THIS DOCUMENT AND THE ACCOMPANYING DOCUMENTS ARE IMPORTANT AND REQUIRE YOUR IMMEDIATE ATTENTION. If you are in any doubt as to the action you should take, you are recommended to seek your own personal financial advice immediately from your stockbroker, bank, solicitor, accountant, fund manager or other appropriate independent financial adviser, who is authorised under the Financial Services and Markets Act 2000 if you are in the United Kingdom, or, if not, from another appropriately authorised independent financial adviser.

If you sell or have sold or otherwise transferred all of your Lloyds TSB Shares you should send this document and the accompanying documents as soon as possible to the purchaser or transferee or to the stockbroker, bank or other agent through whom the sale or transfer is/was effected for delivery to the purchaser or the transferee. However, the distribution of this document and any accompanying documents into certain jurisdictions (including but not limited to the United States) other than the United Kingdom is or may be restricted by law and therefore persons into whose possession this document and any accompanying documents come should inform themselves about and observe any such restrictions. Failure to comply with any such restrictions may constitute a violation of the securities laws of any such jurisdiction. See paragraph 11 of Part III (''Principal Terms of the Acquisition'') of this document. If you sell or have sold or otherwise transferred only part of your holding of Lloyds TSB Shares, you should retain this document and the accompanying documents.

This document does not constitute or form part of any offer or invitation to purchase, otherwise acquire, subscribe for, sell, otherwise dispose of or issue, or any solicitation of any offer to sell, otherwise dispose of, issue, purchase, otherwise acquire or subscribe for, any security.

This document does not constitute a prospectus or prospectus equivalent document. Nothing in this document should be interpreted as a term or condition of the Placing and Open Offer. Any decision to acquire Lloyds TSB Shares under the Placing and Open Offer must be made only on the basis of the information contained in and incorporated by reference into the Prospectus expected to be published in mid-November 2008. Copies of the Prospectus will be available following publication from Lloyds TSB's registered office and as described in paragraph 16 of Part XII (''Additional Information'') of this document.

Application will be made to the FSA for the Consideration Shares proposed to be issued in connection with the Acquisition and the Open Offer Shares to be issued in connection with the Placing and Open Offer to be admitted to the Official List, and will be made to the London Stock Exchange for the Consideration Shares and the Open Offer Shares to be admitted to trading on the London Stock Exchange's main market for listed securities. It is expected that, subject to the satisfaction of certain conditions, Admission of the Open Offer Shares to the Official List and the London Stock Exchange will become effective, and that dealings in the Open Offer Shares will commence, in mid-January 2009. It is expected that Admission of the Consideration Shares to the Official List and the London Stock Exchange will become effective, and that dealings in the Consideration Shares will commence, on the Effective Date which, subject to the satisfaction of certain conditions, including the sanction of the Scheme by the Court, is also expected to occur in mid-January 2009.

Lloyds TSB

Lloyds TSB Group plc

(incorporated under the Companies Act 1985 and registered in Scotland with Registered No. 95000)

Proposed Acquisition of HBOS plc by means of a scheme of arrangement under sections 895 to 899 of the Companies Act 2006

Proposed Placing and Open Offer of 2,596,653,203 Open Offer Shares at 173.3 pence per Open Offer Share

Proposed Capitalisation Issue

Circular to Shareholders and Notice of General Meeting of the Company

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Your attention is drawn to the letter from the Chairman of the Company which is set out on pages 8 to 28 of this document and which recommends you to vote in favour of the Resolutions to be proposed at the General Meeting referred to below. The Acquisition, the Placing and Open Offer and the New Preference Share Issue are conditional, amongst other things, upon the passing of certain of the Resolutions at the General Meeting. Please read the whole of this document and, in particular, the risks relating to Lloyds TSB Group and the Enlarged Group and the other risk factors set out in the section headed ''Risk Factors'' on pages 29 to 46. You should not rely solely on summarised information in this document.

Notice of a General Meeting of the Company to be held at the Scottish Exhibition and Conference Centre, Glasgow G3 8YW at 11.00 a.m. on 19 November 2008 is set out at the end of this document. A Form of Proxy for the General Meeting (the ''Form of Proxy'') is enclosed. To be valid, Forms of Proxy should be completed, signed and returned in accordance with the instructions printed on them so as to be received by the Company's Registrars as soon as possible and in any event no later than 11.00 a.m. on 17 November 2008 (or, in the case of an adjournment, no later than 48 hours before the time fixed for the holding of the adjourned meeting). If you are a member of CREST you may be able to use the CREST electronic proxy appointment service in accordance with the procedures set out in the notice convening the General Meeting at the end of this document. Proxies sent electronically must be sent as soon as possible and, in any event, so as to be received by not later than 11.00 a.m. on 17 November 2008 (or, in the case of an adjournment, not later than 48 hours before the time fixed for the holding of the adjourned meeting). Lloyds TSB Shareholders are requested to complete, sign and return the Form of Proxy, or use the CREST electronic proxy appointment service, whether or not they intend to be present at the General Meeting. Completion and return of a Form of Proxy, or use of the CREST electronic proxy appointment service, will not preclude Lloyds TSB Shareholders from attending and voting in person at the General Meeting, should they so wish.

Citi, which is authorised and regulated in the United Kingdom by the Financial Services Authority, is acting exclusively for Lloyds TSB and for no-one else as joint sponsor, joint bookrunner and joint placing agent (and also in providing financial advice in relation to the Acquisition) in relation to the Placing and Open Offer and the listing of the securities to be issued pursuant to the Placing and Open Offer and the Acquisition on the Official List and their admission to trading on the London Stock Exchange's main market for listed securities, and will not be responsible to any other person for providing the protections afforded to clients of Citi nor for providing advice in connection with the proposed Placing and Open Offer or the Acquisition, proposed listing or admission to trading or contents of this document or any other matters referred to in this document.

Lazard is acting exclusively for Lloyds TSB and for no-one else in providing financial advice in relation to the Acquisition and will not be responsible to any other person for providing the protections afforded to clients of Lazard nor for providing advice in connection with the Acquisition, proposed listing or admission to trading or contents of this document or any other matters referred to in this document.

Merrill Lynch, which is authorised and regulated in the United Kingdom by the Financial Services Authority, is acting exclusively for Lloyds TSB and for no-one else as joint sponsor, joint financial adviser, joint bookrunner and joint placing agent in relation to the Acquisition, the Placing and Open Offer and the listing of the securities to be issued pursuant to the Placing and Open Offer and the Acquisition on the Official List and their admission to trading on the London Stock Exchange's main market for listed securities, and will not be responsible to any other person for providing the protections afforded to clients of Merrill Lynch nor for providing advice in connection with the proposed Placing and Open Offer or the Acquisition, proposed listing or admission to trading or contents of this document or any other matters referred to in this document.

UBS is acting exclusively for Lloyds TSB and for no-one else as joint sponsor, joint financial adviser, joint bookrunner and joint placing agent in relation to the Acquisition, the Placing and Open Offer and the listing of the securities to be issued pursuant to the Placing and Open Offer and the Acquisition on the Official List and their admission to trading on the London Stock Exchange's main market for listed securities, and will not be responsible to any other person for providing the protections afforded to clients of UBS nor for providing advice in connection with the proposed Placing and Open Offer or the Acquisition, proposed listing or admission to trading or contents of this document or any other matters referred to in this document.

Dated: 3 November 2008

PRESENTATION OF INFORMATION

Presentation of Financial Information

Unless otherwise indicated, financial information for Lloyds TSB and the Lloyds TSB Group in this document has been extracted without material adjustment from the Lloyds TSB Interim Results for the six months ended 30 June 2008 published on 30 July 2008 prepared in accordance with the Disclosure and Transparency Rules and with IAS 34, ''Interim Financial Reporting'', as adopted by the European Union, is presented in pounds sterling, and is unaudited. For further information, see ''Accounting policies, presentation and estimates'' on page 36 of the Lloyds TSB Interim Results, such page being incorporated into this document by reference.

See also note 2 ''Segmental analysis'' on pages 37-38 of the Lloyds TSB Interim Results (such pages being incorporated into this document by reference) and paragraph 5 of Part VII (''Information on the Lloyds TSB Group'') of this document.

Unless otherwise indicated, financial information for HBOS and the HBOS Group in this document has been extracted without material amendment from the condensed consolidated half year financial statements of HBOS prepared in accordance with the Disclosure and Transparency Rules and with IAS 34 ''Interim Financial Reporting'' as adopted by the European Union, and is unaudited. For further information, see ''Condensed Financial Statements'' on pages 74 and 75 of the HBOS Interim Results.

Information on Risk Factors

The risk factors set out in Part II of this document have not been extracted from public documents filed or published by Lloyds TSB or HBOS and, instead, are the risks that the Lloyds TSB Group believes apply to Lloyds TSB's business and will apply to the Enlarged Group's business.

Enlarged Group

Unless the context otherwise requires, references in this document to the ''Enlarged Group'' are to Lloyds TSB and its subsidiaries and subsidiary undertakings and, where the context requires, its associated undertakings as constituted immediately following completion of the Acquisition and therefore such references include the Lloyds TSB Group as enlarged by the HBOS Group. Completion of the Acquisition is subject to a number of conditions which are described in detail in Part I (''Letter from Sir Victor Blank, Chairman of Lloyds TSB Group Plc'') and Part III (''Principal Terms of the Acquisition'').

No Profit Forecast

No statement in this document or incorporated by reference into this document is intended to constitute a profit forecast or profit estimate for any period, nor should any statement be interpreted to mean that earnings or earnings per share will necessarily be greater or lesser than those for the relevant preceding financial periods for either Lloyds TSB or HBOS as appropriate.

Rounding

Certain figures included in this document and in the information incorporated by reference into this document have been subject to rounding adjustments. Accordingly, discrepancies in tables between the totals and the sums of the relevant amounts are due to rounding.

Websites

Neither the content of the Company's website (or any other website) nor the content of any website accessible from hyperlinks on the Company's website (or any other website) is incorporated into, or forms part of, this document.

Time

All references in this document to times are to UK time unless otherwise stated.

Definitions

Capitalised terms have the meanings ascribed to them in the section of this document headed ''Definitions''.

NOTICE TO US INVESTORS

The Consideration Shares and the Consideration ADRs will not be, and are not required to be, registered under the Securities Act in reliance upon the exemption from registration requirements of the Securities Act provided by section 3(a)(10) thereof. The Open Offer Shares have not been and will not be registered under the Securities Act or under any securities laws of any state or other jurisdiction of the United States and may not be offered, sold, resold, transferred or delivered, directly or indirectly, within the United States except pursuant to an applicable exemption from the registration requirements of the Securities Act and in compliance with any applicable securities laws of any state or other jurisdiction of the United States. The Open Offer Shares will be offered and sold in the United States in a transaction not involving a public offering within the meaning of Section 4(2) of the Securities Act to persons reasonably believed to be "qualified institutional buyers" within the meaning of Rule 144A under the Securities Act. There will be no public offer of the Consideration Shares, the Consideration ADRs or the Open Offer Shares in the United States. Neither the SEC nor any other US federal or state securities commission or regulatory authority has approved or disapproved the Consideration Shares, the Consideration ADRs or the Open Offer Shares or passed an opinion on the adequacy of this document. Any representation to the contrary is a criminal offence in the United States. Shareholders who are or become affiliates (within the meaning of the Securities Act) of Lloyds TSB will be subject to timing, manner of sale and volume restrictions on the sale of the Consideration Shares or Consideration ADRs received in connection with the Scheme under Rule 145(d) of the Securities Act. The Open Offer Shares offered and sold in the United States will constitute "restricted securities" under Rule 144(a)(3) of the Securities Act.

The securities mentioned herein may not be offered or sold in any Restricted Jurisdiction absent registration or an applicable exemption from the registration requirements of the relevant laws of any Restricted Jurisdiction. There will be no public offer of such securities in any Restricted Jurisdiction.

FORWARD-LOOKING STATEMENTS

This document and the information incorporated by reference to this document includes certain "forward-looking statements". Statements that are not historical facts, including statements about the Lloyds TSB Group's or the HBOS Group's or their respective directors' and or management's beliefs and expectations are forward-looking statements. Words such as "believes", "anticipates", "estimates", "expects", "intends", "aims", "potential", "will", "would", "could", "considered", "likely", "estimate" and variations of these words and similar future or conditional expressions, are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend upon future circumstances that may or may not occur, many of which are beyond the Company's control and all of which are based on the Lloyds TSB Directors' current beliefs and expectations about future events. Such forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance or achievements of Lloyds TSB, HBOS or the Enlarged Group, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such forward-looking statements are based on numerous assumptions regarding Lloyds TSB's, HBOS's and the Enlarged Group's present and future business strategies and the environment in which the Enlarged Group will operate in the future. These forward-looking statements speak only as at the date of this document.

Examples of such forward-looking statements include, but are not limited to, statements about expected benefits and risks associated with the Acquisition and the Placing and Open Offer, projections or expectations of profit attributable to shareholders, anticipated provisions or write-downs, economic profit, dividends, capital structure or any other financial items or ratios; statements of plans, objectives or goals of Lloyds TSB, HBOS or the Enlarged Group following completion of the Acquisition, including in relation to the achievement of anticipated cost synergies, other operating efficiencies, business growth opportunities, revenue and other benefits; statements about the future trends in interest rates, liquidity, foreign exchange rates, stock market levels and demographic trends and any impact that those matters may have on Lloyds TSB, HBOS or the Enlarged Group following completion of the Acquisition; statements concerning any future UK, US or other economic environment or performance; statements about strategic goals, competition, regulation, regulatory approvals, dispositions and consolidation or technological developments in the financial services industry; and statements of assumptions underlying such statements.

Lloyds TSB Shareholders and potential investors should specifically consider all of the information set out in, and incorporated by reference into this document before making any investment decision or any decision whether or not to vote in favour of the Resolutions. In particular, Lloyds TSB Shareholders and potential investors should consider the risks, uncertainties and other factors are set out in Part II ("Risk Factors") of this document, which include general risks relating to the Lloyds TSB Group and, if the Acquisition becomes Effective, the Enlarged Group, risks relating to the Acquisition, and risks relating to the Placing and Open Offer and to investment in Lloyds TSB Shares and Lloyds TSB ADRs.

Except as required by the FSA, the London Stock Exchange, the Takeover Panel, the Listing Rules, the Prospectus Rules, the Disclosure and Transparency Rules, the City Code or any other applicable law or regulation, the Company expressly disclaims any obligations or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this document or incorporated by reference into this document to reflect any change in the Company's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

DEALING DISCLOSURE REQUIREMENTS

Under the provisions of Rule 8.3 of the City Code, if any person is, or becomes, ''interested'' (directly or indirectly) in one per cent. or more of any class of ''relevant securities'' of Lloyds TSB or HBOS, all ''dealings'' in any ''relevant securities'' of that company (including by means of an option in respect of, or a derivative referenced to, any such ''relevant securities'') must be publicly disclosed by no later than 3.30 p.m. on the London business day following the date of the relevant transaction. This requirement will continue until the Effective Date, or on which the ''offer period'' for the purposes of the City Code otherwise ends. If two or more persons act together pursuant to an agreement or understanding, whether formal or informal, to acquire an ''interest'' in ''relevant securities'' of Lloyds TSB or HBOS, they will be deemed to be a single person for the purpose of Rule 8.3.

Under the provisions of Rule 8.1 of the City Code, all ''dealings'' in ''relevant securities'' of Lloyds TSB or HBOS by Lloyds TSB or HBOS, or by any of their respective ''associates'', must be disclosed by no later than 12.00 noon on the London business day following the date of the relevant transaction.

A disclosure table, giving details of the companies in whose ''relevant securities'' ''dealings'' should be disclosed, and the number of such securities in issue, can be found on the Panel's website at www.thetakeoverpanel.org.uk.

''Interests in securities'' arise, in summary, when a person has long economic exposure, whether conditional or absolute, to changes in the price of securities. In particular, a person will be treated as having an ''interest'' by virtue of the ownership or control of securities, or by virtue of any option in respect of, or derivative referenced to, securities.

Terms in quotation marks are defined in the Code, which can also be found on the Panel's website. If you are in any doubt as to whether or not you are required to disclose a ''dealing'' under Rule 8, you should consult the Panel.

