Registered Number 3331873

BOS (SHARED APPRECIATION MORTAGES) NO.4 PLC

ANNUAL REPORT AND ACCOUNTS

YEAR ENDED 31 December 2011

BOS (SHARED APPRECIATION MORTGAGES) NO 4 PLC
DIRECTORS AND COMPANY INFORMATION

DIRECTORS

Ian Gordon Stewart
Tracey Anne Hill

COMPANY SECRETARY

Angela Lockwood	(resigned 25 11 2011)
Paul Gittins	(appointed 25 11 2011)

REGISTERED OFFICE

Trinity Road
Halifax
West Yorkshire
HX1 2RG

INDEPENDENT AUDITORS

PricewaterhouseCoopers LLP
Benson House
33 Wellington Street
Leeds
LS1 4JP

Registered Number 3331873

The directors present their annual report and the audited financial statements for BOS (Shared Appreciation Mortgages) NO 4 PLC (the "Company") for the year ended 31 December 2011

PRINCIPAL ACTIVITY

The principal activity of the Company is to finance mortgage lending In 1998 the Company issued £203 7m floating rate notes (the "Notes") Following a business restructure on 28 February 2011 (see business review below), the terms of the Notes were changed and bear a zero rate of interest until 2073 when the Notes become due Prior to 28 February 2011, the interest payable on the Notes was set at 60% of the three-month LIBOR rate for Sterling deposits less 0 30% per annum until February 2028 Thereafter, the interest rate applicable to the Notes would have been 60% of the three-month LIBOR rate for Sterling deposits plus 0 10% per annum until the due date in 2073 The Notes are secured on the mortgage portfolio The capital appreciation arising on the sale of a mortgage holder's property is shared between the mortgage holder and the Company as set out in the original loan agreement The Company pays its entire share of the appreciation to Note holders

The activities of the Company are conducted primarily by reference to a series of transaction documents (the "Programme Documentation")

Movements in the mortgage book are disclosed in the notes to the financial statements

Business structure

The Company is a subsidiary undertaking of Bank of Scotland plc ("BOS") and ultimately Lloyds Banking Group plc ("LBG")

RESULTS AND DIVIDENDS

No new mortgages were acquired or generated by the Company in the year and no new Notes were issued

The profit after taxation for the year amounted to £763,638 (2010 £4,022,596 profit) The directors do not recommend payment of a dividend (2010 £4,500,000)

BUSINESS REVIEW AND FUTURE DEVELOPMENTS

The Company's business will continue to unwind over the life of the mortgages issued as no further advances will be made Cash is continuing to be collected

The principal asset in the Company is a mortgage portfolio which is subject to an annual impairment review The mortgage portfolio is subject to the economic factors relating to the housing market (see "Credit Risk" below) The Company's results are not impacted by changes in interest rates as the mortgage loans bear a zero rate of interest No impairment provision was deemed necessary as at 31 December 2011 or 31 December 2010

The Company was restructured in 2011 On 23 February 2011, at a meeting of Note holders, it was approved that the Guaranteed Investment Contract ("GIC") account should be closed on 28 February 2011 and that the funds from the GIC account be used to repay a proportion of the Notes in issue on the same date As a result of this agreement, the balance on the GIC account at 28 February 2011 of £80,620,623 was used to pay down an equal amount of the Notes in issue

BUSINESS REVIEW AND FUTURE DEVELOPMENTS (CONTINUED)

It was also agreed to change the remaining Notes in issue from interest-bearing to zero interest with effect from the same date The remaining Notes retain the right to receive the shared appreciation on the underlying mortgage loans as per the original agreement

As part of the restructure, the Note holders provided an additional £500,000 funding that has been placed in the Reserve Account (see "liquidity risk" below), increasing the overall principal amount held to £2,197,250 The additional funds are made available to the Company should it have insufficient funds available to cover its operating expenses The Company's only source of income following the closure of the GIC account is from interest earned on its bank accounts Should the funds be used they will be replenished in future periods from any shared appreciation earned The £500,000 becomes due for repayment at the end of the structure out of available funds, but only after all other payments have been made, including the £1,697,250 provided by BOS, currently held in the Reserve Account

Under International Financial Reporting Standards ("IFRSs") an effective yield adjustment is made on interest receivable and interest payable, reflecting the discount at which the mortgages and Notes were originally issued, with the net difference passed through the income statement Following the closure of the GIC account and partial repayment of Notes on 28 February 2011, the discount on the GIC account was fully amortised and the discount on the Notes was amortised in line with the corresponding effective yield adjustment on the mortgages This resulted in a higher net movement through the income statement of £6,951 profit in 2011 (31 December 2010 £434 profit)

Standard and Poor's, the Rating Agency rating the Notes, has issued updated criteria for counterparties to a structured finance transaction during 2011 and following an assessment of the Company, the Notes in issue are unchanged and remain AAA rated

The key performance indicator used by management in assessing the performance of the Company is the monitoring of actual cash flows against planned cash flows on the Notes The Company's performance is addressed in the quarterly management accounts provided to the directors

