181
Accruals and deferred income	—	—	—	—	—	3,056,774	3,056,774
Deferred taxation	—	—	—	—	—	104	104
Subordinated liabilities including convertible debt	600,000	149,555	—	—	—	—	749,555
Equity shareholders' funds	—	—	—	—	—	1,357,725	1,357,725
Total liabilities	11,974,068	421,202	181,056	18,662	10,110	5,118,208	17,723,306
Derivatives affecting interest rate sensitivity	(325,180)	(340,771)	(61,880)	7,987	(46,058)	—	(765,902)
Interest rate sensitivity gap	(1,178,815)	802,350	1,459,072	235,142	(21,022)	(2,062,629)	(765,902)
Cumulative interest rate sensitivity gap	(1,178,815)	(376,465)	1,082,607	1,317,749	1,296,727	(765,902)	—


NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

22. Derivatives and Other Financial Instruments (continued)

Currency Risk

Since the Group prepares its consolidated financial statements in US dollars, the consolidated balance sheet is affected by the structural currency exposures arising on movements in exchange rates between US dollars and the operating currencies of the overseas entities. The Group's net assets in non-functional currency overseas operations were:

	2004 \$ 000	2003 \$ 000
Functional currency of the operation involved		
Swiss Franc	414,041	329,308
Pound Sterling	131,326	—
Euro	7,437	4,984
Bahraini Dinar	6,689	6,310
Total	<u>559,493</u>	<u>340,602</u>

Transactional currency exposures are non-structural currency exposures, which arise on the monetary assets and monetary liabilities of the Group that are not denominated in the base currency of the operating unit involved. The transactional currency exposures arising from the Group's non-trading book were not material.



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

22. Derivatives and Other Financial Instruments (continued)**Fair Values of Financial Instruments**

The term financial instruments includes financial assets, financial liabilities and derivatives. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than a forced or liquidation sale. Quoted market prices are used where available; otherwise management estimates fair value based upon quoted market prices of financial instruments with similar characteristics.

	Note	2004			2003		
		Notional/ Principal \$ million	Positive Fair Values \$ million	Negative Fair Values \$ million	Notional/ Principal \$ million	Positive Fair Values \$ million	Negative Fair Values \$ million
Non-trading book	(a)						
Interest rate derivatives:							
Interest rate swaps		1,872	8	3	1,137	1	6
Debt securities		3,308	3,312	—	2,493	1	—
Other financial assets	(b)	13,701	13,701	—	12,616	12,616	—
Other financial liabilities	(b)	14,366	—	14,366	12,911	—	12,911
Trading book	(c)						
Foreign exchange derivatives:							
Forward foreign exchange		13,940	2,501	2,788	(3,636)	27,179	29,891
Currency futures		10,660	—	—	(3,146)	—	—
Currency swaps		—	—	—	20	1	1
Currency options		26,270	1,820	2,106	7,185	2,135	2,319
		50,870	4,321	4,894	423	29,315	32,211
Interest rate derivatives:							
Interest rate futures		—	—	—	—	—	—
Interest rate swaps		296,357	781	1,387	77,121	57	96
Forward rate agreements		9,800	32	33	19,680	404	547
		306,157	813	1,420	96,801	461	643

Notes

- (a) Non-trading book fair values are determined by market prices where available or by applying current market information to pricing or valuation models.
- (b) Balance sheet values approximate to fair values.
- (c) Trading book financial instruments are held at market value.
- (d) All off-balance sheet contracts or underlying principal amounts are shown net.


NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

23. Amounts Due to and From Other Merrill Lynch Companies

Amounts due to and from the ultimate parent, Merrill Lynch & Co., Inc., and its subsidiaries are included as follows:

	Group 2004 \$ 000	Group 2003 \$ 000	Company 2004 \$ 000	Company 2003 \$ 000
ASSETS				
Loans and advances to banks	70,106	61,578	589,092	491,810
Loans and advances to customers	2,588,187	2,579,081	2,607,545	2,579,081
Others assets	73,219	19,584	41,833	14,680
Prepayments and accrued income	2,126	294,321	4,623	274,203
	<u>2,733,638</u>	<u>2,954,564</u>	<u>3,243,093</u>	<u>3,359,774</u>
LIABILITIES				
Deposits by banks	104,867	252,046	194,273	296,185
Customer accounts	590,224	468,207	590,224	468,207
Other liabilities	231,214	283,878	218,347	285,542
Accruals and deferred income	2,060	253,610	2,076	244,847
Subordinated liabilities	869,555	749,555	869,555	749,555
	<u>1,797,920</u>	<u>2,007,296</u>	<u>1,874,475</u>	<u>2,044,336</u>

24. Shares in Group Undertakings

The movement in shares in Group undertakings was as follows:

	\$ 000
Company	
Cost	
At start of year	21,561
Additions	131,970
At end of year	<u>153,531</u>

The additions in the year relate to the purchase of the share capital of Majestic Acquisitions Limited (see Note 14).



NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31ST DECEMBER 2004 (continued)

24. Shares in Group Undertakings (continued)

The subsidiary undertakings (held indirectly unless marked *) of the Company as at 31st December 2004 are:

Company	Principal Activity	Country of Incorporation	Proportion of Ordinary shares held
Merrill Lynch Bank (Suisse) SA*	Private Client Banking Services	Switzerland	100 %
MLB(S) Fund Management SA	Fund Management	Switzerland	100 %
Mership Nominees Limited*	Nominee company	United Kingdom	100 %
Majestic Acquisitions Limited*	Holding company	United Kingdom	100 %
Mortgage Holdings Limited	Holding company	United Kingdom	100 %
Mortgages plc	Managing company	United Kingdom	100 %
Mortgages 1 Limited	Residential lending	United Kingdom	100 %
Mortgages 2 Limited	Residential lending	United Kingdom	100 %
Mortgages 3 Limited	Residential lending	United Kingdom	100 %
Mortgages 4 Limited	Residential lending	United Kingdom	100 %
Mortgages 5 Limited	Residential lending	United Kingdom	100 %
Mortgages 6 Limited	Residential lending	United Kingdom	100 %
Mortgages 7 Limited	Residential lending	United Kingdom	100 %
Mortgages DACS Limited	Acquiring investments	United Kingdom	100 %
Mortgages No 2 (DACs) Limited	Acquiring investments	United Kingdom	100 %
Mortgages No 3 (DACs) Limited	Acquiring investments	United Kingdom	100 %
Mortgages No 4 (DACs) Limited	Acquiring investments	United Kingdom	100 %
Mortgages No 5 (DACs) Limited	Acquiring investments	United Kingdom	100 %
WOW! Mortgages & Loans Limited	Mortgage broker	United Kingdom	50 %
Genesis Home Loans plc	Mortgage broker	United Kingdom	100 %

The holding in WOW! Mortgages & Loans Limited has 50% of the voting rights.

25. Ultimate Parent Company

The Company's ultimate parent company and controlling party is Merrill Lynch & Co., Inc., a company incorporated in the state of Delaware, in the United States of America. The parent company of the largest group that includes the Company and for which group accounts are prepared is Merrill Lynch & Co., Inc. The parent company and controlling party of the smallest group that presents group accounts and the immediate parent is Merrill Lynch International Finance Corporation, which is incorporated in the state of New York, in the United States of America.

Copies of the group financial statements of Merrill Lynch & Co., Inc., and Merrill Lynch International Finance Corporation are available from the Investor Relations website at www.ir.ml.com or by contacting:

Corporate Secretary
222 Broadway, Floor 17
New York
NY 10038
United States of America

Copies of the group financial statements of Merrill Lynch International Bank Limited are available from:

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