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EXPECTED TIMETABLE OF PRINCIPAL EVENTS

Latest time for lodging Forms of Proxy for Lloyds TSB General Meeting	11.00 a.m. on 17 November 2008
Expected date of publication of Prospectus	mid-November 2008
Lloyds TSB General Meeting	11.00 a.m. on 19 November 2008
HBOS Court Meeting	12 December 2008
HBOS General Meeting	12 December 2008
Record date for entitlement under the Open Offer for Qualifying CREST Shareholders and Qualifying Non-CREST Shareholders	12 December 2008
Ex-entitlement date for the Open Offer	12 December 2008
Latest time and date for receipt of completed Application Forms and payment in full under the Open Offer and settlement of relevant CREST instructions (as appropriate)	12 January 2009
Scheme Court Hearing to sanction the Scheme	13 January 2009
Admission and commencement of dealings in Open Offer Shares on the London Stock Exchange	14 January 2009(1)
Reduction Court Hearing to confirm the Capital Reduction	16 January 2009(1)
Effective Date of the Scheme	16 January 2009(1)
Delisting of HBOS Shares	19 January 2009(1)
Issue of Consideration Shares	19 January 2009(1)
Admission and commencement of dealings in Consideration Shares on the London Stock Exchange	19 January 2009(1)

Note:
(1) These dates are indicative only and will depend, among other things, on the date upon which the Court sanctions the Scheme.

The above times and dates are indicative only and may be subject to change. If any of the above times and/or dates change, the revised times and/or dates will be notified by announcement through a Regulatory Information Service.

Different deadlines and procedures may apply in certain cases. For example, Lloyds TSB Shareholders that hold their Lloyds TSB Shares through a CREST member or other nominee may be set earlier deadlines by the CREST member or other nominee than the times and dates noted above.

PART I

LETTER FROM SIR VICTOR BLANK, CHAIRMAN OF LLOYDS TSB GROUP PLC

Lloyds TSB

Directors:
Sir Victor Blank *(Chairman)*
J Eric Daniels
Archie G Kane
G Truett Tate
Tim J W Tookey
Helen A Weir CBE
Wolfgang C G Berndt
Ewan Brown CBE FRSE
Jan P du Plessis
Philip N Green
Sir Julian Horn-Smith
Lord Leitch
Sir David Manning GCMG CVO
Carolyn J McCall OBE
Martin A Scicluna

Registered Office:
Henry Duncan House,
120 George Street,
Edinburgh EH2 4LH

3 November 2008

Dear Shareholder

PROPOSED ACQUISITION OF HBOS, PLACING AND OPEN OFFER AND NEW PREFERENCE SHARE ISSUE

The Lloyds TSB Board of Directors has long recognised the attractions of a combination of Lloyds TSB and HBOS. The Acquisition of HBOS represents a compelling opportunity to accelerate Lloyds TSB's strategy and create the UK's leading financial services group. In retail banking, the Acquisition brings together two of the leading retailers in UK financial services with particular expertise in bancassurance, insurance and long-term savings. In wholesale banking, the combination of expertise and products across an enlarged distribution network and customer base is expected to generate significant shareholder value. Importantly, the combination will also drive significant synergy benefits; the Lloyds TSB Board believes it will deliver total annual pre-tax cost savings greater than £1.5 billion by the end of 2011.

Since August 2007, and even more so since September 2008, global financial markets have experienced a period of significant turmoil. On 18 September 2008 the boards of Lloyds TSB and HBOS announced that they had reached agreement on the terms of a recommended acquisition by Lloyds TSB of HBOS. Since that date, conditions in global financial markets have continued to deteriorate, which has negatively affected capital ratios, in part because the banking sector's capital requirements are sensitive to changes in economic conditions under the Basel II accord. In light of the current economic environment, the UK Government decided that it would be appropriate for the UK banking sector to have higher levels of capital. This led to the UK Government announcing, on 8 October 2008, specific and comprehensive measures to ensure the stability of the UK financial system.

Lloyds TSB Group plc is registered in Scotland no. 95000
Registered Office: Henry Duncan House 120 George Street Edinburgh EH2 4LH

Lloyds TSB welcomed the UK Government's proposals and confirmed its commitment to completing the Acquisition. On 13 October 2008, as part of a co-ordinated package of capital and funding measures for the UK banking sector to be implemented by HM Treasury, the boards of Lloyds TSB and HBOS announced that they intended to participate in the Proposed Government Funding with £5.5 billion of new capital to be raised by Lloyds TSB (consisting of £4.5 billion in ordinary shares and £1 billion in preference shares (before costs and expenses)) and £11.5 billion by HBOS (consisting of £8.5 billion in ordinary shares and £3 billion in preference shares (before costs and expenses)). Lloyds TSB and HBOS also announced that they had agreed to proceed with the Acquisition on revised terms, adjusted to 0.605 Lloyds TSB shares for every HBOS share from 0.833 Lloyds TSB shares for every HBOS share.

The Lloyds TSB Directors believe that Lloyds TSB's and HBOS's participation in the Proposed Government Funding provides the capital necessary to complete the Acquisition in a timely fashion, with certainty and on terms that the Lloyds TSB Directors believe are the best available to Lloyds TSB and HBOS in current market conditions.

When combined with the new capital being raised by HBOS, the Proposed Government Funding is designed to provide the Enlarged Group with the capital strength and the funding capabilities to meet the short-term challenges that current markets present and support the longer-term creation of shareholder value. Lloyds TSB believes that HM Treasury will, in accordance with its public statements, act as a value-oriented shareholder with regard to the strategic development of the Enlarged Group and will recognise the importance of delivering the significant cost synergies highlighted above. Details of the conditions attaching to the Proposed Government Funding are set out in Part V of this document. Subject to this, at the Lloyds TSB Board's request, HM Treasury has confirmed that it currently has no intentions or strategic plans concerning the Enlarged Group or its business or employees.

The Lloyds TSB Directors believe that the combination of Lloyds TSB and HBOS, including the required capital raising by both companies, is in the best interests of the Company and Lloyds TSB Shareholders as a whole. The Lloyds TSB Board believes the turbulence in current markets has presented a unique opportunity to pursue the Acquisition, and unanimously recommends that Lloyds TSB Shareholders vote in favour of the Acquisition and the Resolutions associated with the Proposed Government Funding.

In considering the merits of the Acquisition, the Lloyds TSB Directors have been mindful that the landscape of the UK banking industry has shifted materially in recent months. The Lloyds TSB Directors do not believe it is appropriate to compare the Enlarged Group, including the impact of the Proposed Government Funding, with Lloyds TSB as it currently stands but rather compare the Enlarged Group against the position Lloyds TSB would likely be in should the Acquisition not become Effective.

If the Acquisition and Placing and Open Offer do not complete, HM Treasury has stated that it would expect Lloyds TSB to take appropriate action to strengthen its capital position. The FSA has advised Lloyds TSB that if the Acquisition were not to occur, it would require Lloyds TSB to raise £7 billion of additional capital, made up of £5 billion of Core Tier 1 equity and £2 billion of Tier 1 instruments. Whilst Lloyds TSB would be able to seek to raise such additional new capital in the public markets, there can be no certainty that Lloyds TSB would be able to successfully raise such capital or as to the terms on which such capital could be raised, including the terms of any participation by HM Treasury in any such capital raising, or as to whether any such fundraising would be on a pre-emptive basis.

The Lloyds TSB Directors believe that the Enlarged Group will be more competitive and will have significantly greater opportunities to create sustainable shareholder value than Lloyds TSB would on a standalone basis in what is now a materially more challenging market environment.

I am writing to give you further details of the Acquisition, the Placing and Open Offer and the New Preference Share Issue.

- Paragraph 1 provides further insight into the Lloyds TSB Board's views of the proposals, and a chronology of recent events to put the Acquisition and Placing and Open Offer into context.
- Paragraph 2 reminds shareholders of Lloyds TSB's strong track record of delivery of its strategy.
- Paragraphs 4 and 5 highlight the rationale for, and the financial effects of, the Acquisition.

- The Resolutions that will be put to the Lloyds TSB General Meeting are summarised in Paragraph 16.

This letter as a whole explains why the Lloyds TSB Board unanimously considers the Acquisition and Placing and Open Offer to be in the best interests of Lloyds TSB and the Lloyds TSB Shareholders as a whole and seeks your approval of the Resolutions.

1 Introduction and chronology of events

Since August 2007, and even more so since September 2008, global financial markets have experienced a period of significant turmoil, which, among other things, included the UK Government placing Northern Rock into temporary public ownership on 22 February 2008 and the announcement on 15 September 2008 by Lehman Brothers that it intended to file a Chapter 11 Bankruptcy petition in the US.

On 18 September 2008, with the support of the UK Government, the boards of Lloyds TSB and HBOS announced that they had reached agreement on the terms of a recommended acquisition by Lloyds TSB of HBOS. HBOS Shareholders were to receive 0.83 Lloyds TSB Shares for every 1 HBOS Share (amended to 0.833 Lloyds TSB Shares following Lloyds TSB's successful share placing on 19 September 2008). On completion of the transaction on such terms, existing Lloyds TSB Shareholders would have owned approximately 56 per cent. of the enlarged group with the remaining 44 per cent. being held by existing HBOS Shareholders.

Following the announcement on 18 September 2008, conditions in global financial markets continued to deteriorate. Bradford & Bingley was placed into temporary public ownership in the UK on 29 September 2008. This was followed by the Icelandic Financial Services Authority putting Landsbanki into receivership on 7 October 2008, which affected UK savers through its internet brand, Icesave. On 8 October 2008, HM Treasury announced that, after consultation with the Bank of England and the Financial Services Authority, it was bringing forward specific and comprehensive measures to ensure the stability of the UK financial system and to protect ordinary savers, depositors, businesses and borrowers. On the same day, Lloyds TSB announced that it welcomed the announcement by HM Treasury to bring stability and certainty to the UK banking industry and that it continued to progress the Acquisition.

On 13 October 2008, in the context of further unprecedented turbulence in global financial markets and as part of a co-ordinated package of capital and funding measures for the UK banking sector implemented by HM Treasury, the boards of both Lloyds TSB and HBOS announced that they intended to participate in the Proposed Government Funding, thereby gaining access to the UK Government backed provision of liquidity, and that they had agreed to proceed with the Acquisition on revised terms.

A combined total of £17 billion of new capital will be raised by Lloyds TSB and HBOS, of which £5.5 billion (consisting of £4.5 billion in ordinary shares and £1 billion in preference shares (before costs and expenses)) will be raised by Lloyds TSB and £11.5 billion (consisting of £8.5 billion in ordinary shares and £3 billion in preference shares (before costs and expenses)) by HBOS:

- The Lloyds TSB Placing and Open Offer comprises a proposed placing and open offer of approximately 2.6 billion Open Offer Shares at 173.3 pence per Open Offer Share, representing an 8.5 per cent. discount to Lloyds TSB's Closing Price on 10 October 2008. Eligible Lloyds TSB Shareholders will have the opportunity to claw back their proportionate entitlement to Open Offer Shares through the Open Offer and to apply for Open Offer Shares in excess of their Open Offer Entitlement. HM Treasury has agreed that, to the extent the Open Offer Shares are not taken up by Eligible Lloyds TSB Shareholders or placed with placees, HM Treasury will acquire such Open Offer Shares at the Issue Price. The New Preference Share Issue comprises a subscription by HM Treasury of approximately 1,000,000 New Preference Shares at £1,000 per New Preference Share.
- The HBOS Placing and Open Offer comprises a proposed placing and open offer of approximately 7.5 billion new HBOS shares at 113.6 pence per share, representing a discount of 8.5 per cent. to the HBOS Closing Price on 10 October 2008. Eligible HBOS Shareholders will have the opportunity to claw back their proportionate entitlement to these new HBOS shares through the HBOS Open Offer and to apply for new HBOS Shares in excess of their entitlement under the HBOS Placing and Open Offer. HM Treasury has agreed that, to the extent the HBOS Open Offer Shares are not taken up by eligible HBOS Shareholders or placed with placees HM Treasury will acquire such HBOS Open Offer Shares at the issue

price. HBOS will seek approval from its shareholders of certain resolutions in respect of the Acquisition and the HBOS Placing and Open Offer at a general meeting expected to be held in early December 2008.

In the period between 18 September 2008 and 13 October 2008 market conditions continued to deteriorate. Reflecting the additional capital that Lloyds TSB and HBOS agreed to raise and the impact of the continuing severity of the market dislocation on the future prospects of the Enlarged Group, Lloyds TSB and HBOS further agreed to amend the merger ratio for the Acquisition such that HBOS Shareholders will receive 0.605 Lloyds TSB Shares for every 1 HBOS Share. The revised terms of the Acquisition have been unanimously recommended by the boards of Lloyds TSB and HBOS.

It is intended that the Acquisition will be effected by way of a scheme of arrangement under sections 895 to 899 of the Companies Act (although Lloyds TSB reserves the right, in its sole discretion, to implement the Acquisition by means of an Offer) and, subject to the satisfaction, or where appropriate, waiver, of the Conditions, it is expected that the Acquisition will become Effective in January 2009. Upon the Acquisition becoming Effective, if none of the Lloyds TSB Shareholders (in relation to the Lloyds TSB Placing and Open Offer) nor the HBOS Shareholders (in relation to the HBOS Placing and Open Offer) participate in the clawback, existing Lloyds TSB Shareholders will own 36.5 per cent. of the Enlarged Group with existing HBOS Shareholders owning 20.0 per cent. of the Enlarged Group. In such circumstances, the remaining 43.5 per cent. will be owned by HM Treasury. To the extent the Lloyds TSB Shareholders and the HBOS Shareholders (in relation to the HBOS Placing and Open Offer) fully participate in the clawback, existing Lloyds TSB Shareholders will own 52.4 per cent. of the Enlarged Group, existing HBOS Shareholders will own 47.6 per cent. of the Enlarged Group and HM Treasury will own 0 per cent.

An offer will also be made by Lloyds TSB to HM Treasury (by way of scheme of arrangement) to exchange the preference shares in HBOS to be issued by HBOS to HM Treasury for equivalent preference shares in Lloyds TSB. Upon completion of this offer, HM Treasury will hold £4 billion of new preference shares in the enlarged share capital of Lloyds TSB.

The Placing and Open Offer and the Acquisition are interconditional (as explained in Paragraph 7 of this letter). If the Resolutions on which the Placing and Open Offer or the Acquisition are conditional are not approved or for some other reason the Placing and Open Offer Agreement is terminated or the Acquisition does not complete, the Proposed Government Funding would not be available to Lloyds TSB.

HM Treasury has informed Lloyds TSB that it is not a permanent investor in UK banks. Its intention, over time, is to dispose of any Lloyds TSB Shares it may acquire under the Placing and Open Offer or pursuant to the Acquisition in an orderly way and would normally expect to consult the Lloyds TSB Board prior to disposal. In addition to being bound by the restriction on the payment of dividends discussed in Paragraph 9 of this letter, the Company has given certain undertakings to HM Treasury in relation to such matters as availability and active marketing of competitively priced mortgage lending and lending to SMEs and board remuneration aimed at ensuring that any state aid involved in the potential acquisition of Open Offer Shares and Lloyds TSB's potential participation in the guarantee scheme to be promoted by HM Treasury as part of its support for the UK banking industry is compatible with the common market under EU law. However, further undertakings may be required to ensure such compatibility.

The Company has also agreed to use The Mound as its Scottish headquarters and to hold its annual general meetings in Scotland. Pursuant to the conditions attaching to the Proposed Government Funding, a summary of which is set out in Part V of this document, HM Treasury will work with the Lloyds TSB Board on its appointment of two new independent directors following completion of the Acquisition. Thereafter, consistent with best practice the Company will engage constructively with HM Treasury in its role as a shareholder. Further details in relation to such conditions attaching to the Proposed Government Funding are set out in Part V of this document. Subject to this, at the Lloyds TSB Board's request HM Treasury has confirmed that it currently has no intentions or strategic plans concerning the Enlarged Group or its business or employees.

Due to the size of the Acquisition and the number of Lloyds TSB Shares, New Preference Shares and Replacement Lloyds TSB Preference Shares which will be issued to implement the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme (respectively), the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the approval of Lloyds TSB's

Shareholders in a general meeting. Such approval will be sought at the Lloyds TSB General Meeting to be held at 11:00 a.m. on 19 November 2008.

In addition to the Acquisition, it was also announced on 18 September 2008 that the Lloyds TSB Board intends to issue new shares by way of the Capitalisation Issue. This Capitalisation Issue requires Lloyds TSB Shareholders to authorise the capitalisation of non-distributable reserves to allow the Capitalisation Issue Shares to be issued to Lloyds TSB Shareholders. Please refer to Part VI for further details concerning the Capitalisation Issue, including certain general taxation considerations in respect of the Capitalisation Issue.

The Lloyds TSB Prospectus relating to Admission of the Consideration Shares and to the Placing and Open Offer is expected to be published on the Lloyds TSB website in mid-November 2008.

2 Background on the Lloyds TSB Group

Lloyds TSB's strong track record of delivery is built on the successful implementation of its strategy to develop long term customer relationships and build strong customer franchises. Lloyds TSB has continued to extend the depth and reach of its customer relationships, achieving robust sales growth whilst maintaining efficiency and a prudent approach to risk. It is Lloyds TSB's belief that this relationship focused strategy has demonstrated its effectiveness in generating sustainable, high quality returns for shareholders.