POLICY AND PRACTICE ON PAYMENT OF CREDITORS

The Company follows the 'Prompt Payment Code' published by the Department for Business Innovation and Skills (BIS), regarding the making of payments to suppliers Information about the 'Prompt Payment Code' may be obtained by visiting www promptpaymentcode org uk

The Company's policy is to agree terms of payment with suppliers and these normally provide for settlement within 30 days after the date of the invoice, except where other arrangements have been negotiated It is the policy of the Company to abide by the agreed terms of payment, provided the supplier performed according to the terms of the contract

The Company owed no money to trade creditors at 31 December 2011 or at 31 December 2010

DIRECTORS

The directors who served during the year and up to the date of signing the financial statements were as follows

Ian Gordon Stewart
Tracey Anne Hill

THIRD PARTIES INDEMNITIES

The Company has made qualifying third party indemnity provisions for the benefit of the directors These indemnity provisions remain in force at the date of this report A copy of the deed is available for inspection at the registered office of Lloyds Banking Group plc

RISK MANAGEMENT

The majority of the Company's assets and liabilities have been classified as financial instruments in accordance with IAS 32 "Financial Instruments Presentation"

The Company's financial instruments comprise a mortgage portfolio, cash and liquid resources, an embedded derivative, loans and borrowings and various other payables that arise directly from its operations The principal purpose of these financial instruments is to raise finance for the Company's operations

It is, and has been throughout the year under review, the Company's policy that no trading in financial instruments is undertaken

The principal risk arising from the Company's financial instruments is credit risk This and other risks which may affect the Company's performance are detailed below Further analysis of the risks facing the Company on its financial instruments is provided in note 16

Credit Risk

Credit risk arises on the individual loans within the mortgage loan portfolio which are in turn secured on the underlying UK residential properties The performance of these loans is therefore influenced by the economic background and the UK housing market However, the maximum loan-to-value of the original advances was 25% and the credit risk is considered to be low

The extent to which the Company can meet its obligations to repay the Notes will be dependent upon the receipt of funds earned on its bank deposits, principal receipts on the mortgages and monies deposited in the Reserve Account with BOS (see "Liquidity Risk") To the extent that this income does not provide sufficient funds to cover the repayment of the Notes, the Note holders have no claim on the assets of BOS

The terms of the Mortgage Portfolio Agreement given by BOS in respect of the mortgages require BOS to repurchase any mortgage which is found to be in breach of warranty BOS will repurchase any mortgages that are found or held not to be valid, binding and enforceable

Although in such an event the total value of the outstanding loan will be covered by BOS, the Note holder will not receive the benefit of any future payments of appreciation amounts or partial repayment of appreciation amounts in respect of the mortgages repurchased

Shared appreciation is subject to the movement in the market value of the property which is dependent upon house price inflation ("HPI") This may provide a return on the Notes below initial expectations Any expected increase in value cannot be guaranteed

Interest rate risk

Interest rate risk exists where assets and liabilities have interest rates set under a different basis or which reset at a different time

The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of assets and liabilities are similar

RISK MANAGEMENT (CONTINUED)

Interest rate risk (continued)

Following the restructure on 28 February 2011, with the closure of the GIC account and partial repayment of the Notes, the Company's exposure to interest rate risk is limited to interest earned on its bank accounts, as both the mortgage loans and the remaining Notes pay a zero rate of interest Therefore, it is not considered to be a significant risk

Liquidity risk

The Company holds a Reserve Account of £2,197,250, of which £1,697,250 was deposited with BOS which, should it be needed, can be used to meet its obligations under the Notes The reliance on this facility is therefore dependent on the creditworthiness of BOS An additional £500,000 additional funding was provided by the Note holders during 2011 as part of the restructure (see business review) The Company has not drawn on this facility since inception

Operational risk

In accordance with the Programme Documentation the Company is bound to make payments to meet third party expenses BOS has been appointed to act as account bank and servicer of the mortgage book on behalf of the Company The Company also uses the Bank of New York Mellon to provide all corporate services in respect of the Notes in issue

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations

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

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable International Financial Reporting Standards (IFRSs) as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements,

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

Statement of disclosure of information to auditors

So far as the directors are aware, there is no relevant audit information of which the Company's auditors are unaware, and the directors have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information This confirmation is given, and should be interpreted, in accordance with the provisions of section 418 of the Companies Act 2006

EMPLOYEES

The Company has employed no staff during the year ended 31 December 2011 or the previous year

INDEPENDENT AUDITORS

Pursuant to section 487 of the Companies Act 2006, auditors duly appointed by the member of the Company shall, subject to any resolution to the contrary, be deemed to be reappointed for the next financial year and PricewaterhouseCoopers LLP, having expressed their willingness will therefore continue in office

STATEMENT OF GOING CONCERN

The directors are satisfied that the Company has adequate resources to continue to operate for the foreseeable future and is financially sound For this reason, they continue to adopt the going concern basis in preparing the accounts

By Order of the Board

Paul Gittins
Secretary

Trinity Road
Halifax
West Yorkshire
HX1 2RG

DATE 21 March 2012

INDEPENDENT AUDITORS' REPORT
TO THE MEMBER OF BOS (SHARED APPRECIATION MORTGAGES) NO. 4 PLC

We have audited the financial statements of BOS (Shared Appreciation Mortgages) NO 4 PLC for the year ended 31 December 2011 which comprise the Statement of Comprehensive Income, the Balance Sheet, the Statement of Changes in Equity, the Cash Flow Statement and the related notes The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

