

Registered Number: OC310386

**HBOS SOCIAL HOUSING COVERED BONDS LLP
MEMBERS' REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014**

**HBOS SOCIAL HOUSING COVERED BONDS LLP
MEMBERS AND LLP INFORMATION**

DESIGNATED MEMBERS

Bank of Scotland plc
Addison Social Housing Limited, as Liquidation Member

MANAGEMENT COMMITTEE

J Howarth (Bank of Scotland plc)
F Kenny (Addison Social Housing Limited)

REGISTERED OFFICE

Charterhall House
City Road
Chester
CH88 3AN

INDEPENDENT AUDITORS

PricewaterhouseCoopers LLP
7 More London Riverside
London
SE1 2RT

**HBOS SOCIAL HOUSING COVERED BONDS LLP
MEMBERS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2014**

Registered Number OC310386

On behalf of the designated members (the "Members") of HBOS Social Housing Covered Bonds LLP (the "LLP"), the Management Committee present their annual report and financial statements for the year ended 31 December 2014.

The LLP is a limited liability partnership domiciled in England. The LLP is registered in England & Wales.

PRINCIPAL ACTIVITY

The LLP is a special purpose entity whose business is the acquisition and management of Housing Association loans and their related security to guarantee the Social Housing Covered Bonds issued by Bank of Scotland plc ("BOS") a subsidiary of Lloyds Banking Group plc ("LBG").

The activities of the LLP are conducted primarily by reference to a series of transaction documents (the "Transaction Documentation") for the sale of the Housing Association loans. The structure has been established as a means of raising finance for BOS and no business activities will be undertaken by the LLP beyond those set out in the Transaction Documentation.

In consideration for the beneficial interest in the Housing Association loans, the LLP is required to give a combination of:

- i) a cash payment to BOS from the proceeds of a term loan;
- ii) a record of a capital contribution in kind being made by BOS; and
- iii) deferred consideration which will be paid by the LLP on each LLP payment date in accordance with the relevant priority of payments.

The programme allows a maximum Covered Bond issuance of £3bn, providing that the Housing Association loans acquired and other assets available meet the Asset Coverage Test ("the ACT") per the Transaction Documentation, which states that the adjusted aggregate amounts of the Housing Association loans and other assets (primarily cash) must be of an amount equal to or greater than the total amount of Social Housing Covered Bonds in issue after taking into account other deductions. More information on the Asset Coverage Test is provided in Note 13(a).

During the year, the Transaction Documentation was amended to allow for the purchase of Lloyds Bank plc ("Lloyds") originated Housing Association loans. In total £888,925,309.00 (2013: £nil) of Lloyds originated loans were added to the programme.

The inclusion of Lloyds originated loans to the programme provides additional credit enhancement by adding to the amount of overcollateralisation of the beneficial interest in the loans which is monitored using the ACT.

DESIGNATED MEMBERS

The Members during the year and up to the date of signing of the financial statements were as follows:

Bank of Scotland plc
Addison Social Housing Limited, as Liquidation Member

MEMBERS' INTERESTS

The policy regarding the allocation of profits to Members and the treatment of capital contributions is set out in note 1 'Significant accounting policies'.

HBOS SOCIAL HOUSING COVERED BONDS LLP
MEMBERS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

Registered Number OC310386

STATEMENT OF MEMBERS' RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS

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

Company law as applied to limited liability partnerships by the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008 (the "Regulations") requires the Members to prepare financial statements for each financial year. Under that law the Members have prepared the partnership financial statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union. Under company law as applied to limited liability partnerships the Members must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the partnership and of the profit or loss of the partnership for that period. In preparing these financial statements, the Members are required to:

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

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

RISK MANAGEMENT

The LLP's assets and liabilities have been classified as financial instruments in accordance with IAS 32 "Financial Instruments: Presentation".

The LLP's financial instruments principally comprise a deemed loan (the "Deemed Loan") to BOS (the "Originator") (equivalent to the value of the LLP's investment in BOS loans), cash and cash equivalents, loans and borrowings and various other receivables and payables that arise directly from its operations. The main purpose of these financial instruments is to raise finance for BOS.