Strong customer relationships

Customer relationships are critical to Lloyds TSB's strategy. The Lloyds TSB Group seeks to develop deep, long-lasting relationships with its customer base in order to deliver high quality, sustainable growth over time. The focus on both customer acquisition and on building diversified, sustainable revenue streams from existing customers allows Lloyds TSB to drive growth while minimising both its costs and risk profile.

The success of the customer strategy is demonstrated by:

- *The ability to deepen existing customer relationships and generate high quality income through diversified, sustainable revenue streams*

  The retail bank has continued to make excellent progress, delivering strong product sales growth and revenue momentum. Underlying income increased by 9 per cent. in the six months to June 2008, as compared to the same period in 2007, with improvements over a broad range of products including mortgages, personal loans, bank savings and wealth management, while profit before tax increased by 11 per cent. Excellent cost control has allowed Lloyds TSB to reduce its cost income ratio while continuing to make ongoing investments in the business. Retail customer deposits increased by 10 per cent. in the same period, with particularly strong progress in growing relationship-focused bank savings and wealth management deposit balances. The retail business continues to deepen customer relationships, both at the time of customer acquisition and over time. During the first half of 2008, over 99 per cent. of new personal loans and 90 per cent. of new credit cards sold were to existing customers which allows better risk assessment. Retail asset growth was 8 per cent., primarily in the form of mortgages, in the six months to 30 June 2008, as compared to the same period in 2007, and Lloyds TSB enjoyed a 24 per cent. market share of net new lending over the same period. Lloyds TSB also continues to develop its insurance business with an increase in bancassurance sales of 8 per cent. in the six months to 30 June 2008 building on the success of the simplified product range developed for distribution through the Lloyds TSB branch network, Commercial Banking and Wealth Management channels.

  In Corporate Markets further progress has been made in developing the Company's relationship banking franchise supported by strong cross selling performance. Revenues from cross sales to existing customers increased by 64 per cent. in the six months to 30 June 2008, as compared to the same period in 2007. In Commercial Banking growth in business volumes in particular, supported by 22 per cent. growth in lending to SMEs with a turnover of up to £15 million during the twelve months to 30 June 2008, has resulted in strong trading surplus growth. Lending margins have widened in the corporate business and Lloyds TSB enjoyed excellent wholesale liability growth of 18.2 per cent. in the six months to 30 June 2008 as compared to the same period in 2007.

- *The continued acquisition of new customers*

  Lloyds TSB has continued to make good progress in expanding its customer franchise. The retail bank opened nearly half a million new current accounts and achieved a 24.4 per cent. market share of net new mortgage lending in the first half of the year. In Commercial Banking the Lloyds TSB Group has continued to win new high value customers in the £0.5 to £2 million and £2 to £15 million turnover range achieving a market share in these segments of 16 per cent. and 13 per cent. respectively as at 30 June 2008 as a result of attracting customers "switching" from other financial services providers. In the mid market corporate segment, market share has increased from 12 per cent to 14 per cent. over the period from 30 June 2007 to 30 June 2008.

- *Continuous productivity improvement*

  Superior performance requires a continuous focus on productivity improvement, which drives both improved customer service and cost reduction. In recent years, Lloyds TSB has been building a set of strong capabilities in error reduction, operations efficiency and procurement. Alongside those capabilities, the Lloyds TSB Group applies an "income growth must exceed cost growth" discipline in setting goals for each business, requiring a wider gap between income growth and cost growth for lower growth businesses than for higher growth businesses. At the Lloyds TSB Group level, for the six months to June 2008, income increased by 9 per cent. whilst costs increased by 5 per cent. as compared to the same period in 2007.

  All three divisions in Lloyds TSB have demonstrated growing levels of income per employee (pre-dislocation costs) and falling unit costs and Retail Banking and International Banking have demonstrated much reduced error rates in key processes in recent years; achieved without affecting investment in future growth. These improvements in operational effectiveness have led to a further reduction in the Lloyds TSB Group cost: income ratio to 46.6 per cent. for the six months to 30 June 2008, compared to 48.6 per cent. for the six months to 30 June 2007, and 50.6 per cent for the six months to 30 June 2006.

- *Capital and risk management*

  Lloyds TSB measures economic profit growth to determine where value is created or destroyed. It has developed a framework to measure economic equity requirements across all its businesses, taking into account market, credit, insurance, business and operational risk. Using economic profit as a key performance measure enables the Lloyds TSB Group to understand which strategies, products, channels and customer segments are creating the most value and to make better capital allocation decisions as a result. Lloyds TSB Group economic profit for the six months to June 2008 was £1,013 million[1], an increase of 7 per cent. over the same period in 2007.

  The application of these economic profit disciplines, alongside a strategy linked to ensuring that revenue growth exceeds cost growth, has contributed towards a significant improvement in the capital efficiency of the Lloyds TSB Group's Insurance and Investments division. This has been further improved by a shift in business mix towards sectors offering higher risk adjusted returns in wholesale banking. By the continued rigorous application of these disciplines at every level, the Lloyds TSB Group expects to further improve capital efficiency. Post-tax return on equity for the six months to 30 June 2008 was 26.8 per cent. compared with 26.1 per cent. for the six months to 30 June 2007.

The Lloyds TSB Directors believe that Lloyds TSB's relationship based business model, the efficiency of its operations and its effective capital and risk management position the Company well for future development.

3 Information on the HBOS Group

The HBOS Group is a leading and diversified financial services group engaged in a range of banking, insurance, asset management, financial services and finance-related activities throughout the United Kingdom and internationally (Ireland, Europe, North America and Australia). The HBOS Group's products and services can be categorised into the following business divisions:

(1) On a continuing business basis and excluding volatility provisions in respect of US dollar payments, impact of market dislocation and settlement of overdraft claims. Sourced from Lloyds TSB 2008 Interim Results Presentation.

- Retail;
- Corporate;
- Insurance & Investment;
- International; and
- Treasury & Asset Management.

As set out in HBOS's audited accounts for the financial year ended 31 December 2007 and extracted without material adjustment therefrom, HBOS reported net operating income of £21.3 billion and generated profit before taxation of £5.5 billion. For the six months ended 30 June 2008, HBOS reported net operating income of approximately £2.4 billion and generated profit before taxation of £848 million. HBOS reported total assets of £681.4 billion and shareholders' equity of £21.1 billion as at 30 June 2008.

In the first half of 2008, customers opened 478,000 new bank accounts, of which 77 per cent. were full facilities current accounts, which reflected an estimated market share of 21 per cent. of new current accounts opened during this period. In spite of strong competition throughout the first half of 2008, HBOS remained the largest liquid savings provider in the UK with a market share of 15.4 per cent. as at 30 June 2008. In the corporate business, new lending pricing improved in the first half of 2008 as competition in the market lessened. However, slower churn of the back book impacting the timing of fee recognition and higher funding costs exerted downward pressure on margins. For further information on the business of HBOS, please see Part VIII ("Information on the HBOS Group") of this document.

Information on the current trends and prospects for HBOS are set out in Part XIII ("HBOS Interim Management Statement 3 November 2008") of this document.

4 Rationale for the Acquisition

During the recent period of intense change in the banking industry, all banks have been forced to scrutinise their business models, available capital and funding requirements and make important strategic decisions for the future. In the execution of its stated strategy, the Lloyds TSB Board has always sought innovative ways to enhance shareholder value, both organically as well as through mergers and acquisitions. In particular, the Lloyds TSB Board has long recognised the enormous value which it believes could be obtained from the potential combination of Lloyds TSB and HBOS.

The Lloyds TSB Board believes that its success in the UK has resulted in it being in a strong position relative to its peers with new and exciting opportunities to create value. Whilst HBOS has been significantly affected by recent challenging market conditions, including the deteriorating economic environment which has negatively impacted its funding model, the Lloyds TSB Directors believe that HBOS remains an excellent franchise with the potential to contribute substantial value to the Enlarged Group. HBOS has a significant retail customer base and leading savings, mortgage and bancassurance franchises. HBOS also has an international multi-brand presence in the retail and insurance and investment markets, alongside a sound corporate banking franchise. Like Lloyds TSB, HBOS has a successful focus on cost discipline.

The Lloyds TSB Directors believe Lloyds TSB and HBOS are highly complementary. In addition to the cost savings and increased competitive strength expected to be achieved through enhanced size and scale, the combination is expected to create the largest current account base with the strongest mortgage brand and largest retail savings base in the UK. The Enlarged Group is also expected to have excellent breadth and balance with good positions in Retail, Corporate Banking, SME Business Banking and Long Term Savings. The Lloyds TSB Directors believe that the Enlarged Group's substantial customer base will give it excellent access to reliable, low volatility, sources of funding for growth. On the asset side, the Enlarged Group's focus on relationship lending and on robust credit policies is expected to enable sustainable lending growth within its relationship-led customer businesses at relatively low risk.

The Lloyds TSB Directors believe that the Enlarged Group will also be more competitive and significantly better placed to create shareholder value in a rapidly evolving UK banking industry than Lloyds TSB would on a standalone basis, primarily given the Enlarged Group's greater size and market presence. The Proposed Government Funding is designed to provide the Enlarged Group with significant capital strength and funding capabilities to meet the short-term challenges current markets present and support the longer-term prospects to create shareholder value. Lloyds

TSB is establishing plans for the integration of HBOS's businesses to deliver synergies and long-term value for all stakeholders of the Enlarged Group.

Going forward, successful banks will need to have deep customer reach backed up by robust capital and liquidity positions, with liability growth coming principally from retail and commercial deposits and with asset growth founded on the strongest possible credit risk management. They will also need class leading cost and capital efficiency to be economically profitable in a world where capital requirements are likely to be higher.

Both Lloyds TSB and HBOS are acknowledged leaders in efficiency and cost management. Even before actual synergies, the Lloyds TSB Directors believe the Enlarged Group will have one of the lowest cost:income ratios for financial institutions in the UK. Furthermore, the combined skills of the Enlarged Group in areas like lean management and straight-through processing is expected to allow the cost:income ratio to be reduced further over time whilst also further improving customer service. Allied to the Enlarged Group's combined focus on economic profit disciplines, this is expected to enable growth with high levels of profitability, even in a world of higher capital requirements.

The Lloyds TSB Directors believe that the Enlarged Group will have market leading distribution and sales capabilities, best of breed products and services as well as mid and back office processes that deliver a high quality customer experience. The Lloyds TSB Directors therefore believe that the Enlarged Group will be strongly positioned for this new environment.

Retail Banking

In Retail Banking, the Acquisition brings together two of the leading retailers in UK financial services, with strengths in customer relationship management, product design, branch sales processes and telephone and internet banking. The Lloyds TSB Directors believe that significant cost savings can be made by combining the networks and back offices of Lloyds TSB and HBOS whilst creating one of the largest and most effective retail franchises in the UK, enabling better access and service for customers. Future growth is expected to be driven from increased bank deposits, savings and investments. Allied to the Enlarged Group's strengths in savings and in wealth management, the Acquisition is expected to create the market leader in what is likely to be the fastest growing area of retail financial services.

Wholesale and International Banking

In wholesale and international banking, the combination of expertise and products across an enlarged distribution network and customer base is expected to generate material increases in revenues. Both Lloyds TSB and HBOS have focused on the attractive SME, commercial and mid-corporate segments. With the increasing sophistication of smaller and mid-sized companies' financial services needs, this is also expected to be a high growth area for the combined franchise. The Enlarged Group is expected to benefit from greater scale, closer segmentation and a broader range of products to grow its business. A focus on customer relationships, allied to strong credit risk management, is expected to deliver sustainable earnings growth from this business.

Insurance and Investments

The Lloyds TSB Directors believe that the Enlarged Group will have compelling propositions in General Insurance, Asset Management and Life, Pensions and Investment and that its customers will benefit from the deployment of best of breed products and efficient processes. Both Lloyds TSB and HBOS have well developed customer offerings in all three areas which will be combined to capture scale benefits whilst also providing enhanced product development and customer choice. There are also many complementary offerings expected to result from the Acquisition which are expected to provide bancassurance, IFA and institutional clients with a more wide ranging and improved service. The enlarged franchise is expected to build on its strong position and continue to provide good earnings growth.

Across the Enlarged Group, the Lloyds TSB Directors believe that the Proposed Government Funding will provide significant capital strength and funding capabilities to meet the challenges current markets present and support the creation of shareholder value. Lloyds TSB has a clear plan to integrate HBOS's business and deliver synergies and long-term value for all stakeholders of the Enlarged Group. Lloyds TSB expects that HM Treasury will, in accordance with its public statements, act as a value-oriented shareholder with regard to the strategic development of the Enlarged Group and the realisation of the significant expected cost synergies.

5 Financial Effects of the Acquisition

Since the announcement on 18 September 2008, Lloyds TSB has applied considerable resources to the quantification of potential benefits that would result from the combination of Lloyds TSB and HBOS. Following this detailed review, Lloyds TSB believes that through the implementation of cost synergies and other operational efficiencies it will deliver total pre-tax annual cost savings greater than £1.5 billion, or approximately 15.7 per cent. of the combined estimated Lloyds TSB and HBOS 2008 cost base[2], by the end of 2011[3,4].

Whilst Lloyds TSB believes that the combination with HBOS will generally provide enhanced opportunities for employees, there will inevitably be some rationalisation of the combined workforce as a result of these initiatives and consultation will take place with, among others, the recognised trade unions in respect of how this can best be achieved.

Lloyds TSB expects one-off integration costs to achieve these savings to be around 140 per cent. of the expected synergy run rate. It is anticipated that these costs will have been incurred or provided for by 31 December 2011. It is expected that the costs of implementation will significantly exceed the estimated synergy benefits in 2009.

The proposed synergy savings and associated implementation costs are subject to change if any disposals are made by the Enlarged Group.

The table below sets out information on the anticipated cost savings:

	Cost Savings Per Annum by end of 2011[4] (£ million)	*Number of Cost Saving Initiatives*
UK Retail Banking	790	21
Insurance and Investments	235	10
Wholesale and International Banking	430	25
Central and Support Functions and Other	45	5
Total	1,500	61

UK Retail Banking

The Acquisition brings together two of the leading retailers in UK financial services, with strengths in customer relationship management, product design, branch sales processes and in telephone and internet banking. The Lloyds TSB Directors believe that significant cost savings can be made by combining the networks and back offices of Lloyds TSB and HBOS whilst creating the largest and most effective retail franchise in the UK, enabling better access and service for Lloyds TSB and HBOS customers.

Cost savings in UK Retail Banking are expected to originate from:

- optimising the efficiency of the combined retail distribution infrastructure including branch network, call centre operations and associated management and support functions;
- streamlining branch based functions across operations;
- integrating the processing capabilities and information technology platforms of Lloyds TSB and HBOS; and
- removing other areas of duplication across the UK Retail Banking platforms.

Total annual pre-tax cost savings from UK Retail Banking by the end of 2011 are currently estimated to be £790 million.

(2) Addressable cost base, 12 months to 30 June 2008.
(3) The expected synergies have been calculated by Lloyds TSB on the basis of the existing cost and operating structures of Lloyds TSB and HBOS. Statements of estimated synergies, and calculations of the one-off costs of achieving them, relate to future actions and circumstances which, by their nature, involve risks, uncertainties, contingencies and other factors. As a result, the synergies referred to may not be achievable, or those achieved may be materially different from those estimated.
(4) Run rate at 31 December 2011.

Insurance and Investments

The Lloyds TSB Directors believe that the combination provides the Lloyds TSB Group with compelling propositions in General Insurance, Fund Management and Life, Pensions and Investment and that the Enlarged Group's customers will benefit from the deployment of best of breed products and processes.

Cost savings in Insurance and Investments are expected to originate from:

- combining manufacturing in life and pensions;
- combining the best elements of each business's bancassurance and IFA product sets and distribution models;
- creating a single integrated sales structure, consolidating operating platforms and introducing consistent claims processing in General Insurance;
- integration of fund management activities; and
- removing duplicated roles in support functions.

Total annual pre-tax cost savings from Insurance and Investments by the end of 2011 are currently estimated to be £235 million.

Wholesale and International Banking

Both Lloyds TSB and HBOS have focused on the attractive SME, commercial and mid-corporate segments. The financial services needs of smaller and mid-sized companies are becoming increasingly sophisticated and this is also expected to be the fastest growing area of wholesale banking. The Lloyds TSB Directors believe that the Enlarged Group will benefit from better reach, closer segmentation and a broader range of products to grow its business. It is also expected to represent a significant cost-saving opportunity.

Cost savings in Wholesale and International Banking are expected to originate from:

- rationalising commercial and corporate banking approach and removing overlapping management and support functions;
- integrating the processing capabilities and information technology platforms; and
- removing other areas of duplication across Wholesale and International Banking.

Total annual pre-tax cost savings from Wholesale Banking by the end of 2011 are currently estimated to be £430 million.