This report, including the opinions, has been prepared for and only for the company's member as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 December 2011 and of its profit and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements

INDEPENDENT AUDITORS' REPORT
TO THE MEMBER OF BOS (SHARED APPRECIATION MORTGAGES) NO 4 PLC
(CONTINUED)

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit

Mark Hannam

Mark Hannam (Senior Statutory Auditor)
For and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Leeds

Date 21 March 2012

BOS (SHARED APPRECIATION MORTGAGES) NO 4 PLC
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2011

	Notes	2011 £	2010 £
Interest receivable and similar income	2	14,189,247	7,672,592
Interest payable and similar charges	3	(13,070,359)	(2,003,858)
Net interest income		1,118,888	5,668,734
Other operating income	5	4,576	6,450
Operating expenses	6	(93,118)	(93,169)
Profit before tax		1,030,346	5,582,015
Taxation	7	(266,708)	(1,559,419)
Profit / total comprehensive income attributable to equity holders		763,638	4,022,596

The profit shown above is derived from continuing operations The Company operates in a single business segment and all of the Company's activities are in the UK

The accompanying notes on pages 13 to 30 are an integral part of the financial statements

BOS (SHARED APPRECIATION MORTGAGES) NO. 4 PLC
BALANCE SHEET AS AT 31 DECEMBER 2011

	Notes	2011 £	2010 £
Assets			
Cash and cash equivalents	8	8,384,092	78,977,297
Mortgage portfolio	9	22,202,608	22,905,760
Shared appreciation rights receivable	10	161,495,040	166,861,399
Total assets		192,081,740	268,744,456
Equity and liabilities			
Loans and borrowings	11	21,558,833	92,040,116
Shared appreciation rights payable	12	161,495,040	166,861,399
Current tax liability	7	286,469	1,577,154
Deferred tax liability	13	76,006	95,767
Trade and other payables	14	1,353,213	1,621,479
Total liabilities		184,769,561	262,195,915
Share capital	15	50,001	50,001
Retained profits		7,262,178	6,498,540
Shareholders' equity		7,312,179	6,548,541
Total equity and liabilities		192,081,740	268,744,456

The directors approved the financial statements on 21 March 2012

Ian Gordon Stewart
Director

The accompanying notes on pages 13 to 30 are an integral part of the financial statements

Registered Number 3331873

BOS (SHARED APPRECIATION MORTGAGES) NO 4 PLC
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2011

	Share Capital £	Retained Profits £	Total £
Balance at 1 Jan 2011	50,001	6,498,540	6,548,541
Profit / total comprehensive income for the year	-	763,638	763,638
Balance at 31 Dec 2011	50,001	7,262,178	7,312,179

	Share Capital £	Retained Profits £	Total £
Balance at 1 Jan 2010	50,001	6,975,944	7,025,945
Profit / total comprehensive income for the year	-	4,022,596	4,022,596
Dividends paid in the year	-	(4,500,000)	(4,500,000)
Balance at 31 Dec 2010	50,001	6,498,540	6,548,541

The accompanying notes on pages 13 to 30 are an integral part of the financial statements

BOS (SHARED APPRECIATION MORTGAGES) NO 4 PLC
CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2011

	Notes	2011 £	2010 £
Operating Activities			
Inter-company fees paid		(71,104)	(73,584)
External audit fees paid		(6,444)	(3,290)
Administration income / expenses paid		485,361	(9,996)
Tax paid		(1,577,154)	(1,215,472)
Net cash flows from operating activities		(1,169,341)	(1,302,342)
Investing Activities			
Repayments on mortgage portfolio		1,820,812	1,952,726
Shared appreciation rights received		6,459,855	6,739,795
Net cash flows from investing activities		8,280,667	8,692,521
Financing Activities			
Bank interest received		1,177,696	5,828,032
Repayment of borrowings		(83,457,543)	(5,687,893)
Interest paid on borrowings		(43,178)	(130,959)
Restructuring costs paid		(184,029)	-
Shared appreciation rights paid		(7,108,933)	(6,409,651)
Dividends paid		-	(4,500,000)
Net cash flows from financing activities		(89,615,987)	(10,900,471)
Net decrease in cash and cash equivalents		(82,504,661)	(3,510,292)
Cash and cash equivalents at start of year		90,888,753	94,399,045
Cash and cash equivalents at end of year	8	8,384,092	90,888,753

The cash flow statement is presented using the direct method of preparation

The accompanying notes on pages 13 to 30 are an integral part of the financial statements

1 SIGNIFICANT ACCOUNTING POLICIES

BOS (Shared Appreciation Mortgages) NO 4 PLC is a company domiciled in the United Kingdom

(a) Statement of compliance

The financial statements for the year ended 31 December 2011 have been prepared in accordance with International Financial Reporting Standards (IFRSs) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) as adopted by the European Union The standards applied by the Company are those endorsed by the European Union and effective at the date the financial statements are approved by the Board The financial statements comply with IFRSs