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

Further discussion of the LLP's approach to financial instruments are set out in note 1 'Significant accounting policies' and in note 13 'Management of risk'.

**HBOS SOCIAL HOUSING COVERED BONDS LLP
MEMBERS' REPORT FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)**

Registered Number OC310386

EMPLOYEES

The LLP has employed no staff during the year ended 31 December 2014 or the previous year.

INDEPENDENT AUDITORS AND DISCLOSURE OF INFORMATION TO AUDITORS

Pursuant to section 487 of the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008 auditors duly appointed by the Members of the LLP shall, subject to any resolution to the contrary, be deemed to be reappointed for the next financial year. Having indicated their willingness to do so, PricewaterhouseCoopers LLP will therefore continue in office.

So far as the Members are each aware, there is no relevant audit information of which the LLP's auditors are unaware. The Members have each taken all the steps that they ought to have taken as a member in order to make themselves aware of any relevant audit information and to establish that the LLP's auditors are aware of that information.

STATEMENT OF GOING CONCERN

As set out in the statement of compliance in the significant accounting policies section of the notes to the financial statements, the Members are satisfied that the LLP has adequate resources to continue in business for the foreseeable future and consequently the going concern basis continues to be appropriate in preparing the financial statements.

The LLP holds minimal reserves because all available profits are distributed each year to the Members.

By Order of the Members



J Howarth on behalf of
Bank of Scotland plc
Designated Member

28 April 2015

Independent auditors' report to the members of HBOS Social Housing Covered Bonds LLP

Report on the financial statements

Our opinion

In our opinion, HBOS Social Housing Covered Bonds LLP's financial statements (the "financial statements"):

- give a true and fair view of the state of the limited liability partnership's affairs as at 31 December 2014 and of its result and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 as applied to limited liability partnerships by the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008.

What we have audited

HBOS Social Housing Covered Bonds LLP's financial statements, which are prepared by HBOS Social Housing Covered Bonds LLP, comprise:

- the statement of financial position as at 31 December 2014;
- the income statement and statement of comprehensive income for the year then ended;
- the statement of cashflows for the year then ended;
- the statement of changes in equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

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

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

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

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

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

We have no exceptions to report arising from this responsibility.

Independent auditors' report to the members of HBOS Social Housing Covered Bonds LLP (Continued)

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Members' Responsibilities Statement set out on page 3, the members are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

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

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

What an audit of financial statements involves

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

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

We primarily focus our work in these areas by assessing the members' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

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



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

28 April 2015

**HBOS SOCIAL HOUSING COVERED BONDS LLP
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2014**

	Note	2014 £000	2013 £000
Interest receivable and similar income	2	9,933	10,065
Interest payable and similar charges	3	(9,790)	(9,906)
		<hr/>	<hr/>
Net interest income		143	159
Operating expenses	4	(143)	(159)
		<hr/>	<hr/>
Profit for the year		-	-
		<hr/> <hr/>	<hr/> <hr/>

There are no items of comprehensive income which have not already been presented in arriving at the profit for the year. Accordingly, the profit for the year is the same as total comprehensive income for the year.

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

There was no income or expense recognised directly in equity in the current year or preceding years.

The notes on pages 11 to 32 form an integral part of these financial statements.

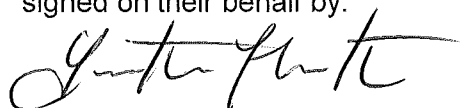
**HBOS SOCIAL HOUSING COVERED BONDS LLP
BALANCE SHEET
AS AT 31 DECEMBER 2014**

Registered Number OC310386

	Note	2014 £000	2013 £000
Assets			
Cash and cash equivalents	5	54,475	203,908
Deemed Loan to Originator	6	1,745,883	1,596,501
Other receivables	7	6	-
		<hr/>	<hr/>
Total assets		1,800,364	1,800,409
		<hr/> <hr/>	<hr/> <hr/>
Members' other interests and liabilities			
Loans and borrowings	8	(1,800,276)	(1,800,310)
Other payables	9	(88)	(99)
		<hr/>	<hr/>
Total liabilities		(1,800,364)	(1,800,409)
		<hr/>	<hr/>
Retained earnings	12	-	-
		<hr/>	<hr/>
Total Members' other interests		-	-
		<hr/>	<hr/>
Total Members' other interests and liabilities		(1,800,364)	(1,800,409)
		<hr/> <hr/>	<hr/> <hr/>
Total Members' interests			
Retained earnings	12	-	-
Deemed Loan to Originator	6	(1,745,883)	(1,596,501)
Loans and borrowings	8	1,800,276	1,800,310
		<hr/>	<hr/>
	12	54,393	203,809
		<hr/> <hr/>	<hr/> <hr/>

The notes on pages 11 to 32 form an integral part of these financial statements

These financial statements were approved by the Members on 28 April 2015 and were signed on their behalf by:



J Howarth on behalf of Bank of Scotland plc
Designated Member

HBOS SOCIAL HOUSING COVERED BONDS LLP
STATEMENT OF CHANGES IN MEMBERS' EQUITY INTERESTS
FOR THE YEAR ENDED 31 DECEMBER 2014

	Note	Retained Earnings £000
Balance at 1 January 2014		-
Total comprehensive income for the year		-
		<hr/>
Balance at 31 December 2014	12	-
		<hr/> <hr/>

	Note	Retained Earnings £000
Balance at 1 January 2013		-
Total comprehensive income for the year		-
		<hr/>
Balance at 31 December 2013	12	-
		<hr/> <hr/>

The notes on pages 11 to 32 form an integral part of these financial statements

**HBOS SOCIAL HOUSING COVERED BONDS LLP
CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2014**

	Note	2014 £000	2013 £000
Operating Activities			
Audit fees paid		(26)	-
Administration expenses		(134)	(140)
		<hr/>	<hr/>
Net cash flows used in operating activities		(160)	(140)
		<hr/>	<hr/>
Investing Activities			
Principal (repayments) / receipts on Deemed Loan to Originator		(148,316)	772,565
Interest on Deemed Loan to Originator		7,335	13,877
Bank interest received		1,532	588
		<hr/>	<hr/>
Net cash flows (used in) / generated from investing activities		(139,449)	787,030
		<hr/>	<hr/>
Financing Activities			
Interest on term loan		(9,812)	(9,992)
Principal repayments on term loan		-	(600,000)
Interest paid to Members		(12)	(12)
		<hr/>	<hr/>
Net cash flows used in financing activities		(9,824)	(610,004)
		<hr/>	<hr/>
Net (decrease) / increase in cash and cash equivalents		(149,433)	176,886
Cash and cash equivalents at 1 January		203,908	27,022
		<hr/>	<hr/>
Cash and cash equivalents at 31 December	5	54,475	203,908
		<hr/> <hr/>	<hr/> <hr/>

The cashflow statement is presented using the direct method to improve the transparency of the financial statements.

The notes on pages 11 to 32 form an integral part of these financial statements.

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014

1. SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

The financial statements were authorised for issue by the Members on 28 April 2015. The financial statements for the year ended 31 December 2014 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.

Changes in accounting policy

The LLP has adopted the following new standards and amendments to standards which became effective for financial years beginning on or after 1 January 2014. Neither of these standards or amendments to standards has had a material impact on these financial statements.

Amendments to IAS 32 Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities

The amendments to IAS 32 clarify the requirements for offsetting financial instruments and address inconsistencies identified in applying the offsetting criteria used in the standard.

IFRIC 21 Levies

This interpretation clarifies that the obligating event that gives rise to a liability to pay a government levy is the activity that triggers the payment of the levy as set out in the relevant legislation and that an entity's expectation of operating in a future period, irrespective of the difficulties involved in exiting a market, does not create a constructive obligation to pay a levy.

The financial statements also comply with the relevant provisions of Part 15 of the Companies Act 2006, as applying to Limited Liability Partnerships.

The LLP is reliant on support provided by BOS. The Members are satisfied that it is the current intention of LBG to ensure that its subsidiaries, including BOS and the LLP, shall have at all times in the foreseeable future (being the period until at least 31 December 2016) 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 financial statements are presented in Sterling which is the LLP's functional and presentation currency and have been prepared on the historical cost basis.

The accounting policies set out below have been applied consistently throughout the year under review.

(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 cashflows are estimated after considering all the contractual terms of the instrument but not future credit losses.

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Accrued interest

Accrued interest has been incorporated within the Deemed Loan to Originator and outstanding balance of loans and borrowings in issue on the Balance Sheet. A split between principal and accrued interest can be found in note 6 and 8.

(d) Financial instruments

The LLP's financial instruments principally comprise a Deemed Loan to BOS (equivalent to the value of the LLP's investment in BOS loans), cash and cash equivalents, loans and borrowings and various other receivables and payables that arise directly from its operations. The main purpose of these financial instruments is to raise finance for BOS. These financial instruments are classified in accordance with the principles of IAS 39 as described below.

(d)(i) Deemed Loan to Originator

Under IAS 39, if a transferor retains substantially all the risks and rewards associated with the transferred assets, the transaction is accounted for as a financing transaction, notwithstanding that it is a sale transaction from a legal perspective. The Members of the LLP have concluded that the Originator has retained substantially all the risks and rewards of the portfolio of Housing Association loans sold to the LLP and as a consequence, the LLP does not recognise the Housing Association loans on its Balance Sheet but rather a Deemed Loan to Originator, where recourse to BOS is limited to the cash flows from the Housing Association loans and any additional credit enhancement provided by BOS.

The initial amount of the Deemed Loan to Originator corresponds to the consideration paid by the LLP for the Housing Association loans. The LLP recognises principal and interest cash flows from the underlying portfolio of Housing Association loans only to the extent that it is entitled to retain such cash flows. Cash flows attributable to the Originator are not recognised by the LLP.

The Deemed Loan is classified within "loans and receivables". The initial measurement is at fair value with subsequent measurement being at amortised cost using the effective interest method. The effective interest on the Deemed Loan is calculated with reference to the interest earned on the beneficial interest in the Housing Association portfolio less the residual interest due to the Originator. Under the terms of the loan sale agreement, the Originator retains the right to receive excess income arising on those loans, after certain higher priority payments have been met by the LLP.

Impairment of financial assets

The Deemed Loan is subject to impairment reviews in accordance with IAS 39. A charge for impairment would be recognised where there is a risk that the income on the Deemed Loan will be significantly reduced. This could occur if the credit quality of the Housing Association assets that are pledged as collateral for the loan significantly deteriorated. Currently the Management Committee consider that no impairment exists.

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d)(i) Deemed Loan to Originator (continued)

Derivative financial instruments

IAS 39 requires all derivative financial instruments to be recognised initially at fair value on the Balance Sheet and to be re-measured to fair value at subsequent reporting dates. Where the value of the derivative is positive, it is carried as a derivative asset and where negative, as a derivative liability.

The LLP uses derivative financial instruments to manage its exposure to interest rate risk arising from operational, financing and investing activities. In accordance with its treasury policy, the LLP does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Interest rate risk associated with the Deemed Loan is managed by means of an interest rate swap with BOS, which requires the LLP to pay the effective yield on the beneficial interest in the loan portfolio and receive payments based on a rate linked to the three-month Sterling LIBOR.

This swap is not recognised separately as a financial instrument as the amounts payable under the swap reflect interest flows from the Housing Association loans which are not recognised by the LLP for accounting purposes. Instead, the Deemed Loan to BOS is recognised with an effective interest rate which reflects the amount received or paid under the swap.

Interest receivable or payable on the interest rate swap is accounted for on an accruals basis within interest on the Deemed Loan.

(d)(ii) Cash and cash equivalents

The LLP holds deposits with the provider of a guaranteed investment contract ("GIC") and a transaction bank account with the same provider, being BOS. These accounts are held in the LLP's name and meet the definition of cash and cash equivalents. All cash disclosed on the face of the Balance Sheet is restricted by a detailed priority of payments set out in the Transaction Documentation. As the cash can only be used to meet specific liabilities and is not available to be used with discretion, it is viewed as restricted cash.

(d)(iii) Loans and borrowings

Loans and borrowings are recognised initially at fair value plus 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 Statement of Comprehensive Income over the period of the borrowings on an effective interest basis. The term loans (equivalent to the proceeds of the covered bonds issued) which are received from BOS are accounted for on this basis.

Capital contributions from Members are non-interest-bearing but a nominal profit share amount is paid out in accordance with the priority of payments (see 1(e) below) and included as part of interest payable and similar charges.

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Contributions and drawings

Under the terms of the LLP Deed, the Originator is treated as having made a capital contribution to the LLP in an amount equal to the difference between the current balance of the loans sold at transfer date and the cash payment made by the LLP for the loans and relevant security on that transfer date. The outstanding capital contributions are not reflected in the financial statements of the LLP as there has been no sale of loans for accounting purposes.

If so requested by the Management Committee, the Members (other than the Liquidation Member) may from time to time make cash contributions to the LLP which will constitute cash capital contributions. Addison Social Housing Limited will not make any capital contributions to the LLP. No interest is paid on the Members' capital balances. Capital distributions may only be made in accordance with the LLP Deed, where sufficient principal receipts are available and higher priority payments have been made.

The LLP has no control over the repayment of the capital contributions, which are driven by actual repayments on the underlying loans in the portfolio which make cash available to be paid in accordance with the priority of payments. These loans may be repaid by the borrowers at any time.

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

(f) 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 is subject to risks and returns that are different from those segments operating in other economic environments.

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

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(g) Critical accounting estimates and judgements

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 accounting 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 but not future credit losses. The calculation includes all amounts expected to be paid or received by the LLP including expected early redemption fees and related penalties and premiums and discounts that are an integral part of the overall return. 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.

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. Fair value is based upon cash flow models which use, wherever possible, independently sourced market parameters, such as interest yield curves. Other factors are also considered, such as counterparty credit quality and liquidity.

Impairment of Deemed Loan

The LLP's accounting policy for losses arising on the Deemed Loan classified as loans and receivables is described in note 1(d)(i). The allowance for impairment losses on loans and receivables is management's best estimate of losses incurred in the portfolio at the Balance Sheet date. Impairment allowances are established to recognise incurred impairment losses in the LLP's loan portfolios carried at amortised cost. In determining whether impairment has occurred at the Balance Sheet date the LLP considers whether there is any observable data indicating that there has been a measurable decrease in the estimated future cash flows or their timings. Where this is the case, the impairment loss is the difference between the carrying value of the loan and the present value of the estimated future cash flows discounted at the loan's original effective interest rate.

At 31 December 2014, impairment allowances against the Deemed Loan totalled £nil (2013: £nil).

(h) Taxation

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

**HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)**

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(i) Related parties

In accordance with the provisions of IAS 24 "Related Party Disclosures", the LLP has disclosed details of transactions with its related parties (note 14).

(j) Other payables

Other payables are stated at cost, or at amortised cost if deemed to be a financial liability.

(k) Value added tax

Value added tax is not recoverable by the LLP and is included with the related costs.

2. INTEREST RECEIVABLE AND SIMILAR INCOME

	2014	2013
	£000	£000
Interest receivable on Deemed Loan	8,401	9,477
Bank interest receivable	1,532	588
	<hr/>	<hr/>
	9,933	10,065
	<hr/> <hr/>	<hr/> <hr/>

3. INTEREST PAYABLE AND SIMILAR CHARGES

	2014	2013
	£000	£000
Interest payable to BOS on term loans	9,778	9,894
Interest payable to Members	12	12
	<hr/>	<hr/>
	9,790	9,906
	<hr/> <hr/>	<hr/> <hr/>

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

4. OPERATING EXPENSES

	2014 £000	2013 £000
Administration charges	130	146
Audit fees	13	13
	<u>143</u>	<u>159</u>

Audit fees relate to the statutory audit. The LLP has also accrued an audit fee of £1,200 (2013: £1,200) on behalf of Addison Social Housing Limited and Addison Social Housing Holdings Limited. There are no fees payable to the auditors and their associates for services other than the statutory audit.

5. CASH AND CASH EQUIVALENTS

The LLP has placed its deposit account with a provider of a GIC, BOS, a subsidiary undertaking of LBG. Withdrawals from this account are restricted by the detailed priority of payments set out in the Transaction Documentation. The LLP is contractually entitled to a variable rate of interest of 0.25 per cent per annum below LIBOR for three-month Sterling deposits, which is recorded as interest receivable in the Statement of Comprehensive Income.

	2014 £000	2013 £000
Bank deposit account	54,475	203,908
	<u>54,475</u>	<u>203,908</u>

6. DEEMED LOAN TO ORIGINATOR

Income on the Deemed Loan to Originator, arising on the underlying loans, reflects fixed, variable and tracker rates. Deferred consideration is deducted from this income in order to arrive at the effective yield on the Deemed Loan.

	2014 £000	2013 £000
Non-current assets		
Deemed Loan to Originator	1,757,499	1,609,183
Current assets		
Deemed Loan to Originator	(11,616)	(12,682)
	<u>1,745,883</u>	<u>1,596,501</u>
TOTAL	1,745,883	1,596,501

**HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)**

6. DEEMED LOAN TO ORIGINATOR (CONTINUED)

The current asset balance above includes accrued swap interest payable and further consideration due to the Originator in-line with the accounting policy in note 1(d)(i), which has resulted in a net credit position as at 31 December 2014 and 31 December 2013.

7. OTHER RECEIVABLES

	2014	2013
	£000	£000
Prepayments and accrued income	6	-
	<hr/>	<hr/>

8. LOANS AND BORROWINGS

This note provides information about the contractual terms of the LLP's loans and borrowings. For more information about the LLP's exposure to interest rate risk, see note 13.

Loans and borrowings comprise a series of term loans from BOS, equivalent to the amounts raised under its Covered Bonds Programme. Each term advance bears interest at a rate equal to LIBOR for three-month Sterling deposits.

BOS will not be relying on repayment of any term loan by the LLP nor the interest thereon in order to meet its repayment or interest obligations under the Covered Bonds Programme. The term loans will not be repaid by the LLP until all amounts payable under the corresponding series of Covered Bonds have been repaid in full. Amounts owed by the LLP will be subordinated to amounts owed under the Covered Bond Guarantee described below.

The Covered Bonds are unconditionally guaranteed by BOS (the "Group Guarantor"). Under the terms of the Trust Deed, the LLP has also provided a guarantee as to payments of interest and principal under the Covered Bonds Programme, where amounts would otherwise be unpaid by BOS or the Group Guarantor. The obligations of the LLP under its guarantee constitute direct obligations of the LLP secured against the assets from time to time of the LLP and recourse against the LLP is limited to such assets. The principal asset is the beneficial interest in the Housing Association loans acquired from BOS.

Where the LLP enters into financial guarantee contracts to guarantee the indebtedness of BOS, the LLP treats the above guarantee contract as a contingent liability until such time as it becomes probable that the LLP will be required to make a payment under the guarantee.

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

8. LOANS AND BORROWINGS (CONTINUED)

	2014 £000	2013 £000
Non-current liabilities		
Term loans with BOS	1,800,000	1,800,000
Current liabilities		
Interest due on term loans	276	310
TOTAL	1,800,276	1,800,310

The term loans due to BOS mature following repayment of the Covered Bonds on the following dates:

Covered Bond issuance	Maturity date	2014 £000	2013 £000
Non-current liabilities			
2004-1	20 December 2024	500,000	500,000
2006-1	8 November 2016	500,000	500,000
2008-1 (Tranche 2)	8 November 2019	100,000	100,000
2008-2 (Tranche 1)	8 November 2016	100,000	100,000
2008-2 (Tranche 2)	8 November 2019	500,000	500,000
2008-2 (Tranche 3)	8 November 2022	100,000	100,000
		<u>1,800,000</u>	<u>1,800,000</u>

9. OTHER PAYABLES

	2014 £000	2013 £000
Accruals and deferred income	75	73
Audit fee accrual	13	26
	<u>88</u>	<u>99</u>

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

10. COVERED BONDS SWAP AGREEMENT

The LLP has entered into a Covered Bonds Swap Agreement with BOS. This agreement provides a hedge against interest rate, currency and/or other risks in respect of amounts received by the LLP from the Housing Association loans and the interest rate swap and amounts payable by the LLP under the Covered Bonds Guarantee in respect of the Covered Bonds.

The Covered Bonds Swap Agreement provides a hedge against risks the LLP is exposed to following a BOS event of default and the service on the LLP of a notice to pay. As such, no payments of interest or exchanges of principal are due and payable under this agreement prior to these events. In accordance with the terms of this swap, the swap provider will pay to the LLP amounts equivalent to the amounts that would be payable by the LLP under the Covered Bonds guarantee in respect of interest and principal payable under the Covered Bonds and, in return, the LLP will pay to the Covered Bonds swap provider on each LLP payment date an amount equal to three-month Sterling LIBOR for the relevant interest period plus a spread.

Following amendments to the Covered Bonds Swap Agreement in December 2012 it has been agreed that BOS is only required to post collateral should its credit rating fall below A (long term) or A-1 (short term) by S&P, or P-1 (short term) by Moody's. The collateral posted would only be utilised by the LLP in the event of a default occurring as referred to in the Transaction Documentation.

11. FINANCIAL GUARANTEE FROM BOS

Financial guarantees are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. BOS have provided a financial guarantee to the LLP, the terms of which, as detailed in the Transaction Documentation, are described below.

BOS is required to buy back all defaulting Housing Association loans from the LLP once they reach more than 60 days in arrears. There is no loss suffered by the LLP, as this buy-back includes all outstanding amounts, including all arrears on the Housing Association loans. There were no such buy backs in the current or prior years.

The maximum potential amount payable to the LLP under the guarantee is equal to the non-current amount outstanding on the Deemed Loan to Originator. This amounted to £1,757,499,070 at 31 December 2014 (2013: £1,609,183,415).

HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)

12. TOTAL MEMBERS' INTERESTS

2014

	Members' Other Interests				
	Members' Capital	Retained Earnings	Total	Loans due to/(from) Members	Total
	£000	£000	£000	£000	£000
Members' interests as at					
1 January 2014	-	-	-	203,809	203,809
Profit for the year available for division among Members	-	-	-	-	-
Loans repaid by BOS	-	-	-	(34)	(34)
Movements in other intercompany amounts	-	-	-	(149,382)	(149,382)
	-----	-----	-----	-----	-----
Members' interests as at 31 December 2014	-	-	-	54,393	54,393
	=====	=====	=====	=====	=====

The loans and other debts due to/(from) Members can be analysed as follows:

	Members' interests as at 31 December 2014 £'000
Amounts due to Members	1,800,276
Amounts due from Members	(1,745,883)

	54,393
	=====

**HBOS SOCIAL HOUSING COVERED BONDS LLP
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014 (CONTINUED)**

12. TOTAL MEMBERS' INTERESTS (CONTINUED)

2013

	Members' Other Interests				
	Members' Capital	Retained Earnings	Total	Loans due to/(from) Members	Total
	£000	£000	£000	£000	£000
Members' interests as at 1 January 2013	-	-	-	26,942	26,942
Profit for the year available for division among Members	-	-	-	-	-
Loans repaid by BOS	-	-	-	(600,098)	(600,098)
Movements in other intercompany amounts	-	-	-	776,965	776,965
Members' interests as at 31 December 2013	-	-	-	203,809	203,809

The loans and other debts due to/(from) Members can be analysed as follows:

	Members' interests as at 31 December 2013 £'000
Amounts due to Members	1,800,310
Amounts due from Members	(1,596,501)
	203,809