Central and Support Functions and Other

The integration of HBOS with Lloyds TSB will also provide the opportunity to make further cost savings from the consolidation of central group corporate and support functions. Based on Lloyds TSB's initial assessment, potential net funding synergies are not considered to be material.

Total annual pre-tax cost savings from Central and Support Functions and Other by the end of 2011 are currently estimated to be £45 million.

Revenue Opportunities

It is expected that there will be the opportunity for significant revenue enhancements as a result of the combination. A wide range of key potential initiatives have been considered but are not incorporated in this numerical analysis.

Basis of Preparation

The evaluation of cost synergies has been jointly undertaken by a broad group of senior and operational management from both Lloyds TSB and HBOS. These estimates have been based on a detailed assessment of the pro forma cost structure of the combined Lloyds TSB and HBOS businesses and a detailed bottom up analysis of the efficiency cost savings that are available following the transaction. Lloyds TSB and HBOS management have applied their understanding of the relative productivity levels between Lloyds TSB and HBOS, experience in delivering operational efficiency improvements, as well as industry benchmarks, to determine the cost savings.

The principal areas for cost savings have been identified and each area carefully scrutinised through a detailed review process involving external advisers. Each individual saving initiative is supported by an implementation plan which is being developed by the relevant management team.

In determining the estimate of cost savings achievable through the combination of Lloyds TSB and HBOS, Lloyds TSB has not included any savings relating to operations where no overlap exists.

In assessing the financial effects of the Acquisition, the Lloyds TSB Directors have been mindful to compare the Enlarged Group, including the impact of the Acquisition and the Proposed Government Funding, with Lloyds TSB on a standalone basis (adjusted for the impact of further new capital that Lloyds TSB has been advised by the FSA it would be required to raise, if the Acquisition were not to occur). Whether or not the Acquisition completes, Lloyds TSB will be required to raise significant capital.

On this basis, it is expected that the Acquisition will lead to accretion in Lloyds TSB's cash earnings per share in excess of 20 per cent. in 2010[5]. Cash earnings per share excludes amortisation of intangibles and fair value adjustments and includes cost synergies.

6 Summary of the Terms of the Acquisition

Under the terms of the Acquisition, and subject to the Conditions, HBOS Shareholders will be entitled to receive 0.605 Consideration Shares for every 1 HBOS Share. Holders of HBOS ADRs will be entitled to receive 0.15125 Consideration ADRs for each HBOS ADR cancelled in connection with the Acquisition.

These exchange ratios assume that neither HBOS nor Lloyds TSB has declared or paid, and will not declare or pay, any dividend in respect of ordinary shares after 13 October 2008, being the date of the announcement of revised terms of the Acquisition.

Based on the Closing Price of 179.2 pence per Lloyds TSB Share on 29 October 2008, being the last practicable Business Day prior to publication of this document, the Acquisition values each HBOS Share at 108.4 pence and the existing issued ordinary share capital of HBOS at approximately £5.9 billion.

Upon the Acquisition becoming Effective, if none of the Lloyds TSB Shareholders (in relation to the Lloyds TSB Placing and Open Offer) nor the HBOS Shareholders (in relation to the HBOS Placing and Open Offer) participate in the clawback, existing Lloyds TSB Shareholders will own 36.5 per cent. of the Enlarged Group with existing HBOS Shareholders owning 20.0 per cent. of the Enlarged Group. In such circumstances, the remaining 43.5 per cent. will be owned by HM Treasury. To the extent the Lloyds TSB Shareholders and the HBOS Shareholders (in relation to the HBOS Placing and Open Offer) fully participate in the clawback, existing Lloyds TSB Shareholders will own 52.4 per cent. of the Enlarged Group, existing HBOS Shareholders will own 47.6 per cent. of the Enlarged Group and HM Treasury will own 0 per cent.

The Consideration Shares will be issued credited as fully paid and will rank *pari passu* in all respects with the existing Lloyds TSB Shares in issue at the time the Consideration Shares are issued pursuant to the Acquisition, including the right to receive and retain dividends and other distributions declared, made or paid (if any) by reference to a record date falling after the Effective Date.

Applications will be made to the UK Listing Authority for the Consideration Shares to be admitted to the Official List and to the London Stock Exchange for the Consideration Shares to be admitted to trading on the London Stock Exchange's main market for listed securities. It is expected that Admission of the Consideration Shares will occur and that dealings in the Consideration Shares on the London Stock Exchange will commence in mid-January 2009. A supplemental listing application will be made to the NYSE for the Consideration Shares to be issued pursuant to the Acquisition to be listed on the NYSE for trading in the form of Consideration ADRs.

Any new HBOS Shares issued to Lloyds TSB or its nominee(s) pursuant to the Scheme will be issued fully paid and free from all liens, charges, equitable interests, encumbrances and rights of pre-emption and any other interests of any nature whatsoever and together with all rights attaching thereto. In the event that the Acquisition is implemented by means of an Offer, the HBOS Shares will be acquired pursuant to such Offer on the same basis.

The Acquisition is subject to antitrust review in a number of jurisdictions, including (but not limited to) the United Kingdom and the United States. Following an intervention by the Secretary of State for Business, Enterprise and Regulatory Reform (the "Secretary of State") in relation to the UK

(5) This statement is not intended to constitute a profit forecast for any period and should not be interpreted to mean that earnings or earnings per share will necessarily be greater than those for any preceding financial period for either Lloyds TSB or HBOS.

antitrust review on public interest grounds (i.e. stability of the UK financial system), the Secretary of State gave regulatory clearance to the Acquisition on 31 October 2008 after concluding that it is in the public interest.

Lloyds TSB and HBOS expect all remaining anti-trust clearances to have been obtained by mid-January 2009. Under the Implementation Agreement, Lloyds TSB and HBOS have agreed to co-operate to obtain all regulatory approvals as promptly as reasonably possible.

7 Summary of the Terms of the Placing and Open Offer

Under the Placing and Open Offer, Lloyds TSB intends to invite Qualifying Shareholders to apply to acquire 2,596,653,203 Open Offer Shares at the Issue Price, raising approximately £4.5 billion (before costs and expenses). Citi, Merrill Lynch and UBS have agreed to use reasonable endeavours to procure placees to take up Open Offer Shares at the Issue Price subject to the passing of certain of the Resolutions and Admission and subject to clawback in respect of valid applications by Qualifying Shareholders at the Issue Price.

The Issue Price represents an 8.5 per cent. discount to the Closing Price of 189.4 pence per Lloyds TSB Share on 10 October 2008.

Qualifying Shareholders, subject to the terms and conditions of the Open Offer, will be given the opportunity under the Open Offer to apply for Open Offer Shares at the Issue Price on the basis of 0.4347 Open Offer Shares for every existing Lloyds TSB Share.

Entitlements to Open Offer Shares will be rounded down to the nearest whole number and fractional entitlements will not be offered to persons pursuant to the Placing and Open Offer but will be aggregated and sold in the market for the benefit of Lloyds TSB. Holdings of Lloyds TSB Shares in certificated and uncertificated form will be treated as separate holdings for the purpose of calculating entitlements under the Open Offer as will holdings under different designations and in different accounts.

An Excess Application Facility will enable Qualifying Shareholders to apply for Open Offer Shares in excess of their Open Offer Entitlement. Further details in relation to the Excess Application Facility will be set out in the Prospectus and the Application Form.

The Open Offer is conditional, *inter alia*, upon:

(i) the Placing and Open Offer Agreement having become unconditional in all respects save for the condition relating to Admission;

(ii) the HBOS Placing and Open Offer Agreement having become unconditional in all respects save for the condition relating to admission of the HBOS Shares issued pursuant to the HBOS Placing and Open Offer;

(iii) Admission of the Open Offer Shares becoming effective by not later than 8.00 a.m. on 19 January 2009 (or such later time and date as HM Treasury may agree); and

(iv) the passing, without amendment, of Ordinary Resolutions 1, and 3 only.

To the extent Open Offer Shares are not placed or taken up under the Open Offer, subject to the terms of the Placing and Open Offer Agreement and the Scheme having been sanctioned at the First Court Hearing, HM Treasury will itself acquire such Open Offer Shares.

The Open Offer Shares, when issued and fully paid, will rank *pari passu* in all respects with the existing Lloyds TSB Shares including the right to receive dividends or distributions made, paid or declared (if any) after the date of this document.

Applications will be made to the UK Listing Authority for the Open Offer Shares to be admitted to the Official List and to the London Stock Exchange for the Open Offer Shares to be admitted to trading on the London Stock Exchange's main market for listed securities.

It is expected that Admission of the Open Offer Shares will occur and that dealings in the Open Offer Shares on the London Stock Exchange will commence in mid-January 2009.

The Placing and Open Offer is conditional on, *inter alia*, the matters set out in (i) to (iv) above and upon the Scheme being sanctioned at the Scheme Court Hearing. Certain of the conditions may be waived by the Treasury in its discretion. The Acquisition is also conditional on the passing of Ordinary Resolutions 1 and 3 at the Lloyds TSB General Meeting; the passing of various resolutions at the HBOS General Meeting and the Court Meeting; and all regulatory conditions and consents having been obtained or waived.

Accordingly, the Placing and Open Offer and the Acquisition are interconditional. If the Resolutions on which the Placing and Open Offer or the Acquisition are conditional are not approved or for some other reason the Placing and Open Offer Agreement is terminated or the Acquisition does not complete, HM Treasury has stated that, in that event, it would expect Lloyds TSB to take appropriate action to address its capital position in the light of the policy objectives set out in HM Treasury's announcement of 8 October 2008 on Financial Support to the Banking Industry.

The FSA has advised Lloyds TSB that if the Acquisition were not to occur, it would require Lloyds TSB to raise £7 billion of additional capital, made up of £5 billion of Core Tier 1 equity and £2 billion of Tier 1 instruments. Whilst Lloyds TSB would be able to seek to raise such additional new capital in the public markets, there can be no certainty that Lloyds TSB would be able to successfully raise such capital or as to the terms on which such capital could be raised, including the terms of any participation by HM Treasury in any such capital raising or as to whether any such fund raising would be on a pre-emptive basis.

Further information in relation to the Placing and Open Offer will be contained in the Prospectus, including some questions and answers in relation to the Placing and Open Offer, together with the terms and conditions of the Placing and Open Offer and the procedure for acceptance and payment. The Prospectus is expected to be made available to Qualifying Shareholders on the Lloyds TSB website (www.investorrelations.lloydstsb.com) in mid-November 2008.

8 New Preference Share Issue

Under the Preference Share Subscription Agreement, Lloyds TSB intends to issue to HM Treasury 1,000,000 New Preference Shares at the issue price of £1,000 per New Preference Share, raising approximately £1 billion (before costs and expenses). Lloyds TSB intends to seek a listing for the New Preference Shares. The New Preference Share Issue is conditional upon the Placing and Open Offer Agreement becoming unconditional in accordance with its terms.

The New Preference Shares rank ahead of the Lloyds TSB Shares. The New Preference Shares do not carry voting rights at general meetings of Lloyds TSB, save in limited circumstances (including if dividends on the New Preference Shares are not paid) described in paragraph 9.1.4 of Part XII ("Additional Information") of this document.

The New Preference Shares will pay a fixed non-cumulative dividend of 12 per cent. per annum, payable semi-annually in arrear, for the first five years after their issue. Thereafter, they will pay a variable dividend, equal to three month sterling LIBOR plus 7 per cent., payable quarterly in arrear. The payment of such dividends is at the sole discretion of the Lloyds TSB Board, however, if such dividends have not been paid in full, holders of the New Preference Shares will be entitled to vote in certain circumstances (see paragraph 9.1.4 of Part XII ("Additional Information") of this document for further information).

For as long as dividend payments have not been made on the New Preference Shares, Lloyds TSB may not (subject to certain exceptions) declare or pay cash dividends or other distributions upon any parity or junior securities, or redeem, repurchase or otherwise acquire any such securities.

In addition, until the Enlarged Group HMT Preference Shares are redeemed or purchased in full, Lloyds TSB may not declare or pay any cash dividend on its ordinary shares or redeem, purchase, cancel or otherwise acquire any of its ordinary shares or effect a reduction of its ordinary share capital which involves a distribution to holders of the ordinary shares.

The New Preference Shares will be issued credited as fully paid and, on any liquidation, will rank *pari passu* in all respects with the most senior preference shares then in issue and any other class of shares in issue at the time the New Preference Shares are issued pursuant to the Preference Share Subscription Agreement, or to be issued, which are expressed to rank equally with the New Preference Shares.

Subject to notifying the FSA and being in compliance with its capital adequacy requirements (to the extent they apply at the time), Lloyds TSB has the right to redeem the New Preference Shares at the liquidation preference of £1,000 plus accrued dividends, in whole or in part, with effect from the date five years and one day after their issue.

In addition to the £1 billion of new preference shares being issued by Lloyds TSB, HBOS is also issuing £3 billion of new preference shares to HM Treasury. Accordingly, upon completion of the Acquisition and the HBOS Preference Share Scheme, HM Treasury will own £4 billion Enlarged Group HMT Preference Shares. As the terms of the New HBOS Preference Shares and the New Preference Shares contain similar provisions, including the restrictions as to ordinary dividends set out above, the Enlarged Group will need to repurchase or redeem an aggregate of £4 billion of new preference shares before payment of dividends on ordinary shares can be resumed.

9 Dividend Policy, Capitalisation Issue and Capital Position

Dividend Policy and Capitalisation Issue

No dividend may be paid on the Lloyds TSB Shares while any of the Enlarged Group HMT Preference Shares are outstanding, unless otherwise agreed by HM Treasury. However, the Lloyds TSB Board recognises the importance of dividends to Shareholders and its clear intention is to achieve the repurchase of the Enlarged Group HMT Preference Shares during 2009 so as to enable it to resume the payment of dividends.

However, the restriction on payment of dividends does not preclude the declaration of a capitalisation issue paid out of non-distributable reserves. Lloyds TSB intends to issue shares by way of Capitalisation Issue for the 2008 financial year at a level to be determined by the Board of Lloyds TSB at the appropriate time.

Repurchases of the Enlarged Group HMT Preference Shares would be subject to FSA approval and would take account of the Group's capital position at the time of the proposed repurchase and prevailing market conditions. The Enlarged Group HMT Preference Shares can be repurchased using replacement Tier 1 capital, retained earnings, the proceeds of disposals (to the extent that these are in excess of the book value of assets disposed), gross reductions in risk-weighted assets or as otherwise permitted by the FSA. Repurchase within five years will also require approval of the holders of the Enlarged Group HMT Preference Shares.

HM Treasury has indicated its encouragement that the Preference Shares be repurchased as soon as practicable, applying a repurchase price of 101 per cent. of nominal value for six months after the close of the Placing and Open Offer and, thereafter, a price reflecting prevailing market conditions (with no value to be attributed to the fact that upon repurchase by the Company it may become able to pay dividends). Any such repurchase arrangements will be subject to such constraints as are necessary to ensure the Enlarged Group HMT Preference Shares constitute Tier 1 capital. HM Treasury has agreed that if it were to dispose of any of the Enlarged Group HMT Preference Shares, it would either impose on any buyer an obligation to allow Lloyds TSB to repurchase the relevant Enlarged Group HMT Preference Shares on the repurchase terms set out above, or (at HMT's sole discretion) release the restriction on payment of dividends. This would be done in a manner consistent with maintaining the Enlarged Group HMT Preference Shares' Tier 1 treatment.

Lloyds TSB will assess the range of options available to allow the repurchase in full of the Enlarged Group HMT Preference Shares as set out above and intends, subject to prevailing market conditions and the restrictions described above, to achieve this during 2009 so that the block on the payment of cash ordinary dividends will be removed. This will allow the Lloyds TSB Board to resume the payment of cash ordinary dividends. The timing of recommencement and the level of dividend will be determined with due regard for the trading and economic environment and the Lloyds TSB Group's capital position at that time.

Capital Position

Based on a review of non-public information provided by HBOS, Lloyds TSB has made a preliminary assessment that net negative capital adjustments of no more than £10 billion after tax would need to be made to HBOS's financial position for Core Tier 1 capital purposes as a result of the Acquisition. The amount of the capital adjustments takes into account the elimination of the HBOS available for sale ("AFS") reserve at 30 September 2008 and includes the effect of the application of market based credit spreads at September 2008 to HBOS's portfolios. A comprehensive assessment of the fair values of HBOS's assets will be undertaken following completion of the Acquisition, the provisional results of which will be published in Lloyds TSB's 2009 interim report. The actual capital adjustments will reflect the conditions that exist at the Effective Date of the Acquisition.