The Company has adopted the following new and relevant IFRS pronouncements which became effective for financial years beginning on or after 1 January 2011 None of these standards or amendments has had a material impact on these company financial statements

- Improvements to IFRSs (issued May 2010) Amends IFRS 7 Financial Instruments Disclosure to require further disclosures in respect of collateral held by the Company as security for financial assets and sets out minor amendments to other IFRS standards as part of the annual improvements process,

- IAS 24 Related Party Disclosures (Revised) Simplifies the definition of a related party and provides a partial exemption from the requirement to disclose transactions and outstanding balances with the government and government-related entities

The financial statements also comply with the relevant provisions of Part XV of the Companies Act 2006

The Company is a subsidiary undertaking of BOS and ultimately LBG The directors of the Company are satisfied that it is the current intention of LBG to ensure that its subsidiaries, including the Company, shall have at all times in the foreseeable future (being the period until at least 31 December 2013) access to adequate capital and liquidity resources to continue as a going concern Accordingly, the financial statements have been prepared on a going concern basis

The Company has opted to align the presentation of the financial statements with those of LBG to improve comparability across all companies within the group This has not resulted in any material changes to the financial statements, with only the split between current and non-current being removed from the face of the balance sheet However, the analysis is unchanged in the notes to the financial statements

The financial statements are presented in sterling which is the Company's functional and presentation currency and have been prepared on the historical cost basis (except that derivative financial instruments are stated at fair value)

(b) Revenue recognition

Interest receivable and similar income have been calculated using the effective interest method The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the expected life of the financial instrument The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability When calculating the effective interest rate, the future cash flows are estimated after considering all the contractual terms of the instrument

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Taxation

Income tax recognised in the income statement comprises both current and deferred tax Current income tax, which is payable on taxable profits, is recognised as an expense in the period in which the profits arise

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements Deferred tax is determined using tax rates that have been enacted or substantially enacted by the balance sheet date which are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled

The Company's tax charge is calculated on an IFRS basis and disclosed in accordance with IAS 12

(d) Financial instruments

The Company's financial instruments comprise a mortgage portfolio, cash and liquid resources, an embedded derivative, loans and borrowings and various other payables that arise directly from its operations

The main purpose of these financial instruments is to raise finance for the Company's operations These financial instruments are classified in accordance with the principles of IAS 39 as described below

(d)(i) Mortgage portfolio

The Company's mortgage portfolio comprises mortgage loans with no fixed maturity date The individual mortgage loans terminate on the earlier of the date of sale of the property or the death of the mortgage account holder

Under IAS 39, the mortgage portfolio is classified within "loans and receivables" The initial measurement is at fair value (excluding amounts for the shared appreciation referred to in (d)(iv) below) Subsequent measurement is at amortised cost with revenue being recognised using the effective interest method The discount arising on initial recognition is being amortised over the expected life of the mortgages

At each reporting period end, the Company assesses whether there is any objective evidence that mortgage loans within the portfolio are impaired The directors do not consider that a provision for impaired assets is currently required

(d)(ii) Cash and cash equivalents

The Company holds bank accounts with BOS, its parent undertaking These accounts are held in the Company's name and meet the definition of cash and cash equivalents The use of certain accounts is restricted by a detailed priority of payments set out in the Programme Documentation As the cash can only be used to meet certain specific liabilities and is not available to be used with discretion, it is viewed as restricted cash

These bank accounts are classified within "loans and receivables" in accordance with IAS 39 and income is being recognised using the effective interest method

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d) Financial instruments (continued)

(d)(iii) Loans and borrowings

The Company's loans and borrowings comprise mortgage-backed Notes that have been issued in the capital market

Loans and borrowings are recognised initially at fair value less directly related incremental transaction costs Subsequent to initial recognition, loans and borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis

(d)(iv) Embedded derivatives

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host instrument, and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivative recognised in the income statement Depending on the classification of the host instrument, the host is then measured in accordance with IAS 39

The capital appreciation arising on the sale of a mortgage holder's property is shared between the mortgage holder and the Company as set out in the original loan agreement The Company pays its entire share of the appreciation to the Note holders

The economic characteristics and risks of the shared appreciation rights receivable and payable are not viewed as being closely related to those arising on the mortgages and Notes, respectively The shared appreciation rights receivable and payable have therefore been valued separately from the mortgages and Notes using current HPI There is uncertainty regarding the timing of any future shared appreciation receipts and the directors do not consider that it is practical to include an estimate of future HPI in these valuations

The resulting fair value movements of these embedded derivatives are recorded in net fair value gains and losses on derivatives in the income statement and the embedded derivatives are shown separately on the face of the balance sheet The host instruments are valued at amortised cost, as noted above in (d)(i) and (d)(iii)

(e) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments

The directors of the Company consider that the entity has only one geographical and one business segment and therefore is not required to produce additional segmental disclosure

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Critical accounting judgements and estimates

The preparation of the financial statements necessarily requires the exercise of judgement both in the application of accounting policies and in the selection of assumptions used in the calculation of estimates These judgements are reviewed on an ongoing basis and are continually evaluated based on historical experience and other factors The most significantly affected components of the financial statements and associated critical judgements are as follows