Based on published information at 30 June 2008, and taking into account Lloyds TSB's equity placing completed on 19 September 2008, the Placing and Open Offer, HBOS's rights issue announced on 29 April 2008 and the HBOS Placing and Open Offer as well as the net negative capital adjustments to HBOS's financial position referred to previously, Lloyds TSB estimates that the Enlarged Group would have had a Core Tier 1 ratio of 8.8 per cent. at 30 June 2008. In calculating this Core Tier 1 ratio no account has been taken of the trading performance of Lloyds TSB or HBOS or of other transactions by Lloyds TSB or HBOS since 30 June 2008, including the sale by HBOS of BankWest and St Andrews, except for the equity placing completed by Lloyds TSB on 19 September 2008. Lloyds TSB has made a preliminary assessment that net negative capital adjustments of no more than £10 billion after tax would need to be made to HBOS's financial position for core Tier 1 capital purposes as a result of the Acquisition, the effect of which would mean that the Enlarged Group would have a Core Tier 1 ratio in excess of 7 per cent.

The impact of the negative capital adjustments referred to above on the Enlarged Group's net tangible assets is reduced by the amount of the HBOS available for sale ("AFS") reserve which at 30 September 2008 amounted to approximately £4 billion.

In addition, the review of non-public information provided by HBOS has identified a positive fair value adjustment for the Enlarged Group's net tangible assets in respect of HBOS's own debt. This is of a similar magnitude to the capital adjustments affecting Core Tier 1 capital (excluding the AFS reserve adjustment) but will be affected, and could theoretically be eliminated by, *inter alia*, movements in credit spreads on HBOS's debt between the date of the review and the Effective Date.

The Enlarged Group has set a target core Tier 1 capital ratio range of 6-7 per cent.

10 Directors, Management and Employees

Lloyds TSB attaches great importance to the skills and experience of the existing management and employees of HBOS. The management structure of the Enlarged Group will be assembled from the combined skills and experience of the current Lloyds TSB and HBOS teams.

The Lloyds TSB Board has also given assurances to the HBOS Directors that, following the Acquisition becoming Effective, the existing contractual employment rights of all employees of the HBOS Group will be fully safeguarded.

As announced on 18 September 2008, Sir Victor Blank will be Chairman and Eric Daniels will be Chief Executive of the Enlarged Group. On 30 October 2008, Lloyds TSB announced that the following Lloyds TSB Board, Company Secretary and other Group Executive Committee appointments will be made to the Enlarged Group following completion of the Acquisition:

- Helen Weir will be appointed as Group Executive Director of UK Retail Banking.
- Truett Tate will be appointed Group Executive Director of Wholesale.
- Archie Kane will be appointed Group Executive Director of Insurance and will represent the new board in Scotland.
- Tim Tookey will be appointed Group Finance Director.
- Harry Baines will be appointed General Counsel and Company Secretary.
- Jo Dawson will be appointed Wealth and International Director.
- Carol Sergeant will be appointed Chief Risk Officer.
- Angie Risley will be appointed Group Human Resources Director.
- Chris Wiscarson will be appointed Group Integration Director.

Pursuant to the conditions attaching to the Proposed Government Funding, a summary of which is set out in Part V of this document, HM Treasury will work with the Lloyds TSB Board on its appointment of two new independent directors following completion of the Acquisition. Thereafter, consistent with best practice, the Company will engage constructively with HM Treasury in its role as a shareholder.

11 Co-operation from HBOS: the Implementation Agreement and Inducement Fee Arrangements

Lloyds TSB and HBOS have entered into an implementation agreement which governs their relationship during the period until the Acquisition becomes Effective or lapses. Among other things, the parties have agreed to co-operate with regard to the process of implementing the Acquisition. The Implementation Agreement will terminate (without prejudice to any obligations on HBOS to pay the inducement fee (see below)) in certain circumstances, including if the Scheme or the Acquisition is not approved at the Court Meeting or the HBOS General Meeting or the Lloyds TSB General Meeting (as appropriate).

Under the Implementation Agreement, HBOS has agreed to pay Lloyds TSB an inducement fee (inclusive of value added tax (if any)) of one per cent. of the offer value under the Acquisition (based on the Closing Price of a Lloyds TSB Share on the Business Day prior to the occurrence of the relevant event below) if, *inter alia*:

- the HBOS Directors do not unanimously and without qualification recommend the HBOS Shareholders to vote in favour of the Scheme; or
- at any time after approval of the Scheme by HBOS Shareholders at the Court Meeting but before the grant of the Court Orders, the HBOS Directors, in exercise of their fiduciary duties, decide not to proceed with the Scheme; or
- without the consent of Lloyds TSB, HBOS withdraws the Scheme or takes steps to defer (or adjourn) the holding of the Court Meeting or the HBOS General Meeting or the Court Hearings to approve the Scheme to a date later than 28 February 2009; or
- a Competing Proposal is announced prior to the Scheme lapsing or being withdrawn, which Competing Proposal subsequently becomes or is declared wholly unconditional or is completed.

12 Pensions

Lloyds TSB and HBOS will continue to pay regular contributions to all group pension schemes in accordance with the current contribution schedules agreed from time to time with the trustees of each scheme. It is expected that the funding and investment strategy in relation to the defined benefit schemes will be reviewed and discussed with the trustees during the 15-month period following the triennial actuarial valuations of the schemes. The valuation date is expected to be 31 December 2009 for the HBOS Final Salary Pension Scheme and was 30 June 2008 for the Lloyds TSB Group Pension Scheme No. 1 and the Lloyds TSB Group Pension Scheme No. 2.

13 Settlement, Listing and Dealing of Open Offer Shares, Consideration Shares and Consideration ADRs

The existing Lloyds TSB Shares are already admitted to CREST. It is expected that all of the Open Offer Shares and Consideration Shares, when issued and fully paid, will be capable of being held and transferred by means of CREST or in certificated form. It is expected that the Open Offer Shares and the Consideration Shares will trade under ISIN GB0008706128.

A supplemental listing application will be made to the NYSE for the Consideration Shares to be listed on the NYSE for trading in the form of Consideration ADRs. The Consideration ADRs will be issued subject to the terms and conditions of the Lloyds TSB Deposit Agreement.

14 Rule 9 Waiver

Following the completion of the Placing and Open Offer and the Acquisition, if none of the existing Lloyds TSB Shareholders acquire any Open Offer Shares pursuant to the Placing and Open Offer and none of the existing HBOS Shareholders acquire any HBOS Shares pursuant to the HBOS Placing and Open Offer, HM Treasury would hold a maximum of 7,123,501,794 Lloyds TSB Shares (representing approximately 43.5 per cent. of the enlarged issued ordinary share capital of Lloyds TSB).

Rule 9 of the City Code is designed to prevent the acquisition or control of a company to which the City Code applies without a general cash offer being made to all shareholders of that company.

Under Rule 9, when any person acquires, whether by a series of transactions over a period of time or not, an interest in shares (as defined in the City Code) which (taken together with shares in which persons acting in concert with him are interested) carry 30 per cent. or more of the voting rights of a company which is subject to the City Code, that person is normally obliged to make a general cash offer to all the remaining shareholders of the company to acquire their equity shares and transferable securities carrying voting rights in the company.

Furthermore, under Rule 9 when a person, together with persons acting in concert with him, is interested in shares which in the aggregate carry not less than 30 per cent. of the voting rights of a company but does not hold shares carrying more than 50 per cent. of such voting rights and such person, or any person acting in concert with him, acquires an interest in any other shares which increases the percentage of shares carrying voting rights in which he is interested, that person is normally obliged to make a general cash offer to all the remaining shareholders of the company to acquire their equity shares and transferable securities carrying voting rights in the company.

However, where the obligation to make a mandatory offer under Rule 9 might arise following an issue of new shares, the Panel will normally consent to a waiver of that obligation provided that, among other things, this is approved by a vote of independent shareholders. In this case, the Panel has been consulted and has agreed, subject to the passing on a poll by the Lloyds TSB Shareholders, other than HM Treasury, of Ordinary Resolution 2 set out in the notice convening the Lloyds TSB General Meeting, to waive the obligation to make a general offer to Lloyds TSB Shareholders under Rule 9 that might otherwise arise on HM Treasury upon completion of the Placing and Open Offer and the Acquisition

Following the Lloyds TSB General Meeting and depending, among other things, on the number of shares acquired by Lloyds TSB Shareholders pursuant to the Placing and Open Offer and the number of shares acquired by HBOS Shareholders pursuant to the HBOS Placing and Open Offer, HM Treasury may in aggregate hold shares carrying more than 30 per cent. but not more than 50 per cent. of the Enlarged Group's voting share capital. In such circumstances any further increase by HM Treasury in its aggregate interests in shares will be subject to the provisions of Rule 9.

15 Current Trading, Trends and Prospects

Lloyds TSB issued an interim management statement on 3 November 2008 commenting on trading since the interim results of the current financial year. This is set out in full in Part VII ("Information on the Lloyds TSB Group") of this document however the highlights are summarised below:

- Lloyds TSB continues to trade well and deliver good income growth from its relationship businesses in an immensely challenging period for financial services companies. However, the impact of market dislocation, insurance related volatility and higher impairments, particularly in Lloyds TSB's corporate lending portfolios, has led to a substantial reduction in statutory profit before tax in the first nine months of the year.
- Excluding the impact of market dislocation and insurance related volatility, each division has achieved revenue growth in excess of cost growth.
- Lloyds TSB has continued to capture market share in a number of key areas, whilst improving new business product margins.
- Lloyds TSB has maintained its strong liquidity and funding position, with its wholesale funding maturity profile at a similar level to twelve months ago.
- Lloyds TSB remains on track to deliver a good trading performance in 2008, notwithstanding the continued deterioration in the UK economic environment.

Against the backdrop of current economic uncertainty, the Lloyds TSB Board has confidence in the opportunities available to the Enlarged Group. The Lloyds TSB Directors believe that the Enlarged Group will be more competitive and will be better placed to create sustainable shareholder value than Lloyds TSB would on a standalone basis in what is now a materially more challenging market environment. The Lloyds TSB Directors therefore believe that the Enlarged Group will be strongly positioned for this new environment.

HBOS also issued an interim management statement on 3 November 2008, which is set out in full in Part XIII ("HBOS Interim Management Statement 3 November 2008") of this document.

16 Lloyds TSB General Meeting

The notice convening the Lloyds TSB General Meeting to be held at the Scottish Exhibition and Conference Centre, Glasgow G3 8YW at 11:00 a.m. on 19 November 2008 is set out at the end of this document. The purpose of the meeting is to approve certain resolutions, including in connection with the Acquisition and the Placing and Open Offer, a summary of which is set out below:

The Acquisition

Ordinary Resolution 1

This resolution will be proposed as an ordinary resolution requiring a simple majority of votes in favour.

This resolution proposes to approve the Acquisition and to authorise the Lloyds TSB Board to make such waivers, extensions, amendments or variations to any of the terms and conditions of the Acquisition and to take all such steps as may be necessary in connection with the Acquisition.

The Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution.

Rule 9 Waiver

Ordinary Resolution 2

This resolution will be proposed as an ordinary resolution requiring a simple majority of votes in favour and will be taken on a poll. In accordance with the City Code, HM Treasury shall not be entitled to vote on this resolution.

Ordinary Resolution 2 proposes to approve the waiver granted by the Panel of the obligation that might otherwise arise on HM Treasury to make a general offer to Lloyds TSB Shareholders as a result of the issue of new Lloyds TSB Shares to HM Treasury pursuant to the Placing and Open Offer and the Acquisition.

The Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution (unless waived by HM Treasury).

The Consideration and Open Offer Shares, New Preference Shares and Replacement Lloyds TSB Preference Shares

Ordinary Resolution 3

This resolution will be proposed as an ordinary resolution requiring a simple majority of votes in favour.

Ordinary Resolution 3 proposes:

- to increase the Company's authorised share capital by £3,884,227,055 by the creation of 14,911,908,221 Lloyds TSB Shares and 625,000,000 Lloyds TSB Preference Shares. This represents an increase of approximately 213 per cent. in the authorised ordinary share capital of the Company and 357 per cent. in the authorised sterling preference share capital as at 29 October 2008, the last practicable date before the publication of this document. This will enable the Company to issue sufficient Consideration Shares, Open Offer Shares and Replacement Lloyds TSB Preference Shares for the purposes of the Acquisition, Placing and Open Offer, HBOS Preference Share Scheme (respectively) and also for general headroom purposes (including in connection with the Capitalisation Issue); and
- to authorise the Lloyds TSB Board to allot the new shares being issued pursuant to Ordinary Resolution 3. The Lloyds TSB Directors at present intend to use this authority to allot some of these Lloyds TSB Shares pursuant to the Acquisition and the Placing and Open Offer, to allot some of these Lloyds TSB Preference Shares pursuant to the HBOS Preference Share Scheme and to allot some of these Lloyds TSB Shares pursuant to any capitalisation effected under the authority covered by Ordinary Resolution 4. This authority will expire on the day of the annual general meeting in 2009 or on 7 August 2009, whichever is the earlier. This authority would relate to Lloyds TSB Shares representing approximately 274 per cent. of the current ordinary issued share capital.

The Acquisition, the Placing and Open Offer, the New Preference Share Issue, the HBOS Preference Share Scheme and the Capitalisation Issue are conditional on the passing of this resolution.

Capitalisation Issue

Ordinary Resolution 4

This resolution will be proposed as an ordinary resolution requiring a simple majority of votes in favour. This resolution is conditional upon Ordinary Resolution 3 being passed.

Ordinary Resolution 4 proposes to authorise the Lloyds TSB Board to capitalise an amount out of the sums standing to the credit of any of the Company's share premium account, capital redemption reserve or other undistributable reserve of up to the maximum amount standing to the credit of such reserves and to authorise the Board to apply such amount in paying up the new Lloyds TSB Shares and to take all such other steps as it may deem necessary, expedient or appropriate to implement such capitalisation.

None of the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution.

Directors' Remuneration

Ordinary Resolution 5

This resolution will be proposed as an ordinary resolution requiring a simple majority of votes in favour.

Ordinary Resolution 5 proposes to increase the ordinary remuneration of the Lloyds TSB Directors, to be divisible among them, to a sum not exceeding £1,000,000 in any year. This resolution would increase the total amount of fees that can be paid to the directors from £750,000 to £1,000,000 in any year. The current amount of £750,000 was approved by Lloyds TSB Shareholders in 2006. This proposed increase is in anticipation of an enlarged Lloyds TSB Board following completion of the Acquisition.

None of the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution.

Share Buy-back

Ordinary Resolution 6

This resolution will be proposed as an ordinary resolution requiring a simple majority of votes in favour.

Ordinary Resolution 6 proposes to grant the Lloyds TSB Board a general authority to repurchase the Enlarged Group HMT Preference Shares on such terms as the Lloyds TSB Board may from time to time determine but subject to certain parameters as set out in the resolution itself.

None of the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution.

Section 89 disapplication

Special Resolution 7

This resolution will be proposed as a special resolution requiring a 75 per cent. majority of votes in favour.

Special Resolution 7 proposes to renew the power conferred on the Lloyds TSB Directors by article 9.3 of the Company's articles of association for the period from the date of the Lloyds TSB General Meeting to the day of the annual general meeting in 2009 or on 7 August 2009, whichever is the earlier, and for that period the section 89 amount shall be £205,577,100 if Ordinary Resolution 3 is passed (equivalent to 822,308,400 ordinary shares of 25 pence each in the capital of the Company) or £75,647,511 if Ordinary Resolution 3 is rejected (equivalent to 302,590,044 ordinary shares of 25 pence each in the capital of the Company). This resolution would, following the cash placing undertaken and announced by the Company, on 19 September 2008, renew the Lloyds TSB Board's power to issue shares for cash to persons other than existing Lloyds TSB Shareholders provided that any such issue of Lloyds TSB Shares to these persons would represent no more than 5 per cent. of the issued ordinary share capital of the Company. In addition, if the Company were to purchase its own shares and hold them in treasury, this resolution would give the Lloyds TSB Board power to sell these shares for cash to persons other than existing Lloyds TSB Shareholders, subject to the same limit that would apply to issues of shares for cash to these persons.

None of the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution.

Change of name

Special Resolution 8

This resolution will be proposed as a special resolution requiring a 75 per cent. majority of votes in favour.

Special Resolution 8 proposes that, subject to the Acquisition being authorised pursuant to Ordinary Resolution 1 above and becoming unconditional, to change the Company's name to Lloyds Banking Group plc.

This resolution is conditional on the Acquisition being completed. None of the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme are conditional on the passing of this resolution.

In accordance with article 62.1 of the Company's articles of association, the Lloyds TSB Board has determined that holders of limited voting shares shall be entitled to vote in respect of such shares on Ordinary Resolution 1 only.

The full text of the Resolutions is set out in the notice convening the Lloyds TSB General Meeting at the end of this document.

In the event that either or both Ordinary Resolution 1 and Ordinary Resolution 3 are not passed, none of the Acquisition, the Placing and Open Offer, the New Preference Share Issue and the HBOS Preference Share Scheme will proceed.