Effective interest rate method

The effective interest rate is calculated on initial recognition of the financial asset or liability, estimating the future cash flows after considering all the contractual terms of the instrument The calculation includes all amounts expected to be paid or received by the Company including expected early redemption fees and related penalties and premiums and discounts that are an integral part of the overall return Direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument are also taken into account in the calculation Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss

For the purpose of the effective yield calculation on the Notes, an average expected life has been calculated based on prepayment expectations for the mortgages This is revised on a regular basis in light of actual redemption experience

Fair value calculations

Fair value is defined as the value at which assets, liabilities or positions could be closed out or sold in a transaction with a willing and knowledgeable counterparty

The value of the embedded derivative has been calculated separately from the host contract using current HPI All inputs into the valuation models are obtained from observable market data No assumption for future HPI has been included as this is not considered to be practical

(g) Fees and commissions

Fees and commissions receivable for the continuing service of loans and advances are recognised on the basis of work done Other fees are recognised when receivable

(h) Dividends

Dividends on ordinary shares are recognised in equity in the year in which they are paid

(i) Trade and other payables

Trade and other payables are stated at cost or at amortised cost if deemed to be a financial liability

2 INTEREST RECEIVABLE AND SIMILAR INCOME

	2011 £	2010 £
Interest receivable on mortgage portfolio	13,011,551	1,100,094
Bank interest receivable	1,177,696	6,572,498
	14,189,247	7,672,592

3 INTEREST PAYABLE AND SIMILAR CHARGES

	2011 £	2010 £
Interest payable on Notes	13,033,570	1,976,755
Amortisation of issue costs	27,103	27,103
Amortisastion of restructuring costs	9,686	-
	13,070,359	2,003,858

4 NET FAIR VALUE GAINS AND LOSSES ON DERIVATIVES

	2011 £	2010 £
Fair value movement on shared appreciation rights receivable	(5,366,359)	3,625,606
Fair value movement on shared appreciation rights payable	5,366,359	(3,625,606)
	-	-

5 OTHER OPERATING INCOME

	2011 £	2010 £
Fees and commissions receivable	4,576	6,450
Shared appreciation receivable	6,459,855	6,739,795
Shared appreciation payable	(6,459,855)	(6,739,795)
	4,576	6,450

6 OPERATING EXPENSES

	2011 £	2010 £
Inter-company fees	70,881	73,283
Administration fees	19,237	16,411
Audit fees	3,000	3,475
	93,118	93,169

The Company has no employees (2010 nil) and none of the directors received any emoluments from the Company in the current or previous year

Audit fees relate to the statutory audit There are no fees payable to the auditors and their associates for services other than the statutory audit

The audit fee for the current year, net of VAT, was £2,500 (2010 £2,870)

7 TAXATION

	2011 £	2010 £
Current Tax		
Corporation tax charge for the year at a rate of 26 5% (2010 28%)	286,469	1,577,154
Deferred Tax		
Deferred tax change in tax rate – credit	(6,333)	(3,547)
Deferred tax credit for the year at a rate of 26 5% (2010 28%)	(13,428)	(14,188)
Total tax charge	266,708	1,559,419

Reconciliation of effective tax rate	2011	2010
The tax assessed for the year is lower than the standard rate of corporation tax in the UK of 26 5% (2010 28%)	£	£
Profit before tax	1,030,346	5,582,015
Profit before tax multiplied by the standard rate of corporation tax in the UK of 26 5% (2010 28%)	273,041	1,562,966
Effects of		
Deferred tax change in tax rate – credit	(6,333)	(3,547)
Total tax charge	266,708	1,559,419

The current tax liability of £286,469 (2010 £1,577,154 liability) represents the net amount of income tax payable in respect of the current year

The standard rate of Corporation Tax in the UK changed from 28% to 26% with effect from 1 April 2011 Accordingly, the Company's profits for this accounting period are taxed at an effective rate of 26 5%

8 CASH AND CASH EQUIVALENTS

	2011 £	2010 £
Bank accounts	8,384,092	90,888,753
Unamortised discount	-	(11,911,456)
	8,834,092	78,977,297
Unamortised discount	-	11,911,456
Cash and cash equivalents per the cash flow statement	8,384,092	90,888,753

The Company holds bank accounts with BOS The use of the accounts is restricted by a detailed priority of payments set out in the Programme Documentation As the cash can only be used to meet certain specific liabilities and is not available to be used with discretion, it is viewed as restricted cash The accounts are held in the Company's name and meet the definition of cash and cash equivalents

9 MORTGAGE PORTFOLIO

	2011 £	2010 £
At 1 January	22,905,760	23,746,981
Mortgage redemptions in the year	(1,803,247)	(1,941,315)
Amortisation of discount	1,100,095	1,100,094
At 31 December	22,202,608	22,905,760

The mortgage loans advanced by the Company have no fixed maturity date but would terminate on the earlier of, the date of sale of the property, or the death of the mortgage account holder

10 SHARED APPRECIATION RIGHTS RECEIVABLE

The right for the Company to receive a share of the capital appreciation arising on the individual mortgages, as set out in the original loan agreements, is classified as an embedded derivative, in accordance with the principles of IAS 39 The embedded derivative has been valued separately from the host contract using current HPI No estimate has been made of the effect of future HPI as the directors consider that this is impractical

The Company is contractually obliged to pay to the Note holders any amounts received from mortgage customers for the shared appreciation A corresponding embedded derivative liability has therefore been recognised in the balance sheet (note 12)

11 LOANS AND BORROWINGS

This note provides information about the contractual terms of the Company's loans and borrowings For more information about the Company's exposure to interest rate risk and the fair value of its financial instruments, see note 16

	2011 £	2010 £
Non-current liabilities		
Notes	22,139,721	92,459,556
Deferred issue costs	(386,218)	(406,545)
Deferred restructuring costs	(165,626)	-
	21,587,877	92,053,011
Current liabilities		
Accrued interest payable to Note holders	-	14,208
Deferred issue costs	(20,327)	(27,103)
Deferred restructuring costs	(8,717)	-
	(29,044)	(12,895)
At 31 December	21,558,833	92,040,116

The mortgage-backed Notes are due in 2073 The interest rate applicable on the Notes up to and including the interest period ending 28 February 2011 was 60% of the three-month LIBOR rate for Sterling deposits less 0 30% per annum Thereafter, the interest rate applicable to the Notes was changed as part of the restructure (referred to in the Directors' Report) and the Notes now bear a zero rate of interest until 2073, which is when the Notes become due At the end of the year the Notes, as rated by S&P, had a rating of AAA (2010 rating of AAA)

The Notes carry, in addition to interest, rights to receive certain amounts calculated by reference to the value of shared appreciation proceeds received from redeemed mortgages The Notes are subject to mandatory part redemption from time to time based on the level of redeemed mortgages and can be redeemed in full, in certain circumstances, at the option of the Company The Notes are secured on the mortgage portfolio, the bank accounts and certain other assets of the Company

12 SHARED APPRECIATION RIGHTS PAYABLE

The Company is contractually obliged to pay to the Note holders any amounts received from mortgage customers for the shared appreciation arising on the sale of the property An embedded derivative liability has therefore been recognised in the balance sheet for the same value as the embedded derivative asset (note 10)

13 DEFERRED TAX LIABILITY

	2011 £	2010 £
At 1 January	95,767	113,502
Credit for year	(13,428)	(14,188)
Change in Tax Rate – credit	(6,333)	(3,547)
At 31 December	76,006	95,767

The deferred tax liability was recognised for the fair value adjustments that arose on transition to IFRS and is being released to the income statement over a period of ten years from adoption

Legislation to reduce the main rate of corporation tax from 26% to 25% with effect from 1 April 2012 was substantively enacted on 5 July 2011 This has resulted in a decrease in the Company's provision for deferred tax at 31 December 2011 of £6,333

14 TRADE AND OTHER PAYABLES

	2011 £	2010 £
Shared appreciation payable	568,321	1,217,399
Note redemptions payable	178,879	311,987
Accruals and deferred income	600,068	85,925
Amounts owed to BOS	5,945	6,168
	1,353,213	1,621,479

15 SHARE CAPITAL

	2011	2010
	£	£
Authorised		
50,000 ordinary shares of £1 each	50,000	50,000
1 deferred share of £ 1	1	1
Allotted, called up and fully paid		
50,000 ordinary shares of £1 each	50,000	50,000
1 deferred share of £1	1	1

The Company is a directly held subsidiary undertaking of BOS

The £1 deferred share is held by Deutsche Trustee Company Limited (formerly Bankers Trustee Company Limited)

The holder of the ordinary shares is entitled to receive dividends as declared from time to time

The deferred share carries no entitlement to any dividend or to any share in any surplus assets of the Company on a winding-up, other than the right to be repaid the amount of any paid-up share capital thereon The right to be repaid any paid-up share capital in the deferred share shall be deferred until after all paid-up share capital has been first repaid on all other classes of issued share capital in the Company

The deferred share carries the right to receive notice of all general meetings of the Company but does not carry the right to attend, speak or vote at a general meeting unless a resolution is to be proposed abrogating, varying or modifying any of the rights or privileges of the holder of the deferred share, or for the winding up or administration of the Company under the Insolvency Act 1986, or for the entry by the Company with any other party into a merger, reconstruction, scheme of arrangement or amalgamation of or affecting the Company, in any of which cases such holder shall have the right to attend such general meeting and shall be entitled to speak and vote Whenever the holder of the deferred share is entitled to vote at a general meeting, such holder shall have one vote and on a poll such number of votes as is equal to 34% of the number of votes attached to all other issued shares of the Company

16 MANAGEMENT OF RISK

The principal risk arising from the Company's financial instruments is credit risk However, considerable resource is given to maintaining effective controls to manage, measure and mitigate this risk Further detailed analysis of this risk and other risks facing the Company in relation to its financial instruments is provided below

The Company's exposure to risk on its financial instruments and the management of such risk is largely determined at the inception of the securitisation transaction The Company's activities and the role of each party to the transaction are clearly defined and documented

16(a) Credit risk

Credit risk is the risk of financial loss arising from a customer's failure to settle financial obligations as they fall due