17 Action to be taken

You will find enclosed with this document a Form of Proxy for use at the Lloyds TSB General Meeting or at any adjournment thereof. You are requested to complete and sign the Form of Proxy whether or not you propose to attend the Lloyds TSB General Meeting in person in accordance with the instructions printed on it and return it as soon as possible, but in any event so as to be received no later than 11.00 a.m. on 17 November 2008, by the Company's Registrar, Equiniti. CREST members may also choose to utilise the CREST electronic proxy appointment service in accordance with the procedures set out in the notice convening the Lloyds TSB General Meeting at the end of this document. The lodging of the Form of Proxy (or the electronic appointment of a proxy) will not preclude you from attending and voting at the meeting in person if you so wish.

18 Further Information

Your attention is drawn to the further information set out in Parts II (''Risk Factors'') to XII (''Additional Information'') of this document. You should read the whole of this document and should not rely solely on the information set out in this letter. **In particular, you should read the risk factors set out in the section headed ''Risk Factors'' on pages 29 to 46 of this document.**

19 Recommendation

The Lloyds TSB Board considers that the Acquisition and the Resolutions are in the best interests of Lloyds TSB and the Lloyds TSB Shareholders as a whole.

The Lloyds TSB Board has received financial advice in respect of the Acquisition from Citi, Lazard, Merrill Lynch and UBS, who, in providing such advice, relied upon the Lloyds TSB Board's commercial assessments of the Acquisition.

The Lloyds TSB Board, which has been so advised by Citi, Merrill Lynch and UBS, further considers that the Placing and Open Offer and the Rule 9 Waiver are fair and reasonable and in the best interests of the Lloyds TSB Shareholders as a whole. In providing such advice, Citi, Merrill Lynch and UBS have taken into account the Lloyds TSB Board's commercial assessments.

The Lloyds TSB Board unanimously recommends that Lloyds TSB Shareholders vote in favour of the Resolutions to be put to the Lloyds TSB General Meeting as they intend to do in relation to their own individual holdings which amount in total to 1,316,034 Lloyds TSB Shares, representing approximately 0.02 per cent. of the existing issued ordinary share capital of Lloyds TSB.

Yours faithfully,

Victor Blank
Chairman

PART II

RISK FACTORS

The Lloyds TSB Group's and/or, following the Acquisition, the Enlarged Group's operating results, financial condition and prospects could be materially and adversely affected by any of the risks described below. In that event, the value of the Lloyds TSB Shares could decline, and investors could lose all or part of their investment in the Lloyds TSB Shares.

This section describes the risk factors which are considered by the Lloyds TSB Directors to be material in relation to the Lloyds TSB Group and/or which will, following the Acquisition, apply to the Enlarged Group. Where risks are described in terms of a risk to an investment in Lloyds TSB Shares these apply and are equally relevant to the Open Offer Shares and to the Consideration Shares as well as to the Lloyds TSB ADRs and Consideration ADRs which represent the underlying Lloyds TSB Shares and Consideration Shares respectively.

These risks should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. Additional risks and uncertainties that are not presently known to the Lloyds TSB Directors, or which they currently deem immaterial, may also have an adverse effect on the Lloyds TSB Group's and/or, if the Acquisition becomes Effective, the Enlarged Group's operating results, financial condition and prospects. The information given is as of the date of this document and, except as required by the FSA, the London Stock Exchange, the Takeover Panel, the Listing Rules, the Prospectus Rules, the Disclosure and Transparency Rules, the City Code or any other applicable law or regulation, will not be updated. Any forward-looking statements are made subject to the reservations specified under "Forward-Looking Statements" on page 3 of this document.

You should consider carefully the risks and uncertainties described below, together with all other information contained in this document and the information incorporated by reference herein, before making any investment decision or any decision whether or not to vote in favour of the Resolutions.

Risks relating to the Lloyds TSB Group and, if the Acquisition becomes Effective, the Enlarged Group

1.1 *The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, subject to inherent risks arising from general and sector specific economic conditions in the markets in which they operate, particularly the United Kingdom. Adverse developments, such as the current and ongoing crisis in the global financial markets and further deterioration of general economic conditions, particularly in the UK, have already adversely affected the Lloyds TSB Group's earnings and profits and could continue to cause its and the Enlarged Group's profitability to decline*

The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, subject to inherent risks arising from general and sector specific economic conditions in the markets in which they operate, particularly the United Kingdom in which the Lloyds TSB Group's earnings are, and the Enlarged Group's earnings will be, predominantly generated. Over approximately the past fifteen months, the global economy and the global financial system have been experiencing a period of significant turbulence and uncertainty, particularly the very severe dislocation of the financial markets around the world that began in August 2007 and has substantially worsened since September 2008 and related problems at many large global and UK commercial banks, investment banks, insurance companies and other financial and related institutions. This dislocation has severely impacted general levels of liquidity, the availability of credit and the terms on which credit is available. This crisis in the financial markets led the United Kingdom and other governments to inject liquidity into the financial system and require (and participate in) recapitalisation of the banking sector to reduce the risk of failure of certain large institutions and provide confidence to the market.

Despite this intervention, the volatility and market disruption in the banking sector have continued to a degree unprecedented in recent history. This market dislocation has also been accompanied by recessionary conditions and trends in many economies throughout the world, including the United Kingdom. There is increasing concern of a deep and prolonged global recession. These conditions have already adversely affected the Lloyds TSB Group's and the

HBOS Group's earnings and profits. Continued general deterioration in the UK or other major economies throughout the world, including, but not limited to, business and consumer confidence, unemployment trends, the state of the housing market, the commercial real estate sector, equity markets, bond markets, foreign exchange markets, counterparty risk, inflation, the availability and cost of credit, lower transaction volumes in key markets, the liquidity of the global financial markets and market interest rates, would reduce the level of demand for, and supply of, the Lloyds TSB Group's and the Enlarged Group's products and services, lead to lower realisations and write downs and impairments of investments and negative fair value adjustments of assets and materially and adversely impact their operating results, financial condition and prospects.

Additionally, the profitability of the Lloyds TSB Group's and the Enlarged Group's insurance businesses could be affected by increased claims from market factors such as increased unemployment. Significantly higher UK unemployment, reduced corporate profitability, increased corporate insolvency rates, increased personal insolvency rates and/or increased interest rates may reduce borrowers' ability to repay loans and may cause prices of residential or commercial real estate or other asset prices to fall further, thereby reducing the collateral value on many of the Lloyds TSB Group's and the Enlarged Group's loans and increasing write downs and, if this happens, impairment losses will occur. Poor general economic conditions and difficulty in valuation have depressed asset valuations for both the Lloyds TSB Group and the HBOS Group and are likely to continue to do so. This would be exacerbated by a further deterioration in general economic conditions.

As discussed in greater detail in the risk factor numbered 1.3 in this Part II ("Risk Factors") below, the Lloyds TSB Group has not yet been able to assess fully the level of fair value adjustments of the assets of the HBOS Group to be acquired in the Acquisition or other aspects of the HBOS business. If the fair valuation of the assets of the HBOS Group is materially less than anticipated, this could have a material and adverse impact on the financial condition and prospects of the Enlarged Group.

The exact nature of the risks faced by the Lloyds TSB Group and the Enlarged Group is difficult to predict and guard against in view of the severity of the global financial crisis and the fact that many of the related risks to the business are totally or in part outside of the control of the Lloyds TSB Group and the Enlarged Group.

1.2 ***The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, inherently subject to the risk of market fluctuations, which could adversely affect operating results, financial condition and prospects***

The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, inherently subject to the risk of financial market fluctuations, including changes in, and increased volatility of, interest rates, inflation rates, credit spreads, foreign exchange rates, commodity, equity, bond and property prices and the risk that their customers act in a manner which is inconsistent with business, pricing and hedging assumptions.

Market movements have (and will have) an impact on the Lloyds TSB Group and the Enlarged Group in a number of key areas. For example, adverse market movements would have an adverse effect, which could be material, upon the financial condition of the pension schemes of the Lloyds TSB Group and the Enlarged Group. In addition, banking and trading activities that are undertaken by the Lloyds TSB Group and will be undertaken by the Enlarged Group are subject to interest rate risk, foreign exchange risk, inflation risk and credit spread risk. For example, changes in interest rate levels, yield curves and spreads may affect the interest rate margin realised between lending and borrowing costs. Since August 2007, there has been a period of unprecedented high and volatile interbank lending rates (to the extent banks have been willing to lend at all), which has exacerbated these risks. Competitive pressures or fixed rates in existing loan commitments or facilities may mean that the Lloyds TSB Group is and the Enlarged Group will be restricted in their ability to increase interest rates charged to customers in response to changes in interest rates that affect wholesale borrowing. In addition, such increases in interest rates may result in each of the Lloyds TSB Group and the Enlarged Group having to increase the rates paid to wholesale and retail customers, which would have an adverse impact on net interest margins.

The insurance and investments businesses of the Lloyds TSB Group, and of the Enlarged Group, will face market risk arising, for example, from equity, bond and property markets in a number of ways depending upon the product and associated contract. Some of these risks are borne directly by the customer and some are borne by the insurance and investments businesses. Some insurance contracts involve guarantees and options that increase in value in adverse investment markets. There is a risk that the insurance and investments businesses will bear some of the cost of such guarantees and options. The insurance and investments businesses also have capital invested in the markets that are exposed to market risk. The performance of the investment markets will thus have a direct impact upon the Embedded Value of insurance and investments contracts and the Lloyds TSB Group's and Enlarged Group's operating results, financial condition and prospects. Adverse investment market conditions can affect investor confidence, which in turn can result in lower sales and/or reduced persistency.

Changes in foreign exchange rates affect the value of assets and liabilities denominated in foreign currencies and may affect earnings reported by the Lloyds TSB Group and the Enlarged Group. In the Lloyds TSB Group's and the Enlarged Group's international businesses, earnings and net assets are denominated in local currency, which will fluctuate with exchange rates in pounds sterling terms. It is difficult to predict with any accuracy changes in economic or market conditions, and such changes could have a material adverse effect on the Lloyds TSB Group's and the Enlarged Group's operating results, financial condition and prospects.

1.3 ***Market conditions have and may in the future result in material negative adjustments to the estimated fair values of financial assets of the Lloyds TSB Group and the Enlarged Group. This may include material negative adjustments to the valuation of financial assets that the Lloyds TSB Group will acquire as part of the Acquisition compared to the book value of such assets as at 30 June 2008. Any such negative fair value adjustments could have a material adverse effect on operating results, financial conditions or prospects***

Financial markets have been subject to significant stress conditions resulting in steep falls in perceived or actual financial asset values. The severity of this phenomenon is exemplified by the current and ongoing crisis in the global financial markets.

The fair value of the Lloyds TSB Group's and the Enlarged Group's financial assets could fall further and therefore result in negative adjustments, particularly in view of current market dislocation and the prospect of recession. Asset valuations in future periods, reflecting then-prevailing market conditions, may result in further negative changes in the fair values of the Lloyds TSB Group's and the Enlarged Group's financial assets. In addition, the value ultimately realised by the Lloyds TSB Group and the Enlarged Group may be lower than the current fair value. Any of these factors could require the Lloyds TSB Group and the Enlarged Group to record further negative fair value adjustments, which may have a material adverse effect on their operating results, financial condition or prospects.

The Lloyds TSB Group has made, and the Enlarged Group may make in the future, asset redesignations as permitted by recent amendments to IAS 39. The effect of such redesignations has been and would be that any effect on the profit and loss account of movements in the fair value of such redesignated assets that has occurred since 1 July 2008, in the case of assets redesignated prior to 1 November 2008, or may occur in the future may not be recognised until such time as the assets become impaired or are disposed of.

In addition, to the extent that fair values are determined using financial valuation models, the data used by such models may not be available or may become unavailable due to changes in market conditions, particularly for illiquid assets, and particularly in times of substantial instability such as the current economic crisis. In such circumstances the Lloyds TSB Group's valuation methodologies require it to make assumptions, judgments and estimates in order to establish fair value. These valuation models are complex and the assumptions used are difficult to make and are inherently uncertain, particularly in light of the uncertainty resulting from the current and ongoing crisis in the global financial markets.

In addition to some exposures of the Lloyds TSB Group to similar investments, the HBOS Group has, and the Enlarged Group will have, a significant portfolio of securities and other investments including asset backed securities, structured investments and private equity investments that are recorded at fair value and are therefore exposed to further negative fair value adjustments in the event of deterioration in market conditions.

Furthermore, fair value adjustments will be required in connection with the Acquisition. The *pro forma* net assets of the HBOS Group set out in Part IX ("Historical Financial Information Relating to HBOS plc") of this document have been extracted from the HBOS Group's interim report for the six months ended 30 June 2008, and do not take account of any fair value adjustments that will be required as a result of the Acquisition. The Lloyds TSB Group has not yet been able to assess fully the level of fair value adjustments of the assets of the HBOS Group. These adjustments may be material. The provisional results of this valuation exercise are not expected to be available until such time as the Lloyds TSB Group publishes its interim financial statements for the six month period ended 30 June 2009. Given the material deterioration in the value of the financial assets since 30 June 2008, and the market outlook for the near future, as well as the different valuation methodologies for such assets, following the Acquisition, such fair valuations will differ from the book value of the HBOS Group's net assets at 30 June 2008 and such difference may be material.

1.4 ***The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, subject to inherent risks concerning borrower and counterparty credit quality which could affect the recoverability and value of assets on the balance sheet. As a result of the Acquisition, the Enlarged Group will have greater exposure to certain sectors and asset classes than the Lloyds TSB Group currently has***

The Lloyds TSB Group makes, and the Enlarged Group will make, both secured and unsecured loans to retail and corporate customers. The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, subject to inherent risks regarding the credit quality of, and the recovery on loans to and amounts due from, customers and market counterparties. Changes in the credit quality of the Lloyds TSB Group's or the Enlarged Group's UK and/or international borrowers and counterparties, or in their behaviour, or arising from systemic risks in the UK and global financial system, could reduce the value of the Lloyds TSB Group's and the Enlarged Group's assets, and increase the Lloyds TSB Group's and the Enlarged Group's write downs and allowances for impairment losses. Factors including higher UK unemployment, reduced corporate profitability, increased corporate and personal insolvencies and/or increased interest rates may reduce borrowers' ability to repay loans. The outlook for the UK (and the global) economy has deteriorated significantly in recent months and this deterioration is expected to continue for the foreseeable future. In addition, changes in economic conditions may result in a deterioration in the value of security held against lending exposures and increase the risk of loss in the event of borrower default.

UK house prices have declined significantly in recent months, reflecting economic downturn and uncertainty, reduced affordability and lower availability of credit. Economic or other factors are likely to lead to further contraction in the mortgage market and further decreases in housing prices. Many borrowers in the UK borrow on short-term fixed or discounted floating rates and when such rates expire the continued reduced supply and stricter terms of mortgages together with the potential for higher mortgage rates have led and will continue to lead to higher delinquency rates. The Lloyds TSB Group and, to a greater extent, the HBOS Group both provide mortgages to buy-to-let investors where an excess supply of rental property or falls in rental demand could also impact the borrowers' income and ability to service the loans. In addition, the HBOS Group has a substantial exposure to the self certified mortgage sector where the Lloyds TSB Group has no exposure. If the current economic downturn continues, with further falls in house prices and increases in unemployment, the Enlarged Group's mortgage portfolios are likely to generate substantial increases in impairment losses which could materially affect the operations, financial condition and prospects of the Enlarged Group.

The average rating of the HBOS Group's corporate lending portfolio is lower than that of the Lloyds TSB Group, with substantial lending to mid-sized and private companies. The HBOS Group also has greater exposure to leveraged finance and subordinated loans, as well as significant exposure to the commercial real estate sector, including hotels and residential property developers. Commercial real estate prices have shown declines over the last year and the construction and real estate sectors are facing very challenging market conditions. If the current economic downturn continues, as expected, with weakening consumer spending and falling corporate profitability, the Enlarged Group's corporate lending portfolios are likely to generate substantial increases in impairment losses which could materially affect the operations, financial condition and prospects of the Enlarged Group.