Credit risk arises on the individual loans within the mortgage portfolio which are in turn secured on the underlying UK residential properties The performance of these loans is therefore influenced by the economic background and the UK housing market Mortgage loans are no longer offered by the Company but the maximum loan-to-value of the original advances was 25% and the credit risk is considered to be low

The ability of the Company to meet its obligations to repay the Notes is dependent upon the receipt of funds earned on the bank deposits, principal receipts on the mortgages and the Reserve Account with BOS (see "Liquidity Risk") To the extent that this income does not provide sufficient funds to cover the repayment of the Notes, the Note holders have no claim on the assets of BOS

The terms of the Mortgage Portfolio Agreement given by BOS in respect of the mortgages require BOS to repurchase any mortgage which is found to be in breach of warranty BOS will repurchase any mortgages that are found or held not to be valid, binding and enforceable

Although in such an event the total value of the outstanding loan and any accrued interest will be covered by BOS, the Note holder will not receive the benefit of any future payments of appreciation amounts or partial repayment of appreciation amounts in respect of the mortgages repurchased In terms of the shared appreciation, in accordance with the Programme Documentation, amounts received by the Company from the borrower are required to be paid over to the Note holders

16 MANAGEMENT OF RISK (CONTINUED)

16(a) Credit risk (continued)

All loans in the mortgage portfolio pay a zero rate of interest As a result, there are no arrears of interest, properties in possession or bad debts within the Company and therefore no impairment provision is considered to be necessary at 31 December 2011 or 31 December 2010

The maximum exposure to credit risk arising on the Company's financial assets at the reporting date is disclosed in the table below

	Note	Carrying Amount 2011 £	Maximum Exposure 2011 £	Carrying Amount 2010 £	Maximum Exposure 2010 £
Assets held at amortised cost					
Cash and cash equivalents	8	8,384,092	8,384,092	78,977,297	90,888,753
Mortgage portfolio	9	22,202,608	38,704,025	22,905,760	40,507,272
Assets held at fair value					
Shared appreciation rights receivable	10	161,495,040	161,495,040	166,861,399	166,861,399
Total Assets		192,081,740	208,583,157	268,744,456	298,257,424

16(b) Interest rate risk

Interest rate risk exists where assets and liabilities have interest rates set under a different basis or which reset at a different time

The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of assets and liabilities are similar

Prior to 28 February 2011, the Notes were exposed to cash flow interest rate risk as the Notes carried a floating interest rate that was reset as market rates change

Following the restructure on 28 February 2011, with the closure of the GIC account and partial repayment of the Notes, the Company's exposure to interest rate risk is limited to interest earned on its bank accounts, as both the mortgage loans and the remaining Notes pay a zero rate of interest Therefore, it is not considered to be a significant risk

Prior to 28 February 2011, the profit was impacted by the interest earned on the GIC balance and the variable rate movements on the Notes However, following the restructure there are no major impacts to profit

16 MANAGEMENT OF RISK (CONTINUED)

16(c) Lıquıdıty Rısk

Lıquıdıty rısk ıs the rısk that the Company ıs not able to meet ıts financıal oblıgatıons as they fall due or can do so only at an unacceptably hıgh cost

The extent to whıch the Company can meet ıts oblıgatıons to repay the Notes wıll be dependent upon the receıpt of funds earned on the bank deposıts, prıncıpal receıpts on the mortgages and monıes deposıted ın the Reserve Account wıth BOS £2,197,250 has been placed on deposıt to assıst the Company should ıt not be able to meet ıts oblıgatıons under the Notes Included wıthın thıs amount ıs an addıtıonal £500,000 that was provıded by the Note holders as part of the restructure on 28 February 2011 The relıance on thıs facılıty ıs therefore dependent upon the credıtworthıness of BOS, whıch currently has a long term ratıng from Standard and Poor's (S&P) of A (2010 S&P long-term ratıng A+) The Company has not drawn on thıs facılıty sınce ınceptıon

The lıquıdıty tables reflect the undıscounted cash payments whıch wıll fall due ıf the structure contınues untıl the earlıest contractual maturıty date as set out ın the Programme Documentatıon The Note repayment profıle mırrors the repayment of the mortgages, and based on current modellıng assumptıons, ıt ıs not antıcıpated that any mortgages wıll stıll be outstandıng beyond the orıgınal step-up date, ın place before restructure, of February 2028

2011	Carryıng amount	Contractual repayment value	Not later than one month	Later than one month but not later than three months	Later than three months but not later than one year	Later than one year and not later than five years	Later than five years
	£	£	£	£	£	£	£
Prıncıpal							
Notes	22 139 721	38,641,138	-	-	-	-	38,641,138
Shared apprecıatıon payable	161,495,040	161 495 040	-	-	-	-	161,495 040
Trade and other payables	1,353,213	1,353,213	-	853 213	-	-	500,000
	184 987 974	201,489,391	-	853 213	-	-	200,636,178

2010	Carrying amount	Contractual repayment value	Not later than one month	Later than one month but not later than three months	Later than three months but not later than one year	Later than one year and not later than five years	Later than five years
	£	£	£	£	£	£	£
Prıncıpal							
Notes	92,459,556	122 277 562	-	-	-	-	122 277 562
Shared apprecıatıon payable	166 861 399	173,161,048	-	-	-	-	173,161,048
Trade and other payables	1,621,479	1 621 479	-	1,618,035	3,444	-	-
Interest payable							
Interest payable on Notes	14 208	2,978,124	-	43 161	131,881	700,650	2,102,432
	260,956 642	300 038,213	-	1,661,196	135 325	700,650	297,541,042