1.5 ***The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, subject to inherent risks concerning liquidity, particularly if current market conditions continue to reduce the availability of traditional sources of funding or the access to wholesale money markets becomes more limited, which could affect the Lloyds TSB Group's and the Enlarged Group's ability to meet its financial obligations as they fall due***

The Lloyds TSB Group's businesses are, and the Enlarged Group's businesses will be, subject to risks concerning liquidity, which are inherent in banking operations, and could affect the Lloyds TSB Group's and the Enlarged Group's ability to meet financial obligations as they fall due or to fulfil commitments to lend. The HBOS Group has a funding profile that involves the need to refinance a significantly higher level of loan assets than that of the Lloyds TSB Group. Accordingly, the Enlarged Group's funding profile will involve higher refinancing risk than for the Lloyds TSB Group on a stand-alone basis. It is expected that the Enlarged Group will be required to refinance a significant amount of funding due to mature during 2009. These risks can be exacerbated by many enterprise-specific factors, including an over-reliance on a particular source of funding (including, for example, securitisations, covered bonds and short-term and overnight money markets), and changes in credit ratings, or market-wide phenomena such as market dislocation and major disasters. There is also a risk that corporate and institutional counterparties may look to reduce aggregate credit exposures to the Enlarged Group or to all banks. The funding needs of the Enlarged Group will increase to the extent that customers, including conduit vehicles of the Enlarged Group, draw down under existing credit arrangements with the Enlarged Group and such increases in funding needs may be material. In order to continue to meet their funding obligations and to maintain or grow their businesses generally the Lloyds TSB Group relies, and the Enlarged Group will rely, on customer savings and transmission balances, as well as ongoing access to the wholesale lending markets and Bank of England liquidity facilities and the UK Government's guarantee scheme. The ability of the Lloyds TSB Group and the Enlarged Group to access wholesale and retail funding sources on favourable economic terms is subject to a variety of factors, including a number of factors outside of their control, such as liquidity constraints, general market conditions, loss of confidence in the UK banking system. See the risk numbered 1.18 for a discussion of the competitive nature of the banking industry and competitive pressures that could have a negative impact on the availability of customer deposits and retail funding. In the current environment of unprecedented market volatility, banks' access to traditional sources of liquidity has been and may continue to be significantly restricted which may affect Lloyds TSB Group's and the Enlarged Group's access to such sources of liquidity.

While various governments including the UK government have taken substantial measures to ease the crisis in liquidity, such as the measures announced in the UK on 8 October 2008 and 13 October 2008, there can be no assurance that these measures will succeed in materially improving the liquidity position of major UK banks, including the Lloyds TSB Group and the Enlarged Group. In addition, the availability and the terms on which any such measures will be made available to the Company (whether in the form of access to HM Treasury's recapitalisation scheme, special liquidity scheme or guarantees scheme for short and medium term debt issuance) and how and when such measures will be implemented are uncertain. Lloyds TSB has, and the Enlarged Group will have, no influence over the policy making behind such measures. Further, there can be no assurance that these conditions will not lead to an increase in the overall cost of funding of the Lloyds TSB Group or the Enlarged Group. The Lloyds TSB Group expects that the Enlarged Group will substantially rely for the foreseeable future on the continued availability of Bank of England liquidity facilities as well as HM Treasury's guarantee scheme for short and medium-term debt issuance. If the Bank of England liquidity facility, HM Treasury's guarantee scheme or other sources of short-term funding are not available after that period, the Lloyds TSB Group, or the Enlarged Group, could face serious liquidity constraints, which would have a material adverse impact on its solvency.

Access to sufficient liquidity might also determine whether or not the Lloyds TSB Group will be in a position to redeem or repurchase the Enlarged Group HMT Preference Shares to be held by HM Treasury in accordance with their terms or, if circumstances permit, to repurchase them early. See the risk numbered 3.4 for a discussion of the limitation on cash dividends and other terms of the Enlarged Group HMT Preference Shares.

1.6 ***The Lloyds TSB Group is subject, and the Enlarged Group will be subject, to the risk of insufficient capital resources to meet the minimum required by regulators***

The Lloyds TSB Group is, and the Enlarged Group will be, subject to the risk, inherent in all regulated financial businesses, of having insufficient capital resources to meet the minimum regulatory capital requirements. In addition, those minimum regulatory requirements may increase in the future.

In the Lloyds TSB Group's announcement of 13 October 2008 it stated that the *pro forma* core Tier 1 capital ratio for the Enlarged Group as at 30 June 2008 would have been in excess of 8.5 per cent.[1] Such pro forma core Tier 1 capital ratio number does not take account of net negative capital adjustments that would be required to be made since that date and is for illustrative purposes only. Lloyds TSB has made a preliminary assessment that net negative capital adjustments of no more than £10 billion after tax would need to be made to HBOS's financial position for core Tier 1 capital purposes as a result of the Acquisition, the effect of which would mean that the Enlarged Group would have a core Tier 1 ratio of 7 per cent.

The Enlarged Group's ability to maintain its targeted and regulatory capital ratios will depend on a number of factors, including post-Acquisition net synergies and implementation costs, the level of Enlarged Group's risk weighted assets, the Enlarged Group's post-tax profit and the level of net negative capital adjustments resulting from the Acquisition. More specifically, the Enlarged Group's ability to maintain its targeted and regulatory capital ratios will be significantly impacted by net negative capital adjustments resulting from the Acquisition. In addition to the impact of net negative capital adjustments, the Enlarged Group's core Tier 1 ratio will be directly impacted by any shortfall in forecasted after-tax profit (which could result, most notably, from greater than anticipated asset impairments and/or adverse volatility relating to the issuance business). Furthermore, under Basel II, capital requirements are inherently more sensitive to market movements than under previous regimes and capital requirements will increase if economic conditions or negative trends in the financial markets worsen. Any failure of the Enlarged Group to maintain its minimum regulatory capital ratios could result in administrative actions or sanctions, which in turn may have a material adverse impact on the Lloyds TSB Group's and the Enlarged Group's operating results, financial condition and prospects. A shortage of available capital would also affect the ability to continue organic growth or to pursue acquisition or other strategic opportunities. For further information see paragraph 9 of Part I ("Letter from Sir Victor Blank, Chairman of Lloyds TSB Group plc") of this document.

The Lloyds TSB Group's life assurance and general insurance businesses in the UK are, and the Enlarged Group's will be, subject to the capital requirements prescribed by the FSA, and the Lloyds TSB Group's life and general insurance companies outside the UK are, and the Enlarged Group's will be, subject to local regulatory capital requirements. In July 2007, the European Commission published a draft proposal for primary legislation to define broad "framework" principles for Solvency II, a fundamental review of the capital adequacy regime for the European insurance industry. Solvency II aims to establish a revised set of EU-wide capital requirements where the required regulatory capital will be dependent upon the risk profile of the entities, together with risk management standards, that will replace the current Solvency I requirements. At this early stage of development, it is not possible to predict the ultimate impact of this proposed regime on the Lloyds TSB Group's or the Enlarged Group's capital. However, the final regime could significantly impact the regulatory capital the Lloyds TSB Group's or the Enlarged Group's life assurance and general insurance businesses are required to hold.

1.7 ***The Lloyds TSB Group and the Enlarged Group could be negatively affected by the soundness and/or the perceived soundness of other financial institutions, which could result in significant systemic liquidity problems, losses or defaults by other financial institutions and counterparties***

Against the backdrop of the lack of liquidity and high cost of funds in the interbank lending market, which is unprecedented in recent history, the Lloyds TSB Group is, and the Enlarged Group will be, subject to the risk of deterioration of the commercial soundness and/or perceived soundness of other financial services institutions within and outside the United Kingdom. Financial services institutions that deal with each other are interrelated as a result of trading, investment, clearing, counterparty and other relationships. This risk is sometimes referred to as "systemic risk" and may adversely affect financial intermediaries, such as clearing agencies, clearing houses, banks, securities firms and exchanges with whom the Lloyds TSB Group interacts and the Enlarged Group will interact on a daily basis, all of which could have an adverse effect on the Lloyds TSB Group's and the Enlarged Group's ability to raise new funding.

The Lloyds TSB Group routinely executes, and the Enlarged Group will routinely execute, a high volume of transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, mutual and hedge funds and other institutional clients, resulting in a significant credit concentration. As a result, the Lloyds TSB Group is, and the Enlarged Group will be, exposed to counterparty risk as a result of recent financial institution failures and nationalisations and will continue to be exposed to the risk of loss if counterparty financial institutions fail or are otherwise unable to meet their obligations. A default by, or even concerns about the ability of, one or more financial services institutions could lead to further significant systemic liquidity problems, or losses or defaults by other financial institutions, which could materially and adversely affect the Lloyds TSB Group's and the Enlarged Group's operating results, financial condition and prospects.

1.8 *If the perceived credit-worthiness of monoline insurers and other market counterparties continues to deteriorate, the Lloyds TSB Group and the Enlarged Group may be forced to record further credit valuation adjustments on securities insured or guaranteed by such parties, which could have a material adverse effect on the Lloyds TSB Group's and the Enlarged Group's results of operations, financial condition and prospects*

The Lloyds TSB Group has, and the Enlarged Group will have, credit exposure to monoline insurers and other market counterparties through securities insured or guaranteed by such parties and credit protection bought from such parties with respect to certain over-the-counter derivative contracts, mainly credit default swaps ("CDSs") which are carried at fair value. The fair value of these underlying CDSs and other securities, and the Lloyds TSB Group's and the Enlarged Group's exposure to the risk of default by the underlying counterparties, depend on the valuation and the perceived credit risk of the instrument insured or guaranteed or against which protection has been bought as well as on the credit-worthiness of the relevant monoline or other insurer. In 2007 and 2008, monoline and other insurers and other market counterparties have been adversely affected by their exposure to residential mortgage-linked products, and their perceived credit-worthiness has deteriorated significantly in 2008. Their credit-worthiness may further deteriorate as a consequence of the deterioration of the value of underlying assets. Although the Lloyds TSB Group tries, and the Enlarged Group will try, to limit and manage direct exposure to monoline or other insurers and other market counterparties, indirect exposure may exist through other financial arrangements and counterparties. If the financial condition of monoline or other insurers or market counterparties or their perceived credit-worthiness deteriorates further, the Lloyds TSB Group and/or the Enlarged Group may record further credit valuation adjustments on the underlying instruments insured by such parties in addition to those already recorded. In addition, to the extent that asset devaluations lower the credit-worthiness of monoline insurers, the Lloyds TSB Group and the Enlarged Group would be further exposed to diminished credit-worthiness of such insurers themselves. Any primary or indirect exposure to the financial condition or credit-worthiness of these counterparties could have a material adverse impact on the results of operations, financial condition and prospects of the Lloyds TSB Group and/or the Enlarged Group.

1.9 *The Lloyds TSB Group's and the Enlarged Group's insurance and investments businesses and employee pension schemes are subject to risks relating to insurance claims rates, pension scheme benefit payment levels and changes in insurance customer and employee pension scheme member behaviour*

The life and pensions insurance businesses of the Lloyds TSB Group and the Enlarged Group and their employee pension schemes are exposed to short-term and longer-term impacts arising from uncertain longevity and ill-health rates. Adverse developments in any of these factors will increase the size of the liabilities and may adversely affect the Lloyds TSB Group's and the Enlarged Group's financial condition and results of operations.

Customer behaviour in the life and pensions insurance business may result in increased propensity to cease contributing to or cancel insurance policies at a rate in excess of business assumptions. The consequent reduction in policy persistency and fee income would have an adverse impact upon the profitability of the life and pensions business of the Lloyds TSB Group and the Enlarged Group. The behaviour of employee pension scheme members affects the levels of benefits payable from the schemes. For example, the rate at which members cease employment affects the aggregate amount of benefits payable by the schemes. This rate may differ from applicable business assumptions. Adverse variances may increase the size of the aggregate pension liabilities and may adversely affect the Lloyds TSB Group's and the Enlarged Group's financial condition and results of operations.

The general insurance businesses of the Lloyds TSB Group and the Enlarged Group are exposed to the risk of uncertain insurance claim rates. For example, extreme weather conditions can result in high property damage claims, higher levels of theft can increase claims on property, contents and motor vehicle insurance and changes to unemployment levels can increase claims on loan protection insurance. These claims rates may differ from business assumptions and negative developments may adversely affect the Lloyds TSB Group's and the Enlarged Group's financial condition and results of operations.

UK banks recognise an asset in their balance sheets representing the value of in-force business ("VIF") in respect of long term life assurance contracts, being insurance contracts and investment contracts with discretionary participation features. This asset represents the present value of future profits expected to arise from the portfolio of in-force life assurance contracts. Adoption of this accounting treatment results in the earlier recognition of profit on new business, but subsequently a lower contribution from existing business, when compared to the recognition of profits on investment contracts under IAS 39 (Financial Instruments: Recognition and Measurement). Differences between actual and expected experience may have a significant impact on the value of the VIF asset, as changes in experience can result in significant changes to modelled future cash flows. The VIF asset is calculated based on best estimate assumptions made by management, including the value of investments under management, mortality experience and persistency. If these assumptions prove incorrect, the VIF asset could be materially reduced, which in turn could have a material adverse effect on the Lloyds TSB Group's and the Enlarged Group's financial condition and results of operations.

Also, as further described in the risk numbered 1.2, the Lloyds TSB Group's and the Enlarged Group's insurance assets are subject to the risk of market fluctuations.

1.10 *The Lloyds TSB Group's and the HBOS Group's borrowing costs and access to the capital markets depend significantly on their credit ratings, as will those of the Enlarged Group*

As at the date of this document, the long-term credit ratings for the Lloyds TSB Group are Aaa from Moody's Investors Service, AA from Standard & Poor's rating service, AA+ from Fitch Ratings and AA(H) from DBRS. As at the date of this document, the long-term credit ratings for the HBOS Group are Aa2 from Moody's Investors Service, A+ from Standard & Poor's rating service, AA from Fitch Ratings and AA(H) from DBRS. Recently, each of these ratings services placed the long-term credit ratings of both the Lloyds TSB Group and the HBOS Group on watch with negative implications. Reduction in the long-term credit ratings of the Lloyds TSB Group, the HBOS Group and/or the Enlarged Group could significantly increase their respective borrowing costs, limit their access to the capital markets and trigger additional collateral requirements in derivative contracts and other secured funding arrangements. Therefore, a reduction in credit ratings could materially adversely affect the Enlarged Group's access to liquidity and competitive position and, hence, have a material adverse effect on the Enlarged Group's business, financial position and results of operations.

1.11 *Weaknesses or failures in the Lloyds TSB Group's and the Enlarged Group's internal processes and procedures and other operational risks could have a negative impact on results and could result in reputational damage*

Operational risks, through inadequate or failed internal processes (including financial reporting and risk monitoring processes) or from people-related or external events, including the risk of fraud and other criminal acts carried out against the Lloyds TSB Group, are present in the Lloyds TSB Group's businesses and will be present in the business of the Enlarged Group. The Lloyds TSB Group's businesses and the HBOS Group's businesses are, and the Enlarged Group's business will be, dependent on their ability to process and report accurately and efficiently a high volume of complex transactions across numerous and diverse products and services, in different currencies and subject to a number of different legal and regulatory regimes. Following the Acquisition, the existing internal controls and procedures of the HBOS Group must be integrated with those of the Lloyds TSB Group. This is a complex and time consuming process and there can be no assurance that delays will not occur or that systems weaknesses or inadequacies will not be uncovered. Any weakness in such internal control systems and processes could have a negative impact on their results during the affected period. Furthermore, damage to the Lloyds TSB Group's or the Enlarged Group's reputation (including to customer confidence) arising from inadequacies, weaknesses or failures in such systems could have a significant adverse impact on the Lloyds TSB Group's and Enlarged Group's businesses.

1.12 *The Lloyds TSB Group relies, and the Enlarged Group will rely, in part on retail deposits to fund lending activities, the ongoing availability of which is sensitive to factors outside the Lloyds TSB Group's control. Loss in consumer confidence could result in high levels of withdrawals, which could have a material adverse effect on the Lloyds TSB Group's and the Enlarged Group's business, financial position and results of operations and could, in extreme circumstances, prevent the Lloyds TSB Group or the Enlarged Group from meeting its minimum liquidity requirements*

Medium-term growth in the Lloyds TSB Group's and the Enlarged Group's lending activities will depend, in part, on the availability of retail funding on appropriate terms, for which there is increasing competition. This reliance has increased in the recent past given the difficulties in accessing wholesale funding. Increases in the cost of such funding will impact on the Lloyds TSB Group's and the Enlarged Group's margins and affect profit, and a lack of availability of such retail deposit funding could impact on the Lloyds TSB Group's and the Enlarged Group's future growth.

The ongoing availability of retail deposit funding is dependent on a variety of factors outside the Lloyds TSB Group's and the Enlarged Group's control, such as general economic conditions and the confidence of retail depositors in the economy in general and the financial services industry specifically and the availability and extent of deposit guarantees. These factors could lead to a reduction in the Lloyds TSB Group's and the Enlarged Group's ability to access retail deposit funding on appropriate terms in the future. If the current difficulties in the wholesale funding markets are not resolved or central bank lending to financial institutions is withdrawn it is likely that wholesale funding will prove even more difficult to obtain.

Any loss in consumer confidence in the banking businesses of the Lloyds TSB Group or the Enlarged Group could significantly increase the amount of retail deposit withdrawals in a short space of time. Should the Lloyds TSB Group or the Enlarged Group experience an unusually high level of withdrawals, this may have an adverse effect on the Lloyds TSB Group's and the Enlarged Group's business, financial position and results of operations and could, in extreme circumstances, prevent the Lloyds TSB Group or the Enlarged Group from meeting its minimum liquidity requirements. In such extreme circumstances the Lloyds TSB Group and/or the Enlarged Group may not be in a position to continue to operate without additional funding support, which it may be unable to access.

1.13 ***Terrorist acts, other acts of war, geopolitical, pandemic or other such events could have a negative impact on the business and results of the Lloyds TSB Group and the Enlarged Group***

Terrorist acts, other acts of war or hostility, geopolitical, pandemic or other such events and responses to those acts/events, may create economic and political uncertainties, which could have a negative impact on UK and international economic conditions generally, and more specifically on the business and results of the Lloyds TSB Group and the Enlarged Group in ways that cannot necessarily be predicted.

1.14 ***The Lloyds TSB Group has agreed to certain undertakings in relation to the operation of its business in the Placing and Open Offer Agreement. The implications and details of some of these undertakings remain unclear and they could have a material adverse effect on the operations of the Lloyds TSB Group and the Enlarged Group***

Under the terms of the Placing and Open Offer Agreement, the Lloyds TSB Group has provided certain undertakings aimed at ensuring that the potential acquisition by HM Treasury of Lloyds TSB Shares and the Lloyds TSB Group's potential participation in the guarantee scheme to be promoted by HM Treasury as part of its support for the banking industry is consistent with the state aid approval. State aid approval means the decision of the European Commission of 13 October 2008 and issued in connection with the state aid aspects of the HM Treasury's recapitalisation scheme, special liquidity and guarantee scheme for short and medium term debt issuance. The state aid rules aim to prevent companies from being given an artificial or unfair competitive advantage as a result of governmental assistance. The undertakings are also aimed at supporting certain objectives of HM Treasury in providing assistance to the UK banking industry. These undertakings, which are consistent with the Lloyds TSB Group's existing focus in its relevant lines of business, include (i) supporting UK government policy in relation to mortgage lending and lending to SMEs through 2011; (ii) regulating management remuneration; (iii) regulating the rate of growth of the Lloyds TSB Group's balance sheet; and (iv) requiring the presentation to HM Treasury of a restructuring plan within six months (as all banks particpating in HM Treasury's recapitalisation and guarantee schemes are required to do). There is a risk that these undertakings or any further requirements introduced by HM Treasury could have a materially adverse effect on the operations of the Lloyds TSB Group and the Enlarged Group. For a description of these undertakings, see Part V ("Conditions Relating to the Proposed Government Funding") of this document. In addition, pursuant to the conditions attaching to the Proposed Government Funding, the Lloyds TSB Board is required to consult with HM Treasury in relation to the appointment of two new independent directors.

Through the influence of its shareholding, the UK Government may seek to influence Lloyds TSB or the Enlarged Group in other ways that would have a materially adverse effect on the Lloyds TSB Group's and the Enlarged Group's business.

HM Treasury has agreed to consult with Lloyds TSB with a view to applying to the Commission to have the undertakings referred to above disapplied where (i) the Lloyds TSB Group is no longer participating in the guarantee scheme and (ii) HM Treasury either does not acquire shares in the Lloyds TSB Group or HM Treasury has substantively reduced its holding of Lloyds TSB Shares and/or preference shares.

1.15 ***The Lloyds TSB Group's businesses are, and the Enlarged Group's business will be, subject to substantial regulation, and regulatory and governmental oversight. Adverse regulatory developments or changes in government policy could have a significant negative impact on the Lloyds TSB Group's and the Enlarged Group's operating results, financial condition and prospects***

The Lloyds TSB Group conducts, and the Enlarged Group will conduct, their businesses subject to ongoing regulation and associated regulatory risks, including the effects of changes in the laws, regulations, policies, voluntary codes of practice and interpretations in the UK and the other markets where it operates. This is particularly the case in the current market environment, which is witnessing increased levels of government intervention in the banking sector. Future changes in regulation, fiscal or other policies are unpredictable and beyond the control of the Lloyds TSB Group and the Enlarged Group and could materially adversely affect the Lloyds TSB Group's and the Enlarged Group's business.

Areas where changes could have an adverse impact include, but are not limited to:

- the monetary, interest rate and other policies of central banks and regulatory authorities;
- general changes in government or regulatory policy or changes in regulatory regimes that may significantly influence investor decisions in particular markets in which the Lloyds TSB Group and the Enlarged Group operate, may change the structure of those markets and the products offered or may increase the costs of doing business in those markets;
- other general changes in regulatory requirements, such as prudential rules relating to the capital adequacy or liquidity frameworks;
- changes to, or increased levies under, the arrangements for funding depositor or investor protection schemes and providing compensation in the event of a failure of another regulated firm, including for example, under the Financial Services Compensation Scheme in the UK to which the Lloyds TSB Group is and the Enlarged Group will be subject;
- external bodies applying or interpreting standards or laws differently to those applied by the Lloyds TSB Group or the HBOS Group historically;
- changes in competition and pricing environments;
- further developments in the financial reporting environment;
- expropriation, nationalisation, confiscation of assets and changes in legislation relating to foreign ownership; and
- other unfavourable political, military or diplomatic developments producing social instability or legal uncertainty which, in turn, may affect demand for the Lloyds TSB Group's and the Enlarged Group's products and services.

In addition, in the United Kingdom and elsewhere, there is continuing political and regulatory scrutiny of the banking industry and, in particular, retail banking. In the United Kingdom, the Competition Commission, the Financial Services Authority and the Office of Fair Trading are carrying out several inquiries, which are referred to in paragraphs 11.1.1 and 11.1.2 of Part XII ("Additional Information") of this document. In recent years there have been several issues in the UK financial services industry in which the FSA has intervened directly, including the sale of personal pensions and the sale of mortgage related endowments. There may be further inquiries in the future which could lead to further regulatory intervention.

For example in clearing the Acquisition without a reference to the Competition Commission the Secretary of State noted that there were some competition concerns identified by the OFT in the markets for personal current accounts and mortgages in Great Britain and the market for SME banking in Scotland. He said that he is asking the OFT to keep relevant markets under review in order to protect the interests of UK consumers and the British economy. It is too soon to tell what form, or implications for the Enlarged Group, those reviews might have.

The UK Government, the FSA or other regulators, in the United Kingdom or overseas, may intervene further in relation to the areas of industry risk already identified, or in new areas, which could adversely affect the Lloyds TSB Group and the Enlarged Group.

1.16 *The Lloyds TSB Group is exposed to various forms of legal and regulatory risk including the risk of misselling financial products, acting in breach of legal or regulatory principles or requirements and giving negligent advice, any of which could have a negative impact on its results or its relations with its customers. This will also be true of the Enlarged Group*

The Lloyds TSB Group is, and the Enlarged Group will be, exposed to many forms of legal and regulatory risk, which may arise in a number of ways. Primarily:

- certain aspects of the Lloyds TSB Group's and the Enlarged Group's business may be determined by the authorities, the Financial Ombudsman Service ("FOS") or the courts as not being conducted in accordance with applicable laws or regulations, or, in the case of FOS, with what is fair and reasonable in the Ombudsman's opinion. For more information on additional constraints that may be imposed as a result of the State Aid Approval, see also the risk factor numbered 1.14;
- the possibility of alleged misselling of financial products which, as a result, may require additional provisions;

- contractual obligations may either not be enforceable as intended or may be enforced against the Lloyds TSB Group and the Enlarged Group in an adverse way;
- the intellectual property of the Lloyds TSB Group and the Enlarged Group (such as trade names) may not be adequately protected; and
- the Lloyds TSB Group and the Enlarged Group may be liable for damages to third parties harmed by the conduct of its business.

In addition, the Lloyds TSB Group faces and the Enlarged Group will face risk where legal or regulatory proceedings or FOS or other complaints are brought against it in the UK High Court or elsewhere, or in jurisdictions outside the UK, including other European countries and the United States. A major focus of US governmental policy relating to financial institutions in recent years has been combating money laundering and terrorist financing and enforcing compliance with US economic sanctions. See paragraph 11.1.3 of Part XII ("Additional Information") of this document. The outcome of any proceeding or complaint is inherently uncertain and could have a material adverse effect on the Lloyds TSB Group's and the Enlarged Group's operations and/or financial condition, particularly if extended more broadly.

Failure to manage these risks adequately could impact the Lloyds TSB Group and the Enlarged Group adversely, both financially and reputationally through an adverse impact on the Lloyds TSB brand.

1.17 *The Lloyds TSB Group is, and the Enlarged Group will be, exposed to tax risk*

Tax risk is the risk associated with changes in taxation rates or law, or misinterpretation of the law. This could result in increased charges or financial loss. Failure to manage this risk adequately could impact the Lloyds TSB Group and the Enlarged Group materially and adversely.

1.18 *The Lloyds TSB Group's businesses are conducted in highly competitive environments. Achieving an appropriate return for shareholders depends upon management's ability to respond effectively to competitive pressures. This will also be true for the Enlarged Group*

The markets for UK financial services and the other markets within which the Lloyds TSB Group operates, and the Enlarged Group will operate, are highly competitive, and management expects such competition to intensify in response to competitor behaviour, consumer demand, technological changes, the impact of consolidation, regulatory actions and other factors. If financial markets remain unstable, financial institution consolidation may accelerate. Moreover, government intervention in the banking sector may impact the competitive position of banks within a country and among international competitors which may be subject to different forms of government intervention, thus potentially putting the Lloyds TSB Group and the Enlarged Group at a competitive disadvantage to local banks in such jurisdictions. Any combination of these factors could result in a reduction in profit. The Lloyds TSB Group's and the Enlarged Group's ability to generate an appropriate return for its shareholders depends significantly upon the competitive environment and management's response to it.

The Lloyds TSB Group's and the Enlarged Group's financial performance may be materially and adversely impacted by competition, including declining lending margins or competition for savings driving up funding costs which cannot be recovered from borrowers. Adverse persistency in the Lloyds TSB Group's insurance and investments business, as well as the Enlarged Group's insurance and investment operations, is a risk to current and future earnings.

A key part of the Lloyds TSB Group's strategy involves, and the Enlarged Group's strategy will involve, building strong customer relationships in order to win a bigger share of its customers' financial services spend. If the Lloyds TSB Group and the Enlarged Group are not successful in retaining and strengthening customer relationships they will not be able to deliver on this strategy, and may lose market share, incur losses on some or all of their activities or fail to attract new and retain existing deposits, which could have a material adverse effect on their business, financial position and results of operations.

As announced by HBOS on 8 October 2008, the HBOS Group has agreed the sale of part of its Australian operations, namely Bank of Western Australia Ltd and St Andrews Australia Pty Ltd, to Commonwealth Bank of Australia Limited for the equivalent of approximately A$2.5 billion (£1.2 billion). In addition to A$2.1 billion (£1.0 billion) of cash consideration for the sale, HBOS will receive a return of excess capital in BankWest of approximately A$360 million, together comprising A$2.5 billion (£1.2 billion) of proceeds. The purchaser will also redeem preferred shares issued to the HBOS Group equivalent to their par value of A$530 million (£250 million). The businesses pending sale comprise the HBOS Group's Australian retail and business banking operations as well as its insurance and wealth management businesses. These businesses generated profits before taxation of A$300 million (£126 million) for the year ended 31 December 2007 and A$126 million (£59 millon) for the six months ended 30 June 2008. The total asset value of these businesses as at 30 June 2008 was approximately A$64 billion (£31 billion).[1,2] Completion is subject to certain regulatory approvals in Australia. A summary of the terms of the sale agreement relating to these businesses is set out in paragraph 9.2.3 Part XII ("Additional Information") in this document.

Following the sale, HBOS retains a presence in Australia through Bank of Scotland International (Australia) Limited and Capital Finance Australia Limited which are engaged in corporate banking and asset finance activities respectively, together with the Bank of Scotland Treasury branch. The corporate banking business, based in Sydney, operates under the BOS International brand and provides acquisition finance, real estate lending and infrastructure/project finance. The division's asset finance business operates under the Capital Finance brand.

Treasury and Asset Management

Bank of Scotland Treasury is the centralised treasury function for the HBOS Group and manages prudential and regulatory liquidity and wholesale multi-currency funding. It arranges the HBOS Group's debt capital issuance and asset securitisation programmes and offers a range of treasury services to HBOS Group customers from its offices in London and its branches in Glasgow, Grand Cayman, New York and Sydney. Bank of Scotland Treasury also has management responsibility for the treasury activities of Bank of Scotland (Ireland) Limited.

Asset Management, comprising Insight Investment Management Limited ("Insight") and Invista Real Estate Investment Management plc ("Invista") (55 per cent. owned) and their respective subsidiary companies, is the investment management business within the HBOS Group.

Insight operates a multi-channel business, managing money for the HBOS Group, retail investors, pension funds, insurance groups and other institutions. Insight's strategic product lines are Fixed Income, Cash, Liability Driven Investment, Equities and Absolute Return.

Invista was formed following the initial public offering of the real estate management division of Insight and is a UK-listed real estate fund manager. Invista currently manages 21 real estate funds spread across the UK and continental Europe. This includes seven funds managed on behalf of the HBOS Group as well as other funds managed on behalf of third-party clients.

3 Current Trading, Trends and Prospects

HBOS today announced an interim management statement, the text of which is set out in Part XIII ("HBOS Interim Management Statement 3 November 2008") of this document.

(1) Exchange rates used in conversion are based on 30 June 2008, except for those relating to profits before taxation. As at 30 June 2008, £1 : A$2.08; average for year ended 31 December 2007, £1 : A$2.39; average for half year ended 30 June 2008, £1 : A$2.14.

(2) Extracted without material adjustment from unaudited management accounts.

HM Treasury is entitled to novate its rights and obligations under the Placing and Open Offer Agreement to any entity which is wholly owned, directly or indirectly, by HM Treasury.

HBOS has undertaken not to declare or pay any dividend or make any distribution on or in respect of its ordinary shares or set aside any sum to provide for payment of any such dividend or distribution; or redeem, purchase, cancel or otherwise acquire in any way any of its ordinary shares or effect a reduction of its ordinary share capital which involves distribution to holders of the ordinary shares until the New HBOS Preference Shares are redeemed or repurchased in full.

HBOS has given certain undertakings to HM Treasury in support of HM Treasury's objective of providing assistance to the UK banking industry, as follows:

(i) HBOS Directors will relinquish bonuses for 2008.

(ii) The enlarged group remuneration will reflect long-term value creation and will take account of risk. The reward for board members will take into account internal relative compensation packages and perceived fairness in the current economic climate. On losing the confidence of the board, the board members can be dismissed at a reasonable and fair cost.

(iii) To commit to a new FSA Code on risk based remuneration.

(iv) HM Treasury will work with the board on its appointment of two new independent directors, unless HM Treasury's holding of the Enlarged Group falls below 25 per cent., in which case it will be consulted on the appointment of one independent director.

(v) In relation to mortgages, to immediately restore and maintain the availability and active marketing of competitively priced mortgage lending until the end of 2011 at a level at least equivalent to that of 2007 (provided that HBOS shall not be required to engage in uncommercial activities); to participate in industry initiatives and comply with government codes/guidance until at least the end of 2011; to make available a sum to be agreed for the establishment and maintenance of shared equity/shared ownership schemes; and to support ongoing expansion of financial capability initiatives.

(vi) In relation to SMEs, to immediately restore and maintain the availability and active marketing of competitively priced lending to SMEs until the end of 2011 at a level at least equivalent to that of 2007 (provided that HBOS shall not be required to engage in uncommercial activities); and to publish an annual report containing specified information relating to SMEs.

The above undertakings shall apply until HM Treasury or the European Commission determines or a court of competent jurisdiction finally determines that HBOS is no longer in receipt of the aid which is the subject of the decision. HM Treasury has agreed in certain circumstances, to consult with HBOS with a view to making submissions to the European Commission to obtain clarity as to the duration of the conditions and/or seek their disapplication.

Lloyds TSB anticipates that following completion of the Acquisition the conditions relating to the Proposed Government funding set out in Part V (and not the conditions set out in the HBOS Placing and Open Offer Agreement) will apply to the Enlarged Group.

HM Treasury is entitled to novate its rights and obligations under the HBOS Placing and Open Offer Agreement to any entity which is wholly-owned, directly or indirectly, by HM Treasury.

9.2.5 *HBOS Preference Share Subscription Agreement entered into with effect from 13 October 2008*

HBOS and HM Treasury entered into the HBOS Preference Share Subscription Agreement with effect from 13 October 2008, pursuant to which HM Treasury agreed to acquire, and HBOS agreed to allot and issue to HM Treasury, the New HBOS Preference Shares for a total consideration of £3,000,000,000 (before costs and expenses). HBOS has agreed to pay the costs and expenses of HM Treasury in relation to the negotiation of the HBOS Preference Share Subscription Agreement and the subscription for, and allotment and issue of, the New HBOS Preference Shares (including, without limitation, any stamp duty or stamp duty reserve tax).