16 MANAGEMENT OF RISK (CONTINUED)

16(d) Fair values

The fair values of the Company's principal financial instruments, together with the carrying amounts shown in the balance sheet are as follows

	Note	Carrying amount 2011 £	Fair value 2011 £	Carrying amount 2010 £	Fair value 2010 £
Loans and Receivables at amortised cost					
Mortgage portfolio	9	22,202,608	34,946,338	22,905,760	5,359,627
Financial liabilities at amortised cost					
Loans and borrowings	11	(21,558,833)	(34,889,556)	(92,040,116)	(89,572,092)

The embedded derivatives for shared appreciation receivable and payable are recognised in the balance sheet at fair value

The following comments summarise the main methods and assumptions used in estimating the fair value of financial instruments

The fair value of the mortgage portfolio and loans and borrowings have been calculated by discounting future cash flows at an appropriate market rate The fair value of the shared appreciation rights receivable and shared appreciation rights payable have been valued using current HPI The valuation method is consistent with commonly used market techniques All significant inputs into the valuation models are obtained from observable market data

For this reason, in accordance with "IFRS 7 Financial Instruments Disclosures", the fair value measurement for the shared appreciation is deemed to be Level 2 in the Fair Value Hierarchy The change in fair value that has been calculated using this valuation technique has been recognised in the income statement for the year ended 31 December 2011

The cash and cash equivalents and other payables are recognised on an amortised cost basis that is considered to be a close approximation to fair value

17 RELATED PARTIES

The Company is a subsidiary undertaking of BOS and ultimately LBG

The Company receives bank interest from BOS on its bank deposits BOS administers the mortgage portfolio on behalf of the Company, for which quarterly service fees are paid During the year no dividend was paid to BOS (2010 £4,500,000)

During the year the Company undertook the following transactions with companies in the LBG Group

	LBG and subsidiary undertakings	LBG and subsidiary undertakings
	2011	2010
	£	£
Statement of Comprehensive Income		
Interest receivable and similar income	1,177,696	6,572,498
Operating expenses	(70,881)	(73,283)
Balance Sheet		
Assets		
Cash and cash equivalents	8,384,092	90,888,753
Liabilities		
Trade and other payables	(5,945)	(6,168)
Equity		
Dividends paid	-	(4,500,000)

18 FUTURE ACCOUNTING PRONOUNCEMENTS

The following pronouncements will be relevant to the Company but are not applicable for the year ending 31 December 2011 and have not been applied in preparing these financial statements The full impact of these accounting changes is currently being assessed by the Company

Pronouncement	Nature of change	IASB effective date
IFRS 9 Financial Instruments [1]	Replaces those parts of IAS 39 Financial Instruments Recognition and Measurement relating to the classification, measurement and derecognition of financial assets and liabilities Requires financial assets to be classified into two measurement categories, fair value and amortised cost, on the basis of the objectives of the entity's business model for managing its financial assets and the contractual cash flow characteristics of the instrument The available-for-sale financial asset and held-to-maturity investment categories in existing IAS 39 will be eliminated The requirements for financial liabilities and derecognition are broadly unchanged from IAS 39	Annual periods beginning on or after 1 January 2015
IFRS 10 Consolidated Financial Statements	Supersedes IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation – Special Purpose Entities and establishes principles for the preparation of consolidated financial statements when an entity controls one or more entities	Annual periods beginning on or after 1 January 2013
IFRS 12 Disclosure of Interests in Other Entities	Requires an entity to disclose information that enables users of financial statements to evaluate the nature of, and risks associated with, its interests in other entities and the effects of those interests on its financial position, financial performance and cash flows	Annual periods beginning on or after 1 January 2013

18 FUTURE ACCOUNTING PRONOUNCEMENTS (CONTINUED)

Pronouncement	Nature of change	IASB effective date
IFRS 13 Fair Value Measurement	The standard defines fair value, sets out a framework for measuring fair value and requires disclosures about fair value measurements It applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements	Annual periods beginning on or after 1 January 2013

[1] IFRS 9 is the initial stage of the project to replace IAS 39 Future stages are expected to result in amendments to IFRS 9 to deal with changes to the impairment of financial assets measured at amortised cost and hedge accounting Until all stages of the replacement project are complete it is not possible to determine the overall impact on the financial statements of the replacement of IAS 39

At the date of this report, these pronouncements are awaiting EU endorsement

19 PARENT UNDERTAKING AND CONTROLLING PARTY

The Company's immediate parent company is Bank of Scotland plc The company regarded by the directors as the ultimate controlling party is Lloyds Banking Group plc, a limited liability company incorporated and domiciled in Scotland, which is also the parent undertaking of the largest group of undertakings for which group financial statements are drawn up and of which the Company is a member Bank of Scotland plc is the parent undertaking of the smallest such group of undertakings Copies of the group accounts of both companies may be obtained from Group Secretariat, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN