

## PEDEFORD MASTER ISSUER PLC

(incorporated in England and Wales with limited liability, registered number 06121308)

### Mortgage Backed Note Programme

Under the mortgage backed notes issuance programme (the **programme**), Pendeford Master Issuer plc (the **issuing entity**) may from time to time issue class A notes, class B notes, class M notes, class C notes and class D notes in one or more series (together, the **notes**). Each series will consist of one or more classes of notes. One or more series and class of notes may be issued at any one time.

This base prospectus has been approved by the Financial Services Authority (the **UK Listing Authority**) in its capacity as competent authority under the Financial Services and Markets Act 2000 (the **FSMA**) as a base prospectus for the purposes of Article 5 of the Prospectus Directive (Directive 2003/71/EC) (the **Prospectus Directive**) and relevant implementing legislation in the United Kingdom. This base prospectus is not a prospectus for purposes of Section 12(a)(2) or any other provision of or rule under the United States Securities Act of 1933, as amended (the **Securities Act**).

Application will be made to the UK Listing Authority for each series and class of notes issued under the programme (other than any which are to be unlisted or listed on any other exchange) during the period of 12 months after the date of this base prospectus to be admitted to the official list of the UK Listing Authority (the **official list**) and application will be made to the London Stock Exchange plc (the **London Stock Exchange**) for such notes to be admitted to trading on the London Stock Exchange's Regulated Market (being a regulated market for purposes of Directive 2004/39/EC (the **Markets in Financial Instruments Directive**)). Such notes are collectively referred to as the **listed notes**. The final terms of an issuance of notes listed on a closing date (including any series and classes or sub-classes of such notes, the aggregate nominal amounts of such notes, interest (if any) payable in respect of such notes, the issue price of such notes and any other terms and conditions of such notes not described in this base prospectus and certain financial and other information about the issuing entity's assets) will be determined by the issuing entity in accordance with the prevailing market conditions at the time of the issue of the relevant notes and will be set out in a separate document (the **final terms**). The final terms for listed notes will be filed with the UK Listing Authority and made available to the public in accordance with the prospectus rules made pursuant to Part VI of the FSMA (the **prospectus rules**). The programme also provides that notes may be listed on such other or further stock exchange(s) as may be agreed between the issuing entity and the relevant dealers and/or managers, or unlisted.

The principal asset from which the issuing entity will make payments on the notes is a master intercompany loan to Funding (No. 1) Limited (referred to in this prospectus as **Funding 1**).

The principal asset from which Funding 1 will make payments on the master intercompany loan is its interest in a master trust over a pool of residential mortgage loans held by Pendeford Mortgages Trustee Limited (referred to in this prospectus as the **mortgages trustee**), which mortgage loans were originated under the brand Birmingham Midshires by Halifax plc (**Halifax**) and following 17 September 2007 (the **reorganisation date**) under the Birmingham Midshires brand by Bank of Scotland plc (**Bank of Scotland**) (being the entity to which the business carried on by Halifax was transferred to in accordance with the HBOS Group Reorganisation Act 2006 on the reorganisation date). References in this prospectus to Halifax or Bank of Scotland as the originator of the mortgage loans and/or as the party to the mortgage sale agreement are references to the relevant legal entity acting as seller at the time of sale of the mortgage loans to the mortgages trustee. The residential mortgage loans are secured over properties located in England, Wales and Scotland.

This prospectus includes information on the transfer of the business and all property and liabilities of Halifax to Bank of Scotland on the reorganisation date following the registration of The Governor and Company of the Bank of Scotland as a public limited company incorporated in Scotland under the Companies Act 1985 and its change of name to Bank of Scotland plc on such date. See "**Bank of Scotland plc**".

The notes have not been and will not be registered under the United States Securities Act of 1933, as amended (the **Securities Act**), or any state securities laws. Subject to certain exceptions, the notes may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act (**Regulation S**)).

The programme provides that the issuing entity may issue notes to be sold outside the United States to non-U.S. persons in reliance on Regulation S. Such notes are collectively referred to herein as **Reg S notes**. The issuing entity may also issue notes which will be sold within the United States only to qualified institutional buyers (**QIBs**) within the meaning of Rule 144A under the Securities Act (**Rule 144A**) in reliance on Rule 144A. Such notes are collectively referred to herein as the **Rule 144A notes**. Prospective purchasers are hereby notified that sellers of the notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. For a description of certain further restrictions on offers, sales and transfers of notes in this base prospectus, see "**Subscription and sale**" and "**Transfer restrictions and investor representations**" below.

The issuing entity may agree with any dealer and/or manager and the note trustee that notes may be issued in a form not contemplated by the terms and conditions of the notes herein in which event (in the case of notes admitted to the official list only) a supplementary prospectus will be made available which will describe the effect of the agreement reached in relation to such notes.

The notes will be assigned certain minimum ratings upon issue by each of Fitch Ratings Ltd. (**Fitch**), Moody's Investors Service Limited (**Moody's**) and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies Inc. (**Standard & Poor's**) which are described in "**Overview of base Prospectus**" and "**Overview of the notes**" below. The ratings assigned to the notes will be specified in the applicable final terms. A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

Notwithstanding any provision in this base prospectus to the contrary, each prospective investor (and each employee, representative or other agent of each such prospective investor) may disclose to any and all persons, without limitation of any kind, the U.S. federal income tax treatment and U.S. federal income tax structure of any transaction contemplated in this base prospectus and all materials of any kind (including opinions or other tax analyses) that are provided to it relating to such U.S. federal income tax treatment and U.S. federal income tax structure.

A note is not a deposit and neither the notes nor the underlying receivables are insured or guaranteed by any United Kingdom or United States governmental agency.

**Neither the United States Securities and Exchange Commission (the SEC) nor any state securities commission in the United States nor any other United States regulatory authority has approved or disapproved the notes or determined that this base prospectus is truthful or complete. Any representation to the contrary is a criminal offence in the United States.**

**Please consider carefully the risk factors beginning on page 28 of this base prospectus.**

**Arranger for the programme**

**Bank of Scotland Treasury**

THE NOTES HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE SECURITIES ACT, OR ANY STATE SECURITIES LAWS, AND UNLESS SO REGISTERED MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, US PERSONS (AS DEFINED IN REGULATION S UNDER THE SECURITIES ACT) EXCEPT PURSUANT TO AN EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND APPLICABLE STATE SECURITIES LAWS. UNTIL 40 DAYS AFTER THE COMMENCEMENT OF THE OFFERING, AN OFFER OR SALE OF THE NOTES WITHIN THE UNITED STATES BY ANY DEALER OR MANAGER (WHETHER OR NOT PARTICIPATING IN THE OFFERING) MAY VIOLATE THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT IF SUCH OFFER OR SALE IS MADE OTHERWISE THAN IN COMPLIANCE WITH RULE 144A OR PURSUANT TO ANOTHER EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT. THERE IS NO UNDERTAKING TO REGISTER THE NOTES UNDER US STATE OR FEDERAL SECURITIES LAWS. FOR A DESCRIPTION OF CERTAIN RESTRICTIONS ON REALES OR TRANSFERS, SEE “**SUBSCRIPTION AND SALE**” AND “**TRANSFER RESTRICTIONS AND INVESTOR REPRESENTATIONS**” BELOW AND THE APPLICABLE FINAL TERMS.

THE NOTES WILL BE OFFERED AND SOLD IN THE UNITED STATES ONLY TO A LIMITED NUMBER OF QUALIFIED INSTITUTIONAL BUYERS IN RELIANCE ON RULE 144A AND IN ACCORDANCE WITH ANY APPLICABLE LAWS OF ANY STATE.

EACH INITIAL AND SUBSEQUENT PURCHASER OF THE NOTES WILL BE DEEMED BY ITS ACCEPTANCE OF SUCH NOTES TO HAVE MADE CERTAIN ACKNOWLEDGEMENTS, REPRESENTATIONS AND AGREEMENTS INTENDED TO RESTRICT THE RESALE OR OTHER TRANSFER OF THE NOTES AS SET FORTH THEREIN AND DESCRIBED IN THIS BASE PROSPECTUS AND, IN CONNECTION THEREWITH, MAY BE REQUIRED TO PROVIDE CONFIRMATION OF ITS COMPLIANCE WITH SUCH RESALE AND OTHER TRANSFER RESTRICTIONS IN CERTAIN CASES. SEE “**SUBSCRIPTION AND SALE**” AND “**TRANSFER RESTRICTIONS AND INVESTOR REPRESENTATIONS**” BELOW AND THE APPLICABLE FINAL TERMS.

THE ISSUING ENTITY, THE DEALERS AND ANY MANAGERS MAKE NO REPRESENTATION TO ANY PROSPECTIVE INVESTOR OR PURCHASER OF THE NOTES REGARDING THE LEGALITY OF INVESTMENT THEREIN BY SUCH PROSPECTIVE INVESTOR OR PURCHASER UNDER APPLICABLE LEGAL INVESTMENT OR SIMILAR LAWS OR REGULATIONS. SEE “**UNITED STATES LEGAL INVESTMENT CONSIDERATIONS OF LAW**”.

THE NOTES WILL BE OBLIGATIONS OF THE ISSUING ENTITY ONLY. THE NOTES WILL NOT BE OBLIGATIONS OF, OR THE RESPONSIBILITY OF, OR GUARANTEED BY, ANY PERSON OTHER THAN THE ISSUING ENTITY. IN PARTICULAR, THE NOTES WILL NOT BE OBLIGATIONS OF, OR THE RESPONSIBILITY OF, OR GUARANTEED BY, ANY OF BANK OF SCOTLAND PLC (**BANK OF SCOTLAND**), THE DEALERS, THE MANAGERS, THE NOTE TRUSTEE, THE FUNDING 1 SECURITY TRUSTEE, THE ISSUING ENTITY SECURITY TRUSTEE, FUNDING 1, THE MORTGAGES TRUSTEE, THE CORPORATE SERVICES PROVIDER, THE FUNDING 1 SWAP PROVIDER, THE ISSUING ENTITY SWAP PROVIDERS OR THEIR GUARANTORS, AS APPLICABLE, THE PAYING AGENTS, THE REGISTRAR, THE TRANSFER AGENT, THE AGENT BANK, THE ACCOUNT BANK, THE ISSUING ENTITY ACCOUNT BANK OR ANY COMPANY IN THE SAME GROUP OF COMPANIES AS BANK OF SCOTLAND OR ANY OTHER PARTY TO THE TRANSACTION DOCUMENTS (BUT WITHOUT PREJUDICE TO THE OBLIGATIONS OF FUNDING 1 TO THE ISSUING ENTITY UNDER THE INTERCOMPANY LOAN AGREEMENT). NO LIABILITY WHATSOEVER IN RESPECT OF ANY FAILURE BY THE ISSUING ENTITY TO PAY ANY AMOUNT DUE UNDER THE NOTES SHALL BE ACCEPTED BY ANY OF BANK OF SCOTLAND, THE DEALERS, THE MANAGERS, THE NOTE TRUSTEE, THE FUNDING 1 SECURITY TRUSTEE, THE ISSUING ENTITY SECURITY TRUSTEE, FUNDING 1, THE MORTGAGES TRUSTEE, THE CORPORATE SERVICES PROVIDER, THE FUNDING 1 SWAP PROVIDER, THE ISSUING ENTITY SWAP PROVIDERS OR THEIR GUARANTORS, AS APPLICABLE, THE PAYING AGENTS, THE REGISTRAR, THE TRANSFER AGENT, THE AGENT BANK, THE ACCOUNT BANK, THE ISSUING ENTITY ACCOUNT BANK OR ANY COMPANY IN THE SAME GROUP OF COMPANIES AS BANK OF SCOTLAND OR ANY OTHER PARTY TO THE TRANSACTION DOCUMENTS.

The notes of each class sold in reliance on Rule 144A will be represented on issue by a global note in registered form for each such class (the **Rule 144A global notes**). The notes of each class sold in reliance on Regulation S will be represented on issue by a global note in registered form for each such class (the **Reg S global notes** and, together with the Rule 144A global notes, the **global notes**).

The issuing entity will maintain a register, to be kept by the registrar, in which it will register the name of (i) a nominee of a common depositary (the **common depositary**) for Euroclear Bank S.A./N.V. (**Euroclear**) and Clearstream Banking, société anonyme (**Clearstream, Luxembourg**), as owner of the Reg S global notes and/or the Rule 144A global notes, as specified in the applicable final terms, and (ii) Cede & Co, as nominee for The Depository Trust Company (**DTC**) as owner of the Rule 144A global notes and/or Reg S global notes, as specified in the applicable final terms. Transfers of all or any portion of the interests in the global notes may be made only through the register maintained by the issuing entity. Each of DTC, Euroclear and Clearstream, Luxembourg will record the beneficial interests in the global notes (**book-entry interests**). Book-entry interests in the global notes will be shown on, and transfers thereof will be effected only through, records maintained in a book-entry form by DTC, Euroclear or Clearstream, Luxembourg, and their respective participants. Except in the limited circumstances described under “**The notes and the global notes – Global clearance and settlement procedures – Definitive notes**”, the issuing entity notes will not be available in definitive form (the **definitive notes**). Definitive notes will be issued in registered form only.

#### **Available Information**

The issuing entity accepts responsibility for the information contained in this base prospectus. To the best of the knowledge of the issuing entity (having taken all reasonable care to ensure that such is the case) the information contained in this base prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information. The issuing entity accepts responsibility accordingly.

A copy of this base prospectus and each of the final terms relating to listed notes will be available for inspection at the registered office of the issuing entity and at the specified office of the paying agents or will be available for inspection on the website of the London Stock Exchange in accordance with the Prospectus Rules. A copy of final terms relating to unlisted notes or notes listed on any other stock exchange will be made available at the specified office of each paying agent.

The issuing entity has agreed that, for so long as any of the Rule 144A notes remain outstanding and are “restricted securities” within the meaning of Rule 144(a)(3) under the Securities Act, the issuing entity will furnish, upon request of a holder or of any beneficial owner of such a Rule 144A note or of any prospective purchaser designated by such holder or beneficial owner, the information required to be delivered under Rule 144A(d)(4) under the Securities Act if at the time of the request the issuing entity is not a reporting company under Section 13 or Section 15(d) of the US Securities Exchange Act of 1934, as amended (the **Exchange Act**) or is not exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act.

No person is or has been authorised in connection with the issue and sale of the notes to give any information or to make any representation not contained in this base prospectus and/or the applicable final terms and, if given or made, such information or representation must not be relied upon as having been authorised by or on behalf of the issuing entity, the directors of the issuing entity, Funding 1, the mortgages trustee, Bank of Scotland, the managers, the dealers, the note trustee, the Funding 1 security trustee, the issuing entity security trustee, the corporate services provider, the Funding 1 swap provider, the issuing entity swap providers or their guarantors, as applicable, the paying agents, the registrar, the transfer agent, the agent bank, the account bank, the issuing entity account bank or any company in the same group of companies as Bank of Scotland or any other party to the transaction documents (but without prejudice to the obligations of Funding 1 to the issuing entity under the intercompany loan agreement).

Neither the delivery of this base prospectus and/or the applicable final terms nor any sale or allotment made in connection with the offering of any of the notes shall under any circumstances constitute a representation or create any implication that there has been no change in the affairs of the issuing entity, Funding 1, the mortgages trustee, Bank of Scotland, the dealers, the managers, the note trustee, the Funding 1 security trustee, the issuing entity security trustee, the corporate services provider, the Funding 1 swap provider, the issuing entity swap providers or their guarantors, as applicable, the paying agents, the registrar, the transfer agent, the agent bank, the account bank, the issuing entity account bank or any company in the same group of companies as Bank of Scotland or any other party to the transaction documents or in the information contained herein or therein since the date hereof or thereof or that the information contained herein or therein is correct as at any time subsequent to the date hereof or thereof or that there has been no change in any other information supplied in connection with the programme as of any time subsequent to the date indicated in the document containing the same or that such information is correct at any time subsequent to the date thereof.

Other than the approval of this base prospectus as a base prospectus by the UK Listing Authority, the filing of this base prospectus with the UK Listing Authority, the making the base prospectus available to the public in accordance with the Prospectus Rules and the filing of each of the final terms relating to listed notes with the UK Listing Authority, no action has been or will be taken to permit a public offering of any notes or the distribution of this base prospectus in any jurisdiction where action for that purpose is required. The distribution of this base

prospectus and the offering of notes in certain jurisdictions may be restricted by law. Persons into whose possession this base prospectus (or any part hereof) comes are required by the issuing entity, the dealers and/or the managers to inform themselves about, and to observe, any such restrictions. For a further description of certain restrictions on offers and sales of notes and distribution of this base prospectus, see “**Subscription and sale**” below and the applicable final terms. Neither this base prospectus nor any part hereof constitutes an offer of, or an invitation by, or on behalf of, the issuing entity or any of the dealers and/or the managers to subscribe for or purchase any of the notes and neither this base prospectus, nor any part hereof, may be used for or in connection with an offer to, or solicitation by, any person in any jurisdiction or in any circumstances in which such offer or solicitation is not authorised or to any person to whom it is unlawful to make such offer or solicitation.

Accordingly, the notes may not be offered or sold, directly or indirectly, and neither this base prospectus nor any part hereof nor any final terms nor any other offering document, prospectus, form of application, advertisement, other offering material or other information may be issued, distributed or published in any country or jurisdiction (including the United Kingdom), except in circumstances that will result in compliance with all applicable laws, orders, rules and regulations.

In connection with any issuance of notes, the dealer(s) and/or manager(s) (if any) named as stabilising manager(s) (or persons acting on behalf of any stabilising manager(s)) in the applicable final terms may over-allot such notes or effect transactions with a view to supporting the market price of the notes at a level higher than that which might otherwise prevail. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the relevant series and class of notes is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the closing date of the relevant series and class of notes and 60 days after the date of the allotment of the relevant series and class of notes. Any stabilisation action or over-allotment shall be conducted in accordance with all applicable laws and rules.

A note is not a deposit and neither the notes nor the underlying receivables are insured or guaranteed by any United Kingdom or United States governmental agency.

#### **NOTICE TO NEW HAMPSHIRE RESIDENTS ONLY**

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE STATE OF NEW HAMPSHIRE REVISED STATUTES ANNOTATED (RSA 421-B) WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE OF NEW HAMPSHIRE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATION OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

## Table of contents

	Page
Overview of base prospectus	1
Overview of the transaction	1
Structural diagram of the programme	4
Diagram of ownership structure of special purpose vehicles	5
The key parties	6
Issuing entity	6
Funding 1	6
The mortgages trustee	6
The issuing entity account bank and the account bank	7
The issuing entity swap providers	7
The note trustee, issuing entity security trustee and Funding 1 security trustee	7
The paying agents, agent bank, registrar and transfer agent	7
Overview of the notes	8
Series	8
Payment	8
Issuance	8
Ratings	8
Listing	9
Denominations of the notes	9
Maturities	9
Currencies	9
Issue price	9
Selling restrictions	9
Relationship between the notes, issuing entity subordinated loans and issuing entity start-up loans and the intercompany loan	9
Payment and ranking of the notes	10
Interest	11
Fixed rate notes	11
Floating rate notes	11
Zero coupon notes	11
Bullet redemption notes	11
Scheduled redemption notes	12
Pass-through notes	12
Money market notes	12
Redemption and repayment	14
Optional redemption or repurchase of the notes	14
Post-enforcement call option	14
Withholding tax	15
The programme date	15
Credit enhancement	15
Swap agreements	15
Funding 1 principal deficiency ledger	15
Trigger events	15
Acceleration and enforcement	16
Operative documents relating to the notes	16
Diagram of the priority of payments by the issuing entity and subordination relationships	16
The loans	18
Sale of the loans	18
The mortgages trust	19
The intercompany loan	20
Issuing entity subordinated loan agreements	24
Security granted by Funding 1 and the issuing entity	24
Swap agreements	25
United Kingdom tax status	25
United States tax status	25
Jersey (Channel Islands) tax status	25
ERISA considerations for investors	26
Fees	27
Risk factors	28

Use of proceeds	61
The issuing entity	62
Directors and secretary	63
Capitalisation statement	63
Bank of Scotland plc	65
Bank of Scotland plc	65
Mortgage Business	65
Recent Developments	65
Funding 1	67
The mortgages trustee	69
Holdings	70
PECOH	71
The Funding 1 swap provider	72
The note trustee, the issuing entity security trustee and the Funding 1 security trustee	73
Affiliations and certain relationships and related transactions of transaction parties	74
The loans	75
The servicer	86
The servicer	86
Servicing of loans	86
Recent changes	86
Arrears and default procedures	87
The servicing agreement	89
Introduction	89
Powers	89
Undertakings by the servicer	89
Setting of interest rates on the loans	90
Reasonable, prudent mortgage lender	91
Compensation of the servicer	91
Removal or resignation of the servicer	91
Right of delegation by the servicer	92
Liability of the servicer	92
Governing law	92
Sale of the loans and their related security	93
Introduction	93
Sale of loans and their related security to the mortgages trustee on the sale dates	93
Legal assignment of the loans to the mortgages trustee	96
Representations and warranties	98
Repurchase of loans under a mortgage account	100
Drawings under flexible loans	100
Further advances	100
Product switches	101
Portable loans	101
Reasonable, prudent mortgage lender	101
Governing law	101
The mortgages trust	102
General legal structure	102
Fluctuation of shares in the trust property	103
Funding 1 share	104
Seller share	105
Minimum seller share	106
Cash management of trust property – revenue receipts	106
Mortgages trust calculation of revenue receipts	107
Cash management of trust property – distribution of principal receipts to Funding 1	108
Definitions	108
Mortgages trust calculation of principal receipts	111
Allocation and distribution of principal receipts prior to the occurrence of a trigger event	111
Allocation and distribution of principal receipts on or after the occurrence of a non-asset trigger event but prior to the occurrence of an asset trigger event	111
Allocation and distribution of principal receipts on or after the occurrence of an asset trigger event	112
Losses	112
Disposal of trust property	112
Additions to trust property	112

Acquisition by Funding 1 of an increased interest in trust property	113
Acquisition by seller of an interest relating to capitalised interest	113
Payment by the seller of the amount outstanding under a loan tranche	114
Compensation of mortgages trustee	114
Termination of mortgages trust	114
Retirement of mortgages trustee	114
Governing law	114
The controlling beneficiary deed	115
The intercompany loan agreement	116
The facility	116
Ratings designations of the rated loan tranches	116
Making of loan tranches	117
Representations and agreements	117
Payments of interest	118
Repayment of principal on the rated loan tranches	118
Repayment of principal on the subordinated loan tranches	119
Repayment of principal on the start-up loan tranches	119
Deferral of principal	119
Limited recourse	119
Intercompany loan events of default	120
Funding 1's bank accounts	121
Governing law	121
Security for Funding 1's obligations	122
Covenants of Funding 1	122
Funding 1 security	122
Nature of security – fixed charge	123
Nature of security – floating charge	123
Funding 1 pre-enforcement priority of payments	124
Enforcement	124
Funding 1 post-enforcement priority of payments	124
New Funding 1 issuing entities	125
Appointment, powers, responsibilities and liabilities of the Funding 1 security trustee	125
Funding 1 security trustee's fees and expenses	126
Retirement and removal	126
Additional provisions of the Funding 1 deed of charge	126
Governing law	128
Security for the issuing entity's obligations	129
Covenants of the issuing entity	129
Issuing entity security	129
Nature of security – fixed charge	130
Nature of security – floating charge	130
Enforcement	131
Issuing entity post-enforcement priority of payments	131
New issuing entity secured creditors	131
Appointment, powers, responsibilities and liabilities of the issuing entity security trustee	131
Issuing entity security trustee's fees and expenses	132
Retirement and removal	133
Additional provisions of the issuing entity deed of charge	133
Governing law	134
Cashflows	135
Definition of Funding 1 available revenue receipts	135
Distribution of Funding 1 available revenue receipts before intercompany loan acceleration	136
Definition of issuing entity revenue receipts	139
Distribution of issuing entity revenue receipts before note acceleration	139
Distribution of issuing entity revenue receipts after note acceleration but before intercompany loan acceleration	142
Distribution of Funding 1 available principal receipts	142
Payment of principal receipts to Funding 1 by the mortgages trustee	142
Definition of Funding 1 available principal receipts	143
Due and payable dates of loan tranches	143
Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes	144
Rule (1) – Repayment deferrals	145

Rule (2) – Repayment of payable pass-through loan tranches after a step-up date	147
Repayment of loan tranches (other than start-up loan tranches) after a non-asset trigger event but before intercompany loan acceleration or acceleration of all notes	148
Repayment of loan tranches (other than start-up loan tranches) after an asset trigger event but before intercompany loan acceleration or acceleration of all notes	148
Repayment of loan tranches (other than start-up loan tranches) after acceleration of all notes but before intercompany loan acceleration	149
Repayment of loan tranches (other than start-up loan tranches) when Funding 1 receives an amount outstanding under the intercompany loan	150
Definition of issuing entity principal receipts	150
Distribution of issuing entity principal receipts before note acceleration	150
Distribution of issuing entity principal receipts after note acceleration but before intercompany loan acceleration	151
Distribution of Funding 1 principal receipts and Funding 1 revenue receipts following intercompany loan acceleration	153
Distribution of issuing entity principal receipts and issuing entity revenue receipts following note acceleration and intercompany loan acceleration	154
Credit structure	157
Credit support for the notes provided by Funding 1 available revenue receipts	157
Level of arrears experienced	158
Use of Funding 1 principal receipts to pay Funding 1 income deficiency	158
Funding 1 general reserve fund	159
Funding 1 principal deficiency ledger	159
Issuing entity available funds	161
Priority of payments among the class A notes, the class B notes, the class M notes, the class C notes, the class D notes and the issuing entity subordinated loans	161
Issuing entity subordinated loan agreements	162
General description	162
Interest	162
Repayment	162
Acceleration	163
Governing law	163
Mortgages trustee GIC account/Funding 1 GIC account	163
Funding 1 liquidity reserve fund	163
Issuing entity start-up loan agreements	164
General description	164
Interest	165
Repayment	165
Acceleration	165
Governing law	165
The swap agreements	166
General	166
The Funding 1 swap	166
Issuing entity currency swaps	168
Issuing entity interest rate swaps	169
Ratings downgrade of swap providers	169
Termination of the swaps	169
Transfer of the swaps	171
Taxation	171
Governing law	171
Cash management for the mortgages trustee and Funding 1	172
Cash management services provided in relation to the mortgages trust	172
Cash management services provided to Funding 1	172
Periodic audit	174
Compensation of cash manager	174
Resignation of cash manager	174
Termination of appointment of cash manager	174
Governing law	174
Cash management for the issuing entity	175
Cash management services to be provided to the issuing entity	175
Periodic audit	176
The issuing entity's bank accounts	176
Compensation of issuing entity cash manager	176



Resignation of issuing entity cash manager	176
Termination of appointment of issuing entity cash manager	176
Governing law	177
Description of the note trust deed	178
General	178
Governing law	178
The notes and the global notes	179
Payment	180
Clearance and settlement	181
DTC	181
Clearstream, Luxembourg and Euroclear	182
Global clearance and settlement procedures	183
Initial settlement	183
Secondary trading	183
Definitive notes	183
Form of Final Terms	185
Terms and conditions of the notes	226
Material legal aspects of the loans	261
English Loans	261
General	261
Nature of property as security	261
Registered title	261
Unregistered title	261
Taking security over land	261
The seller as mortgagee	262
Enforcement of mortgages	262
Scottish loans	262
General	262
Nature of property as security	263
Land Register	263
Sasine Register	263
Taking security over land	263
The seller as heritable creditor	263
Enforcement of mortgages	263
Borrower's right of redemption	264
United Kingdom taxation	265
Payment of interest on the notes	265
EU Savings Directive	265
United States federal income taxation	267
General	267
Characterisation of the Rule 144A notes	268
Taxation of United States holders of the Rule 144A notes	268
Qualified Stated Interest and Original Issue Discount	268
Sales and retirement	269
Taxation of Non-United States holders of the Rule 144A notes	269
Alternative characterisation of the Rule 144A notes	269
Backup withholding and information reporting	270
IRS disclosure reporting requirements	271
Material Jersey (Channel Islands) tax considerations	272
Tax status of the mortgages trustee and the mortgages trust	272
EU Savings Directive	272
ERISA considerations	273
Enforcement of foreign judgments in England and Wales	276
United States legal investment considerations	277
Remarketing Arrangements	278
The remarketing agreement	278
Subscription and sale	279
United Kingdom	279
United States	279
Republic of Italy	280
General	280
Transfer restrictions and investor representations	282
Offers and sales by the initial purchasers	282

Investor representations and restrictions on resale	282
Reports to noteholders	285
Certain relationships	286
Listing and general information	287
Glossary	290
Annex A	1
Annex B	1

## Forward-looking statements

This base prospectus includes forward-looking statements including, but not limited to, statements made under the headings “**Risk factors**”, “**The loans**”, “**The servicer**” and “**The servicing agreement**”. These forward-looking statements can be identified by the use of forward-looking terminology, such as the words “believes”, “expects”, “may”, “intends”, “should” or “anticipates” or the negative or other variations of those terms. These statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results and performance of the notes, Bank of Scotland plc (**Bank of Scotland**) or the UK residential mortgage industry to differ materially from any future results or performance expressed or implied in the forward-looking statements. These risks, uncertainties and other factors include, among others, general economic and business conditions in the United Kingdom, currency exchange and interest rate fluctuations, government, statutory, regulatory or administrative initiatives affecting Bank of Scotland, changes in business strategy, lending practices or customer relationships and other factors that may be referred to in this base prospectus. Some of the most significant of these risks, uncertainties and other factors are discussed in this base prospectus under the heading “**Risk factors**”, and you are encouraged to carefully consider those factors prior to making an investment decision in relation to the notes. The managers and/or dealers have not attempted to verify any such statements, nor do they make any representations, express or implied, with respect thereto. The issuing entity expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statement contained herein to reflect any change in the issuing entity’s expectations with regard thereto or any changes in events, conditions or circumstances on which any such statement is based.

## Defined terms and conventions

References herein to this **base prospectus** are to the base prospectus approved by the UK Listing Authority and references herein to **supplementary prospectus** are to any supplement to such base prospectus approved by the UK Listing Authority during the period of 12 months after the date of such base prospectus.

References in this base prospectus to **issuing entity**, **we** or **us** mean Pendeford Master Issuer plc and references to **you** mean potential investors in the notes.

References in this base prospectus to **£**, **pounds** or **sterling** are to the lawful currency for the time being of the United Kingdom of Great Britain and Northern Ireland. References in this base prospectus to **US\$**, **\$**, **US dollars** or **dollars** are to the lawful currency of the United States of America. References in this base prospectus to **€**, **euro** or **Euro** are to the single currency introduced at the third stage of European Economic and Monetary Union pursuant to the Treaty establishing the European Communities, as amended from time to time.

References to a **class** of notes are to the class A notes or the class B notes or the class M notes or the class C notes or the class D notes of any series or, if applicable, any sub-class of such class of notes.

## Important notice about information provided in this base prospectus and the applicable final terms

Information about each series and class of notes is contained in two separate documents: (a) this base prospectus, which provides general information, some of which may not apply to a particular series and class of notes; and (b) the applicable final terms for a particular series and class of notes, which describes the specific terms of the notes of that series, including:

- the timing of interest and principal payments;
- financial and other information about the assets of the issuing entity;
- the ratings for the series and class of notes;
- information about enhancement for the series and class of notes;
- the method for selling the notes; and
- other terms and conditions not contained herein that are applicable to your series and class of notes.

This base prospectus may be used to offer and sell any series and class of notes only if accompanied by the applicable final terms for that series and class.

Although the applicable final terms for a particular series and class of notes cannot contradict the information contained in this base prospectus, insofar as the applicable final terms contains specific information about the series and class that differs from the more general information contained in this base prospectus, you should rely on the information in the applicable final terms.

You should rely only on the information contained in this base prospectus and the applicable final terms. The issuing entity has not authorised anyone to provide you with information that is different from that contained in this base prospectus and the applicable final terms. The information in this base prospectus and the applicable final terms is only accurate as of the dates on their respective covers.

Cross-references are included in this base prospectus and each applicable final terms to headings in these materials under which you can find further related discussions. The table of contents in this base prospectus and the table of contents included in each applicable final terms provide the pages on which these headings are located.

## Overview of base prospectus

*The information in this section of the base prospectus is an overview of the principal features of the notes, including the transaction documents and the loans that will generate the income for the issuing entity to make payments on the notes. This overview does not contain all of the information that you should consider before investing in the notes. You should read the entire base prospectus carefully, especially the risks of investing in the notes discussed under “Risk factors” and in the applicable final terms under the heading “Risk factors”.*

### Overview of the transaction

The following is a brief overview of the transaction and is further illustrated by the following **Structural diagram of the programme**. The numbers in the diagram refer to the numbered paragraphs below.

- (1) On the programme date and on subsequent dates prior to the reorganisation date (as defined below), Halifax plc (**Halifax**), as the **seller**, sold loans and their **related security** (which is the security for the repayment of each loan, including the relevant mortgage) to the mortgages trustee pursuant to a mortgage sale agreement. On the reorganisation date, the business and all property and liabilities of Halifax were transferred to Bank of Scotland following the registration of The Governor and Company of the Bank of Scotland as a public company under the Companies Act 1985 and change of name from The Governor and Company of the Bank of Scotland to Bank of Scotland plc. These changes were effected pursuant to the HBOS Group Reorganisation Act 2006 on 17 September 2007 (the **reorganisation date**). From time to time, Bank of Scotland, as the **seller** sold and may sell, subject to satisfaction of the conditions to sale set out in “**Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**” below, further loans and their related security to the mortgages trustee. The **loans** are, as at the date hereof, residential mortgage loans originated by Halifax under the Birmingham Midshires brand and, since the reorganisation date, by Bank of Scotland under the Birmingham Midshires brand, and secured over residential properties located in England, Wales and Scotland (but may in future include loans originated by other entities within the HBOS group).
- (2) The mortgages trustee holds and will hold the loans and other property (the **trust property**) on trust for the benefit of the seller and Funding 1 pursuant to a mortgages trust deed. The trust property includes the **portfolio**, which at any time consists of the loans and their related security held by the mortgages trustee together with any accrued interest on the loans and other amounts derived from the loans and their related security. Each of the seller and Funding 1 has a joint and undivided interest in the trust property, but its entitlement to the proceeds from the trust property is in proportion to its respective share of the trust property, as further described under “**The mortgages trust**” below.
- (3) The mortgages trustee distributes interest receipts on the loans, after payment of certain fees and expenses (including those of the mortgages trustee, the servicer, the cash manager and the account bank), to Funding 1 based on its percentage share in the trust property. The mortgages trustee will distribute the remaining interest receipts on the loans to the seller after the allocation of any loss amount. The mortgages trustee allocates losses on the loans to the seller and Funding 1 in accordance with its respective percentage share in the trust property. These percentage shares may fluctuate as described in “**The mortgages trust**” below. The mortgages trustee allocates principal receipts on the loans between the seller and Funding 1 in amounts depending on whether Funding 1 is required to pay amounts on the intercompany loan on the next Funding 1 interest payment date or whether Funding 1 is accumulating cash to repay a bullet loan tranche or a scheduled amortisation instalment under a scheduled amortisation loan tranche. The issuing entity will make loan tranches available to Funding 1 pursuant to the intercompany loan agreement. These loan tranches will be funded from the proceeds of each series and class of notes (the **rated loan tranches**), each advance by the issuing entity subordinated loan provider or a new issuing entity subordinated loan provider of an issuing entity subordinated loan to the issuing entity whether or not in connection with an issuance of notes (the **subordinated loan tranches**) and each advance by the issuing entity start-up loan provider or a new issuing entity start-up loan provider to the issuing entity of an issuing entity start-up loan in connection with an issuance of notes (the **start-up loan tranches**) (see “**Overview of the notes – Relationship between the notes, issuing entity subordinated loans and issuing entity start-up loans and the intercompany loan**” below). The types of loan tranches (namely, bullet loan tranches, scheduled amortisation loan tranches, pass-through loan tranches, subordinated loan tranches and start-up loan tranches) are described under “– **The intercompany loan**” below.
- (4) Funding 1 will use the proceeds of rated loan tranches received from time to time from the issuing entity under the intercompany loan agreement to:

- (i) pay the seller part of the consideration for loans (together with their related security) sold by the seller to the mortgages trustee in connection with the issuance of notes by the issuing entity and the making of the relevant rated loan tranches to Funding 1, which will result in an increase in the Funding 1 share and a corresponding decrease in the seller share;
- (ii) acquire part of the seller share (such payment to be made to the seller), which will result in a corresponding decrease of the seller share and a corresponding increase in the Funding 1 share;
- (iii) fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any); and/or
- (iv) make a payment to the issuing entity to refinance an existing loan tranche (which may be another rated loan tranche or a subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of a new intercompany loan.

Funding 1 will use the proceeds of subordinated loan tranches received from time to time from the issuing entity under the intercompany loan agreement to:

- (i) pay the seller part of the consideration for loans (together with their related security) sold by the seller to the mortgages trustee, which will result in an increase in the Funding 1 share and a corresponding decrease in the seller share;
- (ii) acquire part of the seller share (such payment to be made to the seller), which will result in a corresponding decrease of the seller share and a corresponding increase in the Funding 1 share;
- (iii) fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any); and/or
- (iv) make a payment to the issuing entity to refinance an existing loan tranche (which may be a rated loan tranche or another subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of a new intercompany loan.

Funding 1 will use the proceeds of start-up loan tranches for establishing (or, as applicable, increasing) the Funding 1 general reserve fund on the relevant closing date and/or for meeting the costs and expenses incurred by Funding 1 in connection with any purchase price and related sale of loans and their related security to the mortgages trustee or the acquisition of part of the seller share on the relevant closing date and the fees payable under the intercompany loan agreement which relate to the costs of the series and classes of notes issued on the relevant closing date and/or to contribute towards Funding 1 available revenue receipts on the interest payment date immediately following the relevant closing date.

- (5) Funding 1 will use a portion of the amounts received from its share in the trust property to meet its obligations to pay interest and principal due to the issuing entity under the intercompany loan agreement and to replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any). Funding 1's obligations to the issuing entity under the intercompany loan agreement (among others) are secured under the Funding 1 deed of charge entered into on the programme date by Funding 1 with, among others, the Funding 1 security trustee and the issuing entity by, among other things, the Funding 1 share.
- (6) The issuing entity's obligations to pay principal and interest on the notes will be funded primarily from the payments of principal and interest received by it from Funding 1 under the intercompany loan agreement. The issuing entity's primary assets are its rights under the intercompany loan agreement and the Funding 1 deed of charge. Neither the issuing entity nor the noteholders have any direct interest in the trust property, although the issuing entity shares in the benefit of the Funding 1 security trustee's security interest in the Funding 1 share under the Funding 1 deed of charge. Prior to service of a note acceleration notice, the issuing entity will only repay a class of notes (or part thereof) of any series on the relevant interest payment date if it has received principal repayments in respect of the loan tranche that was funded by the issue of such notes. The issuing entity will only receive a principal repayment in respect of such loan tranche if certain repayment tests are satisfied (as to which, see "**Repayment of loan tranches before a trigger event and before intercompany**

**loan acceleration or acceleration of all notes**”). Following service of a note acceleration notice, the issuing entity will apply amounts received by it from Funding 1 under the intercompany loan agreement to repay all classes of outstanding notes of all series.

- (7) The issuing entity will issue notes in one or more series and/or classes from time to time. Each issue will be subject to the condition that the issuing entity has obtained written confirmation from each rating agency that the then current ratings of all outstanding notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified because of such issue.

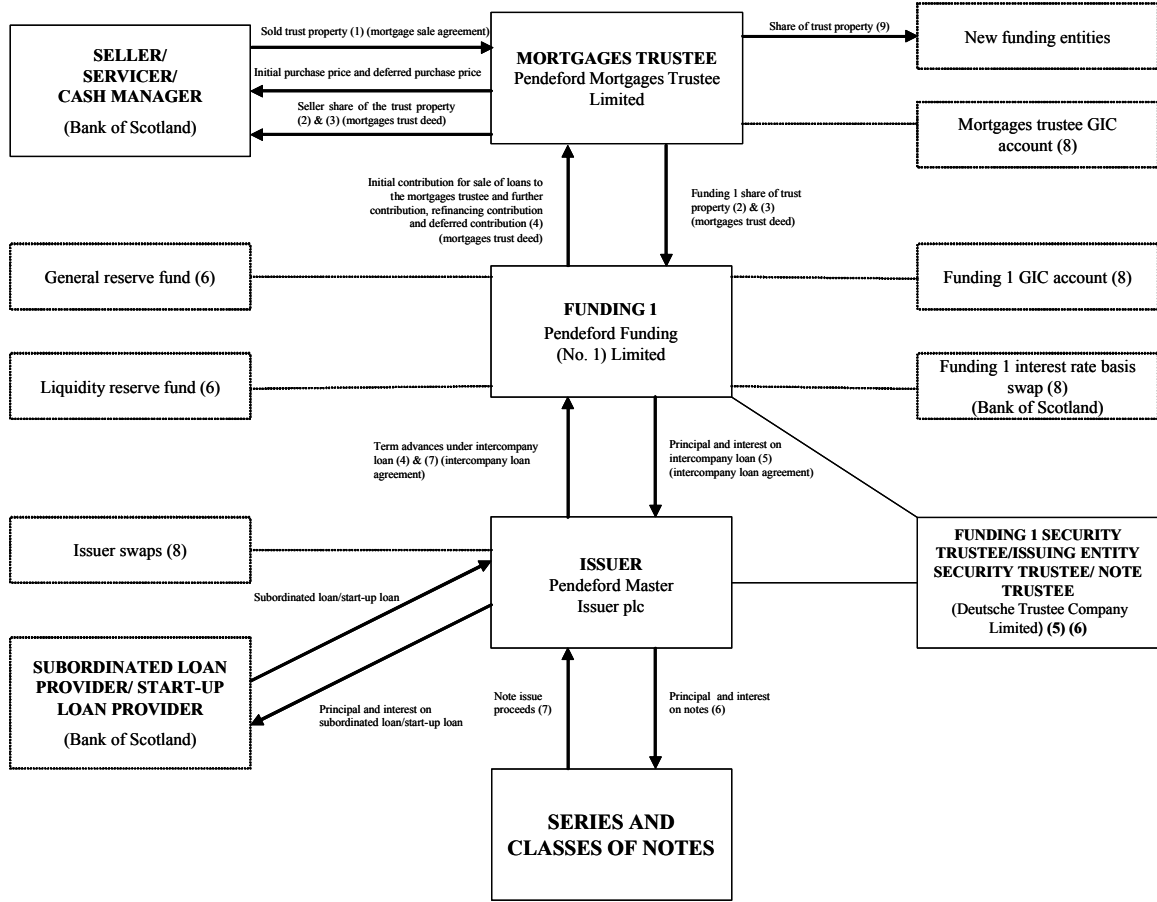
Each series will consist of one or more classes of notes and may be offered under this base prospectus and the applicable final terms setting out the terms of that series and those classes of notes. The issuing entity's obligations under, among other things, the notes are and will be secured under the issuing entity deed of charge entered into by the issuing entity with, among others, the issuing entity security trustee and the note trustee by, among other things, the issuing entity's rights under the intercompany loan agreement and the Funding 1 deed of charge.

- (8) The accounts, the reserve funds and the swap transactions and their function in the programme structure are described later in this base prospectus and in the applicable final terms. They are included in the first diagram below so that investors can refer back to see where they fit into the structure.

- (9) New issuing entities may in the future, in connection with Funding 1 or any new funding beneficiary, issue new notes from time to time and on-lend the proceeds thereof under a new intercompany loan agreement and Funding 1 or any such new funding beneficiary, as the case may be, may apply the proceeds of such new intercompany loan to acquire an interest in the trust property. Thus, the new notes issued by any such new issuing entity will be indirectly secured by the same trust property as the notes offered under this prospectus and the applicable final terms. See “**Risk factors – Holdings may establish other companies, each of which may become an additional beneficiary under the mortgages trust**” below.

- (10) Other legal entities within the HBOS group may in the future sell loans to the mortgages trustee, subject to satisfaction of the conditions precedent to the sale of new loans to the mortgages trustee and confirmation from each of the rating agencies that its then current rating of the notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result thereof.

# Structural diagram of the programme





## Diagram of ownership structure of special purpose vehicles

This diagram illustrates the ownership structure of the principal special purpose entities in respect of the programme, as follows:

- Each of Funding 1, the issuing entity and the post-enforcement call option holder is a wholly-owned subsidiary of Pendeford Holdings Limited (**Holdings**). See “**Funding 1**” and “**The issuing entity**” below.
- The entire issued share capital of Holdings is held on trust by a professional trust company, not affiliated with the seller, under the terms of a discretionary trust for, whilst monies remain due under the notes, the benefit of one or more charities. See “**Holdings**” below.
- The entire issued share capital of the mortgages trustee is held beneficially on trust by another professional trust company, not affiliated with the seller, under the terms of a discretionary trust for the benefit of one or more charities. See “**The mortgages trustee**” below.
- Bank of Scotland, which organises and initiates each issuance of notes under the programme and/or the advance of any subordinated loan and/or start-up loan, has no ownership interest in the issuer, Funding 1 or the mortgages trustee. As a result, no issuance of notes under the programme will be directly linked to the credit of Bank of Scotland, and Bank of Scotland has no obligation to support such transaction financially, although Bank of Scotland may still have a connection with such transaction for other reasons (such as acting as servicer of the loans and as a beneficiary under the **mortgages trust**). See “**Bank of Scotland plc**” below.
- It is expected that any new issuing entities or new funding beneficiaries would, if established, be fully owned subsidiaries of Holdings.
- In certain circumstances (including when new issuing entities are established in connection with Funding 1, when an entity becomes a new funding beneficiary of the mortgages trust, when new series and classes of notes are issued and when loans originated under a different brand within the HBOS group or by a different entity within the HBOS group are sold to the mortgages trustee), the Funding 1 security trustee and/or the issuing entity security trustee may, subject to certain conditions being satisfied, consent to modifications to be made to some of the transaction documents without obtaining your consent. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree modifications to the transaction documents without your prior consent, which may adversely affect your interests**” below.

## The key parties

### Issuing entity

Pendeford Master Issuer plc is a public limited company incorporated in England and Wales, referred to in this base prospectus as the **issuing entity**. Its registered office is 35 Great St. Helen's, London EC3A 6AP, United Kingdom. Its telephone number is +44 (0)20 7398 6300. The issuing entity is a new special purpose company created at the direction of Halifax. The issuing entity has issued and will issue the notes and has borrowed and will borrow subordinated loans and start-up loans and has lent and will lend the gross proceeds of such to Funding 1. See "**The issuing entity**" below.

### Funding 1

Pendeford Funding (No. 1) Limited is a private limited company incorporated in England and Wales, referred to in this base prospectus as **Funding 1**. Its registered office is 35 Great St. Helen's, London EC3A 6AP, United Kingdom. Its telephone number is +44 (0)20 7398 6300. From time to time, Funding 1 will borrow money from the issuing entity pursuant to the terms of the intercompany loan agreement and apply it, among other things, to increase the Funding 1 share, as described under "**Overview of base prospectus**" above. New funding beneficiaries may also acquire a share in the future. See also "**Funding 1**" below.

### The mortgages trustee

Pendeford Mortgages Trustee Limited is a private limited company incorporated in Jersey, Channel Islands, referred to in this base prospectus as the **mortgages trustee**. The purpose of the mortgages trustee is to acquire from time to time additional trust property from the seller and to hold all of the trust property on trust for the seller and Funding 1 and, if applicable, any new funding beneficiary of the mortgages trust. See "**The mortgages trust**" below.

### The seller, the servicer, the Funding 1 swap provider, the cash manager, the issuing entity cash manager, the issuing entity subordinated loan provider and the issuing entity start-up loan provider

Bank of Scotland is a bank incorporated in Scotland as a public limited company. **Birmingham Midshires** is a brand under which Halifax originated and Bank of Scotland originates loans. See "**Bank of Scotland plc**" below.

All of the loans in the initial portfolio and each new portfolio have been originated under the Birmingham Midshires brand. The seller sold such loans to the mortgages trustee on the programme date and on subsequent dates and will from time to time sell additional loans originated by it under the Birmingham Midshires brand to the mortgages trustee under the mortgage sale agreement. See "**Sale of the loans and their related security**" below.

From time to time, any other member of the HBOS group may accede to the mortgage sale agreement and sell loans to the mortgages trustee (each such entity, a **new seller**).

Although the seller has sold and will sell the loans to the mortgages trustee, the seller will continue to have an interest in the loans as one of the beneficiaries of the mortgages trust under the mortgages trust deed. See "**The mortgages trust – Seller share of trust property**" below. Halifax was appointed as, and since the reorganisation date, Bank of Scotland has been, the **servicer**, who performs administration and servicing functions in respect of the loans on behalf of the mortgages trustee and the beneficiaries of the mortgages trust, including collecting payments under the loans and taking steps to recover arrears. Bank of Scotland may not resign as servicer unless a successor servicer has been appointed. In addition, Bank of Scotland may be replaced by a successor servicer if it defaults in its obligations under the servicing agreement or an insolvency event occurs in relation to the servicer. See "**The servicer**" and "**The servicing agreement**" below.

Halifax was, and since the reorganisation date, Bank of Scotland has been the **Funding 1 swap provider** as described under "**The swap agreements – The Funding 1 swap**" below.

Halifax was appointed, on the programme date, as, and since the reorganisation date, Bank of Scotland has been, the **cash manager** for the mortgages trustee and Funding 1 to manage their bank accounts, determine the amounts of and arrange payments of monies to be made by them and keep certain records on their behalf. See "**Cash management for the mortgages trustee and Funding 1**" below.

Halifax plc was also appointed as, and since the reorganisation date, Bank of Scotland has been, the **issuing entity cash manager** to manage the issuing entity's bank accounts, determine the amounts of and arrange payments of monies to be made by the issuing entity and keep certain records on the issuing entity's behalf. See "**Cash management for the issuing entity**" below.

Bank of Scotland may also, from time to time, as the **issuing entity subordinated loan provider**, provide issuing entity subordinated loans to the issuing entity, the proceeds of which will be advanced by the issuing entity to Funding 1 as subordinated loan tranches under the intercompany loan agreement and used by Funding 1 as described in “**Overview of base prospectus**” above.

The issuing entity may also enter into new issuing entity subordinated loan agreements with parties other than Bank of Scotland.

See “**Credit structure – issuing entity subordinated loan agreements**” below.

Bank of Scotland may also, on each closing date, as the **issuing entity start-up loan provider**, provide an issuing entity start-up loan to the issuing entity, the proceeds of which will be advanced by the issuing entity to Funding 1 as start-up loan tranches under the intercompany loan agreement and used by Funding 1 to increase the Funding 1 general reserve fund and/or pay certain costs and expenses of Funding 1 in connection with an issue of notes under the programme and/or contribute towards Funding 1 available revenue receipts on the interest payment date immediately following the relevant closing date. See “**Credit structure – issuing entity start-up loan agreement**” below.

The issuing entity may (in the future) also enter into new issuing entity start-up loan agreements with parties other than Bank of Scotland.

#### **The issuing entity account bank and the account bank**

Bank of Scotland was appointed, on the programme date, as the **issuing entity account bank** to provide banking services to the issuing entity and as the **account bank** to Funding 1 and the mortgages trustee to provide banking services to such entities. See “**Cash management for the issuing entity – The issuing entity’s bank accounts**” and “**The intercompany loan agreement – Funding 1’s bank accounts**” below.

#### **The issuing entity swap providers**

The issuing entity swap providers, if any, in respect of a particular issue of notes will be disclosed in the applicable final terms. See “**The swap agreements – The issuing entity swaps**” below.

#### **The note trustee, issuing entity security trustee and Funding 1 security trustee**

Deutsche Trustee Company Limited is the note trustee. Deutsche Bank Trust Company Americas acts as issuing entity security trustee and is the Funding 1 security trustee. The note trustee acts as trustee for the noteholders under the note trust deed. The issuing entity security trustee acts as trustee for the issuing entity secured creditors under the issuing entity deed of charge. The Funding 1 security trustee acts as trustee for the Funding 1 secured creditors under the Funding 1 deed of charge.

#### **The paying agents, agent bank, registrar and transfer agent**

Deutsche Bank AG, London Branch is the principal paying agent and the agent bank. Deutsche Bank Trust Company Americas is the US paying agent, the registrar, the transfer agent and the exchange agent. The paying agents makes payments on the notes to noteholders, the agent bank calculates the interest rate on the notes and the registrar maintains a register in respect of the notes.

## Overview of the notes

### Series

The issuing entity may from time to time issue class A notes, class B notes, class M notes, class C notes and class D notes in one or more series. Each series will consist of one or more classes of notes. One or more series and classes of notes may be issued at one time. The issuing entity may also issue, from time to time, new classes of notes, subordinated to the class D notes, without your consent (subject to each rating agency confirming that such issuance will not result in a reduction, withdrawal or (in the case of S&P and Moody's) qualification of its then current ratings of the notes then outstanding). Each series and class of notes will be secured over the same assets as all other series and classes of notes. The notes issued from time to time by the issuing entity will constitute direct, secured and unconditional obligations of the issuing entity.

The notes of a particular class, whether of the same or a different series, will not necessarily have all the same terms. Differences may include issue price, principal amount, interest rates and interest rate calculations, currency, permitted redemption dates and final maturity dates. Noteholders holding certain notes may have the benefit of money market note purchase agreements, remarketing arrangements, 2a-7 swap provider arrangements or similar arrangements. The terms of each series and class of notes will be set out in the applicable final terms.

### Payment

Some series of notes will be paid ahead of others, regardless of the class designation of the notes. In particular, some payments on some series of class B notes, class M notes, class C notes and class D notes will be paid before some series of class A notes, as described in “– **Payment and ranking of the notes**” and “– **Diagram of the priority of payments by the issuing entity and subordination relationships**” below. See also “**Cashflows**” below.

In addition, the occurrence of an asset trigger event or non-asset trigger event (which are described below under “– **Trigger events**” below) will alter the payments on the notes.

### Issuance

Notes may only be issued on a closing date if the issuing entity obtains written confirmation from each of the rating agencies that its then current ratings of the outstanding notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified because of such issue.

There are no other restrictions on the issuance of any notes so long as this condition is met.

### Ratings

The ratings assigned to each class of notes will be specified in the applicable final terms.

A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation if, in its judgment, circumstances (including, without limitation, a reduction in the credit rating of the Funding 1 swap provider and/or any issuing entity swap provider (or, where relevant, the credit support provider with respect to the Funding 1 swap provider or any issuing entity swap provider), the mortgages trustee GIC provider and/or the Funding 1 GIC provider) in the future so warrant.

The term **rating agencies**, as used in this base prospectus, means Fitch, Moody's and Standard & Poor's, together with any further or replacement rating agency appointed by the issuing entity with the approval of the note trustee to give a credit rating to any series and class of notes.

Unless specified otherwise in the applicable final terms, the ratings assigned by Fitch and Standard & Poor's to each series and class of notes will address the likelihood of full and timely payment to you of all payments of interest in accordance with the conditions and also the likelihood of ultimate payment of principal on the final maturity date of those notes. Unless specified otherwise in the applicable final terms, the ratings assigned by Moody's to each series and class of notes will address the expected loss in proportion to the initial principal amount of these notes posed to investors by the final maturity date. In Moody's opinion, the structure allows for timely payment of interest and principal at par on or before the final maturity date. The ratings will not address the actual likely rate of prepayments on the loans. The rate of prepayments, if different than originally anticipated, could adversely affect the yield realised on your notes.

Assignment of the expected ratings to each series and class of the notes will be a condition to issue of those notes. No series and class of notes will be issued which does not have a credit rating.

The issuing entity has agreed to pay ongoing surveillance fees to the rating agencies, in exchange for which each rating agency will monitor the ratings it has assigned to each series and class of notes while they are outstanding.

### **Listing**

Application will be made to the UK Listing Authority for notes issued during the period of 12 months from the date of this base prospectus to be admitted to the official list maintained by the UK Listing Authority. Application will also be made to the London Stock Exchange for such notes to be admitted to trading on the London Stock Exchange's Regulated Market.

### **Denominations of the notes**

The notes (in either global or definitive form) will be issued in such denominations as specified in the applicable final terms, save that the minimum denomination of each note will be such as may be allowed or required from time to time by the relevant central bank or regulatory authority (or equivalent body) or any laws or regulations applicable to the relevant currency and save that the minimum denomination of each US dollar denominated note will be \$100,000 and in integral multiples of \$1,000 in excess thereof, each euro denominated issuing entity note will be issued in minimum denominations of €50,000 and in integral multiples of €1,000 in excess thereof, up to and including €99,000 and each sterling-denominated note will be issued in minimum denominations of £50,000 and in integral multiples of £1,000 in excess thereof, up to and including £99,000 provided that sterling-denominated notes issued with a maturity of less than 366 days will be issued in minimum denominations of £100,000 and in integral multiples of £1,000 in excess thereof. No note will be issued in a denomination of less than €50,000 (or its equivalent in the relevant currency).

### **Maturities**

Notes will be issued in such maturities as may be specified in the applicable final terms, subject to compliance with all applicable legal, regulatory and/or central bank requirements.

### **Currencies**

Subject to compliance with all applicable legal, regulatory and/or central bank requirements, a series and class of notes may be denominated in such currency or currencies as may be agreed between the relevant dealer and/or managers and the issuing entity as specified in the applicable final terms.

### **Issue price**

Each series and class of notes may be issued on a fully paid basis and at an issue price which is at par or at discount from, or premium over, par.

### **Selling restrictions**

For a description of certain restrictions on offers, sales and deliveries of notes and on the distribution of offering material in the United States of America, the United Kingdom and certain other jurisdictions see "**Subscription and Sale**" below and in the applicable final terms.

### **Relationship between the notes, issuing entity subordinated loans and issuing entity start-up loans and the intercompany loan**

The intercompany loan agreement will comprise multiple rated loan tranches, subordinated loan tranches and start-up loan tranches. The gross proceeds of each issue of a series and class of notes will fund a single rated loan tranche under the intercompany loan agreement. The repayment terms of each rated loan tranche (for example, dates for payment of principal and the type of amortisation or redemption) will reflect the terms of the related series and class of notes. Subject to the applicable Funding 1 priority of payments and issuing entity priority of payments, the issuing entity will repay each series and class of notes from payments received by it from Funding 1 under the corresponding rated loan tranche and, in each case where the relevant series and class of notes is denominated in a currency other than sterling or otherwise benefits from an issuing entity swap agreement, after making the appropriate currency exchange or such other applicable exchange under the corresponding issuing entity swap agreement.

The repayment terms of each subordinated loan tranche (for example, dates for payment of principal and interest) will reflect the terms of the related issuing entity subordinated loan. Subject to the applicable Funding 1 priority of payments and issuing entity priority of payments, the issuing entity will repay each issuing entity subordinated loan from payments received by it from Funding 1 under the corresponding subordinated loan tranche.

The repayment terms of each start-up loan tranche (for example, dates for payment of principal and interest) will reflect the terms of the related issuing entity start-up loan. Subject to the applicable Funding 1 priority of payments and issuing entity priority of payments, the issuing entity will repay each issuing entity start-up loan from payments received by it from Funding 1 under the corresponding start-up loan tranche.

The ability of Funding 1 to make payments on the intercompany loan will depend to a large extent on Funding 1 receiving its share of collections on the trust property, which will in turn depend principally on the collections the mortgages trustee receives on the loans and the related security and the allocation of monies among the seller and Funding 1 under the mortgages trust. For more information on the intercompany loan, see “**The intercompany loan agreement**” below.

#### **Payment and ranking of the notes**

Payments of interest and principal on the class A notes of any series due and payable on an interest payment date will rank ahead of payments of interest and principal on the class B notes of any series, the class M notes of any series, the class C notes of any series and the class D notes of any series (in each case due and payable on such interest payment date). Payments of interest and principal on the class B notes of any series due and payable on an interest payment date will rank ahead of payments of interest and principal on the class M notes of any series, the class C notes of any series and the class D notes of any series (in each case due and payable on such interest payment date). Payments of interest and principal on the class M notes of any series due and payable on an interest payment date will rank ahead of payments of interest and principal on the class C notes of any series and the class D notes of any series (in each case due and payable on such interest payment date). Payments of interest and principal on the class C notes of any series due and payable on an interest payment date will rank ahead of payments of interest and principal on the class D notes of any series (due and payable on such interest payment date). For more information on the priority of payments, see “**Cashflows**” below and see also “**Risk factors – Subordination of other note classes, issuing entity subordinated loans and issuing entity start-up loans may not protect noteholders from all risk of loss**” below.

Payments of interest and principal on the class A notes of each series will rank equally (but subject to the interest payment dates, scheduled redemption dates and permitted redemption dates of each series of class A notes). Payments of interest and principal on the class B notes of each series will rank equally (but subject to the interest payment dates, scheduled redemption dates and permitted redemption dates of each series of class B notes). Payments of interest and principal on the class M notes of each series will rank equally (but subject to the interest payment dates, scheduled redemption dates and permitted redemption dates of each series of class M notes). Payments of interest and principal on the class C notes of each series will rank equally (but subject to the interest payment dates, scheduled redemption dates and permitted redemption dates of each series of class C notes). Payments of interest and principal on the class D notes of each series will rank equally (but subject to the interest payment dates, scheduled redemption dates and permitted redemption dates of each series of class D notes). The interest payment dates, scheduled redemption dates and permitted redemption dates for a series and class of notes will be specified in the applicable final terms.

Investors should note that subject as further described under “**Cashflows**” below:

- Notes of different series and classes are intended to receive payment of interest and principal at different times. Therefore, lower ranking classes of notes of one series may be paid interest and principal before higher ranking classes of notes of a different series.
- If there is a debit balance on a subordinate ranking principal deficiency sub-ledger (other than the subordinated loan principal deficiency ledger) or the adjusted Funding 1 general reserve fund is less than the Funding 1 general reserve fund threshold or arrears in respect of loans in the mortgages trust exceed a specified amount (each as described below under “**Cashflows**” below) and there is a more senior loan tranche outstanding, no amount of principal will be repayable in respect of a subordinate ranking loan tranche until such situation is cured. The failure to repay principal in respect of such loan tranche on the applicable redemption dates for such reason will not constitute an event of default in respect of such loan tranche.
- To the extent required, but subject to certain limits and conditions, Funding 1 may apply amounts standing to the credit of the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any) in payment of, among other things, amounts due to the issuing entity in respect of the rated loan tranches.

- Prior to service of a note acceleration notice, a series and class of notes will be redeemed on a scheduled redemption date or permitted redemption date only and to the extent of the amount (if any) repaid on the corresponding rated loan tranche in respect of such date.
- If not redeemed earlier, each series and class of notes will be redeemed by the issuing entity on the final maturity date specified in the applicable final terms. The failure to redeem a series and class of notes on its final maturity date will constitute a note event of default in respect of such notes.
- Following a trigger event or service of an intercompany loan acceleration notice or a note acceleration notice, the priority of payments will change and the issuing entity will make payments of interest and principal in accordance with and subject to the relevant issuing entity priority of payments as described below under “**Cashflows**” below.

### **Interest**

Interest will accrue on each series and class of notes from its date of issuance at the applicable interest rate specified in the applicable final terms for that series and class of notes, which may be fixed or floating rate or have a combination of these characteristics. Interest on each series and class of notes will be due and payable on the interest payment dates specified in the applicable final terms.

Any shortfall in payments of interest due on any series of the class B notes (to the extent that any class A notes are outstanding), the class M notes (to the extent that any class A notes and/or class B notes are outstanding), the class C notes (to the extent that any class A notes and/or class B notes and/or class M notes are outstanding) and the class D notes (to the extent that any class A notes and/or class B notes and/or class M notes and/or class C notes are outstanding) on any interest payment date in respect of such notes will be deferred until the immediately succeeding interest payment date in respect of such notes. On that immediately succeeding interest payment date, the amount of interest due on the relevant class of notes will be increased to take account of any deferred interest. If on that interest payment date there is still a shortfall, that shortfall will be deferred again. This deferral process will continue until the final maturity date of the notes, at which point all such deferred amounts will become due and payable. However, if there is insufficient money available to the issuing entity to pay interest on the class B notes, the class M notes, the class C notes or the class D notes, then noteholders may not receive all interest amounts payable on those classes of notes. Payments of interest due on any interest payment date in respect of the most senior class of notes then outstanding may not be deferred and the failure to pay interest on such notes will be a note event of default.

### **Fixed rate notes**

For a series and class of fixed rate notes, interest will be payable at the fixed rate and on such interest payment dates specified in the applicable final terms and will be calculated on the basis of such day count fraction as is specified in the applicable final terms.

### **Floating rate notes**

A series and class of floating rate notes will bear interest in each case on the basis specified in the applicable final terms. The margin, if any, relating to such series and class of notes will be specified in the applicable final terms. Interest on floating rate notes in respect of each interest period will be payable on such interest payment dates and will be calculated on the basis of such day count fraction as specified in the applicable final terms.

### **Zero coupon notes**

A series and class of zero coupon notes may be offered and sold at a discount to their nominal amount as specified in the applicable final terms (**zero coupon notes**).

### **Bullet redemption notes**

A series and class of bullet redemption notes will be redeemable in full on the bullet redemption date specified in the applicable final terms. Funding 1 will seek to accumulate funds relating to principal payments on each bullet loan tranche over a period of time in order to repay such funds as a lump sum payment to the issuing entity so that the issuing entity can redeem the corresponding bullet redemption notes in full on the relevant bullet redemption date. A cash accumulation period in respect of a bullet loan tranche is generally the period of time estimated to be the number of months prior to the relevant Funding 1 interest payment date necessary for Funding 1 to accumulate enough principal receipts derived from its share of the trust property to repay that bullet loan tranche to the issuing entity in full on the relevant scheduled repayment date. The cash accumulation period will

be determined according to a formula described under “**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**” below. To the extent that there are insufficient funds to redeem a series and class of bullet redemption notes on the relevant bullet redemption date, then the issuing entity will be required to pay the shortfall, to the extent it receives funds therefor, on subsequent interest payment dates in respect of such notes. No assurance can be given that Funding 1 will accumulate sufficient funds during the cash accumulation period relating to any bullet loan tranche to enable it to repay such loan tranche on its scheduled repayment date to the issuing entity so that the issuing entity is able to repay principal of the related bullet redemption notes on their bullet redemption date.

Following the earlier to occur of a pass-through trigger event and the step-up date (if any) in relation to a series and class of bullet redemption notes, such notes will be deemed to be pass-through notes and the issuing entity will repay such notes to the extent that funds are available for such purpose and subject to the conditions regarding repayment on subsequent interest payment dates.

### **Scheduled redemption notes**

A series and class of scheduled redemption notes will be redeemable on scheduled redemption dates in two or more scheduled amortisation instalments, the dates and amounts of which will be specified in the applicable final terms. Prior to each scheduled repayment date with respect to the corresponding loan tranches, Funding 1 will seek to accumulate sufficient funds so that it may repay the issuing entity each scheduled amortisation instalment on its scheduled redemption date so that the issuing entity is able to repay principal of the related series and class of scheduled redemption notes on their scheduled redemption date. A cash accumulation period in respect of a scheduled amortisation instalment is the period of time estimated to be the number of months prior to the relevant Funding 1 interest payment date necessary for Funding 1 to accumulate enough principal receipts derived from its share of the trust property to repay that scheduled amortisation instalment to the issuing entity on its scheduled repayment date. The cash accumulation period will be determined according to a formula described under “**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**” below. To the extent there are insufficient funds on a scheduled repayment date for Funding 1 to repay the issuing entity the relevant scheduled amortisation instalment, then the issuing entity will be required to pay the shortfall in respect of the related series and class of scheduled redemption notes, to the extent it receives funds therefor, on subsequent interest payment dates in respect of such notes. No assurance can be given that Funding 1 will accumulate sufficient funds during the cash accumulation period relating to any scheduled amortisation instalment to enable it to repay the relevant scheduled amortisation instalment on its scheduled repayment date to the issuing entity so that the issuing entity is able to repay principal of the related series of scheduled redemption notes on their scheduled redemption date.

Following the earlier to occur of a pass-through trigger event and the step-up date (if any) in relation to a series and class of scheduled redemption notes, such notes will be deemed to be pass-through notes and the issuing entity will repay such notes to the extent that funds are available for such purpose and subject to the conditions regarding repayment on subsequent interest payment dates.

### **Pass-through notes**

A series and class of pass-through notes will be redeemable in full on the final maturity date specified in the applicable final terms. On each Funding 1 interest payment date, Funding 1 may (subject to the repayment tests) make repayments of principal in respect of pass-through loan tranches to the issuing entity so that the issuing entity may, on the applicable interest payment date, repay all or part of the pass-through notes prior to their final maturity dates.

Following the earlier to occur of a pass-through trigger event and the step-up date (if any) in relation to a series and class of notes, the issuing entity will repay such notes to the extent that funds are available and subject to the conditions for repayment on subsequent interest payment dates.

### **Money market notes**

From time to time, the issuing entity may issue a series and class of Rule 144A notes designated as **money market notes** in the applicable final terms. Money market notes will be **Eligible Securities** within the meaning of Rule 2a-7 under the United States Investment Company Act of 1940, as amended (the **Investment Company Act**).

However, any determination as to qualification and compliance with other aspects of Rule 2a-7 is solely the responsibility of each money market fund and its investment adviser, and no representation as to such compliance is made by any of the issuing entity, Funding 1, the mortgages trustee, Bank of Scotland, the dealers, the managers, the note trustee, the issuing entity security trustee, the Funding 1 security trustee, the corporate services provider, the Funding 1 swap provider, the issuing entity swap providers, any swap guarantors (as



applicable), the paying agents, the account bank, the issuing entity account bank, any money market note purchaser, any remarketing agent or any conditional purchaser and no assurance can be given in this regard.

Money market notes will generally be bullet redemption notes or scheduled redemption notes, the final maturity date of which will be less than 397 calendar days from the trade date relating to such notes, being the date on which investors contract to purchase them.

The issuing entity may also repay certain series and classes of money market notes prior to their final maturity dates using amounts received from a third party that has agreed to purchase those notes pursuant to the terms of a money market note purchase agreement. If such arrangements apply to any money market notes, the applicable final terms will, in addition to providing information regarding a series and class of money market notes, identify any money market note purchaser in respect of such money market notes and the terms of the applicable money market note purchase agreement.

Money market notes designated as remarketable notes in the relevant final terms will be issued subject to the mandatory transfer arrangements referred to in Condition 5.8, the remarketing agreement (as defined below) and the note trust deed (the **mandatory transfer**). Under the terms of the mandatory transfer, the issuing entity will procure the purchase of the remarketable notes on the interest payment date specified in the relevant final terms as the initial mandatory transfer date and on each anniversary thereafter (subject to adjustment for non-business days and subject to the mandatory transfer termination event (as defined below) not having occurred) (each such date being a **mandatory transfer date**) until the final maturity or earlier redemption in full of such remarketable notes. Upon payment of the principal amount outstanding on such remarketable notes on the relevant mandatory transfer date (following the application of note principal payments on that date) (the **mandatory transfer price**), all rights in respect of such remarketable notes will be transferred to or for the account of the remarketing agent (as defined below) or as designated by the remarketing agent.

Under the terms of the relevant remarketing agreement, the issuing entity will appoint the remarketing agent specified in the applicable final terms (the **remarketing agent**) to act as its agent to use reasonable efforts to identify third party purchasers for the relevant remarketable notes on each mandatory transfer date prior to the occurrence of a mandatory transfer termination event. If the remarketing agent is unable to identify third party purchasers for all such remarketable notes then outstanding, then the remarketing agent on behalf of the issuing entity will give notice to the conditional purchaser specified in the relevant final terms (the **conditional purchaser**) under an agreement (the **conditional purchase agreement**) to purchase all such remarketable notes. The obligation of the conditional purchaser to purchase such remarketable notes may be subject to limitations on the conditional purchaser's ability to fund its obligations (see "**Risk Factors – Risks related to money market notes**" below) and to certain termination events under the conditional purchase agreement. If a remarketing termination event (as defined below), other than a note event of default, occurs on or before the relevant mandatory transfer date, the conditional purchaser will be obliged to purchase all the relevant remarketable notes on such mandatory transfer date.

The remarketing agent will have the ability to increase or decrease the margin on the remarketable notes from that payable as at the closing date of the relevant remarketable notes on each mandatory transfer date in accordance with the remarketing agreement. Any increase in margin on the remarketable notes may not exceed an amount specified in the relevant final terms as the maximum reset margin. As from the occurrence of a remarketing termination event, the margin applicable to such remarketable notes will equal the maximum reset margin.

The issuing entity may also have the benefit of a 2a-7 swap provider arrangement under which a swap provider (the **2a-7 swap provider**) will be required to make a principal payment under the relevant issuing entity swap agreement to the issuing entity to enable the issuing entity to redeem a series and class of notes in full on their bullet repayment date notwithstanding that it has not received the corresponding principal payment required to be made by the issuing entity under the relevant issuing entity swap agreement. The obligation of the 2a-7 swap provider to make such a payment to the issuing entity may be subject to certain termination events under the relevant issuing entity swap agreement. A failure by the issuing entity to make the full principal repayment on the bullet repayment date of the loan tranche corresponding to the relevant series and class of notes for which the relevant issuing entity swap was entered into will not constitute an event of default or a termination event under the relevant issuing entity swap agreement. If such arrangements apply to any money market notes, the applicable final terms will, in addition to providing information regarding a series and class of money market notes, identify any 2a-7 swap provider in respect of such money market notes and the terms of the applicable issuing entity swap agreement.

Certain risks relating to repayment of remarketable notes and money market notes by means of a money market note purchaser or 2a-7 swap provider are described under "**Risk factors – Risks related to money market notes**".

## Redemption and repayment

If not redeemed earlier, each series and class of notes will be redeemed by the issuing entity on the final maturity date specified for such series and class of notes in the applicable final terms.

For more information on the redemption of the notes, see “**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**” and “**Cashflows**” below. See also “**– Payment and ranking of the notes**” above.

## Optional redemption or repurchase of the notes

The issuing entity may redeem all, but not a portion, of a series and class of notes at their redemption amount, together with any accrued interest in respect thereof, by giving notice in accordance with the terms and conditions of the notes, subject to the detailed conditions set out in the terms and conditions (including the availability of sufficient funds) in the following circumstances:

- if at any time it would become unlawful for the issuing entity to make, fund or to allow to remain outstanding the rated loan tranche which was funded by such notes and the issuing entity requires Funding 1 to prepay such rated loan tranche on a Funding 1 interest payment date, subject to and in accordance with the terms of the intercompany loan agreement, to the extent necessary to cure such illegality (see Condition 5.5); or
- on any interest payment date in the event that the issuing entity would, by virtue of a change in the law or regulations of the United Kingdom or any other jurisdiction (or the application of interpretation thereof), be required to deduct or withhold from any payment of principal or interest or any other amount under such series and class of notes, or Funding 1 would be required to deduct or withhold from amounts due under the rated loan tranche which was funded by such notes, any amount for or on account of any present and future taxes, duties, assessments or governmental charges of whatever nature (see Condition 5.5); or
- on any interest payment date after the issuing entity or Funding 1, as the case may be, has ceased or will cease to fall within the permanent regime for the taxation of securitisation companies established pursuant to the Finance Act 2005 and the regulations made thereunder (in each case as amended from time to time) (the **securitisation tax regime**) (see Condition 5.5).

In addition, provided a note acceleration notice has not been served, the issuing entity may redeem a series and class of notes outstanding in accordance with the terms and conditions of such notes:

- if a call option date is specified in the applicable final terms in relation to such series and class of notes, on such call option date and on any interest payment date thereafter (see Condition 5.4);
- if a step-up date is specified in the applicable final terms in relation to such series and class of notes, on such step-up date and on any interest payment date thereafter (see Condition 5.4); or
- on any interest payment date on which the aggregate principal amount of such series and class of notes and all other classes of notes of the same series is less than 10 per cent. of the aggregate principal amount outstanding of such series of notes as at the relevant closing date (see Condition 5.4).

## Post-enforcement call option

The noteholders are required, at the request of the post-enforcement call option holder, for a nominal consideration, to transfer or procure the transfer of all of the notes to the post-enforcement call option holder pursuant to the option granted to it by the note trustee (as agent for the noteholders) under the terms of the post-enforcement call option agreement. The post-enforcement call option may only be exercised following enforcement and realisation of the issuing entity security to the maximum extent possible (as certified by the issuing entity security trustee) and application of the proceeds of enforcement. See “**PECOH**” below.

## **Withholding tax**

Payments of interest and principal with respect to the notes will be made subject to any withholding or deduction for or on account of any taxes and neither the issuing entity nor any other person will be obliged to pay additional amounts in relation thereto. The applicability of any UK withholding tax is discussed under “**United Kingdom taxation**” below.

## **The programme date**

On 12 April 2007 (the **programme date**) the issuing entity and other principal parties to the programme and the related transactions entered into the transaction documents in relation to the programme.

## **Credit enhancement**

Subject to the detailed description and limitations set out in “**Credit structure**” below, each series and class of notes will have the benefit of the following credit enhancement or support:

- availability of excess portions of **Funding 1 available revenue receipts** (which consist of revenue receipts on the loans distributed by the mortgages trustee to Funding 1 and other amounts set out in “**Cashflows – Definition of Funding 1 available revenue receipts**” below) and of **Funding 1 principal receipts** (which consist of principal receipts on the loans distributed by the mortgages trustee to Funding 1);
- a reserve fund called the **Funding 1 general reserve fund** to be used in certain circumstances by Funding 1 to meet any deficit in revenue (provided that it shall not be available to make payments with respect to the subordinated loan tranches) or to repay certain amounts of principal in respect of the rated loan tranches;
- a reserve fund called the **Funding 1 liquidity reserve fund**, which will be established following a seller rating downgrade to meet interest and principal shortfalls in limited circumstances on the rated loan tranches;
- subordination of junior classes of notes; and
- subordination of issuing entity subordinated loans.

## **Swap agreements**

The notes also have the benefit of derivatives instruments, namely the Funding 1 swap provided by Halifax and since the reorganisation date Bank of Scotland, as the **Funding 1 swap provider**, and any issuing entity swaps in respect of the relevant series and class of notes, as specified in the applicable final terms. See “**The swap agreements**” below.

## **Funding 1 principal deficiency ledger**

A principal deficiency ledger has been established to record principal losses on the loans allocated to Funding 1 and the application of Funding 1 available principal receipts to meet any deficiency in Funding 1 available revenue receipts or to fund the Funding 1 liquidity reserve fund (if any).

The Funding 1 principal deficiency ledger will have six sub-ledgers which will correspond to each of the AAA loan tranches, the AA loan tranches, the A loan tranches, the BBB loan tranches, the BB loan tranches and the subordinated loan tranches, respectively. See “**Credit structure – Funding 1 principal deficiency ledger**” below.

## **Trigger events**

If an asset trigger event or non-asset trigger event should occur, then distributions on the notes may be altered, as described in “**Cashflows**” below.

An **asset trigger event** will occur when losses on the loans in the portfolio (after application of Funding 1 available principal receipts to meet deficiencies in Funding 1 available revenue receipts or to fund the Funding 1 liquidity reserve fund (if any)) reach a level causing an amount to be debited to the AAA principal deficiency sub-ledger, unless such debit is made when (a) the aggregate principal amount outstanding of each of the AA

loan tranches, the A loan tranches, the BBB loan tranches and the BB loan tranches is equal to zero and (b) the sum of the amount standing to the credit of the Funding 1 general reserve ledger, the Funding 1 liquidity reserve ledger (if any) and the Funding 1 revenue ledger together with amounts determined and due to be credited to the Funding 1 revenue ledger prior to the immediately following Funding 1 interest payment date after such debit is made is greater than the amount necessary to pay the items in paragraphs (A) to (F) of the Funding 1 pre-enforcement revenue priority of payments on the immediately following Funding 1 interest payment date after such debit is made.

A **non-asset trigger event** means the occurrence of any of the following on a calculation date: (a) an insolvency event in relation to the seller on or before that calculation date; (b) the seller's role as servicer under the servicing agreement has been terminated and a new servicer has not been appointed within 60 days; (c) as at the calculation date immediately preceding the relevant calculation date, the seller share of the trust property was less than the minimum seller share and this has not been remedied by the relevant calculation date; or (d) as at the calculation date immediately preceding the relevant calculation date, the aggregate outstanding principal balance of loans comprising the trust property was less than the required loan balance amount specified in the most recent final terms and this has not been remedied by the relevant calculation date. See "**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**" below.

A **trigger event** means an asset trigger event and/or a non-asset trigger event.

### **Acceleration and enforcement**

All notes will become immediately due and payable and the issuing entity security trustee will be entitled to enforce the issuing entity security on the service on the issuing entity by the note trustee of a note acceleration notice. The note trustee becomes entitled to serve a note acceleration notice at any time after the occurrence of a note event of default in respect of a class of notes and it shall do so (i) on the instructions of the holders of the applicable class of notes across all series (holding in aggregate at least one quarter in principal amount outstanding of such class of notes) or (ii) if directed to do so by an extraordinary resolution of the holders of the applicable class of notes across all series, provided that, in each case, all notes ranking in priority to such class of notes have been repaid in full.

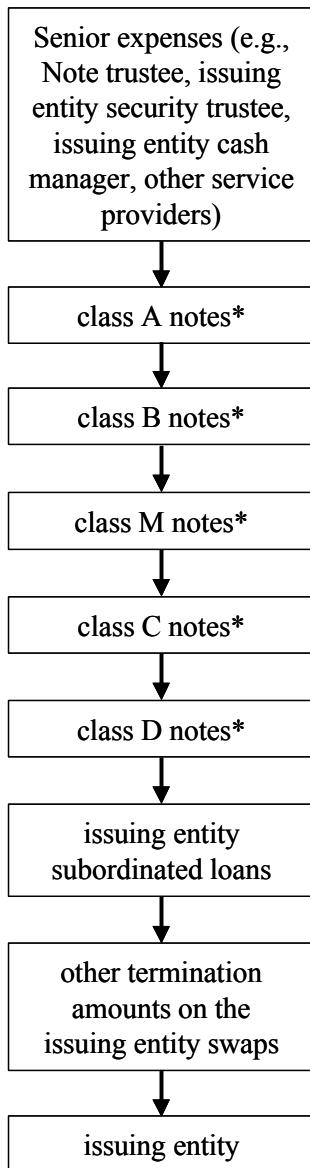
### **Operative documents relating to the notes**

The issuing entity will issue each series of notes under the note trust deed. The notes will also be subject to the paying agent and agent bank agreement. The security for the notes is provided for under the issuing entity deed of charge between the issuing entity, the issuing entity security trustee and the issuing entity's other secured creditors (excluding the noteholders). Operative legal provisions relating to the notes have been included in the note trust deed, the paying agent and agent bank agreement, the issuing entity deed of charge, the issuing entity cash management agreement and the notes themselves, each of which are governed by English law.

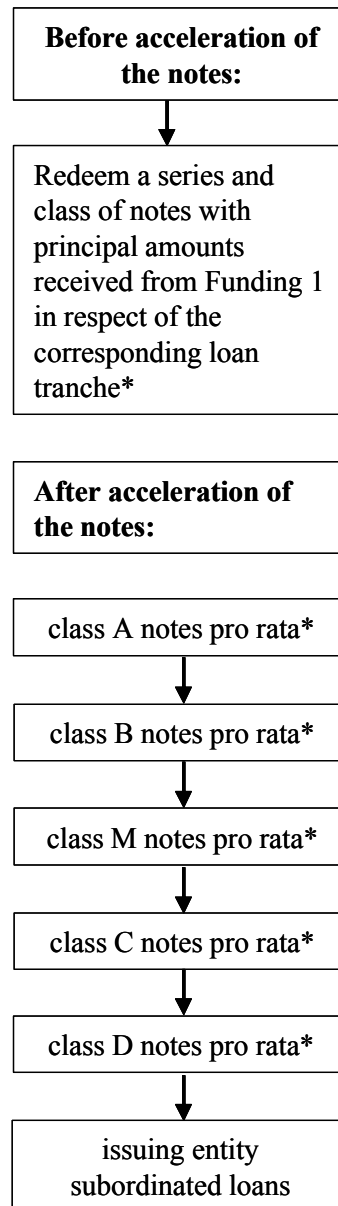
### **Diagram of the priority of payments by the issuing entity and subordination relationships**

The following diagram illustrates in a general way the payment priorities for receipts by the issuing entity representing revenue and principal before acceleration of the notes and also indicates the subordination relationship among the notes. For the sake of simplicity, the diagram omits material details relating to the priority of payments and does not indicate the priority of payments by Funding 1. You should refer to "**Cashflows**" below for a complete understanding of the priorities of payments by Funding 1 and the issuing entity in all circumstances.

### Revenue receipts



### Principal receipts



\* Includes interest and certain termination amounts or principal amounts (as applicable) payable to the issuing entity swap providers in respect of the issuing entity swaps. Amounts received by the issuing entity from such issuing entity swap providers under an issuing entity swap will be used to make payments of interest and principal on the corresponding series and class of notes.

The issuing entity may, in the future, issue new classes of notes, which will be subordinated to the class D notes, provided that the ratings of each class of notes at that time outstanding are not downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of such issue of a new class of notes and none of such ratings is lower than it was upon the date of issue of such outstanding notes.

## The loans

As at the date of this base prospectus, the loans comprising the portfolio from time to time have been and will be originated by Birmingham Midshires (although loans originated under other brands within the HBOS group may in the future be sold to the mortgages trustee, as described in “**Sale of loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**”). Each loan in the portfolio (and any drawings under flexible loans) is secured by either a first ranking legal charge over freehold or leasehold property located in England or Wales or a first ranking standard security over heritable or long leasehold property located in Scotland. The loans included in the portfolio consist of several different types with a variety of characteristics relating to, among other things, calculation of interest and repayment of principal and include or will include:

- loans which are subject to variable rates of interest set by reference to a standard variable rate of interest, which the seller determines based on general interest rates and competitive forces in the UK mortgage market from time to time, or a discount to such standard variable rate of interest;
- loans which track a variable rate of interest other than a variable rate set by the seller (currently this rate is the Bank of England repo rate); and
- loans which are subject to fixed rates of interest.

New loans sold to the mortgages trustee will be required to comply with specified criteria (see “**Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**”). Any new loans sold to the mortgages trustee will increase the total size of the trust property and will increase the Funding 1 share to the extent only that Funding 1 has paid consideration to the seller for the sale of new loans. To the extent that Funding 1 has not paid consideration to the seller for the sale of new loans, the seller share will increase by a corresponding amount.

See “**The loans – Characteristics of the loans**” below for a more detailed description of the loans offered by the seller and see the applicable final terms for statistical information on the portfolio.

No capped loans have been included in the portfolio, although such loans may be sold to the mortgages trustee in the future provided that the rating agencies confirm that the then current ratings of the notes will not be adversely affected.

All loans are originated in accordance with Birmingham Midshires’ lending criteria for mortgage loans applicable at the time of origination. Birmingham Midshires may from time to time change its lending criteria and any other terms applicable to new loans or their related security so that all new loans originated after the date of that change will be subject to the new lending criteria. Notwithstanding any change to the lending criteria or other terms applicable to the loans, the loans and their related security may only be sold to the mortgages trustee if those new loans comply with the seller’s warranties in the mortgage sale agreement. If a loan or its related security does not comply with these warranties, then the seller will have 20 London business days in which to cure the default, failing which it will at the direction of Funding 1 be required to repurchase the loan or loans under the relevant mortgage account and their related security from the mortgages trustee acting at the direction of Funding 1. See “**Sale of the loans and their related security – Repurchase of loans under a mortgage account**” below. Birmingham Midshires’ current lending criteria are described further in “**The loans – Lending criteria**” below.

## Sale of the loans

The seller sold an initial portfolio to the mortgages trustee on the programme date, subject to the terms of the mortgage sale agreement. The seller may sell new loans and their related security to the mortgages trustee from time to time in order to increase or maintain the size of the trust property. The seller may increase the size of the trust property from time to time in relation to an issuance of notes by the issuing entity or the advance of an issuing entity subordinated loan to it, the proceeds of which will be advanced by the issuing entity to Funding 1 under the intercompany loan agreement as described in “**Overview of base prospectus**” above and used by Funding 1 to pay the purchase price for the sale of the new loans and their related security to the mortgages trustee or to comply with the seller’s obligations under the mortgage sale agreement as described under “**Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**” below.

When new loans are sold to the mortgages trustee, the amount of the trust property will increase. Depending on the circumstances, the increase in the trust property may result in an increase in the seller share and/or the

Funding 1 share. For a description of how adjustments are made to the seller share and the Funding 1 share, see “**The mortgages trust**” below.

Some fees payable by the borrowers, such as early repayment fees, will be given back to the seller and not allocated in the same manner as the other receipts arising from the portfolio comprised in the trust property.

For more information on the mortgage sale agreement, see “**Sale of the loans and their related security**” below.

### **The mortgages trust**

The mortgages trustee holds the trust property on bare trust for the beneficiaries of the mortgages trust. As at the date of this base prospectus, the **beneficiaries** of the mortgages trust are Funding 1 and the seller only. Funding 1 and the seller each have a joint and undivided beneficial interest in the trust property. Payments of interest and principal arising from the loans in the portfolio are allocated to Funding 1 and the seller as described below according to their respective shares of the trust property, calculated periodically as described later in this section.

The trust property consists of the loans in the portfolio and their related security and any income generated by the loans or their related security. The trust property also includes any money in the mortgages trustee GIC account. The **mortgages trustee GIC account** is the bank account in which the mortgages trustee holds any cash that is part of the trust property until it is distributed to the beneficiaries.

Payments by borrowers and any recoveries made in respect of the loans in the portfolio are paid initially into an account (a **collection account**) in the name of the servicer and swept into the mortgages trustee GIC account on a regular basis but in any event, in the case of direct debits, no later than the next London business day after they are deposited in the collection account.

In addition, drawings under flexible loans and any new loans and their related security that the seller sells to the mortgages trustee after the programme date will be part of the trust property, unless they are repurchased by the seller. The seller will be solely responsible for funding any drawings under any flexible loans. The composition of the trust property will fluctuate as drawings under any flexible loans and new loans are added and as the loans that are already part of the trust property are repaid or mature or default or are repurchased by the seller.

The applicable final terms will set out the approximate amounts of the Funding 1 share and the seller share as at the relevant closing date.

Income from the trust property will be distributed to Funding 1 and the seller on each distribution date. A **distribution date** is the date which is two London business days after each **calculation date** (being the date on which the mortgages trust is terminated and the first day of each month or, if not a London business day, the next succeeding London business day or any other day on which Funding 1 or the seller acquires a further interest in the trust property (other than due to capitalised interest) and/or the mortgages trustee acquires new loans from the seller). On each calculation date, the Funding 1 share and the seller share are recalculated based on the aggregate outstanding principal balance of the loans constituting the trust property on the London business day immediately before that calculation date. See “**The mortgages trust – Funding 1 share**” below for details of this recalculation.

Adjustments to the trust property may also occur if (among other things) borrowers take payment holidays or make underpayments.

On each distribution date, income (but not principal) from the trust property is allocated to Funding 1 (after paying amounts due to the mortgages trustee, the servicer, the cash manager, the account bank and third parties) in an amount equal to Funding 1’s percentage share of the remaining revenue receipts.

Income from the trust property is then allocated to the seller in an amount equal to any revenue receipts remaining after the above allocations to Funding 1 and the allocation of any loss amount as described under “**The mortgages trust – Cash management of trust property – revenue receipts – Mortgages trust calculation of revenue receipts**” below.

Losses on the loans are allocated to Funding 1 and the seller based on their respective percentage shares in the trust property.

Whether the mortgages trustee allocates principal received on the loans to Funding 1 depends on a number of factors. In general, Funding 1 receives payment of principal in the following circumstances:

- when, in relation to any rated loan tranche, Funding 1 is either accumulating principal during a cash accumulation period (as described below under “– **The intercompany loan**” below) or is scheduled

to make principal repayments on rated loan tranches or subordinated loan tranches (in which case, principal receipts will be paid to Funding 1 based on its cash accumulation requirements or repayment requirements in relation to those loan tranches);

- when a non-asset trigger event has occurred (in which case, all principal receipts on the loans will be paid to Funding 1 until the Funding 1 share has been reduced to zero. When the Funding 1 share is zero, the remaining mortgages trust available principal receipts (if any) will be allocated to the seller); and
- when an asset trigger event has occurred (in which case, all principal receipts on the loans will be paid to Funding 1 and the seller *pro rata* according to the Funding 1 share and the seller share, respectively, until the Funding 1 share is zero. When the Funding 1 share is zero, the remaining mortgages trust available principal receipts (if any) will be allocated to the seller).

Funding 1 is not entitled to receive in aggregate an amount of mortgages trust available principal receipts on a distribution date which is in excess of the Funding 1 share on the relevant distribution date.

For more information on the mortgages trust, cash accumulation periods and the distribution of principal receipts on the loans, including a description of when a non-asset trigger event or an asset trigger event will occur, see “**The mortgages trust**” below.

### **The intercompany loan**

The issuing entity has entered into the intercompany loan agreement with Funding 1. As described under “– **Relationship between the notes, issuing entity subordinated loans, issuing entity start-up loans and the intercompany loan**” above, the intercompany loan will consist of separate loan tranches. Each rated loan tranche will correspond to a particular series and class of notes. The rated loan tranches may comprise AAA loan tranches, AA loan tranches, A loan tranches, BBB loan tranches and BB loan tranches reflecting the designated credit rating assigned to each rated loan tranche (see “**The intercompany loan agreement – Ratings designations of the rated loan tranches**” below). The rated loan tranche related to a series and class of notes will be specified for such series and class of notes in the applicable final terms. Each subordinated loan tranche will correspond to an issuing entity subordinated loan advanced to the issuing entity by the issuing entity subordinated loan provider or, as the case may be, a new issuing entity subordinated loan provider on the relevant advance date. Each start-up loan tranche will correspond to an issuing entity start-up loan advanced by the issuing entity, by the issuing entity start-up loan provider or, as the case may be, a new issuing entity start-up loan provider on the relevant closing date.

The terms of each loan tranche will be set forth in the intercompany loan agreement and the related loan tranche supplement.

From time to time, the issuing entity may also make available to Funding 1 rated loan tranches with a designated credit rating lower than the BB loan tranches. Such loan tranches will be subordinated to the BB loan tranches and will be funded by the issuance of a new class of notes by the issuing entity, which issuance will be subject to the note trustee having received confirmation from each of the rating agencies that its ratings of each class of notes at that time outstanding will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of the issuance of such new notes.

From time to time and subject to certain conditions, the issuing entity will lend amounts to Funding 1 as separate loan tranches using the sterling equivalent proceeds of each issuance of a series and class of notes, issuing entity subordinated loan or, as applicable, issuing entity start-up loan. Funding 1 will use the funds advanced under each such loan tranche (excluding each start-up loan tranche):

- to pay to the seller part of the consideration for the sale of loans (together with their related security) to the mortgages trustee which will result in an increase in Funding 1's beneficial interest in the trust property;
- to acquire part of the seller share;
- to fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any);



- to make a payment to the issuing entity to refinance an existing loan tranche (which may be a rated loan tranche or a subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of a new intercompany loan.

Each start-up loan tranche will be used by Funding 1 for establishing (or, as applicable, increasing) the Funding 1 general reserve fund on the relevant closing date and/or for meeting the costs and expenses incurred by Funding 1 in connection with any purchase price and related sale of loans and their related security to the mortgages trustee or the acquisition of part of the seller share on the relevant closing date and the fees payable under the intercompany loan agreement which relate to the costs of the series of notes issued on the relevant closing date and/or to contribute towards Funding 1 available revenue receipts on the interest payment date immediately following the relevant closing date.

Subject to the provisions of the relevant Funding 1 priority of payments (see “**Cashflows**” below), Funding 1 will repay the intercompany loan from payments received from the mortgages trustee, as described under “– **The mortgages trust**” above. To the extent required, but subject to certain limits and conditions, Funding 1 may also apply amounts standing to the credit of the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any) in making payments of interest and principal due with respect to the rated loan tranches. The issuing entity will make payments of interest and principal:

- in respect of the notes, from payments of interest and principal made by Funding 1 to it with respect to the corresponding rated loan tranches;
- in respect of an issuing entity subordinated loan, from payments of interest and principal made by Funding 1 to it under the corresponding subordinated loan tranche; and
- in respect of an issuing entity start-up loan, from payments of interest and principal made by Funding 1 to it under the corresponding start-up loan tranche.

A rated loan tranche may be a bullet loan tranche, a scheduled amortisation loan tranche or a pass-through loan tranche. A **bullet loan tranche** is a loan tranche that is scheduled to be repaid in full in one instalment on one Funding 1 interest payment date. A **scheduled amortisation loan tranche** is a loan tranche that is scheduled to be repaid in more than one instalment on more than one Funding 1 interest payment date. Such instalments and Funding 1 interest payment dates are respectively referred to as **scheduled amortisation instalments** and **scheduled repayment dates**. A **pass-through loan tranche** is a loan tranche that has no scheduled repayment date other than its final repayment date. Loan tranches with pass-through repayment will be repaid on or after the Funding 1 interest payment date on which the loan tranches with the same series designation and a higher rating designation in respect of the applicable series have been fully repaid. The designation and type of rated loan tranche and the repayment schedule, if any, for the rated loan tranches advanced by the issuing entity in connection with the issuance of a particular series and class of notes will be set out in the applicable final terms.

Funding 1 will repay the intercompany loan primarily from payments received from the Funding 1 share. The issuing entity will make payments of interest and principal on a series and class of notes from payments of interest and principal on the corresponding rated loan tranche made by Funding 1 under the intercompany loan agreement. As further described in “**Cashflows – Distribution of Funding 1 available principal receipts – Due and payable dates of loan tranches**”, under the terms of the intercompany loan agreement, Funding 1 is required, prior to the occurrence of a trigger event or service of a note acceleration notice or an intercompany loan acceleration notice, to:

- repay each loan tranche which is a bullet loan tranche on the Funding 1 interest payment date specified in the relevant final terms, provided that to the extent there are insufficient funds to repay a bullet loan tranche on the relevant Funding 1 interest payment date, the shortfall will be repaid on subsequent Funding 1 interest payment dates to the extent of principal receipts available to Funding 1 for that purpose until that bullet loan tranche is fully repaid;
- repay each loan tranche which is a scheduled amortisation loan tranche in the scheduled amortisation instalments and on the Funding 1 interest payment dates specified in the relevant final terms, provided that to the extent there are insufficient funds to repay a scheduled amortisation instalment on the relevant Funding 1 interest payment date, the shortfall will be repaid on subsequent Funding 1

interest payment dates to the extent of principal receipts available to Funding 1 for that purpose until that scheduled amortisation loan tranche is fully repaid;

- repay each pass-through loan tranche to the extent of principal receipts available to Funding 1 for that purpose on each Funding 1 interest payment date on or after the Funding 1 interest payment date on which the loan tranche with the same series designation and a higher rating designation has been fully repaid.

Funding 1 will seek to accumulate funds for principal repayments on rated loan tranches which are bullet loan tranches or scheduled amortisation instalments over a cash accumulation period in order to repay such loan tranches to the issuing entity:

- as a lump sum payment in the case of a bullet loan tranche, on the Funding 1 interest payment date specified in the applicable final terms; or
- in instalments in the case of a scheduled amortisation loan tranche, in the amounts and on the Funding 1 interest payment dates specified in the applicable final terms.

A **cash accumulation period** for a rated loan tranche is the estimated number of months prior to the relevant scheduled repayment date necessary for Funding 1 to accumulate enough principal receipts on the loans to make the scheduled repayment on that rated loan tranche on that date. The formulas for determination and extension of cash accumulation periods are described under “**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**” and “**Cashflows – Distribution of Funding 1 available principal receipts**” below.

During a cash accumulation period with respect to any bullet loan tranche or scheduled amortisation loan tranche, Funding 1 will continue to make principal repayments on any other loan tranches that are then due and scheduled to be paid, subject to having sufficient funds therefor after meeting its obligations with a higher priority. Such principal repayments may only be made to the extent that the repayment tests are satisfied on the relevant Funding 1 interest payment date. In addition, in certain circumstances, payment on the scheduled amortisation loan tranches and pass-through loan tranches will be deferred. See “**Cashflows – Distribution of Funding 1 available principal receipts**” below. The transaction has been structured in the expectation that Funding 1 will receive sufficient funds under the mortgages trust on or before each scheduled repayment date with respect to any bullet loan tranches and scheduled amortisation instalments in order to repay to the issuing entity such loan tranches, so that the issuing entity can redeem the corresponding series and class of notes on their scheduled redemption dates. However, no assurance can be given that Funding 1 will accumulate sufficient funds during any cash accumulation period.

Whether Funding 1 will have sufficient funds to repay the loan tranches, on the dates described in the applicable final terms, will depend on a number of factors. See “**Risk factors – The yield to maturity of the notes may be adversely affected by prepayments or redemptions on the loans**” and “**Risk factors – The issuing entity’s ability to redeem the notes is affected by the rate of prepayment on the loans**”.

Prior to the occurrence of a trigger event or service of a note acceleration notice or an intercompany loan acceleration notice, Funding 1 is generally required to repay principal on the rated loan tranches based on their respective loan tranche ratings. This means that the AAA loan tranches are repaid before the AA loan tranches, which in turn are repaid before the A loan tranches, which in turn are repaid before the BBB loan tranches, which in turn are repaid before the BB loan tranches. Prior to the occurrence of a trigger event or the service of a note acceleration notice or an intercompany loan acceleration notice, there are a number of exceptions to this priority of payments. For further information on such exceptions you should read the “**Cashflows**” below.

In certain circumstances, principal payments on the BB loan tranches, the BBB loan tranches, the A loan tranches and the AA loan tranches will be deferred. Those circumstances are that as at the relevant Funding 1 interest payment date:

- there is (as a consequence of principal losses on the loans or application of Funding 1 available principal receipts to meet deficiencies in Funding 1 available revenue receipts or to fund any Funding 1 liquidity reserve fund (if any)) a debit balance on a sub-ledger of the Funding 1 principal deficiency ledger (other than the subordinated loan principal deficiency sub-ledger) after application of the Funding 1 available revenue receipts on the relevant Funding 1 interest payment date (see “**Credit structure – Funding 1 principal deficiency ledger**”); or

- the adjusted Funding 1 general reserve fund level is less than the Funding 1 general reserve fund threshold; or
- the aggregate outstanding principal balance of loans in the mortgages trust in respect of which the aggregate amount in arrears is more than three times the monthly payment then due is more than 5 per cent. of the aggregate outstanding principal balance of loans in the mortgages trust,

and, as at that date, there is one or more AAA loan tranches outstanding or, in respect of the BB loan tranches, there is one or more term BBB loan tranches outstanding or, in respect of the BBB loan tranches, there is one or more A loan tranches outstanding or, in respect of the A loan tranches, there is one or more AA loan tranches outstanding (whether or not any such loan tranches are then due and payable). Any deferral of the principal amounts due on the BB loan tranches, the BBB loan tranches, the A loan tranches or the AA loan tranches will result in deferral of principal amounts due on the corresponding classes of notes.

The deferral mechanics described in this section will also apply to any new rated loan tranches with a designated credit rating below the BB loan tranches.

In certain circumstances, payment on the scheduled amortisation loan tranches will be deferred. This will occur if, on a Funding 1 interest payment date, one or more bullet loan tranches are within a cash accumulation period at that time (irrespective of whether any scheduled amortisation instalments are then in a cash accumulation period) and either:

- the quarterly CPR (which is a measure of the annualised principal payment rate on the loans in the portfolio) is less than 10 per cent.; or
- both:
  - (i) the quarterly CPR is equal to or greater than 10 per cent., but less than 15 per cent.; and
  - (ii) the annualised CPR is less than 10 per cent.

In these circumstances, the scheduled amortisation loan tranches will be entitled to receive principal repayments only to the extent permitted under the scheduled amortisation repayment restrictions (see “**Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes**” below).

Furthermore, if, on a Funding 1 interest payment date:

- one or more bullet loan tranches and/or scheduled amortisation instalments are then in a cash accumulation period;
- the quarterly CPR is less than 15 per cent.; and
- there is a shortfall in the amount of cash accumulated at that time,

then, on or before their step-up dates, the original pass-through loan tranches will be entitled to principal repayments only to the extent permitted under the pass-through repayment restrictions (see “**Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes**”).

See also “**Risk factors – The yield to maturity of the notes may be adversely affected by prepayments or redemptions on the loans**” and “**Risk factors – The issuing entity’s ability to redeem the notes is affected by the rate of prepayment on the loan tranches**”.

The circumstances under which the issuing entity can take action against Funding 1 if it does not make a repayment under the intercompany loan are limited. In particular, it will not be an event of default in respect of the intercompany loan if Funding 1 does not repay amounts due in respect of the intercompany loan where Funding 1 does not have the money to make the relevant repayment or where the repayment tests are not satisfied. For more information on the intercompany loan, see “**The intercompany loan agreement**” below.

If any loan tranche is not repaid on the relevant step-up date, then the funds representing principal receipts that Funding 1 can allocate to repay such loan tranche (other than bullet loan tranche or scheduled amortisation instalments) on a Funding 1 interest payment date may not exceed the proportion that such loan tranche bears to the aggregate outstanding principal balance of all of the loan tranches.

If the notes of each series are or have been accelerated, then the outstanding loan tranches will be immediately due and payable, but the Funding 1 security will not automatically be enforced unless Funding 1 is also in default under the intercompany loan agreement and Funding 1 will allocate its funds representing principal receipts to repay the loan tranches in order of rating designation, from highest to lowest and *pro rata* and *pari passu* between loan tranches of the same rating designation.

Funding 1 has and will continue to repay each subordinated loan tranche *pro rata* (a) on each Funding 1 interest payment date, but only to the extent that the aggregate principal amount outstanding of all subordinated loan tranches exceeds the then required subordinated loan tranche principal amount outstanding or, if lower, to the extent that it has Funding 1 available principal receipts after making higher ranking payments or (b) on any date to the extent that it is refinanced by another loan tranche (which may be another subordinated loan tranche). Amounts due with respect to subordinated loan tranches are payable after amounts due on rated loan tranches but prior to amounts due on start-up loan tranches.

Funding 1 will repay each start-up loan tranche on each Funding 1 interest payment date, but only to the extent that it has Funding 1 available revenue receipts after making higher ranking payments. Amounts due with respect to start-up loan tranches are payable after amounts due on the rated loan tranches and amounts due on subordinated loan tranches.

### **Issuing entity subordinated loan agreements**

From time to time, the issuing entity may enter into issuing entity subordinated loan agreements with the issuing entity subordinated loan provider, pursuant to which the issuing entity subordinated loan provider will, on the relevant advance date, advance an issuing entity subordinated loan to the issuing entity. Each issuing entity subordinated loan will be used by the issuing entity to advance to Funding 1 a subordinated loan tranche under the intercompany loan agreement. Each subordinated loan tranche will be used by Funding 1:

- to pay the seller part of the consideration for loans (together with their related security) sold by the seller to the mortgages trustee;
- to acquire part of the seller share (such payment to be made to the seller);
- to fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any); and/or
- to make a payment to the issuing entity to refinance an existing loan tranche (which may be a rated loan tranche or a subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of new intercompany loan.

The amount of each subordinated loan tranche issued at the same time as an issuance of notes will be described in the applicable loan tranche supplement and (if applicable) final terms.

Funding 1 will make repayments on the subordinated loan tranches *pro rata* (a) on each Funding 1 interest payment date, to the extent that the aggregate principal amount outstanding of all of the subordinated loan tranches exceeds the then required subordinated loan tranche principal amount outstanding or, if lower, to the extent that it has Funding 1 available principal receipts remaining after it has made all payments ranking senior thereto in accordance with the applicable Funding 1 pre-enforcement principal priority of payments or (b) on any date, to the extent that they are refinanced by one or more other loan tranches (which may be subordinated loan tranches). The issuing entity will repay each issuing entity subordinated loan to the extent it receives amounts from Funding 1 in respect of the corresponding subordinated loan tranche.

### **Security granted by Funding 1 and the issuing entity**

On the programme date, Funding 1 entered into a Funding 1 deed of charge to secure its obligations to the then existing Funding 1 secured creditors and, in connection with the issuance of future series of notes and/or the advance of any issuing entity subordinated loan, new secured creditors of Funding 1 may accede to the Funding 1 deed of charge from time to time.

Besides the issuing entity, the Funding 1 secured creditors on the programme date were the Funding 1 swap provider, the Funding 1 GIC provider, the corporate services provider, the cash manager, the account bank, the Funding 1 security trustee and the seller.

Pursuant to the terms of the Funding 1 deed of charge, Funding 1 has granted security over all of its assets in favour of the Funding 1 security trustee. The Funding 1 security trustee holds that security for the benefit of the Funding 1 secured creditors. Only the Funding 1 security trustee is entitled to enforce the security granted by Funding 1. For more information on the security granted by Funding 1, see “**Security for Funding 1’s obligations**” below. For details of the Funding 1 post-enforcement priority of payments, see “**Cashflows**” below.

To secure the issuing entity’s obligations to the noteholders and other issuing entity secured creditors, the issuing entity has granted security over all of its assets in favour of the issuing entity security trustee. The issuing entity security trustee holds that security for the benefit of the issuing entity secured creditors, which are the noteholders of each series, the issuing entity security trustee, the note trustee, the paying agents, the agent bank, the registrar, the transfer agent, the exchange agent, the issuing entity cash manager, the issuing entity account bank, the issuing entity swap providers, the issuing entity start-up loan provider and the corporate services provider. Only the issuing entity security trustee is entitled to enforce the security granted by the issuing entity. For more information on the security granted by the issuing entity, see “**Security for the issuing entity’s obligations**” below. For details of the issuing entity post-enforcement priority of payments, see “**Cashflows**” below.

### **Swap agreements**

Some of the loans in the portfolio will pay interest at a variable rate based on the standard variable rate of Birmingham Midshires, some of the loans in the portfolio pay interest at a fixed rate or rates of interest and some of the loans in the portfolio pay interest which tracks an interest rate other than the standard variable rate of Birmingham Midshires (the tracker rate is currently set at a margin above or below a rate set by the Bank of England). These interest rates do not necessarily match the floating rates of interest payable on the loan tranches under the intercompany loan. Funding 1 has entered into a swap documented under the Funding 1 swap agreement to hedge against these potential interest rate mismatches.

Borrowers will make payments under the loans in sterling. Payments made by the mortgages trustee to Funding 1 under the mortgages trust deed and payments made by Funding 1 to the issuing entity under the intercompany loan agreement will also be made in sterling. To enable the issuing entity (a) to make payments on a series and class of notes (other than sterling-denominated notes) in their respective currencies and/or (b) to make payments on a series and class of sterling-denominated fixed rate notes or sterling-denominated notes with monthly interest payment dates, the issuing entity has entered and will enter into issuing entity swap agreements. The identity of and certain additional information about the relevant issuing entity swap provider will be described in greater detail in the applicable final terms.

### **United Kingdom tax status**

You are referred to “**United Kingdom taxation**” below for a discussion of certain UK tax matters, including UK withholding tax on interest payments to noteholders.

### **United States tax status**

A discussion of the material US federal income tax consequences of the purchase, ownership and disposition of the Rule 144A notes is set out in “**United States federal income taxation**” below. As set forth in that discussion, unless otherwise indicated in the applicable final terms, it is anticipated that upon issuance of the notes, Allen & Overy LLP, US tax adviser to the issuing entity and Funding 1, will deliver their opinion that, although there is no authority on the treatment of instruments substantially similar to the Rule 144A notes, the class A Rule 144A notes, class B Rule 144A notes and class M Rule 144A notes, when issued, will be treated as debt for US federal income tax purposes and the class C Rule 144A notes, when issued, should be treated as debt for US federal income tax purposes. Also, as discussed in “**United States federal income taxation**” below, it is anticipated that Allen & Overy LLP, US tax adviser to the issuing entity and Funding 1, will deliver their opinion that, assuming compliance with the transaction documents, the mortgages trustee acting in its capacity as trustee of the mortgages trust, Funding 1 and the issuing entity will not be subject to US federal income tax.

### **Jersey (Channel Islands) tax status**

It is the opinion of Mourant du Feu & Jeune, Jersey (Channel Islands), Jersey tax counsel to the mortgages trustee and the issuing entity, that the mortgages trustee is resident in Jersey for taxation purposes and is and will be liable to income tax in Jersey at a rate of 20 per cent. in respect of the profits it makes from acting as trustee of the mortgages trust. The mortgages trustee will not be liable for any income tax in Jersey in respect of any

income it receives in its capacity as mortgages trustee on behalf of the beneficiaries of the mortgages trust. Legislation has been adopted by the States of Jersey which, on and from 1 January 2009, introduces a standard rate of corporate tax of 0% applicable to all companies (other than any "financial services company" (as defined therein) and certain specified Jersey utility companies). As at the date of this Prospectus the mortgages trustee is neither a "financial services company" nor such a specified utility company. See "**Material Jersey (Channel Islands) tax considerations**" below.

#### **ERISA considerations for investors**

Unless otherwise stated in the Final Terms, the Rule 144A notes are and will be eligible for purchase by employee benefit and other plans subject to Section 406 of ERISA or Section 4975 of the Code and by governmental, church or non-US plans that are subject to any state, local or other federal law of the United States or non-US law that is substantially similar to Section 406 of ERISA or Section 4975 of the Code, subject to consideration of the issues described herein under "**ERISA considerations**" below.

## Fees

The following table sets out the on-going fees to be paid by the issuing entity, Funding 1 and the mortgages trustee to transaction parties. Each of these fees is subject to change at any time without your notification or approval, including upon the appointment of any successor service provider or any other successor transaction party pursuant to the applicable transaction document.

Type of fee	Amount of fee	Priority in cashflow	Frequency
Servicing fee	0.05 per cent. each year of the aggregate amount of the trust property	Ahead of all revenue amounts payable to Funding 1 by the mortgages trustee	Each distribution date
Mortgages trustee fee	£1,500 each year	Ahead of all revenue amounts payable to Funding 1 by the mortgages trustee	Annually on the distribution date following the anniversary of the establishment of the mortgages trust
Cash management fee	0.025 per cent. each year of the aggregate principal amount outstanding of the rated loan tranches, paid in accordance with separate fee letters by Funding 1 and the mortgages trustee	Ahead of all revenue amounts payable to Funding 1 by the mortgages trustee	Each distribution date
Issuing entity cash management fee	Estimated 0.025 per cent. each year of the principal amount outstanding of the notes	Ahead of all loan tranches	Each Funding 1 interest payment date
Corporate expenses of mortgages trustee	Estimated £1,250 each year	Ahead of all revenue amounts payable to Funding 1 by the mortgages trustee	Each distribution date
Corporate expenses of Funding 1	Estimated £1,250 each year	Ahead of all outstanding loan tranches	Each Funding 1 interest payment date
Corporate expenses of issuing entity	Estimated £5,200 each year	Ahead of all outstanding notes	Each quarterly interest payment date
Fee payable to Funding 1 security trustee, issuing entity security trustee and note trustee (including paying agents)	An amount per annum as agreed in accordance with a fee arrangement letter dated on the programme date	Ahead of all outstanding loan tranches and all outstanding notes	Each Funding 1 interest payment date and each quarterly interest payment date (as applicable)

## Risk factors

*This section describes the principal risk factors associated with an investment in the notes. These risk factors are material to an investment in the notes and in the issuing entity. If you are considering purchasing notes, you should carefully read and think about all the information contained in this base prospectus and in the applicable final terms, including the risk factors set out here and in the applicable final terms, prior to making any investment decision.*

### **You cannot rely on any person other than the issuing entity to make payments on the notes**

The notes do not and will not represent an obligation or be the responsibility of Bank of Scotland or any of their affiliates, the dealers, the managers, Funding 1, the mortgages trustee, the Funding 1 security trustee, the issuing entity security trustee, the note trustee or any other party to the transaction documents other than the issuing entity.

### **The issuing entity has a limited set of resources available to make payments on the notes**

The issuing entity's ability to make payments of principal and interest on the notes and to pay its operating and administrative expenses will depend primarily on funds received by it under the intercompany loan agreement. The payment of interest and repayment of principal on each series and class of notes will depend primarily on funds being received by the issuing entity under the corresponding rated loan tranche (and no other loan tranche). In addition, the issuing entity will rely on the issuing entity swaps to provide payments on certain series and classes of notes.

In addition, the Funding 1 general reserve fund was established on the programme date. Subject to certain limits and conditions, Funding 1 may apply amounts standing to the credit of the Funding 1 general reserve fund in payment of, among other things, amounts due to the issuing entity in respect of the rated loan tranches.

In the event that the seller suffers certain ratings downgrades, Funding 1 will be required to fund the Funding 1 liquidity reserve fund, though there can be no assurance that Funding 1 will have sufficient resources to do so at such time, and Funding 1 may draw money from the Funding 1 liquidity reserve fund (see "**Credit structure – Funding 1 liquidity reserve fund**" below), to the extent it has been funded, to pay amounts due to the issuing entity in respect of the rated loan tranches.

The issuing entity does not have any other significant sources of funds available to meet its obligations under the notes and/or any other payments ranking in priority to the notes.

### **Funding 1 is not obliged to make payments on the loan tranches if it does not have enough money to do so, which could adversely affect payments on the notes**

Funding 1's ability to pay amounts due on the loan tranches advanced under the intercompany loan agreement will depend upon:

- Funding 1 receiving enough funds from its entitlement to the trust property on or before each Funding 1 interest payment date;
- Funding 1 receiving the required funds from the Funding 1 swap provider;
- the amount of funds credited to the Funding 1 general reserve fund (as described in "**Credit structure – Funding 1 general reserve fund**" below); and
- the amount of funds credited to the Funding 1 liquidity reserve fund (if any) (as described in "**Credit structure – Funding 1 liquidity reserve fund**" below).

According to the terms of the mortgages trust deed, the mortgages trustee is obliged to pay to Funding 1 the Funding 1 share percentage of revenue receipts on the loans (subject to payment of prior ranking amounts) by crediting those amounts to the Funding 1 GIC account on each distribution date. The mortgages trustee is obliged to pay to Funding 1 principal receipts on the loans by crediting those amounts to the Funding 1 GIC account as and when required pursuant to the terms of the mortgages trust deed.

Funding 1 is obliged to pay amounts (other than principal) due to the issuing entity in respect of a loan tranche under the intercompany loan only to the extent that it has revenue receipts available to it after making payments ranking in priority to such loan tranche, such as payments of certain fees and expenses of Funding 1 and



payments of interest on loan tranches of a more senior ranking, and taking into account payments of interest on loan tranches ranking equally with such loan tranche (such as other loan tranches of the same ratings designation). See “**Cashflows – Distribution of Funding 1 available revenue receipts before intercompany loan acceleration**” below. Funding 1 is obliged to pay principal amounts due to the issuing entity in respect of a loan tranche under the intercompany loan only to the extent it has received principal receipts available for that purpose after repaying amounts ranking in priority to such loan tranche (including repaying any loan tranches with higher rating designations) and taking into account repayments on loan tranches ranking equally with such loan tranche. See “**Cashflows – Distribution of Funding 1 available principal receipts**” below.

If Funding 1 does not pay amounts to the issuing entity in respect of a loan tranche under the intercompany loan agreement because it does not have sufficient funds available, those amounts will be due but not payable until funds are available to pay those amounts in accordance with the relevant Funding 1 priority of payments.

If there is a shortfall between the amounts payable by Funding 1 to the issuing entity in respect of a rated loan tranche under the intercompany loan agreement and the amounts payable by the issuing entity on the related series and class of notes, you may not receive the full amount of interest and/or principal which would otherwise be due and payable on those notes.

**On the final repayment date of the intercompany loan, any outstanding amounts in respect of the loan tranches will be extinguished, which would cause a loss on any notes still outstanding**

The issuance of notes under the programme has been structured in the expectation that, on the latest occurring final repayment date of the corresponding loan tranches under the intercompany loan agreement, the interest and principal due and payable on such notes will be in an amount equal to the sum available to pay all outstanding interest and/or principal (including interest and/or principal deferred and unpaid) on the corresponding rated loan tranches (after paying amounts of a higher priority as required by the Funding 1 priority of payments).

If there is a shortfall between the amount available to pay such interest and/or principal and the amount required to pay all outstanding interest and/or principal on the rated loan tranches, then the shortfall will be deemed to be not due and payable under the intercompany loan agreement and the issuing entity will not have any claim against Funding 1 for the shortfall.

Following enforcement of the Funding 1 security and application of the proceeds of enforcement, any remaining shortfall will be extinguished.

If there is such a shortfall in interest and/or principal payments under the intercompany loan agreement, you may not receive the full amount of interest and/or principal that would otherwise be due and payable on the notes outstanding.

**Enforcement of the issuing entity security is the only remedy for a default in the issuing entity’s obligations, and the proceeds of that enforcement may not be enough to make payments on the notes**

The only remedy for recovering amounts on the notes is through the enforcement of the issuing entity security. The issuing entity has no recourse to the assets of Funding 1 unless Funding 1 has also defaulted on its obligations under the intercompany loan and the Funding 1 security has been enforced.

If the security created under the issuing entity deed of charge is enforced, the proceeds of enforcement may be insufficient to pay all principal and interest due on the notes.

**There is no assurance that the subordination rules will protect the holders of class A notes, the holders of class B notes, the holders of class M notes, the holders of class C notes and the holders of the Class D notes from all risk of loss**

The programme has been structured in the expectation that a series and class of notes will be redeemed in full, at the same time as, prior to or following the redemption of another series and class of notes. This means, for example, that the class B notes, the class M notes, the class C notes and the class D notes of one series may be redeemed before the class A notes of another series, even though the latter notes have a higher class designation than the former notes.

However, there is no assurance that a given series of a particular issuance of notes will be redeemed in full before all the series of notes of the same issuance with a numerically higher series designation. In each case, redemption of the notes is ultimately dependent on, among other things, repayment and redemptions on the loans and on the rating designation of the related loan tranches. Further, if on any interest payment date, amounts are due and payable in respect of the class A notes of any series and amounts are due and payable in respect of the class B notes of any other series, the class M notes of any other series, the class C notes of any other series and/or the class D notes of any other series, then payments of principal will be made on the class A notes in priority to

payments of principal on the class B notes, the class M notes, the class C notes and the class D notes of such other series. Similarly, if on any interest payment date, amounts are due and payable in respect of the class B notes of any series and amounts are due and payable in respect of the class M notes of any other series, the class C notes of any other series and/or the class D notes of any other series, then payments of principal will be made on the class B notes in priority to payments of principal on the class M notes, the class C notes and the class D notes of such other series, and so on. See “**Maturity and prepayment considerations**” in the applicable final terms.

**Subordination of other note classes, issuing entity subordinated loans and issuing entity start-up loans may not protect noteholders from all risk of loss**

The class B notes, the class M notes, the class C notes and class D notes of any series will be subordinated in right of payment of both interest and principal to the class A notes of any series. The class M notes, the class C notes and the class D notes will be subordinated in right of payment of both interest and principal to the class B notes of any series. The class C notes and the class D notes of any series will be subordinated in right of payment of both interest and principal to the class M notes of any series. The class D notes of any series will be subordinated in right of payment of both interest and principal to the class C notes of any series.

Furthermore, all issuing entity subordinated loans will be subordinated in right of payment of both interest and principal to the class D notes and all issuing entity start-up loans will be subordinated in right of payment of both interest and principal to the issuing entity subordinated loans

You should be aware however that not all classes of notes are scheduled to receive payments of interest and principal on the same interest payment dates. The interest payment dates for the payment of interest and principal in respect of each series and class of notes will be specified in the applicable final terms. Each series and class of notes may have interest payment dates in respect of interest and/or principal that are different from other notes of the same class (but of different series) or of the same series (but of different class). Despite the principal priority of payments described above, subject to no trigger event having occurred and satisfaction of the repayment tests, lower ranking classes of notes may nevertheless be repaid principal before higher ranking classes of notes and a series and class of notes may be repaid principal before another series of notes of the same class. Payments of principal are expected to be made to each class of notes in amounts up to the amounts set forth under “**Cashflows – Distribution of issuing entity principal receipts before note acceleration**”, “**Cashflows – Distribution of issuing entity principal receipts after note acceleration but before intercompany loan acceleration**” and “**Cashflows – Distribution of issuing entity principal receipts and issuing entity revenue receipts following note acceleration and intercompany loan acceleration**” below.

However, there is no assurance that these subordination rules will protect the class A noteholders from all risks of loss, the class B noteholders from all risks of loss, the class M noteholders from all risks of loss, the class C noteholders from all risks of loss or the class D noteholders from all risks of loss. If the losses borne by the issuing entity subordinated loans are in an amount equal to the aggregate outstanding principal balance of the issuing entity subordinated loans, then losses on the loans will thereafter be borne by the class D noteholders. Similarly, if the losses borne by the issuing entity subordinated loans and the class D notes are in an amount equal to the aggregate outstanding principal balances of the issuing entity subordinated loans and the class D notes, then losses on the loans will thereafter be borne by the class C notes. Similarly, if the losses borne by the issuing entity subordinated loans, the class D notes and the class C notes are in an amount equal to the aggregate outstanding principal balances of the issuing entity subordinated loans, the class D notes and the class C notes, then losses on the loans will thereafter be borne by the class M notes. Similarly, if the losses borne by the issuing entity subordinated loans, the class D notes, the class C notes and the class M notes are in an amount equal to the aggregate outstanding principal balances of the issuing entity subordinated loans, the class D notes, the class C notes and the class M notes, then losses on the loans will thereafter be borne by the class B notes. Finally, if the losses borne by the issuing entity subordinated loans, the class D notes, the class C notes, the class M notes and the class B notes are in an amount equal to the aggregate outstanding principal balances of the issuing entity subordinated loans, the class D notes, the class C notes, the class M notes and the class B notes, then losses on the loans will thereafter be borne by the class A notes, at which point there will be an asset trigger event.

**Payments of class B notes, class M notes, class C notes and class D notes may be delayed or reduced in certain circumstances**

On any interest payment date on which a payment of principal is due on any series of class B notes, class M notes, class C notes or class D notes, the issuing entity’s obligation to make such principal payments will be subject to the satisfaction of the repayment tests described under “**Cashflows – Distribution of Funding 1 available principal receipts**” below, including an arrears test, a general reserve fund requirement and a principal deficiency sub-ledger test, to the extent that any class A notes (or other more senior ranking notes) of any series are outstanding on that date.

**There may be conflicts between the interests of the holders of the various classes of notes and the interests of other classes of notes may prevail over your interests**

The note trust deed and the terms of the notes will provide that the note trustee is to have regard to the interests of the holders of all classes of notes. There may be circumstances, however, where the interests of one class of the noteholders conflict with the interests of another class or classes of the noteholders. In general, the note trustee will give priority to the interests of the holders of the most senior class of notes, such that:

- the note trustee is to have regard only to the interests of the class A noteholders in the event of a conflict between the interests of the class A noteholders on the one hand and the class B noteholders and/or the class M noteholders and/or the class C noteholders and/or the class D noteholders on the other hand;
- (if there are no class A notes outstanding) the note trustee is to have regard only to the interests of the class B noteholders in the event of a conflict between the interests of the class B noteholders on the one hand and the class M noteholders and/or the class C noteholders and/or the class D noteholders on the other hand;
- (if there are no class A notes or class B notes outstanding) the note trustee is to have regard only to the interests of the class M noteholders in the event of a conflict between the interests of the class M noteholders on the one hand and the class C noteholders and/or the class D noteholders on the other hand; and
- (if there are no class A notes, class B notes or class M notes outstanding) the note trustee is to have regard only to the interests of the class C noteholders in the event of a conflict between the interests of the class C noteholders on the one hand and the class D noteholders on the other hand.

**The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree modifications to the transaction documents without your prior consent, which may adversely affect your interests**

Pursuant to the terms of the Funding 1 deed of charge and the issuing entity deed of charge, the Funding 1 security trustee and the issuing entity security trustee may concur with any person in making or sanctioning any modifications to the transaction documents (in the case of the Funding 1 security trustee) if so directed by the issuing entity security trustee and (in the case of the issuing entity security trustee) if so directed by the note trustee and with the prior consent of any other relevant issuing entity secured creditors. The note trustee may give such direction, without the consent or sanction of the noteholders, provided that:

- the note trustee is of the opinion that such modification will not be materially prejudicial to the interests of the holders of any series and class of notes; or
- in the sole opinion of the note trustee, such modification is necessary to correct a manifest error or is of a formal, minor or technical nature or is to comply with the mandatory provisions of law.

The note trustee will be entitled to assume that the exercise of its rights, powers, duties and discretions will not be materially prejudicial to the interests of any series and class of noteholders if each of the rating agencies has confirmed that the then current rating by it of such series and class of notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified by such exercise.

In addition, as further described in “**Security for Funding 1’s obligations – Appointment, powers, responsibilities and liabilities of the Funding 1 security trustee**” and “**Security for the issuing entity’s obligations – Appointment, powers, responsibilities and liabilities of the issuing entity security trustee**”, below, each of the Funding 1 security trustee and the issuing entity security trustee will give its consent to any modifications to any transaction document that are requested by Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf), provided that Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf) certifies to the Funding 1 security trustee or, as applicable, the issuing entity security trustee in writing that such modifications are required in order to accommodate, among other things, notes to be issued by the issuing entity and/or loan tranches to be made available by the issuing entity to Funding 1 under the intercompany loan agreement (including new classes of notes and their corresponding loan tranches), new intercompany loan agreements to be entered into by Funding 1 or any new funding beneficiary and/or the issue of new notes by the issuing entity or any new issuing entities,

the addition of a new funding beneficiary as a beneficiary of the mortgages trust, the acquisition by Funding 1 or the mortgages trustee of an interest in any other securitisation involving products originated within the HBOS group, the addition of new Funding 1 secured creditors and/or new issuing entity secured creditors, the sale of new types of loans or mortgages to the mortgages trustee (including the assignment of loans and their related security originated under brands and/or by legal entities within the HBOS group other than Birmingham Midshires and the seller respectively), changes to the Funding 1 reserve required amount, the Funding 1 liquidity reserve fund required amount or the manner in which any Funding 1 reserve fund is funded, different Funding 1 interest payment dates, interest periods and/or bases for calculation of interest in respect of any loan tranches then outstanding under the intercompany loan agreement) or changes to the asset trigger events and non-asset trigger events, subject to applicable conditions.

The modifications required to give effect to the matters listed above may include, among other matters, amendments to the provisions of the Funding 1 deed of charge relating to the application of monies. Accordingly, there can be no assurance that the effect of the modifications to the relevant transaction documents will not ultimately adversely affect your interests.

### **Holdings may establish other companies which may become a beneficiary under the mortgages trust**

Holdings may establish separate entities (each, a **new funding beneficiary**) which may issue (directly or indirectly) notes from time to time and use the proceeds to acquire a direct interest in the trust property. Simultaneously with the acquisition by any such new funding beneficiary of an interest in the trust property, the seller and Funding 1, as beneficiaries of the mortgages trust, would be required to agree to a decrease in their beneficial interest in the trust property (and a partial release of security by Funding 1 over its share of the trust property).

The seller, Funding 1 and any new funding beneficiary would each have a joint and undivided interest in the trust property but their entitlement to the proceeds from the trust property would be in proportion to their respective shares of the trust property from time to time. On each distribution date, the mortgages trustee would distribute interest and principal receipts to one or more beneficiaries, depending on the terms of the mortgages trust at that time.

It is anticipated that any such new funding beneficiary would issue notes (directly or indirectly) to investors from time to time backed by its share of the trust property. You would not have a direct or indirect interest in any such new funding beneficiary's share of the trust property.

Amendments could be made to a number of the transaction documents as a result of the inclusion of a new funding beneficiary as a beneficiary of the mortgages trust. In particular (but without limitation), amendments would be made to:

- the mortgage sale agreement to enable (among other things) the purchase by the new funding beneficiary of interests in the trust property by paying the purchase price for new loans and their related security sold by the seller from time to time and to give the new funding beneficiary the benefit of the covenants in the mortgage sale agreement;
- the mortgages trust deed (i) to establish the new funding beneficiary as a beneficiary of the mortgages trust, (ii) to enable the acquisition by the new funding beneficiary of an interest in the trust property from time to time and (iii) to regulate the distribution of revenue receipts and principal receipts to the new funding beneficiary and the other beneficiaries;
- the cash management agreement to regulate the application of monies to the new funding beneficiary;
- the servicing agreement, to ensure that the new funding beneficiary receives the benefit of the servicer's duties under that agreement; and
- the master definitions and construction schedule.

There may be conflicts of interest between Funding 1 and any new funding beneficiary, in which case it is expected that the mortgages trustee will follow the directions given by the relevant beneficiary (excluding the seller) (or the relevant Funding security trustee) representing one or more issuing entities with the highest ranking class of notes or new notes (as applicable) then outstanding and, if each relevant beneficiary (or relevant Funding security trustee) represents one or more issuing entities (as applicable) with the same class as their highest ranking class of notes or new notes (as applicable) then outstanding, then the beneficiary (or the relevant Funding

security trustee) representing one or more issuing entities with the greatest outstanding principal balance of the highest ranking class of notes or new notes (as applicable) then outstanding. The interests of Funding 1 may not prevail in these circumstances, which may adversely affect your interests.

Your prior consent to the inclusion of a new funding beneficiary of the mortgages trust and the subsequent amendments to the documents and/or release of security by Funding 1 will not be required. The mortgages trustee shall agree to a new funding beneficiary of the mortgages trust only if the Funding 1 security trustee notifies the mortgages trustee in writing that a number of conditions precedent have been satisfied, including:

- that the Funding 1 security trustee has received written confirmation from each of the rating agencies that its then current rating of the notes then outstanding at that time will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of the new funding beneficiary of the mortgages trust;
- that no note event of default or intercompany loan event of default under the intercompany loan agreement has occurred which is continuing or unwaived as at such date (as certified in writing to the Funding 1 security trustee by Funding 1 or the cash manager); and
- that no principal deficiency is recorded on the Funding 1 principal deficiency ledger (other than the subordinated loan principal deficiency sub-ledger) as at the most recent Funding 1 interest payment date or, where a principal deficiency is recorded on the Funding 1 principal deficiency ledger (other than the subordinated loan principal deficiency sub-ledger) as at such date, that the Funding 1 available revenue receipts on the forthcoming Funding 1 interest payment date will be sufficient, when applied in accordance with the Funding 1 pre-enforcement revenue priority of payments, to eliminate such principal deficiency (as certified in writing to the Funding 1 security trustee by Funding 1 or the cash manager).

There can be no assurance that the inclusion of a new funding beneficiary of the mortgages trust would not affect cashflows available to pay amounts due on your notes and therefore adversely affect your interests.

**If Funding 1 enters into new intercompany loan agreements, such new intercompany loans and accompanying new notes may be repaid prior to the intercompany loan and your notes**

Subject to satisfaction of certain conditions, Holdings may, in the future, establish additional wholly-owned subsidiary companies as new issuing entities to issue new notes to investors or the issuing entity may issue new notes to investors. The proceeds of each such issue of new notes may be advanced to Funding 1 by way of a new intercompany loan. Funding 1 may use the proceeds of such new intercompany loan to, amongst other things, pay to the seller the consideration for new loans and their related security to be sold to the mortgages trustee and/or to pay to the seller the consideration for the sale of a portion of the seller share (which will each result in an increase in the Funding 1 share) and/or the deposit of some of those proceeds in the Funding 1 general reserve fund and/or Funding 1 liquidity reserve fund (if any) and/or to refinance all or part of the intercompany loan outstanding at that time. If the intercompany loan (or any part thereof) is refinanced, you could be repaid early.

The issuing entity expects that the payment of the amounts owing by Funding 1 under a new intercompany loan will be funded from amounts received by Funding 1 from the trust property. You should note that the obligation to make such payments may rank equally or in priority with payments made by Funding 1 to the issuing entity under the intercompany loan agreement. The terms of the new notes issued by any new Funding 1 issuing entity and the related new intercompany loan made to Funding 1 may result in such new notes and such new intercompany loan being repaid prior to the repayment of the notes and prior to the redemption of the intercompany loan.

You will not have any right of prior review or consent before Funding 1 enters into any new intercompany loans or the issuing entity or any new Funding 1 issuing entity issues the corresponding issuance of new notes. Similarly, the terms of the transaction documents (including, but not limited to, the mortgage sale agreement, the mortgages trust deed and the Funding 1 deed of charge), the definitions of the trigger events and the criteria for the sale of new loans to the mortgages trustee may be amended to reflect such issue of new notes by the new Funding 1 issuing entity and the making of the new intercompany loan to Funding 1. Your consent to these changes will not be required. There can be no assurance that these changes will not affect the cashflow available to pay amounts due on your notes. See “– **The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree modifications to the transaction documents without your prior consent, which may adversely affect your interests**” above.

Before the issuing entity or any new Funding 1 issuing entity issues any new notes, however, the issuing entity or such new Funding 1 issuing entity will be required to satisfy a number of conditions, including that the then current ratings of your notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified at the time of the issuance of such new notes by such new Funding 1 issuing entity.

There may be conflicts of interest between the issuing entity and any new Funding 1 issuing entity and their respective Funding 1 issuing entity security trustees, in which case it is expected that the Funding 1 security trustee will follow the directions given by the Funding 1 issuing entity security trustee representing the highest ranking class of notes or new notes (as applicable) then outstanding and, if each Funding 1 issuing entity security trustee represents the same class as their highest ranking class of notes or new notes (as applicable) then outstanding, then the Funding 1 issuing security trustee representing the greatest outstanding principal balance of the highest ranking class of notes or new notes (as applicable) then outstanding. The interests of the issuing entity and/or the directions of the issuing entity security trustee may not prevail in these circumstances, which may adversely affect your interests.

There may be conflicts of interest between the holders of notes and the holders of any new notes issued by the issuing entity and their respective issuing entity note trustees, in which case it is expected that the issuing entity security trustee will follow the directions given by the holders of the highest ranking class of notes or new notes of the issuing entity (as applicable) then outstanding and, if each issuing entity note trustee represents the same class as their highest ranking class of notes or new notes of the issuing entity (as applicable) then outstanding, then the issuing entity note trustee representing the greatest outstanding principal balance of the highest ranking class of notes or new notes of the issuing entity (as applicable) then outstanding. The interests of the noteholders and/or the directions of the note trustee may not prevail in these circumstances, which may adversely affect your interests.

**New Funding 1 issuing entities may share in the Funding 1 security and this may ultimately cause a reduction in the payments you receive on the notes**

Any new Funding 1 issuing entity may become party to the Funding 1 deed of charge and, if so, will be entitled to share in the security granted by Funding 1 for the benefit of the issuing entity (and the benefit of the other Funding 1 secured creditors) under the Funding 1 deed of charge. If the Funding 1 security is enforced and there are insufficient funds to make the payments that are due to all Funding 1 issuing entities, the issuing entity expects that Funding 1 issuing entity will only be entitled to its proportionate share of those limited funds. This could ultimately cause a reduction in the payments you receive on your notes.

**If the intercompany loan (or any part thereof) is refinanced your notes could be repaid early**

Funding 1 may refinance some or all of the intercompany loan through the proceeds of notes or new notes received from the issuing entity, the proceeds received from a new Funding 1 issuing entity under a new intercompany loan or payments received from the seller. The issuing entity or the new Funding 1 issuing entity would fund such loans through the issuance of notes or new notes. For example, a rated loan tranche outstanding under the intercompany loan might be re-financed in order to provide the issuing entity with funds to redeem a series and class of notes after their step-up date. If the proceeds of a refinanced rated loan tranche under the intercompany loan were used by the issuing entity to exercise an optional redemption of notes prior to their expected maturity, your notes could be repaid early. This, in turn, could have an adverse effect on the yield on your notes.

**The criteria for the sale of new loans to the mortgages trustee may change over time without your consent**

The criteria for new loans to be sold to the mortgages trustee may be amended in the future without your consent. As a result, the mortgages trust may include types of mortgage loans in the future with different characteristics from those currently in the mortgages trust. This may occur, for example, due to the development of new mortgage loan products in response to changing market conditions or sale of loans originated through different brands within the HBOS group or by different entities within the HBOS group. Any such amendments, as provided in the mortgage sale agreement, would require the consent of the parties to the mortgage sale agreement, including the Funding 1 security trustee. The sale of loans originated through different brands within the HBOS group or by different entities within the HBOS group to the mortgages trustee will be subject to receipt of confirmation from each of the rating agencies that its then rating of the notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result thereof.

**As new loans are sold to the mortgages trustee, the characteristics of the trust property may change from those existing at the date of this base prospectus, and those changes may adversely affect payments on the notes**

There is no guarantee that any new loans sold to the mortgages trustee will have the same characteristics as the loans in the portfolio as at the date of this base prospectus. In particular, new loans may have different payment characteristics from the loans in the portfolio as at the date of this base prospectus. The ultimate effect of this could be to delay or reduce the payments you receive on the notes. However, subject to “– **The criteria for the sale of new loans to the mortgages trustee may change over time without your consent**” above, any new loans will be required to meet the conditions described in “**Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**” below.

**The yield to maturity of the notes may be adversely affected by prepayments or redemptions on the loans**

The yield to maturity of the notes of each class will depend mostly on (a) the amount and timing of payment of principal on the loans and (b) the price paid by the noteholders of each class of notes.

The yield to maturity of the notes of each class may be adversely affected by a higher or lower than anticipated rate of prepayments on the loans. The factors affecting the rate of prepayment on the loans are described in “– **The issuing entity’s ability to redeem the notes is affected by the rate of prepayment on the loans**” below. See also “**Characteristics of the United Kingdom residential mortgage market**” in the applicable final terms.

No assurance can be given that Funding 1 will accumulate sufficient funds during the cash accumulation periods relating to bullet loan tranches or scheduled amortisation instalments to enable it to repay these bullet loan tranches or scheduled amortisation instalments to the issuing entity so that the corresponding series and classes of bullet notes and scheduled redemption notes respectively will be redeemed by the issuing entity in accordance with their scheduled redemption dates. During the cash accumulation period for the bullet loan tranches and scheduled amortisation instalments owed to the issuing entity, repayments of principal will only be made on the pass-through loan tranches that are due and payable if the CPR tests and certain cash accumulation shortfall and other repayment tests are met as described in “**Cashflows – Distribution of Funding 1 available principal receipts**” below. The extent to which sufficient funds are saved by Funding 1 during a cash accumulation period or received by it from its share of the mortgages trust for application on a scheduled repayment date will depend on whether the actual principal prepayment rate of the loans is the same as the assumed principal prepayment rate.

If Funding 1 is not able to save enough money during a cash accumulation period or does not receive enough money from its share in the mortgages trust to pay the full amount scheduled to be repaid on a bullet loan tranche or scheduled amortisation instalment on a scheduled repayment date and the issuing entity is therefore unable to redeem the corresponding series and class of bullet notes and scheduled redemption notes respectively on their scheduled redemption dates, then Funding 1 will be required to pay to the issuing entity on those scheduled redemption dates only the amount that it has actually saved or received. Accordingly, the issuing entity will only be obliged to pay the amount of funds received from Funding 1 to holders of the corresponding series and classes of notes. Any shortfall will be deferred and paid on subsequent Funding 1 interest payment dates when Funding 1 has money available to make the payment. In these circumstances, there will be a variation in the yield to maturity of the relevant class of notes.

During the cash accumulation period for a bullet loan tranche, payments of principal in respect of scheduled amortisation loan tranches will be restricted and may not be made if certain CPR tests and other repayment tests are not met as set out in “**Cashflows – Distribution of Funding 1 available principal receipts**” below. Additionally, during the cash accumulation period for a bullet loan tranche and/or a scheduled amortisation instalment, payments of principal on pass-through loan tranches will be restricted and may not be made if certain CPR, cash accumulation shortfall and other repayment tests are not met as set out in the repayment tests under “**Cashflows – Distribution of Funding 1 available principal receipts**” below.

**The issuing entity’s ability to redeem the notes is affected by the rate of prepayment on the loans**

The rate of prepayment of loans is influenced by a wide variety of economic, social and other factors, including prevailing mortgage market interest rates, local and regional economic conditions, homeowner mobility and the availability of financing. For instance, prepayments on the loans may be due to borrowers refinancing their loans and sales of properties by borrowers (either voluntarily or as a result of enforcement action taken). In addition, if the seller is required to repurchase a loan or loans under a mortgage account and their related security because, for example, one of the loans does not comply with the representations and warranties in the mortgage sale agreement or due to a further advance, a transfer of a portable loan or in limited circumstances a product switch, then the payment received by the mortgages trustee will have the same effect as a prepayment of all of the loans under that mortgage account. Because these factors are not within the issuing entity’s control or the control of Funding 1 or the mortgages trustee, no assurances can be given as to the level of prepayments that the portfolio may experience.

Variation in the rate of prepayments of principal on the loans may affect each series and class of notes differently depending upon amounts already repaid by Funding 1 to the issuing entity in respect of the corresponding loan tranche and whether a trigger event has occurred or a note acceleration notice or an intercompany loan acceleration notice has been given. If prepayments on the loans occur less frequently than anticipated, there may be insufficient funds available to the issuing entity to redeem notes of any series and class in full on their respective scheduled redemption dates.

The yield to maturity of each series and class of notes will depend mostly on the amount and timing of payment of principal on the loans and the price paid by the noteholders of such notes. The yield to maturity of each series and class of notes may be adversely affected by a higher or lower rate of prepayment on the loans, as described above.

**The seller may change the lending criteria relating to loans that are subsequently sold to the mortgages trustee, which could affect the characteristics of the trust property and which may adversely affect payments on the notes**

Each of the loans was and will be (other than loans originated by any new seller) originated in accordance with Birmingham Midshires' lending criteria at the time of origination. The lending criteria as at the date of this base prospectus are set out in the section "**The loans – Lending criteria**" below. These lending criteria consider a variety of factors such as a potential borrower's credit history, employment history and status and repayment ability, as well as the value of the property to be mortgaged. In the event of the sale by the seller of any new loans and new related security to the mortgages trustee, the seller will warrant that those new loans and new related security were originated in accordance with the seller's lending criteria at the time of their origination. However, the seller retains the right to revise its lending criteria as determined from time to time, and so the lending criteria applicable to any loan at the time of its origination may not be or have been the same as those set out in the section "**The loans – Lending criteria**" below.

If new loans that have been originated under revised lending criteria, or the lending criteria of a new seller are sold to the mortgages trustee, the characteristics of the trust property could change. This could lead to a delay or a reduction in the payments received on the notes.

**The loans of new sellers may be included in the portfolio**

New sellers may sell loans and their related security to the mortgages trustee. However, this would only be permitted if the conditions precedent relating to new sellers acceding to the programme (more fully described under "**Sale of loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**", below) are met.

Any loans originated by a new seller will have been originated in accordance with the lending criteria of such new seller, which may differ from the lending criteria of loans originated by the seller. If the lending criteria differ in a way that affects the creditworthiness of the loans, that may lead to increased defaults by borrowers and may affect the realisable value of the portfolio or any part thereof. This could lead to a delay or reduction in the payments received on the notes.

**Birmingham Midshires has adopted procedures relating to investigations and searches for remortgages which could affect the characteristics of the trust property and which may adversely affect payments on the notes**

Birmingham Midshires does not require a solicitor, licensed conveyancer or (in Scotland) qualified conveyancer to conduct a full investigation of the title to a property in all cases. Where the borrower is remortgaging there will be a limited investigation to carry out some but not all of the searches and investigations which would normally be carried out by a solicitor or conveyancer conducting a full investigation of the title to a property. Properties which have undergone such a limited investigation may be subject to matters which would have been revealed by a full investigation of title and which may have been remedied or, if incapable of remedy, may have resulted in the properties not being accepted as security for a loan had such matters been revealed. The introduction of loans secured by such properties into the trust property could result in a change of the characteristics of the trust property. This could lead to a delay or a reduction in the payments received on the notes.

**The timing and amount of payments on the loans could be affected by various factors which may adversely affect payments on the notes**

The loans are affected by credit, liquidity and interest rate risks. Various factors influence mortgage delinquency rates, prepayment rates, repossession frequency and the ultimate payment of interest and principal, such as changes in the national or international economic climate, regional economic or housing conditions, changes in tax laws, interest rates, inflation, the availability of financing, yields on alternative investments, political



developments and government policies. Other factors in borrowers' individual, personal or financial circumstances may affect the ability of borrowers to repay loans. Loss of earnings, illness, divorce and other similar factors may lead to an increase in delinquencies by and bankruptcies of borrowers, and could ultimately have an adverse impact on the ability of borrowers to repay loans.

If a borrower fails to repay its loan and the related property is repossessed, the likelihood of there being a net loss on disposition of the property is adversely affected by a higher debt-to-value ratio. In addition, the ability of a borrower to sell a property given as security for a loan at a price sufficient to repay the amounts outstanding under the loan will depend upon a number of factors, including the availability of buyers for that property, the value of that property and property values in general at the time. The applicable final terms will provide information on the distribution of the LTV ratios of the loans sold to the mortgages trustee in connection with a particular issuance of notes. See "**Statistical information on the portfolio – The cut-off date mortgage portfolio – Cut-off date LTV ratios**" in the applicable final terms.

In order to enforce a power of sale in respect of a property, the relevant mortgagee must first obtain possession of the relevant property. Possession is usually obtained by way of a court order although this can be a lengthy and costly process and will involve the mortgagee assuming certain risks. If obtaining possession of properties in such circumstances is lengthy or costly, the issuing entities' ability to service payments on the notes may be reduced.

The portfolio may also be subject to geographic concentration risks. To the extent that specific geographic regions within the United Kingdom have experienced or may experience in the future weaker regional economic conditions and housing markets than other regions, a concentration of the loans in such a region may be expected to exacerbate all of the risks relating to the loans described in this section. The economy of each geographic region within the United Kingdom is dependent on different mixtures of industries. Any downturn in a local economy or particular industry may adversely affect the regional employment levels and consequently the repayment ability of the borrowers in that region or the region that relies most heavily on that industry. Any natural disasters in a particular region may reduce the value of affected mortgaged properties. This may result in a loss being incurred upon sale of the mortgaged property. These circumstances could affect receipts on the loans and ultimately result in losses on the notes. For an overview of the geographical distribution of the loans sold to the mortgages trustee in connection with a particular issuance of notes, see "**Statistical information on the portfolio – The cut-off date mortgage portfolio – Geographical distribution**" in the applicable final terms.

The principal source of income for repayment of the notes by the issuing entity is the intercompany loan. The principal source of income for repayment by Funding 1 of the intercompany loan is its interest in the loans held on trust by the mortgages trustee for Funding 1 and the seller. If the timing and payment of the loans is adversely affected by any of the risks described in this section, then the payments on the notes could be reduced or delayed.

#### **The inclusion of certain types of loans may affect the rate of repayment and prepayment of the loans**

The portfolio contains flexible loans. Flexible loans provide the borrower with a range of options that gives that borrower greater flexibility in the timing and amount of payments made under the loan. Subject to the terms and conditions of the loans (which may require in some cases notification to the seller and in other cases the consent of the seller), under a flexible loan a borrower may (among other things) redraw amounts that have been repaid using available options set out in the relevant flexible option agreement. For a detailed summary of the characteristics of the flexible loans, see "**The loans – Characteristics of the loans – Flexible loans**" below.

To the extent that borrowers under flexible loans exercise any of the options available to them, the timing of payments on your notes may be adversely affected.

#### **Valuation of properties using an automated valuation model may result in a loss on the notes**

The portfolio contains some loans secured on properties valued using an automated valuation model to determine the value of the property. The accuracy of such automated valuation models are based on available prior valuation information on the related property and on the existence of a sufficient amount of similar properties that have been valued or sold recently in the vicinity of the related property. As a result, automated valuation models tend to be less accurate when valuing properties with unique features and properties located in sparsely populated areas with little property turnover. In addition, automated valuation models may have a tendency to overvalue low-value properties and undervalue high-value properties. Potential losses arising from the use of the automated valuation models are not insured by any third-party insurer. Although Birmingham Midshires has taken measures to limit the circumstances in which an automated valuation model is used (as described under "**The loans – Valuation**" below), if any properties are overvalued due to the use of an automated valuation model, the related loan-to-value ratio is likely to be underestimated, which may result in a greater than expected loss upon the default of the related loans and subsequent sale of the related property. See "**Statistical information on the**

**portfolio – The cut off dated mortgage portfolio – Accounts originated using an automated valuation model”** in the applicable final terms.

**Competition in the United Kingdom mortgage loan industry could increase the risk of an early redemption of your notes**

The mortgage loan industry in the United Kingdom is highly competitive. Both traditional and new lenders use heavy advertising, targeted marketing and aggressive pricing in an effort to expand their presence in or to facilitate their entry into the market and compete for customers.

This competitive environment may affect the rate at which Birmingham Midshires originates new mortgage loans and may also affect the level of attrition of Birmingham Midshires’ existing borrowers. If the rate at which new mortgage loans are originated declines significantly or if existing borrowers refinance their mortgage loans with lenders other than Birmingham Midshires then the risk of a trigger event occurring increases, which could result in an early redemption of your notes.

**You may not be able to sell the offered notes**

There currently is no secondary market for the notes to be issued on a closing date (the **offered notes**). If no secondary market develops, you may not be able to sell the offered notes prior to their maturity. The issuing entity cannot offer any assurance that a secondary market will develop or, if one does develop, that it will continue to exist.

**No market for the offered notes; lack of liquidity**

The offered notes are a new issue of securities for which there is currently no market. Neither the issuing entity nor the dealers intend to create a market for the offered notes. Accordingly, no assurance can be given as to the development or liquidity of any market for the offered notes. Because there is currently no market for the offered notes, investors must be able to bear the risks of their investment in the offered notes for an indefinite period of time.

**Lack of liquidity in the secondary market may adversely affect the market value of your notes**

The secondary mortgage markets are currently experiencing severe disruptions resulting from reduced investor demand for mortgage loans and mortgage-backed securities and increased investor yield requirements for those loans and securities. As a result, the secondary market for mortgage-backed securities is experiencing extremely limited liquidity. These conditions may continue or worsen in the future.

Limited liquidity in the secondary market for mortgage-backed securities has had a severe adverse effect on the market value of mortgage-backed securities. Limited liquidity in the secondary market may continue to have a severe adverse effect on the market value of mortgage-backed securities, especially those securities that are more sensitive to prepayment, credit or interest rate risk and those securities that have been structured to meet the investment requirements of limited categories of investors. Consequently, you may not be able to sell your notes readily at the time of their issuance. The market values of the notes may fluctuate. Any of these fluctuations may be significant and could result in significant losses to you.

In addition, the forced sale into the market of mortgage-backed securities held by structured investment vehicles, hedge funds, issuers of collateralised debt obligations and other similar entities that are currently experiencing funding difficulties could adversely affect your ability to sell, and/or the price you receive for, your notes in the secondary market.

**Increases in prevailing market interest rates may adversely affect the performance and market value of your notes**

Borrowers seeking to avoid increased monthly payments (caused by, for example, the expiry of an initial fixed rate or low introductory rate, or a rise in the related mortgage interest rates) by refinancing their mortgage loans may no longer be able to find available replacement loans at comparably low interest rates. Any decline in housing prices may also leave borrowers with insufficient equity in their homes to permit them to refinance. These events, alone or in combination, may contribute to higher delinquency rates and losses.

**If property values decline, payments on the notes could be adversely affected**

The security granted by Funding 1 in respect of the intercompany loan, which is the principal source of funding for your notes, consists, among other things, of Funding 1’s interest in the mortgages trust. Since the value of the portfolio held by the mortgages trustee may increase or decrease, the value of that security will decrease if there is a general decline in property values.

During 2007 and early 2008 the rate of house price inflation fell as a consequence of housing demand being constrained by a combination of subdued earnings growth, greater pressure on household finances, higher interest rates and the effect of the continuing global market volatility that began in the summer of 2007.

Should house prices continue to decline, borrowers may have insufficient equity to refinance their mortgage loans with lenders other than the seller. This could lead to higher delinquency rates and losses.

The principal source of income for repayment of the notes by the issuing entity is the intercompany loan. The principal source of income for repayment by Funding 1 of the intercompany loan is its interest in the loans held on trust by the mortgages trustee for Funding 1 and the seller. If the timing and payment of the loans is adversely affected by any of the risks described in this section, then the payments on the notes could be reduced or delayed.

**The occurrence of trigger events and service of a note acceleration notice and/or an intercompany loan acceleration notice may adversely affect the scheduled redemption dates of any bullet notes or scheduled amortisation notes then outstanding**

Prior to the occurrence of a trigger event or service of a note acceleration notice, payments of principal will not occur on any bullet notes or scheduled amortisation notes before their respective scheduled redemption dates.

Following the occurrence of a trigger event or service of a note acceleration notice prior to the scheduled redemption dates for any bullet notes or scheduled amortisation notes, any such bullet notes or scheduled amortisation notes outstanding will not be repaid on their scheduled redemption dates, but will be repaid on each interest payment date from monies received from Funding 1 on the corresponding loan tranches as described below. There is also a risk that the bullet notes and/or the scheduled amortisation notes then outstanding will not be repaid by their final maturity date.

**No new loans may be sold to the mortgages trustee if the step-up date in respect of any notes issued by the issuing entity has occurred and the issuing entity has not exercised its option to redeem the notes**

No sale of new loans may occur if, at the relevant sale date, the step-up date in respect of any series and class of notes has occurred and the issuing entity has not exercised its option to redeem the relevant series and class of notes as at that date. If the minimum trust size is not maintained, then this could result in the occurrence of a non-asset trigger event. See “Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates” for further details of the conditions new loans are required to meet.

**The occurrence of a non-asset trigger event may accelerate the repayment of certain notes and/or delay the repayment of other notes**

If a non-asset trigger event has occurred and until the occurrence of an asset-trigger event and/or the service of a note acceleration notice and/or an intercompany loan acceleration notice, the mortgages trustee will distribute all principal receipts to Funding 1 until the Funding 1 share percentage is zero and will thereafter apply all principal receipts to the seller. Funding 1 will, on each Funding 1 interest payment date following the occurrence of a non-asset trigger event and until the occurrence of an asset-trigger event and/or the service of a note acceleration notice and/or an intercompany loan acceleration notice, apply these principal receipts received by it from the mortgages trustee, after making the requisite payments to the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any), to repay:

- *first*, the AAA loan tranches in order of final repayment date, beginning with the earliest final repayment date until each of those AAA loan tranches is fully repaid;
- *then*, the AA loan tranches until each of those AA loan tranches is fully repaid;
- *then*, the A loan tranches until each of those A loan tranches is fully repaid;
- *then*, the BBB loan tranches until each of those BBB loan tranches is fully repaid;
- *then*, the BB loan tranches until each of those BB loan tranches is fully repaid;
- *then*, the subordinated loan tranches until the subordinated loan tranches are fully repaid.

The above priority of payments may cause certain series and classes of notes to be repaid more rapidly than expected and other series and classes of notes to be repaid more slowly than expected and there is a risk that such notes may not be repaid by their final maturity date.

**The occurrence of an asset trigger event and/or service of a note acceleration notice and/or an intercompany loan acceleration notice may accelerate the repayment of certain notes and/or delay the repayment of other notes**

If an asset trigger event has occurred, the mortgages trustee will distribute principal receipts on the loans to Funding 1 and the seller proportionally based on their percentage shares of the trust property. Funding 1 will, on each Funding 1 interest payment date following the occurrence of an asset trigger event or the service of a note acceleration notice and/or an intercompany loan acceleration notice, apply those principal receipts received by it from the mortgages trustee, after making the requisite payments (i) to the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any) (other than in the case of the Funding 1 post-enforcement priority of payments) or (ii) to Funding 1's prior ranking secured creditors, to repay:

- *first*, the AAA loan tranches in order of final repayment date, beginning with the earliest final repayment date until each of those AAA loan tranches is fully repaid;
- *then*, the AA loan tranches until each of those AA loan tranches is fully repaid;
- *then*, the A loan tranches until each of those A loan tranches is fully repaid;
- *then*, the BBB loan tranches until each of those BBB loan tranches is fully repaid;
- *then*, the BB loan tranches until each of those BB loan tranches is fully repaid; and
- *then*, the subordinated loan tranches until each of those subordinated loan tranches is fully repaid.

The above priority of payments may cause certain series and classes of notes to be repaid more rapidly than expected and other series and classes of notes to be repaid more slowly than expected and there is a risk that such notes may not be repaid by their final maturity date.

**Loans subject to further advances will be repurchased by the seller from the mortgages trustee, which will affect the prepayment rate of the loans and this may affect the yield to maturity of the notes**

If the seller at its discretion decides to grant a borrower a further advance under a loan which has been sold to the mortgages trustee, then the seller will be required at the direction of Funding 1 to repurchase that loan under the relevant mortgage account and its related security from the mortgages trustee (save for any loan in arrears) at a price equal to the outstanding principal balance of those loans, including accrued and unpaid interest and expenses to the date of purchase. The yield to maturity of the notes may be affected by the repurchase of loans subject to further advances.

**In limited circumstances, loans subject to product switches will be repurchased by the seller from the mortgages trustee, which will affect the prepayment rate of the loans and this may affect the yield to maturity of the notes**

A loan will be subject to a product switch if the borrower and Birmingham Midshires agree on, or the servicer sends an offer of, a variation in the financial terms and conditions applicable to the relevant borrower's loan other than those variations set out in "Sale of the loans and their related security – Product switches" below.

Loans subject to product switches will not be repurchased unless on any distribution date, the seller is in breach of the conditions precedent to the sale of new loans to the mortgages trustee set out in "Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates" below. From and including that date to but excluding the date when those conditions precedent have been satisfied, the seller will be required at the direction of Funding 1 to repurchase any loans and their related security that are subject to product switches (save for any loans in arrears). The seller will be required to repurchase the relevant loan or loans under the relevant mortgage account and their related security from the mortgages trustee at a price equal to the outstanding principal balance of those loans, including accrued and unpaid interest and expenses to the date of purchase.

The yield to maturity of the notes may be affected by the repurchase of loans subject to product switches.

**Portable loans will be repurchased by the seller from the mortgages trustee, which will affect the prepayment rate of the loans and this may affect the yield to maturity of your notes**

Portable loans will be repurchased on the instruction of Funding 1 if the borrower transfers the loan balance at the same interest rate and subject to all the existing terms and conditions to a new property, as described in the “**Sale of loans and their related security – portable loans**”. If the seller is required to repurchase any such portable loans and their related security from the mortgages trustee, the repurchase price will be equal to the outstanding principal balance of those loans, including accrued and unpaid interest and expenses to the date of purchase on the London business day immediately following the transfer date.

The yield to maturity of your notes may be affected by the repurchase of portable loans.

**Ratings assigned to the notes may be lowered or withdrawn after you purchase the notes, which may lower the market value of the notes**

The ratings assigned to each class of notes address the likelihood of full and timely payment to you of all payments of interest on each interest payment date under those classes of notes. The ratings also address the likelihood of ultimate payment of principal on the final maturity date of each class of notes. The expected ratings of a series and class of notes offered under this base prospectus will be set out in the final terms for that series and class of notes. Any rating agency may lower its rating or withdraw its rating if, in the sole judgment of the rating agency, the credit quality of the notes has declined or is in question. If any rating assigned to the notes is lowered or withdrawn, the market value of the notes may be reduced.

**Ratings confirmation in relation to the notes in respect of certain actions**

The terms of certain transaction documents require that certain actions proposed to be taken by the mortgages trustee, the Funding 1 security trustee, the issuing entity security trustee, the note trustee, Funding 1, the issuing entity or certain other parties to the transaction documents may not proceed unless each of the rating agencies confirms that the proposed action will not result in a reduction, withdrawal or (in the case of S&P and Moody's) qualification of its then ratings of the then outstanding notes (a **ratings confirmation**).

By acquiring the notes, you acknowledge and agree that, notwithstanding the foregoing, a credit rating is an assessment of credit risk and does not address other matters that may be of relevance to you. A ratings confirmation does not, for example, confirm that such action (i) is permitted by the terms of the transaction documents or (ii) is in the best interests of, or prejudicial to, you. While each of the Funding 1 secured creditors and the issuing entity secured creditors (including the noteholders) are entitled to have regard to a ratings confirmation, the above does not impose or extend any actual or contingent liability on the rating agencies to the Funding 1 secured creditors or the issuing entity secured creditors (including the noteholders), the mortgages trustee, the Funding 1 security trustee, the issuing entity security trustee, the note trustee or any other parties to the transaction documents or create any legal relationship between the rating agencies and the Funding 1 secured creditors, the issuing entity secured creditors (including the noteholders), the mortgages trustee, the Funding 1 security trustee, the issuing entity security trustee, the note trustee or any other parties to the transaction documents whether by way of contract or otherwise.

Any such ratings confirmation may or may not be given at the sole discretion of each rating agency. It should be noted that, depending on the timing of delivery of the request and any information needed to be provided as part of any such request, it may be the case that a rating agency cannot provide a ratings confirmation in the time available or at all and the rating agency should not be responsible for the consequences thereof. A ratings confirmation, if given, will be given on the basis of the facts and circumstances prevailing at the relevant time and in the context of cumulative changes to the transaction of which the securities form part since the relevant closing date. A ratings confirmation represents only a restatement of the opinions given as at the relevant time and cannot be construed as advice for the benefit of any parties to the transaction.

In accordance with Condition 16, if (a) a confirmation of rating or other response by a rating agency is a condition to any action or step under any transaction document (other than pursuant to condition 15), (b) a written request for such confirmation or response is delivered to each rating agency by the issuing entity and either one or more rating agency (each a **non-responsive rating agency**) indicates that it does not consider such confirmation or response necessary in the circumstances and (c) at least one rating agency gives such a confirmation or response based on the same facts, then such condition shall be deemed to be modified with respect to the facts set out in the request referred to in (b) so that there will be no requirement for the confirmation or response from the non-responsive rating agency.

**Risks related to money market notes**

Notes designated in the applicable final terms as money market notes will be “Eligible Securities” within the meaning of Rule 2a-7 under the Investment Company Act. However, under Rule 2a-7, a money market fund may be required to dispose of the money market notes upon the occurrence of any of the following events:

- the rating currently assigned to the money market notes is lowered or withdrawn;
- a material default occurs with respect to the money market notes;
- the money market fund determines that the money market notes no longer present minimal credit risk;
- upon certain events of insolvency with respect to the issuing entity; or
- the money market notes otherwise cease to meet the eligibility criteria under Rule 2a-7.

Where the issuing entity has entered into a 2a-7 swap provider arrangement, money market note purchase agreement or remarketing agreement in respect of a series and class of money market notes, the eligibility of the notes for investment by money market funds will be dependent upon timely receipt of proceeds from the 2a-7 swap provider, money market note purchaser, remarketing agent or conditional purchaser.

The ability of the remarketing bank to procure payment of the transfer price on a transfer date will depend upon the remarketing bank either (a) procuring third party purchasers for any tendered notes prior to the relevant transfer date and obtaining the transfer price from those third party purchasers or (b) exercising the issuing entity’s rights under the conditional purchase agreement to require the conditional note purchaser to acquire the unremarketed notes. After the occurrence of a mandatory transfer termination event, the remarketable notes will no longer be subject to any mandatory transfer.

There can be no assurance that the remarketing bank will be able to identify purchasers willing to acquire the tendered notes on a transfer date. In such event the transfer of any unremarketed notes would be dependent upon the ability of the conditional purchaser to pay the transfer price and acquire unremarketed notes.

You should consider carefully the risk posed if your tendered notes cannot be remarketed on a transfer date and either (a) the conditions to the conditional note purchaser’s obligation to purchase unremarketed notes are not satisfied or (b) the conditional note purchaser defaults in its obligation to purchase unremarketed notes under the conditional purchase agreement. In those situations you may be unable to sell your notes on the relevant transfer date or at any other time.

If a 2a-7 swap provider swap arrangement is specified as applying to a certain series and class of notes in the relevant final terms, the 2a-7 swap provider will be required to make a principal payment under the relevant issuing entity swap agreement to the issuing entity to enable the issuing entity to redeem the series and class of notes in full on their bullet repayment date notwithstanding that the 2a-7 swap provider has not received the corresponding principal payment required to be made by the issuing entity under the relevant issuing entity swap agreement. A failure by the issuing entity to make the full principal repayment on the bullet repayment date of the loan tranche corresponding to the relevant series and class of notes for which the relevant issuing entity swap was entered into will not constitute an event of default or a termination event under that swap. In such circumstances, noteholders in respect of such notes will be dependent on the performance of the 2a-7 swap provider and no assurance can be given that the issuing entity will have sufficient funds to make payments due on the relevant series and class of notes.

Neither the issuing entity nor any of the dealers, the managers, any remarketing bank or any conditional note purchaser will make any representation as to the suitability of the money market notes for investment by money market funds subject to Rule 2a-7 under the Investment Company Act. Any determination as to such suitability or compliance with Rule 2a-7 under the United States Investment Company Act is solely your responsibility.

### **Issuance of notes may affect the timing and amounts of payments to you**

The issuing entity expects to issue notes from time to time. Notes may be issued from time to time without notice to existing noteholders and without their consent, and may have different terms from the then outstanding notes. For a description of the conditions that must be met before the issuing entity can issue notes, see “**Overview of the notes – Issuance**” above.

The issuance of notes could adversely affect the timing and amount of payments on the then outstanding notes. For example, if notes of the same class as your notes issued after your notes have a higher interest rate than your notes, this could result in a reduction in the available funds used to pay interest on your notes. Also, the voting rights of your notes will be diluted.

**Principal payments on the original pass-through loan tranches and the subordinated loan tranches will be deferred in some circumstances**

Principal repayments on the AA loan tranches, the A loan tranches, the BBB loan tranches, the BB loan tranches and the subordinated loan tranches will be deferred in the following circumstances:

If on a Funding 1 interest payment date:

- there is a debit balance on the BB principal deficiency sub-ledger, BBB principal deficiency sub-ledger, the A principal deficiency sub-ledger or the AA principal deficiency sub-ledger, after application of the Funding 1 available revenue receipts on that Funding 1 interest payment date; or
- the adjusted Funding 1 general reserve fund level is less than the Funding 1 general reserve fund threshold; or
- the aggregate outstanding principal balance of loans in the mortgages trust, in respect to which the aggregate amount in arrears is more than three times the monthly payment then due, is more than 5 per cent. of the aggregate outstanding principal balance of loans in the mortgages trust,

then (i) if any AAA loan tranches remain outstanding (whether or not such AAA loan tranches are then due and payable) after the allocation of principal on that Funding 1 interest payment date to those loan tranches, the AA loan tranches will not be entitled to principal repayments until the relevant circumstance as described above has been remedied or otherwise ceases to exist, (ii) if any AA loan tranches remain outstanding (whether or not such AA loan tranches are then due and payable) after the allocation of principal on that Funding 1 interest payment date to those loan tranches, the A loan tranches will not be entitled to principal repayments until the relevant circumstances as described above have been remedied or otherwise cease to exist, (iii) if any A loan tranches remain outstanding (whether or not such A loan tranches are then due and payable) after the allocation of principal on that Funding 1 interest payment date to those loan tranches, the BBB loan tranches will not be entitled to principal repayments until the relevant circumstances as described above have been remedied or otherwise cease to exist, (iv) if any BBB loan tranches remain outstanding (whether or not such BBB loan tranches are then due and payable) after the allocation of principal on that Funding 1 interest payment date to those loan tranches, the BB loan tranches will not be entitled to principal repayments until the relevant circumstances as described above have been remedied or otherwise cease to exist and (v) if any BB loan tranches remain outstanding (whether or not such BB loan tranches are then due and payable) after the allocation of principal on that Funding 1 interest payment date to those loan tranches, the subordinated loan tranches will not be entitled to principal repayments until the relevant circumstances described above have been remedied or otherwise cease to exist. This means that payments of principal on the class D notes of all series, the class C notes of all series, the class M notes of all series and, as applicable, the class B notes of all series and all subordinated loans will be deferred until the earlier of the time when the relevant circumstance described in this risk factor has been remedied (if ever) and the final maturity date of the relevant notes.

Furthermore, if, on a Funding 1 interest payment date:

- one or more bullet loan tranches and/or scheduled amortisation instalments are then in a cash accumulation period; and
- the quarterly CPR is less than 15 per cent.; and
- there is a cash accumulation shortfall at that time,

then, on or before their step-up dates, the loan tranches which are original pass-through loan tranches will be entitled to principal repayments only to the extent permitted under the pass-through repayment restrictions see **“Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes”**.

**All notes outstanding may be subject to risk if the trust property deteriorates after repayment of previous series and classes of the notes**

If the loans comprising the trust property do not perform as expected at any time after the repayment of previous series and classes of notes, then the unpaid series and classes of notes will be adversely affected.

**You may be subject to risks relating to exchange rates or interest rates on the notes**

Repayments of principal and payments of interest on a series and class of notes may be made in a currency other than sterling but the intercompany loan made by the issuing entity to Funding 1 and repayments of principal and payments of interest by Funding 1 to the issuing entity under the intercompany loan will be in sterling. In addition, interest due and payable by Funding 1 to the issuing entity on any loan tranche under the intercompany loan agreement will be calculated by reference to LIBOR for three-month sterling deposits or, for some loan tranches, such other sterling LIBOR rate as may be specified in the applicable loan tranche supplement, each plus or minus a margin, but interest due and payable on a series and class of notes may be calculated by reference to a fixed or a different floating rate (as set out in the applicable final terms).

To hedge the issuing entity's currency exchange rate exposure and/or interest rate exposure in such cases, on the relevant closing date for a series and class of notes, the issuing entity will (where applicable) enter into appropriate currency and/or interest rate swap transactions for such series and classes of notes with an issuing entity swap provider as specified in the applicable final terms. See "**The swap agreements**" below.

Each issuing entity swap provider is obliged to make payments under an issuing entity swap only for so long as and to the extent that the issuing entity makes its timely payments under it. If such issuing entity swap provider is not obliged to make payments of, or if it defaults in its obligations to make payments of, amounts equal to the full amount scheduled to be paid to the issuing entity on the dates for payment specified under the relevant issuing entity swap or such issuing entity swap is otherwise terminated, the issuing entity will be exposed to changes in the exchange rates between sterling and the currency in which such series and class of notes are denominated and/or in the relevant interest rates applicable to such series and class of notes. Unless a replacement swap transaction is entered into, the issuing entity may have insufficient funds to make payments due on the applicable series and class of notes.

**There may be a delay in payment of interest on money market notes on the occurrence of a trigger event or service of a note acceleration notice**

After the occurrence of a trigger event or service of a note acceleration notice, the interest payments on the money market notes will no longer be payable monthly, but will be payable quarterly. In these circumstances a noteholder will not receive interest under the monthly pay notes on the expected interest payment dates.

**Risks associated with the Funding 1 swap**

To provide a hedge against (a) the standard variable rate payable on the standard variable rate loans, the rates of interest payable on the tracker rate loans and the fixed rates of interest payable on the fixed rate loans and (b) the rate of interest payable by Funding 1 on the loan tranches under the intercompany loan agreement, Funding 1 has entered into the Funding 1 swap agreement. If Funding 1 fails to make timely payments under the Funding 1 swap, it will have defaulted under the Funding 1 swap. The Funding 1

swap provider is obliged only to make payments under the Funding 1 swap if and for so long as Funding 1 makes payments under the same. If the Funding 1 swap provider is not obliged to make payments, if it exercises any right that it may have under the Funding 1 swap to terminate the Funding 1 swap, if it defaults in its obligation to make payments under the Funding 1 swap or if such Funding 1 swap is otherwise terminated, Funding 1 will be exposed to the variance between the rates of interest payable on the loans and the rate of interest payable by it under the intercompany loan unless a replacement Funding 1 swap is entered into. If the Funding 1 swap terminates, Funding 1 may as a result be obliged to make a termination payment to the Funding 1 swap provider. Any variance between the rates of interest payable on the loans and the rate of interest payable by Funding 1 in respect of the loan tranches under the intercompany loan and any termination payment payable by it to the Funding 1 swap provider may adversely affect the ability of Funding 1 to meet its obligations under the intercompany loan agreement (see also "**Funding 1 is not obliged to make payments on the loan tranches if it does not have enough money to do so, which could adversely affect payments on the notes**" above).

Funding 1 will receive interest receipts on the loans on one basis but will pay amounts under the Funding 1 swap on another basis, thereby exposing it to some basis risk. On the one hand, Funding 1 will receive interest on the standard variable rate loans based on the standard variable rate. On the other hand, the payment obligations of Funding 1 under the Funding 1 swap will, among other things, be based on the average of the standard variable mortgage rates or their equivalent charged to existing borrowers on residential mortgage loans as published from



time to time, after excluding the highest and the lowest rate, of Abbey National plc, HSBC Bank plc, Cheltenham & Gloucester plc, Nationwide Building Society, Northern Rock plc, National Westminster Bank Plc and Woolwich plc (and, where those banks have more than one standard variable rate, the highest of those rates). While it is anticipated that this average rate will broadly track Birmingham Midshires' variable rate, the variance between this average rate and Birmingham Midshires' variable rate may affect the ability of Funding 1 to meet its payment obligations under the Funding 1 swap agreement.

**Termination payments on the issuing entity swaps may adversely affect the funds available to make payments on a series and class of notes**

If any of the issuing entity swaps terminates, the issuing entity may as a result be obliged to make a termination payment to the relevant issuing entity swap provider. The amount of the termination payment will be based on the cost of entering into a replacement issuing entity swap. Under the intercompany loan agreement, Funding 1 will be required to pay the issuing entity an amount equal to any termination payment due by the issuing entity to the relevant issuing entity swap provider. Funding 1 will also be obliged to pay the issuing entity any extra amounts which the issuing entity may be required to pay to enter into a replacement swap.

The issuing entity cannot give any assurance that Funding 1 will have the funds available to make that payment or that the issuing entity will have sufficient funds available to make any termination payment under any of the issuing entity swaps or to make subsequent payments to you in respect of the relevant series and class of notes. Nor can the issuing entity give any assurance that the issuing entity will be able to enter into a replacement issuing entity swap or, if one is entered into, that the credit rating of the replacement issuing entity swap provider will be sufficiently high to prevent a downgrading of the then current ratings of the relevant series and class of notes by the rating agencies.

Except where the relevant issuing entity swap provider has caused the relevant issuing entity swap to terminate by its own default or failure to comply with applicable ratings downgrade provisions, any termination payment due by the issuing entity will rank equally not only with payments of interest due to the holders of the series and class of notes to which the relevant issuing entity swap relates but also with payments of interest due to the holders of any other series and class of notes which rank equally with the series and class of notes to which the relevant issuing entity swap relates. Any additional amounts required to be paid by the issuing entity following termination of the relevant issuing entity swap (including any extra costs incurred (for example, from entering into "spot" currency transactions or interest rate swaps) if the issuing entity cannot immediately enter into a replacement issuing entity swap) will also rank equally not only with payments of interest due to the holders of the series and class of notes to which the relevant issuing entity swap relates but also with payments of interest due to the holder of any other series and class of notes which rank equally with the series and class of notes to which the relevant issuing entity swap relates. Furthermore, any termination payment or additional payment or additional amounts required to be paid by the issuing entity following termination of an issuing entity swap will rank ahead of payments due to the holders of any series and class of notes which ranks below the series and class of notes to which the relevant issuing entity swap relates. Therefore, if the issuing entity is obliged to make a termination payment to the relevant issuing entity swap provider or to pay any other additional amount as a result of the termination of the relevant issuing entity swap, this may affect the funds which the issuing entity has available to make payments on a series and class of notes. See "**The swap agreements – Termination of the swaps**" below.

**The issuing entity relies on third parties to perform services in relation to the notes, and you may be adversely affected if they fail to perform their obligations**

The issuing entity is a party to contracts with a number of third parties that have agreed to perform services in relation to the notes. For example, the issuing entity swap providers have agreed or will agree to provide their respective issuing entity swaps, the corporate services provider has agreed to provide corporate services and the paying agents and the agent bank have agreed to provide payment and calculation services in connection with the notes. In the event that any of these parties were to fail to perform their obligations under the respective agreements to which they are a party, you may be adversely affected.

**The mortgages trustee GIC provider or the Funding 1 GIC provider may cease to satisfy certain criteria to provide the mortgages trustee GIC account or the Funding 1 GIC account**

The mortgages trustee GIC provider and the Funding 1 GIC provider are required to satisfy certain criteria (including certain criteria and/or permissions set or required by the FSA from time to time) in order to continue to receive deposits in the mortgages trustee GIC account and the Funding 1 GIC account respectively. If either the mortgages trustee GIC provider or the Funding 1 GIC provider ceases to satisfy those criteria then the relevant account may be transferred to another entity which does satisfy those criteria. In these circumstances the new GIC provider may not offer a GIC on terms as favourable as those provided by the mortgages trustee GIC provider or the Funding 1 GIC provider.

The criteria referred to above include a requirement that the short-term, unguaranteed and unsecured debt ratings of the mortgages trustee GIC provider or the Funding 1 GIC provider, as the case may be, are at least F1 by Fitch, P-1 by Moody's and A-1+ by Standard & Poor's, unless each rating agency confirms that its then current rating of the notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of such ratings falling below these minimum ratings.

**Excess revenue receipts available to Funding 1 may not be sufficient to replenish principal that has been used to pay interest due on loan tranches, which may result in your notes not being repaid in full**

If, on any distribution date, revenue receipts available to Funding 1 (including the Funding 1 reserve funds) are insufficient to enable it to pay interest on the rated loan tranches to the issuing entity and its other expenses ranking in priority to interest due on rated loan tranches, then Funding 1 may use principal receipts received from the mortgages trustee to make up that revenue shortfall.

Funding 1 will use principal receipts that would have been applied to repay the subordinated loan tranche and, then, the rated loan tranches with the lowest rating designation to pay interest on those other rated loan tranches and senior expenses described in the preceding paragraph where there is a shortfall of monies to pay those amounts. If Funding 1 uses principal to repay interest and senior expenses in this manner, there will be less principal available to repay the subordinated loan tranches, then the BB loan tranches, then the BBB loan tranches, then the A loan tranches, then the AA loan tranches and finally the AAA loan tranches at which point an asset trigger event will occur. In such event, there will be a corresponding reduction in principal available to repay the issuing entity subordinated loans, then the class D notes, then the class C notes, then the class M notes, then the class B notes and finally the class A notes, at which point a note event of default will occur.

Funding 1 is obliged to keep a ledger that records any principal applied to pay interest and senior expenses (as well as any losses on the loans causing a principal deficiency). When the amount recorded on the subordinated loan principal deficiency sub-ledger is equal to the principal amount outstanding of the subordinated loan tranches, then Funding 1 will use principal receipts that would have been applied to repay the subordinated loan tranches to pay interest on the rated loan tranches and senior expenses where there is a shortfall of money to pay those amounts. When the amount recorded on the BB principal deficiency sub-ledger is equal to the principal amount outstanding of the BB loan tranches, then Funding 1 will use principal receipts that would have been applied to repay the BBB loan tranches to pay those amounts. When the amount recorded on the BBB principal deficiency sub-ledger exceeds the principal amount outstanding on the BBB loan tranches, Funding 1 will use principal receipts that would have been applied to repay the A loan tranches to pay those amounts. When the amount recorded on the A principal deficiency sub-ledger exceeds the principal amount outstanding on the A loan tranches, Funding 1 will use principal receipts that would have been applied to repay the AA loan tranches to pay those amounts. When the amount recorded on the AA principal deficiency sub-ledger exceeds the principal amount outstanding on the AA loan tranches, Funding 1 will use principal receipts that would have been applied to repay the AAA loan tranches to pay those amounts.

During the term of the programme, however, it is expected that these principal deficiencies will be recouped from subsequent excess Funding 1 available revenue receipts and amounts standing to the credit of the Funding 1 reserve funds.

The revenue receipts will be applied first to cover any principal deficiency in respect of the loan tranches with the highest rating designation, and then the loan tranches with the next highest rating designation and so on down to the loan tranches with the lowest rating designation.

If there are insufficient funds available because of revenue or principal deficiencies, then one or more of the following consequences may occur:

- the interest and other net income of the issuing entity may not be sufficient, after making the payments to be made in priority, to pay, in full or at all, interest due on the subordinated loan tranches, the BB loan tranches, the BBB loan tranches, the A loan tranches and the AA loan tranches;
- there may be insufficient funds to repay the principal due and payable on any of the subordinated loan tranches, the BB loan tranches, the BBB loan tranches, the A loan tranches and the AA loan tranches prior to their final repayment dates unless the other net income of Funding 1 is sufficient, after making other prior ranking payments, to reduce any principal deficiency in respect of the subordinated loan tranches, the BB loan tranches, the BBB loan tranches, the A loan tranches and the AA loan tranches;

- if the amount of principal deficiencies exceeds the principal amount outstanding of any of the subordinated loan tranches or the rated loan tranches (and the principal deficiencies cannot be covered by the other income of Funding 1), then the issuing entity may not receive the full principal amount of any or all of the subordinated loan tranches or the rated loan tranches and, accordingly, the issuing entity subordinated loan tranches may not be repaid or you may not receive the full principal amount of the class D notes, the class C notes, the class M notes, the class B notes and the class A notes, as the case may be; and/or
- the issuing entity may be unable to pay, in full or at all, interest due on the subordinated loan tranches or the class D Notes, the class C notes, the class M notes, the class B notes or the class A notes, as the case may be.

For more information on principal deficiencies, see “**Credit structure – Funding 1 principal deficiency ledger**” below.

**The seller share does not provide credit enhancement for the notes**

Any losses from loans included in the trust property will be allocated to Funding 1 and the seller proportionally on each distribution date in accordance with the Funding 1 share percentage and the seller share percentage respectively of the trust property. The seller share therefore does not provide credit enhancement for the Funding 1 share or the notes. Losses on the loans in the portfolio are allocated proportionately among the seller Funding 1 and, if applicable, any further funding beneficiary, depending on their respective shares in the trust property.

**The issuing entity will only have recourse to the seller if there is a breach of warranty by the seller, but otherwise the seller’s assets will not be available to the issuing entity as a source of funds to make payments on the notes**

After an intercompany loan acceleration notice is given (as described in “**The intercompany loan agreement – intercompany loan events of default**” below and “**Security for Funding 1’s obligations**” below), the Funding 1 security trustee may, but shall not be obliged to, sell the Funding 1 share. There is no assurance that a buyer would be found or that such a sale would realise enough money to repay amounts due and payable under the intercompany loan agreement.

The issuing entity, the issuing entity security trustee and the note trustee will not, and Funding 1, the Funding 1 security trustee and the mortgages trustee will not other than in respect of a breach of warranty under the mortgage sale agreement, have any recourse to the seller.

None of the issuing entity, the issuing entity security trustee, the note trustee, the mortgages trustee, Funding 1 or the Funding 1 security trustee will not undertake any investigations, searches or other actions on any loan or its related security but instead will rely solely on the warranties given in the mortgage sale agreement by the seller.

If any of the warranties made by the seller is materially untrue on the date on which a loan is sold to the mortgages trustee, then the seller will be required to remedy the breach, failing which it at the direction of Funding 1 will be required to repurchase the loan or loans under the relevant mortgage account and their related security at their outstanding principal balance as at the date of repurchase, including any arrears of interest and accrued and unpaid interest and expenses. There can be no assurance that the seller will have the financial resources to repurchase the loan or loans under the relevant mortgage account and their related security. However, if the seller does not repurchase those loans and their related security when required, then the seller share will be deemed to be reduced by an amount equal to the principal amount outstanding of those loans together with any arrears of interest and accrued and unpaid interest and expenses. See “**Sale of the loans and their related security – Repurchase of loans under a mortgage account**” below.

Other than as described here, neither you nor the issuing entity will have any recourse to the assets of the seller.

**There can be no assurance that a borrower will repay principal at the end of the term on an interest-only loan, which may adversely affect repayments on the notes**

Each loan in the portfolio is repayable either on a principal repayment basis, an interest-only basis or a combination of these bases. For interest-only loans and loans repayable on a combined principal repayment/interest-only basis, because the principal (or, as applicable, a part thereof) is repaid in a lump sum at the maturity of the loan, the borrower is informed that it is his or her responsibility to have some repayment mechanism (such as an investment plan) in place which is intended to provide sufficient funds to repay such principal at the end of the term. However, Birmingham Midshires does not ensure that a repayment mechanism is in place and Birmingham Midshires does not take security over these repayment mechanisms (although, since

February 2006, the borrower has been required to declare the type of repayment mechanism in place). It is a condition of the advance of each loan that the borrower takes out a life insurance policy in relation to the loan but, as with repayment mechanisms, the seller does not take security over these life insurance policies.

The ability of a borrower to repay the principal on an interest-only loan at maturity depends on the borrower ensuring that sufficient funds are available from an investment plan or another source, such as ISAs, pension policies, sale of the related security (particularly in the case of buy-to-let mortgages), personal equity plans or endowment policies, as well as the financial condition of the borrower, tax laws and general economic conditions at the time.

There can be no assurance that the borrower will have the funds required to repay the principal at the end of the term. If a borrower cannot repay the loan and a loss occurs on the loan, then this may affect repayments of principal on the notes if that loss cannot be cured by application of excess Funding 1 available revenue receipts. In respect of loans sold to the mortgages trustee in connection with the issuance of notes, the applicable final terms will state the amount of the loans in the expected portfolio that are interest-only loans. See “**Statistical information on the portfolio – The cut-off date mortgage portfolio – Repayment terms**” in the applicable final terms.

#### **Set-off risks in relation to flexible loans may adversely affect the funds available to the issuing entity to repay the notes**

As described in “– **There may be risks associated with the fact that the mortgages trustee has no legal title to the loans and their related security, which may adversely affect payments on the notes**” below, the seller has made, and in the future may make, an equitable assignment of the relevant loans and their related security, or in the case of Scottish loans a transfer of the beneficial interest in the relevant loans and their related security, to the mortgages trustee, with legal title being retained by the seller. Therefore, the rights of the mortgages trustee may be subject to the direct rights of the borrowers against the seller, including rights of set-off existing prior to notification to the borrowers of the sale of the mortgages. The mortgages trust includes flexible loans. Set-off rights (including analogous rights in Scotland) may occur if the seller fails to advance to a borrower a drawing or permit the borrower to make an underpayment or take a payment holiday under a flexible loan when the borrower is entitled to draw additional amounts or make an underpayment or take a payment holiday under a flexible loan.

If the seller fails to advance the drawing or permit the borrower to make an underpayment or take a payment holiday, then the relevant borrower may set-off any damages claim (or exercise analogous rights in Scotland) arising from the seller’s breach of contract against the seller’s (and, as assignee or holder of the beneficial interest in the loans and their related security, the mortgages trustee’s) claim for payment of principal and/or interest under the loan as and when it becomes due. These set-off claims will constitute transaction set-off as described in the immediately following risk factor.

The amount of the claim in respect of a drawing will, in many cases, be the cost to the borrower of finding an alternative source of finance although, in the case of flexible loans which are or relate to Scottish loans, it is possible that the borrower’s rights of set-off could extend to the full amount of the relevant drawing. The borrower may obtain a loan elsewhere in which case the damages would be equal to any difference in the borrowing costs together with any consequential losses, namely the associated costs of obtaining alternative funds (for example, legal fees and survey fees). If the borrower is unable to obtain an alternative loan, he or she may have a claim in respect of other losses arising from the seller’s breach of contract where there are special circumstances communicated by the borrower to the seller at the time the mortgage was taken out or which otherwise were reasonably foreseeable. In either case, the damages claim will be limited by general legal principles concerning remoteness of loss and mitigation. These include (i) the principle that something, which is a real possibility but would only occur in a small minority of cases, will not usually fall within the contractual measure of damages and (ii) the borrower’s duty to mitigate his loss.

A borrower may also attempt to set-off against his or her mortgage payments an amount greater than the amount of his or her damages claim (or exercise analogous rights in Scotland). In that case, the seller will be entitled to take enforcement proceedings against the borrower although the period of non-payment by the borrower is likely to continue until a judgment is obtained.

The exercise of set-off rights by borrowers would reduce the incoming cashflow to the mortgages trustee during such exercise. However, the amounts set-off will be applied firstly to reduce the seller share only.

See also “– **If a significant number of borrowers attempt to setoff claims for damages based on contravention of an FSA rule against the amount owing by the borrower under a loan, there could be a material decrease in receipts from the mortgages trust**” and “– **If Birmingham Midshires’ interpretation of certain technical rules under the CCA were held to be incorrect by a court or the Ombudsman or was**

**challenged by a significant number of borrowers, or borrowers exercise rights of set-off insofar as available under the CCA, there could be material disruption in the income of the mortgages trust”** below.

Further, there may be circumstances in which certain drawings may rank behind security created by a borrower after the date upon which the borrower entered into its mortgage with the seller.

The minimum seller share has been sized in an amount expected to cover this risk, although there is no assurance that it will. If the minimum seller share is not sufficient in this respect then there is a risk that you may not receive all amounts due on the notes or that payments may not be made when due.

**There may be risks associated with the fact that the mortgages trustee has no legal title to the loans and their related security, which may adversely affect payments on the notes**

The sale by the seller to the mortgages trustee of the English mortgages has taken and will take effect in equity only. The sale by the seller to the mortgages trustee of the Scottish mortgages on the programme date and on subsequent dates was given effect by a declaration or declarations of trust by the seller in favour of the mortgages trustee (and any sale of Scottish mortgages in the future will be given effect by further declarations of trust) by which the beneficial interest in the Scottish mortgages was or will be transferred to the mortgages trustee. In each case this means that legal title to the loans in the portfolio remains with the seller, but the mortgages trustee has all the other rights and benefits relating to ownership of each loan and its related security (which rights and benefits are subject to the mortgages trust in favour of the beneficiaries). The mortgages trustee has the right to demand that the seller give it legal title to the loans and the related security in the circumstances described in “**Sale of the loans and their related security – Legal assignment of the loans to the mortgages trustee**” below and until then the mortgages trustee will not give notice of the sale of the English mortgages to any borrower or apply to the Land Registry or the Central Land Charges Registry to register or record its equitable interest in the English mortgages or take any steps to complete or perfect its title to the Scottish mortgages. For more information on the English mortgages see “**Material legal aspects of the loans – English loans**” below. For more information on the Scottish mortgages see “**Material legal aspects of the loans – Scottish loans**” below.

Because the mortgages trustee has not obtained legal title to the loans or their related security, there are risks, as follows:

- first, if the seller wrongly sold a loan to another person which has already been sold to the mortgages trustee, and that person acted in good faith and did not have notice of the interests of the mortgages trustee or the beneficiaries in the loan, then she or he might obtain good title to the loan, free from the interests of the mortgages trustee and the beneficiaries. If this occurred then the mortgages trustee would not have good title to the affected loan and its related security and it would not be entitled to payments by a borrower in respect of that loan. This may affect the ability of the issuing entity to repay the notes; and
- second, the rights of the mortgages trustee and the beneficiaries may be subject to the rights of the borrowers against the seller, such as the rights of set-off (see in particular “– **Set-off risks in relation to flexible loans may adversely affect the funds available to the issuing entity to repay the notes**” above) which occur in relation to transactions or deposits made between some borrowers and the seller and the rights of borrowers to redeem their mortgages by repaying the loan directly to the seller. If these rights were exercised, the mortgages trustee may receive less money than anticipated from the loans, which may affect the ability of the issuing entity to repay the notes.

However, if a borrower exercises any set-off rights, then an amount equal to the amount set-off will firstly reduce the total amount of the seller share only, and the minimum seller share has been (and, in the case of set-off risk in relation to deposits made by some borrowers with other entities in the HBOS group, may in future be) sized in an amount expected to cover this risk, although there is no assurance that it will. If the minimum seller share is exhausted, then the amount of any set-offs would be applied to reduce the Funding 1 share.

**Independent set-off risks which a borrower has against the seller may adversely affect the funds available to the issuing entity to repay the notes**

Once notice has been given to borrowers of the transfer of the loans and their related security to the mortgages trustee, independent set-off rights which a borrower has against the seller will crystallise (such as, for example, set-off rights associated with borrowers holding deposits with the seller) and further rights of independent set-off would cease to accrue from that date and no new rights of independent set-off could be asserted following that notice. Set-off rights arising under transaction set-off (which are set-off claims arising out of a transaction

connected with the loan) will not be affected by that notice. These set-off rights if exercised could reduce the loan receipts available to the mortgages trustee to distribute to Funding 1, and could ultimately affect the amounts available to the issuing entity for payments on the notes.

**If the servicer is removed, there is no guarantee that a substitute servicer would be found, which could delay collection of payments on the loans and ultimately could adversely affect payments on the notes**

The seller was appointed by the mortgages trustee and the beneficiaries as servicer to service the loans. If the servicer breaches the terms of the servicing agreement, then the mortgages trustee, Funding 1 and/or the Funding 1 security trustee will be entitled to terminate the appointment of the servicer and appoint a new servicer in its place.

There can be no assurance that a substitute servicer with sufficient experience of administering mortgages of residential properties would be found who would be willing and able to service the loans on the terms of the servicing agreement. In addition, as described below, any substitute servicer will be required to be authorised under the FSMA (as defined below) in order to administer loans that constitute regulated mortgage contracts. The ability of a substitute servicer fully to perform the required services would depend, among other things, on the information, software and records available at the time of the appointment. Any delay or inability to appoint a substitute servicer may affect payments on the loans and hence the issuing entity's ability to make payments when due on the notes.

You should note that the servicer has no obligation itself to advance payments that borrowers fail to make in a timely fashion.

**Funding 1 or the issuing entity may not receive the benefit of any claims made on the buildings insurance which could adversely affect payments on the notes**

The practice of the seller in relation to buildings insurance is described under "**The loans – buildings insurance**" below. The seller no longer has the benefit of a block insurance policy if a borrower fails to maintain insurance cover in respect of his or her property. As described in that section, no assurance can be given that Funding 1 will always receive the benefit of any claims made under any applicable insurance contracts. This could reduce the principal receipts received by Funding 1 according to the Funding 1 share percentage and could adversely affect the issuing entity's ability to redeem the notes. You should note that buildings insurance is renewed annually.

**If Birmingham Midshires' interpretation of certain technical rules under the CCA were held to be incorrect by a court or the Ombudsman or was challenged by a significant number of borrowers, or borrowers exercise rights of set-off insofar as available under the CCA, there could be material disruption in the income from the mortgages trust**

In the United Kingdom, the Office of Fair Trading (the **OFT**) is responsible for the issue of licences under, and the superintendence of the working and the enforcement of, the CCA, related consumer credit regulations and other consumer protection legislation. The OFT may review businesses and operations, provide guidelines to follow and take actions when necessary with regard to the mortgage market in the United Kingdom.

A credit agreement is regulated by the CCA where (a) the borrower is or includes an "individual" as defined in the CCA, (b) (if the credit agreement was made before 6 April 2008) the amount of "credit" as defined in the CCA does not exceed the financial limit, which is £25,000 for credit agreements made on or after 1 May 1998 or lower amounts for credit agreements made before that date, and (c) the credit agreement is not an exempt agreement under the CCA (for example, in certain circumstances, a credit agreement to finance the purchase of land is an exempt agreement under the CCA).

Any credit agreement that is wholly or partly regulated by the CCA or treated as such has to comply with requirements under the CCA as to documentation and procedures of credit agreements, and (in so far as applicable) pre-contract disclosure. If it does not comply with those requirements, then to the extent that the credit agreement is regulated by the CCA or treated as such, it is unenforceable against the borrower (a) without an order of the OFT, if the lender or any broker does not hold the required licence at the relevant time, (b) totally, if the credit agreement was made before 6 April 2007 and if the form of such credit agreement was not properly signed or omits or mis-states a "prescribed term" or (c) without a court order in other cases and, in exercising its discretion whether to make the order, the court would take into account any prejudice suffered by the borrower and any culpability of the lender. In addition, the CCA imposes licensing requirements on lenders and brokers.

Any credit agreement intended to be a regulated mortgage contract under the FSMA (as defined below) or unregulated might instead be wholly or partly regulated by the CCA or treated as such because of technical rules on (a) determining whether any credit under the CCA arises or whether any applicable financial limit of the CCA is exceeded, (b) determining whether the credit agreement is an exempt agreement under the CCA and (c)

changes to credit agreements. So as to avoid dual regulation, it is intended that regulated mortgage contracts will not be regulated by the CCA. Relevant provisions of the CCA are designed to clarify the position in this regard.

A court order under section 126 of the CCA is necessary to enforce a land mortgage (including, in Scotland, a standard security) securing a credit agreement to the extent that the credit agreement is regulated by the CCA or treated as such. In dealing with such application, the court has the power, if it appears just to do so, to amend the credit agreement or to impose conditions upon its performance or to make a time order (for example, giving extra time for arrears to be cleared).

Under Section 75 of the CCA in certain circumstances (a) the lender is liable to the borrower in relation to misrepresentation and breach of contract by a supplier in a transaction financed by the lender, where the related credit agreement is or is treated as entered into under pre-existing arrangements, or in contemplation of future arrangements, between the lender and the supplier and (b) the lender has a statutory indemnity from the supplier against such liability, subject to any agreement between the lender and the supplier. The borrower may set off the amount of the claim against the lender against the amount owing by the borrower under the loan or under any other loan that the borrower has taken (or exercise analogous rights in Scotland). Any such set-off may adversely affect the issuing entity's ability to make payments on the notes.

The Consumer Credit Act 2006 (the CCA 2006) which amends the Consumer Credit Act 1974, was enacted in March 2006. The Consumer Credit Act 2006 is expected to be fully implemented by October 2008. Some of the relevant reforms are set out below.

The "extortionate credit" regime has been replaced by an "unfair relationship" test. The new test applies to all existing credit agreements. The unfair relationship test explicitly imposes liability to repay the borrower on both the originator and any assignee, such as the mortgages trustee. In applying the new unfair relationship test, the courts will be able to consider a wider range of circumstances surrounding the transaction, including the creditor's conduct before and after making the agreement.

There is no statutory definition of the word "unfair" as the intention is for the test to be flexible and subject to judicial discretion.

The courts may, but are not obliged to, look solely to the CCA 2006 for guidance. The FSA principles for businesses may also be relevant and apply to the way contract terms are used in practice and not just the way they are drafted. Once the debtor alleges that an unfair relationship exists, the burden of proof is on the creditor to prove the contrary.

If a loan subject to the unfair relationship test is found to be unfair, the court may require the creditor to repay sums to the debtor, to do, not do or cease doing anything in relation to the agreement, reduce or discharge any sums payable by the debtor or surety, return surety, alter the terms of the agreement or direct accounts to be taken.

An alternative dispute resolution scheme for consumer credit matters was established on 6 April 2007 and is run by the Ombudsman (as described below). The scheme is mandatory for all businesses licensed under the CCA. The CCA 2006 also introduced an independent Consumer Credit Appeals Tribunal for licensing appeals.

The financial limit for CCA regulation is removed for credit agreements made on or after 6 April 2008, except for certain changes to credit agreements, and except for buy-to-let loans made before 1 October 2008. The Department for Business, Enterprise and Regulatory Reform (the **BERR**) has confirmed that it intends to exempt agreements entered into for buy-to-let purposes, regardless of value, from the CCA. The BERR defines buy-to-let loans as being agreements secured on land where the borrower or a connected person occupies or intends to occupy less than 40 per cent. of the property as a dwelling. It is anticipated that the Legislative Reform (Consumer Credit) Order 2008, which is required to make the changes, will be implemented as from mid-October 2008. A court order under section 126 of the CCA will, however, be necessary to enforce a land mortgage (including, in Scotland, a standard security) securing a buy-to-let loan to the extent that the credit agreement would, apart from this exemption, be regulated by the CCA or be treated as such.

The OFT has far broader powers under the CCA 2006 from 6 April 2008. For instance, it can apply civil penalties, has far greater powers of investigation and can issue indefinite standard licences. The CCA 2006 obliges creditors to comply with more stringent information requirements. Regulations have been made so that, from 1 October 2008, lenders will be obliged to give customers clearer and more regular information on their credit accounts.

These changes to the CCA may result in adverse effects on the issuing entity's ability to make payment in full on the notes when due.

Birmingham Midshires has interpreted certain technical rules under the CCA in a way common with many other lenders in the mortgage market. If such interpretation were held to be incorrect by a court or the Ombudsman, then a credit agreement, to the extent that it is regulated by the CCA or treated as such, would be unenforceable as described above. If such interpretation were challenged by a significant number of borrowers, then this could lead to significant disruption and shortfall in income of the mortgages trustee. Court decisions have been made on technical rules under the CCA against certain mortgage lenders, but such decisions are very few and are generally county court decisions not binding on other courts.

The seller has given warranties to the mortgages trustee in the mortgage sale agreement that, among other things, each loan and its related security is enforceable (subject to certain exceptions). If a loan or its related security does not comply with these warranties, and if the default cannot be or is not cured within 20 London business days, then the seller will upon receipt of notice from the mortgages trustee (acting on the directions of Funding 1) be required to repurchase the loans under the relevant mortgage account and their related security from the mortgages trustee.

**Failure by the seller or any broker to hold relevant authorisations and permissions under FSMA in relation to regulated mortgage contracts may have an adverse effect on enforceability of mortgage contracts**

In the United Kingdom, regulation of residential mortgage business by the FSA under the Financial Services and Markets Act 2000 (the **FSMA**) came into force on 31 October 2004 (**N(M)**). Entering into, arranging or advising in respect of and administering regulated mortgage contracts, and agreeing to do any of these things, are (subject to applicable exemptions) regulated activities under the FSMA.

A credit agreement is a **regulated mortgage contract** under the FSMA if, at the time it is entered into on or after N(M) (a) the borrower is an individual or trustee, (b) the contract provides for the obligation of the borrower to repay to be secured by a first legal mortgage or, in Scotland, a first ranking standard security on land (other than timeshare accommodation) in the United Kingdom and (c) at least 40 per cent. of that land is used, or is intended to be used, as or in connection with a dwelling by the borrower or (in case of credit provided to trustees) by an individual who is a beneficiary of the trust, or by a related person.

The main effects are that, on or after N(M), unless an exclusion or exemption applies: (a) each entity carrying on a regulated mortgage activity by way of business has to hold authorisation and permission from the FSA to carry on that activity and (b) each financial promotion in respect of an agreement relating to qualifying credit has to be issued or approved by a person holding authorisation from the FSA. It should be noted that the definition of "qualifying credit" is broader than that of a "regulated mortgage contract" and may include mortgage loans that are regulated by the CCA or treated as such or unregulated. If requirements as to authorisation and permission of lenders and brokers or as to issue and approval of financial promotions are not complied with, a regulated mortgage contract would be unenforceable against the borrower except with the approval of a court. An unauthorised person who administers a regulated mortgage contract entered into on or after N(M) may commit a criminal offence, but this would not render the contract unenforceable against the borrower.

Any credit agreement intended to be a regulated mortgage contract under the FSMA might instead be wholly or partly regulated by the CCA or treated as such, or unregulated, and any credit agreement intended to be regulated by the CCA or treated as such, or unregulated, might instead be a regulated mortgage contract under the FSMA, because of technical rules on (a) determining whether the credit agreement or any part of it falls within the definition of "regulated mortgage contract" and (b) changes to credit agreements.

The seller is required to hold, and holds, authorisation and permission to enter into and to administer and, where applicable, to advise in respect of regulated mortgage contracts. Subject to any exemption, brokers will be required to hold authorisation and permission to arrange and, where applicable, to advise in respect of regulated mortgage contracts.

None of the issuing entity, Funding 1 or the mortgages trustee are, nor propose to be, authorised persons under the FSMA. The mortgages trustee does not require authorisation in order to acquire legal or beneficial title to a regulated mortgage contract. None of the issuing entity, Funding 1 or the mortgages trustee carry on the regulated activity of administering (servicing) mortgage contracts, because the loans are serviced pursuant to the servicing agreement by the servicer, which has the required FSA authorisation and permission. If the servicing agreement terminates, however, the mortgages trustee will have a period of not more than one month in which to arrange for mortgage servicing to be carried out by a replacement servicer having the required FSA authorisation and permission. In addition, on and after N(M), no variation has been or will be made to the loans and no further advance or product switch has been or will be made in relation to a loan where it would result in the issuing entity, Funding 1 or the mortgages trustee arranging or advising in respect of, administering (servicing) or entering into a regulated mortgage contract or agreeing to carry on any of these activities, if the issuing entity, Funding 1 or the mortgages trustee would be required to be authorised under the FSMA to do so.



**If a significant number of borrowers attempt to set off claims for damages based on contravention of an FSA rule against the amount owing by the borrower under a loan, there could be a material decrease in receipts from the mortgages trust**

The FSA's *Mortgages and Home Finance: Conduct of Business Sourcebook (MCOB)*, which sets out the FSA's rules for regulated mortgage activities, came into force on 31 October 2004. These rules cover, among other things, certain pre-origination matters such as financial promotion and pre-application illustrations, pre-contract and start-of-contract and post-contract disclosure, contract changes, charges and arrears and repossessions. FSA rules for prudential and authorisation requirements for mortgage firms, and for extending the appointed representatives regime to mortgages, came into force on 31 October 2004.

A borrower who is a private person is entitled to claim damages for loss suffered as a result of any contravention by an authorised person of an FSA rule, and may set off the amount of the claim against the amount owing by the borrower under the loan or any other loan that the borrower has taken (or exercise analogous rights in Scotland). Any such set-off may adversely affect the issuing entity's ability to make payments on the notes.

So as to avoid dual regulation, it is intended that regulated mortgage contracts will not be regulated by the CCA. The relevant regulations made in 2005 and 2008 under the FSMA are designed to clarify the position in this regard. This exemption only affects credit agreements made on or after N(M) and credit agreements made before N(M) but subsequently changed such that a new contract is entered into on or after N(M) and constitutes a regulated mortgage contract. A court order under section 126 of the CCA is, however, necessary to enforce a land mortgage (including, in Scotland, a standard security) securing a regulated mortgage contract to the extent that the credit agreement would, apart from this exemption, be regulated by the CCA or be treated as such.

No assurance can be given that additional regulatory changes by the OFT, the FSA or any other regulatory authority will not arise with regard to the mortgage market in the United Kingdom generally, the seller's particular sector in that market or specifically in relation to the seller. Any such action or developments or compliance costs may have a material adverse effect on the seller, the servicer, the issuing entity, the mortgages trustee, Funding 1 and their respective businesses and operations. This may adversely affect the issuing entity's ability to make payments in full on the notes when due.

As some of the loans in the portfolio were offered on or after N(M), the FSMA regime as set out above is intended to apply to such loans (except all or most buy-to-let loans). Thus the seller has given warranties to the mortgages trustee and others in the mortgage sale agreement that, *inter alia*, each loan is enforceable (subject to certain exceptions). If a loan does not comply with these warranties, and if the default is not cured, then the seller will, upon receipt of notice from the mortgages trustee (acting on the directions of Funding 1), be required to repurchase the loan.

Prior to N(M), in the United Kingdom, self-regulation of mortgage business existed under the Mortgage Code (the **CML Code**) issued by the Council of Mortgage Lenders (the **CML**). Halifax and Bank of Scotland each subscribed to the CML Code and on and from N(M), as an authorised person, have been subject to the FSA requirements in MCOB. Membership of the CML and compliance with the CML Code were voluntary. The CML Code set out minimum standards of good mortgage business practice, from marketing to lending procedures and dealing with borrowers experiencing financial difficulties. Since 30 April 1998 lender-subscribers to the CML Code could not accept mortgage business introduced by intermediaries who were not registered with (before 1 November 2000) the Mortgage Code Register of Intermediaries or (on and after 1 November 2000 until 31 October 2004) the Mortgage Code Compliance Board. Complaints relating to breach of the CML Code were dealt with by the relevant scheme, such as the Banking Ombudsman Scheme or the Mortgage Code Arbitration Scheme.

**If a significant number of borrowers challenge the validity of any lender fees paid to brokers, there could ultimately be a material adverse impact on the issuing entity's ability to make payments when due on the notes**

In the context of fees paid to brokers, where the broker acts as the borrower's agent and fiduciary, and as the lender's agent and subcontractor, or otherwise, a right of rescission of the loan and related security would, depending on the circumstances of the particular case, arise for the borrower. This would normally be the case where the lender (actual or potential) fees were not disclosed to the borrower, or where the borrower gave uninformed consent to the payment of those fees. Accordingly, there would be a risk of rescission of the loan and related security, unless the borrower had demonstrably given informed consent to the payment of the actual or potential lender fees. Any such rescission may, if successfully sought by a material number of borrowers in respect of the loans and related security may ultimately adversely impact on the issuing entity's ability to make payments in full when due on the notes.

**A new European directive concerning consumer credit and initiatives on mortgage credit may have an adverse effect on enforceability of the loans**

In April 2008, the European Parliament and the Council adopted a second directive on consumer credit (the **Consumer Credit Directive**), which provides that, subject to exemptions, Consumer Credit agreements between €200 and €75,000 will be regulated. However, loans secured by a land mortgage (including, in Scotland, a standard security) will be exempted. This directive will repeal and replace the first consumer credit directive. The official journal states that the directive should be implemented by Member States by 12 May 2010.

In July 2005, the European Commission published a Green Paper on mortgage credit, in which it announced its intention that loans secured by a mortgage on land (including, in Scotland, a standard security) will be excluded from the Consumer Credit Directive.

The European Commission published a White Paper on mortgage credit in December 2007.

The European Commission has indicated that it is yet to be determined as to whether legislation is the most appropriate way forward. The Commission is therefore undertaking further assessments and cost benefit analyses during 2008. The Commission has stated that no directive will be tabled if the costs of legislative measures outweigh their benefits.

On 14 March 2008, the European Commission published a notice, requesting tenders to undertake a study on the costs and benefits of the different policy options for mortgage credit. Tenders were required to be made by 13 May 2008. The tender anticipates that the study should take 9 months to complete.

Until the final text of any initiatives resulting from the White Paper process are decided and the details of the United Kingdom implementation of the Consumer Credit Directive are published, it is not certain what effect the adoption and implementation of the Consumer Credit Directive or any initiatives implemented in respect of mortgage credit would have on the seller, the servicer, the issuing entity, the mortgages trustee, Funding 1 and their respective businesses and operations. This may adversely affect the issuing entity's ability to make payments in full on the notes when due.

**Under distance marketing regulations, some of the loans may be cancellable, which may have an adverse effect on the issuing entity's ability to make payments on the notes**

The Financial Services (Distance Marketing) Regulations 2004 apply to, among other things, credit agreements entered into on or after 31 October 2004 by means of distance communication (i.e. without any substantive simultaneous physical presence of the originator and the borrower). A regulated mortgage contract under the FSMA, if originated by a UK lender from an establishment in the United Kingdom, will not be cancellable under these regulations. Certain other credit agreements will be cancellable under these regulations if the borrower does not receive prescribed information at the prescribed time. Where the credit agreement is cancellable under these regulations, the borrower may send notice of cancellation at any time before the end of the fourteenth day after the day on which the cancellable agreement is made, where all the prescribed information has been received, or, if later, the borrower receives the last of the prescribed information.

If the borrower cancels the credit agreement under these regulations, then:

- (a) the borrower is liable to repay the principal and any other sums paid by the originator to the borrower under or in relation to the cancelled agreement, within 30 days beginning with the day of the borrower sending notice of cancellation or, if later, the originator receiving notice of cancellation;
- (b) the borrower is liable to pay interest, or any early repayment charge or other charge for credit under the cancelled agreement, only if the borrower received certain prescribed information at the prescribed time and if other conditions are met; and
- (c) any security provided in relation to the contract is to be treated as never having had effect.

If a significant portion of the loans in the mortgages trust are characterised as being cancellable under these regulations, then there could be an adverse effect on the issuing entity's receipts in respect of the loans, affecting the issuing entity's ability to make payments on the notes.

**Regulations in the United Kingdom could lead to some terms of the loans being unenforceable, which may adversely affect payments on the notes**

In the United Kingdom, the Unfair Terms in Consumer Contracts Regulations 1999 as amended (the **1999 Regulations**), which, together with (in so far as applicable) the Unfair Terms in Consumer Contracts Regulations

1994 (together with the 1999 Regulations, the **UTCCR**), apply to agreements made on or after 1 July 1995 and affect all or almost all of the loans, provide that:

- a consumer may challenge a standard term in an agreement on the basis that it is “unfair” within the UTCCR and therefore not binding on the consumer; and
- the OFT and any **qualifying body** within the 1999 Regulations (such as the FSA) may seek to enjoin (or in Scotland interdict) a business from relying on unfair terms.

The UTCCR will not generally affect "core terms" which define the main subject matter of the contract, such as the borrower's obligation to repay the principal (provided that these terms are written in plain and intelligible language and are drawn adequately to the consumer's attention), but may affect terms that are not considered to be core terms, such as the lender's power to vary the interest rate and certain terms imposing early repayment charges and mortgage exit administration fees.

For example, if a term permitting the lender to vary the interest rate (as the seller is permitted to do) is found to be unfair, the borrower would not be liable to pay interest at the increased rate or, to the extent that the borrower has paid it, would be able, as against the lender or any assignee such as the mortgages trustee, to claim repayment of the extra interest amounts paid or to set off the amount of the claim against the amount owing by the borrower under the loan or any other loan that the borrower has taken (or exercise analogous rights in Scotland). Any such non-recovery, claim or set-off may adversely affect the issuing entity's ability to make payments on the notes.

In February 2000, the OFT issued a guidance note on what the OFT considers to be fair terms and unfair terms for interest variation in mortgage contracts. Where the interest variation term does not provide for precise and immediate tracking of an external rate outside the lender's control, and if the borrower is locked in, for example by an early repayment charge that is considered to be a penalty, the term is likely to be regarded as unfair under the UTCCR unless the lender (a) notifies the affected borrower in writing at least 30 days before the rate change and (b) permits the affected borrower to repay the whole loan during the next three months after the rate change without paying the early repayment charge. The seller has reviewed the guidance note and has concluded that its compliance with it will have no material adverse effect on the loans or its business. The guidance note has been withdrawn from the OFT website, but may remain in effect as the OFT's view and as a factor that the FSA may take into account.

The division of responsibilities between the OFT and the FSA for enforcing the UTCCR is set out in concordats made between them in October 2001 and in July 2006. Generally, the FSA is responsible for enforcement of the UTCCR in relation to regulated mortgage contracts under the FSMA and other mortgage loans originated by lenders authorised by the FSA, and the OFT is responsible for enforcement of the UTCCR in other mortgage contracts.

In May 2005, the FSA issued a statement of good practice on fairness of terms in consumer contracts, which is relevant to firms authorised and regulated by the FSA in relation to products and services within the FSA's regulatory scope. The statement provides that, for locked-in borrowers, a lender may consider drafting the contract to permit a change in the contract to be made only where any lock-in clause is not exercised. In the context of the OFT's investigation into credit card default charges, the OFT on 5 April 2006 publicly announced that the principles the OFT considers should be applied in assessing the fairness of credit card default charges shall apply (or are likely to apply) also to analogous default charges in other agreements including those for mortgages.

In January 2007, the FSA issued a statement of good practice on mortgage exit administration fees. This statement provides that the lender should ensure that the fee represents in fact the cost of the administration services that the lender provides when a borrower exits the mortgage. The FSA issued a follow-up communication in November 2007 emphasising that this statement should not be interpreted narrowly and, where appropriate, firms should consider applying its principles to other charges. In August 2007, the FSA's Unfair Contract Terms Regulatory Guide came into force. This guide is designed to explain the FSA's policy on how it will use its powers under the 1999 Regulations.

The broad and general wording of the UTCCR makes any assessment of the fairness of terms largely subjective and makes it difficult to predict whether or not a court would find a term to be unfair. It is therefore possible that any loans which have been made or may be made to borrowers covered by the UTCCR may contain unfair terms, which may result in the possible unenforceability of the terms of such loans.

In August 2002, the Law Commission for England and Wales and the Scottish Law Commission issued a joint consultation LCCP No. 166/SLCDP 119 on proposals to rationalise the UK Unfair Contract Terms Act 1977 and

the 1999 Regulations into a single piece of legislation and a final report, together with a draft bill on unfair terms, was published in February 2005. It is not proposed that there should be any significant increase in the extent of controls over terms in consumer contracts. Some changes are proposed, however, such as that (a) a consumer may also challenge a negotiated term in an agreement on the basis that it is “unfair” and “unreasonable” within the legislation and therefore not binding on the consumer and (b) in any challenge by a consumer (but not by the OFT or a qualifying body) of a standard term or a negotiated term, the burden of proof lies on the business to show that the term is fair and reasonable.

No assurance can be given that any changes enacted in the 1999 Regulations, or any changes adopted in guidance on interest variation terms, would not have a material adverse effect on the seller, the servicer, the issuing entity, the mortgages trustee, Funding 1 and their respective businesses and operations. This may adversely affect the issuing entity’s ability to make payments in full on the notes when due.

### **The UK Banking (Special Provisions) Act 2008 gives the UK treasury wide-ranging powers to make certain orders in respect of deposit-taking institutions**

Under the Banking (**Special Provisions**) Act 2008 (the Special Provisions Act), until 21 February 2009, the UK Treasury has wide powers to make certain orders in respect of a UK authorised deposit-taking institution (such as Bank of Scotland) and, in certain circumstances, certain related corporate undertakings (such as Bank of Scotland Treasury). The orders which may be made under the Act in respect of relevant deposit-taking institutions (and/or, in certain circumstances, certain related corporate undertakings) relate to (amongst other things) (i) transfers of securities issued by relevant entities (and/or securing that rights of holders of securities cease to be exercisable by such holders, discontinuing the listing of securities and/or varying or nullifying the terms of securities), (ii) transfers of property, rights and liabilities of relevant entities notwithstanding any restrictions, requirements or interest (and/or modifying related interests, rights or liabilities of third parties), (iii) the disapplication or modification of laws, (iv) the imposition of a moratorium on the commencement or continuation of any legal process in relation to any body or property and/or (v) the dissolution of any relevant entity. Significantly, orders may have retrospective effect (as from not earlier than three months before 21 February 2008) and may make provision for nullifying the effect of transactions or events taking place after the time in question.

While certain orders under the Act may be made by the UK Treasury only in certain circumstances for the purposes of maintaining the stability of the UK financial system in circumstances and/or protecting the public interest where financial assistance has been provided by the Treasury to the deposit-taking institution, such purpose conditions may not apply in respect of all orders which may be made under the Act. The Act includes provisions related to compensation in respect of any transfer orders made.

If the UK Treasury were to make an order in respect of Bank of Scotland and/or certain related corporate undertakings, such order may (amongst other things) impact on various aspects of the transaction (including the enforceability of the transaction documents and/or the ability of certain parties to perform their obligations under such documents) which may negatively affect the ability of the issuing entity to meet its obligations in respect of the notes. At present, the UK Treasury has not made any orders under the Act in respect of the entities referred to above and there has been no indication that it will make any such order under the Act, but there can be no assurance that this will not change and/or that noteholders will not be adversely affected by any such order if made. **Non-Status Lending Guidelines for lenders and brokers**

On 18 July 1997, the OFT issued Non-Status Lending Guidelines for lenders and brokers, which were revised in November 1997. These guidelines apply to all residential mortgage loans made to non-status borrowers, which are defined for the purposes of these guidelines as individuals with a low or impaired credit rating. These guidelines regulate the activities of lenders in areas such as advertising and marketing, loan documentation and contract terms, the relationship between lenders and brokers, selling methods, underwriting, dual interest rates and early repayment charges. None of the loans in the portfolio has been made to non-status borrowers but, in any event, the seller currently complies with these guidelines.

The actions of the lender and of any broker or other intermediary involved in marketing the lender's products can jeopardise the lender's fitness to hold a consumer credit licence. These guidelines make clear that lenders must take all reasonable steps to ensure that such brokers and other intermediaries comply with the guidelines and all relevant statutory requirements, even if the lender has no formal or informal control or influence over the broker or other intermediary.

The guidelines provide that lenders must carry on responsible lending, with all underwriting decisions being subject to a proper assessment of the borrower's ability to repay, taking into account all relevant circumstances, such as the purpose of the loan, the borrower's income, outgoings, employment and credit history. Lenders must take all reasonable steps to verify the accuracy of information provided by borrowers on or in support of the loan application, and all underwriting staff must be properly trained and supervised.

Charges payable on any early repayment (in whole or in part) are also restricted under these guidelines. Part repayments must be permitted, and any early repayment charges must do no more than cover the costs reasonably incurred by the lender in processing the payments. A formula for calculating the maximum amount payable on early settlement is prescribed by the CCA and applies to the extent that a credit agreement is regulated by the CCA or to be treated as such. These guidelines state that, for other credit agreements, the then current formula prescribed by the CCA (which continues to apply until 31 May 2010 for certain credit agreements) is unfair and oppressive, and that lenders must discontinue its use at the earliest opportunity.

No assurance can be given that additional regulations from the OFT, the FSA or any other regulatory authority will not arise with regard to the mortgage market in the United Kingdom generally, the seller's particular sector in that market or specifically in relation to the seller. Any such action or developments or compliance costs may have a material adverse effect on the loans, the seller, Funding 1 and/or the servicer and their respective businesses and operations. This may adversely affect the issuing entity's ability to make payments in full on the notes when due.

**Decisions of the Ombudsman could lead to some terms of the loans being varied, which may adversely affect payments on the notes**

Under FSMA, the Financial Ombudsman Service is required to make decisions on, among other things, complaints relating to activities and transactions under its jurisdiction on the basis of what, in the Ombudsman's opinion, would be fair and reasonable in all circumstances of the case, taking into account, among other things, law and guidance. Transitional provisions exist pursuant to which certain complaints relating to breach of the CML Code occurring before N(M) may be dealt with by the Financial Ombudsman Service. Complaints brought before the Financial Ombudsman Service for consideration must be decided on a case-by-case basis, with reference to the particular facts of any individual case. Each case would first be adjudicated by an adjudicator. Either party to the case may appeal against the adjudication. In the event of an appeal, the case proceeds to a final decision by the Ombudsman.

As the Financial Ombudsman Service is required to make decisions on the basis of, among other things, the principles of fairness and may order a money award to the borrower, it is not possible to predict how any future decision of the Financial Ombudsman Service would affect the ability of the issuing entity to repay the notes.

**The mortgages trustee's entitlement to be indemnified for liabilities undertaken during the enforcement process may adversely affect the funds available to Funding 1 to pay amounts due under the intercompany loan agreement, which may in turn adversely affect the funds available to pay the notes**

In order to enforce a power of sale in respect of a mortgaged property, the relevant mortgagee or (in Scotland) heritable creditor (which may be the seller or the mortgages trustee) must first obtain possession of the mortgaged property unless the property is vacant. Possession is usually obtained by way of a court order although this can be a lengthy process and the mortgagee or heritable creditor must assume certain risks. The mortgages trustee is entitled to be indemnified to its satisfaction against personal liabilities which it could incur if it were to become a mortgagee or heritable creditor in possession before it is obliged to seek possession.

**United Kingdom taxation position of Funding 1 and the issuing entity**

Regulations have been made to establish a permanent regime for the taxation of "securitisation companies" such as Funding 1 and the issuing entity (the **securitisation tax regime**). For accounting periods beginning on or after 1 January 2007, companies to which the regulations apply are taxed broadly by reference to their "retained profit" rather than by reference to their accounts. Funding 1 and the issuing entity should fall within the securitisation tax regime, but if either of them does not (or subsequently does not), then profits or losses could arise in Funding 1 and/or the issuing entity which could have tax effects not contemplated in the cashflows for the transaction described in this base prospectus and as such adversely affect the tax treatment of Funding 1 and/or the issuing entity and consequently payment on the notes. In these circumstances the issuing entity may, subject to certain conditions, redeem the notes (as described in Condition 5.5 (Optional redemption for tax and other reasons) in the section "**Terms and Conditions of the Notes**" below).

**EU Savings Directive**

Under EC Council Directive 2003/48/EC on the taxation of savings income (the **EU Savings Directive**), a Member State is required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State. However, for a transitional period, Belgium, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information

exchange with certain other countries). A number of non-EU countries and territories including Switzerland have agreed to adopt similar measures (a withholding system in the case of Switzerland).

For additional disclosure in relation to the EU Savings Directive in relation to Jersey, see “**Material Jersey (Channel Islands) tax considerations**” below.

#### **Your interests may be adversely affected by a change of law in relation to UK withholding tax**

In the event that amounts due under the notes are subject to withholding tax, neither the issuing entity nor any other person will be obliged to pay additional amounts in relation thereto. The issuing entity may, in certain circumstances, redeem the notes (as described in Condition 5.5 (Optional redemption for tax and other reasons) in the section “**Terms and conditions of the notes**” below). The applicability of any UK withholding tax under current English law is discussed under “**United Kingdom taxation**” below.

#### **Your interests may be adversely affected if the United Kingdom joins the European Monetary Union**

If the United Kingdom joins the European Monetary Union prior to the maturity of the notes, the issuing entity cannot assure you that this would not adversely affect payments on your notes.

It is possible that prior to the maturity of the notes the United Kingdom may become a participating member state in the European economic and monetary union and that the euro may become the lawful currency of the United Kingdom. In that event, (a) all amounts payable in respect of any notes denominated in sterling may become payable in euro, (b) applicable provisions of law may allow or require the issuing entity to re-denominate such notes into euro and take additional measures in respect of such notes and (c) the introduction of the euro as the lawful currency of the United Kingdom may result in the disappearance of published or displayed rates for deposits in pounds sterling used to determine the rates of interest on such notes or changes in the way those rates are calculated, quoted and published or displayed. The introduction of the euro could also be accompanied by a volatile interest rate environment which could adversely affect a borrower’s ability to repay its loan as well as adversely affect investors. It cannot be said with certainty what effect, if any, adoption of the euro by the United Kingdom will have on investors in the notes.

#### **Changes of law**

The transactions described in this base prospectus (including the issuance of the notes) and the ratings which are to be assigned to the notes are based on the relevant law and administrative practice in effect as at the date hereof and having regard to the expected tax treatment of all relevant entities under such law and practice. No assurance can be given as to the impact of any possible change to the law (including any change in regulation which may occur without a change in primary legislation), administrative practice or tax treatment after the date of this base prospectus nor can any assurance be given as to whether any such change would adversely affect the ability of the issuing entity to make payments under the notes.

#### **Security and insolvency considerations**

The issuing entity has entered into the issuing entity deed of charge pursuant to which it granted the issuing entity security in respect of certain of its obligations, including its obligations under the notes (as to which, see “**Security for the issuing entity’s obligations**”). Similarly, Funding 1 has entered into the Funding 1 deed of charge pursuant to which Funding 1 granted the Funding 1 security in respect of certain of its obligations, including its obligations under the intercompany loan agreement. In certain circumstances, including the occurrence of certain insolvency events in respect of the issuing entity or Funding 1, the ability to realise the issuing entity security and/or the Funding 1 security, respectively, may be delayed and/or the value of the relevant security impaired. While the transaction structure is designed to minimise the likelihood of the issuing entity or Funding 1 becoming insolvent, there can be no assurance that the issuing entity and/or Funding 1 will not become insolvent and/or the subject of insolvency proceedings and/or that the noteholders would not be adversely affected by the application of insolvency laws (including English insolvency laws).

In addition, it should be noted that, to the extent that any of the assets of the issuing entity or Funding 1 are subject only to a floating charge (including, in England, any fixed charge recharacterised by the courts as a floating charge), in certain circumstances under the provisions of section 176A of the Insolvency Act 1986, certain floating charge realisations which would otherwise be available to satisfy the claims of the Funding 1 secured creditors and/or the issuing entity secured creditors may be used to satisfy any claims of unsecured creditors. While certain of the covenants given by the issuing entity and Funding 1 in the transaction documents are intended to ensure it has no significant creditors other than the issuing entity secured creditors and the Funding 1 secured creditors respectively, it will be a matter of fact as to whether the issuing entity or, as applicable, Funding 1 has any other such unsecured creditors at any time. There can be no assurance that the

noteholders will not be adversely affected by any such reduction in floating charge realisations upon the enforcement of the issuing entity security or, as applicable, the Funding 1 security.

### **Liquidation expenses**

On 6 April 2008, a provision in the Insolvency Act 1986 came into force which effectively reversed by statute the House of Lords' decision in the case of *Leyland Daf* in 2004. Accordingly, it is now the case that the costs and expenses of a liquidation (including certain tax charges) will be payable out of floating charge assets in priority to the claims of the floating charge-holder. In respect of certain litigation expenses of the liquidator only, this is subject to approval of the amount of such expenses by the floating charge-holder (or, in certain circumstances, the court) pursuant to provisions set out in the Insolvency Rules 1986.

As a result of the changes described above, upon the enforcement of the floating charge security granted by the issuing entity and Funding 1, respectively, floating charge realisations which would otherwise be available to satisfy the claims of secured creditors under the issuing entity deed of charge and the Funding 1 deed of charge will be reduced by at least a significant proportion of any liquidation expenses. There can be no assurance that the noteholders will not be adversely affected by such a reduction in floating charge realisations.

### **You will not receive notes in physical form, which may cause delays in distributions and hamper your ability to pledge or resell the notes**

Unless the global notes are exchanged for definitive notes, which will only occur under a limited set of circumstances, beneficial ownership of the notes will only be recorded in book-entry form with DTC, Euroclear, Clearstream, Luxembourg or with any alternative clearing system agreed by the issuing entity. The lack of notes in physical form could, among other things:

- result in payment delays on such notes because the issuing entity will be sending distributions on the notes to DTC, Euroclear, Clearstream, Luxembourg or any alternative clearing system agreed by the issuing entity instead of directly to you;
- make it difficult for you to pledge such notes if notes in physical form are required by the party demanding the pledge; and
- hinder your ability to resell such notes because some investors may be unwilling to buy notes that are not in physical form.

### **If you have a claim against the issuing entity it may be necessary for you to bring suit against it in England to enforce your rights**

The issuing entity has agreed to submit to the non-exclusive jurisdiction of the courts of England, and it may be necessary for you to bring a suit in England to enforce your rights against the issuing entity.

### **Implementation of Basel II risk-weighted asset framework may result in changes to the risk-weighting of the notes**

Following the issue of proposals from the Basel Committee on Banking Supervision for reform of the 1988 Capital Accord, a framework has been developed which places enhanced emphasis on market discipline and sensitivity to risk. A comprehensive version of the text of the proposed framework was published in June 2006 under the title "*International Convergence of Capital Measurement and Capital Standards: a Revised Framework (Comprehensive Version)*" (the **Framework**). The Framework is being implemented in stages: the Basel II standard approach and the Foundation IRB approach for credit risk was implemented from 1 January 2007 and the most advanced Basel II IRB approach and the advanced measurement approach (AMA) for operational risks was required to be implemented from 1 January 2008. However, the Framework is not self-implementing and, accordingly, implementation dates in participating countries are dependent on the relevant national implementing process in those countries. In the United Kingdom, Basel II and the EU Capital Requirements Directive have been implemented through the Prudential Sourcebook for Banks, Building Societies and Investment Firms (**BIPRU**) and the Capital Requirements Regulations 2006 SI 2006/3221, although the most advanced approaches referred to above have only become available from 1 January 2008.

The Basel Committee announced in April 2008 that it would take steps to strengthen certain aspects of the Framework and, to this end, it confirmed that it would introduce a number of measures over the coming months. The European Commission also published in April 2008 a consultation paper on certain changes proposed to the

Capital Requirements Directive and it has also sought technical advice on its proposed changes from the Committee of European Banking Supervisors.

As and when implemented, the Framework could affect the risk-based capital treatment of the notes for investors who are subject to bank capital adequacy requirements that follow the Framework. Consequently, investors should consult their own advisers as to the consequences of and effect on them of the implementation of the Framework. Proposals and guidelines for implementing the Framework in certain participating jurisdictions are still in development, and no predictions can be made as to the precise effects of potential changes on the notes, the originator or any investor in respect of such jurisdiction.

**The minimum denominations on the notes may adversely affect payments on the notes if issued in definitive form**

The notes will have a denomination consisting of a minimum authorised denomination of \$100,000 (in the case of dollar-denominated notes), £50,000 (in the case of sterling-denominated notes, provided that the minimum authorised denomination of sterling-denominated notes with a maturity of 366 days or less will be £100,000) or €50,000 (in the case of euro-denominated notes) (or, in each case, such higher denomination as may be specified in the applicable final terms) plus higher integral multiples of \$1,000, £1,000 or €1,000, as applicable. Accordingly, it is possible that the notes may be traded in amounts in excess of the minimum authorised denomination that are not integral multiples of such denomination. In such a case, if definitive notes are required to be issued, a noteholder who holds a principal amount less than the minimum authorised denomination at the relevant time may not receive a definitive note in respect of such holding and may need to purchase a principal amount of notes such that its holding amounts to the minimum authorised denomination (or another relevant denomination amount).

If definitive notes are issued, noteholders should be aware that definitive notes which have a denomination that is not an integral multiple of the minimum authorised denomination may be illiquid and difficult to trade.



### **Use of proceeds**

The use of proceeds from an issuance of notes will be described in the applicable final terms.

### The issuing entity

The issuing entity was incorporated in England and Wales on 21 February 2007 (registered number 06121308) and is a public limited company under the Companies Act 1985. The registered office of the issuing entity is at 35 Great St. Helen's, London EC3A 6AP, United Kingdom.

The authorised share capital of the issuing entity comprises 50,000 ordinary shares of £1 each. The issued share capital of the issuing entity comprises 50,000 ordinary shares of £1 each, 49,998 of which are partly paid to £0.25 each and 2 of which are fully paid and all of which are beneficially owned by Holdings (see "**Holdings**" below).

The issuing entity is organised as a special purpose company. The issuing entity has no subsidiaries. The seller does not own directly or indirectly any of the share capital of Holdings or the issuing entity.

The issuing entity was established as a special purpose vehicle for the purposes of issuing the notes and making the advance of loan tranches to Funding 1 under the intercompany loan agreement. The activities of the issuing entity are limited to passively owing or holding the loan tranches, issuing the notes and borrowing the issuing entity subordinated loans and issuing entity start-up loans and other activities reasonably incidental thereto. The principal objects of the issuing entity are set out in its memorandum of association and include:

- lending money and giving credit, with or without security;
- borrowing or raising money and obtaining credit or finance;
- securing payment or repayment of money, credit or finance by any security over the issuing entity's property; and
- acquiring or entering into financial instruments, including derivative instruments.

Under the Companies Act 1985, the issuing entity's governing documents, including the principal objects of the issuing entity, may be altered by a special resolution of the shareholders.

The activities of the issuing entity are further restricted by the terms and conditions of the notes and are limited to the issue of the notes, the making of the advances of loan tranches under the intercompany loan agreement to Funding 1, the exercise of related rights and powers and other activities referred to in this base prospectus or incidental to those activities.

Since its incorporation, the issuing entity has not commenced operations (save in relation to the issuance of the notes) and has not engaged in any material activities other than those incidental to its incorporation as a public company under the Companies Act 1985 and to the issuance of the notes and to the authorisation of, entry into and performance of its obligations under the other transaction documents referred to in this base prospectus to which it is or will be a party.

The accounting reference date (i.e. the last day of the fiscal year) of the issuing entity is the last day of December. Statutory accounts to 31 December 2007 have been prepared and delivered to the Registrar of Companies on behalf of the issuing entity (see Annex A to this base prospectus).

## Directors and secretary

The following table sets out the directors of the issuing entity and their respective business addresses and occupations. Each director has served in office since the incorporation of the issuing entity.

Name	Business address	Principal activities/business occupation	Age	Term of office
SFM Directors Limited	35 Great St. Helen's London EC3A 6AP United Kingdom	Provision of directors to special purpose companies	–	Indefinite, subject to resignation or disqualification under the Companies Act of 1985
SFM Directors (No.2) Limited	35 Great St. Helen's London EC3A 6AP United Kingdom	Provision of directors to special purpose companies	–	Indefinite, subject to resignation or disqualification under the Companies Act of 1985
David Balai	Bank of Scotland plc, Treasury Division 33 Old Broad Street London EC2N 1HZ United Kingdom	Senior Director, Securitisation	52	Indefinite, subject to resignation or disqualification under the Companies Act of 1985

Bank of Scotland has caused David Balai, Senior Director, Securitisation of the Arranger to be a director of the issuing entity. David Balai does not receive any compensation for acting as director.

Bank of Scotland has caused SFM Directors Limited and SFM Directors (No.2) Limited, companies specialising in acting as directors of special purpose companies, to be directors of the issuing entity.

The directors of each of SFM Directors Limited and SFM Directors (No.2) Limited are Jonathan Eden Keighley, James Macdonald, Robert Berry, Claudia Wallace, J-P Nowacki, Cane Pickersgill, Helena Whitaker, Annika Goodwille and Debra Parsall. Their principal activities include the provision of directors and corporate management services to structured finance transactions as directors on the boards of SFM Directors Limited and SFM Directors (No.2) Limited. The business address of each of the directors of SFM Directors Limited and SFM Directors (No.2) Limited is 35 Great St. Helen's, London EC3A 6AP, United Kingdom.

The company secretary of the issuing entity is SFM Corporate Services Limited, 35 Great St. Helen's, London EC3A 6AP, United Kingdom.

In accordance with the corporate services agreement, the corporate services provider has and will continue to provide to the issuing entity directors, a registered and administrative office, the service of a company secretary and the arrangement of meetings of directors and shareholders and procure book-keeping services and preparation of accounts by Bank of Scotland. No other remuneration is paid by the issuing entity to or in respect of any director or officer of the issuing entity for acting as such. There will at all times be at least one independent director of the issuing entity.

The issuing entity has no employees.

## Capitalisation statement

The following table shows the capitalisation of the issuing entity as the date of this base prospectus:

	£
<b>Authorised share capital</b>	
<i>Ordinary shares of £1 each</i>	50,000.00

**Issued share capital***2 ordinary shares of £1 each fully paid*

2.00

*49,998 ordinary shares each one quarter paid*

12,499.50

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12,501.50

## Bank of Scotland plc

### Bank of Scotland plc

Bank of Scotland plc (**Bank of Scotland**) was originally established in 1695 as The Governor and Company of the Bank of Scotland by an Act of the Parliament of Scotland. On 17 September 2007, in accordance with the provisions of the HBOS Group Reorganisation Act 2006 (the **Act**), The Governor and Company of the Bank of Scotland registered as a public limited company under the Companies Act and changed its name to Bank of Scotland plc, registered number SC 327000. On the same day, under the Act, the business activities, assets (including investments in subsidiaries) and liabilities of Capital Bank plc, Halifax plc and HBOS Treasury Services plc transferred to Bank of Scotland. Accordingly, Bank of Scotland has become the **seller**, the **servicer**, the **cash manager**, the **issuing entity cash manager**, the **Funding 1 swap provider** and the **Funding 1 start-up loan provider**.

Bank of Scotland together with its subsidiaries and subsidiary undertakings (as defined in the Companies Act 1985) are collectively referred to as **Bank of Scotland group**. The registered office of Bank of Scotland is located at The Mound, Edinburgh EH1 1YZ, Scotland, with telephone number +44 (0)870 600 5000.

Bank of Scotland is a United Kingdom clearing bank with its headquarters in Edinburgh and an “authorised person” under the Financial Services and Markets Act 2000. The Bank of Scotland group is engaged in a range of banking, insurance broking, financial services and finance-related activities throughout the UK and internationally. As at 31 December 2007, it operated from branch outlets throughout the UK, overseas branches in Amsterdam, Frankfurt, Grand Cayman, Hong Kong, Madrid, New York City, Paris, Stockholm and Sydney and representative offices in Boston, Chicago, Dallas, Houston, Los Angeles, Miami, Minneapolis and Seattle. It is a member of the British Bankers’ Association and the Committee of Scottish Clearing Bankers. The Bank Notes (Scotland) Act 1845 confirmed Bank of Scotland’s right to issue bank notes in Scotland. At 31 December 2007, circulation of such notes was approximately £881 million.

Bank of Scotland is a wholly owned subsidiary of HBOS plc.

### Mortgage Business

As at 31 December 2007, the HBOS Group was the fourth largest banking group in the United Kingdom in terms of assets and was the United Kingdom's largest savings banking group. HBOS was incorporated in Scotland on 3 May 2001.

HBOS had total consolidated assets of £681,404 million at 30 June 2008. HBOS's consolidated underlying profit before tax for the half year to 30 June 2008 was £1,451 million.

The HBOS Group originates mortgages under four brands, of which the Birmingham Midshires brand is one.

Birmingham Midshires focuses on specialist lending, such as buy-to-let and self certification, however it also maintains a mainstream lending business. The vast majority of the lending undertaken by Birmingham Midshires takes place through intermediary agents. Mortgage loans and advances secured on residential properties originated under the Birmingham Midshires brand as at 31 December 2007 was approximately £44.6 billion compared with £40.2 billion as at 31 December 2006.

### Recent Developments

#### *Bank charges test case*

On 27 July 2007 it was announced that members of the HBOS Group, along with seven other major UK current account providers, had reached agreement with the OFT to commence legal proceedings in the High Court of England and Wales for a declaration (or declarations) to resolve legal uncertainties concerning the fairness and lawfulness of unarranged overdraft charges (the **Test Case**). It was also announced that HBOS and those other providers will seek a stay or sist of all current and potential future court proceedings which are brought against them in the UK concerning these charges and have obtained the consent of the Financial Ombudsman Service not to proceed with consideration of the merits of any complaints concerning these charges that are referred to them prior to the resolution of the Test Case. By virtue of a waiver granted by the FSA of its complaints handling rules, HBOS (and other banks, including the banks party to the Test Case) will not be dealing with or resolving customer complaints about unarranged overdraft charges while the waiver is in force. On 21 July 2008, the FSA confirmed that it is extending its waiver regarding unarranged overdraft charges complaints until 26 January 2009.

The first step in the Test Case was a trial of certain “preliminary” issues concerning the legal status and enforceability of contractual terms relating to unarranged overdraft charges. This preliminary trial concluded on 8 February 2008 and the judgment was handed down on 24 April 2008. The judgment held that the contractual terms relating to unarranged overdraft charges currently used by the HBOS Group (i) are not unenforceable as penalties, but (ii) are not exempt from assessment for fairness under the 1999 Regulations.

At a court hearing on 22 and 23 May 2008, the Judge granted HBOS and the other Test Case banks permission to appeal his decision that unarranged overdraft charges are assessable for fairness under the 1999 Regulations. This appeal is due to take place at the end of October/early November 2008.

A further hearing took place in early July 2008, at which the Court was asked to consider whether terms and conditions previously used by the Test Case banks are capable of being penalties. The judgment is awaited. Depending on the outcome of the appeal and the further hearing that took place in July 2008, another hearing may be required in order for the Court to determine the fairness of the charges.

A definitive outcome of the Test Case is unlikely to be known for at least twelve months.

Given the early stage of these proceedings and the uncertainty as to their outcome, it is not practicable at this time to estimate any potential financial effect. Consistent with HBOS’s obligations as a company admitted to the Official List, HBOS will give further details in relation to the Test Case when they become available, including its potential impact on the company.

#### *Underwritten rights issue*

On 18 July 2008, HBOS completed the rights issue announced on 29 April 2008, raising £4.0 billion of capital after expenses.

#### *Merger*

On 18 September 2008 Lloyds TSB and HBOS announced that they had reached agreement on the terms of a recommended acquisition by Lloyds TSB of HBOS. The terms of the acquisition value HBOS at £12.2 billion (based on Lloyds TSB’s closing price on 17 September 2008 of 279.75 pence). Existing Lloyds TSB Shareholders will own approximately 56 per cent. of the issued share capital of Lloyds TSB as enlarged by the Acquisition and existing HBOS Shareholders approximately 44 per cent.

The acquisition is conditional on, among other things, certain approvals by Lloyds TSB Shareholders and HBOS Shareholders as well as merger control approvals and regulatory clearances from, inter alia, the Financial Services Authority. It is expected that, subject to the satisfaction, or where relevant waiver, of all relevant conditions, the acquisition will be completed at the end of 2008 or early 2009.

## Funding 1

Pendeford Funding (No. 1) Limited was incorporated in England and Wales on 21 February 2007 (registered number 06121306) as a private limited company under the Companies Act 1985. The authorised share capital of Funding 1 comprises 100 ordinary shares of £1 each. The issued share capital of Funding 1 comprises two ordinary shares of £1, which are beneficially owned by Holdings (see “**Holdings**” below).

Funding 1 was organised as a special purpose company for the securitisation of residential mortgages originated by Birmingham Midshires. Funding 1 has no subsidiaries. The seller does not own directly or indirectly any of the share capital of Holdings or Funding 1.

The principal objects of Funding 1 are set out in its memorandum of association and are, among other things, to:

- carry on business as a general commercial company;
- borrow or raise money by any method and to obtain any form of credit or finance in any way the directors think fit (whether secured or unsecured);
- carry on business as a money lender, financier and investor;
- acquire and enter into financial instruments, including derivative instruments; and
- undertake and carry on all kinds of loan, financial and other operations.

Since its incorporation, Funding 1 has not engaged in any material activities, other than those incidental to the authorisation of, entry into and performance of its obligations under the transaction documents referred to in this base prospectus to which it is or will be a party and other matters which are incidental to those activities. Funding 1 has no employees.

Funding 1 has no continuing duties with respect to the notes but will receive payments in respect of the Funding 1 share and distribute such receipts as payments under the intercompany loan in accordance with the priorities of payments set out under “**Cashflows**”.

The accounting reference date of Funding 1 is the last day of December. Statutory accounts to 31 December 2007 have been prepared and delivered to the Registrar of Companies on behalf of Funding 1 (see Annex B to this base prospectus).

The registered office of Funding 1 is 35 Great St. Helen’s, London EC3A 6AP, United Kingdom. The telephone number of Funding 1’s registered office is +44 (0)20 7398 6300.

The following table sets out the directors of Funding 1 and their respective business addresses and occupations.

Name	Business address	Business occupation
SFM Directors Limited	35 Great St. Helen’s London EC3A 6AP United Kingdom	Director of special purpose companies
SFM Directors (No.2) Limited	35 Great St. Helen’s London EC3A 6AP United Kingdom	Director of special purpose companies
David Balai	Bank of Scotland plc, Treasury Division 33 Old Broad Street London EC2N 1HZ United Kingdom	Senior Director, Securitisation

David Balai is an employee of a company in the same group of companies as the seller.

The directors of SFM Directors Limited and SFM Directors (No.2) Limited are set out in the section “**The issuing entity**” above.

The company secretary of Funding 1 is SFM Corporate Services Limited, 35 Great St. Helen's, London EC3A 6AP, United Kingdom.

The directors and secretary of Funding 1 have no potential conflicts of interest between any duties to Funding 1 and their private interests and/or other duties.

In accordance with the corporate services agreement, the corporate services provider has and will continue to provide to Funding 1 directors, a registered and administrative office, the service of a company secretary and the arrangement of meetings of directors and shareholders and procure book-keeping services and preparation of accounts by Bank of Scotland. No other remuneration is paid by Funding 1 to or in respect of any director or officer of Funding 1 for acting as such. There will at all times be at least one independent director of Funding 1.



## **The mortgages trustee**

The mortgages trustee was incorporated in Jersey, Channel Islands on 12 February 2007 (registered number 95911) as a private company with limited liability under the Companies (Jersey) Law 1991, as amended, for a period of unlimited duration. The authorised share capital of the mortgages trustee is £2 divided into 2 ordinary shares of £1 each. Two ordinary shares have been issued and fully paid and are held in trust for charitable purposes by Structured Finance Management Offshore Limited pursuant to an instrument of trust dated 12 February 2007. Any profits received by the mortgages trustee, after payment of the costs and expenses of the mortgages trustee, will, ultimately, be paid for the benefit of charities and charitable purposes selected at the discretion of Structured Finance Management Offshore Limited. The payments on the notes will not be affected by this arrangement. The registered office of the mortgages trustee is at 47 Esplanade, St. Helier, Jersey JE1 0BD, Channel Islands. Its telephone number is +44 (0)1534 510 924.

The mortgages trustee has been organised as a special purpose company to act as trustee of the mortgages trust. The mortgages trustee has no subsidiaries. The seller does not own directly or indirectly any of the share capital of the mortgages trustee.

The constitutional documents of the mortgages trustee permit it, among other things, to:

- invest and deal in mortgage loans secured on residential or other properties within England, Wales and Scotland;
- invest in, buy, sell and otherwise acquire and dispose of mortgage loans, advances, other similar investments and all forms of security;
- carry on business as a money lender, financier and investor;
- undertake and carry on all kinds of loan, financial and other operations; and
- act as trustee in respect of carrying on any of these activities.

The mortgages trustee has not engaged, since its incorporation, in any material activities other than those incidental to its incorporation, the settlement of the trust property on the mortgages trustee, acting as trustee of the mortgages trust since the programme date, the issue of notes by the issuing entity, the authorisation of, entry into and performance of its obligations under the transaction documents to which it is a party, making an application for a standard licence under the CCA, filing a notification under the Data Protection Act 1998, registering as a data user under the Data Protection (Jersey) Law 2005, as amended and other matters which are incidental or ancillary to the foregoing. The mortgages trustee has no employees.

The accounting reference date of the mortgages trustee is the last day of December.

In accordance with the mortgages trustee corporate services agreement, the mortgages trustee corporate services provider (amongst other things) provides to the mortgages trustee directors, a registered and administrative office, the service of a company secretary and the arrangement of meetings of directors and shareholders. Halifax prepares the accounts of the mortgages trustee. No other remuneration is paid by the mortgages trustee to or in respect of any director or officer of the mortgages trustee for acting as such.

## **Holdings**

Holdings was incorporated in England and Wales on 21 February 2007 (registered number 06121391) as a private limited company under the Companies Act 1985. The registered office of Holdings is 35 Great St. Helen's, London EC3A 6AP, United Kingdom. The telephone number of Holdings' registered office is +44 (0)20 7398 6300.

Holdings has an authorised share capital of £100 divided into 100 ordinary shares of £1 each, of which two shares have been issued, one share at par value and one share at a premium, and are beneficially owned by SFM Corporate Services Limited on discretionary trust for the benefit, whilst monies remain due under the notes, of certain trusts, foundations, institutions or other organisations established in England and Wales which are regarded as exclusively charitable under the laws of England and Wales. Any profits received by Holdings from its shareholdings, after payment of the corporate administration costs and expenses of Holdings, will ultimately be paid for the benefit of those charities selected at the discretion of the trustee. The payments on the notes will not be affected by this arrangement.

Holdings is organised as a special purpose company. The seller does not own directly or indirectly any of the share capital of Holdings.

The principal objects of Holdings are set out in its memorandum of association and are, among other things, to acquire and hold, by way of investments or otherwise, and deal in or exploit, in such manner as may from time to time be considered expedient, all or any part of any securities or other interests of or in any company (including the issuing entity, Funding and PECO).

Holdings has acquired all of the issued share capital of the issuing entity, Funding and PECO. Holdings has not engaged in any other activities since its incorporation other than those incidental to the authorising of and entry into the transaction documents to which it is or will be a party and other matters which are incidental to those activities. Holdings has no employees.

The accounting reference date of Holdings is the last day of December.

## PECOH

The post-enforcement call option holder (or PECO) was incorporated in England and Wales on 21 February 2007 (registered number 06121342) as a private limited company under the Companies Act 1985. The registered office of PECO is 35 Great St. Helen's, London EC3A 6AP, United Kingdom.

The authorised share capital of PECO comprises 100 ordinary shares of £1 each. The issued share capital of PECO comprises one ordinary share of £1, which is beneficially owned by Holdings (see "**Holdings**" above).

PECO is organised as a special purpose company. PECO has no subsidiaries. The seller does not own directly or indirectly any of the share capital of PECO.

The principal objects of PECO are as set out in its memorandum of association and are, among others, to hold bonds, notes, obligations and securities issued or guaranteed by any company and any options or rights in respect of them. PECO has not engaged since its incorporation in any material activities other than those activities relating to the issue of the notes and those incidental to the authorising of and entry into the transaction documents referred to in this prospectus to which it is or will be a party and other matters which are incidental to those activities. PECO has no employees.

The accounting reference date of PECO is the last day of December.

Pursuant to the terms of an option to be granted to PECO under the post-enforcement call option agreement, following the enforcement, realisation and payment of the proceeds of the security granted by the issuing entity pursuant to the issuing entity deed of charge, PECO can require the transfer to it of all of the notes outstanding for a nominal amount.

As the post-enforcement call option to be granted pursuant to the issuing entity post-enforcement call option agreement can be exercised by PECO only after the issuing entity security trustee has enforced and realised the security granted by the issuing entity under the issuing entity deed of charge and has determined that there are no further assets available to pay amounts due and owing to the noteholders, the exercise of the post-enforcement call option and delivery by the noteholders of the notes to PECO will not extinguish any other rights or claims other than the rights to payment of interest and repayment of principal under the notes that such noteholders may have against the issuing entity.

### **The Funding 1 swap provider**

The Funding 1 swap provider is Bank of Scotland. See “**Bank of Scotland plc**” above.

### **The note trustee, the issuing entity security trustee and the Funding 1 security trustee**

The note trustee is Deutsche Trustee Company Limited. Its principal address is Winchester House, 1 Great Winchester Street, London EC2N 2DB. The issuing entity security trustee and the Funding 1 security trustee is Deutsche Bank Trust Company Americas. Its principal address is 1741 E St. Andrew Place, Santa Ana, CA 92705, United States.

Both Deutsche Bank Trust Company Americas and Deutsche Trustee Company Limited have served and currently are serving as indenture trustee and trustee for numerous securitisation transactions and programmes involving pools of mortgage loans.

Pursuant to the note trust deed, the note trustee is required to take certain actions as described in “**Description of the note trust deed**” and “**Terms and conditions of the notes**” below. Pursuant to the note trust deed and the issuing entity deed of charge, the issuing entity security trustee is required to take certain actions as described in “**Security for the issuing entity’s obligations – Appointment, powers, responsibilities and liabilities of the issuing entity security trustee**” below.

The limitations on liability of the note trustee are described in “**Terms and conditions of the notes**” below. The limitations on the liability of the issuing entity security trustee are described in “**Security for the issuing entity’s obligations – Appointment, powers, responsibilities and liabilities of the issuing entity security trustee**” and “**Security for the issuing entity’s obligations – Additional provisions of the issuing entity deed of charge**” below.

The indemnifications available to the note trustee and the issuing entity security trustee are described in Condition 12 under “**Terms and conditions of the notes**” below.

Provisions for the removal of the issuing entity security trustee are described in “**Security for the issuing entity’s obligations – Appointment, powers, responsibilities and liabilities of the issuing entity security trustee – Retirement and removal**” below.

The Funding 1 deed of charge sets out the terms under which the Funding 1 security trustee is appointed and the indemnification of the Funding 1 security trustee. Pursuant to the Funding 1 deed of charge, the Funding 1 security trustee is required to take certain actions as described under “**Security for Funding 1’s obligations**” below. Provisions for the removal of the Funding 1 security trustee are described in “**Security for Funding 1’s obligations Appointment, powers, responsibilities and liabilities of the Funding 1 security trustee – Retirement and removal**” below.

### **Affiliations and certain relationships and related transactions of transaction parties**

HBOS is the holding company of Bank of Scotland. Bank of Scotland provides residential mortgages through its Retail Division through a number of brands including "Halifax", "Birmingham Midshires" and "Bank of Scotland". Residential mortgages originated under the Birmingham Midshires brand are underwritten, marketed and serviced at Birmingham Midshires offices.

Bank of Scotland has several roles in the programme including being the seller of the loans originated under the Birmingham Midshires brand. Bank of Scotland may sell loans to the mortgages trustee that are originated by Bank of Scotland other than under the Birmingham Midshires brand. In addition, new entities within the HBOS group may in the future, subject to conditions set out in the transaction documents, sell loans to the mortgages trustee.

Bank of Scotland also provides the services of (a) cash manager to the mortgages trustee and Funding 1, (b) issuing entity cash manager and (c) Funding 1 swap provider.

Except as described in the preceding paragraph, there are no other affiliations or relationships or related transactions under the programme.

## The loans

### The portfolio

Each final terms issued in connection with an issuance of notes will contain tables summarising information in relation to the relevant portfolio which (if applicable) will include loans expected to be sold to the mortgages trustee on the relevant closing date. The tables will contain information in relation to various criteria as at the applicable cut-off date. Tables will indicate, among other things, composition by type of property, seasoning, period to maturity, geographical distribution, LTV ratios, outstanding balance and repayment terms, product ranges as well as other information that may be described from time to time. The portfolio as at the cut-off date, for which statistics are presented in the applicable final terms, and the portfolio as at the relevant closing date may differ due to, among other things, amortisation of loans in the portfolio.

Each final terms relating to an issuance of notes also will contain tables summarising certain characteristics of the United Kingdom mortgage market. Tables will provide historical information on, among other things, repossession rates and house price to earnings ratios, as well as other information that may be described from time to time.

### Introduction

The following is a description of some of the characteristics of the loans currently or previously originated by the seller, including details of loan types, the underwriting process and lending criteria. The issuing entity believes the loans in the portfolio at any time will have characteristics that demonstrate the capacity to produce funds to service any payments due and payable on the notes.

On the programme date the seller sold the initial loans and, on subsequent dates, the seller has sold and may sell further loans, in each case together with their related security, to the mortgages trustee pursuant to the mortgage sale agreement. On the relevant closing dates, Funding 1 paid the seller consideration for loans (together with their related security) sold to the mortgages trustee and, on further subsequent dates, Funding 1 will pay the seller for any further loans sold to the mortgages trustee pursuant to the terms of the mortgage sale agreement. Such loans (other than loans sold on subsequent dates and further subsequent dates), together with their related security, accrued interest and other amounts derived from the loans, made up the trust property on the programme date.

The seller selects the loans for transfer into the portfolio and any loans to be substituted into the portfolio using an internally developed system containing defined data on each of the qualifying loans in the seller's overall portfolio of loans available for selection. This system allows the setting of exclusion criteria among others corresponding to relevant representations and warranties that the seller makes in the mortgage sale agreement in relation to the loans (see "**Sale of the loans and their related security – Representations and warranties**" below), for instance, the representation and warranty relating to a maximum outstanding principal balance of £750,000. Once the criteria have been determined, the system identifies all loans owned by the seller that are consistent with the criteria. From this subset, loans are selected at random until the target balance for new loans has been reached or the subset has been exhausted. After a pool of new loans is selected in this way, the constituent loans are monitored so that they continue to comply with the relevant criteria on the date of transfer.

Unless otherwise indicated, the description that follows relates to types of loans that have been and will be or could be sold to the mortgages trustee, either as part of the initial portfolio on the programme date or as part of a new portfolio sold to the mortgages trustee at a later date.

The loans in the portfolio have been and will be originated by Birmingham Midshires at least three months prior to their inclusion in the portfolio and in relation to loans sold to the mortgages trustee in relation to a particular issuance of notes will be originated no later than the date specified in the applicable final terms. No loans in the portfolio have been and will be in arrears by an amount in excess of one monthly payment then due under such loan at the time it is sold to the mortgages trustee.

The seller may sell new loans and their related security to the mortgages trustee from time to time. The seller reserves the right to amend the Birmingham Midshires lending criteria, to sell to the mortgages trustee new loans which are based upon mortgage terms different from those upon which loans forming the initial portfolio are based and to sell loans to the mortgages trustee which are originated by the seller under a brand other than Birmingham Midshires or by members of the HBOS group other than the seller. Those new loans may include loans which are currently being offered to borrowers which may or may not have some of the characteristics described here, but may also include loans with other characteristics that are not currently being offered to borrowers or that have not yet been developed and loans originated through others brands within the seller (or by other entities within the HBOS group). All new loans will be required to comply with the representations and warranties set out in the mortgage sale agreement from time to time. All the material representations and

warranties in the mortgage sale agreement as at the programme date are described in this prospectus. See “**Sale of the loans and their related security – Representations and warranties**” below.

## **Characteristics of the loans**

### ***Repayment terms***

Loans are typically repayable on one of the following bases:

- **repayment:** the borrower makes monthly payments of both interest and principal so that, when the loan matures, the full amount of the principal of the loan will have been repaid;
- **interest-only:** the borrower makes monthly payments of interest but not of principal so that, when the loan matures, the entire principal amount of the loan is still outstanding and is payable in one lump sum; or
- a combination of both these options.

In the case of either repayment loans or interest-only loans, the required monthly payment may alter from month to month for various reasons, including changes in interest rates.

For interest-only loans, because the principal is repaid in a lump sum at the maturity of the loan, the borrower is required, at the time of application, to declare the general type of repayment mechanism (such as an investment plan) which is intended to provide sufficient funds to repay the principal at the end of the term. However, Birmingham Midshires does not request specific details of the arrangements put in place by the borrower, nor does it take security over these repayment mechanisms.

Principal prepayments may be made in whole or in part at any time during the term of a loan, subject to the payment of any repayment fees (as described in “– **Early repayment of the loans**” below). A prepayment of the entire outstanding balance of all loans under a mortgage account discharges the mortgage. Any prepayment in full must be made together with all accrued interest, arrears of interest, any unpaid expenses and any applicable repayment fees(s).

### ***Payment methods***

All payments on the loans must be made in sterling and most payments are made by a direct debit (**DDR**) instruction through the UK direct debit system from another bank or building society account. A valid DDR instruction must be in place prior to completion.

### ***Interest payments and interest rate setting***

Birmingham Midshires currently offers the following special rate loans and is able to combine these to suit the requirements of the borrower:

- (a) **tracker rate loans**, which are set at a fixed margin above or below rates set by the Bank of England;
- (b) **fixed rate loans**, which are subject to a fixed rate of interest;
- (c) **standard variable rate loans**, which allow the borrower to pay interest at the standard variable rate of Birmingham Midshires which is administered, at the discretion of the seller, by reference to the general level of interest rates and competitive forces in the UK mortgage market (the **standard variable rate**); and
- (d) **discount loans**, which allow the borrower to pay interest at a specified discount to the standard variable rate of Birmingham Midshires.

The special rates described in (a), (b) and (d) above under tracker rate loans, fixed rate loans and discount loans are offered for a predetermined period, usually between one and five years, at the commencement of the loan (the **product period**). At the end of the product period, the rate of interest charged will either (a) move to some other interest rate type for a predetermined period or (b) revert to, or remain at, the standard variable rate or a fixed margin above or below rates set by the Bank of England for the remainder of the term. In certain instances, early repayment fees are payable by the borrower if the loan is redeemed within the product period. See “– **Early repayment of the loans**” below.



Birmingham Midshires has, in the past, offered **capped rate loans**, which allow the borrower to pay interest by reference to the standard variable rate set by the seller or another variable rate, but subject to a cap for a predetermined period, usually between one and five years. As at the date of the base prospectus, capped rate loans have not been sold into the mortgages trust, but may be sold as new loans in the future if such products are offered to borrowers, subject to receipt of confirmation from each of the rating agencies that such sale of capped rate loans will not result in its then current rating of the notes being downgraded, withdrawn or (in the case of S&P and Moody's) qualified.

Interest is calculated on a daily basis rather than on an annual basis. Any payment by the borrower will reduce the borrower's balance on which interest will be calculated the following day.

Birmingham Midshires may change the interest rate under a standard variable rate loan or a discount loan linked to the standard variable rate of Birmingham Midshires by altering the standard variable rate and giving the borrowers notice, on any part of the loan, unless otherwise agreed in the loan agreement and subject to certain restrictions set forth in the loan agreement. Birmingham Midshires may also change the borrowers' monthly payments, the repayment period and the accounting period by giving the borrowers notice. In the case of special rate loans, Birmingham Midshires may cancel the special rate under certain circumstances specified in the loan agreement.

The mortgage conditions applicable to all of the standard variable rate loans and discount loans linked to the standard variable rate of Birmingham Midshires provide that the standard variable rate may only be varied in accordance with a number of reasons that are specified in the mortgage conditions. These reasons include:

- to reflect changes in market conditions outside the seller's control;
- to reflect changes in the cost of funds used by the seller in its mortgage lending business;
- to reflect a change in the general lending practice of other major lenders (including the terms on which mortgages are offered by them);
- to maintain or improve the general market position of the seller's products in all areas of its business;
- to reflect changes in the way the seller administers its mortgage accounts (including changes to the technology used by the seller);
- to reflect any regulatory requirements or guidance or any change in the law or a decision or recommendation by or requirement of a court, ombudsman, regulator or similar body or an undertaking given to the Director General of Fair Trading;
- to reflect changes to the interest period;
- to regularise the way that all customers are treated following an acquisition, merger or takeover of or by another bank or organisation offering similar services;
- to reflect changes to the way that the property over which the mortgage is granted is used or occupied; or
- for any other valid reason.

If applicable, the servicer will be responsible for setting any variable margins in respect of new tracker rate loans that are sold to the mortgages trustee in the future. However, in maintaining, determining or setting these variable margins, except in the limited circumstances as set out in "**The servicing agreement – Undertakings by the servicer**" below, the servicer has undertaken to maintain, determine or set the variable margins at a level which is not higher than the variable margins set in accordance with the seller's policy from time to time. Currently there are no such variable margins.

The English loans are governed by the laws of England and Wales. The Scottish loans are governed by Scots law.

### ***Product range***

The initial portfolio consisted and each new portfolio will consist of loans categorised by Birmingham Midshires as prime loans being **mainstream loans** (being loans, backed by first ranking security, for the purchase or re-mortgage of residential property), **buy-to-let loans** (being loans, backed by first ranking security, for the purchase or re-mortgage of property for letting purposes) and **self-certification loans** (being loans, backed by first ranking security, for the purchase or re-mortgage of residential property where borrowers certify their own yearly income (see “**Status of Applicant(s)**” below)).

Some loans are portable, meaning that the borrower has a right, subject to meeting Birmingham Midshires’ lending policy at the time, to retain the terms of the mortgage when the borrower moves home (although this does not apply to the interest rate charged, which may vary). The relevant policy is that of Birmingham Midshires rather than its successors and assigns to the mortgage.

Other types of loan product may be sold to the mortgages trust in the future, subject to written confirmation being received from the rating agencies that such sale of new products will not result in the reduction, withdrawal or (in the case of S&P and Moody's) qualification of the ratings of the notes.

Sub-prime loans will not be sold to the mortgages trustee.

### ***Early repayment of the loans***

Principal prepayments may be made in whole or in part at any time during the term of a loan unless the offer letter states otherwise. A prepayment of the whole of the outstanding balance of all loans under a mortgage account discharges the mortgage in question but must be made together with all outstanding charges, arrears of interest and accrued interest thereon.

Currently, any lump sum capital prepayment made in respect of a mortgage account is credited after repayment of any outstanding charges, arrears of interest and accrued interest thereon to reduce the outstanding balance of the relevant mortgage account. Unless otherwise specified in the mortgage conditions, borrowers are encouraged to make lump sum prepayments in a minimum amount of £1,000 but partial prepayments will be processed by Birmingham Midshires regardless of amount. Once a lump sum capital prepayment is made, a new monthly interest payment/repayment will be calculated based on the reduced outstanding balance. Borrowers with flexible loans also have the option to increase their normal monthly repayment above the scheduled minimum, thereby facilitating repayment of the loan in a shorter time period than originally envisaged, or they may underpay or take a payment holiday subject to certain limits. See “**Characteristics of the loans – Flexible loans**”, below.

Subject as follows, early repayment charges and repayment administration fees will be charged to a borrower making a lump sum prepayment. Such charges and fees may, at the discretion of Birmingham Midshires, not be charged if early repayment is due to the death of the borrower (except in the case of buy-to-let loans). Birmingham Midshires also retains the discretion not to charge such fees in other circumstances, for example, where the borrower is refinancing the existing loan shortly before the end of the product period with a new loan originated by Birmingham Midshires. Where a borrower moves to a new property and takes out a new mortgage with Birmingham Midshires in the same names as the original borrowers and for the same amount within 6 months of repayment of the existing loan, Birmingham Midshires will refund such charges and fees in full.

The mortgages trustee has agreed to reimburse the seller any administration related fees received in relation to the loans.

### ***Further advances***

None of the loans (other than the flexible loans) obliges Birmingham Midshires to make further advances. If a borrower wishes to take out a further loan secured by the same mortgage (other than additional borrowing under a flexible loan), the borrower will need to repeat the application process and Birmingham Midshires will apply the lending criteria in determining whether to approve the application. In the case of Mortgage Plus loans, no further advance applications will be accepted within six months of completion of the original loan (though this does not impact the unsecured element of the loan).

Where an application is made for a further advance and there have been no arrears or other difficulties in relation to the existing mortgage account, Birmingham Midshires retains a discretion to determine the amount of the further advance on the basis of the value of the property shown on the Halifax Property Index provided that the existing formal valuation of the property was carried out within the preceding two years and the aggregate amount advanced and secured on the property does not exceed 90 per cent. (or lower, depending on which scheme the borrower’s product belongs to) of the figure given by the Halifax Property Index.

In the case of further advances that would result in the aggregate amount advanced and secured on the property exceeding 90 per cent. of the figure given by the Halifax Property Index a formal revaluation of the property is required before an application for a further advance is approved. The minimum amount of a further advance is £1,000.

In relation to a flexible loan, a further advance will only be allowed once a drawdown facility has been utilised in full and any accrued overpayments have been redrawn.

### ***Flexible loans***

Certain loans are subject to a range of options selected by the borrower that give the borrower greater flexibility in the timing and amount of payments made under the loan as well as access to pre-approved further advances under the loan (**flexible loans**). These flexible loans are tracker rate loans or, in limited circumstances, fixed rate loans or discount loans and offer all of the optional features described below, subject to certain conditions and financial limits. The flexible option provisions are contained in the mortgage offer. Loans governed by the CCA cannot be taken out as flexible loans. During the time that the seller has offered flexible loans, borrowers have not frequently exercised the various options available to them, although no assurance can be given that they will not exercise their options with greater frequency in the future.

Flexible loans include the following options, all subject to the further conditions described below and other offer specific conditions. Flexible features can be withdrawn under certain circumstances outlined in the relevant terms and conditions.

*Overpayments.* Borrowers may, subject to providing Birmingham Midshires with 14 days' prior notification, either increase their regular monthly payments above the normal monthly payment then applicable or make lump sum payments (of not less than £50) at any time. Where a borrower has made an overpayment, he or she can redraw the lump sums or amounts overpaid at any time, subject to a minimum redraw of £50. However, if a borrower has a drawdown facility, such borrower must use this facility before he or she can drawdown overpayments.

*Drawdown facility.* Borrowers may access a drawdown facility for a minimum of £25,001 up to an amount agreed with Birmingham Midshires, provided there is sufficient equity in addition to the minimum initial advance of £25,001. The drawdown facility must be taken in withdrawals of not less than £1,000. The drawdown facility is valid for three years after completion but sums repaid under a drawdown facility cannot be redrawn. Drawdown requests may be made without notice by calling Birmingham Midshires' lending call centre and funds will be paid by cheque made out to the borrowers. A drawdown request may be declined if any payment has been missed in the previous 6 months (other than approved underpayments or payment holidays). The drawdown facility is not available on further advance applications.

*Underpayments.* Borrowers may, subject to agreement and providing Birmingham Midshires with 14 days' prior notification, make underpayments to the extent that previous overpayments have been made provided that at least six months consecutive payments have been made since completion of the mortgage loan at the monthly payment advised from completion. The amount underpaid cannot exceed the total of accrued overpayments.

*Payment holidays.* Borrowers may, subject to agreement and providing Birmingham Midshires with 14 days' prior notification, skip up to two monthly payments in any 12 month rolling period provided that the borrower's account has been conducted satisfactorily, there have been no arrears in the previous six months and at least six consecutive payments have been made since completion of the mortgage loan at the monthly payment advised from completion.

Birmingham Midshires may agree to make a credit limit available to the borrower immediately, without providing 14 days' prior notification, to enable the options described above to be utilised by the borrower immediately following drawdown (except with regard to the underpayment and payment holiday options).

In addition to the above restrictions, Birmingham Midshires has the right to withdraw all or any part of the drawdown facility where (a) an event of default (as set out in the applicable terms and conditions) occurs or (b) the borrower's income falls to a material extent such that Birmingham Midshires believes that the borrower will be unable to maintain monthly repayments or (c) the borrower is declared bankrupt or enters in to an arrangement with creditors or (d) the borrower creates any subsequent charges over the mortgaged property or (e) the borrower dies or, if more than one, all parties to the account die or (f) any party to the account requests that the facility be cancelled or (g) the borrower leaves the property or sells or transfers an interest in the property. If the credit limit is withdrawn, the underpayment, payment holiday and/or drawdown facility options will cease to be available and any unused part of the credit limit will not be able to be utilised.

### ***Mortgage Plus loans***

Birmingham Midshires also offered **Mortgage Plus loans**, which are linked to an unsecured credit facility. Birmingham Midshires currently does not offer Mortgage Plus loans. The unsecured credit facility is a line of credit available to be drawn down by the borrower over and above the amount of the mortgage loan. Amounts drawn under the credit facility are not secured by a mortgage on the borrower's property. Mortgage Plus loans allow a borrower to make one monthly payment of amounts due under the mortgage loan and under the unsecured credit facility, to the extent the borrower has made a drawing under the unsecured credit facility. Birmingham Midshires applies the borrower's regular monthly payments and any underpayments and overpayments received on a Mortgage Plus loan in proportion to the contractual monthly payment due on the mortgage loan and the amount due on the unsecured credit facility, until the account is in arrears. At the point of the account going into arrears, allocation of payments will be based on discussions with the customer and arrangements being agreed, with the overall aim of maintaining payments to both elements and preventing litigation action taking place. Once litigation action has commenced on the secured loan, all future payments will be paid to the secured loan until the point that the secured loan is rehabilitated or litigation action is complete.

The amount of a Mortgage Plus loan was agreed at origination, subject to a maximum loan-to-value ratio (**LTV ratio**) on the secured portion of 95 per cent. The total unsecured amount agreed can be drawn down over a period of three years after completion. Any balance reductions (e.g. capital repayments to the unsecured element) cannot be re-drawn during this three-year period. After three years any funds that have not been drawn down are no longer available to the customer. A request for an additional drawdown received within the first six-month post-completion will be granted unless the customer has missed any regular payments on the Mortgage Plus account. After the six-month period has elapsed, in addition to checking the performance of the Mortgage Plus account, additional checks will be carried out to assess whether the drawdown will be granted. Amounts available under the unsecured credit facility (currently a maximum of £30,000 or 30 per cent. LTV, whichever is lower) are not secured by the mortgaged property, and Birmingham Midshires will not assign to the mortgages trustee amounts due under the unsecured credit facility. This means that only the secured mortgage loan is assigned to the mortgages trustee.

Other than as stated above, the secured element of the Mortgage Plus loan is subject to Birmingham Midshires' standard terms and conditions for mainstream lending, supplemented by additional terms and conditions for the unsecured element.

The seller did not sell any Mortgage Plus loans to the mortgages trustee on the programme date. The secured element (though not the unsecured element) may however be sold to the mortgages trustee in the future, subject to certain conditions. The unsecured element will not be eligible for sale to the mortgages trustee.

### ***Origination Channels***

Birmingham Midshires currently derives its mortgage-lending business primarily through intermediaries with a small volume through direct channels.

Birmingham Midshires can provide customers with an agreement in principle to lend almost immediately upon application at point of sale through its bespoke on-line application system.

The seller is subject to FSMA (and other FSA rules), MCOB and the Financial Ombudsman Service, which is a statutory scheme under the FSMA, and follows the Code of Banking Practice. The seller has pledged its support for regulation of the UK mortgage industry by the FSA and, in particular, the implementation of CAT marked loans. CAT is a voluntary UK Government standard that was introduced for mortgages in 2000. The CAT mark indicates that the product meets minimum standards for charges, access and terms.

### ***Lending criteria***

The loans were originated according to Birmingham Midshires' lending policy at the relevant time. The current lending criteria are set out below. Birmingham Midshires' lending criteria and underwriting policies are subject to change within the seller's sole discretion. New loans may only be included in the portfolio if they were originated in accordance with the lending criteria applicable at the time the loan is offered and the conditions contained in "**Sale of loans and their related security – Sales of loans and their related security to the mortgages trustee on the sale date**" above have been satisfied.

### ***Tenure of Property***

Properties may be either freehold or leasehold or (in Scotland) heritable or long leasehold. Commonhold properties are considered on an individual basis. In the case of leasehold properties, the minimum requirement is that the unexpired portion of the lease must normally be at least, as at the date of application, of such length to ensure that at least 30 years remain after the term of the loan.

## ***Valuations***

A valuation must be completed before an offer can be made. Up to November 2006, for all Birmingham Midshires loans, properties were required to be valued on-site by a qualified surveyor chosen from a panel of Birmingham Midshires approved valuation firms, as described below. From November 2006, certain qualifying cases may be valued using an automated valuation model (AVM). All other cases continue to be valued on-site by a qualified surveyor.

Birmingham Midshires' current automated mortgage application process requires that each application follows a set of rules to assess whether a case qualifies for an AVM and the level of acceptability of the borrowers' stated value of the property. An acceptable AVM value will allow an application to proceed to the next stage in the application to offer mortgage process.

Birmingham Midshires has used AVMs to value properties in such cases since November 2006.

AVMs are computer based systems which are used to provide instant open market valuations on residential properties. The third party AVM provider for Birmingham Midshires is Hometrack Data Systems Limited (**Hometrack**). The Hometrack system works through drawing comparable data from a large database, which in the United Kingdom is derived from sources including surveyors, the Land Registry, Ordnance Survey information and socio-demographic information. The Hometrack system contains full physical inspection surveys and physical inspection valuations within its database. In addition to full physical inspection data, the Hometrack system has most United Kingdom residential properties digitally mapped via the Ordnance Survey and access to full Land Registry data. The Hometrack system also utilises a proprietary index, which enables historical valuation points to be indexed, giving a current market value for each property on the database. Postcode changes are currently only updated quarterly, meaning the system may at times contain out-of-date information on the related property.

The reliability and accuracy of the AVM is based on the effectiveness and complexity of the algorithmic modelling of the system and the data upon which the model runs. The confidence level in the accuracy of an AVM is based on available prior valuation sale information on the related property and on the existence of a sufficient amount of similar properties that have been valued or sold recently in the vicinity of the related property. For every Birmingham Midshires AVM valuation, Hometrack provides a confidence level in addition to the valuation amount in the form of a number between 0 and 7. The higher the confidence level, the more accurate the AVM result is estimated to be. The confidence level is a statistically derived figure that is ultimately a function of the quality and amount of comparables used to determine the value of the subject property. There is no physical exterior or interior inspection of the property when an AVM is used for the purposes of Birmingham Midshires' valuation.

An application for a loan will only qualify for an AVM if certain conditions are met. An AVM may be used if the related loan amount is not greater than £500,000 and does not breach any product rules, as applicable. An AVM will not be used for loans related to certain types of properties deemed to be higher risk, for example new constructions. Any buy-to-let loans, packaged business loans and new business loans in Scotland will also not be eligible. Furthermore, an AVM will only be considered if the valuation is not greater than £750,000 and the LTV based on the value stated by the borrower is not greater than 85% for purchase applications and 90% for re-mortgage applications.

Once an AVM has been generated, a determination is made if the AVM is an acceptable valuation. An AVM can be accepted for a purchase application with a LTV of 60% and a confidence level of 4, for a purchase application with a LTV of between 60% and 85% with a confidence level of 6, for a re-mortgage application with a LTV of 85% with a confidence level of 4 and for a re-mortgage application with a LTV of between 85% and 90% with a confidence level of 6. These levels are however subject to change.

Where applications do not qualify for an AVM or where the returned AVM fails the related business rules, a physical valuation is obtained by a MRICS or FRICS qualified surveyor chosen from the panel of Birmingham Midshires approved valuation firms. The valuation report or AVM must be no more than 6 months old at the time of completion.

## ***Term of Loan***

The minimum term in respect of a loan is 5 years. The maximum term is 40 years (35 years in the case of Mortgage Plus loans).

## ***Age of Applicant***

All borrowers must be aged 18 or older (or 21 years or older in the case of Mortgage Plus loans).

The maximum age limit at the end of the mortgage term is 65 years (in the case of mainstream loans and self-certification loans) and 75 years (in the case of buy-to-let loans). On an exceptional basis (in the case of mainstream loans only), the maximum age limit at the end of the mortgage term may be extended to 75 years. The seller will attempt to ascertain the borrower's anticipated income in retirement. If the seller determines that the borrower will not be able to afford the mortgage into retirement, the application will be declined. If the borrower is already retired, the seller will consider the borrower's ability to support the loan.

### ***Loan amount***

The minimum amount that can be borrowed under a loan is £25,001 and the maximum amount is £2 million (£1 million in the case of buy-to-let loans and self-certification loans). Applications for mainstream loans between £2 million and £4 million may be considered on an individual basis. Loans above the maximum level of £750,000 will not be eligible for the pool.

### ***Security***

Security for each loan consists of a first mortgage (or, in Scotland, a first ranking standard security) on freehold properties in England and Wales, heritable properties in Scotland, leasehold properties in England and Wales with, as at the application date, at least 30 years remaining unexpired after the term of the loan and long-leasehold properties in Scotland with at least 70 years remaining on the lease at the time of application.

The seller requires that a newly built property (or one being occupied for the first time) has the benefit of a 10 year warranty from the National House Building Council (NHBC) or Zurich Municipal Insurance. The Zurich warranty may be extended to 15 years. The exception to NHBC or Zurich Municipal cover is where an architect or qualified surveyor (or, in some cases, another qualified consultant) is employed by the applicant to supervise the building of the property.

### ***Loan-to-Value Ratio***

The maximum original loan-to-value ratio (**LTV ratio**) of loans is as at the date hereof 95 per cent. (85 per cent. in the case of buy-to-let loans and 80 per cent. for self-certification loans). Previously, the maximum LTV ratio for self-certification loans has been 90 per cent., although such Loans with an original LTV ratio of above 85 per cent. will not be eligible for the portfolio.

In the case of a property which is being purchased, the "value" for the purposes of the LTV ratio is determined on the lower of the valuer's valuation and 100 per cent. of the purchase price.

Any higher lending charge (where payable, as described below) and arrangement fee may be "added on" to the loan amount. The maximum loan, including such "add-ons", as a percentage of purchase price or valuation (whichever is lower) must not be more than 99 per cent. or 89 per cent. for buy-to-let loans.

### ***Deposits***

The deposit for any purchase should normally be met from a borrower's own resources. However, a builder's deposit or a vendor deposit of up to a maximum of 5 per cent. of the purchase price is allowable. In addition, parental gifts are acceptable (provided that the deposit is not a loan and does not have to be repaid) and, in the case of military personnel, the long service advance of pay can be used to fund a deposit. In all other respects loans taken out to fund the deposit are not allowed. Where there is a purchase at undervalue, the maximum loan will be based on the discounted purchase price. The valuer must be aware of any incentive and refer to this in the valuation report.

### ***Higher lending charge***

Birmingham Midshires does not maintain a domestic mortgage indemnity insurance policy for the loans. Instead, where the LTV ratio exceeds 90 per cent., Birmingham Midshires levies a higher lending charge on the borrower, calculated on the amount by which the LTV ratio exceeds 75 per cent. The mortgages trustee will not have the benefit of any higher lending charges levied by Birmingham Midshires. Any higher lending charge received by the mortgages trustee will be paid to the seller upon receipt.

### ***Status of Applicant(s)***

The maximum amount of the aggregate loan(s) under a mortgage account is determined by the application of an affordability model. This model delivers an individualised result that reflects the applicant's net income, existing credit commitments and burden of family expenditure. The model also calculates the full debt servicing cost at a stressed rate of interest before comparing this cost to the net disposable income that the applicant has available. In the case of Mortgage Plus loans, where the unsecured element is being used for debt consolidation and the

applicants are first-time buyers, no benefit is given in terms of affordability. Otherwise, where the borrower is using the unsecured loan to consolidate debts, any associated savings will be taken into account in determining affordability. Credit scoring (as described below) also influences the decision of how much to lend using the principle that high credit scores infer a proven ability to manage financial affairs. Birmingham Midshires maintains rules on the amount of overtime, bonus or commission income (whether regular or non-guaranteed) that it will allow into the model and as a general rule will allow no more than 60 per cent. of these items (for self-certification loans, 100 per cent. can be allowed). Certain benefit payments are allowed (including tax credits) as these quite often compensate for the taxation and National Insurance deductions that would normally cause lower levels of income to fall below minimum wage levels. This model returns “answers” of zero up to amounts that would equate to over five times income. Regardless, the seller maintains a general policy rule that it will not lend more than an amount equal to five times income.

Since February 2006, Birmingham Midshires does not take income from a second job into account in determining affordability for mainstream applications. When there are two applicants, Birmingham Midshires adds joint incomes together for the purpose of calculating the applicants’ total income. When there are more than two applicants, Birmingham Midshires will only take into account the two highest incomes when assessing affordability.

Employed applicants will be expected to have been employed for a minimum of 6 months in their current role (3 months in the case of buy-to-let loans and self-certification loans) and to have had continuous employment for the last 12 months. Self-employed applicants would normally be expected to have been self-employed for a minimum of 2 years (12 months in the case of buy-to-let loans and self-certification loans).

Birmingham Midshires may exercise discretion within its lending criteria in applying those factors that are used to determine the maximum amount of the loan(s). Accordingly, these parameters may vary for some loans. Birmingham Midshires may take the following into account when exercising discretion: credit score result, existing customer relationship, percentage of LTV, stability of employment and career progression, availability of living allowances and/or mortgage subsidy from the employer, employer’s standing, regularity of overtime, bonus or commission (up to a maximum of 60 per cent. of the income except in the case of self-certification loans, in respect of which 100 per cent. can be allowed), credit commitments, quality of security (such as type of property, repairs, location or saleability) and the increase in income needed to support the loan.

All local authority and housing association tenants must provide rent payment history for the last 12 months. The conduct of an existing mortgage holder will be confirmed from the credit search. All first-time buyers must provide three months’ bank statements. In the case of mainstream mortgages, an employed applicant must provide a form P60 and the latest payslip or the last three months’ payslips or the latest payslip and three months’ bank statements showing salary credit. A self-employed applicant for a mainstream loan must provide the last two years’ accounts or HM Customs & Revenue self-assessment forms or an accountant’s certificate. For loans of up to £100,000, accounts provided by a bookkeeper will be accepted. For all Mortgage Plus applications, income will be verified by means of an income reference, P60 and payslips, accounts or an accountant’s certificate.

Borrowers may be able to exercise the “self-certification” option in respect of their loan (**self-certification loans**) where the original LTV is less than or equal to 80 per cent., pursuant to which they certify their own yearly income figure on the application form and Birmingham Midshires will not normally request proof of income. This is particularly useful for persons such as the self-employed or company directors for whom such a figure will be difficult to determine. In the case of a “self-certification” applicant who is employed, Birmingham Midshires may telephone the stated employer for confirmation that the applicant was indeed employed within the stated organisation. In addition, Birmingham Midshires reserves the right to carry out such checks and to request evidence necessary to satisfy itself as to the borrower’s ability to pay. Self-certification loans with a LTV above 85 per cent. as at origination will not be eligible for inclusion in the pool.

In cases where the original LTV ratio is up to 95 per cent., Birmingham Midshires may, taking into account the results of credit scoring, exercise its discretion and no verification (other than random verification in respect of five per cent. of the loans) will be carried out on the borrower’s ability to pay. However, all Mortgage Plus applications are subject to Birmingham Midshires’ verification procedures regardless of credit score. For all Mortgage Plus applications, income will be verified by means of an income reference, P60 and payslips, accounts or an accountant’s certificate.

The “self-certification” option is available where the borrower wishes to borrow up to £1,000,000.

All self-certification borrowers are alerted to the following criteria when they receive their offer:

- the offer is made based upon the declared income on the application form;

- Birmingham Midshires retains the right to withdraw the offer if any of the declared details relating to income, employment or any other information are found to be incorrect, misleading or untrue or if Birmingham Midshires believes them likely to be incorrect, misleading or untrue;
- if the offer is withdrawn as a result of Birmingham Midshires' enquiries, then the applicant will be responsible for all costs incurred in processing the application, including valuation fees, arrangement fees and any abortive legal costs;
- if the applicant is in any doubt at all about the information that has been provided on the application form or elsewhere, he or she must immediately notify Birmingham Midshires by telephone (in this event, the applicant must not proceed with the transaction until he or she receives Birmingham Midshires' prior approval);
- making a false, misleading or inaccurate declaration is a criminal offence and may lead to prosecution of the applicant and/or the financial adviser, resulting in a fine and/or imprisonment and the applicant and/or his or her financial adviser may also face civil action for recovery of any losses that Birmingham Midshires may have incurred.

### ***Buy-to-let loans***

Buy-to-let loans have been available where, at the time of application, the expected annual rental income equates to a certain percentage, which could not be less than 100 per cent. (the **interest cover percentage**) of the annual (interest only) mortgage payment calculated using the Bank of England base rate + 0.5 per cent. (or, for selected products, the actual product rate). As at the date of this base prospectus, the minimum interest cover percentage for new applications for buy-to-let loans is 125 per cent. Confirmation of the expected rental income will be confirmed as part of the standard valuation at the time of application. Birmingham Midshires categorises each buy-to-let loan according to its interest cover percentage and limits the number of loans with a low interest cover percentage that it has on its books. Borrowers of loans with a higher interest cover percentage usually pay a lower rate of interest to reflect the reduced risk Birmingham Midshires is taking. The maximum LTV ratio for buy-to-let loans is currently 85 per cent. A borrower can borrow up to £1 million for an individual buy-to-let property, with a limit of £10 million across the HBOS group applying to a portfolio of properties. All lettings must be on assured shorthold tenancies (or, in Scotland, short assured tenancies) or to a company on a corporate let and certain types of properties are not considered. The minimum acceptable property value or purchase price (whichever is the lower) is currently £40,000 (£75,000 in London postal districts). Buy-to-let loans are available to UK residents only. If the applicant is a first time buyer, then the maximum loan will be based on earned income. Confirmation of anticipated rental income will be provided by the valuer as part of the valuation.

The maximum term of the applicable assured shorthold tenancy, short assured tenancy or corporate let is 12 months. This can be renewed without the consent of the seller. Multiple lets are not acceptable, with a maximum of five tenants being allowed. For the avoidance of doubt, children are not included in the maximum number of tenants. All tenants must be party to the same tenancy agreement. Student lets, holiday lets and tenants who are asylum seekers, have the benefit of diplomatic immunity or are claiming housing benefit, rent rebate or rent allowance are not acceptable. If the property is in Scotland, the landlord must register with the relevant local authority.

If a borrower (other than a borrower under a buy-to-let loan) has let the property, then Birmingham Midshires will change that borrower's loan to a product from the buy-to-let range.

### ***Credit search***

Credit searches are carried out in respect of all applicants' residential addresses for the 3 years prior to the date of application. Applications may be declined where an adverse credit history (e.g. county court judgment, Scottish court decree for payment, default, bankruptcy notice or sequestration) is revealed which falls outside the criteria for prime customers. Birmingham Midshires does offer loans to customers with an adverse credit history but these loans will not be eligible for the pool.

### ***Credit scoring***

Birmingham Midshires uses some of the criteria described here and various other criteria to produce an overall score for the application that reflects a statistical analysis of the risk of advancing the loan. The lending policies and processes are determined centrally to ensure consistency in the management and monitoring of credit risk exposure. Full use is made of software technology in credit scoring new applications. Credit scoring applies



statistical analysis to publicly available data and customer-provided data to assess the likelihood of an account going into arrears.

Birmingham Midshires reserves the right to decline an application that has received a passing score. Birmingham Midshires does have an appeals process if a potential borrower believes his or her application has been unfairly denied. It is Birmingham Midshires' policy to allow only authorised individuals to exercise discretion in granting variances from the credit score decision.

### ***Buildings insurance***

It is the borrower's responsibility to ensure that comprehensive insurance cover under normal terms (including subsidence and flooding cover) with a reputable insurance company is in place throughout the term of their mortgage to cover the full rebuilding cost of the property, together with professional fees, on a new-for-old basis. The sum insured must be index-linked and the interest of Birmingham Midshires must be noted on the policy.

In the case of most leasehold properties, the insurance will be effected by the landlord in accordance with the terms of the relevant lease.

The conditions of the loans and the mortgages provide that, if a borrower fails to continue to effect buildings insurance, Birmingham Midshires may, upon becoming aware of the same, insure the property itself in which case Birmingham Midshires may determine who the insurer will be, what will be covered by the policy, the amount of the sum insured and any excess. The costs incurred by Birmingham Midshires in arranging and maintaining the buildings insurance policy in force will be charged to the borrower, will form part of the mortgage debt and will bear interest from the date they are incurred until they are repaid. Birmingham Midshires retains the right to settle all insurance claims on reasonable terms without the borrower's consent.

When a mortgaged property is taken into possession by Birmingham Midshires individual policies will be taken out with Legal and General Insurance Limited to ensure that the appropriate insurance cover is provided on the property. Birmingham Midshires may claim under such policy for any damage occurring to the property while in Birmingham Midshires' possession.

## The servicer

### The servicer

Birmingham Midshires services all loans originated by Birmingham Midshires. Pursuant to the servicing agreement Halifax was appointed as and since the reorganisation date Bank of Scotland has been the **servicer** of the loans (originated under the Birmingham Midshires brand). The day-to-day servicing of the loans is performed by the servicer in accordance with the servicing agreement through the servicer's telephone and customer service centres. The servicer's registered office is The Mound, Edinburgh EH1 1Z, United Kingdom.

Basic information on the organisation and history of the servicer is set out in this base prospectus under "**Bank of Scotland plc**" above. For over 100 years the former Birmingham Midshires Building Society, its predecessors and successors, was, and the Bank of Scotland has been, engaged in the servicing of residential mortgage loans originated by them under the Birmingham Midshires brand.

This section describes the servicer's procedures in relation to loans generally. A description of the servicer's obligation under the servicing agreement follows in the next section.

### Servicing of loans

Servicing responsibilities and procedures include responding to customer enquiries, monitoring compliance with and servicing the loans, managing the facilities applicable to the loans and managing the arrears process in connection with the loans. See "**The servicing agreement**" below.

Pursuant to the terms and conditions of the loans, borrowers must pay the monthly amount required on or before each monthly instalment due date. Interest accrues in accordance with the terms and conditions of each loan and is collected from borrowers monthly.

In the case of standard variable rate loans, the servicer sets the standard variable rate and (if applicable) the margin applicable to any tracker rate loan on behalf of the mortgages trustee and the beneficiaries, except in the limited circumstances as set out in the servicing agreement. In the case of loans at a fixed rate of interest, the borrower pays and will pay interest at the relevant fixed rate until the fixed rate period ends in accordance with the borrower's offer conditions. After that period ends, and unless the servicer sends an offer of and the borrower accepts another option, interest will be payable at the standard variable rate or a fixed margin above rates set by the Bank of England.

The servicer will take all steps necessary under the mortgage terms to notify borrowers of any change in the interest rates applicable to the loans, whether due to a change in the standard variable rate or any variable margin or as a consequence of any provisions of those mortgage terms.

Payments of interest and principal on repayment loans are payable monthly in arrear. Payments of interest on interest-only loans are paid in the month that they are due. The servicer is responsible for ensuring that all payments are made by the relevant borrower into the collection account and transferred into the mortgages trustee GIC account on a regular basis but in any event, in the case of payments by direct debits, no later than the next business day after they are deposited in the collection account. All amounts which are paid to the collection account will be held on trust by the seller for the seller and the mortgages trustee until they are transferred to the mortgages trustee GIC account. Payments from borrowers are generally made by direct debits from a suitable bank or building society account, although in some circumstances borrowers pay by cash, cheque or standing order.

The servicer initially credits the mortgages trustee GIC account with the full amount of the monthly payments made by borrowers into the collection account. However, direct debits may be returned unpaid up to three days after the due date for payment and, under the Direct Debit Indemnity Scheme, a borrower may make a claim at any time to its bank for a refund of direct debit payments. In each case, the servicer is permitted to reclaim from the mortgages trustee GIC account the corresponding amounts previously credited. In these circumstances, the usual arrears procedures described in "**– Arrears and default procedures**" below will apply.

### Recent changes

From time to time, Birmingham Midshires reviews and updates its policies and procedures in relation to the servicing of the loans. Some of these changes are market-driven, for example in connection with the introduction of UK mortgage regulation under the FSMA on 31 October 2004. See "**Risk factors – Failure by the seller or any servicer to hold relevant authorisations and permissions under FSMA in relation to regulated mortgage contracts may have an adverse effect on enforceability of mortgage contracts**" above and "**Risk factors – If a significant number of borrowers attempt to set off claims for damages based on**

**contravention of an FSA rule against the amount owing by the borrower under a loan, there could be a material decrease in receipts to the issuing entity from the mortgages trust” above.**

Other changes are driven by Birmingham Midshires from time to time reviewing its procedures and amending them to reflect current trading conditions.

### **Arrears and default procedures**

The servicer regularly provides and will continue to provide the mortgages trustee and the beneficiaries with written details of loans that are in arrears. A loan is identified as being **in arrears** where an amount equal to or greater than a full month’s contractual payment is past its due date. In general, the servicer attempts to collect all payments due under or in connection with the loans, having regard to the circumstances of the borrower in each case. Mortgage collection is conducted through payment collection departments located in Pendeford. The servicer will work constructively with the borrower to agree a course of action. Collections and recovery interventions, including legal action, will be commensurate with the rate of deterioration and the borrower’s willingness to address the arrears as well as risk of further default. The servicer uses an automated collections system to collect and/or negotiate with the borrower through letter/telephone contact.

The servicer’s system tracks arrears and advances and calculates when an amount is in arrears. When arrears are first reported or an amount paid does not satisfy the full contractual monthly payment (calculated as at the due date), the relevant borrower is contacted and asked for payment of the arrears. An automated process exists in which the borrower is contacted through a series of letters and/or structured phone contacts with specific manual intervention at a certain stage commensurate with risk. Where manual intervention is required, the servicer’s personnel will decide on the appropriate course of action. Where no contact has been made or no agreement has been reached, this could result in telephone contact via a dialler and/or the use of an external agent in an attempt to reach a solution with the borrower. The servicer’s employees responsible for settling arrears are trained in all collection and negotiation techniques.

Where considered appropriate, the servicer may enter into arrangements with the borrower regarding the arrears, including:

- arrangements to make each future monthly payment as it falls due plus an additional amount to pay the arrears over a period of time;
- arrangements to make each monthly payment as it falls due;
- arrangements to pay only a portion of each monthly payment as it falls due; and
- a deferment for an agreed period of time of all payments, including interest and principal (in whole or in part).

Any arrangements may be varied from time to time at the discretion of the servicer, the primary aim being to rehabilitate the borrower and recover the situation.

For residential loans, legal proceedings do not usually commence until the arrears become at least two months overdue for high risk loans (loans of above 90 per cent. LTV or balances above £500,000) and overdue for longer periods in the case of lower risk loans. However, the servicer’s employees review each case and have discretion to vary the usual timeframes, having due regard to the case history, reasonable attempts to find a solution, risk and type of lending. For very low risk loans, legal action may be delayed where appropriate to allow more time for recovery.

Once legal proceedings have commenced, the servicer or the servicer’s solicitor may send further letters to the borrower encouraging the borrower to enter into discussions to pay the arrears and may still enter into an arrangement with a borrower at any time prior to a court hearing. If a court order is made for payment and the borrower subsequently defaults in making the payment, then the servicer may take such action as it considers appropriate, including entering into a further arrangement with the borrower. If the servicer applies to the court for an order for possession, the court has discretion as to whether it will grant the order.

After possession, the servicer may take such action as it considers appropriate, including to:

- secure, maintain or protect the property and put it into a suitable condition for sale;

- (other than in Scotland) create any estate or interest on the property, including a leasehold; and
- dispose of the property (in whole or in part) or of any interest in the property by auction, private sale or otherwise, for a price it considers appropriate.

The servicer has discretion as to the timing of any of these actions, including whether to postpone the action for any period of time. The servicer may also carry out such work on the property as it considers appropriate to maintain the market value of the property.

The servicer has discretion to deviate from these procedures. In particular, the servicer may deviate from these procedures where a borrower suffers from a mental or physical infirmity, is deceased or where the borrower is otherwise prevented from making payment due to causes beyond the borrower's control. This applies to both sole and joint borrowers.

It should also be noted that the lender's ability to exercise its power of sale in respect of the property is dependent upon mandatory legal restrictions as to notice requirements. In addition, there may be factors outside the control of the lender, such as whether the borrower contests the sale and the market conditions at the time of sale, that may affect the length of time between the decision of the lender to exercise its power of sale and final completion of the sale.

It should also be noted that, in relation to Scottish mortgages, the Mortgage Rights (Scotland) Act 2001 confers upon the court a discretion (upon application by the borrower or certain other specified persons) to suspend the exercise of the lender's statutory enforcement remedies for such period and to such extent as the court considers reasonable, having regard, among other factors, to the nature of the default, the applicant's ability to remedy it and the availability of alternative accommodation. See "**Material legal aspects of the loans – Scottish loans**" below.

The net proceeds of sale of the property are applied against the sums owed by the borrower to the extent necessary to discharge the mortgage including any accumulated fees, expenses of the servicer and interest. Where the funds arising from application of default procedures are insufficient to pay all amounts owing in respect of a loan, the funds are applied first in paying interest and costs and second in repaying principal. The servicer may then institute recovery proceedings against the borrower. If, after sale of the property and redemption of the mortgage, there are funds remaining, those funds will be distributed by the acting solicitor to the next entitled parties.

These arrears and security enforcement procedures may change over time as a result of a change in the servicer's business practices or legislative and regulatory changes.

## The servicing agreement

The following section contains a summary of the material terms of the servicing agreement. The summary does not purport to be complete and is subject to the provisions of the servicing agreement.

### Introduction

On the programme date, Halifax was appointed by the mortgages trustee, Funding 1 and the seller under the servicing agreement to be their agent to service the loans and their related security. Bank of Scotland has been the servicer since the reorganisation date and must comply with any proper directions and instructions that the mortgages trustee, Funding 1, the seller or, following service of an intercompany loan acceleration notice, the Funding 1 security trustee may from time to time give to it in accordance with the provisions of the servicing agreement. The servicer is required to administer the loans:

- in accordance with the servicing agreement; and
- as if the loans and their related security had not been sold to the mortgages trustee but remained with the seller, and in accordance with the seller's procedures and administration and enforcement policies as they apply to those loans from time to time.

The servicer's actions in servicing the loans in accordance with its procedures are binding on the mortgages trustee. The servicer may, in some circumstances, delegate or sub-contract some or all of its responsibilities and obligations under the servicing agreement. However, the servicer remains liable at all times for servicing the loans and for the acts or omissions of any delegate or sub-contractor.

### Powers

Subject to the guidelines for servicing set forth in the preceding section, the servicer has the power, among other things:

- to exercise the rights, powers and discretions of the mortgages trustee, the seller and Funding 1 in relation to the loans and their related security and to perform their duties in relation to the loans and their related security; and
- to do or cause to be done any and all other things which it reasonably considers necessary or convenient or incidental to the administration of the loans and their related security or the exercise of such rights, powers and discretions.

### Undertakings by the servicer

The servicer has undertaken, among other things:

1. to maintain approvals, authorisations, permissions, consents and licences required in order to perform its obligations under the servicing agreement;
2. to notify borrowers when required of any change in interest rates;
3. to keep records and accounts on behalf of the mortgages trustee in relation to the loans and their related security;
4. to keep customer files in safe custody and maintain records necessary to enforce each mortgage;
5. to provide the mortgages trustee, Funding 1, the respective auditors of the foregoing, the Funding 1 security trustee and any other person nominated by Funding 1 with access to records relating to the administration of the loans and their related security;
6. to make available on a monthly basis to beneficial owners of the notes, who have provided beneficial ownership certification as described in the servicing agreement, a report containing information about the loans in the mortgages trust;
7. to assist the cash manager in the preparation of a quarterly report;

8. to take all reasonable steps, in accordance with the usual procedures undertaken by a reasonable, prudent mortgage lender, to recover all sums due to the mortgages trustee, including instituting proceedings and enforcing any relevant loan or its related security;
9. to enforce any loan which is in default in accordance with its enforcement procedures or, if these are inapplicable, with the usual procedures undertaken by a reasonable, prudent mortgage lender on behalf of the mortgages trustee; and
10. to provide to the rating agencies such information relating to its mortgage business and financial condition as the rating agencies may reasonably request in connection with the ratings of the notes, provided that such request does not adversely interfere with the servicer's day-to-day provision of services under the servicing agreement, and, in particular, to facilitate an annual review if required by the rating agencies of the portfolio.

### Setting of interest rates on the loans

The servicer has undertaken, pursuant to the servicing agreement, to determine and set the standard variable rate and (if applicable) any variable margin applicable in relation to any tracker rate loan in relation to the loans comprising the trust property, provided that (if variable margins are introduced in respect of tracker rate loans in the future) it will not at any time, without the prior consent of the mortgages trustee and Funding 1, set or maintain:

- (i) a margin in respect of any tracker rate loan in respect of which the offer conditions for that loan provide that the margin shall be the same as the margin applicable to all other loans having the same offer conditions in relation to interest rate setting at a rate which is higher or lower than the margin then applying to loans with such offer conditions as are beneficially owned by the seller outside the portfolio; and
- (ii) a margin in respect of any other tracker rate loan at a rate which is higher than the margin which would then be set in accordance with Birmingham Midshires' policy from time to time in relation to that loan if it had remained beneficially owned by the seller outside the portfolio.

In particular, the servicer shall determine on each Funding 1 interest payment date having regard to:

- (A) the revenue which Funding 1 would expect to receive during the next succeeding interest period;
- (B) the standard variable rate and (if applicable) any variable margins applicable in relation to any tracker rate loans which the servicer proposes to set under the servicing agreement; and
- (C) the other resources available to Funding 1, including the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any) and the Funding 1 swap agreement,

whether Funding 1 would receive an amount of revenue during the relevant interest period which is less than the amount which is the aggregate of (1) the amount of interest which is payable by Funding 1 in respect of the term AAA loan tranches on the Funding 1 interest payment date falling at the end of that interest period and (2) all other amounts payable by Funding 1 at or before the end of that interest period which rank equally with or in priority to interest due in respect of the term AAA loan tranches.

If the servicer determines that there would be a shortfall in the foregoing amounts, it will give written notice to the mortgages trustee, Funding 1 and the Funding 1 security trustee, within one London business day of such determination, of the amount of the shortfall and the standard variable rate and/or (if applicable) any variable margins applicable in relation to any tracker rate loans which would, in the servicer's opinion, need to be set in order for no shortfalls to arise, having regard to the date(s) on which the change to the standard variable rate and any variable margins (if applicable) would take effect and at all times acting in accordance with the standards of a reasonable, prudent mortgage lender as regards the competing interests of borrowers with standard variable rate loans and (if applicable) borrowers with tracker rate loans. If the mortgages trustee and/or Funding 1 notifies the servicer that, having regard to the obligations of Funding 1, the standard variable rate and/or (if applicable) any variable margins should be increased, the servicer will take all steps which are necessary to increase the standard variable rate and/or (if applicable) any variable margins, including publishing any notice which is required in accordance with the applicable mortgage terms.

The mortgages trustee or Funding 1 (with the consent of the Funding 1 security trustee) may terminate the authority of the servicer to determine and set the standard variable rate and (if applicable) any variable margins on the occurrence of a **servicer termination event** as defined under “– **Removal or resignation of the servicer**” below, in which case the mortgages trustee will set the standard variable rate and any variable margins itself in accordance with the above provisions.

### **Reasonable, prudent mortgage lender**

The requirement for any action to be taken according to the standards of a **reasonable, prudent mortgage lender** is as defined in the Glossary. For the avoidance of doubt, any action taken by the servicer to set standard variable rates and (if applicable) any variable margins applicable in relation to any tracker rate loans which are lower than that of the competitors of the seller will be deemed to be in accordance with the standards of a reasonable, prudent mortgage lender.

### **Compensation of the servicer**

The servicer receives a fee for servicing the loans and their related security. The mortgages trustee pays to the servicer a servicing fee (inclusive of VAT, if any) of 0.05 per cent. per annum on the aggregate amount of the trust property as at the immediately preceding calculation date. The fee is payable in arrear on each distribution date only to the extent that the mortgages trustee has sufficient funds to pay it. Any unpaid balance is carried forward until the next distribution date and, if not paid earlier, is payable on the latest occurring final repayment date of any loan tranche advanced under the intercompany loan agreement or on the earlier repayment in full by Funding 1 of all loan tranches under the intercompany loan agreement.

### **Removal or resignation of the servicer**

The mortgages trustee, Funding 1 (with the consent of the Funding 1 security trustee) or (following service of an intercompany loan acceleration notice) the Funding 1 security trustee may, upon written notice to the servicer, terminate the servicer's rights and obligations immediately if, among other things, any of the following events (each a **servicer termination event**) occurs:

- the servicer defaults in the payment of any amount due and fails to remedy that default for a period of five London business days after the earlier of becoming aware of the default and receipt of written notice from the mortgages trustee, Funding 1 and/or (following service of an intercompany loan acceleration notice) the Funding 1 security trustee requiring the default to be remedied;
- the servicer fails to comply with any of its other covenants or obligations under the servicing agreement which the Funding 1 security trustee is directed by the issuing entity security trustee, which is directed by the note trustee, is, in the opinion of the note trustee, materially prejudicial to the interests of the noteholders and (in each case) does not remedy that failure within 20 London business days after becoming aware of the failure; or
- an insolvency event occurs in relation to the servicer.

Subject to the fulfilment of a number of conditions (including the appointment of a substitute servicer), the servicer may voluntarily resign by giving not less than 12 months' notice to the mortgages trustee, Funding 1, the Funding 1 security trustee and the seller. The substitute servicer is required to have experience of administering mortgages in the United Kingdom and to enter into a servicing agreement with the mortgages trustee, Funding 1, the seller and the Funding 1 security trustee substantially on the same terms as the servicing agreement. It is a further condition precedent to the resignation of the servicer that the current ratings of the notes are not downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of the resignation, unless the relevant classes of noteholders otherwise agree by extraordinary resolutions.

If the appointment of the servicer is terminated, the servicer must deliver customer files relating to the loans to, or at the direction of, the mortgages trustee. The servicing agreement will terminate when Funding 1 ceases to have any interest in the trust property.

No provision is made in the servicing agreement or otherwise for any costs and expenses associated with the transfer of servicing to a substitute servicer and therefore such costs and expenses will be borne by the seller and Funding 1 as beneficiaries of the mortgages trust. The servicing fee payable to a substitute servicer will be agreed with that substitute servicer prior to its appointment.

### **Right of delegation by the servicer**

The servicer may sub-contract or delegate the performance of its duties under the servicing agreement, provided that it meets particular conditions, including that:

- Funding 1 and the Funding 1 security trustee consent to the proposed sub-contracting or delegation (except in respect of any delegation to a wholly-owned subsidiary of Bank of Scotland or HBOS plc from time to time or to persons such as receivers, lawyers or other relevant professionals);
- notification has been given to each of the rating agencies;
- where the arrangements involve the custody or control of any customer files, the sub-contractor or delegate has provided a written acknowledgement that those customer files will be held to the order of the mortgages trustee (as trustee for the beneficiaries);
- where the arrangements involve the receipt by the sub-contractor or delegate of monies belonging to the beneficiaries (which are to be paid into the mortgages trustee GIC account and/or the Funding 1 GIC account), the sub-contractor or delegate has executed a declaration that any such monies are held on trust for the beneficiaries and will be paid forthwith into the mortgages trustee GIC account or, as applicable, the Funding 1 GIC account in accordance with the terms of the mortgages trust deed;
- the sub-contractor or delegate has executed a written waiver of any security interest arising in connection with the delegated services; and
- the mortgages trustee, Funding 1 and the Funding 1 security trustee shall have no liability for any costs, charges or expenses in relation to the proposed sub-contracting or delegation.

If the servicer sub-contracts or delegates the performance of its duties, it will nevertheless remain responsible for the performance of those duties to the mortgages trustee, Funding 1 and the Funding 1 security trustee.

### **Liability of the servicer**

The servicer will indemnify the mortgages trustee and the beneficiaries against all losses, liabilities, claims, expenses or damages incurred as a result of negligence or wilful default by the servicer in carrying out its functions under the servicing agreement or any other transaction document or as a result of a breach of the terms of the servicing agreement. If the servicer does breach the terms of the servicing agreement and thereby causes loss to the beneficiaries, then the seller share will be reduced by an amount equal to such loss.

### **Governing law**

The servicing agreement is governed by English law, provided that any terms of the servicing agreement particular to Scots law will be construed in accordance with the laws of Scotland.



## Sale of the loans and their related security

The following section contains a summary of the material terms of the mortgage sale agreement. The summary does not purport to be complete and is subject to the provisions of the mortgage sale agreement.

### Introduction

Loans and their related security will from time to time be sold to the mortgages trustee pursuant to the terms of a mortgage sale agreement entered into on the programme date between the seller, the mortgages trustee, Funding 1 and the Funding 1 security trustee. The mortgage sale agreement has six primary functions:

- it provides for the sale of the loans and their related security and the transfer of the beneficial interest therein;
- it sets out the circumstances under which new loans can be sold to the mortgages trustee;
- it provides for the legal assignment or assignation (as appropriate) of the loans and their related security to the mortgages trustee;
- it sets out the representations and warranties to be given by the seller; and
- it provides for the repurchase of mortgage accounts and related security with respect to loans (1) which (in limited circumstances) are subject to a product switch, (2) which are subject to a further advance or (3) which cause the seller to be in breach of any of its representations and warranties in respect of the loans.

### Sale of loans and their related security to the mortgages trustee on the sale dates

Pursuant to the mortgage sale agreement, the seller transferred, on the programme date, by way of an equitable assignment (or, in the case of Scottish loans, by way of a declaration of trust) to the mortgages trustee the initial loans, together with their related security.

The mortgage sale agreement provides that the seller may sell new loans and their related security to the mortgages trustee, which may have the effect of increasing or maintaining the overall size of the trust property. The new loans may include loans with characteristics that are not currently being offered to borrowers or that have not yet been developed. New loans and their related security can only be sold to the mortgages trustee if certain conditions, as described in this section, are met.

In addition, any other member of the HBOS group (each, a **new seller**) may in the future sell loans and their related security to the mortgages trustee. Each new seller will accede to the terms of the mortgage sale agreement (with such subsequent amendments as may be agreed by the parties thereto) so that it has, in relation to those new loans and their related security to be sold by the relevant new seller, substantially the same rights and obligations as the seller had in relation to those loans and their related security comprised in the initial portfolio under the mortgage sale agreement.

It is also expected that each new seller will:

- accede to the terms of the mortgages trust deed and the controlling beneficiary deed (with such subsequent amendments as may be agreed by the parties thereto) so that it has, in relation to the mortgages trust, substantially the same rights and obligations as the seller has in relation to the mortgages trust as at the programme date;
- enter into hedging arrangements in order to provide hedging between the rates of interest payable on the loans it has sold to the mortgages trustee and the floating rates of interest payable in respect of the loan tranches; and
- accede to the programme agreement and enter into such other documentation as may be required by the Funding 1 security trustee and/or the mortgages trustee to give effect to the addition of a new seller to the transactions contemplated under the transaction documents and the programme.

Any loans and their related security sold by a new seller to the mortgages trustee will comply with the conditions precedent to the sale of new loans and their related security as summarised below.

The Funding 1 security trustee, the issuing entity security trustee and, as applicable, the note trustee shall agree to any modifications to the transaction documents that are requested by Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf), provided that Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf) certifies to the Funding 1 security trustee, the issuing entity security trustee or, as applicable, the note trustee in writing that such modifications are required in order to accommodate the accession of such new seller to the mortgage sale agreement and any other transaction documents (which consent shall be subject to confirmation from each of the rating agencies then rating the notes that the relevant modifications will not result in a reduction, withdrawal or (in the case of S&P and Moody's) qualification of the then current ratings of the notes).

If the above conditions are met, the consent of noteholders will not be obtained to the accession of a new seller to the programme.

The mortgages trustee will hold the new loans and their related security on trust for the seller and Funding 1 pursuant to the terms of the mortgages trust deed. Full legal assignment or assignation (as appropriate) of the loans will be deferred until a later date, as described under “– **Legal assignment of the loans to the mortgages trustee**” below. Changes may be required to the mortgage sale agreement if new types of loans are sold to the mortgages trustee. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may adversely affect your interests**”, “**Security for Funding 1’s obligations**” and “**Security for the issuing entity’s obligations**”.

On and following the programme date, on the date of each relevant sale, the consideration paid to the seller consisted and will consist of:

- payment by Funding 1 to the seller by telegraphic transfer of the proceeds of any loan tranches under the intercompany loan agreement;
- a covenant by Funding 1 to pay, at a later date, deferred consideration to the seller; and/or
- the promise by the mortgages trustee to hold the trust property on trust for the seller and Funding 1 (in each case, as to their respective shares) in accordance with the terms of the mortgages trust deed.

Funding 1 and the seller (as beneficiaries of the mortgages trust) are not entitled to retain any fees received by the mortgages trustee, which (except in relation to fees payable to the mortgages trustee for the work undertaken by it as trustee of the mortgages trust) the mortgages trustee will return to the seller upon receipt and identification thereof by the servicer.

The sale of new loans and their related security to the mortgages trustee will, in all cases, be subject to certain conditions precedent (each of which may be varied or waived by the mortgages trustee where it has received written confirmation from the rating agencies that such variation or waiver will not cause its ratings of the notes then outstanding to be downgraded, withdrawn or (in the case of S&P and Moody's) qualified) being satisfied on the date of the relevant sale date (**sale date**), including the following conditions:

- that, on the relevant sale date, no intercompany loan event of default and no note event of default has occurred which is continuing as at the relevant sale date;
- the Funding 1 principal deficiency ledger (other than the subordinated loan principal deficiency sub-ledger) does not have a debit balance as at the most recent Funding 1 interest payment date after applying all Funding 1 available revenue receipts on that Funding 1 interest payment date (for a description of the Funding 1 principal deficiency ledger, see “**Credit structure – Funding 1 principal deficiency ledger**” below);
- the mortgages trustee is not aware that the purchase of the new loans on the relevant sale date would adversely affect the then current ratings by Fitch, Moody’s or Standard & Poor’s of any of the notes;

- as at the relevant sale date, the seller has not received any notice that the short-term, unsecured, unguaranteed and unsubordinated debt obligations of the seller are rated below F1 by Fitch, P-1 by Moody's and A-1 by Standard and Poor's at the time of, and immediately following, the sale of new loans to the mortgages trustee;
- as at the relevant sale date, the aggregate outstanding principal balance of loans in the mortgages trust in respect of which the aggregate amount in arrears is more than three times the monthly payment then due is less than 5 per cent. of the aggregate outstanding principal balance of the loans in the mortgages trust or any higher percentage that each of the rating agencies (other than Moody's) have confirmed will not cause its then current ratings of the notes to be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of the proposed sale of loans;
- except where Funding 1 pays amounts to the seller in consideration of the new loans to be sold to the mortgages trustee on the relevant sale date, the aggregate outstanding principal balance (excluding arrears of interest) of new loans transferred in any one interest period must not, without the prior consent of Fitch & S&P, exceed 15 per cent. of the aggregate outstanding principal balance of loans (excluding arrears of interest) in the mortgages trust as at the beginning of that interest period;
- the sale of new loans on the relevant sale date does not result in the product of the weighted average foreclosure frequency (**WAFF**) and the weighted average loss severity (**WALS**) for the loans comprised in the portfolio (calculated on such sale date in the same way as it was calculated for the loans comprised in the portfolio as at the most recent closing date (or as otherwise agreed by the servicer and the rating agencies from time to time)) exceeding the product of the WAFF and WALS (when tested at the "AAA level") for the loans comprised in the portfolio calculated as at the most recent closing date, plus 0.25 per cent.;
- the yield of the loans in the mortgages trust together with the yield of the new loans to be sold to the mortgages trustee on the relevant sale date is at least 0.50 per cent. greater than sterling-LIBOR for three-month sterling deposits as at the previous Funding 1 interest payment date after taking into account the weighted average yield on the loans which are standard variable rate loans, tracker rate loans and fixed rate loans and the margins on the Funding 1 swap, in each case as at the relevant sale date;
- the sale of new loans on the relevant sale date does not result in the loan-to-value ratio of the loans comprised in the portfolio, after application of the LTV test on the relevant sale date, exceeding the loan-to-value ratio (based on the LTV test) as determined in relation to the loans comprised in the portfolio on the most recent previous closing date, plus 0.25 per cent.;
- the sale of new loans on the relevant sale date does not result in the loans comprised in the portfolio (other than fixed rate loans) that, after taking into account the Funding 1 swap, will yield less than sterling-LIBOR plus 0.50 per cent. as at the relevant sale date and have more than 2 years remaining on their incentive period accounting for more than 15 per cent. of the aggregate outstanding principal balance of loans comprised in the trust property;
- the sale of the new loans on the relevant sale date does not result in the fixed rate loans comprised in the portfolio that have more than 1 year remaining on their incentive period accounting for more than the percentage specified in the most recent final terms of the aggregate outstanding principal balance of loans comprised in the trust property (the **fixed rate loans percentage**);
- the sale of loans on the relevant sale date does not result in buy-to-let loans accounting for more than the percentage specified in the most recent final terms of the aggregate principal amount outstanding of loans comprised in the portfolio (the **buy-to-let loans percentage**);
- the sale of loans on the relevant sale date does not result in self-certification loans accounting for more than the percentage specified in the most recent final terms of the aggregate principal amount outstanding of loans comprised in the portfolio (the **self-certification loans percentage**);

- the sale of loans on the relevant sale date does not result in any self-certification loans with an original LTV ratio of more than 85 per cent. being transferred into the portfolio;
- as at the relevant sale date, no step-up date in respect of any note issued which is still outstanding has been reached provided that, for the avoidance of doubt, upon the redemption of any such note the sale of new loans to the mortgages trustee may be resumed in accordance with the terms of the mortgage sale agreement;
- as at the relevant sale date, the adjusted Funding 1 general reserve fund level is equal to or greater than the Funding 1 general reserve fund threshold;
- if the sale of loans would include the sale of new types of loan products to the mortgages trustee (including where the sale is of loans originated under a brand within the HBOS group other than Birmingham Midshires or is from an entity other than the seller), the Funding 1 security trustee and/or Funding 1 has received written confirmation from each of the rating agencies that such new types of loan products may be sold to the mortgages trustee and that such sale of new types of loan products would not have an adverse effect on the then current ratings of the notes;
- Funding 1 has entered into appropriate hedging arrangements to hedge against the interest rates payable in respect of the loans being sold and the floating rate of interest payable under the intercompany loan; and
- no trigger event has occurred on or before the relevant sale date.

On the relevant sale date, the representations and warranties in respect of new loans being sold to the mortgages trustees and their related security (described below in “– **Representations and warranties**” below) will also be given by the seller.

In the mortgage sale agreement, the seller undertakes, in respect of each series and class of notes issued by the issuing entity and each issuing entity subordinated loan advanced to the issuing entity and the corresponding rated loan tranches and subordinated loan tranches made available to Funding 1 under the intercompany loan, to use reasonable efforts to offer to sell to the mortgages trustee, and the mortgages trustee has undertaken to use reasonable efforts to acquire from the seller and hold in accordance with the terms of the mortgages trust deed, until the earlier of the latest occurring step-up date for any series and class of notes (or such later date as may be notified by Funding 1 to the seller) and the occurrence of a trigger event, sufficient new loans and their related security so that the aggregate outstanding principal balance of loans in the mortgages trust during the period from (and including) the relevant closing date to (but excluding) the interest payment date specified in the most recent final terms is not less than the amount specified in the most recent final terms. However, the seller is not obliged to sell to the mortgages trustee, and the mortgages trustee is not obliged to acquire, new loans and their related security if, in the opinion of the seller, that sale would adversely affect the business of the seller. In the event that Funding 1 borrows further loan tranches under the intercompany loan following further series and classes of notes being issued by the issuing entity and/or an issuing entity subordinated loan being advanced to the issuing entity and the corresponding loan tranches being made available to Funding 1 under the intercompany loan, then the period during which the seller covenants to use reasonable efforts to maintain the aggregate outstanding principal balance of loans in the mortgages trust at a specified level may be extended.

#### **Legal assignment of the loans to the mortgages trustee**

The English loans in the portfolio have been and will be sold to the mortgages trustee by way of equitable assignment. The Scottish loans in the portfolio have been and will be sold to the mortgages trustee by way of declarations of trust under which the beneficial interest in such Scottish loans has been or will be transferred to the mortgages trustee. In relation to Scottish loans, references in this base prospectus to the sale of loans are to be read as references to the making of such declarations of trust. This means that legal title to both English loans and Scottish loans and their related security remains with the seller until legal assignments or assignments (as appropriate) are delivered by the seller to the mortgages trustee (and, in the case of Scottish loans, registered or recorded in the relevant property register) and notice of such assignments or assignments (as appropriate) is given by the seller to the borrowers. Legal assignment or assignment (as appropriate) of the loans and their related security (including, where appropriate, their registration or recording in the relevant property register) to the mortgages trustee will be deferred and will only take place in the limited circumstances described below. See

**“Risk factors – There may be risks associated with the fact that the mortgages trustee has no legal title to the loans and their related security, which may adversely affect payments on the notes”** above.

Legal assignment or assignation (as appropriate) of the loans and their related security to the mortgages trustee is completed on the 20th London business day after the earliest to occur of any of, amongst other things:

- the service of an intercompany loan acceleration notice or a note acceleration notice;
- the seller being required to perfect the mortgages trustee’s legal title to the mortgages by an order of a court of competent jurisdiction or by a regulatory authority to which the seller is subject or any organisation whose members comprise, but are not necessarily limited to, mortgage lenders with whose instructions it is customary for the seller to comply;
- it being rendered necessary by law to take actions to perfect legal title to the mortgages;
- the security under the Funding 1 deed of charge or any material part of that security being in jeopardy and the Funding 1 security trustee deciding to take action to reduce materially that jeopardy;
- unless otherwise agreed by the rating agencies and the Funding 1 security trustee, the termination of the seller’s role as servicer under the servicing agreement;
- the seller requesting perfection by serving notice in writing on the mortgages trustee, Funding 1, and the Funding 1 security trustee;
- the date on which the seller ceases to be assigned a long-term unsecured, unsubordinated unguaranteed debt obligation rating by Fitch of at least BBB-, by Moody’s of at least Baa3 or by Standard & Poor’s of at least BBB-;
- the occurrence of an insolvency event in relation to the seller; or
- the latest occurring final repayment date of any loan tranches advanced under the intercompany loan agreement that have not been discharged in full.

Pending completion of the transfer, the right of the mortgages trustee to exercise the powers of the legal owner of the mortgages has been and will be secured by an irrevocable power of attorney granted by the seller in favour of the mortgages trustee, Funding 1 and the Funding 1 security trustee.

To the extent not held at the relevant land registry electronically, the customer files relating to the loans are currently held by or to the order of the seller or by solicitors, licensed conveyancers or (in Scotland) qualified conveyancers acting for the seller in connection with the creation of the loans and their related security. The seller has undertaken that all the title deeds and customer files relating to the loans which are at any time in its possession or under its control or held to its order will be held to the order of the mortgages trustee.

## Representations and warranties

None of the mortgages trustee, Funding 1, the Funding 1 security trustee, the issuing entity, the issuing entity security trustee or the note trustee has made or has caused to be made on its behalf any enquiries, searches or investigations in respect of the loans and their related security. Instead, each is relying entirely on the representations and warranties by the seller contained in the mortgage sale agreement. The representations and warranties in relation to each loan are made on the relevant sale date that loan (together with its related security) is sold to the mortgages trustee (including loans which were repurchased by the seller pursuant to a further advance or a product switch). The parties to the mortgage sale agreement may, with the prior written consent of the Funding 1 security trustee (which consent shall (subject to Condition 16) be given if each of the rating agencies confirms in writing that its ratings of the notes as at that time will not be downgraded, withdrawn or qualified as a result), amend the representations and warranties contained in the mortgage sale agreement. The material representations and warranties are as follows:

- each loan was originated by the seller in pounds sterling and is denominated in pounds sterling (or was originated and is denominated in euro if the euro has at the time of origination been adopted as the lawful currency of the United Kingdom);
- each loan in the portfolio was made no earlier than 1 January 2003;
- the final maturity date of each loan is no later than (a) May 2057 or (b) such later date specified in the most recent final terms;
- no loan has an outstanding principal balance of more than £750,000;
- no loan is a sub-prime loan;
- no loan is a staff loan;
- no loan is a right-to-buy loan;
- no borrower is or has within the previous six years been subject to a county court judgment or Scottish court decree for payment, default, bankruptcy notice or sequestration;
- prior to the making of each advance under a loan, the lending criteria and all preconditions to the making of any loan were satisfied in all material respects subject only to such exceptions made on a case by case basis as would be acceptable to a reasonable, prudent mortgage lender;
- in relation to a Mortgage Plus loan, not more than 5 per cent. of the aggregate outstanding principal amount of the portfolio are Mortgage Plus loans, subject to receipt of confirmation from each of the rating agencies that its then rating of the notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result thereof;
- other than with respect to monthly payments, no borrower is or has, since origination of the relevant loan, been in material breach of any obligation owed in respect of such loan or under the related security and accordingly no steps have been taken by the seller to enforce any related security;
- the total amount of arrears of interest or principal on any loan (together with any fees, commissions and premiums payable at the same time as an interest payment or principal repayment in respect of such loan) is not on the relevant sale date in respect of such loan, nor has been during the 12 months immediately preceding the relevant sale date, more than the amount of the monthly payment then due;
- all of the borrowers are individuals and were aged 18 years or older at the date of origination of the relevant loan;

- at least two monthly payments have been made in respect of each loan;
- the whole of the outstanding principal balance on each loan, including any arrears of interest and all accrued interest is secured by a mortgage;
- each mortgage constitutes a valid and subsisting first charge by way of legal mortgage or (in Scotland) standard security over the relevant property, subject only in certain appropriate cases to applications for registrations at the Land Registry or Registers of Scotland which where required have been made and are pending and, in relation to which, the seller is not aware of any notice or any other matter that would prevent such registration;
- all of the properties are in England, Wales or Scotland;
- each property constitutes a separate completed dwelling unit (subject to such limited case by case exceptions as would be acceptable to a reasonable, prudent mortgage lender) and is either freehold, leasehold or (in Scotland) heritable or held under a long lease;
- not more than 12 months (or such longer period as may be acceptable to a reasonable, prudent mortgage lender) prior to the grant of each mortgage (other than a remortgage), the seller received a valuation report on the relevant property (or such other form of report concerning the valuation of the relevant property as would be acceptable to a reasonable, prudent mortgage lender), the contents of which were such as would be acceptable to a reasonable, prudent mortgage lender;
- the benefit of all valuation reports, any other report concerning valuation referred to in this section (if any) and certificates of title (if any) can be validly assigned to the mortgages trustee without obtaining the consent of the relevant valuer, solicitor, licensed conveyancer or (in Scotland) qualified conveyancer;
- prior to the taking of each mortgage (other than a remortgage), the seller (a) instructed its solicitor, licensed conveyancer or (in Scotland) qualified conveyancer to carry out an investigation of title to the relevant property and to undertake such other searches, investigations, enquiries and other actions on behalf of the seller in accordance with the instructions which the seller issued to the relevant solicitor, licensed conveyancer or qualified conveyancer as are set out (in the case of English loans) in the CML's Lenders' Handbook for England & Wales and (in the case of Scottish loans) the CML's Lenders' Handbook for Scotland or such other comparable or successor instructions and/or guidelines as may for the time being be in place, subject only to such variations as would be acceptable to a reasonable, prudent mortgage lender and (b) received a certificate of title from such solicitor, licensed conveyancer or qualified conveyancer relating to such property, the contents of which would have been acceptable to a reasonable, prudent mortgage lender at that time;
- insurance cover for each property is available under a seller-introduced insurance policy, another policy arranged by the relevant borrower or landlord or any properties in possession cover;
- the seller has good title to, and is the absolute unencumbered legal and beneficial owner of, all property, interests, rights and benefits agreed to be sold and/or assigned by the seller to the mortgages trustee under the mortgage sale agreement;
- each loan and its related security is valid, binding and enforceable in accordance with its terms and is non-cancellable except in relation to any term of any loan or its related security, that is not binding by virtue of the Unfair Terms in Consumer Contracts Regulations 1994 as amended, extended or re-enacted from time to time or (as the case may be) the Unfair Terms in Consumer Contracts Regulations 1999 as amended, extended or re-enacted from time to time;
- to the best of the seller's knowledge, none of the terms of any loan or its related security is not binding by virtue of its being unfair within the meaning of the UTCCR as amended, extended or re-enacted from time to time;

- the seller has, since the making of each loan, kept or procured the keeping of full and proper accounts, books and records showing clearly all transactions, payments, receipts, proceedings and notices relating to such loan; and
- there are no authorisations, permissions, approvals, licences or consents required, as appropriate, for the seller to enter into or to perform its obligations under the mortgage sale agreement or to make the mortgage sale agreement legal, valid, binding and enforceable.

If new types of loans are to be sold to the mortgages trustee, then the representations and warranties in the mortgage sale agreement will be modified as required to accommodate these new types of loans. Your prior consent to the requisite amendments will not be obtained.

### **Repurchase of loans under a mortgage account**

Under the mortgage sale agreement, if a loan does not, on the relevant sale date, materially comply with the representations and warranties made under the mortgage sale agreement with respect to such loan:

- the seller is required to remedy the breach within 20 London business days of the seller becoming aware of the breach; or
- if the breach is not remedied within the 20 London business day period, then the mortgages trustee will at the direction of Funding 1 require the seller to purchase the loan or loans under the relevant mortgage account and their related security from the mortgages trustee at a price equal to their outstanding principal balances, including any arrears of interest and accrued and unpaid interest and expenses as at the date of repurchase.

The seller is also required, at the direction of Funding 1, to repurchase the loan or loans under any mortgage account and its or their related security if a court or other competent authority or any ombudsman makes any determination in respect of any such loan and its related security that:

- any term which relates to the recovery of interest under the standard documentation applicable to that loan and its related security is unfair; or
- (if variable margins are introduced in respect of tracker rate loans in the future) the variable margin above the Bank of England repo rate under any tracker rate loan must be set by the seller (rather than its successors or assigns or those deriving title from them); or
- the interest payable under any loan is to be set by reference to an interest rate other than that set or purported to be set by either the servicer or the mortgages trustee as a result of the seller having more than one standard variable rate.

If the seller fails to pay the consideration due for the repurchase (or otherwise fails to complete the repurchase), then the seller share shall be deemed to be reduced by an amount equal to that consideration.

### **Drawings under flexible loans**

The seller is solely responsible for funding all future drawings in respect of any flexible loans included in the trust property. The amount of the seller share will increase by the amount of the drawing.

### **Further advances**

If, at its discretion, the seller makes or causes the servicer to send an offer of a further advance under a loan to a borrower, then the seller will be required at the direction of Funding 1 to repurchase the relevant loan or loans under the relevant mortgage account (save for any loan in arrears, where no repurchase will be required) at a price equal to the outstanding principal balance of those loans, including accrued and unpaid interest and expenses to the date of purchase. For the avoidance of doubt, neither the mortgages trustee nor Funding 1 is under any obligation to fund any further advance.



## **Product switches**

If the seller would be in breach of the conditions precedent to the sale of new loans to the mortgages trustee listed in “**Sale of loans and their related security to the mortgages trustee on the sale dates**” above on any distribution date immediately preceding a product switch (as tested on each such date), then from (and including) such distribution date to (but excluding) the date when those conditions precedent have been satisfied, the seller is required at the direction of Funding 1 to repurchase any loans and their related security that are subject to product switches (save for any loan in arrears, where no repurchase will be required). The seller is required to repurchase the loan or loans under the relevant mortgage account and their related security from the mortgages trustee at a price equal to the outstanding principal balance of those loans, including accrued and unpaid interest and expenses to the date of purchase.

A loan will be subject to a **product switch** if the relevant borrower and the seller agree on, or the servicer sends an offer of, a variation in the financial terms and conditions applicable to the relevant loan other than:

- (a) any variation agreed with a borrower to control or manage arrears on the loan;
- (b) any variation in the maturity date of the loan unless, while any loan tranche under the intercompany loan agreement is outstanding, it is extended beyond the later of May 2057 and the date specified in the most recent final terms;
- (c) any variation imposed by statute; or
- (d) any variation to the frequency with which the interest payable in respect of the loan is charged.

## **Portable loans**

The seller is also required at the direction of Funding 1 to repurchase a loan that is a portable loan, together with its related security, on the London business day following the date that the borrower transfers the loan balance at the same interest rate and subject to all the existing terms and conditions to a new property. The seller will repurchase the portable loan and its related security from the mortgages trustee at a price equal to its outstanding principal balance, including accrued and unpaid interest and expenses to the date of purchase, as of the London business day immediately following the transfer date.

## **Reasonable, prudent mortgage lender**

Reference in the documents to the seller and/or the servicer acting to the standard of a **reasonable, prudent mortgage lender** means the seller and/or the servicer, as applicable, acting in accordance with the standards of a reasonably prudent prime residential mortgage lender lending to borrowers in England Wales and Scotland who generally satisfy the lending criteria of traditional sources of residential mortgage capital.

## **Governing law**

The mortgage sale agreement is governed by English law, provided that any terms of the mortgage sale agreement particular to Scots law shall be construed in accordance with the laws of Scotland.

## The mortgages trust

The following section contains a summary of the material terms of the mortgages trust deed. The summary does not purport to be complete and is subject to the provisions of the mortgages trust deed.

### General legal structure

The mortgages trust was established on the programme date under English law with the mortgages trustee as trustee for the benefit of the seller and Funding 1 as beneficiaries. New funding beneficiaries may become beneficiaries of the mortgages trust from time to time, subject to confirmation having been received from each of the rating agencies that its then rating of the notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result thereof (see "**Risk Factors – Holdings may establish other companies, each of which may become an additional beneficiary under the mortgages trust**").

This section describes the material terms of the mortgages trust, including how money is distributed from the mortgages trust to Funding 1 and the seller. If other funding beneficiaries become beneficiaries of the mortgages trust and/or new types of loans are added to the mortgages trust and/or loans are sold to the mortgages trustee that are originated under any brand other than Birmingham Midshires or by an entity other than the seller, then the terms of the mortgages trust may be amended. Such amendments may affect the timing of payments on the notes. Your prior consent will not be sought in relation to any such proposed amendments to the mortgages trust deed, provided (among other things) that the rating agencies confirm that the then current ratings of the notes will not be adversely affected by such amendments. There can be no assurance that the effect of any such amendments will not ultimately adversely affect your interests. See "**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree modifications to the transaction documents without your prior consent, which may adversely affect your interests**", "**Security for Funding 1's obligations**" and "**Security for the issuing entity's obligations**".

Under the terms of the mortgages trust deed, the mortgages trustee holds all of the trust property on trust absolutely for the benefit of Funding 1 and the seller. The **trust property** consists of:

- the portfolio of loans and their related security sold to the mortgages trustee by the seller;
- any new loans and their related security sold to the mortgages trustee by the seller after the programme date;
- any increase in the outstanding principal balance of a loan due to capitalised interest, capitalised expenses, capitalised arrears or a borrower making a drawing under any flexible loan and accrued interest on such loan;
- any interest and principal paid by borrowers on their loans prior to distribution under the mortgages trust deed;
- any other amounts received under the loans and related security (excluding third party amounts);
- amounts on deposit in the mortgages trustee GIC account and interest earned thereon; and
- any other property representing the above,

less:

- any actual losses in relation to the loans and any actual reductions occurring in respect of the loans as described in paragraph (1) in "**– Funding 1 share**" below; and
- distributions of revenue receipts and principal receipts made from time to time to the beneficiaries of the mortgages trust.

Funding 1 is not entitled to particular loans and their related security separately from the seller. Instead each of the beneficiaries has an undivided interest in all of the loans and their related security forming part of the trust property. The beneficial interests of Funding 1 and the seller represent *pro rata* interests in the trust property.

The applicable final terms will set out the approximate Funding 1 share and seller share as at the relevant closing date.

### **Fluctuation of shares in the trust property**

The Funding 1 share and the seller share will fluctuate depending on a number of factors, including:

- the allocation of principal receipts on the loans to Funding 1 and/or the seller;
- losses arising on the loans;
- new loans and their related security being sold to the mortgages trustee;
- Funding 1 acquiring part of the seller share (see further under “– **Acquisition by Funding 1 of an increased interest in the trust property**”);
- a borrower making underpayments or taking payment holidays under a loan;
- a borrower making a drawing under a flexible loan; and
- the seller acquiring part of the Funding 1 share as described in “– **Acquisition by the seller of an interest relating to capitalised interest**” below and “– **Payment by the seller of the amount outstanding under a loan tranche**” below.

The Funding 1 share may not be reduced below zero. The seller is not entitled to receive principal receipts which would reduce the seller share to an amount less than the minimum seller share (as defined below), unless and until the Funding 1 share has been reduced to zero or following the occurrence of an asset trigger event.

On the programme date, Funding 1, pursuant to the terms of the mortgages trust deed, used the proceeds of loan tranches (excluding start-up loan tranches) to be made on such date by the issuing entity pursuant to the intercompany loan agreement to make a payment to the seller of the initial purchase price in respect of the initial portfolio to be assigned to the mortgages trustee on such date. Subsequently, Funding 1 will from time to time use the proceeds of loan tranches (excluding start-up loan tranches) (less any amount utilised to fund the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any)) to make payment to the seller of the initial purchase price in respect of any new portfolio assigned to the mortgages trustee, to increase the Funding 1 share in accordance with the terms of the mortgages trust deed and/or to refinance existing loan tranches under the intercompany loan agreement and/or a new intercompany loan.

The Funding 1 share and the seller share are recalculated by the cash manager on each calculation date.

A **calculation date** is the date on which the mortgages trust is terminated and the first day (or, if not a London business day, the next succeeding London business day) of each month (each being a **normal calculation date**) or the date on which Funding 1 or the seller acquires or increases its interest in the trust property (otherwise than due to capitalised interest) and/or the mortgages trustee acquires new loans from the seller. The recalculation is based on the total outstanding principal balance of the loans in the portfolio as at the close of business on the business day immediately preceding the relevant calculation date (as adjusted from time to time). The period from (and including) one calculation date to (but excluding) the next calculation date is known as a **calculation period**.

The reason for the recalculation is to determine the new Funding 1 share percentage and seller share percentage. The Funding 1 share percentage and the seller share percentage determines the entitlement of Funding 1 and the seller to revenue receipts and principal receipts from the loans in the portfolio and also the allocation of losses arising on the loans. The method for determining those new percentage shares is set out in the next three sections.

Two London business days after each calculation date (the **distribution date**) the mortgages trustee distributes principal and revenue receipts to Funding 1 and the seller, as described below. In relation to each distribution date, the **relevant share calculation date** means the calculation date at the start of the most recently completed calculation period.

## Funding 1 share

On each calculation date (also referred to in this section as the **relevant calculation date**) or such time as the mortgages trust terminates, the interest of Funding 1 is recalculated in accordance with the following formulae:

- the share of Funding 1 (the **Funding 1 share**) is an amount equal to:

$$A - B - C + D + E + F - G$$

- the percentage share of Funding 1 (the **Funding 1 share percentage**) is an amount equal to:

$$\frac{A - B - C + D + E + F - G}{H} \times 100$$

in the latter case, expressed as a percentage and rounded upwards to five decimal places, where:

A = the amount of the share of Funding 1 in the trust property calculated on the immediately preceding calculation date;

B = the amount of any principal receipts on the loans to be distributed to Funding 1 on the distribution date immediately following the relevant calculation date (as described under “– **Allocation and distribution of principal receipts prior to the occurrence of a trigger event**”, “– **Allocation and distribution of principal receipts on or after the occurrence of a non-asset trigger event but prior to the occurrence of an asset trigger event**” and “– **Allocation and distribution of principal receipts on or after the occurrence of an asset trigger event**” below);

C = the amount of losses sustained on the loans in the period from (and including) the immediately preceding calculation date to (but excluding) the relevant calculation date and the amount of any reductions occurring in respect of the loans as described in paragraph (1) below, in each case allocated to Funding 1 in the calculation period ending on (but excluding) the relevant calculation date;

D = the amount of any consideration to be paid by Funding 1 to the seller with respect to any new loans to be sold to the mortgages trustee on the relevant calculation date;

E = the amount of any consideration to be paid by Funding 1 to the seller in relation to the acquisition by Funding 1 from the seller on the relevant calculation date of an interest in the trust property;

F = the amount equal to any capitalised interest accruing on a loan which has been allocated to Funding 1 from (and including) the immediately preceding calculation date, less the amount to be paid by the seller on the distribution date immediately following the relevant calculation date to acquire an interest in trust property as described in “– **Acquisition by seller of an interest relating to capitalised interest**” below; and

G = an amount equal to any payment to be received by Funding 1 from the seller in relation to any acquisition by the seller from Funding 1 on such calculation date of an interest in the trust property; and

H = the aggregate outstanding principal balance of all the loans constituting the trust property as at the relevant calculation date after making the distributions, allocations and additions referred to in “B”, “C”, “D”, “E”, “F” and “G” above and after taking account of:

- any distribution of principal receipts to be made to Funding 1 and the seller;
- the amount of any losses allocated to Funding 1 and the seller;
- the amount of any increase in the loan balances due to capitalised interest, capitalised expenses and capitalised arrears or borrowers making drawings under flexible loans;

- interest accrued but unpaid by the relevant borrower during the calculation period ending on (but excluding) the relevant calculation date and the payment of previously accrued interest during such calculation period;
- the adjustments referred to in paragraphs (1) to (4) below (or, if the seller share is zero, the adjustments referred to in paragraph (1) only); and
- the amount of any other additions or subtractions to the trust property.

If any of the following events occurs during a calculation period, then the aggregate total outstanding principal balance of the loans in the portfolio will be reduced or deemed to be reduced (for, among other things, the purposes of the calculation of “H” on the calculation date at the end of that calculation period):

- (1) any borrower exercises a right of set-off so that the amount of principal and interest owing under a loan is reduced, but no corresponding payment is received by the mortgages trustee. In this event, the aggregate outstanding principal balance of the loans in the portfolio will be reduced by an amount equal to the amount of that set-off; and/or
- (2) a loan or its related security is (i) in breach of the representations and warranties contained in the mortgage sale agreement, (ii) the subject of a further advance or (iii) in limited circumstances, the subject of a product switch or other obligation of the seller to repurchase, and, in each case, the seller fails to repurchase the loan or loans under the relevant mortgage account and their related security to the extent required by the terms of the mortgage sale agreement. In any of these events, the aggregate outstanding principal balance of the loans in the portfolio will be deemed to be reduced for the purposes of the calculation in “H” by an amount equal to the outstanding principal balance of the relevant loan or loans under the relevant mortgage account (including any arrears of interest and accrued and unpaid interest); and/or
- (3) the seller would be required at the direction of Funding 1 to repurchase a loan and its related security as required by the terms of the mortgage sale agreement, but the loan is not capable of being repurchased. In this event, the aggregate outstanding principal balance of the loans in the portfolio will be deemed to be reduced for the purposes of the calculation in “H” by an amount equal to the outstanding principal balance of the relevant loan or loans under the relevant mortgage account (including any arrears of interest and accrued and unpaid interest); and/or
- (4) the seller materially breaches any other material warranty under the mortgage sale agreement and/or (for so long as the seller is the servicer) the servicing agreement, which will also be grounds for terminating the appointment of the servicer. In this event, the aggregate outstanding principal balance of the loans in the portfolio will be deemed to be reduced by an amount equal to the resulting loss incurred by the beneficiaries.

The reductions or deemed reductions set out in paragraphs (1) to (4) above will be made on the relevant calculation date first to the seller share (including the minimum seller share) and thereafter (in respect of paragraph (1) only) will be made to the Funding 1 share.

Any sums that are subsequently recovered by the mortgages trustee in connection with a reduction or deemed reduction of the trust property under paragraphs (1) to (4) above will constitute a revenue receipt under the relevant loan. Such revenue receipt will belong to Funding 1 (but only if and to the extent that the related reductions were applied against the Funding 1 share) and, thereafter, will belong to the seller.

### **Seller share**

On each calculation date or such time as the mortgages trust terminates, the interest of the seller in the trust property is recalculated as follows:

- The share of the seller (the **seller share**) will be an amount equal to the aggregate outstanding principal balance of all the loans in the trust property as at that calculation date (adjusted as provided in item “H” of “– **Funding 1 share**” above) minus the Funding 1 share (as calculated on that calculation date).
- The percentage share of the seller (the **seller share percentage**) is an amount equal to 100 per cent. minus the Funding 1 share percentage (as calculated on that calculation date).

## Minimum seller share

The seller share includes an amount known as the **minimum seller share**. The amount of the minimum seller share will fluctuate depending on changes to the characteristics of the loans in the portfolio. The seller is not entitled to receive principal receipts which would reduce the seller share to an amount less than the minimum seller share unless and until the Funding 1 share is in an amount equal to zero or an asset trigger event has occurred. The minimum seller share is the amount determined on each calculation date (after any sale of loans to the mortgages trustee on that calculation date), in accordance with the following formula:

$$X + Y + Z$$

where:

X = (i) (while the short-term unsecured, unguaranteed and unsubordinated debt obligations of the seller are rated at least F-1 by Fitch) 5 per cent. of the aggregate outstanding principal balance of loans in the portfolio on the relevant calculation date or, as at the date of notification to borrowers of the sale of the mortgage loans to the mortgages trust, an amount equal to the then aggregate amount of all deposits of the borrowers held with the seller; and

(ii) (while the short-term unsecured, unguaranteed and unsubordinated debt obligations of the seller are rated less than F-1 by Fitch) the greater of (A) 5 per cent.; and (B) such percentage as calculated quarterly by the seller of the aggregate outstanding principal balance of loans in the portfolio on the relevant calculation date or, as at the date of notification to borrowers of the sale of the mortgage loans to the mortgages trust, an amount equal to the then aggregate amount of all deposits of the borrowers held with the seller;

Y = the product:  $p \times q \times r$

where:

p = 8 per cent.;

q = the **relevant draw capacity**, being the aggregate of (1) an amount equal to the excess of (i) the maximum amount that borrowers may draw under flexible loans included in the trust property (whether or not drawn) over (ii) the aggregate principal balance of flexible loans in the trust property on the relevant calculation date (such amount, the **flexible draw capacity**) and (2) an amount equal to the excess of (i) the maximum amount that borrowers may draw under unsecured loans comprised in Mortgage Plus loans, the secured loan element of which is included in the trust property over (ii) the aggregate principal balance of such unsecured loans (such amount the **Mortgage Plus draw capacity**); and

r = 3;

and

Z = the aggregate sum of reductions deemed made (if any) in accordance with paragraphs (2), (3) and (4) as described in “– **Funding 1 share**” above.

The purpose of “X” is to mitigate the risks relating to certain set-off risks relating to the loans. The amount of “X” may be reduced from time to time at the request of the seller or Funding 1 (acting reasonably) provided that Funding 1 and/or the Funding 1 security trustee has received written confirmation from the rating agencies that there will be no adverse effect on the then current ratings of the notes as a result thereof.

The purpose of the calculation in “Y” is to mitigate the risk of the seller failing to fund a drawing under a flexible loan or the unsecured element of a Mortgage Plus loan.

The purpose of the calculation in “Z” is to mitigate the risk of the seller materially breaching any material warranty under the mortgage sale agreement and/or the servicing agreement and/or failing to repurchase certain loans and their related security to the extent required by the terms of the mortgage sale agreement.

## Cash management of trust property – revenue receipts

Under the cash management agreement, the cash manager is responsible for distributing revenue receipts on behalf of the mortgages trustee on each distribution date in accordance with the priority described in the following section. For further information on the role of the cash manager, see “**Cash management for the mortgages trustee and Funding 1**” below.

### **Mortgages trust calculation of revenue receipts**

**Mortgages trust available revenue receipts** is calculated by the cash manager on each calculation date and is an amount equal to:

- revenue receipts on the loans (but excluding principal receipts);
- plus interest payable to the mortgages trustee on the mortgages trustee GIC account;
- less amounts due to third parties (also known as **third party amounts**), including:
  - (1) amounts under a direct debit which are repaid to the bank making the payment if that bank is unable to recoup that amount itself from its customer’s account;
  - (2) payments by borrowers of any fees and other charges which are due to the seller; or
  - (3) recoveries in respect of amounts deducted from loans as described in paragraphs (1) to (4) in “– **Funding 1 share**” above, which will belong to and be paid to Funding 1 and/or the seller as described therein,

which amounts may be paid daily from monies on deposit in the mortgages trustee GIC account.

On each distribution date, the cash manager will apply mortgages trust available revenue receipts in the following priority:

- (A) without priority among them but in proportion to the respective amounts due, to pay amounts due and payable, or to become due and payable during the following calculation period:
  - to the mortgages trustee under the provisions of the mortgages trust deed; and
  - to third parties from the mortgages trustee in respect of the mortgages trust, but only if:
    - (1) payment is not due as a result of a breach by the mortgages trustee of the transaction documents to which it is a party; and/or
    - (2) payment has not already been provided for elsewhere;
- (B) without priority among them but in proportion to the respective amounts due, to pay amounts due and payable or to become due and payable by the mortgages trustee during the following calculation period to:
  - the servicer under the provisions of the servicing agreement;
  - the cash manager under the provisions of the cash management agreement;
  - the account bank under the provisions of the bank account agreement;
  - the mortgages trustee corporate services provider under the provisions of the mortgages trustee corporate services agreement;
- (C) to allocate and pay to Funding 1 an amount equal to the amount determined by multiplying the total amount of the remaining mortgages trust available revenue receipts by the Funding 1 share percentage as calculated on the relevant share calculation date;
- (D) to allocate and pay to the mortgages trustee and/or Funding 1 (as applicable) an amount equal to any loss amount (as defined below) suffered or incurred by it or them (as applicable); and

- (E) to allocate and pay to the seller an amount (if positive) equal to the amount of the mortgages trust available revenue receipts less the amount of such mortgages trust available revenue receipts applied and/or allocated under (A) to (D) above.

For the purposes of item (D) above, **loss amount** means the amount of any costs, expenses, losses or other claims suffered or incurred by, as applicable, the mortgages trustee and/or Funding 1 in connection with any recovery of interest on the loans to which the seller, the mortgages trustee or Funding 1 was not entitled or could not enforce as a result of any determination by any court or other competent authority or any ombudsman in respect of any loan and its related security that:

- any term which relates to the recovery of interest under the standard documentation applicable to that loan and its related security is unfair; or
- (if variable margins are introduced in respect of tracker rate loans in the future) the variable margin above the Bank of England repo rate under any tracker rate loan must be set by the seller; or
- the interest payable under any loan is to be set by reference to an interest rate other than that set or purported to be set by either the servicer or the mortgages trustee as a result of the seller having more than one standard variable rate.

### Cash management of trust property – distribution of principal receipts to Funding 1

Under the cash management agreement, the cash manager is also responsible for distributing principal receipts to Funding 1 on behalf of the mortgages trustee on each distribution date in accordance with the priority described in the next two following sections. To understand how the cash manager distributes principal receipts to Funding 1 on the loans on each distribution date you need to understand the definitions set out below.

On each calculation date, the cash manager will, in respect of Funding 1, ascertain whether the following distribution date will be within a cash accumulation period relating to a bullet loan tranche or a scheduled amortisation instalment (each such bullet loan tranche or scheduled amortisation instalment that is within a cash accumulation period being a **cash accumulation loan tranche**) and will ascertain the cash accumulation requirement (as defined below) and repayment requirement (as defined below) for Funding 1.

The cash accumulation period (as defined below) will be calculated separately for each bullet loan tranche and scheduled amortisation instalment.

The applicable loan tranche supplement and (if applicable) final terms will set out whether each loan tranche is a bullet loan tranche, a scheduled amortisation loan tranche, a pass-through loan tranche, a subordinated loan tranche or a start-up loan tranche and, in relation to bullet loan tranches and the scheduled amortisation loan tranches, will set out the **scheduled repayment date** (being the Funding 1 interest payment date falling in the indicated month) and **relevant accumulation amount** (being the amount of funds to be accumulated over a cash accumulation period in order to repay a bullet loan tranche or a scheduled amortisation instalment on its scheduled repayment date, whether or not actually repaid on that scheduled repayment date).

### Definitions:

**anticipated cash accumulation period** means, on any normal calculation date, the anticipated number of months required by Funding 1 to accumulate sufficient principal receipts to pay the relevant accumulation amount in relation to a cash accumulation loan tranche, which will be equal to:

$$\frac{J + K - L}{M \times N \times O}$$

calculated in months and rounded up to the nearest whole number, where:

J = the relevant accumulation amount;

K = the aggregate principal amount outstanding on that normal calculation date of:

- each other bullet loan tranche or scheduled amortisation instalment that was not fully repaid on its scheduled repayment date;



- each other bullet loan tranche or scheduled amortisation instalment, the scheduled repayment date of which falls on or before the scheduled repayment date of the relevant cash accumulation loan tranche;
- L = the amount of any available cash already standing to the credit of the Funding 1 cash accumulation ledger at the start of that normal calculation date plus the aggregate amount of cash accumulation requirement paid to Funding 1 since the previous Funding 1 interest payment date;
- M = means the sum of each monthly CPR on the 12 most recent normal calculation dates which have occurred prior to that date divided by 12;
- N = 0.85; and
- O = the aggregate outstanding principal balance of the loans comprising the trust property on the previous normal calculation date.

**cash accumulation period** means the period beginning on the earlier of:

- commencement of the anticipated cash accumulation period relating to the relevant accumulation amount; and
- unless otherwise specified in the applicable final terms, in respect of an original bullet loan tranche, six months prior to the scheduled repayment date of that original bullet loan tranche and, in respect of an original scheduled amortisation instalment, three months prior to the scheduled repayment date of that original scheduled amortisation instalment,

and ending when Funding 1 has fully repaid that original bullet loan tranche or scheduled amortisation instalment, as applicable.

**cash accumulation requirement** means, on a calculation date:

- the outstanding principal amounts in relation to each cash accumulation loan tranche;
- plus amounts due on the immediately following Funding 1 interest payment date in respect of items (A) and (B) of the Funding 1 pre-enforcement principal priority of payments under “**Cashflows – Distribution of Funding 1 available principal receipts**” below;
- less the amount standing to the credit of the Funding 1 cash accumulation ledger as at the last Funding 1 interest payment date (which amount was not distributed on that Funding 1 interest payment date to the issuing entity);
- less the sum of each cash accumulation requirement amount paid to Funding 1 on a previous distribution date during the relevant interest period.

**Funding 1 cash accumulation ledger** means a ledger maintained by the cash manager for Funding 1, which records amounts accumulated by Funding 1 to pay relevant accumulation amounts.

**monthly CPR** means, on any normal calculation date, the total principal receipts received by the mortgages trustee during the period of one month ending on that normal calculation date divided by the aggregate outstanding principal balance of the loans comprised in the trust property as at the immediately preceding normal calculation date.

**rated loan tranche repayment requirement** means the requirement pursuant to which, on a calculation date, the amount (if any) by which:

- the aggregate of all amounts that will be payable by Funding 1 on the next Funding 1 interest payment date as described in items (C) to (H) (inclusive) of the priority of payments under “**Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes**” on the basis:

- that there would be no deferral of loan tranches pursuant to Rule (1) as set out in that section;
- that where Rule (2) set out in that section applies to any pass-through loan tranches, the amount so payable by Funding 1 in respect of those pass-through loan tranches shall be treated as the lesser of (A) the amount due and payable in respect of those pass-through loan tranches and (B) the product of (a) the Funding 1 share percentage as at the start of the most recently ended calculation period, (b) the aggregate amount of principal receipts received by the mortgages trustee during the most recently ended calculation period and (c) the outstanding principal balance of those pass-through loan tranches, divided by the aggregate outstanding principal balance of the intercompany loan (excluding subordinated loan tranches and start-up loan tranches), each as at the most recent Funding 1 interest payment date;
- that loan tranches will be treated as due and payable if they are already due and payable or would become due and payable on or before the next Funding 1 interest payment date if all principal receipts were paid to Funding 1 on that calculation date; and
- excluding amounts due and payable in respect of bullet loan tranches and scheduled amortisation instalments,

exceeds the sum of:

- the amounts standing to the credit of the Funding 1 principal ledger as at the last Funding 1 interest payment date (which amount was not distributed on that Funding 1 interest payment date to the issuing entity); and
- the sum of each repayment requirement amount paid to Funding 1 on a previous distribution date during the relevant interest period.

**repayment requirement** means, on any calculation date, the amount (if any) equal to the sum of:

- (a) the rated loan tranche repayment requirement; and
- (b) the subordinated loan tranche repayment requirement.

**scheduled amortisation instalment** means that part of a scheduled amortisation loan tranche which is payable on each of the scheduled repayment dates of that scheduled amortisation loan tranche.

**subordinated loan tranche repayment requirement** means the aggregate of all amounts that will be payable by Funding 1 on the next Funding 1 interest payment date as described in item (I) of the priority of payments under “**Cashflows – Distribution of Funding 1 Available Principal Receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes**” on the basis that the subordinated loan tranches will not exceed the required subordinated loan tranche principal amount outstanding.

**trigger event** means an asset trigger event and/or a non-asset trigger event.

An **asset trigger event** will occur when principal losses on loans in the portfolio (after application of Funding 1 available principal receipts to meet deficiencies in Funding 1 available revenue receipts or to fund the Funding 1 liquidity reserve fund) reach a level causing an amount to be debited to the AAA principal deficiency sub-ledger, unless such debit is made when (a) the aggregate principal amount outstanding of each of the AA loan tranches, the A loan tranches, the BBB loan tranches and the BB loan tranches is equal to zero; and (b) the sum of the amount standing to the credit of Funding 1 general reserve ledger and the Funding 1 revenue ledger, together with amounts determined and due to be credited to the Funding 1 revenue ledger prior to the immediately following Funding 1 interest payment date after such debit is made, is greater than the amount necessary to pay the items in paragraphs (A) to (F) of the Funding 1 pre-enforcement revenue priority of payments on the immediately following Funding 1 interest payment date after such debit is made. For more information on the Funding 1 principal deficiency ledger, see “**Credit structure – Funding 1 principal deficiency ledger**”.

A **non-asset trigger event** will occur on a calculation date if:

- (a) an insolvency event occurs in relation to the seller on or before that calculation date;
- (b) the seller's role as servicer under the servicing agreement is terminated and a new servicer is not appointed within 60 days; or
- (c) as at the calculation date immediately preceding the relevant calculation date, the seller share was less than the minimum seller share and this has not been remedied by the relevant calculation date; or
- (d) as at the calculation date immediately preceding the relevant calculation date, the aggregate outstanding principal balance of loans comprising the trust property was less than the required loan balance amount specified in the most recent final terms and this has not been remedied by the relevant calculation date.

Changes may be made to the definitions of asset trigger event and non-asset trigger event. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may adversely affect your interests**”, “**Security for Funding 1's obligations**” and “**Security for the issuing entity's obligations**”.

#### **Mortgages trust calculation of principal receipts**

**Mortgages trust available principal receipts** are calculated by the cash manager on each calculation date and will be equal to the amount that is standing to the credit of the principal ledger on that calculation date. The repayment requirement and the cash accumulation requirement of Funding 1 are calculated by the cash manager on each calculation date and the relevant amounts notified to the mortgages trustee (who will be entitled to rely on such notifications).

#### **Allocation and distribution of principal receipts prior to the occurrence of a trigger event**

On each distribution date, where no trigger event has occurred on or before the immediately preceding calculation date, the cash manager will allocate the mortgages trust available principal receipts to the beneficiaries and distribute such amounts as follows:

- (A) *first*, to Funding 1 an amount up to but not exceeding Funding 1's cash accumulation requirement on that distribution date;
- (B) *second*, to Funding 1 an amount up to but not exceeding Funding 1's repayment requirement on that distribution date; and
- (C) *third*, the remainder of such receipts will be allocated and paid to the seller until the seller share (as calculated on the relevant share calculation date) is equal to the minimum seller share.

Provided that in relation to paragraphs (A) through (C) above, the following rules will apply:

- (1) The amount of mortgages trust available principal receipts to be allocated and paid to Funding 1 on a distribution date will be reduced by an amount equal to the aggregate of Funding 1 available revenue receipts which are to be applied on the immediately succeeding Funding 1 interest payment date in reduction of deficiencies on the Funding 1 principal deficiency ledger.
- (2) Funding 1 will not be entitled to receive in aggregate an amount of mortgages trust available principal receipts on a distribution date which is in excess of the Funding 1 share on the calculation date at the start of the most recently completed calculation period.
- (3) On any calculation date prior to the occurrence of a trigger event, the mortgages trustee will make provision for any amount that would, if paid to the seller, result in the seller share being equal to or less than the minimum seller share and the seller will not receive that amount until such time as the seller share would, upon receipt by the seller of such amount, be greater than the minimum seller share and provided that (i) the seller will not receive nor have allocated to it any such amount if a non-asset trigger event occurs and is occurring and (ii) if an asset trigger event occurs and is occurring, the seller will have allocated to it and will be paid such amount but only to the extent permitted by the rules governing distribution of principal receipts after the occurrence of an asset trigger event.

#### **Allocation and distribution of principal receipts on or after the occurrence of a non-asset trigger event but prior to the occurrence of an asset trigger event**

On each distribution date where a non-asset trigger event has occurred on or before the immediately preceding calculation date but an asset trigger event has not occurred on or before that calculation date, the cash manager

will allocate mortgages trust available principal receipts to the beneficiaries and distribute such amounts as follows:

- (A) *first*, all such receipts will be allocated and paid to Funding 1 until the Funding 1 share (as calculated on the relevant share calculation date) has been reduced to zero; and
- (B) *then*, the remainder, if any, to the seller.

Following the occurrence of a non-asset trigger event, the notes will be subject to prepayment risk (that is, they may be repaid earlier than expected). See “**Risk factors – The occurrence of a non-asset trigger event may accelerate the repayment of certain notes and/or delay the repayment of other notes**” above.

#### **Allocation and distribution of principal receipts on or after the occurrence of an asset trigger event**

On each distribution date where an asset trigger event has occurred on or before the immediately preceding calculation date, the cash manager will allocate and pay mortgages trust available principal receipts, without priority among them but in proportion to the respective amounts due, to Funding 1 and the seller according to the Funding 1 share percentage and the seller share percentage (in each case, as calculated on the relevant share calculation date) respectively until the Funding 1 share is zero (and, for the avoidance of doubt, such payments may reduce the seller share to an amount less than the minimum seller share). When the Funding 1 share is zero, the remaining mortgages trust available principal receipts (if any) will be allocated to the seller.

Following the occurrence of an asset trigger event, certain series and classes of notes will be subject to prepayment risk and other series and classes of notes will be subject to extension risk (that is they may be repaid later than expected). See “**Risk factors – The occurrence of an asset trigger event may accelerate the repayment of certain notes and/or delay the repayment of other notes**” above.

#### **Losses**

Losses shall be applied in reducing proportionately the Funding 1 share and the seller share. The losses to be allocated to Funding 1 will be determined by multiplying the amount of losses during a calculation period by the Funding 1 share percentage (as calculated on the relevant calculation date) and losses to be allocated to the seller will be determined by multiplying the amount of losses during a calculation period by the seller share percentage (as calculated on the relevant calculation date). Losses will be allocated to Funding 1 and the seller accordingly on each calculation date prior to calculating the allocation of mortgages trust available principal receipts on that calculation date.

For a description of how losses on the loans that have been allocated to Funding 1 on any date will be allocated to the loan tranches under the intercompany loan, see “**Credit structure – Funding 1 principal deficiency ledger**” below.

In the event that any sums are recovered from a borrower in respect of which a loss has been recorded on the losses ledger (other than in the event that such recovery occurs subsequent to completion of enforcement procedures), they shall be applied in reducing the balance of the losses ledger. Any such reduction of the balance of the losses ledger will be apportioned *pro rata* and *pari passu* between the Funding 1 share and the seller share as at the date on which such provision was originally made in the losses ledger.

If a recovery is made on a loan after Funding 1 has discharged all its obligations to all of its secured creditors (including to the issuing entity under the intercompany loan agreement), then the sums recovered shall be held by the mortgages trustee for the benefit of the seller only).

#### **Disposal of trust property**

The trust property is held on trust for the benefit of Funding 1 and the seller. Subject to the terms of the mortgages trust deed, the mortgages trustee is not entitled to dispose of the trust property or create any security interest over the trust property.

If an event of default occurs under the intercompany loan agreement (an **intercompany loan event of default**) and the issuing entity security trustee, acting on the instructions of the note trustee, determines to serve an intercompany loan acceleration notice on Funding 1, then the Funding 1 security trustee will be entitled, among other things, to sell the Funding 1 share. For further information on the security granted by Funding 1 over its assets, see “**Security for Funding 1’s obligations**” below.

#### **Additions to trust property**

The trust property may be increased from time to time by the sale of new loans and their related security to the mortgages trustee. The mortgages trustee will hold the new loans and their related security on trust for Funding 1 and the seller according to the terms of the mortgages trust deed. For further information on the sale of new loans and their related security to the mortgages trustee, see “**Sale of the loans and their related security**” above.

#### **Acquisition by Funding 1 of an increased interest in trust property**

If a new loan tranche (other than a start-up loan tranche) is made available to Funding 1 under the intercompany loan agreement, then it may apply the proceeds of that loan tranche to make a payment to the seller so as to give rise to an increase in the Funding 1 share (and giving rise to a corresponding decrease in the seller share). Funding 1 will be permitted to do this only if it meets a number of conditions (each of which may be varied or waived by the mortgages trustee where it receives written confirmation from each of the rating agencies that such variation or waiver will not cause its then current ratings of the notes then outstanding to be downgraded, withdrawn or (in the case of S&P and Moody's) qualified), including:

- that, on the relevant date, no intercompany loan event of default and no note event of default have occurred that have not been remedied or waived;
- as at the most recent Funding 1 interest payment date, no deficiency is recorded on the Funding 1 principal deficiency ledger (other than the subordinated loan principal deficiency sub-ledger);
- the Funding 1 security trustee is notified that the proposed increase in the Funding 1 share (or the corresponding decrease in the seller share) would not result in the then current ratings by each of the rating agencies of any of the outstanding notes being downgraded, withdrawn or (in the case of S&P and Moody's) qualified;
- as at the relevant date, the aggregate outstanding principal balance of loans in the trust property in respect of which the aggregate amount in arrears is more than three times the monthly payment then due is less than 5 per cent. of the aggregate outstanding principal balance of all loans constituting the trust property or any higher percentage that each rating agency has confirmed will not cause its then current ratings of the notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result thereof;
- the Funding 1 general reserve fund has not been debited on or before the relevant date for the purposes of curing a principal deficiency in respect of the loan tranches under the intercompany loan agreement in circumstances where the Funding 1 general reserve fund has not been replenished by a corresponding amount by the relevant date;
- where Funding 1 makes the offer to the seller, the seller has not received written notice that the short term, unsecured, unguaranteed and unsubordinated debt obligations of the seller are not rated at least F1 by Fitch, P-1 by Moody's and A-1 by Standard & Poor's at the time of, and immediately following, the payment to be made by Funding 1 on the relevant date;
- the product of the WAFF and WALs for the loans constituting the trust property calculated on the relevant date in the same way as for the initial portfolio (or as agreed by the servicer and the rating agencies from time to time) does not exceed the product of the WAFF and WALs (when tested at the "AAA level") for the loans constituting the trust property calculated on the most recent previous closing date, plus 0.25 per cent.; and
- the loan-to-value ratio of loans constituting the trust property, after application of the LTV test on the relevant date, does not exceed the loan-to-value ratio (based on the LTV test) of loans in the trust property on the most recent previous closing date plus 0.25 per cent.

#### **Acquisition by seller of an interest relating to capitalised interest**

If a borrower takes a payment holiday or makes an underpayment under a loan (as permitted by the terms of the loan), then the outstanding principal balance of the loan will increase by the amount of interest that would have been paid on the relevant loan if not for such payment holiday or underpayment (the **capitalised interest**).

The increase in the principal balance of the loan due to the capitalised interest will be allocated to the Funding 1 share and the seller share based on their respective percentage shares as calculated on the previous calculation date.

Prior to an insolvency event occurring in respect of the seller, on each distribution date, the seller will make a cash payment to Funding 1 in an amount equal to Funding 1's share of the capitalised interest in respect of those loans that are subject to payment holidays. As a result of such payment:

- the seller share will increase by an amount equal to the amount paid to Funding 1 in respect of Funding 1's share of the capitalised interest and the Funding 1 share will decrease by a corresponding amount; and
- Funding 1 will apply the proceeds of the amount paid by the seller in accordance with the Funding 1 pre-enforcement revenue priority of payments and, after enforcement of the Funding 1 security, in accordance with the Funding 1 post-enforcement priority of payments.

If an insolvency event occurs in respect of the seller, then the seller may continue to make payments to Funding 1 in an amount equal to Funding 1's share of the capitalised interest in the same manner and for the same purpose described above, but it is not obliged to do so.

#### **Payment by the seller of the amount outstanding under a loan tranche**

If the seller offers to make a payment to Funding 1 of the amount outstanding under a loan tranche (other than a start-up loan tranche), then Funding 1 may accept that offer but only if:

- Funding 1 and/or the Funding 1 security trustee have received written confirmation from each of the rating agencies that there would not be any downgrading, withdrawal or (in the case of S&P and Moody's) qualification of its then current ratings of the notes if Funding 1 accepted the offer;
- (except in the case of a subordinated loan tranche) Funding 1 would receive the payment on a Funding 1 interest payment date; and
- Funding 1 will apply the proceeds to repay the relevant loan tranche (the proceeds of which repayment the issuing entity will use to repay the corresponding series and class of notes or, as applicable, the relevant issuing entity subordinated loan).

The Funding 1 share would decrease by an amount equal to the payment made by the seller and the seller share would increase by a corresponding amount.

#### **Compensation of mortgages trustee**

The mortgages trustee is paid a fee (inclusive of VAT, if any) of £1,500 each year for the performance of its duties, which will be paid annually on the distribution date following each anniversary of the mortgages trust deed having been entered into.

#### **Termination of mortgages trust**

The mortgages trust will terminate on the later to occur of:

- the date on which all amounts due from Funding 1 to the Funding 1 secured creditors have been paid in full; and
- any other date agreed in writing by Funding 1 and the seller.

#### **Retirement of mortgages trustee**

The mortgages trustee is not entitled to retire or otherwise terminate its appointment. The seller and Funding 1 cannot replace the mortgages trustee.

#### **Governing law**

The mortgages trust deed is governed by English law.

### **The controlling beneficiary deed**

Pursuant to the terms of the controlling beneficiary deed dated the programme date (as amended from time to time, the **controlling beneficiary deed**), Funding 1 and the seller have agreed to, among other things, arrangements amongst themselves in respect of certain decisions (relating to authorisations, consents, waivers, instructions or other acts) of the beneficiaries to be made from time to time in respect of the transaction documents. In the event that any further funding beneficiary should become a beneficiary of the mortgages trust, such further funding beneficiary will accede to the controlling beneficiary deed and agree to such and other arrangements.

The controlling beneficiary deed is governed by English law.

## The intercompany loan agreement

The following section contains a summary of the material terms of the intercompany loan agreement. The summary does not purport to be complete and is subject to the provisions of the intercompany loan agreement.

Changes may be required to the intercompany loan agreement from time to time to accommodate a further issuance of notes by the issuing entity, entry by the issuing entity into an issuing entity subordinated loan agreement or entry by the issuing entity into an issuing entity start-up loan agreement and/or the on-lending of the proceeds thereof by means of loan tranches to be made available to Funding 1. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may adversely affect your interests**”, “**Security for Funding 1’s obligations**” and “**Security for the issuing entity’s obligations**”.

### The facility

Pursuant to the terms of the intercompany loan agreement, the issuing entity lends to Funding 1 from time to time, on each closing date with respect to an issuance of notes and/or an advance date with respect of an issuing entity subordinated loan, an aggregate amount in sterling equal to the proceeds of (a) the issuance of such notes, (b) the issuing entity subordinated loan advanced to it on such closing date and/or advance date by the issuing entity subordinated loan provider or a new issuing entity subordinated loan provider and/or (c) the issuing entity start-up loan advanced to it on such closing date by the issuing entity start-up loan provider or a new issuing entity start-up loan provider. Each advance of funds corresponding to a particular series and class of notes will be a separate loan tranche under the intercompany loan agreement (each, a **rated loan tranche**). Each advance of funds corresponding to an issuing entity subordinated loan will be a separate loan tranche under the intercompany loan agreement (each, a **subordinated loan tranche**). Each advance of funds corresponding to an issuing entity start-up loan will be a separate loan tranche under the intercompany loan agreement (each, a **start-up loan tranche**).

The loan tranche supplement to the intercompany loan agreement dated the relevant closing date and/or advance date and (if applicable) the relevant final terms will contain the terms of each loan tranche to be made on such date.

Funding 1 will use the proceeds of each loan tranche (except for each start-up loan tranche) to:

- pay the seller part of the consideration for loans (together with their related security) sold by the seller to the mortgages trustee in connection with the issuance of notes by the issuing entity and/or the advance of an issuing entity subordinated loan to the issuing entity, which will result in an increase in the Funding 1 share and a corresponding decrease in the seller share;
- acquire part of the seller share (such payment to be made to the seller which will result in a corresponding decrease in the seller share and a corresponding increase in the Funding 1 share);
- fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any);
- make a payment to the issuing entity to refinance an existing loan tranche (which may be a rated loan tranche or a subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of a new intercompany loan.

### Ratings designations of the rated loan tranches

The ratings assigned to a rated loan tranche are collectively referred to as the **designated loan tranche ratings**. The designated loan tranche ratings of the AAA loan tranches reflect the ratings expected to be assigned to any class A notes by the rating agencies on the relevant closing date, except that money market notes will have different short-term ratings. The designated loan tranche ratings of the AA loan tranches reflect the ratings expected to be assigned to any class B notes by the rating agencies on the relevant closing date. The designated loan tranche ratings of the A loan tranches reflect the ratings expected to be assigned to any class M notes by the rating agencies on the relevant closing date. The designated loan tranche ratings of the BBB loan tranches reflect the ratings expected to be assigned to any class C notes by the rating agencies on the relevant closing date. The designated loan tranche ratings of the BB loan tranches reflect the ratings expected to be assigned to any class D notes by the rating agencies on the relevant closing date. If, after any closing date, the rating agencies change the



rating assigned to a series and class of notes, this will not affect the designated loan tranche ratings of the related loan tranche under the intercompany loan agreement.

Loan tranches with designated loan tranche ratings lower than the BB loan tranches may be made available by the issuing entity to Funding 1 from time to time pursuant to the intercompany loan agreement, subject to confirmation from each of the rating agencies that the creation of such new loan tranches (and corresponding classes of notes) will not result in the reduction, withdrawal or (in the case of S&P and Moody's) qualification of its then ratings of the notes then outstanding. The issuing entity security trustee and the Funding 1 security trustee will give their consent to any modifications to any transaction document that are requested by Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf) if Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf), as the case may be, certifies that such modifications are required in order to accommodate the introduction of such new loan tranches.

### **Making of loan tranches**

The issuing entity may advance loan tranches to Funding 1 and issue corresponding series and classes of notes or enter into corresponding issuing entity subordinated loans and/or issuing entity start-up loans from time to time without obtaining the consent of existing noteholders. The issuing entity will not be obliged to advance loan tranches to Funding 1 unless on the relevant date certain conditions have been met, including:

- that the related series and class of notes has been issued or, as applicable, the related issuing entity subordinated loan or, as applicable, the related issuing entity start-up loan has been advanced and, in each case, the proceeds received by or on behalf of the issuing entity;
- that Funding 1 has delivered a certificate certifying that it is solvent;
- each of the rating agencies has confirmed in writing to the issuing entity and/or issuing entity security trustee and/or the note trustee that there will not, as a result of the issuing entity issuing the corresponding notes and/or borrowing the corresponding issuing entity subordinated loans and/or issuing entity start-up loan, as the case may be, be any reduction, withdrawal or (in the case of S&P and Moody's) qualification of its then current ratings by the of any notes then outstanding.

### **Representations and agreements**

Funding 1 makes several representations to the issuing entity in the intercompany loan agreement, including representations that Funding 1 has been duly incorporated and that it has the requisite corporate power and authority to enter into the transaction documents to which it is a party.

In addition, Funding 1 agrees that:

- it will not create or permit to subsist any encumbrance or other security interest over any of its assets, unless arising by operation of law or pursuant to the transaction documents;
- it will not carry on any business or engage in any activity whatsoever which is not incidental to or necessary in connection with any of the activities in which the transaction documents provide or envisage that Funding 1 will engage;
- it will not have any subsidiaries, any subsidiary undertakings, both as defined in the Companies Act 1985, as amended, or any employees or premises;
- it will not transfer, sell, lend, part with or otherwise dispose of all or any of its assets, properties or undertakings or any interest, estate, right, title or benefit therein other than as contemplated in the transaction documents;
- it will not pay any dividend or make any other distribution to its shareholders, other than in accordance with the Funding 1 deed of charge, and it will not issue any new shares;

- it will not incur any indebtedness in respect of any borrowed money or give any guarantee in respect of any indebtedness (other than indebtedness contemplated by the transaction documents) or of any obligation of any person whatsoever; and
- it will not enter into any amalgamation, demerger, merger or reconstruction, nor acquire any assets or business nor make any investments, other than as contemplated in the transaction documents.

### **Payments of interest**

Payment of interest and issuing entity fees pursuant to the intercompany loan agreement will be made only from and to the extent of distributions by the mortgages trustee of amounts constituted from mortgages trust available revenue receipts to Funding 1 in respect of the Funding 1 share. Such payments of interest and issuing entity fees will be made on Funding 1 interest payment dates in the order of priorities set forth in “**Cashflows**” below.

The interest rates applicable to the loan tranches from time to time will be determined (other than, in each case, in respect of the first interest period) by reference to LIBOR for three-month sterling deposits or such other sterling LIBOR rate as may be specified in the applicable loan tranche supplement plus or minus, in each case, a margin which may differ for each separate loan tranche. Any applicable final terms will also set out details relating to the Funding 1 interest payment dates and payment of interest on each loan tranche.

In addition, prior to enforcement of the Funding 1 security, Funding 1 will agree to pay an additional fee (inclusive of VAT, if any) to the issuing entity (the **issuing entity fee**) on each Funding 1 interest payment date or otherwise when required. The issuing entity fee will be equal to the amount needed by the issuing entity to pay or provide for amounts falling due, if any, to be paid to its creditors (other than amounts of interest and principal due on the notes, corresponding payments to be made by the issuing entity to any issuing entity swap providers (excluding termination payments, unless made using any premium received from any replacement swap provider) and tax that can be met out of the issuing entity’s profits). In addition, the issuing entity fee shall include a sum (in an amount equal to £5,000 (or such lesser amount as the directors of the issuing entity may determine)) to be retained by the issuing entity as profit. The issuing entity fee will be paid by Funding 1 out of the Funding 1 available revenue receipts.

### **Repayment of principal on the rated loan tranches**

Repayment of a rated loan tranche may be made by way of bullet repayment, scheduled amortisation instalments or on a pass-through basis. A rated loan tranche with a bullet repayment date is an advance that is scheduled to be repaid in full in one instalment on one Funding 1 interest payment date (a **bullet loan tranche**). A rated loan tranche with scheduled amortisation is an advance that is scheduled to be repaid in instalments (each a **scheduled amortisation instalment**) on more than one Funding 1 interest payment date (a **scheduled amortisation loan tranche**). A rated loan tranche with pass-through repayment is an advance that has no scheduled repayment date other than its final repayment date (a **pass-through loan tranche**). Rated loan tranches with pass-through repayment will be repaid on or after the Funding 1 interest payment date on which the rated loan tranches with the same series designation and a higher rating designation in respect of the relevant series have been fully repaid.

Repayment of principal on the rated loan tranches will only be made from and to the extent of distributions by the mortgages trustee of amounts constituted from mortgages trust available principal receipts to Funding 1 in respect of the Funding 1 share.

The applicable loan tranche supplement and the applicable final terms will set forth (i) the bullet repayment dates (for a bullet loan tranche), (ii) the scheduled repayment dates (for a scheduled amortisation loan tranche) or (iii) the Funding 1 interest payment date on which principal is expected to be repaid (for a pass-through loan tranche), as applicable. Each such date will be the same as the equivalent dates for the related series and class of notes.

A rated loan tranche (or part thereof) will become due on the earlier to occur of:

- the final repayment date of such rated loan tranche;
- the date upon which a trigger event occurs;
- the date upon which an intercompany loan acceleration notice is served on Funding 1; and

- the step-up date, if any, in relation to the relevant rated loan tranche as specified in the applicable loan tranche supplement and applicable final terms,

in each case subject to the applicable Funding 1 priority of payments.

#### **Repayment of principal on the subordinated loan tranches**

Funding 1 will repay each subordinated loan tranche, but only (a) on any Funding 1 interest payment date, to the extent that the aggregate outstanding principal balance of the subordinated loans exceeds the required subordinated loan tranche principal amount outstanding and to the extent that it has Funding 1 available principal receipts after making higher ranking payments or (b) on any date, to the extent that it is being refinanced by another loan tranche (which may be another subordinated loan tranche). Principal due on the subordinated loan tranches are payable after principal is due on the rated loan tranches.

A subordinated loan tranche (or part thereof) will become due on the earlier to occur of:

- the date on which all notes have been redeemed in full;
- the date upon which a trigger event occurs; and
- the date upon which an intercompany loan acceleration notice is served on Funding 1,

in each case subject to the applicable Funding 1 priority of payments.

#### **Repayment of principal on the start-up loan tranches**

Funding 1 will repay each start-up loan tranche, but only to the extent that it has Funding 1 available revenue receipts after making higher ranking payments. Principal due on the start-up loan tranches are payable in accordance with the Funding 1 pre-enforcement revenue priority of payments.

A start-up loan tranche (or part thereof) will become due on the earlier to occur of:

- the date on which all notes have been redeemed in full and all of the issuing entity subordinated loans have been repaid in full;
- the date upon which a trigger event occurs; and
- the date upon which an intercompany loan acceleration notice is served on Funding 1,

in each case subject to the applicable Funding 1 priority of payments.

#### **Deferral of principal**

In each case, when a loan tranche becomes due, it shall continue to be due until it is fully repaid. If there are insufficient funds available to repay a loan tranche on a Funding 1 interest payment date upon which that loan tranche has become or remains due, then the shortfall will be repaid on subsequent Funding 1 interest payment dates from Funding 1 available principal receipts until that loan tranche is fully repaid.

#### **Limited recourse**

Funding 1 is only obliged to pay amounts to the issuing entity in respect of any loan tranche to the extent that it has funds to do so after making payments ranking in priority to amounts due on such loan tranches (including amounts due on loan tranches of a more senior ranking).

If, prior to the latest final repayment date of the loan tranches outstanding under the intercompany loan agreement, there is a shortfall between the amount of interest and/or principal due on that loan tranche and the amount available to Funding 1 to make that payment, then that shortfall shall not be due and payable to the issuing entity until such time (if ever) as Funding 1 has enough money available to pay the shortfall on that loan tranche (after making any other payments due that rank higher in priority to that loan tranche).

If, following the latest final repayment date of the loan tranches outstanding under the intercompany loan agreement, there is a shortfall between the amount required to pay all outstanding interest and/or principal and/or

other amounts outstanding under the intercompany loan agreement, then all outstanding claims of the issuing entity against Funding 1 will be extinguished.

### **Intercompany loan events of default**

The intercompany loan agreement contains events of default (each an **intercompany loan event of default**), which include, among others, the following events:

- a default by Funding 1 for a period of three London business days in the payment of any amount payable under the intercompany loan agreement (but subject to the limited recourse provisions described in this section);
- Funding 1 does not in the opinion of the issuing entity security trustee (as instructed by the note trustee) comply in any material respect with its obligations under any of the transaction documents (other than non-payment as set out in the preceding paragraph) and that non-compliance, if capable of remedy, is not remedied promptly and in any event within 20 London business days of the earlier to occur of Funding 1 becoming aware of its non-compliance and receipt of written notice from the issuing entity security trustee requiring Funding 1's non-compliance to be remedied; or
- an insolvency event occurs in relation to Funding 1 or it is, or becomes, unlawful for Funding 1 to perform its obligations under any of the transaction documents.

Investors should note that, as described in “– **Repayment of principal on the loan tranches**” and “– **Limited recourse**” above, it will not be an intercompany loan event of default if default is made by Funding 1 in paying amounts due under the intercompany loan agreement where Funding 1 does not have the money available to make the relevant payment or where the repayment tests are not satisfied. The ability of the issuing entity to repay each series and class of notes will depend, among other things, upon payments received by the issuing entity from Funding 1 under the corresponding loan tranches pursuant to the intercompany loan agreement. See “**Risk factors – Funding 1 is not obliged to make payments on the loan tranches if it does not have enough money to do so, which could adversely affect payments on the notes**” above.

If an intercompany loan event of default occurs and is continuing under the intercompany loan agreement, then the issuing entity security trustee (acting at the direction of the note trustee) will be entitled to serve an intercompany loan acceleration notice on Funding 1 stating that an intercompany loan event of default has occurred. Upon the service of such an intercompany loan acceleration notice, the issuing entity security trustee may direct that all loan tranches outstanding under the intercompany loan agreement become immediately due and payable or that all loan tranches outstanding under the intercompany loan agreement shall become due and payable on the demand of the issuing entity security trustee, subject to its being indemnified and/or secured to its satisfaction.

## **Funding 1's bank accounts**

Funding 1 maintains two bank accounts in England in its name with Bank of Scotland, as the **account bank**. These are:

- the **Funding 1 GIC account**: the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any) and/or amounts received by Funding 1 under a start-up loan tranche for the purposes of contributing to Funding 1 available revenue receipts on the following interest payment date will be credited to this account and, on each distribution date, any distribution of mortgages trust available revenue receipts or mortgages trust available principal receipts to Funding 1 under the mortgages trust deed and any balance remaining in the Funding 1 cash accumulation ledger will initially be deposited in this account; and
- the **Funding 1 transaction account**: on each Funding 1 interest payment date, monies standing to the credit of the Funding 1 GIC account are transferred to the Funding 1 transaction account and applied by the cash manager in accordance with the relevant Funding 1 priority of payments. Amounts representing Funding 1's profits are retained in the Funding 1 transaction account.

These accounts may be required to be transferred to an alternative bank if the short-term, unguaranteed and unsecured ratings of the account bank fall below F1 by Fitch, P-1 by Moody's or A-1+ by Standard & Poor's, unless each rating agency confirms that its then current rating of the notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of such ratings falling below these minimum ratings.

## **Governing law**

The intercompany loan agreement is governed by English law.

## Security for Funding 1's obligations

Funding 1 provided security for its obligations under the intercompany loan agreement and the other transaction documents to which it is or will be a party by entering into the Funding 1 deed of charge with the Funding 1 secured creditors on the programme date. A summary of the material terms of the Funding 1 deed of charge is set out below. The summary does not purport to be complete and is subject to the provisions of the Funding 1 deed of charge.

The Funding 1 deed of charge has seven primary functions:

- it sets out certain covenants of Funding 1;
- it creates security interests in favour of the Funding 1 security trustee, which the Funding 1 security trustee holds on trust for itself and each of the other Funding 1 secured creditors (including secured creditors that accede to the Funding 1 deed of charge in connection with future loan tranches or new intercompany loans);
- it sets out the order in which the cash manager applies money received by Funding 1 prior to enforcement of the security;
- it sets out the enforcement procedures relating to a default by Funding 1 on its covenants under the transaction documents to which it is a party (including provisions relating to the appointment of a receiver);
- it sets out the order in which the Funding 1 security trustee applies money received by Funding 1 after the service of an intercompany loan acceleration notice on Funding 1;
- it sets out the appointment of the Funding 1 security trustee, its powers and responsibilities and the limitations on those responsibilities; and
- it sets out how new creditors of Funding 1 can accede to the terms of the Funding 1 deed of charge as new Funding 1 secured creditors.

### Covenants of Funding 1

The Funding 1 deed of charge contains covenants made by Funding 1 in favour of the Funding 1 security trustee on trust for the benefit of itself and the other Funding 1 secured creditors, including that it will comply with its other obligations under the transaction documents to which it is or will be a party.

### Funding 1 security

Under the Funding 1 deed of charge, Funding 1 has created the following security interests in favour of the Funding 1 security trustee for itself and as trustee on behalf of the other Funding 1 secured creditors (the **Funding 1 security**) in respect of its obligations under the intercompany loan agreement and the other transaction documents to which it is or will be a party:

- an assignment by way of first fixed security (or, to the extent not assignable, charge by way of a first fixed charge) (which is likely to take effect as a floating charge) of its rights in respect of the Funding 1 share;
- an assignment by way of first fixed security (or, to the extent not assignable, charge by way of a first fixed charge) (which is likely to take effect as a floating charge) of all of its rights in the transaction documents to which Funding 1 is a party from time to time;
- a first fixed charge (which is likely to take effect as a floating charge) over all of Funding 1's rights in respect of all amounts standing to the credit of the Funding 1 GIC account, the Funding 1 transaction account and any other Funding 1 account from time to time, all interest paid or payable in relation to those amounts and all debts represented by those amounts;

- all authorised investments made or purchased from time to time by or on behalf of Funding 1 using monies standing to the credit of those accounts and all interest, monies and proceeds paid or payable in relation to the Funding 1 authorised investments;
- a first fixed charge (which is likely to take effect as a floating charge) over all of its rights in respect of the benefit of all authorisations (statutory or otherwise) held in connection with the use of any of the property charged by Funding 1 pursuant to the Funding 1 deed of charge and any compensation which may be payable to it in respect of those authorisations.
- a first floating charge over all of the property, assets and undertaking of Funding 1 not otherwise secured by any fixed security interest detailed above (but excepting from the foregoing exclusion all of Funding 1's property, assets and undertaking situated in Scotland or the rights to which are governed by Scots law, all of which are charged by the floating charge).

#### *Nature of security – fixed charge*

Whether a fixed security interest expressed to be created by the Funding 1 deed of charge will be upheld under English law as a fixed security interest rather than floating security will depend, among other things, on whether the Funding 1 security trustee has the requisite degree of control over Funding 1's ability to deal in the relevant assets and the proceeds thereof and, if so, whether such control is exercised by the Funding 1 security trustee in practice. However, it is likely that the Funding 1 security trustee does not exert sufficient control over the accounts of Funding 1 for the charges over those account to take effect as fixed charges. In addition, any assignment, charge or security granted over an asset which is expressed to be a fixed charge may be characterised as a floating charge if the proceeds thereof are paid into a bank account over which the Funding 1 security trustee is not deemed to have sufficient control. Such is likely to be the case in respect of the other security expressed above to be fixed security.

Scots law does not recognise any equivalent concept of fixed charges taking effect as floating charges, as described above in relation to English law.

#### *Nature of security – floating charge*

Unlike the fixed charges, the **floating charge** does not attach to specific assets but instead “floats” over a class of assets which may change from time to time, allowing Funding 1 to deal with those assets and to give third parties title to those assets free from any encumbrance in the event of sale, discharge or modification, provided those dealings and transfers of title are in the ordinary course of Funding 1's business. Any of Funding 1's assets acquired after the programme date (including assets acquired as a result of the disposition of any other asset of Funding 1), which are not subject to the fixed charges mentioned in this section (including all of Funding 1's Scottish assets) will be subject to the floating charge.

The existence of the floating charge will allow the Funding 1 security trustee to appoint an administrative receiver of Funding 1 as long as the capital markets exception is available. The main advantage of the Funding 1 security trustee being able to appoint an administrative receiver is that a person entitled to appoint an administrative receiver can prevent the appointment of an administrator of Funding 1, which allows the Funding 1 security trustee to control proceedings in the event any of Funding 1's other creditors seek such action. See “**Risk factors – Changes of law**” above relating to the appointment of an administrative receiver.

The interest of the Funding 1 secured creditors in property and assets over which there is a floating charge only will rank behind the expenses of any liquidation or any administration and the claims of certain preferential creditors on enforcement of the Funding 1 security. This means that the expenses of any liquidation or any administration and preferential creditors will be paid out of the proceeds of enforcement of the floating charge ahead of amounts due to the issuing entity under the intercompany loan agreement. Section 250 of the Enterprise Act abolishes crown preference in relation to all insolvencies (and thus reduces the categories of preferential debts that are to be paid in priority to the debts due to the holder of a floating charge) but a new Section 176A of the Insolvency Act (as inserted by Section 251 of the Enterprise Act) requires a “prescribed part” (up to a maximum amount of £600,000) of the floating charge realisations available for distribution to be set aside to satisfy the claims of unsecured creditors. This means that the expenses of any liquidation or administration, the claims of preferential creditors and the beneficiaries of the prescribed part will be paid out of the proceeds of enforcement of the floating charge ahead of amounts due to the issuing entity and ultimately the noteholders. The prescribed part will not be relevant to property subject to a valid fixed security interest or to a situation in which there are no unsecured creditors.

The floating charge created by the Funding 1 deed of charge may “crystallise” and become a fixed charge over the relevant class of assets owned by Funding 1 at the time of crystallisation. Crystallisation will occur automatically following the occurrence of specific events set out in the Funding 1 deed of charge, including, among other events, notice to Funding 1 from the Funding 1 security trustee following an intercompany loan event of default, except in relation to Funding 1’s Scottish assets where crystallisation will occur only on the appointment of an administrative receiver or on the commencement of the winding-up of Funding 1. A crystallised floating charge will rank ahead of the claims of unsecured creditors, which are in excess of the prescribed part, but will continue to rank behind the expenses of any liquidation or any administration and the claims of preferential creditors (as referred to in this section) and the beneficiaries of the prescribed part on enforcement of the Funding 1 security.

### **Funding 1 pre-enforcement priority of payments**

The Funding 1 deed of charge sets out the priority of distribution by the cash manager, as at the programme date and prior to the service of an intercompany loan acceleration notice on Funding 1, of amounts standing to the credit of the Funding 1 transaction account on each Funding 1 interest payment date. This priority is described in “**Cashflows – Distribution of Funding 1 available revenue receipts before intercompany loan acceleration**” and “**Cashflows – Distribution of Funding 1 available principal receipts**” below.

### **Enforcement**

The Funding 1 deed of charge sets out the general procedures by which the Funding 1 security trustee may take steps to enforce the Funding 1 security so that the Funding 1 security trustee can protect the interests of each of the Funding 1 secured creditors.

The Funding 1 deed of charge provides that the Funding 1 security trustee will not, and will not be bound to, take any steps, institute any proceedings, exercise its rights and/or take any other action under or in connection with the transaction documents (including, without limitation, enforcing the Funding 1 security), unless it is directed to do so by the issuing entity security trustee, which (for so long as any notes remain outstanding) must act only in accordance with the directions of the note trustee. This provision may be amended in the event that Funding 1 enters into a new intercompany loan agreement with any new Funding 1 issuing entity or Funding 1 issues any new notes directly. The Funding 1 security trustee will only act if it is indemnified and/or secured to its satisfaction.

The Funding 1 security will become enforceable upon the service of an intercompany loan acceleration notice under the intercompany loan, provided that, if the Funding 1 security has become enforceable otherwise than by reason of a default in payment of any amount due in respect of the loan tranches with the highest designated credit rating then outstanding, the Funding 1 security trustee will not be entitled to dispose of all or part of the assets comprised in the Funding 1 security unless either:

- a sufficient amount would be realised to allow a full and immediate discharge of all amounts owing in respect of all the loan tranches with the highest designated credit rating then outstanding and all prior ranking amounts due by Funding 1; or
- the Funding 1 security trustee is of the sole opinion that the cashflow prospectively receivable by Funding 1 will not (or that there is a significant risk that it will not) be sufficient, having regard to any other relevant actual, contingent or prospective liabilities of Funding 1, to discharge in full in due course all amounts owing in respect of all the loan tranches with the highest designated credit rating then outstanding and all prior ranking amounts due by Funding 1.

Each of the Funding 1 secured creditors (other than the Funding 1 security trustee) have agreed under the Funding 1 deed of charge that they will not take steps or proceedings against Funding 1 for the purposes of recovering any amounts owing to them.

### **Funding 1 post-enforcement priority of payments**

The Funding 1 deed of charge sets out the priority of distribution as at the programme date by the Funding 1 security trustee, following service of an intercompany loan acceleration notice, of amounts received or recovered by the Funding 1 security trustee or a receiver appointed on its behalf. This priority is described in “**Cashflows – Distribution of Funding 1 principal receipts and Funding 1 revenue receipts following intercompany loan acceleration**” below.



## **New Funding 1 issuing entities**

If any other Funding 1 issuing entities are established to issue notes and accordingly to make advances to Funding 1, such Funding 1 issuing entities and other applicable creditors of Funding 1 will enter into deeds of accession or supplemental deeds in relation to the Funding 1 deed of charge which may, depending on the type of notes to be issued, require amendments, among other things, to any of the Funding 1 pre-enforcement revenue priority of payments, the Funding 1 pre-enforcement principal priority of payments and the Funding 1 post-enforcement priority of payments.

## **Appointment, powers, responsibilities and liabilities of the Funding 1 security trustee**

The Funding 1 security trustee was appointed to act as trustee on behalf of the Funding 1 secured creditors on the terms and conditions of the Funding 1 deed of charge. It holds the benefit of the Funding 1 security created by the Funding 1 deed of charge on trust for itself and each of the other Funding 1 secured creditors in accordance with the terms and conditions of the Funding 1 deed of charge.

The Funding 1 security trustee may concur with any person in making any modifications to the transaction documents only if so directed by the issuing entity security trustee so long as there is any loan tranche outstanding under the intercompany loan agreement and otherwise with the prior consent of all of the Funding 1 secured creditors. This provision may be amended in the event that Funding 1 enters into a new intercompany loan agreement with any new Funding 1 issuing entity or Funding 1 issues any new notes directly. The issuing entity security trustee may give such direction only (for so long as any notes remain outstanding) if so directed by the note trustee. The note trustee may give such direction, without the consent or sanction of the noteholders, provided that:

- the note trustee is of the opinion that such modification will not be materially prejudicial to the interests of the holders of any series or class of notes; or
- in the sole opinion of the note trustee, such modification is necessary to correct a manifest error or is of a formal, minor or technical nature or is to comply with the mandatory provisions of law.

The note trustee is entitled to assume that such modification will not be materially prejudicial to the interests of the noteholders if each of the rating agencies has confirmed that the then current rating by it of the notes would not be adversely affected by such modification.

In addition, the Funding 1 security trustee will give its consent to any modifications to any transaction document that are requested by Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf), provided that Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf), as the case may be, certifies to the Funding 1 security trustee (in writing) that such modifications are required in order to accommodate (among other things):

- (i) notes to be issued by the issuing entity and/or loan tranches to be made available by the issuing entity to Funding 1 under the intercompany loan agreement (including further classes of notes and their corresponding loan tranches);
- (ii) the entry by Funding 1 into a new intercompany loan agreement and/or the issue of new notes by Funding 1 issuing entities or by Funding 1 directly;
- (iii) the accession of new Funding 1 secured creditors and/or new issuing entity secured creditors;
- (iv) the assignment of new types of loans or their related security to the mortgages trustee (including the assignment of loans and their related security originated under brands other than Birmingham Midshires and/or by entities in the HBOS group other than the seller);
- (v) the inclusion of a new funding beneficiary as a beneficiary of the mortgages trust;
- (vi) the acquisition by Funding 1, a new funding beneficiary or the mortgages trustee of an interest in any other securitisation involving products originated by the HBOS group;
- (vii) changes to be made to the Funding 1 reserve required amount, the Funding 1 liquidity reserve fund required amount and/or the manner in which any Funding 1 reserve fund is funded;
- (viii) different Funding 1 interest payment dates, interest periods and/or bases for the calculation of interest in respect of any loan tranches then outstanding under the intercompany loan agreement); and/or

(ix) changes to be made to the definitions of asset trigger event and non-asset trigger event,

and provided further that:

- in respect of the matters listed in paragraph (i) to (v), the conditions precedent to notes being issued by the issuing entity and/or loan tranches being made available to Funding 1, new notes being issued by Funding 1 issuing entities or by Funding 1 directly and/or new loans being made available to Funding 1, the accession of new Funding 1 secured creditors and/or new issuing entity secured creditors, the assignment of new types of loans to the mortgages trustee and the inclusion of a new funding beneficiary as a beneficiary of the mortgages trust have been satisfied; and
- in respect of the matters listed in paragraphs (i) to (ix), Funding 1 and/or the Funding 1 security trustee has received written confirmation from each of the rating agencies then rating the notes that the relevant modifications will not result in a reduction, withdrawal or (in the case of S&P and Moody's) qualification of the then current ratings of the notes.

#### *Funding 1 security trustee's fees and expenses*

Funding 1 shall pay to the Funding 1 security trustee a fee (inclusive of VAT, if any) payable on dates and in the amount agreed from time to time by the Funding 1 security trustee and Funding 1. Funding 1 will also pay, on written request, all costs, charges and expenses (including any amount in respect of irrecoverable VAT chargeable thereon) properly incurred in relation to:

- the negotiation, preparation and execution of and the exercise of its powers and the performance of its duties under transaction documents; or
- any action taken or contemplated by the Funding 1 security trustee for enforcing the transaction documents.

The Funding 1 security trustee is entitled to additional fees if it undertakes duties of an exceptional nature or otherwise outside the scope of the normal duties of the Funding 1 security trustee, as further set out in the Funding 1 deed of charge.

Furthermore, Funding 1 agrees to indemnify the Funding 1 security trustee against all liabilities to which it may be or become subject or which may be incurred by it in the proper execution or purported execution of any of its trusts, powers, authorities and discretions under the transaction documents or its functions pursuant to its appointment as Funding 1 security trustee.

Funding 1 is not responsible under the Funding 1 deed of charge for any liabilities, losses, damages, costs or expenses resulting from fraud, wilful default or gross negligence by the Funding 1 security trustee.

#### *Retirement and removal*

Subject to the appointment of a trust corporation as a successor Funding 1 security trustee, the Funding 1 security trustee may retire after giving three months' notice in writing to Funding 1. In order to be eligible to act as Funding 1 security trustee, such successor must meet the applicable eligibility requirements under the Funding 1 deed of charge, including the requirement that it satisfies the minimum capitalisation and other applicable conditions in regards to trustee eligibility set forth in the Investment Company Act. If within two months of having given notice of its intention to retire, Funding 1 has failed to appoint a replacement Funding 1 security trustee, the Funding 1 security trustee will be entitled to appoint its own successor trustee being a trust corporation.

The noteholders may, by extraordinary resolution of each class thereof, instruct the note trustee to instruct the issuing entity security trustee to remove the Funding 1 security trustee at any time.

In addition, the Funding 1 security trustee may, subject to conditions specified in the Funding 1 deed of charge, appoint a co-trustee to act jointly with it.

#### *Additional provisions of the Funding 1 deed of charge*

The Funding 1 deed of charge contains a range of provisions regulating the scope of the Funding 1 security trustee's duties and liabilities. These include the following:

- the Funding 1 security trustee is not responsible for the execution, delivery, legality, validity, adequacy, admissibility in evidence or enforceability of the Funding 1 deed of charge or any other transaction document or the title, ownership, value, sufficiency, enforceability or existence of any of the property charged by Funding 1 (or the security relating thereto);
- the Funding 1 security trustee is not, and will not be bound, to exercise its powers under the Funding 1 deed of charge without being directed to do so by the issuing entity security trustee (and then only to the extent that it is indemnified and/or secured to its satisfaction), which direction (for so long as the notes remain outstanding) may not be given unless the issuing entity security trustee has been directed or requested to do so by the note trustee. The note trustee is not obliged to give such direction or request to the issuing entity security trustee unless it is directed or requested to do so by an extraordinary resolution of any class of the noteholders (which for this purpose means the noteholders of all series of notes constituting that class) or in writing by the holders of at least 25 per cent. of the aggregate principal amount outstanding of any class of the notes then outstanding (which for this purpose means the noteholders of all series of notes constituting that class) (and then only to the extent that it is indemnified and/or secured to its satisfaction) provided that:
  - (i) the note trustee shall not be obliged to act at the direction or request of the class B noteholders unless either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class A noteholders or the action is sanctioned by an extraordinary resolution of the class A noteholders;
  - (ii) the note trustee shall not be obliged to act at the direction or request of the class M noteholders unless (i) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class A noteholders or the action is sanctioned by an extraordinary resolution of the class A noteholders and (ii) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class B noteholders or the action is sanctioned by an extraordinary resolution of the class B noteholders;
  - (iii) the note trustee shall not be obliged to act at the direction or request of the class C noteholders unless (i) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class A noteholders or the action is sanctioned by an extraordinary resolution of the class A noteholders and (ii) either so to do would not, in its sole discretion, be materially prejudicial to the interests of the class B noteholders or the action is sanctioned by an extraordinary resolution of the class B noteholders and (iii) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class M noteholders or the action is sanctioned by an extraordinary resolution of the class M noteholders; and
  - (iv) the note trustee shall not be obliged to act at the direction or request of the class D noteholders unless (i) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class A noteholders or the action is sanctioned by an extraordinary resolution of the class A noteholders and (ii) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class B noteholders or the action is sanctioned by an extraordinary resolution of the class B noteholders and (iii) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class M noteholders or the action is sanctioned by an extraordinary resolution of the class M noteholders and (iv) either so to do would not, in its sole opinion, be materially prejudicial to the interests of the class C noteholders or the action is sanctioned by an extraordinary resolution of and the class C noteholders;
- the Funding 1 security trustee may rely (without investigation or further inquiry) on a certificate or confirmation of the agent bank, any paying agent, any of the ratings agencies or any reference bank and shall not be bound in any such case to call for further evidence or be responsible for any loss, liability, costs, damages, expenses or inconvenience that may be occasioned by its failing so to do or the exercise or non-exercise by the Funding 1 security trustee of any of its powers, duties and discretions under the transaction documents;
- the Funding 1 security trustee is not bound to take steps to ascertain whether any intercompany loan event of default has occurred and, until it shall have actual written notice to the contrary, shall be entitled to assume that no intercompany loan event of default has occurred and that Funding 1 is

observing and performing all its obligations under the Funding 1 deed of charge and the other transaction documents;

- each Funding 1 secured creditor must make its own independent appraisal of and investigations into the financial condition, creditworthiness, condition, affairs, status and nature of Funding 1 and the Funding 1 security trustee shall not at any time have any responsibility for the same and no Funding 1 secured creditor shall rely on the Funding 1 security trustee in respect thereof; and
- the Funding 1 security trustee and its directors, officers, holding companies and associated companies may enter into any contract, transaction or arrangement with Funding 1 or any of the other parties to the transaction documents as if it were not the Funding 1 security trustee and shall be entitled to exercise and enforce its rights, comply with its obligations and perform its duties under any such contract, transaction or arrangement without regard to the interests of the Funding 1 secured creditors.

The Funding 1 security trustee makes no statement or representation in this base prospectus, has not authorised or caused the issue of any part of it and expressly disclaims and takes no responsibility for any part of it. The Funding 1 security trustee does not guarantee the performance of the intercompany loan or the payment of principal of or interest on the intercompany loan.

### **Governing law**

The Funding 1 deed of charge is governed by English law, provided that any terms that are particular to Scots law shall be construed in accordance with the laws of Scotland.

### Security for the issuing entity's obligations

The issuing entity has provided security for its obligations under the notes and the other transaction documents to which it is or will be a party by entering into the issuing entity deed of charge with the issuing entity secured creditors (other than the noteholders).

A summary of the material terms of the issuing entity deed of charge is set out below. The summary does not purport to be complete and is subject to the provisions of the issuing entity deed of charge.

The issuing entity deed of charge has seven primary functions:

- it sets out certain covenants of the issuing entity;
- it creates security interests in favour of the issuing entity security trustee, which the issuing entity security trustee then holds on trust for itself and each of the other issuing entity secured creditors (including secured creditors that accede to the issuing entity deed of charge in connection with future series and classes of notes or future issuing entity subordinated loans);
- it sets out the order in which the issuing entity cash manager applies money received by the issuing entity prior to enforcement of the security;
- it sets out the enforcement procedures relating to a default by the issuing entity of its covenants under the transaction documents (including the appointment of a receiver);
- it sets out the order in which the issuing entity security trustee applies monies standing to the credit of the issuing entity transaction account following the service of a note acceleration notice on the issuing entity;
- it sets out the appointment of the issuing entity security trustee, its powers and responsibilities and the limitations on those responsibilities; and
- it sets out how creditors of the issuing entity can accede to the terms of the issuing entity deed of charge.

### Covenants of the issuing entity

The issuing entity deed of charge contains covenants made by the issuing entity in favour of the issuing entity security trustee on trust for the benefit of itself and the other issuing entity secured creditors, including that it will comply with its other obligations under the transaction documents to which it is or will be a party.

### Issuing entity security

Under the issuing entity deed of charge, the issuing entity created the following security interests in favour of the issuing entity security trustee for and on behalf of the issuing entity secured creditors (the **issuing entity security**), in respect of its obligations under the notes and the other transaction documents to which it is or will be a party:

- an assignment by way of first fixed security (or, to the extent not assignable, charge by way of first fixed charge) (which is likely to take effect as a floating charge) of all of the issuing entity's rights in respect of the transaction documents to which it is a party from time to time (without prejudice to, in respect of any issuing entity swap agreements and after giving effect to, any contractual netting provision confined in such agreements);
- a first fixed charge (which is likely to take effect as a floating charge) over all of issuing entity's rights in respect of all amounts standing to the credit of the issuing entity transaction account and any other issuing entity bank account from time to time, all interest paid or payable in relation to those amounts and all debts represented by those amounts;

- a first fixed charge (which is likely to take effect as a floating charge) over all of the issuing entity's rights in all authorised investments made or purchased by or on behalf of the issuing entity using monies standing to the credit of the issuing entity accounts and all interest, monies and proceeds paid or payable in relation to those authorised investments; and
- a first floating charge over all of the issuing entity's property, assets (including, without limitation, its uncalled capital) and undertaking not otherwise effectively charged or assigned by way of fixed charge or assignment detailed above (but excepting from the foregoing exclusion all of the issuing entity's property, assets and undertaking situated in Scotland or the rights to which are governed by Scots law, all of which are charged by the floating charge).

#### *Nature of security – fixed charge*

Whether a fixed security interest expressed to be created by the issuing entity deed of charge will be upheld under English law as a fixed security interest rather than floating security will depend, among other things, on whether the issuing entity security trustee has the requisite degree of control over the issuing entity's ability to deal in the relevant assets and the proceeds thereof and, if so, whether such control is exercised by the issuing entity security trustee in practice. However, it is likely that the issuing entity security trustee does not exert sufficient control over the issuing entity transaction account for the charges over such account to take effect as a fixed charge. In addition, any assignment, charge or security granted over an asset which is expressed to be a fixed charge may be characterised a floating charge if the proceeds thereof are paid into a bank account over which the issuing entity security trustee is not deemed to have sufficient control. Such may be the case in respect of the other security expressed above to be fixed security.

Scots law does not recognise any equivalent concept of fixed charges taking effect as floating charges, as described above in relation to English law.

#### *Nature of security – floating charge*

Unlike the fixed charges, the floating charge does not attach to specific assets but instead “floats” over a class of assets which may change from time to time, allowing the issuing entity to deal with those assets and to give third parties title to those assets free from any encumbrance in the event of sale, discharge or modification, provided those dealings and transfers of title are in the ordinary course of the issuing entity's business. Any assets acquired by the issuing entity after the programme date (including assets acquired as a result of the disposition of any other assets of the issuing entity) which are not subject to the fixed charges mentioned in this section (including all of the issuing entity's Scottish assets) will be subject to the floating charge.

The existence of the floating charge allows the issuing entity security trustee to appoint an administrative receiver of the issuing entity as long as the capital markets exception is available. The main advantage of the issuing entity security trustee being able to appoint an administrative receiver is that a person entitled to appoint an administrative receiver can prevent the appointment of an administrator of the issuing entity, which allows the issuing entity security trustee to control proceedings in the event the issuing entity's other creditors seek such action. However, see “**Risk factors – Changes of law**” above relating to the appointment of administrative receivers.

The interest of the issuing entity secured creditors in property and assets over which there is a floating charge will rank behind the expenses of any liquidation or administration and the claims of certain preferential creditors on enforcement of the issuing entity security. This means that the expenses of any liquidation or any administration and the claims of preferential creditors will be paid out of the proceeds of enforcement of the floating charge ahead of amounts due to the noteholders. Section 250 of the Enterprise Act abolishes crown preference in relation to all insolvencies (and thus reduces the categories of preferential debts that are to be paid in priority to debts due to the holder of a floating charge) but a new Section 176A of the Insolvency Act (as inserted by Section 251 of the Enterprise Act) requires a “prescribed part” (up to a maximum amount of £600,000) of the floating charge realisations available for distribution to be set aside to satisfy the claims of unsecured creditors. This means that the expenses of any liquidation or administration, the claims of preferential creditors and the beneficiaries of the prescribed part will be paid out of the proceeds of enforcement of the floating charge ahead of amounts due to noteholders. The prescribed part will not be relevant to property subject to a valid fixed security interest or to a situation in which there are no unsecured creditors.

The floating charge created by the issuing entity deed of charge may “crystallise” and become a fixed charge over the relevant class of assets owned by the issuing entity at the time of crystallisation. Except in relation to the issuing entity's Scottish assets, crystallisation will occur automatically following the occurrence of specific events set out in the issuing entity deed of charge, including, among other events, service of a note acceleration

notice to the issuing entity from the note trustee following an event of default under the notes. In relation to the issuing entity's Scottish assets, crystallisation will occur only on the appointment of an administrative receiver or on the commencement of the winding-up of the issuing entity. A crystallised floating charge will rank ahead of the claims of unsecured creditors which are in excess of the prescribed part, but will rank behind the expenses of any liquidation or administration, the claims of preferential creditors (as referred to in this section) and the beneficiaries of the prescribed part on enforcement of the issuing entity security.

### **Enforcement**

The issuing entity deed of charge sets out the general procedures by which the issuing entity security trustee may take steps to enforce the issuing entity security so that the issuing entity security trustee can protect the interests of each of the issuing entity secured creditors.

The issuing entity deed of charge provides that the issuing entity security trustee will not, and will not be bound to take any steps, institute any proceedings, exercise its rights and/or take any other action under or in connection with the transaction documents (including, without limitation, enforcing the issuing entity security) unless it is so directed by the note trustee (for so long as any notes remain outstanding) and indemnified and/or secured to its satisfaction.

The issuing entity security will become enforceable upon the service of a note acceleration notice or, if there are no notes outstanding, following a default in payment of any other secured obligation of the issuing entity, provided that, if the issuing entity security has become enforceable otherwise than by reason of a default in payment of any amount due on the class A notes or any other most senior class of notes then outstanding, the issuing entity security trustee will not be entitled to dispose of all or part of the assets comprised in the issuing entity security unless either:

- a sufficient amount would be realised to allow a discharge in full of all amounts owing in respect of the class A notes or such other most senior class of notes then outstanding and all prior ranking amounts due by the issuing entity; or
- the issuing entity security trustee is of the sole opinion that the cashflow prospectively receivable by the issuing entity will not (or that there is a significant risk that it will not) be sufficient, having regard to any other relevant actual, contingent or prospective liabilities of the issuing entity, to discharge in full in due course all amounts owing in respect of the class A notes or such other most senior class of notes then outstanding and all prior ranking amounts due by the issuing entity.

Each of the issuing entity secured creditors (other than the note trustee acting on behalf of the noteholders and the issuing entity security trustee) will agree under the issuing entity deed of charge that they will not take steps or proceedings against the issuing entity for the purposes of recovering any amounts owing to them.

### **Issuing entity post-enforcement priority of payments**

The issuing entity deed of charge sets out the priority of distribution by the issuing entity security trustee (following service of a note acceleration notice on the issuing entity but prior to service of an intercompany loan acceleration notice on Funding 1 and following service of both a note acceleration notice on the issuing entity and an intercompany loan acceleration notice on Funding 1) of amounts received or recovered by the issuing entity security trustee or a receiver appointed on its behalf. There are two separate payment orders of priority depending on whether the Funding 1 security trustee has served an intercompany loan acceleration notice. These orders of priority are described in “**Cashflows**” below.

### **New issuing entity secured creditors**

New issuing entity secured creditors may from time to time enter into deeds of accession in relation to the issuing entity deed of charge upon or immediately prior to an issue of notes.

### **Appointment, powers, responsibilities and liabilities of the issuing entity security trustee**

The issuing entity security trustee was appointed to act as trustee on behalf of the issuing entity secured creditors on the terms and conditions of the issuing entity deed of charge. It holds the benefit of the security created by the issuing entity deed of charge on trust for itself and each of the other issuing entity secured creditors in accordance with the terms and conditions of the issuing entity deed of charge.

The issuing entity security trustee may concur, or direct the Funding 1 security trustee to concur with any person in making any modifications to the transaction documents only (for so long as any notes remain outstanding) if so

directed by the note trustee and (as provided for in the issuing entity deed of charge) with the prior consent of any other relevant issuing entity secured creditors. The note trustee may give such direction, without the consent or sanction of the noteholders provided that:

- the note trustee is of the opinion that such modification will not be materially prejudicial to the interests of the holders of any series or class of notes; or
- in the sole opinion of the note trustee, such modification is necessary to correct a manifest error or is of a formal, minor or technical nature or is to comply with the mandatory provisions of law.

The note trustee is entitled to assume that such modification will not be materially prejudicial to the interests of the noteholders if each of the rating agencies has confirmed that the then current rating by it of the notes would not be adversely affected by such modification.

In addition, the issuing entity security trustee will give its consent to any modifications to any transaction document that are requested by Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf), provided that Funding 1 (or the cash manager on its behalf) or the issuing entity (or the issuing entity cash manager on its behalf) certifies to the issuing entity security trustee in writing that such modifications are required in order to accommodate (among other things):

- (i) notes to be issued by the issuing entity and/or loan tranches to be made available by the issuing entity to Funding 1 under the intercompany loan agreement (including new further classes of notes and their corresponding loan tranches);
- (ii) the entry by Funding 1 into a new intercompany loan agreement and/or the issue of new notes by Funding 1 issuing entities or Funding 1 directly;
- (iii) the accession of Funding 1 secured creditors and/or issuing entity secured creditors;
- (iv) the assignment of new types of loans or their related security to the mortgages trustee (including the assignment of loans and their related security originated under brands other than Birmingham Midshires and/or by entities in the HBOS group other than the seller);
- (v) the inclusion of a new funding beneficiary as a beneficiary of the mortgages trust;
- (vi) the acquisition by Funding 1, a new funding beneficiary or the mortgages trustee of an interest in any other securitisation involving products originated by the HBOS group;
- (vii) changes to be made to the Funding 1 reserve required amount, the Funding 1 liquidity reserve fund required amount and/or the manner in which any Funding 1 reserve fund is funded;
- (viii) different Funding 1 interest payment dates, interest periods and/or bases for the calculation of interest in respect of any loan tranches then outstanding under the intercompany loan agreement; and/or
- (ix) changes to be made to the definitions of asset trigger event and non-asset trigger event,

and provided further that:

- in respect of the matters listed in paragraph (i) to (v), the conditions precedent to notes being issued by the issuing entity and/or loan tranches being made available to Funding 1, new notes being issued by Funding 1 issuing entities or by Funding 1 directly and/or new loans being made available to Funding 1, the accession of new Funding 1 secured creditors and/or new issuing entity secured creditors, the assignment of new types of loans or mortgages to the mortgages trustee and the inclusion of a new funding beneficiary as a beneficiary of the mortgages trust have been satisfied; and
- in respect of the matters listed in paragraphs (i) to (ix), the issuing entity security trustee has received written confirmation from each of the rating agencies then rating the notes that the relevant modifications will not result in a reduction, withdrawal or (in the case of S&P and Moody's) qualification of the then current ratings of the notes.

#### **Issuing entity security trustee's fees and expenses**



The issuing entity shall pay to the issuing entity security trustee a fee (inclusive of VAT, if any) payable on dates and in the amount agreed from time to time by the issuing entity security trustee and the issuing entity. The issuing entity will also pay, on written request, all costs, charges and expenses (including any amount in respect of irrecoverable VAT chargeable thereon) properly incurred by the issuing entity security trustee in relation to:

- the negotiation, preparation and execution of and the exercise of its powers and the performance of its duties under the transaction documents; or
- any action taken or contemplated by the issuing entity security trustee for enforcing the transaction documents.

The issuing entity security trustee is entitled to additional fees if it undertakes duties of an exceptional nature or otherwise outside the scope of the normal duties of the issuing entity security trustee, as further set out in the issuing entity deed of charge.

Furthermore, the issuing entity agrees to indemnify the issuing entity security trustee against all liabilities to which it may be or become subject or which may be incurred by it in the proper execution or purported execution of any of its trusts, powers, authorities and discretions under the transaction documents or its functions pursuant to its appointment as issuing entity security trustee.

The issuing entity is not responsible under the issuing entity deed of charge for any liabilities, losses, damages, costs or expenses resulting from the fraud, wilful default or gross negligence on the part of the issuing entity security trustee.

### **Retirement and removal**

Subject to the appointment of a trust corporation as a successor issuing entity security trustee, the issuing entity security trustee may retire after giving three months' notice in writing to the issuing entity. In order to be eligible to act as issuing entity security trustee, such successor issuing entity security trustee must meet the applicable eligibility requirements under the issuing entity deed of charge, including the requirement that it satisfies the minimum capitalisation and other applicable conditions in regards to trustee eligibility set forth in the Investment Company Act. If within two months of having given notice of its intention to retire, the issuing entity has failed to appoint a replacement issuing entity security trustee, the issuing entity security trustee will be entitled to appoint its own successor trustee being a trust corporation.

The noteholders may, by extraordinary resolution of each class thereof, instruct the note trustee to remove the issuing entity security trustee at any time.

In addition, the issuing entity security trustee may, subject to the conditions specified in the issuing entity deed of charge, appoint a co-trustee to act jointly with it.

### **Additional provisions of the issuing entity deed of charge**

The issuing entity deed of charge contains a range of provisions regulating the scope of the issuing entity security trustee's duties and liability. These include the following:

- the issuing entity security trustee is not responsible for the execution, delivery, legality, validity, adequacy, admissibility in evidence or enforceability of the issuing entity deed of charge or any other transaction document or the title, ownership, value, sufficiency, enforceability or existence of any property charged by the issuing entity (or the security relating thereto);
- the issuing entity security trustee will not, and will not be bound, to exercise its powers under the issuing entity deed of charge without (for so long as the notes remain outstanding) being directed or requested to do so by the note trustee (and then only to the extent that it is indemnified and/or secured to its satisfaction);
- the issuing entity security trustee may rely (without investigation or further inquiry) on a certificate or confirmation of the agent bank, any paying agent, any of the rating agencies or any reference bank and shall not be bound in any such case to call for further evidence or be responsible for any loss, liability, costs, damages, expenses or inconveniences that may be occasioned by its failing so to do or the exercise or non-exercise by the issuing entity security trustee of any of its powers, duties and discretions under the transaction documents;

- the issuing entity security trustee is not bound to take steps to ascertain whether a note event of default has occurred and, until it shall have actual written notice to the contrary, shall be entitled to assume that no note event of default has occurred and that the issuing entity is observing and performing all its obligations under the issuing entity deed of charge and the other transaction documents;
- each issuing entity secured creditor must make its own independent appraisal of and investigations into the financial condition, creditworthiness, condition, affairs, status and nature of the issuing entity and the issuing entity security trustee shall not at any time have any responsibility for the same and no issuing entity secured creditor shall rely on the issuing entity security trustee in respect thereof; and
- the issuing entity security trustee and its directors, officers, holdings companies and associated companies may enter into any contract, transaction or arrangement with the issuing entity or any of the other parties to the transaction documents as if it were not the issuing entity security trustee and shall be entitled to exercise and enforce its rights, comply with its obligations and perform its duties under any such contract, transaction or arrangement without regard to the interests of the issuing entity secured creditors.

The issuing entity security trustee makes no statement or representation in this base prospectus, has not authorised or caused the issue of any part of it and expressly disclaims and takes no responsibility for any part of it. The issuing entity security trustee does not guarantee the success of the notes or the payment of principal or interest on the notes.

#### **Governing law**

The issuing entity deed of charge is governed by English law, provided that any terms that are particular to Scots law shall be construed in accordance with the laws of Scotland.

## Cashflows

### Definition of Funding 1 available revenue receipts

**Funding 1 available revenue receipts** for each Funding 1 interest payment date will be calculated by the cash manager on the day falling four business days prior to such Funding 1 interest payment date and will be an amount equal to the sum of:

- all mortgages trust available revenue receipts distributed or to be distributed to Funding 1 during the then current interest period;
- any amounts paid or to be paid by the seller to Funding 1 during the then current interest period in consideration of the seller acquiring a further interest in the trust property (see “**The mortgages trust – Acquisition by seller of an interest relating to capitalised interest**” above);
- other net income of Funding 1, including all amounts of interest received on the Funding 1 GIC account, the Funding 1 transaction account and/or authorised investments and amounts received by Funding 1 under the Funding 1 swap agreement (other than any early termination amount received by Funding 1 under the Funding 1 swap agreement to be applied to pay the premium payable to a replacement Funding 1 swap provider), in each case received or to be received during the then current interest period;
- the amounts then standing to the credit of the Funding 1 general reserve ledger, subject to any limits or conditions on the purposes for which the Funding 1 general reserve fund may be utilised;
- if a liquidity reserve fund rating event has occurred and is continuing and there are no amounts standing to the credit of the Funding 1 general reserve ledger, the amounts then standing to the credit of the Funding 1 liquidity reserve ledger and available to be drawn, to the extent necessary to pay the items in paragraphs (A) to (E), (G), (I), (K) and (M) in the Funding 1 pre-enforcement revenue priority of payments;
- if a liquidity reserve fund rating event has occurred but is no longer continuing due to an increase in the seller’s rating since the preceding Funding 1 interest payment date, all amounts standing to the credit of the liquidity reserve ledger;
- any amounts standing to the credit of the Funding 1 liquidity reserve ledger in excess of the Funding 1 liquidity reserve fund required amount as a result of a reduction in the Funding 1 liquidity reserve fund required amount; and
- any amounts standing to the credit of the start-up loan revenue contribution ledger (which, for the avoidance of doubt, shall only apply on the Funding 1 interest payment date immediately following a closing date on which a start-up loan tranche is advanced by the issuing entity to Funding 1 in whole or in part for such purpose).

Funding 1 available revenue receipts do not include:

- any payment made by the seller to Funding 1 on the applicable Funding 1 interest payment date as described in “**The mortgages trust – Payment by the seller of the amount outstanding under a loan tranche**” above;
- any proceeds of a loan tranche received by Funding 1 during the then current interest period as described in “**The intercompany loan agreement – The facility**” above.

Four business days prior to each Funding 1 interest payment date, the cash manager will calculate whether Funding 1 available revenue receipts (as calculated above) will be sufficient to pay items (A) to (E), (G), (I), (K) and (M) of the Funding 1 pre-enforcement revenue priority of payments.

If the cash manager determines that there is an insufficiency, then Funding 1 shall pay or provide for that insufficiency by (a) first, applying amounts then standing to the credit of the Funding 1 principal ledger (if any) and (b) second, applying any amounts standing to the credit of the Funding 1 cash accumulation ledger after first applying the amounts standing to the credit of the Funding 1 principal ledger (if any) from such ledger, and the cash manager shall make a corresponding entry in the relevant Funding 1 principal deficiency sub-ledger, as described in “**Credit structure – Funding 1 principal deficiency ledger**” below. Funding 1 principal receipts thus applied may not be used to pay interest on any rated loan tranche if and to the extent that would result in a deficiency being recorded, or an existing deficiency being increased, on a principal deficiency sub-ledger relating to a rated loan tranche with a higher rating designation.

If the cash manager determines that there is an excess of Funding 1 available revenue receipts over the amount required to pay the specified items in the Funding 1 pre-enforcement revenue priority of payments, then Funding 1 shall apply such excess to extinguish any balance on the Funding 1 principal deficiency ledger, as described in “**Credit structure – Funding 1 principal deficiency ledger**” below.

#### **Distribution of Funding 1 available revenue receipts before intercompany loan acceleration**

This section sets out the priority of payments of Funding 1 available revenue receipts as at the programme date. If Funding 1 enters into new intercompany loan agreements or if loan tranches with lower ratings designations are advanced to Funding 1 pursuant to the intercompany loan agreement, then this priority will change. See “**Risk Factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may adversely affect your interests**”, “**Security for Funding 1’s obligations**” and “**Security for the issuing entity’s obligations**”.

Except for amounts due to third parties by Funding 1 under item (B) below and amounts due to the account bank under item (C) below and amounts in (B) below corresponding to amounts due to third parties and the issuing entity account bank by the issuing entity, which will be paid when due, on each Funding 1 interest payment date prior to the service of an intercompany loan acceleration notice on Funding 1, the cash manager will apply (i) the Funding 1 available revenue receipts for such date and (ii) if Funding 1 available revenue receipts for such date are insufficient to pay items (A) to (E), (G), (I), (K) and (M) below, amounts standing to the credit of the Funding 1 principal ledger and the Funding 1 cash accumulation ledger (in the manner described above), in the following order of priority (the **Funding 1 pre-enforcement revenue priority of payments**):

- (A) without priority among them but in proportion to the respective amounts due, to pay:
- all fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable in the immediately following interest period to the Funding 1 security trustee under the Funding 1 deed of charge (together with interest and any amount in respect of VAT on those amounts); and
  - amounts due to the issuing entity, by way of payment of the issuing entity fee, in respect of the issuing entity fee payable pursuant to the intercompany loan agreement corresponding to the issuing entity’s obligations specified in item (A) of the issuing entity pre-enforcement revenue priority of payments or, as the case may be, in item (A) of the issuing entity post-enforcement priority of payments or provide for any such amounts due or to become due in the immediately following interest period to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, as described in “– **Distribution of issuing entity revenue receipts before note acceleration**” below and “– **Distribution of issuing entity principal receipts and issuing entity revenue receipts after note acceleration and intercompany loan acceleration**” below;
- (B) without priority among them but in proportion to the respective amounts due, to pay:
- amounts due to the issuing entity in respect of the issuing entity fee payable pursuant to the intercompany loan agreement corresponding to the issuing entity’s obligations specified in items (B) to (D) inclusive of the issuing entity pre-enforcement revenue priority of payments or, as the case may be, in items (B) and (C) of the issuing entity post-enforcement priority of payments or provide for any such amounts due or to become due in the immediately following interest period to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, as described in “–

**Distribution of issuing entity revenue receipts before note acceleration” below and “–  
Distribution of issuing entity principal receipts and issuing entity revenue receipts  
after note acceleration and intercompany loan acceleration” below; and**

- any third party creditors of Funding 1 (other than those referred to later in this priority of payments), which amounts have been incurred without breach by Funding 1 of the transaction documents to which it is a party and to provide for any of these amounts expected to become due and payable in the immediately following interest period by Funding 1 and to pay or discharge any liability of Funding 1 for corporation tax on any chargeable income or gain of Funding 1;
- (C) without priority among them but in proportion to the respective amounts due, towards payment of amounts, if any, due and payable by Funding 1 to:
- the cash manager, together with any amount in respect of VAT on those amounts, and to provide for any amounts to become due to the cash manager in the immediately succeeding interest period, under the terms of the cash management agreement;
  - the corporate services provider, together with any amount in respect of VAT on those amounts, and to provide for any amounts to become due to the corporate services provider in the immediately succeeding interest period, under the terms of the corporate services agreement; and
  - the account bank, together with any amount in respect of VAT on those amounts, and to provide for any amounts to become due to the account bank in the immediately succeeding interest period, under the terms of the bank account agreement;
- (D) towards payment of all amounts (if any) due and payable to the Funding 1 swap provider under the Funding 1 swap agreement (including termination payments, but excluding any Funding 1 swap excluded termination amount);
- (E) without priority among them, but in proportion to the respective amounts due, towards payment of interest due and payable on the AAA loan tranches and towards payment of any amounts due to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, corresponding to the issuing entity’s obligations (if any) to make a termination payment to an issuing entity swap provider (but excluding any issuing entity swap excluded termination amount) under an issuing entity swap agreement in respect of the class A notes;
- (F) towards a credit to the AAA principal deficiency sub-ledger in an amount sufficient to eliminate any debit on that ledger;
- (G) without priority among them, but in proportion to the respective amounts due, towards payment of interest due and payable on the AA loan tranches and towards payment of any amounts due to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, corresponding to the issuing entity’s obligations (if any) to make a termination payment to an issuing entity swap provider (but excluding any issuing entity swap excluded termination amount) under an issuing entity swap agreement in respect of the class B notes;
- (H) towards a credit to the AA principal deficiency sub-ledger in an amount sufficient to eliminate any debit on that ledger;
- (I) without priority among them, but in proportion to the respective amounts due, towards payment of interest due and payable on the A loan tranches and towards payment of any amounts due to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, corresponding to the issuing entity’s obligations (if any) to make a termination payment to an issuing entity swap provider (but excluding any issuing entity swap excluded termination amount) under an issuing entity swap agreement in respect of the class M notes;
- (J) towards a credit to the A principal deficiency sub-ledger in an amount sufficient to eliminate any debit on that ledger;
- (K) without priority among them, but in proportion to the respective amounts due, towards payment of interest due and payable on the BBB loan tranches and towards payment of any amounts due to the

issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, corresponding to the issuing entity's obligations (if any) to make a termination payment to an issuing entity swap provider (but excluding any issuing entity swap excluded termination amount) under an issuing entity swap agreement in respect of the class C notes;

- (L) towards a credit to the BBB principal deficiency sub-ledger in an amount sufficient to eliminate any debit on that ledger;
- (M) without priority among them, but in proportion to the respective amounts due, towards payment of interest due and payable on the BB loan tranches and towards payment of any amounts due to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, corresponding to the issuing entity's obligations (if any) to make a termination payment to an issuing entity swap provider (but excluding any issuing entity swap excluded termination amount) under an issuing entity swap agreement in respect of the class D notes;
- (N) towards a credit to the BB principal deficiency sub-ledger in an amount sufficient to eliminate any debit on that ledger;
- (O) towards a credit to the Funding 1 general reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 reserve required amount, taking into account any net replenishment of the Funding 1 general reserve fund on that Funding 1 interest payment date from Funding 1 available principal receipts (see item (A) of the relevant Funding 1 pre-enforcement principal priority of payments);
- (P) if a liquidity reserve fund rating event has occurred and is continuing, towards a credit to the Funding 1 liquidity reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 liquidity reserve fund required amount, taking into account any net replenishment of the Funding 1 liquidity reserve fund on that Funding 1 interest payment date from Funding 1 available principal receipts (see item (B) of the relevant Funding 1 pre-enforcement principal priority of payments);
- (Q) without priority among them, but in proportion to the respective amounts due, towards payment of interest due and payable on the subordinated loan tranches;
- (R) towards a credit to the subordinated loan principal deficiency sub-ledger in an amount sufficient to eliminate any debit on that ledger;
- (S) without priority among them but in proportion to the respective amounts due, to pay (without double counting):
  - after the occurrence of a Funding 1 swap provider default or a Funding 1 swap provider downgrade termination event, any termination amount due and payable by Funding 1 under the Funding 1 swap agreement;
  - to the issuing entity, by way of issuing entity fee payable pursuant to the intercompany loan agreement, corresponding to the issuing entity's obligations (if any) to pay any issuing entity swap excluded termination amount; and
  - any other amounts due to the issuing entity under the intercompany loan agreement and not otherwise provided for in this priority of payments;
- (T) towards payment to Funding 1 of a retained profit of £5,000 per annum (or such lesser amount as the directors of Funding 1 may determine);
- (U) without priority among them but in proportion to the respective amounts due, towards payment of amounts due and payable to the issuing entity in respect of the start-up loan tranches; and
- (V) towards payment to the seller of any deferred consideration due to the seller pursuant to the terms of the mortgage sale agreement (the **deferred consideration**).

## Definition of issuing entity revenue receipts

**Issuing entity revenue receipts** will be calculated by the issuing entity cash manager four business days prior to each quarterly interest payment date and will be an amount equal to the sum of:

- interest to be paid by Funding 1 on the corresponding Funding 1 interest payment date in respect of the loan tranches under the intercompany loan agreement;
- principal to be repaid by Funding 1 on the corresponding Funding 1 interest payment date in respect of the start-up loan tranches under the intercompany loan agreement;
- issuing entity fees to be paid to the issuing entity by Funding 1 on the relevant Funding 1 interest payment date under the terms of the intercompany loan agreement;
- interest payable on the issuing entity bank accounts and any authorised investments which will be received on or before the relevant quarterly interest payment date;
- other net income of the issuing entity including amounts received or to be received under the issuing entity swap agreements on or before the relevant quarterly interest payment date (including any amount received by the issuing entity in consideration of entering into a replacement issuing entity swap agreement, but excluding (i) the return or transfer of any excess swap collateral as set out under any issuing entity swap agreement and (ii) in respect of each issuing entity swap provider, prior to the designation of an early termination date under the relevant issuing entity swap agreement and the resulting application of the collateral by way of netting or set-off, an amount equal to the value of all collateral (other than excess swap collateral) provided by such issuing entity swap provider to the issuing entity pursuant to the relevant issuing entity swap agreement (and any interest or distributions in respect thereof)); and
- any additional amount the issuing entity receives from any taxing authority on account of amounts paid to that taxing authority for and on account of tax by an issuing entity swap provider under an issuing entity swap agreement.

On each Funding 1 interest payment date, all Funding 1 available revenue receipts received by or to the order of the issuing entity in respect of interest paid on a loan tranche will be credited to a sub-ledger (in respect of the related series and class of notes) on the **issuing entity revenue ledger** (being, the ledger on which the issuing entity cash manager records issuing entity revenue receipts received and paid out of the issuing entity).

On each Funding 1 interest payment date, all Funding 1 available revenue receipts received by or to the order of the issuing entity in respect of principal repaid on a start-up loan tranche will be credited to a sub-ledger (in respect of the related issuing entity start-up loan) on the issuing entity revenue ledger.

## Distribution of issuing entity revenue receipts before note acceleration

In addition, the issuing entity deed of charge sets out the priority of distribution by the issuing entity cash manager, prior to the service of a note acceleration notice on the issuing entity, of amounts received by the issuing entity on each quarterly interest payment date. The order of priority will be as described in this section.

Except for amounts due to third parties under item (C) below, amounts due to the issuing entity account bank under item (D) below, amounts due to the issuing entity swap provider(s) on the first payment date under the issuing entity swap agreement(s) in respect of any money market notes issued on the programme date and (to the extent that amounts, excluding principal, are received from the issuing entity swap provider(s) under the issuing entity swap agreement(s) in respect of the related series and class of money market notes) to the noteholders of any corresponding money market notes under items (E), (F), (G), (H) and (I), amounts payable to any replacement swap provider using any termination payment received by the issuing entity in respect of the corresponding issuing entity swap agreement or amounts payable to an issuing entity swap provider (other than amounts pursuant to item (K) below) using any premium recovered from any replacement swap provider, which will be paid when due, on each quarterly interest payment date, the issuing entity cash manager will apply issuing entity revenue receipts in the following order of priority (the **issuing entity pre-enforcement revenue priority of payments**):

- (A) without priority among them, but in proportion to the respective amounts due, to pay:

- all fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable in the immediately following interest period to the issuing entity security trustee under the issuing entity deed of charge (together with interest and any amount in respect of VAT thereon); and
  - all fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable in the immediately following interest period to the note trustee under the note trust deed (together with interest and any amount in respect of VAT thereon);
- (B) without priority among them, but in proportion to the respective amounts due, to pay all fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable during the immediately following interest period to the agent bank, the paying agents, the registrar, the exchange agent and the transfer agent under the paying agent and agent bank agreement (together with interest and any amount in respect of VAT on those amounts);
- (C) to pay amounts due and payable to any third party creditors of the issuing entity (other than those referred to elsewhere in this priority of payments), which amounts have been incurred without breach by the issuing entity of the transaction documents to which it is a party and for which payment has not been provided for elsewhere and to provide for any of those amounts expected to become due and payable during the following interest period by the issuing entity and to pay or discharge any liability of the issuing entity for corporation tax on any chargeable income or gain of the issuing entity;
- (D) without priority among them, but in proportion to the respective amounts due, to pay amounts due and payable by the issuing entity to:
- the issuing entity cash manager, together with any amount in respect of VAT on those amounts, and to provide for any amounts to become due to the issuing entity cash manager in the immediately succeeding interest period, under the issuing entity cash management agreement;
  - the corporate services provider, together with VAT on those amounts, and to provide for any amounts to become due to the corporate service provider in the immediately succeeding interest period, under the corporate services agreement; and
  - the issuing entity account bank, together with VAT on those amounts, and to provide for any amounts to become due to the issuing entity account bank in the immediately succeeding interest period, under the issuing entity bank account agreement;
- (E) from amounts (excluding principal) received by the issuing entity from Funding 1 in respect of each AAA loan tranche and by way of issuing entity fee in respect of any termination payment as referred to in (i) below (and, in respect of (ii) below, the amounts (if any), excluding principal, received from the issuing entity swap provider(s) under the issuing entity swap agreement(s) in respect of the related series and class of notes):
- (i) to pay the amounts due and payable on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class A notes (including any termination payment, but excluding any issuing entity swap excluded termination amount) in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay interest due and payable (if any) on such quarterly interest payment date on the related series and class of class A notes on such interest payment date;
- (F) from amounts (excluding principal) received by the issuing entity from Funding 1 in respect of each AA loan tranche and by way of issuing entity fee in respect of any termination payment as referred to in (i) below (and, in respect of (ii) below, the amounts (if any), excluding principal, received from the issuing entity swap provider(s) under the issuing entity swap agreement(s) in respect of the related series and class of notes):
- (i) to pay the amounts due and payable on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class



- of class B notes (including any termination payment, but excluding any issuing entity swap excluded termination amount) in accordance with the terms of the relevant issuing entity swap agreement(s); and
- (ii) to pay interest due and payable (if any) on such quarterly interest payment date on the related series and class of class B notes on such interest payment date;
- (G) from amounts (excluding principal) received by the issuing entity from Funding 1 in respect of each A loan tranche and by way of issuing entity fee in respect of any termination payment as referred to in (i) below (and, in respect of (ii) below, the amounts (if any), excluding principal, received from the issuing entity swap provider(s) under the issuing entity swap agreement(s) in respect of the related series and class of notes):
- (i) to pay the amounts due and payable on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class M notes (including any termination payment, but excluding any issuing entity swap excluded termination amount) in accordance with the terms of the relevant issuing entity swap agreement(s); and
- (ii) to pay interest due and payable (if any) on such quarterly interest payment date on the related series and class of class M notes on such interest payment date;
- (H) from amounts (excluding principal) received by the issuing entity from Funding 1 in respect of each BBB loan tranche and by way of issuing entity fee in respect of any termination payment as referred to in (i) below (and, in respect of (ii) below, the amounts (if any), excluding principal, received from the issuing entity swap provider(s) under the issuing entity swap agreement(s) in respect of the related series and class of notes):
- (i) to pay the amounts due and payable on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class C notes (including any termination payment, but excluding any issuing entity swap excluded termination amount) in accordance with the terms of the relevant issuing entity swap agreement(s); and
- (ii) to pay interest due and payable (if any) on such quarterly interest payment date on the related series and class of class C notes on such interest payment date;
- (I) from amounts (excluding principal) received by the issuing entity from Funding 1 in respect of each BB loan tranche and by way of issuing entity fee in respect of any termination payment as referred to in (i) below (and, in respect of (ii) below, the amounts (if any), excluding principal, received from the issuing entity swap provider(s) under the issuing entity swap agreement(s) in respect of the related series and class of notes):
- (i) to pay the amounts due and payable on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class D notes (including any termination payment, but excluding any issuing entity swap excluded termination amount) in accordance with the terms of the relevant issuing entity swap agreement(s); and
- (ii) to pay interest due and payable (if any) on such quarterly interest payment date on the related series and class of class D notes on such interest payment date;
- (J) from amounts (excluding principal) received by the issuing entity from Funding 1 in respect of each subordinated loan tranche, to pay interest due and payable (if any) on the related issuing entity subordinated loan on such interest payment date;
- (K) without priority among them but in proportion to the respective amounts due, to pay any issuing entity swap excluded termination payment due to an issuing entity swap provider;
- (L) to pay to the issuing entity a retained profit of £5,000 per annum (or such lesser amount as the directors of the issuing entity may determine); and
- (M) from amounts received by the issuing entity from Funding 1 in respect of each start-up loan tranche, to pay all amounts due and payable (if any) on the related issuing entity start-up loan on such interest payment date.

Prior to the service of a note acceleration notice on the issuing entity, on each quarterly interest payment date, the amounts standing to the credit of any sub-ledger of the issuing entity revenue ledger (in respect of a series and class of notes, an issuing entity subordinated loan or an issuing entity start-up loan) may only be applied by the issuing entity cash manager to pay interest and other amounts due in respect of such series and class of notes (including under any corresponding issuing entity swap), such issuing entity subordinated loan or, as applicable, such issuing entity start-up loan under the issuing entity pre-enforcement revenue priority of payments, provided that (a) to the extent that, on any quarterly interest payment date, amounts standing to the credit of the issuing entity expense ledger and the issuing entity revenue ledger (excluding amounts standing to the credit of the sub-ledgers for each series and class of notes, each issuing entity subordinated loan and each issuing entity start-up loan) are insufficient to pay items (A) to (D) of the issuing entity pre-enforcement revenue priority of payments, then the issuing entity cash manager will (i) first, apply amounts standing to the credit of the issuing entity expense ledger to meet such shortfall and (ii) second, in no order of priority among them but in proportion to the amount required, apply amounts standing to the credit of the sub-ledgers of the issuing entity revenue ledger in respect of the issuing entity start-up loans on such date to meet such shortfall (until the balance of such sub-ledgers is zero), then amounts standing to the credit of the sub-ledgers of the issuing entity revenue ledger in respect of the issuing entity subordinated loans on such date to meet such shortfall (until the balance of such sub-ledgers is zero), then amounts standing to the credit of the sub-ledgers of the issuing entity revenue in respect of the class D notes of each series on such date to meet such shortfall (until the balance of such sub-ledgers is zero), then amounts standing to the credit of the sub-ledgers of the issuing entity revenue ledger in respect of the class C notes of each series (until the balance of such sub-ledgers is zero), then amounts standing to the credit of the sub-ledgers of the issuing entity revenue ledger in respect of the class M notes of each series (until the balance of such sub-ledgers is zero), then amounts standing to the credit of the sub-ledgers of the issuing entity revenue ledger in respect of the class B notes of each series (until the balance of such sub-ledgers is zero) and then amounts standing to the credit of the sub-ledgers of the issuing entity revenue ledger in respect of the class A notes (until the balance of such sub-ledgers is zero) and (b) any amount remaining on any sub-ledger after payment in full of the corresponding series and class of notes, issuing entity subordinated loan or issuing entity start-up loan may be transferred to the issuing entity expense ledger.

Prior to the service of a note acceleration notice on the issuing entity, on each quarterly interest payment date, the amounts standing to the credit of any sub-ledger of the issuing entity revenue ledger in respect of amounts (excluding principal) on an issuing entity start-up loan may only be applied by the issuing entity cash manager to pay interest, capitalised interest and other amounts due (except for principal) in respect of such issuing entity start-up loan and the amounts standing to the credit of any sub-ledger of the issuing entity revenue ledger in respect of principal of an issuing entity start-up loan may only be applied by the issuing entity cash manager to repay principal due in respect of such issuing entity start-up loan.

#### **Distribution of issuing entity revenue receipts after note acceleration but before intercompany loan acceleration**

Following the service of a note acceleration notice on the issuing entity, but prior to the service of an intercompany loan acceleration notice on Funding 1, the issuing entity security trustee will apply issuing entity revenue receipts in the same order of priority as set out in the issuing entity pre-enforcement revenue priority of payments, except that:

- in addition to the amounts due to the issuing entity security trustee under item (A) of the issuing entity pre-enforcement revenue priority of payments, issuing entity revenue receipts will be applied to pay amounts due to any receiver appointed by the issuing entity security trustee together with interest and any amount in respect of VAT on those amounts and to provide for any amounts due or to become due to the receiver during the following interest period (which may be paid when due); and
- the issuing entity security trustee will not be required to pay amounts due to any entity which is not an issuing entity secured creditor.

#### **Distribution of Funding 1 available principal receipts**

##### *Payment of principal receipts to Funding 1 by the mortgages trustee*

On each distribution date, mortgages trust available principal receipts will be paid to Funding 1 in the manner and to the extent provided by the mortgages trust principal priority of payments (see “**The mortgages trust – Mortgages trust calculation of principal receipts**” above) and shall be deposited in the Funding 1 GIC account and credited by the cash manager to the **Funding 1 principal ledger** (being a ledger maintained by the cash

manager for Funding 1 to record the amount of principal receipts received by Funding 1 from the mortgages trustee).

*Definition of Funding 1 available principal receipts*

**Funding 1 available principal receipts** will be calculated by the cash manager on the day falling four business days prior to each Funding 1 interest payment date and will be an amount equal to the sum of:

- all mortgages trust available principal receipts distributed or to be distributed to Funding 1 during the then current interest period;
- all other Funding 1 principal receipts standing to the credit of the Funding 1 cash accumulation ledger which are to be applied on the next Funding 1 interest payment date to repay a bullet loan tranche and/or, subject to Rule (1) below, a scheduled amortisation instalment in respect of a scheduled amortisation loan tranche or to make a payment under items (A) or (B) of the Funding 1 pre-enforcement principal priority of payments and, if such Funding 1 interest payment date occurs on or after a trigger event, the remainder of such receipts standing to the credit of the Funding 1 cash accumulation ledger;
- the amount, if any, to be credited to the Funding 1 principal deficiency ledger pursuant to items (F), (H), (J), (L) and (N) of the Funding 1 pre-enforcement revenue priority of payments on the relevant Funding 1 interest payment date;
- in so far as available for and needed to make a Funding 1 reserve principal payment (see “**Credit structure – Funding 1 general reserve fund**” below), the amount that would then be standing to the credit of the Funding 1 general reserve ledger, less any amounts applied or to be applied on the relevant Funding 1 interest payment date in payment of interest and other revenue expenses as set out in items (A) to (N) (inclusive) of the Funding 1 pre-enforcement revenue priority of payments, plus any amounts which will be credited to the Funding 1 general reserve ledger under item (A) of the relevant Funding 1 pre-enforcement principal priority of payments on the next Funding 1 interest payment date (i.e. occurring at the end of such period of four business days);
- in so far as available for and needed to make a Funding 1 reserve principal payment (see “**Credit structure – Funding 1 liquidity reserve fund**” below), the amount that would then be standing to the credit of the Funding 1 liquidity reserve ledger, less any amounts applied or to be applied on the relevant Funding 1 interest payment date in payment of interest and other revenue expenses as set out in items (A) to (E) (inclusive) and (G), (I) (K) and (M) of the Funding 1 pre-enforcement revenue priority of payments, plus any amounts which will be credited to the liquidity reserve ledger under item (B) of the relevant Funding 1 pre-enforcement principal priority of payments on the next Funding 1 interest payment date (i.e. occurring at the end of such period of four business days); and
- any other amount standing to the credit of the Funding 1 principal ledger (without double-counting the amounts described above);

less

- amounts to be applied on the relevant Funding 1 interest payment date to pay items (A) to (E) (inclusive) and (G), (I), (K) and (M) of the Funding 1 pre-enforcement revenue priority of payments.

*Due and payable dates of loan tranches*

The repayment of any loan tranche prior to the occurrence of a trigger event, service of a note acceleration notice or service of an intercompany loan acceleration notice will be made in accordance with the terms of the intercompany loan agreement. The applicable loan tranche supplement and (if applicable) final terms will specify the Funding 1 interest payment dates of the loan tranches related to the series and classes of notes issued and/or the issuing entity subordinated loan and/or the issuing entity start-up loan made to the issuing entity.

The following sections set out various priorities of payments for Funding 1 available principal receipts under the following circumstances, and are collectively referred to as the “**Funding 1 pre-enforcement principal priority of payments**”:

- repayment of loan tranches (other than start-up loan tranches) before a trigger event and before intercompany loan acceleration or acceleration of all notes;
- repayment of loan tranches (other than start-up loan tranches) after a non-asset trigger event but before intercompany loan acceleration or acceleration of all notes;
- repayment of loan tranches (other than start-up loan tranches) after an asset trigger event but before intercompany loan acceleration or acceleration of all notes; and
- repayment of loan tranches (other than start-up loan tranches) after acceleration of all notes but before intercompany loan acceleration.

*Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes*

On each Funding 1 interest payment date prior to the occurrence of a trigger event or the service on Funding 1 of an intercompany loan acceleration notice or the service on the issuing entity of a note acceleration notice, the cash manager shall apply Funding 1 available principal receipts in the following order of priority:

- (A) to the extent only that monies have been drawn from the Funding 1 general reserve fund to make Funding 1 reserve principal payments, towards a credit to the Funding 1 general reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 reserve required amount;
- (B) if a liquidity reserve fund rating event has occurred and is continuing, (i) to the extent only that monies have been drawn from the Funding 1 liquidity reserve fund in order to make Funding 1 reserve principal payments or (ii) to the extent that the Funding 1 liquidity reserve fund has not been fully funded, towards a credit to the Funding 1 liquidity reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 liquidity reserve fund required amount;
- (C) in order of their final repayment dates, beginning with the earliest such date (and, if two or more AAA loan tranches have the same final repayment date, in proportion to the respective amounts due) to repay the principal amounts due (if any) on such Funding 1 interest payment date on the AAA loan tranches, in each case subject to Rules (1) and (2) below;
- (D) in no order of priority among them, but in proportion to the respective amounts due, to repay the principal amounts due (if any) on such Funding 1 interest payment date on the AA loan tranches, in each case subject to Rules (1) and (2) below;
- (E) in no order of priority among them, but in proportion to the respective amounts due, to repay the principal amounts due (if any) on such Funding 1 interest payment date on the A loan tranches, in each case subject to Rules (1) and (2) below;
- (F) in no order of priority among them, but in proportion to the respective amounts due, to repay the principal amounts due (if any) on such Funding 1 interest payment date on the BBB loan tranches, in each case subject to Rules (1) and (2) below;
- (G) in no order of priority among them, but in proportion to the respective amounts due, to repay the principal amounts due (if any) on such Funding 1 interest payment date on the BB tranches, in each case subject to Rules (1) and (2) below;
- (H) towards a credit to the Funding 1 cash accumulation ledger until the balance is equal to Funding 1's cash accumulation liability (as calculated after any payments are made at items (A) to (G) above);
- (I) in no order of priority among them, but in proportion to the respective amounts due, to repay the principal amounts due (if any) on such Funding 1 interest payment date on the subordinated loan tranches, in each case subject to Rule (1); and
- (J) the remainder to be credited to the Funding 1 principal ledger.

In the applicable circumstances, the following Rules apply in determining the amounts to be paid under items (C) to (G) (inclusive) and (I) of the Funding 1 pre-enforcement principal priority of payments set out above:

*Rule (1) – Repayment deferrals*

(A) If on a Funding 1 interest payment date:

- (1) there is a debit balance on the BB principal deficiency sub-ledger, the BBB principal deficiency sub-ledger, the A principal deficiency sub-ledger or the AA principal deficiency sub-ledger, after application of the Funding 1 available revenue receipts on that Funding 1 interest payment date; or
- (2) the adjusted Funding 1 general reserve fund level is less than the Funding 1 general reserve fund threshold; or
- (3) the aggregate outstanding principal balance of loans in the mortgages trust in respect of which the aggregate amount in arrears is more than three times the monthly payment then due is more than 5 per cent. of the aggregate outstanding principal balance of loans in the mortgages trust,

then, until the relevant circumstance as described in sub-paragraph (1), (2) or (3) above has been cured or otherwise ceases to exist, if:

- (a) any AAA loan tranche (whether or not such AAA loan tranche is then due and payable) remains outstanding after making the payments under item (C) of the above Funding 1 pre-enforcement principal priority of payments, then the AA loan tranches will not be entitled to principal repayments under item (D) of the above Funding 1 pre-enforcement principal priority of payments;
- (b) any AAA loan tranche or any AA loan tranche (whether or not such AAA loan tranche or AA loan tranche is then due and payable) remains outstanding after making the payments under items (C) and/or (D) of the above Funding 1 pre-enforcement principal priority of payments, then the A loan tranches will not be entitled to principal repayments under item (E) of the above Funding 1 pre-enforcement principal priority of payments;
- (c) any AAA loan tranche, any AA loan tranche or any A loan tranche (whether or not such AAA loan tranche, AA loan tranche or A loan tranche is then due and payable) remains outstanding after making the payments under items (C), (D) and/or (E) of the above Funding 1 pre-enforcement principal priority of payments, then the BBB loan tranches will not be entitled to principal repayments under item (F) of the above Funding 1 pre-enforcement principal priority of payments;
- (d) any AAA loan tranche, any AA loan tranche, any A loan tranche or any BBB loan tranche (whether or not such AAA loan tranche, AA loan tranche, A loan tranche or BBB loan tranche is then due and payable) remains outstanding after making the payments under items (C), (D), (E), and/or (F) of the above Funding 1 pre-enforcement principal priority of payments, then the BB loan tranches will not be entitled to principal repayments under item (G) of the above Funding 1 pre-enforcement principal priority of payments; and/or
- (e) any AAA loan tranche, any AA loan tranche, any A loan tranche, any BBB loan tranche or any BB loan tranche (whether or not such AAA loan tranche, AA loan tranche, A loan tranche, BBB loan tranche or BB loan tranche is then due and payable) remains outstanding after making the payments under items (C), (D), (E), (F) and/or (G) of the above Funding 1 pre-enforcement principal priority of payments, then the subordinated loan tranches will not be entitled to principal repayments under item (I) of the above Funding 1 pre-enforcement principal priority of payments.

(B) If on a Funding 1 interest payment date:

- (1) one or more bullet loan tranches are within a cash accumulation period at that time; and
- (2) either:
  - (a) the quarterly CPR is less than 10 per cent.; or
  - (b) both:

- (i) the quarterly CPR is equal to or greater than 10 per cent., but less than 15 per cent., and
- (ii) the annualised CPR is less than 10 per cent.;

then, on or before their step-up dates, the scheduled amortisation loan tranches will be entitled to principal repayments under items (C), (D), (E), (F) and (G) of the above Funding 1 pre-enforcement principal priority of payments only to the extent permitted under the scheduled amortisation repayment restrictions (as defined below).

(C) If on a Funding 1 interest payment date:

- (1) one or more bullet loan tranches and/or scheduled amortisation instalments are within a cash accumulation period at that time;
- (2) the quarterly CPR is less than 15 per cent.; and
- (3) there is a cash accumulation shortfall at that time,

then, on or before their step-up dates, the original pass-through loan tranches will be entitled to principal repayments under items (C), (D), (E), (F) and (G) of the above Funding 1 pre-enforcement principal priority of payments only to the extent permitted under the pass-through repayment restrictions (as defined below).

In this base prospectus:

**annualised CPR** means the result of:

$$1 - ((1 - M)^{12})$$

where

**M** is expressed as a percentage and determined as at the most recent normal calculation date as indicated in the definition of **anticipated cash accumulation period** (see “**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**” above);

**bullet accumulation liability** means, on any Funding 1 interest payment date prior to any payment under item (C) of the above priority of payments, the aggregate of the relevant accumulation amounts at that time of all of the bullet loan tranches which are within a cash accumulation period;

**bullet accumulation shortfall** means, at any time, the amount by which the cash accumulation ledger amount is less than the bullet accumulation liability;

**cash accumulation liability** means, on any Funding 1 interest payment date prior to any payment under item (C) of the above priority of payments, the sum of:

- (1) the bullet accumulation liability at that time; and
- (2) the aggregate of the relevant accumulation amounts at that time of all of the scheduled amortisation instalments which are within a cash accumulation period;

**cash accumulation shortfall** means, at any time, the amount by which the cash accumulation ledger amount is less than the cash accumulation liability;

**cash accumulation ledger amount** means, at any time, the amount standing to the credit of the Funding 1 cash accumulation ledger at that time (immediately prior to any drawing to be applied on that Funding 1 interest payment date and prior to any payment under item (H) of the above Funding 1 pre-enforcement principal priority of payments);

The **pass-through repayment restrictions** require that, at any time on a Funding 1 interest payment date, no amount may be applied in repayment of any original pass-through loan tranche unless:

- (1) the sum of the cash accumulation ledger amount and the amount of Funding 1 available principal receipts after the application of items (A) and (B) and before item (C) of the above Funding 1 pre-enforcement principal priority of payments,

is greater than or equal to:

- (2) the sum of the cash accumulation liability and the aggregate amount of all original pass-through loan tranches which are due and payable as at that time;

The **scheduled amortisation repayment restrictions** require that, at any time on a Funding 1 interest payment date:

- (1) where there is no bullet accumulation shortfall at that time, the total amount withdrawn from the Funding 1 cash accumulation ledger on that Funding 1 interest payment date for repayment of the relevant scheduled amortisation instalments shall not exceed the cash accumulation ledger amount less the bullet accumulation liability at that time; and
- (2) where there is a bullet accumulation shortfall at that time:
- (a) no amount may be withdrawn from the Funding 1 cash accumulation ledger on that Funding 1 interest payment date to be applied in repayment of the relevant scheduled amortisation instalments; and
- (b) no amount may be applied in repayment of the relevant scheduled amortisation instalments unless:
- (i) the sum of the cash accumulation ledger amount and the amount of Funding 1 available principal receipts after the application of items (A) and (B) and before item (C) of the above Funding 1 pre-enforcement principal priority of payments,
- is greater than or equal to:
- (ii) the sum of the bullet accumulation liability and the aggregate amount of scheduled amortisation instalments which are due and payable as at that time; and

**relevant accumulation amount** means the amount of funds to be accumulated over a cash accumulation period in order to repay a bullet loan tranche or a scheduled amortisation instalment on its scheduled repayment date whether or not actually repaid on that scheduled repayment date.

*Rule (2) – Repayment of payable pass-through loan tranches after a step-up date*

Following the occurrence of the step-up date under the rated loan tranches corresponding to a particular issuance of the notes (the **issue A loan tranches**) and provided that the Funding 1 share is greater than zero, the aggregate amount repaid on a Funding 1 interest payment date in relation to rated loan tranches (other than bullet loan tranches or scheduled amortisation instalments) comprising those issue A loan tranches under items (C), (D), (E), (F) and (G) of the above Funding 1 pre-enforcement principal priority of payments shall be limited to an amount calculated as follows:

$$\text{Funding 1 - principal funds x} \frac{\text{Outstanding principal balance of issue A loan tranches}}{\text{Aggregate outstanding principal balance of all rated loan tranches}}$$

where **Funding 1 principal funds** means, in respect of any Funding 1 interest payment date, the sum of:

- (A) the aggregate of the following amount for each calculation period which has ended in the period from the previous Funding 1 interest payment date to the most recent normal calculation date, such amount being the product of:
- (1) the Funding 1 share percentage as calculated at the start of the relevant calculation period; and
- (2) the aggregate amount of principal receipts received by the mortgages trustee in the relevant calculation period;
- (B) the amount credited to the Funding 1 principal deficiency ledger on the relevant Funding 1 interest payment date; and
- (C) the amount, if any, credited to the Funding 1 principal ledger pursuant to item (A) of the Funding 1 pre-enforcement principal priority of payments on the immediately preceding Funding 1 interest payment date.

### ***Allocations involving Rule (2)***

Where Rule (2) applies at a level of the relevant Funding 1 pre-enforcement principal priority of payments, the funds available for making payments at that level shall first be allocated without reference to Rule (2). However, if the amount so allocated to one or more rated loan tranches exceeds the amount permitted under Rule (2) to be paid in respect of those rated loan tranches (the **capped loan tranches**), the excess shall then be reallocated among any other relevant rated loan tranches then due and payable at that level using such method of allocation as applies at that level but without reference to the capped loan tranches in calculating such reallocation. If a further such excess arises as a result of the reallocation process, the reallocation process shall be repeated at that level in relation to each such further excess that arises until no further funds can be allocated at that level, following which the remaining excess shall then be applied at the next level of that priority of payments.

Rules (1) and (2) above are referred to in this base prospectus as the **repayment tests**.

#### *Repayment of loan tranches (other than start-up loan tranches) after a non-asset trigger event but before intercompany loan acceleration or acceleration of all notes*

Following the occurrence of a non-asset trigger event (where no asset trigger event has occurred) under the mortgages trust deed but prior to the service on Funding 1 of an intercompany loan acceleration notice and prior to the service on the issuing entity of a note acceleration notice, the bullet loan tranches and the scheduled amortisation loan tranches will be deemed to be pass-through loan tranches and, on each Funding 1 interest payment date, Funding 1 will be required to apply Funding 1 available principal receipts in the following order of priority:

- (A) to the extent only that monies have been drawn from the Funding 1 general reserve fund to make Funding 1 reserve principal payments, towards a credit to the Funding 1 general reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 reserve required amount;
- (B) if a liquidity reserve fund rating event has occurred and is continuing, (i) to the extent only that monies have been drawn from the Funding 1 liquidity reserve fund in order to make Funding 1 reserve principal payments or (ii) to the extent that the Funding 1 liquidity reserve fund has not been fully funded and Funding 1 available revenue receipts on such Funding 1 interest payment date are insufficient to do so, towards a credit to the Funding 1 liquidity reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 liquidity reserve fund required amount;
- (C) in order of their final repayment dates, beginning with the earliest such date (and if two or more AAA loan tranches have the same final repayment date, in proportion to the respective amounts due) to repay the AAA loan tranches until the AAA loan tranches are fully repaid;
- (D) in no order of priority among them, but in proportion to the amounts due, to repay the AA loan tranches until the AA loan tranches are fully repaid;
- (E) in no order of priority among them, but in proportion to the amounts due, to repay the A loan tranches until the A loan tranches are fully repaid;
- (F) in no order of priority among them, but in proportion to the amounts due, to repay the BBB loan tranches until the BBB loan tranches are fully repaid;
- (G) in no order of priority among them, but in proportion to the amounts due, to repay the BB loan tranches until the BB loan tranches are fully repaid; and
- (H) in no order of priority among them, but in proportion to the amounts due, to repay the subordinated loan tranches until the subordinated loan tranches are fully repaid.

#### *Repayment of loan tranches (other than start-up loan tranches) after an asset trigger event but before intercompany loan acceleration or acceleration of all notes*

Following the occurrence of an asset trigger event (whether or not a non-asset trigger event occurs or has occurred) but prior to the service on Funding 1 of an intercompany loan acceleration notice and prior to the service on the issuing entity of a note acceleration notice, the bullet loan tranches and the scheduled amortisation loan tranches will be deemed to be pass-through loan tranches and, on each Funding 1 interest payment date, Funding 1 will be required to apply Funding 1 available principal receipts in the following order of priority:



- (A) to the extent only that monies have been drawn from the Funding 1 general reserve fund to make Funding 1 reserve principal payments, towards a credit to the Funding 1 general reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 reserve required amount;
- (B) if a liquidity reserve fund rating event has occurred and is continuing, (i) to the extent only that monies have been drawn from the Funding 1 liquidity reserve fund in order to make Funding 1 reserve principal payments or (ii) to the extent that the Funding 1 liquidity reserve fund has not been fully funded, towards a credit to the Funding 1 liquidity reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 liquidity reserve fund required amount;
- (C) without priority among them, but in proportion to the amounts due, to repay the AAA loan tranches until the AAA loan tranches are fully repaid;
- (D) without priority among them, but in proportion to the amounts due, to repay the AA loan tranches until the AA loan tranches are fully repaid;
- (E) without priority among them, but in proportion to the amounts due, to repay the A loan tranches until the A loan tranches are fully repaid;
- (F) without priority among them, but in proportion to the amounts due, to repay the BBB loan tranches until the BBB loan tranches are fully repaid;
- (G) without priority among them, but in proportion to the amounts due, to repay the BB loan tranches until the BB loan tranches are fully repaid; and
- (H) without priority among them, but in proportion to the amounts due, to repay the subordinated loan tranches until the subordinated loan tranches are fully repaid.

*Repayment of loan tranches (other than start-up loan tranches) after acceleration of all notes but before intercompany loan acceleration*

If a note acceleration notice is served on the issuing entity, then that will not result in automatic enforcement of the Funding 1 security under the Funding 1 deed of charge. In those circumstances, however, the bullet loan tranches and any scheduled amortisation loan tranches will be deemed to be pass-through loan tranches and, on each Funding 1 interest payment date, Funding 1 will be required to apply Funding 1 available principal receipts in the following order of priority:

- (A) to the extent only that monies have been drawn from the Funding 1 general reserve fund to make Funding 1 reserve principal payments, towards a credit to the Funding 1 general reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 reserve required amount;
- (B) if a liquidity reserve fund rating event has occurred and is continuing, (i) to the extent only that monies have been drawn from the Funding 1 liquidity reserve fund in order to make Funding 1 reserve principal payments or (ii) to the extent that the Funding 1 liquidity reserve fund has not been fully funded, towards a credit to the Funding 1 liquidity reserve ledger to the extent that the amount standing to the credit thereof is less than the Funding 1 liquidity reserve fund required amount;
- (C) without priority among them, but in proportion to the amounts due, to repay the AAA loan tranches until the AAA loan tranches are fully repaid;
- (D) without priority among them, but in proportion to the amounts due, to repay the AA loan tranches until the AA loan tranches are fully repaid;
- (E) without priority among them, but in proportion to the amounts due, to repay the A loan tranches until the A loan tranches are fully repaid;
- (F) without priority among them, but in proportion to the amounts due, to repay the BBB loan tranches until the BBB loan tranches are fully repaid;
- (G) without priority among them, but in proportion to the amounts due, to repay the BB loan tranches until the BB loan tranches are fully repaid; and
- (H) without priority among them, but in proportion to the amounts due, to repay the subordinated loan tranches until the subordinated loan tranches are fully repaid.

*Repayment of loan tranches (other than start-up loan tranches) when Funding 1 receives an amount outstanding under the intercompany loan*

If Funding 1 receives a payment from the seller in the circumstances described in “**The mortgages trust – Payment by the seller of the amount outstanding under a loan tranche**” above or the proceeds of a loan tranche (other than a start-up loan tranche) which is to be used to refinance another loan tranche (other than a start-up loan tranche) as described in “**The intercompany loan agreement – The facility**” above (such payment by the seller or such proceeds being a **full repayment amount**), then Funding 1 will not apply the full repayment amount as described in “– **Distribution of Funding 1 available principal receipts**” above. Rather, Funding 1 will apply the full repayment amount to repay the relevant loan tranche.

#### **Definition of issuing entity principal receipts**

Prior to the service of a note acceleration notice on the issuing entity, **issuing entity principal receipts** will be calculated by the issuing entity cash manager four business days prior to each quarterly interest payment date and will be an amount equal to all principal amounts to be repaid by Funding 1 to the issuing entity under the intercompany loan during the relevant interest period (excluding with respect to start-up loan tranches). Following the service of a note acceleration notice on the issuing entity, but prior to the service of an intercompany loan acceleration notice on Funding 1, **issuing entity principal receipts** means the sum calculated by the issuing entity cash manager four business days prior to each quarterly interest payment date as the amount to be repaid by Funding 1 to the issuing entity under the intercompany loan during the relevant interest period (excluding with respect to the start-up loan tranches) and/or the sum otherwise recovered by the issuing entity security trustee (or the receiver appointed on its behalf) upon enforcement of the issuing entity security.

On each Funding 1 interest payment date, all Funding 1 available principal receipts received by the issuing entity from Funding 1 constituting principal repayments on a loan tranche (other than a start-up loan tranche) will be credited to a sub-ledger (in respect of the related series and class of notes or, as applicable, issuing entity subordinated loan) to the **issuing entity principal ledger**.

#### **Distribution of issuing entity principal receipts before note acceleration**

Prior to the service of a note acceleration notice on the issuing entity, the issuing entity or the issuing entity cash manager on its behalf will apply any issuing entity principal receipts on each quarterly interest payment date to repay the notes and the issuing entity subordinated loans in the following manner (the **issuing entity pre-enforcement principal priority of payments**):

- the class A notes: from principal amounts received by the issuing entity from Funding 1 in respect of each AAA loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class A notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class A notes;
- the class B notes: from principal amounts received by the issuing entity from Funding 1 in respect of each AA loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class B notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class B notes;

- the class M notes: from principal amounts received by the issuing entity from Funding 1 in respect of each A loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class M notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class M notes;
- the class C notes: from principal amounts received by the issuing entity from Funding 1 in respect of each BBB loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class C notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class C notes;
- the class D notes: from principal amounts received by the issuing entity from Funding 1 in respect of each BB loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) (if any) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class D notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class D notes; and
- the issuing entity subordinated loans: from principal amounts received by the issuing entity from Funding 1 in respect of each subordinated loan tranche to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related issuing entity subordinated loan.

The amounts standing to the credit of any sub-ledger of the issuing entity principal ledger (in respect of a series and class of notes or, as applicable, issuing entity subordinated loan) may only be applied by the issuing entity cash manager to repay principal due (if any) in respect of such series and class of notes or, as applicable, issuing entity subordinated loan under the issuing entity pre-enforcement principal priority of payments.

**Distribution of issuing entity principal receipts after note acceleration but before intercompany loan acceleration**

The issuing entity deed of charge sets out the priority of distribution of issuing entity principal receipts received or recovered by the issuing entity security trustee (or a receiver appointed on its behalf) from Funding 1 following the service of a note acceleration notice on the issuing entity but prior to the service of an intercompany loan acceleration notice on Funding 1. In these circumstances, the issuing entity security trustee will apply issuing entity principal receipts on each quarterly interest payment date to repay the notes and issuing entity subordinated loans in the following manner:

- the class A notes: from principal amounts received by the issuing entity from Funding 1 in respect of each AAA loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the

issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):

- (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class A notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class A notes;
- the class B notes: from principal amounts received by the issuing entity from Funding 1 in respect of each AA loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class B notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class B notes;
- the class M notes: from principal amounts received by the issuing entity from Funding 1 in respect of each A loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class M notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class M notes;
- the class C notes: from principal amounts received by the issuing entity from Funding 1 in respect of each BBB loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class C notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class C notes;
- the class D notes: from principal amounts received by the issuing entity from Funding 1 in respect of each BB loan tranche (and in respect of (ii) below, the principal amounts received (if any) from the issuing entity swap provider(s) under the relevant issuing entity swap agreement(s) in respect of the related series and class of notes):
  - (i) to pay amounts due and payable (in respect of principal) on such quarterly interest payment date to the relevant issuing entity swap provider(s) (if any) in respect of the related series and class of class D notes in accordance with the terms of the relevant issuing entity swap agreement(s); and
  - (ii) to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related series and class of class D notes.

- the issuing entity subordinated loans: from principal amounts received by the issuing entity from Funding 1 in respect of each subordinated loan tranche to pay amounts due and payable in respect of principal (if any) on such quarterly interest payment date on the related issuing entity subordinated loan.

The amounts standing to the credit of any sub-ledger of the issuing entity principal ledger (in respect of a series and class of notes or, as applicable, issuing entity subordinated loan) may only be applied by the issuing entity security trustee to repay principal due (if any) in respect of such series and class of notes or, as applicable, issuing entity subordinated loan under the above issuing entity principal priority of payments.

#### **Distribution of Funding 1 principal receipts and Funding 1 revenue receipts following intercompany loan acceleration**

The Funding 1 deed of charge sets out the priority of distribution of amounts received or recovered by the Funding 1 security trustee or a receiver appointed on its behalf following the service of an intercompany loan acceleration notice on Funding 1. If Funding 1 enters into new intercompany loan agreements or loan tranches with lower designated ratings are advanced to Funding 1 pursuant to the intercompany loan agreement, then this priority will change. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may adversely affect your interests**”, “**Security for Funding 1’s obligations**” and “**Security for the issuing entity’s obligations**”.

The Funding 1 security trustee will apply amounts received or recovered following the service of an intercompany loan acceleration notice on Funding 1 on each Funding 1 interest payment date in accordance with the following priority (the **Funding 1 post-enforcement priority of payments**):

- (A) without priority among them, but in proportion to the respective amounts due, to pay:
- all fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable in the immediately following interest period to the Funding 1 security trustee and any receiver appointed by the Funding 1 security trustee under the Funding 1 deed of charge (together with interest and any amount in respect of VAT on those amounts); and
  - the issuing entity in respect of the issuing entity fee payable pursuant to the intercompany loan agreement corresponding to the issuing entity’s obligations specified in item (A) of the issuing entity post-enforcement priority of payments;
- (B) to pay the issuing entity in respect of the issuing entity fee payable pursuant to the intercompany loan agreement corresponding to the issuing entity’s obligations specified in items (B) and (C) of the issuing entity post-enforcement priority of payments;
- (C) without priority among them but in proportion to the respective amounts due, towards payment of amounts (if any) due and payable by Funding 1 to:
- the cash manager under the terms of the cash management agreement;
  - the corporate services provider under the terms of the corporate services agreement; and
  - the account bank under the terms of the bank account agreement;
- (D) towards payment of amounts (if any) due to the Funding 1 swap provider under the Funding 1 swap agreement (including any termination payment, but excluding any Funding 1 swap excluded termination amount);
- (E) without priority among them, but in proportion to the respective amounts due, towards payments of interest, principal and issuing entity fees (other than as provided for in item (K) below) due and payable on or in respect of the AAA loan tranches;

- (F) without priority among them, but in proportion to the respective amounts due, towards payments of interest, principal and issuing entity fees (other than as provided for in item (K) below) due and payable on or in respect of the AA loan tranches;
- (G) without priority among them, but in proportion to the respective amounts due, towards payments of interest, principal and issuing entity fees (other than as provided for in item (K) below) due and payable on or in respect of the A loan tranches;
- (H) without priority among them, but in proportion to the respective amounts due, towards payments of interest, principal and issuing entity fees (other than as provided for in item (K) below) due and payable on or in respect of the BBB loan tranches;
- (I) without priority among them, but in proportion to the respective amounts due, towards payments of interest, principal and issuing entity fees (other than as provided for in item (K) below) due and payable on or in respect of the BB loan tranches;
- (J) without priority among them, but in proportion to the respective amounts due, towards payments of interest, principal and issuing entity fees (other than as provided for in item (K) below) due and payable on or in respect of the subordinated loan tranches;
- (K) towards payment of any amounts due to the issuing entity in respect of the issuing entity fee payable pursuant to the intercompany loan agreement corresponding to the issuing entity's obligations (if any) to make a termination payment to an issuing entity swap provider (but excluding any issuing entity swap excluded termination amount);
- (L) without priority among them, but in proportion to the respective amounts due, to pay (without double counting):
- amounts due to the issuing entity in respect of the issuing entity fee payable pursuant to the intercompany loan agreement corresponding to the issuing entity's obligations (if any) to pay any issuing entity swap excluded termination amount to an issuing entity swap provider following an issuing entity swap provider default or an issuing entity swap provider downgrade termination event;
  - any other amounts due to the issuing entity under the intercompany loan agreement and not otherwise provided for earlier in this priority of payments; and
  - amounts due to the Funding 1 swap provider in respect of Funding 1's obligation to pay any termination amount to the Funding 1 swap provider as a result of a Funding 1 swap provider default or a Funding 1 swap provider downgrade termination event;
- (M) without priority among them, but in proportion to the amounts then due, towards payment of interest, principal and other amounts due and payable on the start-up loan tranches; and
- (N) towards payment of any deferred consideration due to the seller pursuant to the terms of the mortgage sale agreement.

**Distribution of issuing entity principal receipts and issuing entity revenue receipts following note acceleration and intercompany loan acceleration**

If an intercompany loan acceleration notice is served on Funding 1, then there will be an automatic enforcement of the issuing entity security under the issuing entity deed of charge. The issuing entity deed of charge sets out the priority of distribution by the issuing entity security trustee, following the service of a note acceleration notice on the issuing entity and the service of an intercompany loan acceleration notice on Funding 1 or the recovery of any sum by the issuing entity security trustee (or any receiver appointed on its behalf) upon enforcement of the issuing entity security (other than from Funding 1 in accordance with the intercompany loan agreement) (the **issuing entity post-enforcement priority of payments**), of amounts received or recovered by the issuing entity security trustee (or a receiver appointed on its behalf).

On each quarterly interest payment date, the issuing entity security trustee will apply amounts (other than amounts representing swap collateral which shall be returned directly to the relevant issuing entity swap provider received or recovered following enforcement of the issuing entity security as follows:

- (A) without priority among them, but in proportion to the respective amounts due, to pay:

- any fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable in the immediately following interest period to the issuing entity security trustee and any receiver appointed by the issuing entity security trustee under the issuing entity deed of charge (together with interest and any amount in respect of VAT on those amounts); and
  - any fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable in the immediately following interest period to the note trustee under the note trust deed (together with interest and any amount in respect of VAT on those amounts);
- (B) without priority among them, but in proportion to the respective amounts due, to pay any fees, costs, expenses, other remuneration and indemnity payments due and payable or to become due and payable during the immediately following interest period to the agent bank, the paying agents, the registrar and the transfer agent under the paying agent and agent bank agreement (together with interest and any amount in respect of VAT on those amounts);
- (C) without priority among them, but in proportion to the respective amounts due, towards payment of amounts (together with any amount in respect of VAT on those amounts) due and payable to:
- the issuing entity cash manager under the issuing entity cash management agreement;
  - to the corporate services provider under the corporate services agreement; and
  - to the issuing entity account bank under the issuing entity bank account agreement;
- (D) subject to item (E) below, without priority among them but in proportion to the respective amounts due, to pay amounts due to the issuing entity swap providers for each series of class A notes (excluding any termination payment);
- (E) without priority among them, but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the applicable series of class A notes and to pay any swap termination payment due to the issuing entity swap provider for each series of class A notes (but excluding any issuing entity swap excluded termination amount) provided that if the amounts available for distribution under this item (E) (on the assumption that no amounts are due and payable under item (D) and no amounts are received from any issuing entity swap provider) would be insufficient to pay the sterling equivalent of the amounts due and payable under this item (E), the shortfall will be divided amongst all such amounts on a *pro rata* basis and the amount payable by the issuing entity to the issuing entity swap provider in respect of any series of class A notes under item (D) above will be reduced by the amount of the shortfall applicable to that series of class A notes;
- (F) subject to item (G) below, without priority among them but in proportion to the respective amounts due, to pay amounts due to the issuing entity swap providers for each series of class B notes (excluding any termination payment);
- (G) without priority among them but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the applicable series of class B notes and to pay any swap termination payment due to the issuing entity swap provider for each series of class B notes (but excluding any issuing entity swap excluded termination amount) provided that if the amounts available for distribution under this item (G) (on the assumption that no amounts are due and payable under item (F) and no amounts are received from any issuing entity swap provider) would be insufficient to pay the sterling equivalent of the amounts due and payable under this item (G), the shortfall will be divided amongst all such amounts on a *pro rata* basis and the amount payable by the issuing entity to the issuing entity swap provider in respect of any series of class B notes under item (F) above will be reduced by the amount of the shortfall applicable to that series of class B notes;
- (H) subject to item (I) below, without priority among them but in proportion to the respective amounts due, to pay amounts due to the issuing entity swap providers for each series of class M notes (excluding any termination payment);
- (I) without priority among them but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the applicable series of class M notes and to pay any swap

termination payment due to the issuing entity swap provider for each series of class M notes (but excluding any issuing entity swap excluded termination amount) provided that if the amounts available for distribution under this item (I) (on the assumption that no amounts are due and payable under item (H) and no amounts are received from any issuing entity swap provider) would be insufficient to pay the sterling equivalent of the amounts due and payable under this item (I), the shortfall will be divided amongst all such amounts on a *pro rata* basis and the amount payable by the issuing entity to the issuing entity swap provider in respect of any series of class M notes under item (H) above will be reduced by the amount of the shortfall applicable to that series of class M notes;

- (J) subject to item (K) below, without priority among them but in proportion to the respective amounts due, to pay amounts due to the issuing entity swap providers for each series of class C notes (excluding any termination payment);
- (K) without priority among them but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the applicable series of class C notes and to pay any swap termination payment due to the issuing entity swap provider for each series of class C notes (but excluding any issuing entity swap excluded termination amount) provided that if the amounts available for distribution under this item (K) (on the assumption that no amounts are due and payable under item (J) and no amounts are received from any issuing entity swap provider) would be insufficient to pay the sterling equivalent of the amounts due and payable under this item (K), the shortfall will be divided amongst all such amounts on a *pro rata* basis and the amount payable by the issuing entity to the issuing entity swap provider in respect of any series of class C notes under item (J) above will be reduced by the amount of the shortfall applicable to that series of class C notes;
- (L) subject to item (M) below, without priority among them but in proportion to the respective amounts due, to pay amounts due to the issuing entity swap providers for each series of class D notes (excluding any termination payment);
- (M) without priority among them but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the applicable series of class D notes and to pay any swap termination payment due to the issuing entity swap provider for each series of class D notes (but excluding any issuing entity swap excluded termination amount) provided that if the amounts available for distribution under this item (M) (on the assumption that no amounts are due and payable under item (L) and no amounts are received from any issuing entity swap provider) would be insufficient to pay the sterling equivalent of the amounts due and payable under this item (M), the shortfall will be divided amongst all such amounts on a *pro rata* basis and the amount payable by the issuing entity to the issuing entity swap provider in respect of any series of class D notes under item (L) above will be reduced by the amount of the shortfall applicable to that series of class D notes;
- (N) without priority among them but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the issuing entity subordinated loans;
- (O) without priority among them but in proportion to the respective amounts due, to pay any issuing entity swap excluded termination amounts to the issuing entity swap providers; and
- (P) without priority among them but in proportion to the respective amounts due, to pay interest due or overdue on, and to repay principal of, the issuing entity start-up loans.

Notwithstanding the above, amounts standing to the credit of any sub-ledger of the issuing entity revenue ledger and/or the issuing entity principal ledger (in respect of a series and class of notes, any issuing entity subordinated loan or, as applicable, any issuing entity start-up loan) may only be applied by the issuing entity security trustee to pay interest, principal and other amounts due in respect of such series and class of notes, such issuing entity subordinated loan or, as applicable, such issuing entity start-up loan or any shortfall in the amounts available to pay items (A) to (C) under the issuing entity post-enforcement priority of payments and may not be applied in payment of interest, principal and other amounts due in respect of any other series and class of notes or in respect of any issuing entity subordinated loan or issuing entity start-up loan.



## **Credit structure**

The notes are and will be obligations of the issuing entity only and are and will not be obligations of, or the responsibility of, or guaranteed by, any other party. However, the transaction has a number of features which enhances the likelihood of timely receipt of payments to noteholders, as follows:

- Funding 1 available revenue receipts are expected to exceed interest payable on rated loan tranches under the intercompany loan agreement and the amounts ranking senior thereto;
- subject to certain restrictions, a shortfall in Funding 1 available revenue receipts may be met from Funding 1's principal receipts;
- a Funding 1 general reserve fund and/or Funding 1 liquidity reserve fund has been established to help meet shortfalls in principal due on the original bullet loan tranches and original scheduled amortisation loan tranches in the circumstances described below;
- the Funding 1 general reserve fund and/or Funding 1 liquidity reserve fund may also be used to help meet any deficit in Funding 1 available revenue receipts available for payment of interest and issuing entity fees due under the intercompany loan agreement (other than with respect to the subordinated loan tranches or the start-up loan tranches) and to help meet any deficit on the Funding 1 principal deficiency ledger (excluding any deficit on the subordinated loan principal deficiency sub-ledger);
- Funding 1 will be obliged to establish a liquidity reserve fund if the seller ceases to have a long-term unsecured, unsubordinated and unguaranteed credit rating by Moody's of at least A3 (unless Moody's confirms that its current rating of the notes will not be downgraded, withdrawn or qualified as a result of the rating downgrade of the seller);
- payments on the issuing entity subordinated loans will be subordinated to payments on the class A notes, the Class B notes, the class M notes, the class C notes and the class D notes;
- payments on the class D notes will be subordinated to payments on the class A notes, the class B notes, the class M notes and the class C notes;
- payments on the class C notes will be subordinated to payments on the class A notes, the class B notes and the class M notes;
- payments on the class M notes will be subordinated to payments on the class A notes and the class B notes;
- payments on the class B notes will be subordinated to payments on the class A notes;
- the mortgages trustee GIC account and the Funding 1 GIC account will each earn interest at a specified rate; and
- issuing entity start-up loans may be provided to the issuing entity, to be on-lent to Funding 1 by way of start-up loan tranches in connection with each issuance of notes to fund the Funding 1 general reserve fund and/or Funding 1 liquidity reserve fund (if any) and/or to meet the costs and expenses in connection with the issuance of notes and/or to contribute towards Funding 1 available revenue receipts on the interest payment date immediately following a closing date.

Each of these factors is considered more fully in the remainder of this section.

### **Credit support for the notes provided by Funding 1 available revenue receipts**

It is anticipated that, during the life of the notes issued under the programme, the Funding 1 share of the interest received from borrowers on the loans will, assuming that all of the loans are fully performing, be greater than the sum of interest which Funding 1 is required to pay on the rated loan tranches under the intercompany loan

agreement in order for the issuing entity to fund (by payment to an issuing entity swap provider or otherwise) the interest payments due on the notes and the other senior costs and expenses of the structure. In other words, it is anticipated that Funding 1 available revenue receipts will be sufficient to pay the amounts payable under items (A) to (E), (G), (I), (K) and (M) of the Funding 1 pre-enforcement revenue priority of payments assuming all loans are fully performing.

The actual amount of any excess will vary during the life of the notes. Two of the key factors determining the variation are as follows:

- the interest rate on the loans in the portfolio; and
- the level of arrears experienced.

On any Funding 1 interest payment date, any excess will be available to meet the payments referred to under items (N) to (V) (inclusive) of the Funding 1 pre-enforcement revenue priority of payments, including the payment of any deferred consideration to the seller.

#### **Level of arrears experienced**

If the level of arrears of interest payments made by the borrowers results in Funding 1 experiencing an income deficit, Funding 1 will be able to use the following amounts to cure that income deficit:

- *first*, amounts standing to the credit of the Funding 1 general reserve fund, as described in “**Funding 1 general reserve fund**” below;
- *second*, drawings under the Funding 1 liquidity reserve fund, if established, as described in “**Funding 1 liquidity reserve fund**” below; and
- *third*, principal receipts, if any, as described in “– **Use of Funding 1 principal receipts to pay Funding 1 income deficiency**” below,

provided that such amounts may not be used in respect of the subordinated loan tranches or the start-up loan tranches.

Any excess of Funding 1 available revenue receipts will be applied on each Funding 1 interest payment date to the extent described in the Funding 1 pre-enforcement revenue priority of payments, including to extinguish amounts standing to the debit of any principal deficiency sub-ledger and to replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any).

#### **Use of Funding 1 principal receipts to pay Funding 1 income deficiency**

Four business days prior to each Funding 1 interest payment date, the cash manager will calculate whether there will be an excess or a deficit of Funding 1 available revenue receipts to pay items (A) to (E), (G), (I), (K) and (M) of the Funding 1 pre-enforcement revenue priority of payments.

If there is a deficit, then Funding 1 shall pay or provide for that deficit by the application of any amounts standing to the credit of the Funding 1 principal ledger (plus, if necessary, any amounts standing to the credit of the Funding 1 cash accumulation ledger which is not comprised in Funding 1 available principal receipts). The cash manager shall make a corresponding entry in the relevant principal deficiency sub-ledger, as described in “– **Funding 1 principal deficiency ledger**” below as well as making a debit in the Funding 1 principal ledger (and, as applicable, Funding 1 cash accumulation ledger). Any such entry and debit shall be made and taken into account (including as to which priority of payments shall apply) prior to the application of Funding 1 available principal receipts on the relevant Funding 1 interest payment date.

Funding 1 principal receipts may not be used to pay interest on any loan tranche if and to the extent that such payment would result in a deficiency being recorded, or an existing deficiency being increased, on a principal deficiency sub-ledger relating to a rated loan tranche with a higher rating designation.

## Funding 1 general reserve fund

A Funding 1 general reserve fund was established on the programme date:

- to contribute to Funding 1 available revenue receipts (including to help meet any deficit recorded on the Funding 1 principal deficiency ledger (excluding the subordinated loan principal deficiency sub-ledger); and
- to make, where necessary, **Funding 1 reserve principal payments**, being:
  - (i) prior to the occurrence of a trigger event;
    - (A) repayments of principal which are then due and payable in respect of the original bullet loan tranches; and
    - (B) repayments of principal in respect of original scheduled amortisation loan tranches on their respective final repayment dates only; and
  - (ii) on or after the occurrence of a trigger event, repayments of principal in respect of original bullet loan tranches and original scheduled amortisation loan tranches on their respective final repayment dates only,

in each case prior to the service of an intercompany loan acceleration notice on Funding 1.

The Funding 1 general reserve fund will be funded and replenished from:

- Funding 1 available revenue receipts in accordance with item (O) of the Funding 1 pre-enforcement revenue priority of payments up to an amount equal to the Funding 1 reserve required amount (see “**Cashflows – Distribution of Funding 1 available revenue receipts before intercompany loan acceleration**” above);
- Funding 1 available principal receipts to the extent applied in making Funding 1 reserve principal payments; and
- issuing entity start-up loans advanced to the issuing entity by the issuing entity start-up loan provider or new issuing entity start-up loan providers in connection with each issuance of notes, the proceeds of which will be advanced to Funding 1 by way of start-up loan tranches under the intercompany loan agreement for the purposes of, among other things, funding the Funding 1 general reserve fund.

The **Funding 1 reserve required amount** as at any date will be the amount specified as such in the most recent final terms. Changes may be made to the Funding 1 reserve required amount and/or the manner in which the Funding 1 general reserve is funded. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may severely affect your interests**”, “**Security for Funding 1’s obligations**” and “**Security for the issuing entity’s obligations**”.

Funding 1 may adjust, at any time, the Funding 1 reserve required amount without the consent of noteholders so long as the Funding 1 security trustee and/or Funding 1 obtain confirmation from the rating agencies that such adjustments will not cause a reduction, withdrawal or (in the case of Moody's) qualification of the ratings of any outstanding notes.

A Funding 1 general reserve ledger is maintained by the cash manager to record the balance from time to time of the Funding 1 general reserve fund.

On each Funding 1 interest payment date the amount of the Funding 1 general reserve fund is added to the other income of Funding 1 in calculating Funding 1 available revenue receipts.

## Funding 1 principal deficiency ledger

A principal deficiency ledger has been established to record:

- on each calculation date, any principal losses on the loans allocated to Funding 1; and/or

- on each Funding 1 interest payment date, any application of amounts standing to the credit of the Funding 1 principal ledger and/or the Funding 1 cash accumulation ledger to meet any deficiency in Funding 1 available revenue receipts (as described in “– **Use of Funding 1 principal receipts to pay Funding 1 income deficiency**” above); and
- the application of Funding 1 available principal receipts which are allocated to fund the Funding 1 liquidity reserve fund up to the Funding 1 liquidity reserve fund required amount.

The Funding 1 principal deficiency ledger is split into six sub-ledgers which correspond to each of the AAA loan tranches, the AA loan tranches, the A loan tranches, the BBB loan tranches, the BB loan tranches and the subordinated loan tranches, respectively.

Losses on the loans and/or the application of amounts standing to the credit of the Funding 1 principal ledger and/or the Funding 1 cash accumulation ledger to meet any deficiency in Funding 1 available revenue receipts (as described in “– **Use of Funding 1 principal receipts to pay Funding 1 income deficiency**” above) and will be recorded as follows:

- *first*, on the subordinated loan principal deficiency sub-ledger until the balance of the subordinated loan principal deficiency sub-ledger is equal to the aggregate principal amount outstanding of the subordinated loan tranches;
- *second*, on the BB principal deficiency sub-ledger until the balance of the BB principal deficiency sub-ledger is equal to the aggregate principal amount outstanding of all BB loan tranches;
- *third*, on the BBB principal deficiency sub-ledger until the balance of the BBB principal deficiency sub-ledger is equal to the aggregate principal amount outstanding of all BBB loan tranches;
- *fourth*, on the A principal deficiency sub-ledger until the balance of the A principal deficiency sub-ledger is equal to the aggregate principal amount outstanding of all A loan tranches;
- *fifth*, on the AA principal deficiency sub-ledger until the balance of the AA principal deficiency sub-ledger is equal to the aggregate principal amount outstanding of all AA loan tranches; and
- *sixth*, on the AAA principal deficiency sub-ledger, at which point there will be an asset trigger event (unless such losses are recorded when (a) the aggregate principal amount outstanding of all BB loan tranches, BBB loan tranches, A loan tranches and AA loan tranches is equal to zero and (b) the sum of (i) the amount standing to the credit of the Funding 1 general reserve ledger and (ii) the amount standing to the credit of the Funding 1 revenue ledger together with amounts determined and due to be credited to the Funding 1 revenue ledger prior to the Funding 1 interest payment date immediately following such recording of losses, is greater than the amount necessary to pay the items in paragraphs (A) to (F) in the Funding 1 pre-enforcement revenue priority of payments on the Funding 1 interest payment date immediately following such recording of losses).

Losses on the loans and/or the application of amounts standing to the credit of the Funding 1 principal ledger and/or the Funding 1 cash accumulation ledger to meet any deficiency in Funding 1 available revenue receipts (as described in “– **Use of Funding 1 principal receipts to pay Funding 1 income deficiency**” above) and will not be recorded on the Funding 1 principal deficiency ledger on any day to the extent that the Funding 1 share together with amounts standing to the credit of the Funding 1 cash accumulation ledger and the Funding 1 principal ledger in aggregate is greater than or equal to the aggregate outstanding principal balance of the rated loan tranches and the subordinated loan tranches on that day, after taking account of such losses or the relevant application of principal receipts.

Prior to the service of an intercompany loan acceleration notice on Funding 1, Funding 1 available revenue receipts will be applied on each Funding 1 interest payment date in the manner and to the extent described in the Funding 1 pre-enforcement revenue priority of payments as follows:

- *first*, provided that interest due on the AAA loan tranches has been paid, in an amount necessary to reduce to zero the balance on the AAA principal deficiency sub-ledger;

- *second*, provided that interest due on the AA loan tranches has been paid, in an amount necessary to reduce to zero the balance on the AA principal deficiency sub-ledger;
- *third*, provided that interest due on the A loan tranches has been paid, in an amount to reduce to zero the balance on the A principal deficiency sub-ledger;
- *fourth*, provided that interest due on the BBB loan tranches has been paid, in an amount necessary to reduce to zero the balance on the BBB principal deficiency sub-ledger;
- *fifth*, provided that interest due on the BB loan tranches has been paid, in an amount necessary to reduce to zero the balance on the BB principal deficiency sub-ledger; and
- *sixth*, provided that interest due on the subordinated loan tranches has been paid, in an amount necessary to reduce to zero the balance on the subordinated loan principal deficiency sub-ledger.

See also “– Use of Funding 1 principal receipts to pay Funding 1 income deficiency” above.

### **Issuing entity available funds**

On each Funding 1 interest payment date, the issuing entity will receive from Funding 1 in respect of the intercompany loan agreement an amount equal to or less than the amount which it needs to pay out on the corresponding interest payment date in respect of the notes, the issuing entity subordinated loans and the issuing entity start-up loans in accordance with the issuing entity pre-enforcement principal priority of payments and the issuing entity pre-enforcement revenue priority of payments. It is not intended that any surplus cash will be accumulated in the issuing entity.

Please see also the description of the issuing entity swaps under “**The swap agreements**” below.

### **Priority of payments among the class A notes, the class B notes, the class M notes, the class C notes, the class D notes and the issuing entity subordinated loans**

Payments of interest on the notes and the issuing entity subordinated loans are and will be prioritised so that interest payments due on the issuing entity subordinated loans on any interest payment date are and will be subordinated to interest payments on the class D notes, the Class M notes, the class C notes, the class B notes and the class A notes due on the same interest payment date, interest payments due on the class D notes on any interest payment date are and will be subordinated to interest payments on the class C notes, the class M notes, the class B notes and the class A notes due on the same interest payment date, interest payments due on the class C notes on any interest payment date will be subordinated to interest payments on the class M notes, the class B notes and the class A notes due on the same interest payment date, interest payments due on the class M notes on any interest payment date will be subordinated to interest payments on the class B notes and the class A notes due on the same interest payment date and interest payments due on the class B notes on any interest payment date are and will be subordinated to interest payments on the class A notes due on the same interest payment date, in each case in accordance with the applicable issuing entity priority of payments.

Any shortfall in payments of interest due on any issuing entity subordinated loan and/or any series of class D notes and/or class C notes and/or class M notes and/or class B notes on any interest payment date in respect of such issuing entity subordinated loan or notes will be deferred until the next interest payment date in respect of such notes and will accrue interest. On that next interest payment date, the amount of interest due on the relevant issuing entity subordinated loan or class of notes will be increased to take account of any deferred interest. If, on that interest payment date, there is still a shortfall, that shortfall will be deferred again. This deferral process will continue until the final maturity date of the notes, at which point all such deferred amounts (including interest thereon) will become due and payable. You may therefore not receive all interest amounts payable on those classes of notes.

The issuing entity is not able to defer payments of interest due on any interest payment date in respect of the class A notes or other most senior class of notes then outstanding. The failure to pay interest on such notes will be a note event of default.

The class A notes, the class B notes, the class M notes, the class C notes and the class D notes are and will be constituted by the note trust deed and, together with the issuing entity subordinated loans, share the same security. However, upon the service of a note acceleration notice and the recovery of any sum by the issuing entity security trustee (or any receiver appointed on its behalf) upon enforcement of the issuing entity security

(other than from Funding 1 in accordance with the intercompany loan agreement) or the occurrence of a trigger event, the class A notes of each series will rank in priority to each series of class B notes, each series of class M notes, each series of class C notes, each series of class D notes and each issuing entity subordinated loan and the class B notes of each series will rank in priority to each series of class M notes, each series of class C notes, each series of class D notes and each issuing entity subordinated loan and the class M notes of each series will rank in priority to each series of class C notes, each series of class D notes and each issuing entity subordinated loan and the class C notes of each series will rank in priority to each series of class D notes and each issuing entity subordinated loan and the class D notes of each series will rank in priority to each issuing entity subordinated loan.

### **Issuing entity subordinated loan agreements**

The following section contains a summary of the expected material terms of issuing entity subordinated loan agreements. The summary does not purport to be complete and is subject to the provisions of each relevant issuing entity subordinated loan agreement.

#### *General description*

Pursuant to issuing entity subordinated loan agreements to be entered into from time to time, Bank of Scotland (acting as **issuing entity subordinated loan provider**) will, on the applicable date, advance an issuing entity subordinated loan to the issuing entity. Each issuing entity subordinated loan will be used by the issuing entity to fund a subordinated loan tranche to be advanced by the issuing entity to Funding 1 pursuant to the intercompany loan agreement. Each subordinated loan tranche will be used to:

- (a) pay the seller part of the consideration for loans (together with their related security) sold by the seller to the mortgages trustee in connection with the making of the issuing entity subordinated loan to the issuing entity and the issuing entity advancing the corresponding loan tranches to Funding 1;
- (b) acquire part of the seller share (such payment to be made to the seller);
- (c) fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any); and/or
- (d) make a payment to the issuing entity to refinance an existing loan tranche (which may be a rated loan tranche or a subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of a new intercompany loan.

The issuing entity may, from time to time, enter into issuing entity subordinated loan agreements with entities other than Bank of Scotland (as **new issuing entity subordinated loan providers**). On entering into an issuing entity subordinated loan agreement, the issuing entity subordinated loan provider or, as applicable, any new issuing entity subordinated loan provider will enter into a deed of accession to the issuing entity deed of charge.

#### *Interest*

Each issuing entity subordinated loan bears and will continue to bear interest until repaid at a rate which corresponds and will continue to correspond to the interest paid under the corresponding subordinated loan tranche as set out in the applicable loan tranche supplement and (if applicable) final terms. Any unpaid interest will not fall due but instead is due on the next following quarterly interest payment date on which sufficient funds are available to pay such unpaid amount and pending such payment itself bears and will continue to bear interest. Interest in respect of each issuing entity subordinated loan is and will continue to be payable by the issuing entity on each quarterly interest payment date.

#### *Repayment*

Funding 1 will make repayments of each subordinated loan tranche on a *pro rata* basis (a) on each Funding 1 interest payment date, but only to the extent that the aggregate principal amount outstanding on all subordinated loan tranches exceeds the required subordinated loan tranche principal amount outstanding and to the extent that it has Funding 1 available principal receipts after making higher ranking payments (see further “**Cashflows – Distribution of Funding 1 available principal receipts**” and “**Cashflows – Distribution of Funding 1 principal receipts and Funding 1 revenue receipts following intercompany loan acceleration**” above) or (b) on any date, to the extent that such subordinated loan tranches are being refinanced on such date by other loan tranches (which may be other subordinated loan tranches). The issuing entity will make repayment on each issuing entity subordinated loan if and to the extent that it receives amounts from Funding 1 representing repayment of principal on the corresponding subordinated loan tranche. After the issuing entity has repaid an issuing entity subordinated loan, it will have no further recourse to the issuing entity subordinated loan provider

or, as applicable, the relevant new issuing entity subordinated loan provider in respect of such issuing entity subordinated loan.

The **required subordinated loan tranche principal amount outstanding**, as at any date, is the amount specified as such in the most recent loan tranche supplement and (if applicable) final terms or such other amount (which may be higher or lower) that Funding 1 and the issuing entity may designate and have notified to the cash manager, the Funding 1 security trustee, the issuing entity cash manager and the issuing entity security trustee, at any time, without the consent of noteholders so long as the Funding 1 security trustee and/or Funding 1 obtain confirmation from each of the rating agencies that such adjusted amount will not cause a reduction, withdrawal or (in the case of S&P and Moody's) qualification of its then ratings of any outstanding notes. See “**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may severely affect your interests**”, “**Security for Funding 1’s obligations**” and “**Security for the issuing entity’s obligations**”.

#### *Acceleration*

If an intercompany loan acceleration notice is served by the issuing entity security trustee on Funding 1, then each issuing entity subordinated loan will become immediately due and payable.

#### *Governing law*

Each issuing entity subordinated loan agreement and each new issuing entity subordinated loan agreement is and will be (as applicable) governed by English law.

#### **Mortgages trustee GIC account/Funding 1 GIC account**

All amounts held by the mortgages trustee are deposited in the mortgages trustee GIC account with the mortgages trustee GIC provider. This account is subject to the mortgages trustee guaranteed investment contract under which the mortgages trustee GIC provider agrees to pay a variable rate of interest on funds in the mortgages trustee GIC account of 0.25 per cent. per annum below LIBOR for three-month sterling deposits.

Amounts held in the collection account do not have the benefit of a guaranteed investment contract but following receipt will be transferred into the mortgages trustee GIC account on a regular basis and in any event in the case of direct debits no later than the next London business day after they are deposited in the collection account.

All amounts held by Funding 1 are deposited in the **Funding 1 GIC account** in the first instance. The Funding 1 GIC account is maintained with the Funding 1 GIC provider. This account is subject to the Funding 1 guaranteed investment contract under which the Funding 1 GIC provider agrees to pay a variable rate of interest on funds in the Funding 1 GIC account of 0.25 per cent. per annum below LIBOR for three-month sterling deposits.

The mortgages trustee GIC provider and the Funding 1 GIC provider are required to satisfy certain criteria (including certain criteria and/or permissions set or required by the FSA from time to time) in order to continue to receive deposits in the mortgages trustee GIC account and the Funding 1 GIC account respectively. These criteria include a requirement that the short-term, unguaranteed and unsecured ratings of the mortgages trustee GIC provider or the Funding 1 GIC provider, as the case may be, are at least F1 by Fitch, P-1 by Moody's and A-1+ by Standard & Poor's, unless (in each case) each rating agency confirms that its then current rating of the notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of such ratings falling below these minimum ratings. If either the mortgages trustee GIC provider or the Funding 1 GIC provider ceases to satisfy these criteria, then the relevant account may be transferred to another entity which does satisfy these criteria.

#### **Funding 1 liquidity reserve fund**

Funding 1 will be required to establish a liquidity reserve fund to the extent of the Funding 1 liquidity reserve fund required amount if, and for as long as, the long-term, unsecured, unsubordinated and unguaranteed debt obligations of the seller cease to be rated at least A3 by Moody's (unless Moody's, as applicable, confirms that its then current ratings of the notes will not be downgraded, withdrawn or (in the case of Moody's) qualified as a result of such ratings downgrade). If, following a subsequent increase in the seller's rating, Funding 1 would no longer be required to maintain the Funding 1 liquidity reserve fund, then all amounts standing to the credit of the Funding 1 liquidity reserve ledger will be treated as Funding 1 available revenue receipts for the next following Funding 1 interest payment date. In addition, following a reduction in the Funding 1 liquidity reserve fund required amount, amounts standing to the credit of the Funding 1 liquidity reserve ledger in excess of the Funding 1 liquidity reserve fund required amount will be treated as Funding 1 available revenue receipts for the next following Funding 1 interest payment date.

Prior to enforcement of Funding 1 security or service of an intercompany loan acceleration notice on Funding 1, the Funding 1 liquidity reserve fund may be used as part of Funding 1 available revenue receipts available to fund payment of certain senior expenses and interest due on rated loan tranches under the intercompany loan agreement. Prior to the service of an intercompany loan acceleration notice on Funding 1 and taking into account any allocation of principal to meet any deficiency in Funding 1's available revenue receipts, the Funding 1 liquidity reserve fund will also be available to make Funding 1 reserve principal payments (as to which, see "**Funding 1 general reserve fund**" above).

The Funding 1 liquidity reserve fund, if required to be funded, will be funded initially from Funding 1 available principal receipts or (if insufficient funds are available therefrom) from Funding 1 available revenue receipts in accordance with the Funding 1 pre-enforcement principal priority of payments or Funding 1 pre-enforcement revenue priority of payments, as applicable. The Funding 1 liquidity reserve fund will be deposited in Funding 1's name in the Funding 1 GIC account (into which the Funding 1 general reserve fund is also deposited). All interest or income accrued on the amount of the Funding 1 liquidity reserve fund while on deposit in the Funding 1 GIC account will belong to Funding 1. The cash manager will maintain a separate Funding 1 liquidity reserve ledger to record the balance from time to time of the Funding 1 liquidity reserve fund.

The Funding 1 liquidity reserve fund, if required, will be funded and replenished up to and including an amount equal to the Funding 1 liquidity reserve fund required amount on Funding 1 interest payment dates from Funding 1 available revenue receipts at item (P) of the Funding 1 pre-enforcement revenue priority of payments and from Funding 1 available principal receipts at item (B) of the relevant Funding 1 pre-enforcement principal priority of payments.

The **Funding 1 liquidity reserve fund required amount** is an amount, as at any Funding 1 interest payment date, equal to the excess (if any) of 3 per cent. of the aggregate outstanding balance of the notes on that Funding 1 interest payment date (taking into account any principal repayments to be made by the issuing entity on that date) over the aggregate of amounts standing to the credit of the Funding 1 general reserve fund on that Funding 1 interest payment date (taking into account any amount credited to the Funding 1 general reserve ledger on that date). Changes may be made to the Funding 1 liquidity reserve required amount and/or the manner in which the Funding 1 liquidity reserve fund is funded. See "**Risk factors – The Funding 1 security trustee and/or the issuing entity security trustee and/or the note trustee may agree to modifications to the transaction documents without your prior consent, which may severely affect your interests**", "**Security For Funding 1's obligations**" and "**Security for the issuing entity's obligations**".

Following enforcement of the Funding 1 security, amounts standing to the credit of the Funding 1 liquidity reserve ledger may be applied in making payments of principal due under the loan tranches.

### **Issuing entity start-up loan agreements**

The following section contains a summary of the material terms of the issuing entity start-up loan agreements. The summary does not purport to be complete and is subject to the provisions of the issuing entity start-up loan agreements.

#### *General description*

Pursuant to an issuing entity start-up loan agreement dated the programme date, Halifax (succeeded by Bank of Scotland) (acting as an **issuing entity start-up loan provider**) agreed to make available to the issuing entity an issuing entity start-up loan. On any closing date after the reorganisation date, new issuing entity start-up loan agreements may be entered into by Bank of Scotland (acting as an **issuing entity start-up loan provider**) pursuant to which the issuing entity start-up loan provider or, as applicable, a new issuing entity start-up loan provider will make further issuing entity start-up loans available to the issuing entity. Each issuing entity start-up loan will be a subordinate-ranking loan which will be used by the issuing entity to advance start-up loan tranches to Funding 1 pursuant to the intercompany loan agreement. The proceeds of each start-up loan tranche will be used by Funding 1 for establishing (or, as applicable, increasing) the Funding 1 general reserve fund on the relevant closing date and/or for meeting the costs and expenses incurred by Funding 1 in connection with any purchase price and related sale of loans and their related security sold to the mortgages trustee or the acquisition of part of the seller share on the relevant closing date and the fees payable under the intercompany loan agreement which relate to the costs and expenses of the related issuance of notes and/or to contribute towards Funding 1 available revenue receipts on the interest payment date immediately following the relevant closing date. The amount of each issuing entity start-up loan will be described in the applicable final terms.

The issuing entity may, from time to time, enter into issuing entity start-up loan agreements with entities other than Bank of Scotland (as **new issuing entity start-up loan providers**) subject to (i) such new issuing entity start-up loan agreement being on similar terms to the issuing entity start-up loan agreement and (ii) such new entity entering into a deed of accession to the issuing entity deed of charge.



### *Interest*

Each issuing entity start-up loan will bear interest until repaid at a rate which will be described in the applicable final terms. Any unpaid interest will not fall due but will instead be due on the next following quarterly interest payment date on which sufficient funds are available to pay such unpaid amount and pending such payment will itself bear interest. Interest in respect of each issuing entity start-up loan will be payable by the issuing entity on each quarterly interest payment date. The rate of interest on each start-up loan tranche will match the rate of interest on the corresponding issuing entity start-up loan.

### *Repayment*

Funding 1 will repay each start-up loan tranche, but only to the extent that it has Funding 1 available revenue receipts after making higher ranking payments (see further “**Cashflows – Distribution of Funding 1 available revenue receipts**” and “**Cashflows – Distribution of Funding 1 principal receipts and Funding 1 revenue receipts following intercompany loan acceleration**” above). The issuing entity will repay each issuing entity start-up loan if and to the extent that it receives amounts from Funding 1 representing repayments of principal on the corresponding start-up loan tranche. Amounts due to the issuing entity start-up loan provider or a new issuing entity start-up loan provider are payable after amounts due on the notes and the issuing entity subordinated loans. After the issuing entity has repaid an issuing entity start-up loan, it will have no further recourse to the issuing entity start-up loan provider or, as applicable, the relevant new issuing entity start-up loan provider in respect of such issuing entity start-up loan.

### *Acceleration*

If an intercompany loan acceleration notice is served by the issuing entity security trustee on Funding 1, then each issuing entity start-up loan will become immediately due and payable.

### *Governing law*

The issuing entity start-up loan agreement and each new issuing entity start-up loan agreement is and will be (as applicable) governed by English law.

## The swap agreements

The following section contains a summary of the material terms of the Funding 1 swap agreement and the issuing entity swap agreements. The summary does not purport to be complete and is subject to the provisions of those swap agreements.

### General

Funding 1 has entered into the Funding 1 swap agreement with Halifax (as the **Funding 1 swap provider**) and the Funding 1 security trustee and since the reorganisation date Bank of Scotland has been a party thereto in place of Halifax. The issuing entity will enter into issuing entity swap agreements with the issuing entity swap providers and the issuing entity security trustee. In general, the swaps are designed to do the following:

- Funding 1 swap: to hedge against the possible variance between the standard variable rate payable on the standard variable rate loans, the rates of interest payable on the tracker rate loans and the fixed rates of interest payable on the fixed rate loans and a weighted average of the LIBOR-based rates for sterling deposits payable in respect of any outstanding loan tranches under the intercompany loan agreement; (other than the start-up loan tranches); and
- Issuing entity swaps: to protect the issuing entity against certain interest rate and/or currency risks in respect of amounts received by the issuing entity from Funding 1 under rated loan tranches under the intercompany loan agreement and amounts payable by the issuing entity under the corresponding series and class of notes.

### The Funding 1 swap

Some of the loans in the portfolio pay a variable rate of interest for a period of time which may be linked to the standard variable rate, a variable interest rate other than the standard variable rate, such as a rate set by the Bank of England. Other loans pay a fixed rate of interest for a period of time. However, the interest rate payable by Funding 1 with respect to the loan tranches under the intercompany loan agreement is calculated by reference to LIBOR for three-month sterling deposits or, in certain circumstances, such other sterling LIBOR rate as may be specified in the applicable loan tranche supplement, each plus or minus a margin. To provide a hedge against the possible variance between:

- (1) the standard variable rate payable on the standard variable rate loans, the rates of interest payable on the tracker rate loans and the fixed rates of interest payable on the fixed rate loans; and
- (2) the LIBOR-based rates for sterling deposits payable in respect of any outstanding loan tranches (other than the start-up loan tranches),

Funding 1, the Funding 1 swap provider and the Funding 1 security trustee entered into the Funding 1 swap agreement on the programme date and (if necessary) will amend and restate the Funding 1 swap agreement on each relevant closing date such that the Funding 1 swap will:

- have a notional amount that is sized to hedge against any potential interest rate mismatches in relation to the loan tranches which remain outstanding (other than the start-up loan tranches); and
- provide for the notional amount to be increased as appropriate to hedge against similar potential interest rate mismatches in relation to any future loan tranches made available from time to time. (other than the start-up loan tranches)

Under the Funding 1 swap, on each calculation date the following amounts will be calculated:

- the amount produced by applying a weighted average of the LIBOR-based rates for sterling deposits payable in respect of any outstanding loan tranches (other than the start-up loan tranches) (as determined in respect of the corresponding interest period under such loan tranches) plus a spread for the relevant calculation period to the notional amount of the Funding 1 swap (known as the **calculation period swap provider amount**); and

- the amount produced by applying a rate equal to the weighted average of:
  - (i) the average of the standard variable rates or their equivalent charged to existing borrowers on residential mortgage loans as published from time to time, after excluding the highest and the lowest rate, of Abbey National plc, HSBC Bank plc, Cheltenham & Gloucester plc, National Westminster Bank Plc, Nationwide Building Society, Northern Rock plc and Woolwich plc (and, where those banks have more than one standard variable rate, the highest of those rates);
  - (ii) the rates of interest payable on the tracker rate loans;
  - (iii) the rates of interest payable on the fixed rate loans,

for the relevant calculation period to the notional amount of the Funding 1 swap (known as the **calculation period Funding 1 amount**).

On each Funding 1 interest payment date, the following amounts will be calculated:

- the sum of each of the calculation period swap provider amounts calculated during the preceding interest period; and
- the sum of each of the calculation period Funding 1 amounts calculated during the preceding interest period.

After these two amounts are calculated in relation to a Funding 1 interest payment date, the following payments will be made on that Funding 1 interest payment date:

- if the first amount is greater than the second amount, then the Funding 1 swap provider will pay the difference to Funding 1;
- if the second amount is greater than the first amount, then Funding 1 will pay the difference to the Funding 1 swap provider; and
- if the two amounts are equal, neither party will make a payment to the other.

If a payment is to be made by the Funding 1 swap provider, that payment will be included in the Funding 1 available revenue receipts and will be applied on the relevant Funding 1 interest payment date according to the Funding 1 pre-enforcement revenue priority of payments or, as applicable, the Funding 1 post-enforcement priority of payments. If a payment is to be made by Funding 1, it will be made according to the Funding 1 pre-enforcement revenue priority of payments or, as applicable, the Funding 1 post-enforcement priority of payments.

The notional amount of the Funding 1 swap in respect of a calculation period during an interest period will be an amount in sterling equal to:

- the aggregate principal amount outstanding of the loan tranches under the intercompany loan agreement (other than start-up loan tranches) during the relevant calculation period, less
- the balance of the Funding 1 principal deficiency ledger attributable to such loan tranches during the relevant calculation period, less
- the amount of the principal receipts in the Funding 1 GIC account attributable to such loan tranches during the relevant calculation period.

Unless a relevant swap early termination event occurs, the Funding 1 swap will terminate on the date on which the aggregate principal amount outstanding of loan tranches under the intercompany loan agreement (other than start-up loan tranches) is reduced to zero. In the event that the Funding 1 swap is terminated prior to the service of an intercompany loan acceleration notice or the latest occurring final repayment date of any loan tranche outstanding under the intercompany loan agreement (other than start-up loan tranches), Funding 1 shall enter into a replacement Funding 1 swap on terms acceptable to the rating agencies, with the Funding 1 security trustee and

with a swap provider whom each rating agency has previously confirmed in writing to Funding 1, the issuing entity, the note trustee, the issuing entity security trustee and/or the Funding 1 security trustee will not cause its then current ratings of the notes to be downgraded, withdrawn or (in the case of S&P and Moody's) qualified. If Funding 1 is unable to enter into a replacement Funding 1 swap on terms acceptable to the rating agencies, this may affect amounts available to pay interest on the loan tranches under the intercompany loan agreement (other than start-up loan tranches).

### **Issuing entity currency swaps**

The rated loan tranches under the intercompany loan agreement are denominated in sterling and interest payable by Funding 1 to the issuing entity under the rated loan tranches is calculated by reference to LIBOR for three-month sterling deposits or, in certain circumstances, such other sterling LIBOR rate as may be specified in the applicable loan tranche supplement, each plus or minus a margin. However, the issuing entity may (subject to compliance with all applicable legal, regulatory and central bank requirements) issue a series or class of notes in such currency as may be agreed with the relevant dealers and/or managers and/or (in the case of any privately placed notes) the relevant noteholders. Such series and class of notes will accrue interest at a rate calculated by reference to a rate for one-month deposits in such currency, three-month deposits in such currency or such other rate specified in the applicable final terms. To deal with the potential currency mismatch between (i) its receipts and liabilities in respect of a rated loan tranche and (ii) its receipts and liabilities under a corresponding series and class of such notes, the issuing entity will, pursuant to the terms of an issuing entity swap agreement in respect of such series and class of notes, swap its receipts and liabilities in respect of the relevant rated loan tranche on terms that match the issuing entity's obligations under the relevant series and class of the notes.

The currency amount of each such issuing entity swap will be the principal amount outstanding under the series and class of the notes to which the relevant issuing entity swap relates or an amount equal to the principal amount of the relevant series and class of notes issued on the programme date, subject to reduction from time to time as described below. Subject, in the case of the issuing entity's obligations under certain series and classes of notes, to certain deferral of interest provisions that will apply when payment of interest is deferred in accordance with the terms and conditions of such notes, and to the extent that the issuing entity makes its corresponding payments to the issuing entity swap providers, the issuing entity swap providers will pay to the issuing entity amounts in the specified currency that correspond to the amounts of interest to be paid on the relevant series and class of the notes. The issuing entity will pay to the issuing entity swap providers the sterling interest amounts received on the rated loan tranche corresponding to the relevant series and class of notes. In order to allow for the effective currency amount of each relevant issuing entity swap to amortise at the same rate as the relevant series and class of notes, each issuing entity swap agreement will provide that, as and when the notes amortise, either (i) a corresponding portion of the currency amount of the relevant issuing entity swap will amortise or (ii) that the issuing entity will have the right to partially terminate the relevant issuing entity swap. Pursuant to each such issuing entity swap agreement, in respect of any such amortisation or termination, there will be an exchange of sterling for an amount of the specified currency equal to the amount by which the currency amount of the relevant issuing entity swap has reduced at the specified currency exchange rate for such series and class of notes.

On the final maturity date of each relevant series and class of notes or, if earlier, the date on which such notes are redeemed in full (other than pursuant to Condition 5.6 (Optional redemption or purchase for implementation of EU Capital Requirements Directive) (as to which, see "**Terms and conditions of the notes**" below) or following delivery of a note acceleration notice in respect of all notes), the relevant issuing entity swap provider will pay to the issuing entity an amount in the specified currency, that corresponds to the principal amount outstanding under the relevant series and class of notes or the currency amount of the relevant issuing entity swap at such time, as applicable, and the issuing entity will pay to the relevant issuing entity swap provider an equivalent amount in sterling, converted by reference to the specified currency exchange rate for such series and class of notes. If the issuing entity does not have sufficient principal available pursuant to the issuing entity cash management agreement and the issuing entity deed of charge to pay such amount in full on such date and accordingly pays only a part of such amount to the relevant issuing entity swap provider, the relevant issuing entity swap provider will be obliged on such date to pay only the equivalent of such partial amount in the specified currency, in each case converted by reference to the specified currency exchange rate for such series and class of notes.

Subject to any partial termination provisions as described above, in the event that any issuing entity swap is terminated prior to service of a note acceleration notice or final redemption of the relevant series and class of notes, the issuing entity shall enter into a replacement currency swap in respect of that series and class of notes. Any replacement currency swap must be entered into on terms acceptable to the rating agencies, the issuing entity and the issuing entity security trustee and with a replacement currency swap provider whom each rating agency has previously confirmed in writing to the issuing entity and/or the issuing entity security trustee will not cause its then current ratings of the series and class of notes to be downgraded, withdrawn or (in the case of S&P and Moody's) qualified. If the issuing entity is unable to enter into any replacement currency swaps on terms

acceptable to the rating agencies, this may affect amounts available to pay amounts due under such series and class of notes.

If such an issuing entity currency swap agreement is terminated and the issuing entity is unable to enter into a replacement swap as described above, then any payments received by the issuing entity from Funding 1 on each Funding 1 interest payment date shall be deposited in the issuing entity transaction account (or such other account opened for this purpose) and applied by the issuing entity to repay the notes on each quarterly interest payment date after exchanging at the “spot” rate the relevant proceeds from sterling into the specified currency as required.

#### **Issuing entity interest rate swaps**

The rated loan tranches under the intercompany loan agreement are denominated in sterling and interest payable by Funding 1 to the issuing entity under the rated loan tranches is calculated by reference to LIBOR for three-month sterling deposits or, in certain circumstances, such other sterling LIBOR rate as may be specified in the applicable loan tranche supplement, each plus or minus a margin. However, the issuing entity may (subject to compliance with all applicable legal, regulatory and central bank requirements) issue a series and class of notes in sterling and such series and class of notes may accrue interest at a fixed rate. To deal with the potential interest rate mismatch between (i) its receipts and liabilities in respect of a loan tranche and (ii) its receipts and liabilities under a corresponding series and class of such notes, the issuing entity will, pursuant to the terms of an issuing entity swap agreement in respect of such series and class of notes, swap its receipts and liabilities in respect of the relevant loan tranche on terms that match the issuing entity’s obligations under the relevant series and class of notes.

In the event that any such issuing entity swap is terminated prior to the service of a note acceleration notice or its scheduled termination date, the issuing entity shall enter into a replacement interest rate swap in respect of that series and class of notes. Any replacement interest rate swap must be entered into on terms acceptable to the rating agencies, the issuing entity and the issuing entity security trustee and with a replacement interest rate swap provider whom each rating agency has previously confirmed in writing to the issuing entity and/or the issuing entity security trustee will not cause its then current ratings of the notes of the relevant series and class to be downgraded, withdrawn or (in the case of S&P and Moody's) qualified. If the issuing entity is unable to enter into any replacement interest rate swaps on terms acceptable to the rating agencies, this may affect amounts available to pay amounts due under such series and class of notes.

If such an issuing entity swap agreement is terminated and the issuing entity is unable to enter into a replacement swap as described above, then any payments received by the issuing entity from Funding 1 on each Funding 1 interest payment date shall be deposited in the issuing entity transaction account (or such other account opened for this purpose) and applied by the issuing entity to pay interest to the holders of the relevant series and class of notes on each quarterly interest payment date.

#### **Ratings downgrade of swap providers**

Under each of the swap agreements, in the event that the relevant rating(s) of a swap provider or its respective guarantor (if any), as applicable, is or are, as applicable, downgraded by a rating agency below the rating(s) specified in the relevant swap agreement with respect to such swap provider (in accordance with the requirements of the rating agencies) and, as a result of the downgrade, the then current ratings of the notes, in respect of the Funding 1 swap, or the notes corresponding to the relevant issuing entity swap, in respect of the relevant issuing entity swap, would or may be downgraded, withdrawn or (in the case of S&P and Moody's) qualified, then the relevant swap provider will, in accordance with the Funding 1 swap or the relevant issuing entity swap, as applicable, be required to take certain remedial measures which may include (a) providing collateral for its obligations under the relevant swap, (b) arranging for its obligations under the relevant swap to be transferred to an entity with rating(s) required by the relevant rating agency as specified in the relevant swap agreement (in accordance with the requirements of the relevant rating agency), (c) procuring another entity with rating(s) required by the relevant rating agency as specified in the relevant swap agreement (in accordance with the requirements of the relevant rating agency) to become co-obligor or guarantor in respect of its obligations under the relevant swap or (d) taking such other action as it may agree with the relevant rating agency.

#### **Termination of the swaps**

Any swap agreement may also be terminated in certain other circumstances, which may include the following, each referred to as a **swap early termination event**:

- at the option of one party to the swap agreement, if there is a failure by the other party to pay any amounts due under that swap agreement and any applicable grace period has expired;

- in respect of the issuing entity swaps, at the option of the relevant issuing entity swap provider, if a note event of default occurs and the note trustee serves a note acceleration notice on the issuing entity;
- in respect of the Funding 1 swap, at the option of the Funding 1 swap provider, if an intercompany loan event of default occurs and the Funding 1 security trustee serves an intercompany loan acceleration notice on Funding 1;
- in respect of the issuing entity swaps, at the option of either party, if a redemption of the relevant series and class of notes occurs pursuant to Condition 5.6 (Optional Redemption or Purchase for Implementation of EU Capital Requirements Directive) (as to which, see “**Terms and conditions of the notes**” below);
- if applicable, at the option of the issuing entity (in the case of an issuing entity swap) or Funding 1 (in the case of the Funding 1 swap), if certain tax representations made by the relevant swap provider prove to have been incorrect or misleading in any material respect;
- at the option of the relevant swap provider, if certain insolvency events occur with respect to the issuing entity (in the case of an issuing entity swap) or Funding 1 (in the case of the Funding 1 swap);
- at the option of the issuing entity (in the case of an issuing entity swap) or Funding 1 (in the case of the Funding 1 swap), upon the occurrence of an insolvency of the relevant swap provider or its guarantor (if any), or the merger of the relevant swap provider without an assumption of its obligations under the relevant swap agreement, or if a material misrepresentation is made by the swap provider under the relevant swap agreement, or if the relevant swap provider defaults under an over-the-counter derivatives transaction under another agreement between the issuing entity and such swap provider, or if a breach of a provision of the relevant swap agreement by the relevant swap provider is not remedied within the applicable grace period, or, if applicable, if the guarantor of the relevant swap provider fails to comply with its obligations under the relevant guarantee;
- if a change in law results in the obligations of one of the parties to the relevant swap agreement becoming illegal;
- at the option of the relevant swap provider, if withholding taxes are imposed on payments made by the relevant swap provider or issuing entity due to a change in law; and
- at the option of the issuing entity (in the case of an issuing entity swap) or Funding 1 (in the case of the Funding 1 swap) if the relevant swap provider or its guarantor (if any), as applicable, is downgraded and fails to comply with the requirements of the ratings downgrade provision contained in the relevant swap agreement and described under “– **Ratings downgrade of swap providers**” above.

Upon the occurrence of a swap early termination event, the issuing entity or the relevant issuing entity swap provider may be liable to make a termination payment to the other or, as applicable, Funding 1 or the Funding 1 swap provider may be liable to make a termination payment to the other. This termination payment will be calculated and payable in sterling. The amount of any termination payment will be based on the market value of the terminated swap as determined on the basis of quotations sought from leading dealers as to the cost of entering into a swap with the same terms and conditions that would have the effect of preserving the economic equivalent of the respective full payment obligations of the parties (or based upon a good faith determination of total losses and costs (or gains) if an insufficient number of quotations can be obtained or if basing the valuation on quotations would not produce a commercially reasonable result) and will include any unpaid amounts that became due and payable prior to the date of termination. Any such termination payment could be substantial.

If any issuing entity swap is terminated early and a termination payment is due by the issuing entity to an issuing entity swap provider, then, pursuant to its obligations under the intercompany loan agreement, Funding 1 shall pay to the issuing entity an amount equal to the termination payment due to the relevant issuing entity swap provider less any amount received by the issuing entity under any replacement issuing entity swap agreement. These payments will be made by Funding 1 only after paying interest amounts due on the loan tranches and after

providing for any debit balance on the Funding 1 principal deficiency ledger. The issuing entity shall apply amounts received from Funding 1 under the intercompany loan agreement in accordance with the issuing entity pre-enforcement revenue priority of payments or, as the case may be, the issuing entity post-enforcement priority of payments. The application by the issuing entity of termination payments due to an issuing entity swap provider may affect the funds available to pay amounts due to the noteholders (see further “**Risk factors – You may be subject to risks relating to exchange rates or interest rates on the notes**” above).

If the issuing entity receives a termination payment from an issuing entity swap provider, then the issuing entity shall use those funds towards meeting its costs in effecting any currency exchanges at the applicable spot rate of exchange until a replacement issuing entity swap is entered into and/or to acquire a replacement issuing entity swap.

Noteholders will not receive extra amounts (over and above interest and principal payable on the notes) as a result of the issuing entity receiving a termination payment.

### **Transfer of the swaps**

Each swap provider may, subject to certain conditions specified in the relevant swap agreement, including (without limitation) the satisfaction of certain requirements of the rating agencies, transfer its obligations under any of the swaps to another entity.

### **Taxation**

Neither Funding 1 nor the issuing entity is obliged under any of the swaps to gross up payments made by them if withholding taxes are imposed on payments made under the Funding 1 swap or the issuing entity swaps.

Each swap provider will generally be obliged to gross up payments made by it to Funding 1 or the issuing entity, as appropriate, if withholding taxes are imposed on payments made under the Funding 1 swap or the issuing entity swaps. However, if a swap provider is required to gross up a payment under a swap due to a change in law, the relevant swap provider may be entitled to terminate the relevant swap.

### **Governing law**

The Funding 1 swap agreement and the issuing entity swap agreements are and will be (as applicable) governed by English law.

### **Cash management for the mortgages trustee and Funding 1**

The following section contains a summary of the material terms of the cash management agreement. The summary does not purport to be complete and is subject to the provisions of the cash management agreement. Halifax was appointed by the mortgages trustee, Funding 1 and the Funding 1 security trustee to provide cash management services in relation to the mortgages trust and Funding 1.

On the programme date, Funding 1 appointed Halifax (acting as **cash manager**) to provide cash management service to the mortgages trustee and Funding 1 and since the reorganisation date Bank of Scotland has been responsible for such services.

#### **Cash management services provided in relation to the mortgages trust**

The cash manager's duties in relation to the mortgages trust include, but are not limited to:

- (A) determining the current shares of Funding 1 and the seller in the trust property in accordance with the terms of the mortgages trust deed;
- (B) maintaining the following ledgers on behalf of the mortgages trustee:
  - a ledger designated the Funding 1 share/seller share ledger, which records the current shares and share percentage of Funding 1 and the seller in the trust property;
  - the losses ledger, which records losses on the loans;
  - the principal ledger, which records principal receipts on the loans received by the mortgages trustee and payments of principal from the mortgages trustee GIC account to Funding 1 and the seller; and
  - the revenue ledger, which records revenue receipts on the loans received by the mortgages trustee and payments of revenue receipts from the mortgages trustee GIC account to Funding 1 and the seller;
- (C) distributing the mortgages trust available revenue receipts and the mortgages trust available principal receipts to Funding 1 and the seller in accordance with the terms of the mortgages trust deed;
- (D) providing the mortgages trustee, Funding 1, the Funding 1 security trustee and the rating agencies with a quarterly report in relation to the trust property; and
- (E) making all returns and filings in relation to the mortgages trustee and providing or procuring the provision of secretarial services to the mortgages trustee.

#### **Cash management services provided to Funding 1**

The cash manager's duties in relation to Funding 1 include, but are not limited to:

- (A) four business days before each Funding 1 interest payment date, determining:
  - the amount of Funding 1 available revenue receipts to be applied to pay interest and issuing entity fees in relation to the loan tranches (and principal in relation to the start-up loan tranches) under the intercompany loan agreement on the following Funding 1 interest payment date; and
  - the amount of Funding 1 available principal receipts to be applied to repay the loan tranches (excluding the start-up loan tranches) under the intercompany loan agreement on the following Funding 1 interest payment date;
- (B) if required, making drawings under the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any);



- (C) maintaining the following ledgers on behalf of Funding 1:
- the Funding 1 principal ledger, which records the amount of principal receipts received by Funding 1 on each distribution date;
  - the Funding 1 revenue ledger, which records all amounts (other than principal receipts) received by Funding 1 on each distribution date, together with interest received by Funding 1 on its authorised investments or pursuant to the bank account agreement;
  - the Funding 1 general reserve ledger, which records (i) the amount credited to the Funding 1 general reserve fund from a portion of the proceeds of start-up loan tranches on the programme date and the other relevant closing dates, (ii) other amounts standing to the credit of the Funding 1 general reserve fund up to the Funding 1 reserve required amount and (iii) all deposits and other credits in respect of the Funding 1 general reserve fund;
  - the Funding 1 liquidity reserve ledger, which records the amounts credited to the Funding 1 liquidity reserve fund from Funding 1 available revenue receipts and from Funding 1 available principal receipts up to the Funding 1 liquidity reserve fund required amount and drawings made under the Funding 1 liquidity reserve fund;
  - the Funding 1 principal deficiency ledger, which records principal deficiencies arising from losses on the loans which have been allocated to the Funding 1 share or the use of Funding 1 available principal receipts to meet any deficiency in Funding 1 available revenue receipts (as described in “– **Use of Funding 1 principal receipts to pay Funding 1 income deficiency**” above);
  - the intercompany loan ledger, which will record payments of interest and repayments of principal made on each of the loan tranches under the intercompany loan agreement;
  - the Funding 1 cash accumulation ledger, which will record the amount accumulated by Funding 1 from time to time to pay the amounts due on the bullet loan tranches and the scheduled amortisation instalments; and
  - the start-up loan revenue contribution ledger, which will record amounts received by Funding 1 under a start-up loan tranche contributing towards Funding 1 available revenue receipts on the interest payment date immediately following the relevant closing date (which shall, for the avoidance of doubt, not be credited to the Funding 1 general reserve ledger) and amounts paid out by Funding 1 out of such amounts on such interest payment date.
- (D) investing sums standing to the credit of the Funding 1 GIC account in authorised investments as determined by Funding 1, (insofar as permitted by applicable law, including without limitation, the FSMA) the cash manager and the Funding 1 security trustee;
- (E) making withdrawals from the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any) as and when required;
- (F) applying Funding 1 available revenue receipts and Funding 1 available principal receipts in accordance with the relevant Funding 1 priority of payments;
- (G) providing Funding 1, the issuing entity, the Funding 1 security trustee, the issuing entity security trustee and the rating agencies with a quarterly report in relation to Funding 1; and
- (H) making all returns and filings in relation to Funding 1 and providing or procuring the provision of company secretarial and administration services to Funding 1.

For the definitions of Funding 1 available revenue receipts and Funding 1 available principal receipts, see “**Cashflows**” above.

### **Periodic audit**

The cash manager's external auditors reviews the mortgages trustee's and Funding 1's bank accounts and account activity as part of their periodic audits.

### **Compensation of cash manager**

The cash manager is paid a fee (inclusive of VAT, if any) of 0.025 per cent. per annum of the aggregate of the principal amount outstanding of the rated loan tranches under the intercompany loan agreement for the services provided to the mortgages trustee and Funding 1, which is paid by the mortgages trustee unless otherwise agreed between the mortgages trustee, Funding 1, the Funding 1 security trustee and the cash manager.

In addition, the cash manager is entitled to be reimbursed for any expenses or other amounts properly incurred by it in carrying out its duties. The cash manager is paid by (a) the mortgages trustee prior to payment of mortgages trust available revenue receipts to Funding 1 on each distribution date and (b) Funding 1 prior to payment of interest due on the loan tranches on each Funding 1 interest payment date.

### **Resignation of cash manager**

The cash manager may resign only on giving 12 months' written notice to the Funding 1 security trustee, Funding 1 and the mortgages trustee and if (among other things) a substitute cash manager has been appointed and a new cash management agreement is entered into on terms substantially the same as the cash management agreement and the ratings of the notes at that time would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of that replacement (unless otherwise agreed by an extraordinary resolution of the noteholders of each class).

### **Termination of appointment of cash manager**

The mortgages trustee, Funding 1 or the Funding 1 security trustee may, upon written notice to the cash manager, terminate the cash manager's rights and obligations immediately if any of the following events occurs:

- the cash manager defaults in the payment of any amount due and fails to remedy the default for a period of three London business days after the earlier of the cash manager becoming aware of the default and receiving a notice from the mortgages trustee, Funding 1 or the Funding 1 security trustee requiring the same to be remedied;
- the cash manager fails to comply with any of its other obligations under the cash management agreement which the Funding 1 security trustee is directed by the issuing entity security trustee, which is directed by the note trustee, is, in the opinion of the note trustee, materially prejudicial to the noteholders and does not remedy that failure within 20 London business days after the earlier of becoming aware of the failure and receiving a notice from Funding 1, the Funding 1 security trustee or the mortgages trustee requiring the same to be remedied; or
- Bank of Scotland, while acting as the cash manager, suffers an insolvency event.

If the appointment of the cash manager is terminated or it resigns, the cash manager must deliver its books of account relating to the loans to or at the direction of the mortgages trustee, Funding 1 or the Funding 1 security trustee, as the case may be. The cash management agreement will terminate automatically when Funding 1 has no further interest in the trust property and the intercompany loan has been repaid or otherwise discharged.

### **Governing law**

The cash management agreement is governed by English law.

### **Cash management for the issuing entity**

The following section contains a summary of the material terms of the issuing entity cash management agreement. The summary does not purport to be complete and is subject to the provisions of the issuing entity cash management agreement.

On the programme date, the issuing entity appointed Halifax (acting as **issuing entity cash manager**) to provide cash management services to the issuing entity and since the reorganisation date Bank of Scotland has been responsible for such services.

#### **Cash management services to be provided to the issuing entity**

The issuing entity cash manager's duties include, but are not limited to:

- (A) four business days before each quarterly interest payment date, determining:
- the amount of issuing entity revenue receipts to be applied to pay interest on the notes and the issuing entity subordinated loans on the following quarterly interest payment date and to pay amounts due to other creditors of the issuing entity; and
  - the amount of issuing entity principal receipts to be applied to repay the notes and issuing entity subordinated loans on the following quarterly interest payment date;
- (B) applying issuing entity revenue receipts and issuing entity principal receipts in accordance with the relevant issuing entity priority of payments set out in the issuing entity deed of charge;
- (C) maintaining the following ledgers on behalf of the issuing entity:
- the issuing entity revenue ledger, which records issuing entity revenue receipts (excluding certain issuing entity fees to be paid by Funding 1 on each Funding 1 interest payment date under the terms of the intercompany loan agreement (other than in respect of any non-subordinated termination payment due by the issuing entity in respect of any issuing entity swap), which will be credited to the issuing entity expense ledger) received and paid out by the issuing entity. The issuing entity revenue ledger will be split into sub-ledgers corresponding to each series and class of notes issued by the issuing entity, each issuing entity subordinated loan advanced to the issuing entity and each issuing entity start-up loan advanced to the issuing entity and will record any interest received from Funding 1 in respect of a loan tranche, any payment due by the issuing entity to an issuing entity swap provider in relation to the corresponding class of notes (other than in respect of any subordinated termination payment by the issuing entity in respect of such issuing entity swap) and any principal received from Funding 1 in respect of a start-up loan tranche will be credited to the relevant corresponding sub-ledger;
  - the issuing entity principal ledger, which records all Funding 1 available principal receipts received by the issuing entity from Funding 1 constituting principal repayments on a loan tranche (other than a start-up loan tranche). All such Funding 1 available principal receipts in relation to each loan tranche (other than a start-up loan tranche) will be credited to a sub-ledger (in respect of the related series and class of notes or, as applicable issuing entity subordinated loan);
  - the issuing entity expense ledger, which records payments of certain issuing entity fees received from Funding 1 under the intercompany loan (other than in respect of any non-subordinated termination payment due by the issuing entity in respect of any issuing entity swap) and payments made by the issuing entity in accordance with the applicable issuing entity priority of payments; and
  - the issuing entity sub-ledgers, which record payments of interest and repayments of principal on each series and class of notes and any payment of issuing entity fees in respect of any termination payment due by the issuing entity in respect of a corresponding issuing entity swap (other than in respect of any subordinated termination payment by the issuing entity in respect of such issuing entity swap);

- (D) providing the issuing entity, the issuing entity security trustee and the rating agencies with quarterly reports in relation to the issuing entity;
- (E) making all returns and filings required to be made by the issuing entity and providing or procuring the provision of company secretarial and administration services to the issuing entity;
- (F) arranging payment of all fees to the London Stock Exchange or, as applicable, the FSA; and
- (G) if necessary, performing all currency and interest rate conversions (whether it be a conversion from sterling to another specified currency or vice versa, or floating rates of interest to fixed rates of interest or vice versa) free of charge, cost or expense at the relevant exchange rate.

#### **Periodic audit**

The issuing entity cash manager's external auditors reviews the issuing entity bank accounts and account activity as part of their periodic audits.

#### **The issuing entity's bank accounts**

On the programme date, the issuing entity established a sterling bank account in its name with Bank of Scotland acting through its offices at 116 Wellington Street, Leeds LS1 4LT, the right, benefit and interest of which is assigned to the issuing entity security trustee under the issuing entity deed of charge (the **issuing entity transaction account** and, together with any other accounts of the issuing entity from time to time, the **issuing entity bank accounts**). The issuing entity may, with the prior written consent of the issuing entity security trustee, open additional or replacement bank accounts.

The issuing entity bank accounts may be required to be transferred to an alternative bank if the short-term, unguaranteed and unsecured ratings of the issuing entity account bank falls below F1 by Fitch, P-1 by Moody's or A-1+ by Standard & Poor's, unless each rating agency confirms that its then current rating of the notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified as a result of such ratings falling below these minimum ratings.

#### **Compensation of issuing entity cash manager**

The issuing entity cash manager is paid a fee (inclusive of VAT, if any) of 0.025 per cent. per annum of the principal amount outstanding of the notes for its services which is paid in arrears on each quarterly interest payment date.

In addition, the issuing entity cash manager is entitled to be reimbursed for any expenses or other amounts properly incurred by it in carrying out its duties. The issuing entity cash manager is paid by the issuing entity in priority to amounts due on the notes.

#### **Resignation of issuing entity cash manager**

The issuing entity cash manager may resign only on giving 12 months' written notice to the issuing entity security trustee and the issuing entity and if a substitute issuing entity cash manager has been appointed and a new issuing entity cash management agreement is entered into on terms substantially the same as the issuing entity cash management agreement and the ratings of the notes at that time would not be downgraded, withdrawn, or (in the case of S&P and Moody's) qualified as a result of that replacement (unless otherwise agreed by an extraordinary resolution of the noteholders of each class).

#### **Termination of appointment of issuing entity cash manager**

The issuing entity or the issuing entity security trustee may, upon written notice to the issuing entity cash manager, terminate the issuing entity cash manager's rights and obligations immediately if any of the following events occurs:

- the issuing entity cash manager defaults in the payment of any amount due and fails to remedy the default for a period of three London business days after the earlier of the issuing entity cash manager becoming aware of the default and receipt by the issuing entity cash manager of written notice from the issuing entity or the issuing entity security trustee requiring the same to be remedied;
- the issuing entity cash manager fails to comply with any of its other obligations under the issuing entity cash management agreement which the issuing entity security trustee is directed by the note trustee is, in the opinion of the note trustee, materially prejudicial to noteholders and does not remedy

that failure within 20 London business days after the earlier of becoming aware of the failure and receiving a notice from the issuing entity or the issuing entity security trustee requiring the same to be remedied; or

- the issuing entity cash manager suffers an insolvency event.

If the appointment of the issuing entity cash manager is terminated or it resigns, the issuing entity cash manager must deliver its books of account relating to the notes to or at the direction of the issuing entity security trustee. The issuing entity cash management agreement will terminate automatically when the notes have been fully redeemed.

### **Governing law**

The issuing entity cash management agreement is governed by English law.

## Description of the note trust deed

### General

The principal agreement governing the notes is the note trust deed which was entered into on the programme date between the issuing entity and the note trustee (the **note trust deed**). The note trust deed has four primary functions. It:

- constitutes the notes;
- sets out the covenants of the issuing entity in relation to the notes;
- sets out the enforcement and post-enforcement procedures relating to the notes; and
- sets out the appointment, powers and responsibilities of the note trustee.

The following section contains a summary of the material terms of the note trust deed. The summary does not purport to be complete and is subject to the provisions of the note trust deed.

The note trust deed sets out the form of the global notes and the definitive notes. It also sets out the terms and conditions and the conditions for the issue of definitive notes and/or the cancellation of any notes. It stipulates, among other things, that the paying agents, the registrar, the transfer agent and the agent bank have been appointed. The detailed provisions regulating these appointments are contained in the paying agent and agent bank agreement.

The note trust deed also contains covenants made by the issuing entity in favour of the note trustee and the noteholders. The main covenants are that the issuing entity will (subject to the deferral provisions contained in the terms and conditions of the notes) pay interest and repay principal on each of the notes when due. Other covenants are included to, among other things, ensure that the issuing entity remains insolvency-remote and to give the note trustee access to all information and reports that it may need in order to discharge its responsibilities in relation to the noteholders. Some of the covenants also appear in the terms and conditions of the notes. See Condition 3 (Covenants), in “**Terms and conditions of the notes**” below. The issuing entity also covenants that it will (in respect of those notes that are listed) do all things necessary to maintain the listing of the notes on the official list of the UK Listing Authority and to maintain the trading of those notes on the London Stock Exchange’s Regulated Market. In addition, the issuing entity covenants to keep in place a common depositary, paying agents and an agent bank.

The note trust deed provides that the interests of the holders of the class A notes or other most senior class of notes outstanding at the relevant time take precedence over the interests of the other classes of noteholders then outstanding. Certain basic terms of each class of notes may not be amended without the consent of the majority of the holders of that class of note and the consent of the majority of the holders of the other classes of affected notes outstanding. This is described further in Condition 11 (Meetings of Noteholders, Modifications and Waiver) in “**Terms and conditions of the notes**” below.

The note trust deed also sets out the terms on which the note trustee is appointed, the indemnification of the note trustee, the payment it receives and the extent of the note trustee’s authority to act beyond its statutory powers under English law. The note trustee is also given the ability to appoint a co-trustee or any delegate or agent in the execution of any of its duties under the note trust deed. The note trust deed also sets out the circumstances in which the note trustee may resign or retire.

### Governing law

The note trust deed is governed by English law.

## The notes and the global notes

The issuance of notes from time to time has been authorised by a resolution of the board of directors of the issuing entity passed on 3 April 2007. While the material terms of the notes, the definitive notes and the global notes are described in this base prospectus, the statements set out in this section with regard to the notes, the definitive notes and the global notes are subject to the detailed provisions of the note trust deed. The note trust deed includes the form of the global notes and the form of definitive notes. The note trust deed includes provisions which enable it to be modified or supplemented and any reference to the note trust deed is a reference also to the document as modified or supplemented in accordance with its terms.

A paying agent and agent bank agreement between the issuing entity, the note trustee, Deutsche Bank AG, London Branch as the principal paying agent and the agent bank and Deutsche Bank Trust Company Americas as the US paying agent, the registrar, the transfer agent and the exchange agent regulates how payments are made on the notes and how determinations and notifications will be made. The note trust deed and the paying agent and agent bank agreement were entered into on the programme date and the parties thereto include, on an ongoing basis, any successor party appointed in accordance with their terms.

Each class of each series of notes is represented initially by a global note in registered form without interest coupons attached. A series and class of notes is initially represented by a Rule 144A global note or a Reg S global note or both, as specified in the relevant final terms. The Rule 144A notes are each represented by a Rule 144A global note. The Reg S notes are each represented by a Reg S global note.

The Rule 144A global notes and/or the Reg S global notes, as specified in the applicable final terms, are and will be deposited on behalf of the beneficial owners of those notes with Deutsche Bank Trust Company Americas, as the custodian for, and registered in the name of Cede & Co. as nominee of, The Depository Trust Company – called **DTC**. On confirmation from the custodian that it holds such global note, DTC will record book-entry interests in the beneficial owner's account or the participant account through which the beneficial owner holds its interests in such global notes. These book-entry interests represent and will represent the beneficial owner's beneficial interest in the relevant global note.

The Reg S global notes and/or the Rule 144A global notes are and will be deposited on behalf of the beneficial owners of those notes with, and registered in the name of a nominee of the common depository for Clearstream Banking, société anonyme (**Clearstream, Luxembourg**), Euroclear Bank S.A./N.V. (**Euroclear**) and any alternative clearing system agreed by the issuing entity. On confirmation from the common depository that it holds such global note, Clearstream, Luxembourg and/or Euroclear, as the case may be, records and will record book-entry interests in the beneficial owner's account or the participant account through which the beneficial owner holds its interests in such global note. These book-entry interests represent and will represent the beneficial owner's beneficial interest in the relevant global note.

The amount of notes represented by each global note is evidenced by the register maintained for that purpose by the registrar. Together, the notes represented by the global notes and any outstanding definitive notes are and will equal the aggregate principal amount of the notes outstanding at any time. However, except as described under “–**Definitive notes**” below, definitive certificates representing individual notes shall not be issued.

Beneficial owners may hold their interests in the global notes only through DTC, Clearstream, Luxembourg or Euroclear, as applicable, or through any alternative clearing system agreed by the issuing entity, or indirectly through organisations that are participants in any of those systems. Ownership of these beneficial interests in a global note are and will be shown on, and the transfer of that ownership will be effected only through, records maintained by DTC, Clearstream, Luxembourg or Euroclear (with respect to interests of their participants) and the records of their participants (with respect to interests of persons other than their participants) or by any alternative clearing system agreed by the issuing entity. By contrast, ownership of definitive notes and direct interests in a global note will be shown on, and the transfer of that ownership will be effected through, the register maintained by the registrar. Because of this holding structure of notes, beneficial owners of notes may look only to DTC, Clearstream, Luxembourg or Euroclear, as applicable, or their respective participants for their beneficial entitlement to those notes or to any alternative clearing system agreed by the issuing entity. The issuing entity expects that DTC, Clearstream, Luxembourg or Euroclear will take any action permitted to be taken by a beneficial owner of notes only at the direction of one or more participants to whose account the interests in a global note is credited and only in respect of that portion of the aggregate principal amount of notes as to which that participant or those participants has or have given that direction.

Beneficial interests in a Reg S global note may be exchanged for beneficial interests in the corresponding Rule 144A global note only if such exchange occurs in connection with a transfer of the offered notes pursuant to Rule 144A and the transferring noteholder first delivers to the transfer agent and registrar (i) instructions given in accordance with the procedures of Euroclear, Clearstream, Luxembourg and/or DTC, as the case may be, directing the transfer agent and registrar to credit or cause to be credited a beneficial interest in the Rule 144A

global note in an amount equal to the beneficial interest in the corresponding Reg S global note to be exchanged or transferred, (ii) a written order given in accordance with the procedures of Euroclear, Clearstream, Luxembourg and/or DTC, as the case may be, containing information regarding the account to be credited with such increase and the name of such account and (iii) prior to the first business day that is 40 days following the later of the commencement of the offering and the relevant closing date (the **distribution compliance period**), a written certificate in the form required by the note trust deed to the effect that the transfer is being made to a person who the transferor reasonably believes is a QIB purchasing for its own account or the account of a QIB in a transaction meeting the requirements of Rule 144A and in accordance with all applicable securities laws of the states of the United States and other jurisdictions.

Beneficial interests in the Rule 144A global note may be transferred to a person who takes delivery in the form of an interest in a Reg S global note, whether before or after the distribution compliance period, only if the transferring noteholder first delivers to the transfer agent and registrar (i) instructions given in accordance with DTC's, Euroclear's and/or Clearstream's, as applicable, procedures from or on behalf of beneficial owners of the Rule 144A global note, directing the transfer agent and registrar to credit or cause to be credited a beneficial interest in the corresponding Reg S global note in an amount equal to the beneficial interest in the Rule 144A global note to be exchanged or transferred, (ii) a written order in accordance with the clearing agency's procedures containing information regarding the DTC, Euroclear or Clearstream, Luxembourg, as applicable, account to be credited with such increase and the name of such account and (iii) a written certificate in the form required by the note trust deed to the effect that such transfer is being made in accordance with Rule 903 or Rule 904 of Regulation S.

Transfers involving an exchange of a beneficial interest in Reg S global note for a beneficial interest in the corresponding Rule 144A global note or vice versa will be effected in DTC, Euroclear or Clearstream, Luxembourg (as applicable) by means of an instruction originated by the transfer agent and registrar through the facilities of DTC, Euroclear or Clearstream, Luxembourg (as applicable).

Any beneficial interest in one of the global notes that is transferred to a person who takes delivery in the form of an interest in the other of the global notes will, upon transfer, cease to be an interest in such global note and will become an interest in the other global note and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to a beneficial interest in such other global note for so long as it remains such an interest.

Beneficial owners will be entitled to the benefit of, will be bound by and will be deemed to have notice of, all the provisions of the note trust deed and the paying agent and agent bank agreement. Beneficial owners can see copies of these agreements at the principal office for the time being of the principal paying agent, which is, as at the date of this base prospectus, Winchester House, 1 Great Winchester Street, London EC2N 2DB and at the specified office for the time being of each of the other paying agents. Pursuant to its obligations under the listing rules made by the UK Listing Authority, the issuing entity will maintain a paying agent in the United Kingdom until the date on which the notes are finally redeemed for as long as any note is outstanding. The issuing entity will endeavour to maintain a paying agent in a member state of the European Union that will not be obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive.

## **Payment**

Principal and interest payments on the global notes will be made via the paying agents to DTC, Euroclear or Clearstream, Luxembourg (as applicable) or to any alternative clearing system agreed by the issuing entity or their respective nominee, as the registered holder of the global notes. DTC's practice is to credit its participants' accounts on the applicable interest payment date according to their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on that interest payment date.

Payments by DTC, Clearstream, Luxembourg and Euroclear participants, or by any participants of any alternative clearing system agreed by the issuing entity, to the beneficial owners of notes will be governed by standing instructions, customary practice, and any statutory or regulatory requirements as may be in effect from time to time, as is now the case with securities held by the accounts of customers registered in "street name". These payments will be the responsibility of the DTC, Clearstream, Luxembourg or Euroclear participant or the participant of such alternative clearing system and not of DTC, Clearstream, Luxembourg, Euroclear, any such alternative clearing system, any paying agent, the note trustee or the issuing entity. Neither the issuing entity, the note trustee nor any paying agent will have any responsibility or liability for any aspect of the records of DTC, Clearstream, Luxembourg or Euroclear or such alternative clearing system relating to payments made by DTC, Clearstream, Luxembourg or Euroclear on account of beneficial interests in the global notes or for maintaining, supervising or reviewing any records of DTC, Clearstream, Luxembourg or Euroclear or such alternative clearing system relating to those beneficial interests.



DTC will only process payments of principal and interest in US dollars. Payments in US dollars of principal and interest in respect of a global note accepted by DTC will be made to the order of DTC or its nominee as the registered holder of such note. In the case of any payment in a currency other than US dollars in respect of a global note accepted by DTC, payment will be made by the exchange agent and the exchange agent will (in accordance with express written instructions received by it) remit all or a portion of such payment for credit directly to the beneficial holders of interests in the global note in the currency in which such payment was made and/or cause all or a portion of such payment to be converted into US dollars and credited to the applicable participants' accounts.

### **Clearance and settlement**

#### *DTC*

DTC has advised the issuing entity, the dealers and the managers that it intends to follow the following procedures:

DTC acts as securities depository for the global notes as specified in the applicable final terms. Such notes were and will be issued as securities registered in the name of Cede & Co. (DTC's nominee).

DTC has advised the issuing entity that it is a:

- limited-purpose trust company organised under the New York Banking Law;
- **banking organisation** within the meaning of the New York Banking Law;
- member of the Federal Reserve System;
- **clearing corporation** within the meaning of the New York Uniform Commercial Code; and
- **clearing agency** registered under the provisions of Section 17A of the US Securities Exchange Act of 1934, as amended (the **Exchange Act**).

DTC holds securities for its participants and facilitates the clearance and settlement among its participants of securities transactions, including transfers and pledges, in deposited securities through electronic book-entry changes in its participants' accounts. This eliminates the need for physical movement of securities certificates. DTC participants include securities brokers and dealers, banks, trust companies, clearing corporations and other organisations. Indirect access to the DTC system is also available to others, including securities brokers and dealers, banks and trust companies that clear through or maintain a custodial relationship with a participant, either directly or indirectly. The rules applicable to DTC and its participants are on file with the SEC. Transfers between participants on the DTC system will occur under DTC rules.

Purchases of notes under the DTC system must be made by or through DTC participants, which will receive a credit for the notes on DTC's records. The ownership interest of each actual beneficial owner is in turn to be recorded on the DTC participants' and indirect participants' records. Beneficial owners will not receive written confirmation from DTC of their purchase. However, beneficial owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the DTC participant or indirect participant through which the beneficial owner entered into the transaction. Transfer of ownership interests in the global notes are to be accomplished by entries made on the books of DTC participants acting on behalf of beneficial owners. Beneficial owners will not receive certificates representing their ownership interest in notes unless use of the book-entry system for the notes described in this section is discontinued.

To facilitate subsequent transfers, all global notes deposited with DTC are registered in the name of DTC's nominee, Cede & Co. The deposit of these global notes with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the ultimate beneficial owners of the notes. DTC's records reflect only the identity of the DTC participants to whose accounts the beneficial interests are credited, which may or may not be the actual beneficial owners of the notes. The DTC participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to DTC participants, by DTC participants to indirect participants and by DTC participants and indirect participants to beneficial owners, will be governed by arrangements among them and by any statutory or regulatory requirements in effect from time to time.

Redemption notices for the global notes will be sent to DTC. If less than all of those global notes are being redeemed by investors, DTC's practice is to determine by lot the amount of the interest of each participant in those global notes to be redeemed.

Neither DTC nor Cede & Co. will consent or vote on behalf of the global notes. Under its usual procedures, DTC will mail an omnibus proxy to the issuing entity as soon as possible after the record date, which assigns the consenting or voting rights of Cede & Co. to those DTC participants to whose accounts the book-entry interests are credited on the record date, identified in a list attached to the proxy.

The issuing entity understands that under existing industry practices, when the issuing entity requests any action of noteholders or when a beneficial owner desires to give or take any action which a noteholder is entitled to give or take under the note trust deed, DTC generally will give or take that action, or authorise the relevant participants to give or take that action, and those participants would authorise beneficial owners owning through those participants to give or take that action or would otherwise act upon the instructions of beneficial owners through them.

#### *Clearstream, Luxembourg and Euroclear*

Clearstream, Luxembourg and Euroclear each hold securities for their participating organisations and facilitate the clearance and settlement of securities transactions between their respective participants through electronic book-entry changes in accounts of those participants, thereby eliminating the need for physical movement of securities. Clearstream, Luxembourg and Euroclear provide various services, including safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Clearstream, Luxembourg and Euroclear also deal with domestic securities markets in several countries through established depository and custodial relationships. Clearstream, Luxembourg and Euroclear have established an electronic bridge between their two systems across which their respective participants may settle trades with each other. Transactions may be settled in Clearstream, Luxembourg and Euroclear in any of numerous currencies, including United States dollars. Transfer between participants on the Clearstream, Luxembourg system and participants of the Euroclear system will occur under their respective rules and operating procedures.

Clearstream, Luxembourg is incorporated under the laws of Luxembourg as a professional depository. Clearstream, Luxembourg participants are financial institutions around the world, including underwriters, securities brokers and dealers, banks, trust companies and clearing corporations. Indirect access to Clearstream, Luxembourg is also available to others, including banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Clearstream, Luxembourg participant, either directly or indirectly.

The Euroclear system was created in 1968 to hold securities for its participants and to clear and settle transactions between Euroclear participants through simultaneous electronic book-entry delivery against payment. The Euroclear system is operated by Euroclear, under contract with Euroclear Clearance System, Co-operative, a Belgium co-operative corporation (the **Euroclear co-operative**). All operations are conducted by Euroclear. All Euroclear securities clearance accounts and Euroclear cash accounts are accounts with Euroclear, not the Euroclear co-operative. The board of the Euroclear co-operative establishes policy for the Euroclear system.

Euroclear participants include banks – including central banks – securities brokers and dealers and other professional financial intermediaries. Indirect access to the Euroclear system is also available to other firms that maintain a custodial relationship with a Euroclear participant, either directly or indirectly.

Securities clearance accounts and cash accounts with Euroclear are governed by the Terms and Conditions Governing use of Euroclear and the related Operating Procedures of the Euroclear system. These terms and conditions govern transfers of securities and cash within the Euroclear system, withdrawal of securities and cash from the Euroclear system and receipts of payments for securities in the Euroclear system. All securities in the Euroclear system are held on a fungible basis without attribution of specific certificates to specific securities clearance accounts. Euroclear acts under these terms and conditions only on behalf of Euroclear participants and has no record of or relationship with persons holding through Euroclear participants.

The information in this section concerning DTC and DTC's book-entry system, and the book-entry system of any alternative clearing system agreed by the issuing entity, Clearstream, Luxembourg and Euroclear has been obtained from sources that the issuing entity believes to be reliable, but the issuing entity takes no responsibility for the accuracy thereof.

As the holders of book-entry interests, beneficial owners do not have the right under the note trust deed to act on solicitations by the issuing entity for action by noteholders. Beneficial owners will only be able to act to the extent they receive the appropriate proxies to do so from DTC, Clearstream, Luxembourg or Euroclear or any alternative clearing system agreed by the issuing entity or, if applicable, their respective participants. No

assurances are made about these procedures or their adequacy for ensuring timely exercise of remedies under the note trust deed.

No beneficial owner of an interest in a global note will be able to transfer that interest except in accordance with applicable procedures, in addition to those provided for under the note trust deed, of DTC, Clearstream, Luxembourg and Euroclear, as applicable. The laws of some jurisdictions require that some purchasers of securities take physical delivery of those securities in definitive form. These laws and limitations may impair the ability to transfer beneficial interests in the global notes.

#### *Global clearance and settlement procedures*

##### **Initial settlement**

The Rule 144A global notes and/or the Reg S global notes, as specified in the applicable final terms, will be delivered at initial settlement to Deutsche Bank Trust Company Americas as custodian for DTC and the Reg S global notes and/or the Rule 144A global notes, as specified in the applicable final terms, will be delivered to a common depository for Clearstream, Luxembourg and Euroclear or any alternative clearing system agreed by the issuing entity. Customary settlement procedures will be followed for participants of each system at initial settlement. Notes will be credited to investors' securities accounts on the settlement date against payment in same-day funds.

##### **Secondary trading**

Secondary market sales of book-entry interests in notes between DTC participants will occur in accordance with DTC rules and will be settled using the procedures applicable to conventional United States corporate debt obligations.

Although DTC, Clearstream, Luxembourg and Euroclear have agreed to these procedures to facilitate transfers of interests in securities among participants of DTC, Clearstream, Luxembourg, Euroclear and any alternative clearing system agreed by the issuing entity, they are not obligated to perform these procedures. Additionally, these procedures may be discontinued at any time. None of the issuing entity, the note trustee, any agent, the dealers, the managers or any affiliate of any of the foregoing, or any person by whom any of the foregoing is controlled for the purposes of the Securities Act, will have any responsibility for the performance by DTC, Clearstream, Luxembourg, Euroclear, any alternative clearing system agreed by the issuing entity or their respective direct or indirect participants or accountholders of their respective obligations under the rules and procedures governing their operations or for the sufficiency for any purpose of the arrangements described herein.

##### **Definitive notes**

Beneficial owners of global notes will only be entitled to receive definitive notes (such as exchanged global notes, the **definitive notes**) under the following limited circumstances:

- as a result of a change in UK law, the issuing entity or any paying agent is or will be required to make any deduction or withholding on account of tax from any payment on the notes that would not be required if the notes were in definitive form;
- in the case of the global notes held by Cede & Co., as nominee for DTC, DTC notifies the issuing entity that it is unwilling or unable to hold such global notes or is unwilling or unable to continue as, or has ceased to be, a clearing agency under the Exchange Act and, in each case, the issuing entity cannot appoint a successor within 90 days; or
- in the case of the global notes held by a nominee of the common depository, Clearstream, Luxembourg and Euroclear are closed for business for a continuous period of 14 days or more (other than by reason of legal holidays) or announce an intention to cease business permanently or do in fact do so and no alternative clearing system satisfactory to note trustee is available.

In no event will definitive notes in bearer form be issued. Any definitive notes will be issued in registered form in minimum denominations as specified in the applicable final terms. Any definitive notes will be registered in that name or those names as the registrar shall be instructed by DTC, Clearstream, Luxembourg, Euroclear and any alternative clearing system agreed by the issuing entity, as applicable. It is expected that these instructions will be based upon directions received by DTC, Clearstream, Luxembourg, Euroclear and any alternative clearing system agreed by the issuing entity, from their participants reflecting the ownership of book-entry interests. To the extent

permitted by law, the issuing entity, the note trustee and any paying agent shall be entitled to treat the person in whose name any definitive notes are registered as the absolute owner thereof. The paying agent and agent bank agreement contains provisions relating to the maintenance by a registrar of a register reflecting ownership of the notes and other provisions customary for a registered debt security.

Any person receiving definitive notes will not be obligated to pay or otherwise bear the cost of any tax or governmental charge or any cost or expense relating to insurance, postage, transportation or any similar charge, which will be solely the responsibility of the issuing entity. No service charge will be made for any registration of transfer or exchange of any definitive notes.

## Form of Final Terms

Set out below is the form of final terms which, subject to any necessary amendment, will be completed for each issuance of notes issued under the programme.

**Final Terms dated [●]**

### PENDEFORD MASTER ISSUER PLC

*(Incorporated with limited liability in England and Wales with registered number 06121308)*

### Mortgage Backed Note Programme

#### [●]-[●] Notes

Series	Class	Interest rate	Initial principal amount	Issue price (%)	Scheduled redemption dates	Maturity date
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]
[●]	[●]	[●]	[●]	[●]	[●]	[●]

Terms used herein shall be deemed to be defined as such for the purposes of the conditions set forth in the base prospectus dated [●] 2008 which constitutes a base prospectus (the **base prospectus**) for the purposes of the Prospectus Directive (Directive 2003/71/EC) (the **Prospectus Directive**). This document constitutes the final terms (the **final terms**) of the series and classes notes of Pendeford Master Issuer plc (the **issuing entity**) described herein for the purposes of Article 5.4 of the Prospectus Directive and must be read in conjunction with the base prospectus. Full information on the issuing entity and the offer of the series and classes of notes subject thereof is only available on the basis of the combination of these final terms and the base prospectus. The base prospectus is available for viewing at the offices of the Principal Paying Agent, Deutsche Bank AG, London Branch at Winchester House, 1 Great Winchester Street, London EC2N 2DB, United Kingdom and copies may be obtained from the registered office of the issuing entity at 35 Great St. Helen's London EC3A 6AP.

*[Include whichever of the following apply or specify as "Not Applicable" (N/A). Note that the numbering should remain as set out below, even if "Not Applicable" is indicated for individual paragraphs or subparagraphs. Italics denote directions for completing the Final Terms.]*

*[When adding any other final terms or information consideration should be given as to whether such terms or information constitute "significant new factors" and consequently trigger the need for a supplement to the base prospectus under Article 16 of the Prospectus Directive.]*

*[If the Notes have a maturity of less than one year from the date of their issue, the minimum denomination must be £100,000 or its equivalent in any other currency.]*

**Arranger for the programme  
HBOS  
Joint Lead Managers for [specify Series and Class]**

[•]

[•]

[•]

**Co-Managers for [specify Series and Class]**

[•]

[•]

[•]

- |     |   |   |
|-----|---|---|
| 1.  | Series and Class:   | [•]   |
| 2.  | Issuer:   | Pendeford Master Issuer plc   |
| 3.  | Specified Currency or Currencies:                               | [•]   |
| 4.  | Initial Principal Amount:                                       | [•]   |
| 5.  | (a) Issue Price:  | [•] per cent. of the Initial Principal Amount [plus accrued interest from [insert date] (if applicable)]  |
|     | (b) Gross proceeds:   | [•]   |
| 6.  | Ratings (Fitch/Moody's/Standard & Poor's):                      | [•]/[•]/[•] (the above disclosure should reflect the rating allocated to the Notes of the type being issued under the programme generally or, where the issue has been specifically rated, that rating) |
| 7.  | Specified Denominations:  | [•]   |
| 8.  | (a) Closing Date:   | [•]   |
|     | (b) Interest Commencement Date:                                 | [•]   |
| 9.  | Final Maturity Date:  | [Fixed rate – specify date/Floating rate – Interest Payment Date falling in or nearest to [specify month]]  |
| 10. | Interest Basis:   | [[•] per cent. Fixed Rate]<br>[[LIBOR/EURIBOR] Floating Rate]<br>[Zero Coupon]<br>[specify other]<br>(further particulars specified below)  |
| 11. | Redemption/Payment Basis:                                       | [Bullet Redemption]<br>[Scheduled Redemption]<br>[Pass-Through]<br>[specify other]  |
| 12. | Change of Interest Basis or Redemption/Payment Basis:           | [Not applicable - Specify details of any provision for change of Notes into another Interest Basis or Redemption/Payment Basis]   |
| 13. | (a) Listing:  | [London Stock Exchange's Regulated Market/specify other/none]   |
|     | (b) Estimate of total expenses related to admission to trading: | [•]   |
| 14. | Method of distribution:   | [Syndicated/Non-syndicated]   |

PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE

15. Fixed Rate Note Provisions: [Applicable/Not Applicable]  
*(If not applicable, delete the remaining subparagraphs of this paragraph)*
- (a) Rate(s) of Interest: [●] per cent. per annum [payable  
annually/semi-annually/quarterly] in arrear]  
*(If payable other than quarterly, consider amending Condition 4.1 (Interest on Fixed Rate Notes))*
- (b) Interest Payment Date(s): [[●], [●], [●] and [●] in each year up to and  
including the Final Maturity Date *(all Notes other than Money Market Notes)*
- [The [●] day of each calendar month in each year up to and including the Final Maturity Date or, following the occurrence of a Pass-Through  
Trigger Event, [●], [●], [●] and [●] in each year up to and including the Final Maturity Date] *(if Money Market Notes)*  
*(N.B. This will need to be amended in the case of long or short coupons)*
- (c) Fixed Coupon Amount(s): [●] per [●] in nominal amount
- (d) Broken Amount(s): *[Insert particulars of any initial or final broken interest amounts which do not correspond with the Fixed Coupon Amount]*
- (e) Day Count Fraction: [30/360 or Actual/Actual (ICMA) or [specify other]]
- (f) Determination Date(s): [●] in each year  
*[Insert regular Interest Payment Dates, ignoring Closing Date or Final Maturity Date in the case of a long or short first or last coupon]*  
*N.B. This will need to be amended in the case of regular Interest Payment Dates which are not of equal duration*  
*N.B. Only relevant where Day Count Fraction is Actual/Actual (ICMA)]*
- (g) Other terms relating to the method of calculating interest for Fixed Rate Notes: *[None/Give details]*
16. Floating Rate Note Provisions: [Applicable/Not Applicable]  
*(If not applicable, delete the remaining subparagraphs of this paragraph)*
- (a) Interest Payment Dates: [[●], [●], [●] and [●] in each year up to and  
including the Final Maturity Date] *(all Notes other than Money Market Notes)*
- [The [●] day of each calendar month in each year up to and including the Final Maturity Date or, following the occurrence of a Pass-Through  
Trigger Event, [●], [●], [●] and [●] in each year up to and including the Final Maturity Date] *(if Money Market Notes)*
- (b) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/[specify other]]

- (c) Manner in which the Rate of Interest and Interest Amount is to be determined: [Screen Rate Determination/ISDA Determination/*specify other*]
- (d) Party responsible for calculating the Rate of Interest and Interest Amount (if not the Agent Bank): [●]
- (e) Screen Rate Determination:
- Reference Rate: [●]  
*(Either LIBOR, EURIBOR or other, although additional information is required if other – including fallback provisions in the Paying Agent and Agent Bank Agreement)*
  - Interest Determination Date(s): [●]  
*(Second London business day prior to the start of each Interest Period if LIBOR (other than Sterling or euro LIBOR), first day of each Interest Period if Sterling LIBOR and the second day on which the TARGET System is open prior to the start of each Interest Period if EURIBOR or euro LIBOR)*
  - Relevant Screen Page: [●]  
*(In the case of EURIBOR, if not, Reuters' page EURIBORO1 ensure it is a page which shows a composite rate or amend the fallback provisions appropriately)*
- (f) ISDA Determination:
- Floating Rate Option: [●]
  - Designated Maturity: [●]
  - Reset Date: [●]
- (g) Margin(s): [ +/- ] [●] per cent. per annum
- (h) Minimum Rate of Interest: [Not Applicable/[●] per cent. per annum]
- (i) Maximum Rate of Interest: [Not Applicable/[●] per cent. per annum]
- (j) Step-Up Date [Not Applicable/Interest Payment Date occurring in [●]]  
*(If not applicable, delete the remaining subparagraphs of this paragraph)*
- Step-Up Margin(s): [ +/- ] [●] per cent. per annum
  - Step-Up Minimum Rate of Interest: [●] per cent. per annum
  - Step-Up Maximum Rate of Interest: [●] per cent. per annum
- (k) Call Option Date: [Not Applicable/Interest Payment Date occurring in [●]]
- (l) Day Count Fraction: [Actual/365  
Actual/365 (Fixed)  
Actual/365 (Sterling)  
Actual/360  
30/360  
30E/360  
Other]  
*(See Condition 4.2 (Interest on Floating Rate Notes) for alternatives)*



	(m) Fallback provisions, rounding provisions and any other terms relating to the method of calculating interest on Floating Rate Notes if different from those set out in the Conditions:	[●]
17.	Zero Coupon Note Provisions:	[Applicable/Not Applicable] <i>(If not applicable, delete the remaining subparagraphs of this paragraph)</i>
	(a) Accrual Yield:	[●] per cent. per annum
	(b) Reference Price:	[●]
	(c) Any other formula/basis of determining amount payable:	[●]
	(d) Day Count Fraction in relation to Redemption Amounts and late payment:	[Condition [5.7] [ <i>Redemption, Purchase and Cancellation – Redemption Amounts</i> ] <i>applies/specify other</i> ] <i>(Consider applicable day count fraction if not US dollar denominated)</i>
GENERAL PROVISIONS APPLICABLE TO THE NOTES		
18.	Form of Notes: Registered Notes: [Reg S Global Note [and Rule 144A Global Note] registered in the name of a nominee for a common depository for Euroclear and Clearstream, Luxembourg][and][Rule 144A Global Note [and Reg S Global Note] registered in the name of a nominee for the Depository Trust Company] [other]	
19.	Additional Business Centre(s) or other special provisions relating to Interest Payment Dates:	[Not Applicable/give details] <i>(Note that this item relates to the place of payment and not Interest Period end dates to which item 17(c) relates)</i>
20.	Details relating to Bullet Redemption Notes:	[Applicable/Not Applicable] <i>(If not applicable, delete the remaining subparagraphs of this paragraph)</i>
	(a) Redemption Amount:	[●]
	(b) Bullet Redemption Date:	Interest Payment Date occurring in [●]
21.	Details relating to Scheduled Redemption Notes:	[Applicable/Not Applicable] <i>(If Scheduled Redemption Notes are applicable, specify the Scheduled Redemption Dates and Scheduled Amortisation Instalments below)</i> <i>(If not applicable, delete the remaining subparagraphs of this paragraph)</i>
	(a) Scheduled Redemption Dates:	Interest Payment Dates occurring in [●]
	(b) Scheduled Amortisation Instalments:	[●]
22.	Details relating to Pass-Through Notes:	[Applicable/Not Applicable]
23.	Redemption Amount:	<i>[If Redemption Amount is not calculated in accordance with Condition 5.7, specify alternative formula]</i>
24.	Interest Payment Date for Regulatory Call:	[Not Applicable/Interest Payment Date occurring in [●]]
25.	Issuing Entity Swap Provider(s):	[[●]/Not Applicable]
26.	Specified Currency Exchange Rate (Sterling/specified currency):	GBP 1.00/[●]
27.	Redenomination applicable:	Redenomination [not] applicable <i>(If Redenomination is applicable, specify the terms of the redenomination in an Annex to the Final</i>

28.	US tax treatment:	<i>Terms</i> [Will be debt for United States federal income tax purposes, subject to the considerations in the “ <b>United States federal income taxation</b> ” in the Base Prospectus/Not Applicable (These Notes are not being offered or sold in the United States)]
29.	ERISA eligible:	[Yes, subject to the considerations in “ <b>ERISA considerations</b> ” in the Base Prospectus/Not Applicable (The Notes are not being offered or sold in the United States)]
30.	Other final terms:	[Not Applicable/give details] <i>(When adding any other final terms consideration should be given as to whether such terms constitute “significant new factors” and consequently trigger the need for a supplement to the Base Prospectus under Article 16 of the Prospectus Directive.)</i>
31.	Money Market Notes (2a-7)	[Yes/No]
	(a) name of money market note purchaser (if applicable);	
	(b) Name of 2a-7 swap provider (if applicable)	
	(c) Do the Notes have the benefit of remarketing arrangements:	[Yes/No] <i>(If not applicable, delete the remaining subparagraphs of this paragraph)</i>
	If yes:	
	• Name of remarketing bank	[•]
	• Name of conditional purchaser	[•]
	• Name of the tender agent:	[•]
	• Mandatory transfer date:	[•]
	• Maximum reset margin:	[•]
	• Other details:	[•]
DISTRIBUTION		
32.	(a) If syndicated, names [and addresses]** of Managers[and underwriting commitments]**:	[Not Applicable/give names [ <i>and addresses and underwriting commitments</i> ]**] <i>(Include names and addresses of entities agreeing to underwrite the issue on a firm commitment basis and names and addresses of the entities agreeing to place the issue without a firm commitment or on a “best efforts” basis if such entities are not the same as the Managers.) **</i>
	(b) Stabilising Manager (if any):	[Not Applicable/give name]
33.	If non-syndicated, name [and address]** of relevant Dealer:	[Name [and address]**]
34.	Total commission and concession:**	[•] per cent. of the Initial Principal Amount**
35.	Whether TEFRA D or TEFRA C rules applicable or TEFRA rules not applicable:	[TEFRA D/TEFRA C/TEFRA not applicable]
36.	Additional selling restrictions:	[Not Applicable/give details]
OPERATIONAL INFORMATION		
37.	Any clearing system(s) other than DTC, Euroclear or Clearstream, Luxembourg and the relevant identification numbers:	[Not Applicable/give name(s) and number(s)]
38.	Delivery:	Delivery [against/free of payment]
39.	Names and addresses of additional Paying Agent(s) (if any):	[Rule 144A: [•]/Reg S: [•]]
40.	ISIN Code:	[Rule 144A: [•]/Reg S [•]]

41.	Common Code:	[Rule 144A: [●]/Reg S [●]]
42.	CUSIP:	[●]
LOAN TRANCHE INFORMATION		
43.	Loan Tranche:	[●] <i>(specify loan tranche applicable to the relevant Series and Class of Notes)</i>
44.	Borrower:	Pendeford Funding (No. 1) Limited
45.	Designated Loan Tranche rating:	[●] <i>(specify AAA Loan Tranche, AA Loan Tranche, A Loan Tranche, BBB Loan Tranche or B Loan Tranche, as applicable)</i>
46.	Designation of Loan Tranche:	[Bullet Loan Tranche/Scheduled Amortisation Loan Tranche/Pass-Through Loan Tranche/other]
47.	Initial Principal Amount:	£[●]
	(a) Closing Date:	[●]
	(b) Interest Commencement Date:	[●]
48.	Loan Tranche rate:	[●] [+/-] [●] per cent.
49.	Step-Up Date (if any):	[The Funding 1 Interest Payment Date occurring in [●]/Not Applicable]
50.	Stepped-up Loan Tranche rate:	[[●] per cent./Not Applicable]
51.	Details relating to Bullet Loan Tranches:	[Applicable/Not Applicable] <i>(If not applicable, delete the remaining subparagraphs of this paragraph)</i>
	(a) Bullet Repayment Date:	The Funding 1 Interest Payment Date occurring [●]
	(b) Relevant Accumulation Amount:	[●] <i>(Insert any other information applicable in respect of cash accumulation period to the extent not specified in the Base Prospectus)</i>
52.	Details relating to Scheduled Amortisation Loan Tranches:	[Applicable/Not Applicable] <i>(If applicable, specify the Scheduled Repayment Dates and Scheduled Amortisation Instalments below)</i> <i>(If not applicable, delete the remaining subparagraphs of this paragraph)</i>
	(a) Scheduled Repayment Dates:	The Funding 1 Interest Payment Date occurring [●] and [●]
	(b) Relevant Accumulation Amounts:	[●] and [●] <i>(Insert any other information applicable in respect of cash accumulation period to the extent not specified in the Base Prospectus)</i>
53.	Details relating to Pass-Through Loan Tranches:	[Applicable/Not Applicable]
54.	Final Repayment Date:	The Funding 1 Interest Payment Date falling in [●]
55.	Funding 1 Interest Payment Dates:	Each Interest Payment Date
56.	Details relating to Subordinated Loan Tranches:	[Applicable/Not Applicable]
	(a) Initial Principal Amount:	[●]
	(b) Rate of Interest:	[●]
57.	Details relating to Start-up Loan Tranches:	[Applicable/Not Applicable]

58. Initial Principal Amount: [●]
59. Rate of Interest: [●]

Notes

\*\* Delete if minimum denomination is €50,000

**Issuing Entity Swap Provider(s)**

*[To be inserted for issuing entity swap providers (if any)]*

## Currency Presentation

Unless otherwise stated in these final terms, any translations of pounds sterling into US dollars have been made at the rate of £1.00 = US\$[●] which was the closing buying rate in the City of New York for cable transfers in dollars per £1.00 as certified for customs purposes by the Federal Reserve Bank of New York on [●]. Use of this rate does not mean that sterling amounts actually represent those US dollar amounts or could be converted into US dollars at that rate at any particular time.

	Sterling/US dollar exchange rate history							
	Years ended 31 December							
	Period ending 12 September 2008							
	2008	2007	2006	2005	2004	2003	2002	2001
Last <sup>(1)</sup>	1.7896	1.9843	1.9586	1.7188	1.9160	1.7842	1.6095	1.4543
Average <sup>(2)</sup>	1.9558	2.0016	1.8434	1.8204	1.8330	1.6347	1.5025	1.4396
High	2.0311	2.1104	1.9794	1.9292	1.9482	1.7842	1.6095	1.5045
Low	1.7497	1.9235	1.7256	1.7138	1.7544	1.5500	1.4074	1.3730

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Notes:

<sup>(1)</sup> The closing exchange rate on the last operating business day of each of the periods indicated, years commencing from 1 January or the next operating business day.

<sup>(2)</sup> Average daily exchange rate during the period.

Source: *Bloomberg – Close of Business Mid Price*

Unless otherwise stated in these final terms, any translations of pounds sterling into euro have been made at the rate of €1.00 = £[●] which was the closing buying rate in the City of New York for cable transfers in pounds sterling per €1.00 as certified for customs purposes by the Federal reserve Bank of New York on [●]. Use of this rate does not mean that pound sterling amounts actually represent those euro amounts or could be converted into euro at that rate at any particular time.

	Euro/sterling exchange rate history							
	Years ended 31 December							
	Period ending 12 September 2008							
	2008	2007	2006	2005	2004	2003	2002	2001
Last <sup>(1)</sup>	0.7929	0.7349	0.6739	0.6877	0.7066	0.7058	0.6517	0.6110
Average <sup>(2)</sup>	0.7810	0.6846	0.6818	0.6838	0.6786	0.6922	0.6288	0.6218
High	0.8160	0.7376	0.7007	0.7071	0.7092	0.7247	0.6538	0.6434
Low	0.7350	0.6553	0.6683	0.6628	0.6567	0.6471	0.6089	0.5961

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Notes:

<sup>(1)</sup> The closing exchange rate on the last operating business day of each of the periods indicated, years commencing from 1 January or the next operating business day.

<sup>(2)</sup> Average daily exchange rate during the period.

Source: *Bloomberg – Close of Business Mid Price*

### Issuing entity subordinated loans

Issuing entity subordinated loans to be made available to the issuing entity on the closing date in connection with the issue of the [●]-[●] notes will have the terms as set out in Annex B – [[The issuing entity subordinated loan provider/[●]] has previously made issuing entity subordinated loans available to the issuing entity with the terms set out in Annex D.]

The required subordinated loan tranche principal amount will be, as of the closing date, £[●].

### Issuing entity start-up loans

The issuing entity start-up loan to be made available to the issuing entity on the closing date in connection with the [●]-[●] notes will have the terms as set out in Annex C – [[The issuing entity start-up loan provider/[●]] has previously made issuing entity start-up loans available to the issuing entity with the terms set out in Annex D in connection with previously issued series and classes of notes.]

### Other series issued

As of the closing date, the aggregate principal amount outstanding of notes issued by the issuing entity (converted, where applicable, into sterling at the applicable specified currency exchange rate), including the issue of the [●]-[●] notes described herein, will be as set out in Annex A.

### Other loan tranches

As of the closing date, the aggregate outstanding principal balance of loan tranches advanced by the issuing entity to Funding 1 under the intercompany loan agreement, including the loan tranches described herein, will be as set out in Annex A.

### Mortgages Trust and the Portfolio

As at the closing date:

- the minimum seller share will be approximately £[●];
- the Funding 1 share will be approximately £[●], representing approximately [●] per cent. of the trust property; and
- the seller share will be approximately £[●], representing approximately [●] per cent. of the trust property.

The actual amounts of the Funding 1 share and the seller share as at the closing date will not be determined until the day before the closing date, which will be after the date of these final terms.

For the purposes of paragraph (d) of the definition of **non-asset trigger event**, the aggregate outstanding balance of loans comprising the trust property must be at least £[●]. See “**The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1**” in the base prospectus.

For the purposes of paragraph (c) of the definition of **product switch** (See “**Sale of loans and their related security – Product switches**” in the base prospectus) any variation to the maturity date of a loan must not extend beyond [●] while any rated loan tranche under the intercompany loan is outstanding.

For the purposes of the conditions precedent to a sale of new loans and their related security to the mortgages trustee, as set out in “**Sale of loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**”):

- the **fixed rate loans percentage** shall be [●] per cent.

- the **buy-to-let loans percentage** shall be [●] per cent.
- the **self-certification loan percentage** shall be [●] per cent.

[For the purposes of the representation and warranties of the seller under the mortgage sale agreement:

- each loan in the portfolio was made no earlier than 1 January 2003 and no later than [●];
- the final maturity date of each loan is no later than [●];]

The Funding 1 reserve required amount will be, as at the closing date, [●].



### Use of proceeds

The gross proceeds from the issue of the [●]-[●] notes equal approximately £[●] and (after exchanging, where applicable, the proceeds of the [●]-[●] notes for sterling, calculated by reference to the applicable specified currency exchange rate) will be used by the issuing entity to make available rated loan tranches to Funding 1 pursuant to the terms of the intercompany loan agreement. Funding 1 will use the gross proceeds of each rated loan tranche: [(i) to pay the purchase price to the seller for the sale of the new portfolio to the mortgages trustee on the closing date; and/or (ii) to pay the purchase price to the seller for the sale of part of its share in the trust property to Funding 1 on the closing date; and/or (iii) to pay the seller for an increase in its share of the trust property on the closing date; and/or (iv) to fund or replenish the Funding 1 general reserve fund and/or the Funding 1 liquidity reserve fund (if any); and/or (v) to make a payment to the issuing entity to refinance an existing loan tranche (which may be a rated loan tranche or a subordinated loan tranche) or to a new issuing entity to refinance some or all of a new intercompany loan or to make a payment to any new funding beneficiary so that it may refinance some or all of a new intercompany loan.

### Maturity and prepayment considerations

The average lives of any class of the [●]-[●] notes cannot be stated, as the actual rate of repayment of the loans and redemption of the mortgages and a number of other relevant factors are unknown. However, calculations of the possible average lives of each series and class of the [●]-[●] notes can be made based on certain assumptions.

The assumptions used to calculate the possible average lives of each series and class of the [●]-[●] notes in the following table include that:

1. neither the issuing entity security nor the Funding 1 security has been enforced;
2. the seller is not in breach of the terms of the mortgage sale agreement;
3. the seller sells no new loans to the mortgages trustee after the closing date and the loans are assumed to amortise in accordance with the assumed constant payment rate indicated in the table below (subject to assumption 4 below);
4. [the seller sells to the mortgages trustee sufficient new loans and their related security (i) in the period up to (but excluding) the interest payment date in [●], such that the aggregate principal amount outstanding of loans in the portfolio at any time is not less than £[●] or such higher amount as may be required to be maintained as a result of the issuing entity advancing loan tranches to Funding 1 which Funding 1 uses to pay to the seller for an increase in its share of the trust property and/or to pay the seller for the sale of new loans to the mortgages trustee]/[the aggregate principal amount outstanding of loans in the portfolio will not fall below an amount equal to the product of [●] and the principal amount outstanding of all notes of the issuing entity and any other Funding 1 issuing entities at any time after giving effect to principal distributions];
5. neither an asset trigger event nor a non-asset trigger event occurs;
6. no event occurs that would cause payments on scheduled amortisation loan tranches or pass-through loan tranches to be deferred (unless such advances are deferred in accordance with Rule (1) (C) or Rule (1) (D) as set out in “Cashflows – Rule (1) – Repayment deferrals” in the accompanying base prospectus)/[no event occurs that would cause payments on the [●]-[●] notes to be deferred];
7. the annualised CPR as at the closing date is assumed to be the same as the various assumed rates in the table below;
8. there is a balance of £[●] in the Funding 1 cash accumulation ledger at the closing date;
9. [the issuing entity exercises its option to redeem the [●]-[●] notes on the step-up date, relating to the [●]-[●] notes]; [and]
10. the closing date is [●][./; and]
11. the outstanding principal amount of the [●]-[●] class [●] notes is paid on the interest payment date falling in [●].

**CPR and possible average lives of each series and class of [●]-[●] notes (in years)**

Based upon the foregoing assumptions, the approximate average life in years of each series and class of [●]-[●] notes, at various assumed rates of repayment of the loans, would be as follows:

Constant payment rate <sup>(1)</sup> (per annum)	serie s [●] class [●] notes	serie s [●] class [●] notes	serie s [●] class [●] notes	serie s [●] class [●] notes	serie s [●] class [●] notes	serie s [●] class [●] notes	serie s [●] class [●] notes
5%	[●]	[●]	[●]	[●]	[●]	[●]	[●]
10%	[●]	[●]	[●]	[●]	[●]	[●]	[●]
15%	[●]	[●]	[●]	[●]	[●]	[●]	[●]
20%	[●]	[●]	[●]	[●]	[●]	[●]	[●]
25%	[●]	[●]	[●]	[●]	[●]	[●]	[●]
30%	[●]	[●]	[●]	[●]	[●]	[●]	[●]
35%	[●]	[●]	[●]	[●]	[●]	[●]	[●]

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 (1) Includes both scheduled and unscheduled payments.  
 [insert in the case of remarketable notes:

- (1) This represents the average lives to the first class [●] note mandatory transfer date in [●].
- (2) This represents the average lives of all class [●] note remarketed after the first class [●] note mandatory transfer date in [●].]

Assumptions (1), (2), (3), (4), (5), (6) [, (9)] and (10) relate to circumstances which are not predictable. [No assurance can be given that the issuing entity will be in a position to redeem the [●]-[●] notes on their step-up date. If the issuing entity does not so exercise its option to redeem, then the average lives of the then outstanding [●]-[●] notes would be extended.]

The average lives of the [●]-[●] notes are subject to factors largely outside the control of the issuing entity and consequently no assurance can be given that these assumptions and estimates will prove in any way to be realistic and they must therefore be viewed with considerable caution. For more information in relation to the risks involved in the use of these estimated average lives, see “**Risk factors – The yield to maturity of the notes may be adversely affected by prepayments or redemptions on the loans**” in the base prospectus.

## Statistical information on the portfolio

### The cut-off date mortgage portfolio

The statistical and other information contained in these final terms has been compiled by reference to the loans in the portfolio as at the cut-off date that, subject as provided, are expected to indirectly secure the [•]-[•] notes and all other notes of the issuing entity as at [•] (the cut-off date). Columns stating percentage amounts may not add up to 100 per cent. due to rounding. A loan will be removed from [the portfolio]\* [any new portfolio (which comprises a portion of the portfolio as at the cut-off date)]\*\* if, in the period up to (and including) the assignment date relating to [the portfolio]\* [such new portfolio]\*\*, the loan is repaid in full or if the loan does not comply with the terms of the mortgage sale agreement on or about the applicable assignment date. Once such loans are removed, the seller will then randomly select from the loans remaining in [the portfolio]\* [the new portfolio]\*\* those loans to be assigned on the applicable assignment date once the determination has been made as to the anticipated principal balances of the [•]-[•] notes to be issued and the corresponding size of the trust that would be required ultimately to support payments on the [•]-[•] notes [and all other notes of the issuing entity]\*. The loans in the mortgages trust are selected on the basis of the seller's selection criteria for inclusion in the mortgages trust. The material aspects of Birmingham Midshires' lending criteria are described under "The loans – Lending criteria" in the base prospectus. Standardised credit scoring is not used in the UK mortgage market. For an indication of the credit quality of borrowers in respect of the loans, investors may refer to such lending criteria and to the historical performance of the loans in the mortgages trust as set forth in these final terms. One significant indicator of obligor credit quality is arrears and losses. The information presented under ["Delinquency and loss experience of the portfolio"]\*\* ["Delinquency and loss experience of the portfolio (including loans which previously formed part of the portfolio)"]\*\* on page [•] in these final terms reflects the arrears and repossession experience for loans in the portfolio, [including loans that were contained in the portfolio since the inception of the mortgages trust and loans expected to be transferred to the mortgages trust on the closing date]\*\*. All of the loans in the table were originated by Birmingham Midshires, [but not all of the loans form part of the portfolio]\*. Birmingham Midshires services all of the loans originated by Birmingham Midshires. It is not expected that the characteristics of the portfolio as at the closing date will differ materially from the characteristics of the portfolio as at the cut-off date. Except as otherwise indicated, these tables have been prepared using the current balance as at the cut-off date, which includes all principal and accrued interest for the loans in the portfolio.

The portfolio as at the cut-off date consisted of [•] mortgage accounts, comprising loans originated by Birmingham Midshires and secured over properties located in England and Wales and Scotland and having an aggregate outstanding principal balance of £[•] as at that date. The loans in the portfolio as at the cut-off date were originated by Birmingham Midshires between 1 January 2003 and [•].

As at the cut-off date, [•] per cent. of the loans in the portfolio by value and [•] per cent. by number were special rate loans. [•] per cent. by value and [•] per cent. by number were discount variable rate loans or tracker rate loans and [•] per cent. by value and [•] per cent. by number were fixed rate loans. Approximately [•] per cent. by value and [•] per cent. by number of the loans in the portfolio were as at the cut-off date flexible loans and approximately [•] per cent. by value and [•] per cent. by number were Mortgage Plus loans.

[As at [•], the standard variable rate of Birmingham Midshires was [•] per cent. per annum.]

As at [•], [•] per cent. of the loans in portfolio were valued using AVM.

## Outstanding balances as at the cut-off date

The following table shows the range of outstanding mortgage account balances (including accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) as at the cut-off date.

Range of outstanding balances as at the cut-off date*	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
£0 – £24,999.99	£[•]	[•]	[•]	[•]
£25,000 – £49,999.99	£[•]	[•]	[•]	[•]
£50,000 – £74,999.99	£[•]	[•]	[•]	[•]
£75,000 – £99,999.99	£[•]	[•]	[•]	[•]
£100,000 – £124,999.99	£[•]	[•]	[•]	[•]
£125,000 – £149,999.99	£[•]	[•]	[•]	[•]
£150,000 – £174,999.99	£[•]	[•]	[•]	[•]
£175,000 – £199,999.99	£[•]	[•]	[•]	[•]
£200,000 – £224,999.99	£[•]	[•]	[•]	[•]
£225,000 – £249,999.99	£[•]	[•]	[•]	[•]
£250,000 – £299,999.99	£[•]	[•]	[•]	[•]
£300,000 – £349,999.99	£[•]	[•]	[•]	[•]
£350,000 – £399,999.99	£[•]	[•]	[•]	[•]
£400,000 – £449,999.99	£[•]	[•]	[•]	[•]
£450,000 – £499,999.99	£[•]	[•]	[•]	[•]
£500,000 – £549,999.99	£[•]	[•]	[•]	[•]
£550,000 – £599,999.99	£[•]	[•]	[•]	[•]
£600,000 – £649,999.99	£[•]	[•]	[•]	[•]
£650,000 – £699,999.99	£[•]	[•]	[•]	[•]
£700,000 – £749,999.99	£[•]	[•]	[•]	[•]
Totals	£[•]	100.00%	[•]	100.00

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\* Including capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees.

The largest mortgage account (including accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) had an outstanding current balance as at the cut-off date of £[•] and the smallest mortgage account had an outstanding current balance as at the cut-off date of £[•]. The average current balance (including capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) as at the cut-off date was approximately £[•].

## LTV ratios at origination

The following table shows the range of LTV ratios, which express the outstanding balance of the aggregate of loans in a mortgage account (excluding accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) as at the date of the initial loan origination divided by the value of the property securing the loans in that mortgage account at the same date. The seller has not revalued any of the mortgaged properties since the date of the origination of the related loan other than where an additional lending has been applied for or advanced on an account since origination, in which case the original valuation may have been updated with a more recent valuation. Where this is the case, this revised valuation has been used in formulating this data.

Range of LTV ratios at origination*	Aggregate outstanding balance at origination (£)	% of total	Number of mortgage accounts	% of total
0% – 24.99%	£[•]	[•]	[•]	[•]
25% – 49.99%	£[•]	[•]	[•]	[•]
50% – 74.99%	£[•]	[•]	[•]	[•]
75% – 79.99%	£[•]	[•]	[•]	[•]
80% – 84.99%	£[•]	[•]	[•]	[•]
85% – 89.99%	£[•]	[•]	[•]	[•]
90% – 94.99%	£[•]	[•]	[•]	[•]
95% – 96.99%	£[•]	[•]	[•]	[•]
97% – 99.99%	£[•]	[•]	[•]	[•]
Totals	£[•]	100.00	[•]	100.00

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\* Excluding accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees.

The weighted average LTV ratio of the mortgage accounts (excluding any accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) at origination was [•] per cent. The highest LTV ratio of any mortgage account (excluding any accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) at origination was [•] per cent. and the lowest was [•] per cent.

## Cut-off date LTV ratios

The following table shows the range of LTV ratios, which express the outstanding balance of the aggregate of loans in a mortgage account (including accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) as at the cut-off date divided by the indexed valuation of the property securing the loans in that mortgage account at the same date.

Range of LTV ratios at current balance as at the cut-off date*	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
0% – 24.99%	£[•]	[•]	[•]	[•]

25% – 49.99%	£[•]	[•]	[•]	[•]
50% – 74.99%	£[•]	[•]	[•]	[•]
75% – 79.99%	£[•]	[•]	[•]	[•]
80% – 84.99%	£[•]	[•]	[•]	[•]
85% – 89.99%	£[•]	[•]	[•]	[•]
90% – 94.99%	£[•]	[•]	[•]	[•]
95% – 96.99%	£[•]	[•]	[•]	[•]
97% – 99.99%	£[•]	[•]	[•]	[•]
100%+	£[•]	[•]	[•]	[•]
Totals	£[•]	100.00	[•]	100.00

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\* Including accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees.

The weighted average LTV ratio of the mortgage accounts (including any accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) as at the cut-off date was [•] per cent. The highest LTV ratio of any mortgage account (including any accrued interest, capitalised interest, capitalised high LTV fees, insurance fees, booking fees and valuation fees) was [•] per cent. and the lowest was [•] per cent.

### Geographical distribution

The following table shows the distribution of properties securing the loans throughout England, Wales and Scotland as at the cut-off date. No such properties are situated outside England, Wales or Scotland]. The seller's lending criteria and current credit scoring tests do not take into account the geographical location of the property securing a loan.

Regions	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
Scotland	£[•]	[•]	[•]	[•]
North	£[•]	[•]	[•]	[•]
North West	£[•]	[•]	[•]	[•]
East	£[•]	[•]	[•]	[•]
Midlands	£[•]	[•]	[•]	[•]
South Wales & West	£[•]	[•]	[•]	[•]
Greater London	£[•]	[•]	[•]	[•]
South East	£[•]	[•]	[•]	[•]
Unidentified	£[•]	[•]	[•]	[•]
Totals	£[•]	100.00	[•]	100.00

House prices and incomes vary throughout England, Wales and Scotland. The table below summarises the average industry house price and the average income for each region for the year ended [●] in order to produce a house price to earnings ratio for each region.

Regions	Average earnings (£ per annum)*	House Price (£)**	Price/earnings ratio
Scotland	[●]	[●]	[●]
North	[●]	[●]	[●]
North West	[●]	[●]	[●]
East	[●]	[●]	[●]
Midlands	[●]	[●]	[●]
South Wales & West	[●]	[●]	[●]
Greater London	[●]	[●]	[●]
South East	[●]	[●]	[●]
Unidentified	[●]	[●]	[●]

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\* Average recorded income of borrowers.

\*\* Simple average house price.

[Source: [www.communities.gov.uk/index.asp?id=1156110](http://www.communities.gov.uk/index.asp?id=1156110)]



## Seasoning of loans

The following table shows the number of months since the date of origination of the initial loan in a mortgage account. The ages (but not the balances) of the loans in this table have been forecast forward to the expected closing date of [●] for the purpose of calculating the seasoning.

Forecasted age of loans in months as at expected closing date	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
6	£[●]	[●]	[●]	[●]
6 to 12	£[●]	[●]	[●]	[●]
12 to 18	£[●]	[●]	[●]	[●]
18 to 24	£[●]	[●]	[●]	[●]
24 to 30	£[●]	[●]	[●]	[●]
30 to 36	£[●]	[●]	[●]	[●]
36 to 42	£[●]	[●]	[●]	[●]
42 to 48	£[●]	[●]	[●]	[●]
48 to 54	£[●]	[●]	[●]	[●]
54 to 60	£[●]	[●]	[●]	[●]
60 to 66	£[●]	[●]	[●]	[●]
66 to 72	£[●]	[●]	[●]	[●]
72+	£[●]	[●]	[●]	[●]
Totals	£[●]	100.00	[●]	100.00

The forecasted maximum, minimum and weighted average seasoning of loans as at [●] will be [●], [●] and [●] months, respectively.

## Years to maturity of loans

The following table shows the number of remaining years of the term of the initial loan in a mortgage account as at the cut-off date.

Years to maturity	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
5	£[●]	[●]	[●]	[●]
5 to 10	£[●]	[●]	[●]	[●]
10 to 15	£[●]	[●]	[●]	[●]
15 to 20	£[●]	[●]	[●]	[●]

20 to 25	£[●]	[●]	[●]	[●]
25 to 30	£[●]	[●]	[●]	[●]
30 to 35	£[●]	[●]	[●]	[●]
35 to 40	£[●]	[●]	[●]	[●]
Totals	£[●]	100.00	[●]	100.00

The maximum, minimum and weighted average remaining term of the loans as at the cut-off date was [●], [●] and [●] years, respectively.

### Purpose of loan

The following table shows whether the purpose of the initial loan in a mortgage account on origination was to finance the purchase of a new property or to remortgage a property already owned by the borrower.

Use of proceeds	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
Purchase	£[●]	[●]	[●]	[●]
Remortgage	£[●]	[●]	[●]	[●]
Totals	£[●]	100.00	[●]	100.00

As at the cut-off date, the weighted average balance of loans used to finance the purchase of a new property was £[●] and the weighted average balance of loans used to remortgage a property already owned by the borrower was £[●].

### Property type

The following table shows the types of properties to which the mortgage accounts relate.

Property type	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
Detached	£[●]	[●]	[●]	[●]
Semi-Detached	£[●]	[●]	[●]	[●]
Terraced	£[●]	[●]	[●]	[●]
Other*	£[●]	[●]	[●]	[●]
Totals	£[●]	100.00	[●]	100.00

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\* Primarily flats or maisonettes.

As at the cut-off date, the weighted average balance of loans secured by [list types] was £[●], £[●] and £[●], respectively.

### Special rate, flexible and Mortgage Plus loans

The following table shows the distribution of special rate loans, flexible loans and Mortgage Plus loans as at the cut-off date.

Type of rate	Aggregate outstanding interest bearing balance as at the cut-off date (£)	% of total	Number of product holdings	% of total
Variable and tracker rate loans	£[●]	[●]	[●]	[●]
Fixed rate loans	£[●]	[●]	[●]	[●]
Total special rate loans	£[●]	100.00	[●]	100.00

### Repayment terms

The following table shows the repayment terms for the loans in the mortgage accounts as at the cut-off date. Where any loan in a mortgage account is interest-only, then that entire mortgage account is classified as interest-only.

Repayment terms	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
Repayment	£[●]	[●]	[●]	[●]
Interest-only	£[●]	[●]	[●]	[●]
Totals	£[●]	100.00	[●]	100.00

As at the cut-off date, the weighted average balance of repayment loans and interest-only loans was £[●] and £[●], respectively.

### Payment methods

The following table shows the payment methods for the mortgage accounts as at the cut-off date.

Payment method	Aggregate outstanding balance as at the cut-off date (£)	% of total	Number of mortgage accounts	% of total
Direct debit	£[●]	[●]	[●]	[●]
Other	£[●]	[●]	[●]	[●]
Totals	£[●]	100.00	[●]	100.00

### Distribution of fixed rate loans

As at the cut-off date, approximately [●] per cent. of the loans in the portfolio were fixed rate loans. The following tables show the distribution of fixed rate loans by their fixed rate of interest as at such date and the year in which the loans cease to bear a fixed rate of interest and instead bear a floating rate of interest. Unlike the prior tables in this section, the figures in these tables have been calculated on the basis of loan product holdings rather than mortgage accounts. A mortgage account may have more than one active loan product.

Fixed rate loans remain at the relevant fixed rate for a period of time as specified in the offer conditions, after which they move to a standard variable rate or some other rate as specified in the offer conditions.

Fixed rate %	Aggregate outstanding interest bearing balance as at the cut-off date (£)	% of total	Number of product holdings	% of total
0 – 3.99	£[•]	[•]	[•]	[•]
4.00 – 4.99	£[•]	[•]	[•]	[•]
5.00 – 5.99	£[•]	[•]	[•]	[•]
6.00 – 6.99	£[•]	[•]	[•]	[•]
Totals	£[•]	100.00	[•]	100.00

Year in which current fixed rate period ends	Aggregate outstanding interest bearing balance as at the cut-off date (£)	% of total	Number of product holdings	% of total
2007	£[•]	[•]	[•]	[•]
2008	£[•]	[•]	[•]	[•]
2009	£[•]	[•]	[•]	[•]
2010	£[•]	[•]	[•]	[•]
2011	£[•]	[•]	[•]	[•]
2012	£[•]	[•]	[•]	[•]
2013	£[•]	[•]	[•]	[•]
2014	£[•]	[•]	[•]	[•]
2015	£[•]	[•]	[•]	[•]
2016	£[•]	[•]	[•]	[•]
2017	£[•]	[•]	[•]	[•]
Totals	£[•]	100.00	[•]	100.00

Product Ranges	Aggregate outstanding interest bearing balance as at the cut-off date (£)	% of the total	Number of product holdings	% of the total
Mainstream	£[•]	[•]	£[•]	[•]
Self-certification	£[•]	[•]	£[•]	[•]

Buy-to-let	£[•]	[•]	£[•]	[•]
Totals	£[•]	100.00	[•]	100.00
Mortgage plus (included within Mainstream above)	£[•]	[•]	[•]	[•]

### Payment rate analysis

The following table shows the annualised payment rate for the most recent one-month, three-month and 12 month period for the mortgage accounts in the portfolio.

As of month-end	one-month annualised	three- month annualised	12-month annualised
[•]	[•]	[•]	[•]

In the table above,

- one-month annualised CPR is calculated as  $1 - ((1 - R) ^ 12)$ ,
- three-month annualised CPR is calculated as the average of the one-month annualised CPR for the most recent three months, and
- 12-month annualised CPR is calculated as the average of the one-month annualised CPR for the most recent 12 months,

where in each case R is (i) total principal receipts received plus the principal balance of loans repurchased by the seller (primarily due to further advances) during the relevant period, divided by (ii) the aggregate outstanding principal balance of the loans in the portfolio as at the start of that period.

### Delinquency and loss experience of the [portfolio (including loans which previously formed part of the portfolio)/residential mortgage loans in the Birmingham Midshires mortgage book]

[The loans and related security in the provisional portfolio have been drawn from the Birmingham Midshires mortgage book. Set out below is some information relating to the characteristics of the Birmingham Midshires mortgage book. The information includes sub-prime loans, which will not be eligible for the portfolio. Investors should note that there is no assurance that the future performance of the loans will reflect the historic performance of the loans in the Birmingham Midshires mortgage book.]

[The following table summarises loans in arrears and repossession experience for loans in the portfolio (including loans which previously formed part of the portfolio) as at the cut-off date.] The seller will represent and warrant on the closing date that no loan to be transferred to the mortgages trust on the closing date will have experienced any arrears in the prior 12 months. All of the loans in the table were originated by Birmingham Midshires. Birmingham Midshires services all of the loans originated by Birmingham Midshires.

Birmingham Midshires identifies a loan as being in arrears where an amount equal to or greater than a full month's contractual payment is past its due date. Birmingham Midshires does not define a loan as defaulted at any particular delinquency level, but rather at the time it takes the related property into possession. Birmingham Midshires does not write off a loan as uncollectible until it disposes of the property relating to that loan following default.

**Birmingham Midshires residential mortgage loans**

	31 Dec 2002	31 Dec 2003	31 Dec 2004	31 Dec 2005	31 Dec 2006	31 Dec 2007
Outstanding balance (£m)	[•]	[•]	[•]	[•]	[•]	[•]
Number of loans outstanding (£000s)	[•]	[•]	[•]	[•]	[•]	[•]
Outstanding balance of loans in arrears (£m)						
1 – 2 months	[•]	[•]	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]	[•]	[•]
Total outstanding balance of loans in arrears	[•]	[•]	[•]	[•]	[•]	[•]
Total outstanding balance of loans 3 or more months in arrears as a percentage of the outstanding balance	[•]	[•]	[•]	[•]	[•]	[•]
Outstanding balance of loans relating to properties in possession	[•]	[•]	[•]	[•]	[•]	[•]
Outstanding balance of loans relating to properties sold during the period <sup>(1)</sup>	[•]	[•]	[•]	[•]	[•]	[•]
Net loss on sales of all repossessed properties <sup>(2)</sup>	[•]	[•]	[•]	[•]	[•]	[•]
Ratio of aggregate net losses to aggregate outstanding balance of loans	[•]	[•]	[•]	[•]	[•]	[•]
Average net loss on all properties sold (£000)	[•]	[•]	[•]	[•]	[•]	[•]
Number of loans outstanding in arrears (thousands)						
1 – 2 months	[•]	[•]	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]	[•]	[•]
Total number of loans outstanding in arrears	[•]	[•]	[•]	[•]	[•]	[•]
Total number of loans outstanding 3 or more months in arrears as a percentage of the number of loans outstanding	[•]	[•]	[•]	[•]	[•]	[•]
Number of properties in possession	[•]	[•]	[•]	[•]	[•]	[•]

Number of properties sold during the year

[•] [•] [•] [•] [•] [•]

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- (1) Properties sold may relate to properties taken into possession in prior periods.
- (2) Net loss is net of recoveries in the current period on properties sold in prior periods.

There can be no assurance that the arrears experience with respect to the loans comprising the portfolio in the future will correspond to the experience of the portfolio as set forth in the foregoing table. If the property market experiences an overall decline in property values so that the value of the properties in the portfolio falls below the principal balances of the loans, the actual rates of arrears could be significantly higher than those previously experienced. In addition, other adverse economic conditions, whether or not they affect property values, may nonetheless affect the timely payment by borrowers of principal and interest and, accordingly, the rates of arrears and losses with respect to the loans in the portfolio. Noteholders should observe that the United Kingdom experienced relatively low and stable interest rates during the periods covered in the preceding table. If interest rates were to rise, it is likely that the rate of arrears would rise.

The level of mortgage arrears on loans originated by Birmingham Midshires has reduced since the recession in the United Kingdom in the early nineties. The introduction of the scorecard in judging applications – and thus reducing discretion – has helped to keep the arrears level low, as have a healthy economic climate and historically low interest rates.

House price inflation has indirectly contributed to the improved arrears situation by enabling borrowers to sell at a profit if they encounter financial hardship. In the late 1980s house prices rose substantially faster than inflation as housing turnover increased to record levels. This was at a time when the economy grew rapidly, which led to falling unemployment and relatively high rates of real income growth. These fed into higher demand for housing, and house prices rose rapidly. Demand was further increased by changes in taxation legislation with regard to tax relief on mortgage payments in 1988. When monetary policy was subsequently tightened (in terms of both locking in sterling to the European Exchange Rate Mechanism and higher interest rates), the pace of economic activity first slowed and then turned into recession. Rising unemployment combined with high interest rates led to a fall in housing demand and increased default rates and repossessions. The ability of borrowers to refinance was limited as house prices began to fall and many were in a position of negative equity (borrowings greater than the resale value of the property) in relation to their mortgages.

Birmingham Midshires regularly reviews its lending policies in the light of prevailing market conditions and reviews actions so as to mitigate possible problems. The performance of Birmingham Midshires new business and the arrears profiles are continuously monitored in monthly reports. Any deterioration of the arrears level is investigated and the internal procedures are reviewed if necessary.



## Characteristics of the United Kingdom residential mortgage market

The UK housing market is primarily one of owner-occupied housing, with the remainder in some form of public, private landlord or social ownership. The mortgage market, whereby loans are provided for the purchase of a property and secured on that property, is the primary source of household borrowings in the United Kingdom.

Set out in the following tables are certain characteristics of the United Kingdom mortgage market.

### Industry CPR rates

In the following tables, quarterly industry constant repayment rate (**industry CPR**) data was calculated by dividing the amount of scheduled and unscheduled repayments of mortgages made by building societies in a quarter by the quarterly balance of mortgages outstanding for building societies in the United Kingdom. These quarterly repayment rates were then annualised using standard methodology.

Quarter	Industry CPR rate for the quarter (%)	12-month rolling average (%)	Quarter	Industry CPR rate for the quarter (%)	12-month rolling average (%)
March 1985	10.02	11.61	June 1985	11.67	11.49
September 1985	13.46	11.76	December 1985	13.68	12.21
March 1986	11.06	12.47	June 1986	15.53	13.43
September 1986	17.52	14.45	December 1986	15.60	14.92
March 1987	10.57	14.80	June 1987	14.89	14.64
September 1987	16.79	14.46	December 1987	16.18	14.61
March 1988	13.55	15.35	June 1988	16.03	15.64
September 1988	18.23	16.00	December 1988	12.60	15.10
March 1989	8.85	13.93	June 1989	13.04	13.18
September 1989	11.53	11.51	December 1989	10.38	10.95
March 1990	8.91	10.96	June 1990	9.37	10.05
September 1990	9.66	9.58	December 1990	10.58	9.63
March 1991	9.07	9.67	June 1991	10.69	10.00
September 1991	11.57	10.48	December 1991	10.24	10.39
March 1992	9.14	10.41	June 1992	9.12	10.02
September 1992	9.75	9.56	December 1992	7.96	8.99
March 1993	8.53	8.84	June 1993	10.01	9.06
September 1993	10.68	9.30	December 1993	10.03	9.81
March 1994	9.00	9.93	June 1994	10.52	10.06
September 1994	11.10	10.16	December 1994	10.72	10.33
March 1995	9.15	10.37	June 1995	10.51	10.37
September 1995	11.76	10.53	December 1995	11.61	10.76
March 1996	10.14	11.00	June 1996	11.32	11.21
September 1996	13.20	11.57	December 1996	12.58	11.81
March 1997	9.75	11.71	June 1997	15.05	12.65
September 1997	12.18	12.39	December 1997	11.17	12.04
March 1998	10.16	12.14	June 1998	12.05	11.39
September 1998	13.79	11.79	December 1998	13.44	12.36
March 1999	11.14	12.60	June 1999	14.39	13.19
September 1999	15.59	13.64	December 1999	14.94	14.02
March 2000	13.82	14.69	June 2000	13.86	14.55
September 2000	14.89	14.38	December 2000	15.55	14.53
March 2001	15.47	14.94	June 2001	17.36	15.81
September 2001	19.12	16.87	December 2001	19.01	17.74
March 2002	18.68	18.54	June 2002	19.88	19.17
September 2002	22.40	19.99	December 2002	22.16	20.78
March 2003	19.51	20.99	June 2003	20.18	21.06
September 2003	21.65	20.88	December 2003	21.33	20.67
March 2004	19.90	20.77	June 2004	21.42	21.07
September 2004	21.41	21.01	December 2004	18.71	20.36
March 2005	17.76	19.83	June 2005	17.75	18.91
September 2005	20.24	18.62	December 2005	20.36	19.03
March 2006	19.65	19.50	June 2006	19.37	19.90

Quarter	Industry CPR rate for the quarter (%)	12-month rolling average (%)	Quarter	Industry CPR rate for the quarter (%)	12-month rolling average (%)
September 2006	21.24	20.15	December 2006	21.07	20.33
March 2007	19.57	20.32	June 2007	19.25	20.29
September 2007	21.22	20.28	December 2007	18.63	19.67
March 2008	14.54	18.41	June 2008	16.31	17.67

Source of repayment and outstanding mortgage information: Council of Mortgage Lenders

You should note that the CPR table above presents the historical CPR experience only of building societies in the United Kingdom. During the late 1990s, a number of former building societies (including the seller) converted stock to form UK banks and the CPR experience of these banks is therefore not included in the foregoing building society CPR data.

### Repossession rate

The table below sets out the repossession rate of residential properties in the United Kingdom since 1985.

Year	Repossessions (%)	Year	Repossessions (%)	Year	Repossessions (%)
1985	0.25				
1986	0.30	1993	0.58	2000	0.20
1987	0.32	1994	0.47	2001	0.16
1988	0.22	1995	0.47	2002	0.11
1989	0.17	1996	0.40	2003	0.07
1990	0.47	1997	0.31	2004	0.07
1991	0.77	1998	0.31	2005	0.13
1992	0.69	1999	0.27	2006	0.18
				2007	0.22

Source: Council of Mortgage Lenders

### House price to earnings ratio

The following table shows the ratio for each year of the average annual value of houses compared to the average annual salary in the United Kingdom. The average annual earnings figures are constructed using the CML's new earnings survey figures referring to weekly earnings in April of each year for those male employees whose earnings were not affected by their absence from work. While this is a good indication of house affordability, it does not take into account the fact that the majority of households have more than one income to support a mortgage loan.

Year	House Price to Earnings Ratio	Year	House Price to Earnings Ratio
1994	3.86	2001	5.09
1995	3.80	2002	5.74
1996	3.84	2003	6.35
1997	4.08	2004	6.77
1998	4.35	2005	6.92
1999	4.60	2006	6.96
2000	5.00	2007	7.44

Source: Council of Mortgage Lenders

### House price index

UK residential property prices, as measured by the Nationwide House Price Index and Halifax Price Index (collectively the **Housing Indices**), have generally followed the UK Retail Price Index over an extended period. (Nationwide is a UK building society and Halifax is a UK bank.)

The UK housing market has been through various economic cycles in the recent past, with large year-to-year increases in the Housing Indices occurring in the late 1980s and large decreases occurring in the early 1990s.

Quarter	Retail Price Index		Nationwide House Price Index		Halifax House Price Index	
	Index	% annual change	Index	% annual change	Index	% annual change
March 1985	92.0	5.4	66.2	11.2	113.5	8.6
June 1985	95.1	6.8	68.2	10.3	115.4	8.5
September 1985	95.4	6.1	69.2	10.5	116.8	7.5
December 1985	95.9	5.4	70.7	8.5	120.6	8.3

Quarter	Retail Price Index		Nationwide House Price Index		Halifax House Price Index	
	Index	% annual change	Index	% annual change	Index	% annual change
March 1986	96.5	4.8	71.1	7.1	124.0	8.8
June 1986	97.8	2.8	73.8	8.0	128.1	10.4
September 1986	97.9	2.6	76.3	9.7	132.2	12.4
December 1986	99.1	3.3	79.0	11.1	136.8	12.6
March 1987	100.3	3.9	81.6	13.7	142.3	13.8
June 1987	101.9	4.1	85.8	15.0	146.7	13.6
September 1987	102.1	4.2	88.6	15.0	151.5	13.6
December 1987	103.2	4.1	88.5	11.4	158.0	14.4
March 1988	103.7	3.3	90.0	9.8	167.0	16.0
June 1988	106.2	4.1	97.6	13.0	179.4	20.1
September 1988	107.7	5.3	108.4	20.1	197.4	26.5
December 1988	109.9	6.3	114.2	25.5	211.8	29.3
March 1989	111.7	7.4	118.8	27.8	220.7	27.9
June 1989	114.9	7.9	124.2	24.1	226.1	23.1
September 1989	116.0	7.4	125.2	14.4	225.5	13.3
December 1989	118.3	7.4	122.7	7.2	222.5	4.9
March 1990	120.4	7.5	118.9	0.1	223.7	1.4
June 1990	126.0	9.2	117.7	(5.4)	223.3	(1.2)
September 1990	128.1	9.9	114.2	(9.2)	222.7	(1.2)
December 1990	130.1	9.5	109.6	(11.3)	223.0	0.2
March 1991	130.8	8.3	108.8	(8.8)	223.1	(0.3)
June 1991	133.6	5.9	110.6	(6.2)	221.9	(0.6)
September 1991	134.2	4.7	109.5	(4.2)	219.5	(1.4)
December 1991	135.5	4.1	107.0	(2.4)	217.7	(2.4)
March 1992	136.2	4.0	104.1	(4.4)	213.2	(4.5)
June 1992	139.1	4.0	105.1	(5.1)	208.8	(6.1)
September 1992	139.0	3.5	104.2	(5.0)	206.9	(5.9)
December 1992	139.6	3.0	100.1	(6.7)	199.5	(8.7)
March 1993	138.7	1.8	100.0	(4.0)	199.6	(6.6)
June 1993	140.9	1.3	103.6	(1.4)	201.7	(3.5)
September 1993	141.3	1.6	103.2	(1.0)	202.6	(2.1)
December 1993	141.8	1.6	101.8	1.7	203.5	2.0
March 1994	142.0	2.4	102.4	2.4	204.6	2.5
June 1994	144.5	2.5	102.5	(1.1)	202.9	0.6
September 1994	144.6	2.3	103.2	0.0	202.7	0.0
December 1994	145.5	2.6	104.0	2.1	201.9	(0.8)
March 1995	146.8	3.3	101.9	(0.5)	201.8	(1.4)
June 1995	149.5	3.4	103.0	0.5	199.3	(1.8)
September 1995	149.9	3.6	102.4	(0.8)	197.8	(2.4)
December 1995	150.1	3.1	101.6	(2.3)	199.2	(1.3)
March 1996	150.9	2.8	102.5	0.6	202.1	0.1
June 1996	152.8	2.2	105.8	2.7	206.7	3.6
September 1996	153.1	2.1	107.7	5.1	208.8	5.4
December 1996	154.0	2.6	110.1	8.0	213.9	7.1
March 1997	154.9	2.6	111.3	8.3	216.7	7.0
June 1997	156.9	2.6	116.5	9.6	220.2	6.3

	Retail Price Index		Nationwide House Price Index		Halifax House Price Index	
	Index	% annual change	Index	% annual change	Index	% annual change
September 1997	158.4	3.4	121.2	11.8	222.6	6.4
December 1997	159.7	3.6	123.3	11.4	225.4	5.2
March 1998	160.2	3.4	125.5	12.0	228.4	5.3
June 1998	163.2	3.9	130.1	11.0	232.1	5.3
September 1998	163.7	3.3	132.4	8.8	234.8	5.3
December 1998	164.4	2.9	132.3	7.0	237.2	5.1
March 1999	163.7	2.2	134.6	7.0	238.6	4.4
June 1999	165.5	1.4	139.7	7.1	245.5	5.6

	Retail Price Index		Nationwide House Price Index		Halifax House Price Index	
September 1999	165.6	1.2	144.4	8.6	255.5	8.4
December 1999	166.8	1.4	148.9	11.8	264.1	10.7
March 2000	167.5	2.3	155.0	14.1	273.1	13.5
June 2000	170.6	3.0	162.0	14.8	272.8	10.5
September 2000	170.9	3.2	161.5	11.2	275.9	7.7
December 2000	172.0	3.1	162.8	9.0	278.6	5.3
March 2001	171.8	2.5	167.5	7.8	281.7	3.1
June 2001	173.9	1.9	174.8	7.6	293.2	7.2
September 2001	174.0	1.8	181.6	11.8	302.4	9.2
December 2001	173.8	1.0	184.6	12.5	311.8	11.3
March 2002	173.9	1.2	190.2	12.7	327.3	15.0
June 2002	176.0	1.2	206.5	16.6	343.7	15.9
September 2002	176.6	1.5	221.1	19.7	366.1	19.1
December 2002	178.2	2.5	231.3	22.6	392.1	22.9
March 2003	179.2	3.0	239.3	22.9	403.8	21.0
June 2003	181.3	3.0	250.1	19.2	419.0	19.8
September 2003	181.8	2.9	258.9	15.8	434.5	17.1
December 2003	182.9	2.6	267.1	14.4	455.3	14.9
March 2004	183.8	2.5	277.3	14.8	480.3	17.3
June 2004	186.3	2.7	296.2	16.9	508.4	19.3
September 2004	187.4	3.0	306.2	16.8	522.0	18.3
December 2004	189.2	3.4	304.1	13.0	523.5	14.0
March 2005	189.7	3.2	304.8	9.4	526.9	9.3
June 2005	191.9	3.0	314.2	5.9	526.8	3.6
September 2005	192.6	2.7	314.4	2.7	537.7	3.0
December 2005	193.7	2.4	314.0	3.2	550.3	5.0
March 2006	194.2	2.3	319.8	4.8	560.4	6.2
June 2006	197.6	2.9	329.2	4.7	574.9	8.7
September 2006	199.3	3.4	336.1	6.6	581.7	7.9
December 2006	201.4	3.9	343.2	8.9	606.0	9.6
March 2007	203.0	4.4	350.2	9.1	623.5	10.7
June 2007	206.3	4.3	362.7	9.7	639.4	10.6
September 2007	207.1	3.8	367.3	8.9	643.0	10.0
December 2007	209.8	4.1	367.0	6.7	636.9	5.0
March 2008	211.1	3.9	357.8	2.1	630.2	1.1
June 2008	215.3	4.3	348.1	(4.1)	600.8	(6.2)

Source: Office for National Statistics, Nationwide Building Society and Halifax, respectively. "NA" indicates that the relevant figure is not available.

The percentage annual change in the table above is calculated in accordance with the following formula:

$LN(x/y)$  where  $x$  is equal to the current quarter's index value and  $y$  is equal to the index value of the previous year's corresponding quarter.

All information contained in these final terms in respect of the Nationwide House Price Index has been reproduced from information published by Nationwide Building Society. All information contained in these final terms in respect of the Halifax House Price Index has been reproduced from information published by HBOS plc. The issuing entity confirms that all information in these final terms in respect of the Nationwide House Price Index and the Halifax House Price Index has been accurately reproduced and that, so far as it is aware and is able to ascertain from information published by Nationwide Building Society and HBOS plc, no facts have been omitted which would render the reproduced information inaccurate or misleading.

Note, however, that the issuing entity has not participated in the preparation of that information nor made any enquiry with respect to that information. Neither the issuing entity nor Nationwide Building Society nor HBOS plc makes any representation as to the accuracy of the information or has any liability whatsoever to you in connection with that information. Anyone relying on the information does so at their own risk.

*[Update above tables with more recent source data, if available]*

## **Annex A**

### **Notes**

#### **Notes issued by issuing entity and loan tranches advanced by issuing entity to Funding 1 in connection therewith**

As at the closing date, the aggregate principal amount outstanding of notes issued by the issuing entity (converted, where applicable, into sterling at the applicable specified currency exchange rate), including the notes described herein, will be:

[•]

As at the closing date, the aggregate outstanding principal balance of loan tranches advanced by the issuing entity to Funding 1 under the intercompany loan agreement, including the loan tranches described herein, will be:

[•]

[Annex B

**Issuing entity subordinated loans and previous issuing entity subordinated loans**

The issuing entity subordinated loan to be advanced to the issuing entity on the closing date in connection with the issue of the [●]-[●] notes will have the following terms:

**issuing entity subordinated loan provider:**

[●]

initial outstanding principal balance:

£[●]

interest rate:

Three-month sterling LIBOR plus [●] per cent. per annum

[The following issuing entity subordinated loans have been made available to the issuing entity by [●] (in its capacity as the issuing entity subordinated loan provider)/[●] (in its capacity as the new issuing entity subordinated loan provider)] (where applicable) in connection with the issuance of notes set out below for the stated initial outstanding principal balance and interest rate set out below.

Issue	Initial outstanding principal balance	Current outstanding principal balance	Interest rate
[●]	£[●]	£[●]	£[●]]

**Annex C**

**Series issuing entity start-up loan and previous issuing entity start-up loans to the issuing entity**

The issuing entity start-up loan to be made available to the issuing entity on the closing date in connection with the [●]-[●] notes will have the following terms:

**issuing entity start-up loan provider/new issuing entity start-up loan provider:** [●]  
 initial outstanding principal balance: £[●]  
 interest rate: Three-month sterling LIBOR plus [●] per cent. per annum

[The following issuing entity start-up loans have been made available to the issuing entity by [●] (in its capacity as the issuing entity start-up loan provider)/[●] (in its capacity as the new issuing entity start-up loan provider)] in connection with the issuance of notes set out below for the stated initial outstanding principal balance and interest rate set out below.

Issue	Initial outstanding principal balance	Current outstanding principal balance	Interest rate
[●]	£[●]	£[●]	£[●]



## Annex D

### Static Pool Data

The tables on the following pages set out static pool information with respect to [all mortgage loans originated by Birmingham Midshires between 2003 and [●] (other than sub-prime loans, which will not be included in the mortgages trust)/comprised in the trust property]. These tables show, for originations in each year, the distribution of such loans originated in that year by delinquency category, as at each year end. Not all the loans included in the following tables will be included in the mortgages trust.

The issuing entity has not included static pool information in this annex on prepayments because changes in prepayment and payment rates are not anticipated to have a significant effect on future payments on the [●]-[●] notes because the mechanics of the mortgages trust require an extended cash accumulation period when prepayment rates fall below certain minima dictated by the rating agencies, serving to limit the extent to which slow prepayments would cause the average lives of the [●]-[●] notes to extend. Conversely, rapid prepayments should not cause the average lives of the [●]-[●] notes to shorten so long as the seller maintains the minimum required mortgages trust size. Furthermore, only a limited amount of note principal in relation to the mortgages trust size is actually due to be repaid on any particular interest payment date.

The sale of new loans by the seller to the mortgages trustee is subject to conditions, including ones required by the rating agencies, designed to maintain certain credit-related and other characteristics of the mortgages trust. These include limits on loans in arrears in the mortgages trust at the time of sale, limits on the aggregate balance of loans sold, limits on changes in the weighted average foreclosure frequency (WAFF) and the weighted average loss severity (WALS), minimum yield for the loans in the mortgages trust after the sale and maximum LTV for the loans in the mortgages trust after the sale. See a description of these conditions in “**Sale of the loans and their related security – Sale of loans and their related security to the mortgages trustee on the sale dates**” in the base prospectus.

The following tables show, for each of the last four years of origination, the distribution of Birmingham Midshires loans originated in that year by delinquency category as at each year end starting in 2003.

**Birmingham Midshires arrears by year of origination**

**Loans originated in 2003  
as at each specified date**

31 December 2007

	Number	Principal balance	% by number	% by balance
1 month	[•]	[•]	[•]	[•]
1 – 2 months	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]
<b>Total</b>	[•]	[•]	[•]	[•]

**Loans originated in 2004  
as at each specified date**

31 December 2007

	Number	Principal balance	% by number	% by balance
1 month	[•]	[•]	[•]	[•]
1 – 2 months	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]
<b>Total</b>	[•]	[•]	[•]	[•]

**Loans originated in 2005  
as at each specified date**

31 December 2007				
	Number	Principal balance	% by number	% by balance
1 month	[•]	[•]	[•]	[•]
1 – 2 months	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]
<b>Total</b>	[•]	[•]	[•]	[•]

**Loans originated in 2006**

31 December 2007				
	Number	Principal balance	% by number	% by balance
1 month	[•]	[•]	[•]	[•]
1 – 2 months	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]
<b>Total</b>	[•]	[•]	[•]	[•]

### All loans originated between 2003 and 2007

	31 December 2007			
	Number	Principal balance	% by number	% by balance
1 month	[•]	[•]	[•]	[•]
1 – 2 months	[•]	[•]	[•]	[•]
2 – 3 months	[•]	[•]	[•]	[•]
3 – 6 months	[•]	[•]	[•]	[•]
6 – 12 months	[•]	[•]	[•]	[•]
12+ months	[•]	[•]	[•]	[•]
<b>Total</b>	[•]	[•]	[•]	[•]

**[Listing and admission to trading application]**

These final terms comprise the final terms required for the notes described herein to be admitted to the Official List of the UK Listing Authority and admitted to trading on the London Stock Exchange's Regulated Market pursuant to the Mortgage Backed Note Programme of Pendeford Master Issuer plc.]

**Responsibility**

The issuing entity accepts responsibility for the information contained in these final terms.

Signed on behalf of the issuing entity:

By: \_\_\_\_\_

*Duly authorised*

**[END OF FINAL TERMS]**

## Terms and conditions of the notes

The following are the terms and conditions (the **Conditions**, and any reference to a **Condition** shall be construed accordingly) of the Notes in the form (subject to amendment) which will be incorporated by reference into each Global Note and each Definitive Note, in the latter case only if permitted by the relevant stock exchange or other relevant authority (if any) and agreed by Pendeford Master Issuer plc (the **Issuer**) and the relevant Dealer(s) and/or Manager(s) at the time of issue but, if not so permitted and agreed, such Definitive Note will have endorsed thereon or attached thereto such Conditions. The Final Terms in relation to the relevant Series and Class of Notes may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Conditions, replace or modify these Conditions for the purpose of such Series and Class of Notes. The applicable Final Terms (or the relevant provisions thereof) will be endorsed upon, or attached to, each Global Note and each Definitive Note.

The Notes are constituted by the Note Trust Deed. The security for the Notes is created pursuant to, and on the terms set out in, the Issuer Deed of Charge. By the Paying Agent and Agent Bank Agreement, provision is made for, *inter alia*, the payment of principal and interest in respect of the Notes.

References herein to the **Notes** shall, unless the context otherwise requires, be references to all the Notes issued by the Issuer and constituted by the Note Trust Deed and shall mean:

- (a) in relation to any Series and Class of Notes represented by a Global Note or Global Notes, units of the lowest Specified Denomination in the Specified Currency in each case of such Series and Class of Notes;
- (b) any Global Note; and
- (c) any Definitive Note issued in exchange for a Global Note.

Notes constituted by the Note Trust Deed are issued in series (each a **Series**) and each Series comprises one or more classes of Notes (each a **Class**). Each Series and Class of Notes is subject to the applicable Final Terms. The applicable Final Terms in relation to each Series and Class of Notes (or the relevant provisions thereof) will be endorsed upon, or attached to, such Series and Class of Notes and will supplement these Conditions in respect of such Series and Class of Notes and may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Conditions, replace or modify these Conditions for the purpose of such Series and Class of Notes. References to the **applicable Final Terms** are, in relation to a Series and Class of Notes, to the Final Terms (or the relevant provisions thereof) attached to or endorsed on such Series and Class of Notes.

The statements in these Conditions include summaries of, and are subject to, the detailed provisions of the Note Trust Deed, the Issuer Deed of Charge and the Paying Agent and Agent Bank Agreement.

Copies of the Note Trust Deed, the Issuer Deed of Charge, the Paying Agent and Agent Bank Agreement and each of the other Transaction Documents are available for inspection during normal business hours at the registered office of the Issuer, being 35 Great St. Helen's, London EC3A 6AP, United Kingdom and the specified office for the time being of (a) the Principal Paying Agent, being at Winchester House, 1 Great Winchester Street, London EC2N 2DB, United Kingdom and (b) the US Paying Agent, being at 1741 E St. Andrew Place, Santa Ana CA 92705, United States. Copies of the Final Terms of each Series and Class of Notes are obtainable by Noteholders during normal business hours at the registered office of the Issuer and the specified office for the time being of (i) the Principal Paying Agent and (ii) the US Paying Agent and any Noteholder must produce evidence satisfactory to the relevant Paying Agent as to its holding of Notes and identity.

The Holders of any Series and Class of Notes are entitled to the benefit of, are bound by, and are deemed to have notice of all the provisions of, and definitions contained or incorporated in, the Note Trust Deed, the Issuer Deed of Charge, the Paying Agent and Agent Bank Agreement, each of the other Transaction Documents and the applicable Final Terms and to have notice of each other Final Terms relating to each other Series and Class of Notes.

A glossary of definitions appears in **Condition 19**.

References herein to the **Class A Noteholders**, the **Class B Noteholders**, the **Class M Noteholders**, the **Class C Noteholders** and the **Class D Noteholders** shall, in each case and unless specified otherwise, be references to the Holders of the Notes of all Series of the applicable Class.

References herein to the **Class A Notes**, the **Class B Notes**, the **Class M Notes**, the **Class C Notes** or the **Class D Notes** shall, in each case and unless specified otherwise, be references to the Notes of all Series of the applicable Class.

## 1. Form, Denomination, Register, Title and Transfers

### 1.1 Form and Denomination

Each Series and Class of Notes will be issued in the Specified Currency and in the Specified Denomination. Each Series and Class of Rule 144A Notes will be initially represented by a Rule 144A Global Note, which, in the aggregate, will represent the Principal Amount Outstanding from time to time of such Series and Class of Rule 144A Notes. Each Series and Class of Reg S Notes will be initially represented by a Reg S Global Note, which, in the aggregate, will represent the Principal Amount Outstanding from time to time of such Series and Class of Reg S Notes.

Each Reg S Global Note and/or Rule 144A Global Note, as specified in the applicable final terms, will be deposited with, and registered in the name of a nominee of, a common depositary for Euroclear and Clearstream, Luxembourg. Each Rule 144A Global Note and/or Reg S Global Note, as specified in the applicable final terms, will be deposited with a custodian for, and registered in the name of Cede & Co. (or such other name as may be requested by an authorised representative of DTC) as nominee of DTC. Each Global Note will be numbered serially with an identifying number which will be recorded on the relevant Global Note and in the Register. Each Series and Class of Notes may be Fixed Rate Notes, Floating Rate Notes, Zero Coupon Notes or a combination of any of the foregoing, depending upon the Redemption/Payment Basis shown in the applicable Final Terms.

Global Notes will be exchanged for notes in definitive registered form (**Definitive Notes**) only under certain limited circumstances (as described in the relevant Global Note). If Definitive Notes are issued, they will be serially numbered and issued in an aggregate principal amount equal to the Principal Amount Outstanding of the relevant Global Note and in registered form only.

The Notes (in either global or definitive form) will be issued in such denominations as specified in the applicable Final Terms, save that the minimum denomination of each Note will be such as may be allowed or required from time to time by the relevant central bank or regulatory authority (or equivalent body) or any laws or regulations applicable to the relevant Specified Currency and save that the Dollar Notes will be issued in minimum denominations of \$100,000 and in integral multiples of \$1,000 in excess thereof, the Euro Notes will be issued in minimum denominations of €50,000 and in integral multiples of €1,000 in excess thereof, up to and including €99,000 and the Sterling Notes will be issued in minimum denominations of £50,000 and in integral multiples of £1,000 in excess thereof, up to and including £99,000 (provided that Sterling Notes issued with a maturity of less than 366 days will be issued in minimum denominations of £100,000 and integral multiples of £1,000 in excess thereof). No Note will be issued in a denomination of less than €50,000 (or its equivalent in the relevant Specified Currency).

In the case of a Series and Class of Notes with more than one Specified Denomination, Notes of one Specified Denomination may not be exchanged for Notes of such Series and Class of another Specified Denomination.

### 1.2 Register

The Registrar will maintain the Register in respect of the Notes in accordance with the provisions of the Paying Agent and Agent Bank Agreement. In these Conditions, the **Holder** of a Note means the person in whose name such Note is for the time being registered in the Register (or, in the case of a joint holding, the first named thereof). A Note will be issued to each Noteholder in respect of its registered holding. Each Note will be numbered serially with an identifying number which will be recorded in the Register.

### 1.3 Title

The Holder of each Note shall (to the fullest extent permitted by applicable law) be treated by the Issuer, the Note Trustee, the Issuer Security Trustee, the Agent Bank and any other Agent as the absolute owner of such Note for all purposes (including the making of any payments) regardless of any notice of ownership, theft or loss or any trust or other interest therein or of any writing thereon (other than the endorsed form of transfer).

### 1.4 Transfers

- (a) Title to the Notes shall pass by and upon registration in the Register. Subject as provided otherwise in this **Condition 1.4**, a Note may be transferred upon surrender of the relevant Note, with the endorsed form of transfer duly completed, at the Specified Office of the Registrar or the Transfer Agent, together with such evidence as the Registrar or (as the case may be) such Transfer Agent may reasonably require to prove the title of the transferor and the authority of the individuals who have executed the form of transfer; provided, however, that a Note may only be transferred in the minimum denominations specified in the applicable Final Terms. Where not all the Notes represented by the surrendered Note are the subject of the transfer, a new Note in respect of the balance of the Notes will be issued to the transferor.

Within five Business Days of such surrender of a Note, the Registrar will register the transfer in question and deliver a new Note of a like principal amount to the Notes transferred to each relevant Holder at its Specified Office or (as the case may be) the Specified Office of the Transfer Agent or (at the request and risk of any such relevant Holder) by uninsured first class mail (and by airmail if the Holder is overseas) to the address specified for such purpose by such relevant Holder.

The transfer of a Note will be effected without charge by the Registrar, but subject to payment of (or the giving of such indemnity as the Registrar may require for) any tax or other governmental charges which may be imposed in relation to it.

Noteholders may not require transfers of Notes to be registered during the period of 15 days ending on the due date for any payment of principal or interest in respect of the Notes.

All transfers of Notes and entries on the Register are subject to the detailed regulations concerning the transfer of Notes scheduled to the Paying Agent and Agent Bank Agreement. The regulations may be changed by the Issuer with the prior written approval of the Note Trustee and the Registrar. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests in writing a copy of such regulations.

The Notes are not issuable in bearer form.

- (b) Prior to expiry of the applicable Distribution Compliance Period, transfers by the holder of, or a beneficial interest in, a Reg S Note to a transferee in the United States or who is a US person will only be made:
- (i) upon receipt by the Registrar of a duly completed transfer certificate from the transferor of the Note or beneficial interest therein to the effect that such transfer is being made to a person whom the transferor reasonably believes is a QIB in a transaction meeting the requirements of Rule 144A; or
  - (ii) otherwise pursuant to the Securities Act or an exemption therefrom, subject to receipt by the Issuer of such satisfactory evidence as the Issuer may reasonably require, which may include an opinion of US counsel, that such transfer is in compliance with any applicable securities laws or any state of the United States,

and, in each case, in accordance with any applicable securities laws of any state of the United States or any other jurisdiction. In the case of (i) above, such transferee may take delivery through a Rule 144A Note. After expiry of the applicable Distribution Compliance Period (i) beneficial interests in Reg S Notes registered in the name of a nominee for DTC may be held through DTC directly, by a participant in DTC or indirectly through a participant in DTC and (ii) such certification requirements will no longer apply to such transfers.

- (c) Transfers of Rule 144A Notes or beneficial interests therein may be made:
- (i) to a transferee who takes delivery of such interest through a Reg S Note, upon receipt by the Registrar of a duly completed transfer certificate from the transferor to the effect that



such transfer is being made in accordance with Regulation S and that in the case of a Reg S Note registered in the name of a nominee for DTC, if such transfer is being made prior to expiry of the applicable Distribution Compliance Period, the interest in the Notes being transferred will be held immediately thereafter through Euroclear and/or Clearstream, Luxembourg; or

- (ii) to a transferee who takes delivery of such interest through a Rule 144A Note where the transferee is a person whom the transferor reasonably believes is a QIB in a transaction meeting the requirements of Rule 144A, without certification; or
- (iii) otherwise pursuant to the Securities Act or an exemption therefrom, subject to receipt by the Issuer of such satisfactory evidence as the Issuer may reasonably require, which may include an opinion of US counsel, that such transfer is in compliance with any applicable securities laws of any state of the United States,

and, in each case, in accordance with any applicable securities laws of any state of the United States or any other jurisdiction. Upon the transfer, exchange or replacement of Rule 144A Notes, or upon specific request for removal of the legend thereon, the Registrar shall deliver only Rule 144A Notes or refuse to remove the legend, as the case may be, unless there is delivered to the Issuer such satisfactory evidence as may reasonably be required by the Issuer, which may include an opinion of US counsel, that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

## **2. Status, Priority and Security**

### **2.1 Status**

The Notes are direct, secured and unconditional obligations of the Issuer.

Subject to the provisions of **Conditions 4** and **5** and subject to the other payment conditions set out in the applicable Final Terms and the other Transaction Documents:

- (a) the Class A Notes of each Series will rank *pari passu* without any preference or priority among themselves and with the Class A Notes of each other Series but in priority to the Class B Notes, the Class M Notes, the Class C Notes and the Class D Notes of any Series;
- (b) the Class B Notes of each Series will rank *pari passu* without any preference or priority among themselves and with the Class B Notes of each other Series but in priority to the Class M Notes, the Class C Notes and the Class D Notes of any Series;
- (c) the Class M Notes of each Series will rank *pari passu* without any preference or priority among themselves and with the Class M Notes of each other Series but in priority to the Class C Notes and the Class D Notes of any Series;
- (d) the Class C Notes of each Series will rank *pari passu* without any preference or priority among themselves and with the Class C Notes of each other Series but in priority to the Class D Notes of any Series; and
- (e) the Class D Notes of each Series will rank *pari passu* without any preference or priority among themselves and with the Class D Notes of each other Series.

### **2.2 Conflict between the classes of Notes**

The Note Trust Deed contains provisions requiring the Note Trustee to have regard to the interests of the Class A Noteholders, the Class B Noteholders, the Class M Noteholders, the Class C Noteholders and the Class D Noteholders equally as regards all powers, trusts, authorities, duties and discretions of the Note Trustee under these Conditions or any of the Transaction Documents (except where expressly provided otherwise), but requiring the Note Trustee to have regard (except as expressly provided otherwise):

- (a) for so long as there are any Class A Notes outstanding, only to the interests of the Class A Noteholders if, in the opinion of the Note Trustee, there is or may be a conflict between the interests of the Class A Noteholders and the interests of the Class B Noteholders and/or the interests of the Class M Noteholders and/or the interests of the Class C Noteholders and/or the interests of the Class D Noteholders;

- (b) subject to (a) above and for so long as there are any Class B Notes outstanding, only to the interests of the Class B Noteholders if, in the opinion of the Note Trustee, there is or may be a conflict between the interests of the Class B Noteholders and the interest of the Class M Noteholders and/or the interests of the Class C Noteholders and/or the interests of the Class D Noteholders;
- (c) subject to (a) and (b) above and for so long as there are any Class M Notes outstanding, only to the interests of the Class M Noteholders if, in the opinion of the Note Trustee, there is or may be a conflict between the interests of the Class M Noteholders and the interests of the Class C Noteholders and/or the interests of the Class D Noteholders; and
- (d) subject to (a), (b) and (c) above and for so long as there are any Class C Notes outstanding, only to the interests of the Class C Noteholders if, in the opinion of the Note Trustee, there is or may be a conflict between the interests of the Class C Noteholders and the Class D Noteholders.

The Note Trust Deed also contains provisions:

- (i) limiting the powers of the Class B Noteholders, the Class M Noteholders, the Class C Noteholders and the Class D Noteholders, in each case of any Series, *inter alia*, to request or direct the Note Trustee to take any action or to pass an effective Extraordinary Resolution according to the effect thereof on the interests of the Class A Noteholders of that Series or of any other Series. Except in certain circumstances described in **Condition 11**, the Note Trust Deed contains no such limitation on the powers of the Class A Noteholders, the exercise of which will be binding on the Class B Noteholders, the Class M Noteholders, the Class C Noteholders and the Class D Noteholders, in each case of any Series, irrespective of the effect thereof on their respective interests;
- (ii) limiting the powers of the Class M Noteholders, the Class C Noteholders and the Class D Noteholders, in each case of any Series, *inter alia*, to request or direct the Note Trustee to take any action or to pass an effective Extraordinary Resolution according to the effect thereof on the interests of the Class B Noteholders of that Series or of any other Series. Except in certain circumstances described above and in **Condition 11**, the Note Trust Deed contains no such limitation on the powers of the Class B Noteholders, the exercise of which will be binding on the Class M Noteholders, the Class C Noteholders and the Class D Noteholders, in each case of any Series, irrespective of the effect thereof on their respective interests;
- (iii) limiting the powers of the Class C Noteholders and the Class D Noteholders, in each case of any Series, *inter alia*, to request or direct the Note Trustee to take any action or to pass an effective Extraordinary Resolution according to the effect thereof on the interests of the Class M Noteholders of that Series or of any other Series. Except in certain circumstances described above and in **Condition 11**, the Note Trust Deed contains no such limitation on the powers of the Class M Noteholders, the exercise of which will be binding on the Class C Noteholders and the Class D Noteholders, in each case of any Series, irrespective of the effect thereof on their interests; and
- (iv) limiting the powers of the Class D Noteholders of any Series, *inter alia*, to request or direct the Note Trustee to take any action or to pass an effective Extraordinary Resolution according to the effect thereof on the interests of the Class C Noteholders of that Series or of any other Series. Except in certain circumstances described above and in **Condition 11**, the Note Trust Deed contains no such limitation on the powers of the Class C Noteholders, the exercise of which will be binding on the Class D Noteholders of any Series, irrespective of the effect thereof on their respective interests.

The Note Trustee shall be entitled to assume, for the purpose of exercising any right, power, trust, authority, duty or discretion under or in relation to these Conditions or any of the Transaction Documents, without further investigation or inquiry, that such exercise will not be materially prejudicial to the interests of the Noteholders (or any Series and Class thereof), if each of the Rating Agencies rating the relevant Series and Class has confirmed in writing that the then current ratings of the relevant Series and Class of Notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified by such exercise.

## **2.3 Security**

As security for, *inter alia*, the payment of all monies payable in respect of the Notes, the Issuer has entered into the Issuer Deed of Charge creating the Issuer Security in favour of the Issuer Security Trustee on trust for, *inter alios*, itself, the Note Trustee and the Noteholders.

## **3. Covenants**

Save with the prior written consent of the Note Trustee or unless provided in or contemplated under these Conditions or any of the Transaction Documents to which the Issuer is a party, the Issuer shall not, so long as any Note remains outstanding:

### **3.1 Negative Pledge**

create or permit to subsist any mortgage, standard security, pledge, lien, charge or other Security Interest whatsoever (unless arising by operation of law), upon the whole or any part of its assets (including any uncalled capital) or its undertakings, present or future, except where the same is given in connection with an Issuance of Notes or the advance of an Issuer Subordinated Loan;

### **3.2 Disposal of Assets**

sell, assign, transfer, lend, lease or otherwise dispose of, or deal with, or grant any option or present or future right to acquire all or any of its properties, assets or undertakings or any interest, estate, right, title or benefit therein or thereto or agree or attempt or purport to do any of the foregoing;

### **3.3 Equitable Interest**

permit any person other than itself and the Issuer Security Trustee (as to itself and on behalf of the Issuer Secured Creditors) to have any equitable or beneficial interest in any of its assets or undertakings or any interest, estate, right, title or benefit therein;

### **3.4 Bank Accounts**

have an interest in any bank account, other than the Issuer Bank Accounts, except in connection with an Issuance of Notes or the advance of an Issuer Subordinated Loan where such bank account is immediately charged in favour of the Issuer Security Trustee pursuant to the Issuer Deed of Charge;

### **3.5 Restrictions on Activities**

carry on any business other than as described in the Base Prospectus and the related activities described therein or as contemplated in the Transaction Documents;

### **3.6 Borrowings**

incur any indebtedness in respect of borrowed money whatsoever or give any guarantee or indemnity in respect of any indebtedness or obligation of any person, except where the same is incurred or given or the Issuer becomes so obligated in connection with an Issuance of Notes or the advance of an Issuer Subordinated Loan;

### **3.7 Merger**

consolidate or merge with any other person or convey or transfer substantially all of its properties or assets to any other person;

### **3.8 Waiver or Consent**

permit the validity or effectiveness of any of the Note Trust Deed or the Issuer Deed of Charge or the priority of the security interests created thereby to be amended, terminated, postponed, waived or discharged, or permit any other person whose obligations form part of the Issuer Security to be released from such obligations;

### **3.9 Employees or premises**

have any employees or premises or subsidiaries;

### 3.10 Dividends and Distributions

pay any dividend or make any other distribution to its shareholders, except where the proceeds of such dividend will be used entirely by Holdings to pay interest on or repay principal of the Issuer Capitalisation Loan, or issue any further shares or alter any rights attaching to its shares as at the date of the Issuer Deed of Charge;

### 3.11 Purchase Notes

purchase or otherwise acquire any Note or Notes; or

### 3.12 United States activities

engage in any activities in the United States (directly or through agents), or derive any income from United States sources as determined under United States income tax principles, or hold any property if doing so would cause it to be engaged in a trade or business within the United States as determined under United States income tax principles.

## 4. Interest

### 4.1 Interest on Fixed Rate Notes

Each Fixed Rate Note bears interest on its Principal Amount Outstanding from (and including) the Interest Commencement Date at the rate(s) per annum payable equal to the Rate(s) of Interest specified in the applicable Final Terms, subject as provided in these Conditions, in arrear on the Interest Payment Date(s) in each year specified in the applicable Final Terms for such Fixed Rate Note up to (and including) the Final Maturity Date.

Except as provided in the applicable Final Terms, the amount of interest payable in respect of any Fixed Rate Note on each Interest Payment Date for an Interest Period ending on (but excluding) such date will amount to the Fixed Coupon Amount. Payments of interest on any Interest Payment Date will, if so specified for such Fixed Rate Note in the applicable Final Terms, amount to the Broken Amount so specified.

If interest is required to be calculated in respect of any Fixed Rate Note for a period other than an Interest Period, such interest shall be calculated by applying the Rate of Interest specified in the applicable Final Terms to the Principal Amount Outstanding on such Fixed Rate Note, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention and (in the case of a Global Note) apportioning the resulting total between the Noteholders in respect thereof *pro rata* and *pari passu*.

**Day Count Fraction** means, in respect of the calculation of an amount of interest for any Fixed Rate Note in accordance with this **Condition 4.1**:

- (a) if “Actual/Actual (ICMA)” is specified for such Fixed Rate Note in the applicable Final Terms:
  - (i) in the case of Fixed Rate Notes where the number of days in the relevant period from (and including) the most recent Interest Payment Date for such Fixed Rate Notes (or, if none, the Interest Commencement Date) to (but excluding) the relevant Interest Payment Date (the **Accrual Period**) is equal to or shorter than the Determination Period during which the Accrual Period ends, the number of days in such Accrual Period divided by the product of (A) the number of days in such Determination Period and (B) the number of Determination Dates (as specified in the applicable Final Terms) that would occur in one calendar year; or
  - (ii) in the case of Fixed Rate Notes where the Accrual Period is longer than the Determination Period during which the Accrual Period ends, the sum of:
    - (A) the number of days in such Accrual Period falling in the Determination Period in which the Accrual Period begins divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Dates that would occur in one calendar year; and

- (B) the number of days in such Accrual Period falling in the next Determination Period divided by the product of (I) the number of days in such Determination Period and (II) the number of Determination Dates that would occur in one calendar year; and
- (b) if “30/360” is specified for such Fixed Rate Note in the applicable Final Terms, the number of days in the period from (and including) the most recent Interest Payment Date for such Fixed Rate Note (or, if none, the Interest Commencement Date) to (but excluding) the relevant Interest Payment Date (such number of days being calculated on the basis of a year of 360 days with twelve 30-day months) divided by 360.

As used in these Conditions, **Determination Period** means each period from (and including) a Determination Date (as defined in the applicable Final Terms) to (but excluding) the next Determination Date (including where either the Interest Commencement Date or the final Interest Payment Date is not a Determination Date, the period commencing on the first Determination Date prior to, and ending on the first Determination Date falling after, such date).

## 4.2 Interest on Floating Rate Notes

### (a) Interest Payment Dates

Each Floating Rate Note bears interest on its Principal Amount Outstanding from (and including) the Interest Commencement Date and such interest will be payable in arrear on the Interest Payment Date(s) in each year specified in the applicable Final Terms for such Floating Rate Note. Such interest will be payable in respect of each Interest Period.

If a Business Day Convention is specified for a Floating Rate Note in the applicable Final Terms and (x) if there is no numerically corresponding day in the calendar month in which a Interest Payment Date should occur or (y) if any Interest Payment Date would otherwise fall on a day which is not a Business Day, then, if the Business Day Convention specified is:

- (i) the “Following Business Day Convention”, the Interest Payment Date for such Floating Rate Note shall be postponed to the next day which is a Business Day; or
- (ii) the “Modified Following Business Day Convention”, the Interest Payment Date for such Floating Rate Note shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event such Interest Payment Date shall be brought forward to the immediately preceding Business Day; or
- (iii) the “Preceding Business Day Convention”, the Interest Payment Date for such Floating Rate Note shall be brought forward to the immediately preceding Business Day.

In these Conditions, **Business Day** means a day which is both:

- (i) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London, New York and any Additional Business Centre specified in the applicable Final Terms;
- (ii) a day on which the Trans-European Automated Real-Time Gross Settlement Express Transfer (TARGET and TARGET2) System (the **TARGET System**) is open; and
- (iii) in relation to any sum payable in a Specified Currency other than sterling, dollars or euro, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial centre of the country of the relevant Specified Currency (if other than London, New York and any Additional Business Centre).

### (b) Rate of Interest

The Rate of Interest payable from time to time in respect of a Floating Rate Note will be determined in the manner specified for such Floating Rate Note in the applicable Final Terms.

#### (i) ISDA Determination for Floating Rate Notes

Where “ISDA Determination” is specified for such Floating Rate Note in the applicable Final Terms as the manner in which the Rate of Interest is to be determined, the Rate of

Interest for each Interest Period will be the relevant ISDA Rate plus or minus (as indicated for such Floating Rate Note in the applicable Final Terms) the Margin (if any). For the purposes of this subparagraph (i), **ISDA Rate** for an Interest Period means a rate equal to the Floating Rate that would be determined by the Agent Bank or other person specified in the applicable Final Terms under an interest rate swap transaction if the Agent Bank or that other person were acting as Calculation Agent for that swap transaction under the terms of an agreement incorporating the ISDA Definitions and under which:

- (A) the Floating Rate Option is as specified for such Floating Rate Note in the applicable Final Terms;
- (B) the Designated Maturity is the period specified for such Floating Rate Note in the applicable Final Terms; and
- (C) the relevant Reset Date is either (i) if the applicable Floating Rate Option is based on LIBOR or EURIBOR for a currency, the first day of that Interest Period or (ii) in any other case, as specified for such Floating Rate Note in the applicable Final Terms.

For the purposes of this subparagraph (i), **Floating Rate, Calculation Agent, Floating Rate Option, Designated Maturity** and **Reset Date** have the meanings given to those terms in the ISDA Definitions.

(ii) Screen Rate Determination for Floating Rate Notes

Where **Screen Rate Determination** is specified for a Floating Rate Note in the applicable Final Terms as the manner in which the Rate of Interest is to be determined for such Floating Rate Note, the Rate of Interest for each Interest Period will, subject as provided below, be either:

- (A) the offered quotation (if there is only one quotation on the Relevant Screen Page); or
- (B) the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the offered quotations,

(expressed as a percentage rate per annum) for the Reference Rate which appears or appear, as the case may be, on the Relevant Screen Page as at 11.00 a.m. (London time, in the case of LIBOR, or Brussels time, in the case of EURIBOR) on the Determination Date in question plus or minus the Margin (if any), all as determined by the Agent Bank. If five or more of such offered quotations are available on the Relevant Screen Page, the highest (or, if there is more than one such highest quotation, one only of such quotations) and the lowest (or, if there is more than one such lowest quotation, one only of such quotations) shall be disregarded by the Agent Bank for the purpose of determining the arithmetic mean (rounded as provided above) of such offered quotations.

The Paying Agent and Agent Bank Agreement contains provisions for determining the Rate of Interest pursuant to this subparagraph (ii) in the event that the Relevant Screen Page is not available or if, in the case of (A) above, no such offered quotation appears or, in the case of (B) above, fewer than three such offered quotations appear, in each case as at the time specified in the preceding paragraph.

If the Reference Rate from time to time in respect of a Floating Rate Note is specified for such Floating Rate Note in the applicable Final Terms as being other than LIBOR or EURIBOR, the Rate of Interest in respect of such Floating Rate Note will be determined as provided for such Floating Rate Note in the applicable Final Terms.

(c) Minimum Rate of Interest and/or Maximum Rate of Interest

If the applicable Final Terms specifies a Minimum Rate of Interest for a Floating Rate Note for any Interest Period, then, in the event that the Rate of Interest for such Floating Rate Note in respect of such Interest Period determined in accordance with the provisions of paragraph (b) above is less than such Minimum Rate of Interest, the Rate of Interest for such Floating Rate Note for such Interest Period shall be such Minimum Rate of Interest.

If the applicable Final Terms specifies a Maximum Rate of Interest for such Note for any Interest Period, then, in the event that the Rate of Interest for such Floating Rate Note in respect of such Interest Period determined in accordance with the provisions of paragraph (b) above is greater than such Maximum Rate of Interest, the Rate of Interest for such Floating Rate Note for such Interest Period shall be such Maximum Rate of Interest.

(d) Determination of Rate of Interest and calculation of Interest Amounts

The Agent Bank will at or as soon as practicable after each time at which the Rate of Interest is to be determined, determine the Rate of Interest for the relevant Interest Period.

The Agent Bank will calculate the amount of interest payable on the Floating Rate Notes in respect of each Specified Denomination or (in the case of a Global Note) the Principal Amount Outstanding thereunder (each an **Interest Amount**) for the relevant Interest Period. Each Interest Amount shall be calculated by applying the Rate of Interest to the Principal Amount Outstanding of each Floating Rate Note, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention and (in the case of a Global Note) apportioning the resulting total between the Noteholders in respect thereof *pro rata* and *pari passu*.

**Day Count Fraction** means, in respect of the calculation of an amount of interest for a Floating Rate Note in accordance with this Condition 4.2(d) for any Interest Period:

- (a) if **Actual/365** or **Actual/Actual (ISDA)** is specified for such Floating Rate Note in the applicable Final Terms, the actual number of days in the Interest Period divided by 365 (or, if any portion of that Interest Period falls in a leap year, the sum of (A) the actual number of days in that portion of the Interest Period falling in a leap year divided by 366 and (B) the actual number of days in that portion of the Interest Period falling in a non-leap year divided by 365);
- (b) if **Actual/365 (Fixed)** is specified for such Floating Rate Note in the applicable Final Terms, the actual number of days in the Interest Period divided by 365;
- (c) if **Actual/365 (Sterling)** is specified for such Floating Rate Note in the applicable Final Terms, the actual number of days in the Interest Period divided by 365 or, in the case of a Interest Payment Date falling in a leap year, 366;
- (d) if **Actual/360** is specified for such Floating Rate Note in the applicable Final Terms, the actual number of days in the Interest Period divided by 360;
- (e) if **30/360**, **360/360** or **Bond Basis** is specified for such Floating Rate Note in the applicable Final Terms, the number of days in the Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with twelve 30-day months (unless (a) the last day of the Interest Period is the 31st day of a month but the first day of the Interest Period is a day other than the 30th or 31st day of a month, in which case the month that includes that last day shall not be considered to be shortened to a 30-day month, or (b) the last day of the Interest Period is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month)); and
- (f) if **30E/360** or **Eurobond Basis** is specified for such Floating Rate Note in the applicable Final Terms, the number of days in the Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with twelve 30-day months, without regard to the date of the first day or last day of the Interest Period unless, in the case of the final Interest Period, the Final Maturity Date is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month).

(e) Notification of Rate of Interest and Interest Amounts

The Agent Bank will cause the Rate of Interest and each Interest Amount for each Interest Period and the relevant Interest Payment Date to be notified to the Note Trustee, the Issuer Security Trustee, the Issuer Cash Manager, the Paying Agents, the Registrar and to any stock exchange or other relevant competent authority or quotation system on which the relevant Floating Rate Notes are for the time being listed, quoted and/or traded or by which they have been admitted to listing and to be published

in accordance with **Condition 14** as soon as possible after their determination but in no event later than the fourth Business Day thereafter. Each Interest Amount and Interest Payment Date so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without notice in the event of an extension or shortening of the Interest Period. Any such amendment or alternative arrangements will be promptly notified to the Note Trustee and each stock exchange or other relevant authority on which the relevant Floating Rate Notes are for the time being listed or by which they have been admitted to listing and to Noteholders in accordance with **Condition 14**.

(f) Determination or Calculation by Note Trustee

If, for any reason at any relevant time, the Agent Bank or, as the case may be, the Calculation Agent defaults in its obligation to determine the Rate of Interest for a Floating Rate Note or the Agent Bank defaults in its obligation to calculate any Interest Amount for such Note in accordance with **subparagraph (i) or (ii) above** or as otherwise specified for such Note in the applicable Final Terms, as the case may be, and in each case in accordance with **paragraph (d) above**, the Note Trustee shall use reasonable efforts to determine the Rate of Interest at such rate as, in its absolute discretion (having such regard as it shall think fit to the foregoing provisions of this Condition, but subject always to any Minimum Rate of Interest or Maximum Rate of Interest specified for such Note in the applicable Final Terms), it shall deem fair and reasonable in all the circumstances or, as the case may be, the Note Trustee shall calculate the Interest Amount(s) in such manner as it shall deem fair and reasonable in all the circumstances and each such determination or calculation shall be deemed to have been made by the Agent Bank or the Calculation Agent, as the case may be.

(g) Certificates to be final

All certificates, communications, opinions, determinations, calculations, quotations and decisions given, expressed, made or obtained for the purposes of the provisions of this **Condition 4.2**, whether by the Agent Bank or the Calculation Agent or the Note Trustee shall (in the absence of wilful default, bad faith or manifest error) be binding on the Issuer, the Issuer Cash Manager, the Principal Paying Agent, the Calculation Agent, the other Paying Agents, the Note Trustee and all Noteholders and (in the absence of wilful default or bad faith) no liability to the Issuer or the Noteholders shall attach to the Agent Bank or the Calculation Agent or the Note Trustee in connection with the exercise or non-exercise by it of its powers, duties and discretions pursuant to such provisions.

#### 4.3 Accrual of interest

Interest (if any) will cease to accrue on each Note (or in the case of the redemption of part only of a Note, that part only of such Note) on the due date for redemption thereof unless, upon due presentation thereof, payment of principal is improperly withheld or refused, in which event interest will continue to accrue until the earlier of:

- (a) the date on which all amounts due in respect of such Note have been paid; and
- (b) the seventh day after notice is duly given by the Principal Paying Agent or the US Paying Agent (as the case may be) to the Holder thereof that such payment will be made, provided that subsequently payment is in fact made.

#### 4.4 Deferred Interest

To the extent that, subject to and in accordance with the relevant Issuer Priority of Payments, the funds available to the Issuer to pay interest on any Series and Class of Notes (other than any Series and Class of Notes if then the most senior Class of Notes then outstanding) on an Interest Payment Date (after discharging the Issuer's liabilities of a higher priority) are insufficient to pay the full amount of such interest, payment of the shortfall attributable to such Series and Class of Notes (**Deferred Interest**) will not then fall due but will instead be deferred until the first Interest Payment Date for such Series and Class of Notes thereafter on which sufficient funds are available (after allowing for the Issuer's liabilities of a higher priority and subject to and in accordance with the relevant Issuer Priority of Payments) to fund the payment of such Deferred Interest to the extent of such available funds.

Such Deferred Interest will accrue interest (**Additional Interest**) at the Rate of Interest applicable from time to time to the applicable Series and Class of Notes and payment of any Additional Interest will also be deferred until the first Interest Payment Date for such Series and Class of Notes thereafter on which funds are available (after allowing for the Issuer's liabilities of a higher priority subject to



and in accordance with the relevant Issuer Priority of Payments) to the Issuer to pay such Additional Interest to the extent of such available funds.

Amounts of Deferred Interest and Additional Interest shall not be deferred beyond the Final Maturity Date of the applicable Series and Class of Notes, when such amounts will become due and payable.

Payments of interest due on an Interest Payment Date in respect of the most senior Class of Notes of any Series then outstanding will not be deferred. In the event of the delivery of a Note Acceleration Notice (as described in **Condition 9**), the amount of interest in respect of any such Notes that was due but not paid on such Interest Payment Date will itself bear interest at the applicable rate until both the unpaid interest and the interest on that interest are paid as provided in the Note Trust Deed.

## **5. Redemption, Purchase and Cancellation**

### **5.1 Final Redemption**

Unless previously redeemed in full as provided in this **Condition 5**, the Issuer shall redeem a Series and Class of Notes at their then Principal Amount Outstanding together with all accrued interest on the Final Maturity Date in respect of such Notes.

The Issuer may not redeem such Notes in whole or in part prior to their Final Maturity Date except as provided in **Conditions 5.2, 5.4, 5.5 or 5.6**, but without prejudice to **Condition 9**.

### **5.2 Mandatory Redemption of the Notes in Part**

On each Interest Payment Date, other than an Interest Payment Date on which a Series and Class of Notes are to be redeemed under **Conditions 5.1, 5.4, 5.5 or 5.6**, the Issuer shall repay principal in respect of such Series and Class of Notes in an amount equal to the amount (if any) repaid on the corresponding Funding 1 Interest Payment Date in respect of the related Loan Tranche and pursuant to the Intercompany Loan Agreement converted, where the Specified Currency for such Notes is not Sterling, into the Specified Currency at the Specified Currency Exchange Rate for such Series and Class of Notes.

To the extent that there are insufficient funds available to the Issuer to repay the amount due to be paid on such Interest Payment Date, the Issuer will be required to repay the shortfall to the extent that it receives funds therefor (and subject to the terms of the Issuer Deed of Charge and the Issuer Cash Management Agreement) on subsequent Interest Payment Dates in respect of such Series and Class of Notes.

### **5.3 Note Principal Payments and Principal Amount Outstanding**

The principal amount redeemable (the **Note Principal Payment**) in respect of each Note of a particular Series and Class on any Interest Payment Date under **Condition 5.2** shall be a proportion of the amount required as at that Interest Payment Date to be applied in redemption of such Series and Class of Notes on such date equal to the proportion that the Principal Amount Outstanding of the relevant Note bears to the aggregate Principal Amount Outstanding of such Series and Class of Notes rounded down to the nearest sub-unit of the Specified Currency; provided always that no such Note Principal Payment may exceed the Principal Amount Outstanding of the relevant Note.

On each Note Determination Date the Issuer shall determine (or cause the Agent Bank to determine) (a) the amount of any Note Principal Payment payable in respect of each Note of the relevant Series and Class on the immediately following Interest Payment Date and (b) the Principal Amount Outstanding of each such Note which shall be the Specified Denomination less (in each case) the aggregate amount of all Note Principal Payments in respect of such Note that has been paid since the relevant Closing Date and on or prior to that Note Determination Date (the **Principal Amount Outstanding**) and (c) the fraction expressed as a decimal to the fifth decimal point (the **Pool Factor**), of which the numerator is the Principal Amount Outstanding of that Note (as referred to in (b) above) and the denominator is the Specified Denomination. Each determination by or on behalf of the Issuer of the Note Principal Payment of a Note, the Principal Amount Outstanding of a Note and the Pool Factor shall in each case (in the absence of wilful default, bad faith or manifest error) be final and binding on all persons.

The Issuer will cause each determination of the Note Principal Payment and the Principal Amount Outstanding and the Pool Factor in respect of a Series and Class of Notes to be notified forthwith, and in any event not later than 1.00 p.m. (London time) on the Business Day immediately succeeding the Note Determination Date, to the Note Trustee, the Issuer Security Trustee, the Issuer Cash Manager,

the Paying Agents, the Agent Bank, the Registrar and (for so long as such Notes are listed on one or more stock exchanges) the relevant stock exchanges and will cause notice of each determination of the Note Principal Payment and the Principal Amount Outstanding to be given to Noteholders in accordance with **Condition 14** by no later than the Business Day after the relevant Interest Payment Date.

If the Issuer does not at any time for any reason determine (or cause the Agent Bank to determine) a Note Principal Payment, the Principal Amount Outstanding or the Pool Factor in accordance with the preceding provisions of this **Condition 5.3**, such Note Principal Payment and/or Principal Amount Outstanding and/or Pool Factor may be determined by the Note Trustee in accordance with this **Condition 5.3** in the manner the Note Trustee in its discretion considers fair and reasonable in the circumstances, having regard to this **Condition 5.3**, and each such determination or calculation shall be deemed to have been made by the Issuer. Any such determination shall (in the absence of wilful default, bad faith or manifest error) be binding on the Issuer, the Agent Bank and the Noteholders.

#### **5.4 Optional Redemption in Full**

Provided a Note Acceleration Notice has not been served and subject to the provisos below, upon giving not more than 60 nor less than 30 days' prior written notice to the Note Trustee, the relevant Issuer Swap Provider(s) and the Noteholders in accordance with **Condition 14**, the Issuer may redeem a Series and Class of Notes at their aggregate Redemption Amount together with any accrued and unpaid interest in respect thereof on the following dates:

- (a) the date specified as the Call Option Date (if any) for such Series and Class of Notes in the applicable Final Terms and on any Interest Payment Date for such Series and Class of Notes thereafter; or
- (b) the date specified as the Step-Up Date for such Series and Class of Notes (if any) in the applicable Final Terms and on any Interest Payment Date for such Series and Class of Notes thereafter; or
- (c) on such Interest Payment Date on which the aggregate Principal Amount Outstanding of such Series and Class of Notes and all other Classes of Notes of the same Series is less than 10 per cent. of the aggregate Principal Amount Outstanding of such Series of Notes as at the Closing Date on which such Series of Notes were issued,

PROVIDED THAT (in either of the cases above), on or prior to giving any such notice, the Issuer shall have provided to the Note Trustee a certificate signed by two directors of the Issuer to the effect that (i) it will have the necessary funds to pay all amounts due in respect of the relevant Series and Class of Notes on the relevant Interest Payment Date and to discharge all other amounts required to be paid by it on the relevant Interest Payment Date in priority to or *pari passu* with such Series and Class of Notes in accordance with the applicable Issuer Priority of Payments.

The Issuer may only redeem the Notes as described (a) and (b) above if (1) the amount standing to the credit of the Funding 1 general reserve ledger is equal to or greater than the Funding 1 reserve required amount; or (2) each rating agency has provided written confirmation that the redemption will not result in a reduction, withdrawal or (in the case of S&P and Moody's) qualification of the then current ratings of the notes then outstanding.

#### **5.5 Optional Redemption for Tax and other Reasons**

Provided a Note Acceleration Notice has not been served, if the Issuer at any time satisfies the Note Trustee immediately prior to the giving of the notice referred to below that:

- (a) on the next Interest Payment Date, the Issuer would by virtue of a change in the law or regulations of the United Kingdom or any other jurisdiction (or the application or interpretation thereof) be required to deduct or withhold from any payment of principal or interest or any other amount under a Series and Class of Notes any amount for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature (other than where the relevant Holder or beneficial owner has some connection with the relevant jurisdiction other than the holding of the Notes); or
- (b) on the next Interest Payment Date, Funding 1 would be required to deduct or withhold from amounts due in respect of the Rated Loan Tranche under the Intercompany Loan Agreement which was funded by such Series and Class of Notes any amount for or on

account of any present or future taxes, duties, assessments or governmental charges of whatever nature; or

- (c) the Issuer or Funding 1, as the case may be, has ceased or will cease to fall within the Securitisation Tax Regime; and
- (d) in relation to any of the events described in (a), (b) and (c) above, such obligation of the Issuer or Funding 1 (as the case may be) or such ceasing to fall within the Securitisation Tax Regime cannot be avoided by the Issuer or Funding 1 (as the case may be) taking reasonable measures available to the Issuer or Funding 1 (as the case may be),

then (in the case of the events described in (a) and (b) above) the Issuer shall use its reasonable endeavours to arrange the substitution of a company incorporated in another jurisdiction approved by the Note Trustee as principal debtor under such Notes, upon the Note Trustee being satisfied that such substitution will not be materially prejudicial to the interests of the Noteholders of any Series and Class and upon the Issuer Security Trustee being satisfied that (A) the position of the Issuer Secured Creditors will not thereby be adversely affected and (B) such substitution would not require registration of any new security under United States securities laws or materially increase the disclosure requirements under United States law or the costs of issuance. In the case of the events described in (a) and (b) above, only if the Issuer is unable to arrange a substitution will the Issuer be entitled to redeem the Notes as described in this **Condition 5.5**.

Subject to the proviso below, if the Issuer is unable to arrange a substitution as described above and, as a result, one or more of the events described in (a) and (b) above (as the case may be) is continuing, then the Issuer may, having given not more than 60 nor less than 30 days' notice to the Note Trustee, the relevant Issuer Swap Provider(s) and the Noteholders in accordance with **Condition 14**, redeem all (but not some only) of the relevant Series and Class of Notes on the immediately succeeding Interest Payment Date for such Series and Class of Notes at their aggregate Redemption Amount together with any accrued and unpaid interest in respect thereof provided that (in either case), prior to giving any such notice, the Issuer shall have provided to the Note Trustee:

- (i) a certificate signed by two directors of the Issuer stating the circumstances referred to in (a) or (b) and (d) above prevail and setting out details of such circumstances; and
- (ii) an opinion in form and substance satisfactory to the Note Trustee of independent legal advisors of recognised standing to the effect that the Issuer or, as the case may be, Funding 1 has or will become obliged to deduct or withhold such amounts as a result of such change or amendment.

Subject to the proviso below, if the event described in (c) above is continuing, then the Issuer may, having given not more than 60 nor less than 30 days' notice to the Note Trustee, the relevant Issuer Swap Provider(s) and the Noteholders in accordance with **Condition 14**, redeem all (but not some only) of all Series and Classes of Notes on the immediately succeeding Quarterly Interest Payment Date for such Series and Class of Notes at their aggregate Redemption Amount together with any accrued and unpaid interest in respect thereof provided that (in either case), prior to giving any such notice, the Issuer shall have provided to the Note Trustee:

- (i) a certificate signed by two directors of the Issuer stating the circumstances referred to in (c) and (d) above prevail and setting out details of such circumstances; and
- (ii) an opinion in form and substance satisfactory to the Note Trustee of independent legal advisors of recognised standing to the effect that the Issuer or, as the case may be, Funding 1, has or will cease to fall within the Securitisation Tax Regime.

The Note Trustee shall be entitled to accept such certificate and opinion as sufficient evidence of the satisfaction of the circumstance set out in (a), (b) or (c) and (d) above, in which event they shall be conclusive and binding on the Noteholders. The Issuer may only redeem such Series and Class of Notes as aforesaid if, on or prior to giving such notice, the Issuer shall have provided to the Note Trustee a certificate signed by two directors of the Issuer to the effect that it will have the necessary funds to pay all amounts due in respect of the relevant Series and Class of Notes on the relevant Interest Payment Date and to discharge all other amounts required to be paid by it on the relevant Interest Payment Date in priority to or *pari passu* with such Series and Class of Notes in accordance with the applicable Issuer Priority of Payments.

In addition to the foregoing, if at any time the Issuer delivers a certificate to Funding 1, the Note Trustee and the Issuer Security Trustee to the effect that it would be unlawful for the Issuer to make, fund or allow to remain outstanding a Rated Loan Tranche under the Intercompany Loan Agreement, then the Issuer may require Funding 1 to prepay the relevant Loan Tranche on a Funding 1 Interest Payment Date subject to and in accordance with the provisions of the Intercompany Loan Agreement to the extent necessary to cure such illegality and the Issuer may redeem all (but not some only) of the relevant Series and Class of Notes at their Redemption Amount together with any accrued interest upon giving not more than 60 nor less than 30 days' (or such shorter period as may be required under any relevant law) prior written notice to the Issuer Security Trustee, the Note Trustee, the relevant Issuer Swap Provider(s) and the Noteholders in accordance with **Condition 14**, provided that, prior to giving any notice, the Issuer shall have provided to the Note Trustee a certificate signed by two directors of the Issuer to the effect that it will have the funds, not subject to the interest of any other person, required to redeem the relevant Series and Class of Notes as provided above and any amount to be paid in priority to or *pari passu* with the relevant Series and Class of Notes. Such monies received by the Issuer shall be used to redeem the relevant Series and Class of Notes in full, together with any accrued and unpaid interest, on the equivalent Interest Payment Date.

## 5.6 Reserved

## 5.7 Redemption Amounts

For the purposes of this **Condition 5**, **Redemption Amount** means, in respect of any Series and Class of Notes, the amount specified in relation to such Notes in the applicable Final Terms or, if not so specified:

- (a) in respect of each Note (other than a Zero Coupon Note), the Principal Amount Outstanding of such Note; and
- (b) in respect of each Zero Coupon Note, an amount calculated in accordance with the following formula:

$$\text{Redemption Amount} = \text{RP} \times (1 + \text{AY})^y$$

where:

- RP = the Reference Price;
- AY = the Accrual Yield expressed as a decimal; and
- y = the Day Count Fraction.

If the amount payable in respect of any Zero Coupon Note upon redemption of such Zero Coupon Note pursuant to **Condition 5.1, 5.2, 5.4, 5.5** or **5.6** or upon its becoming due and repayable as provided in **Condition 9** is improperly withheld or refused, the amount due and repayable in respect of such Note shall be the amount calculated as provided in paragraph (b) above as though the reference therein to the date fixed for the redemption or, as the case may be, the date upon which such Note becomes due and payable were replaced by reference to the date which is the earlier of:

- (a) the date on which all amounts due in respect of such Note have been paid; and
- (b) the date on which the full amount of the monies payable in respect of such Note has been received by the Principal Paying Agent or the Note Trustee or the Registrar and notice to that effect has been given to the Noteholders in accordance with Condition 14.

**Day Count Fraction** means, in respect of the calculation of the Redemption Amount for a Zero Coupon Note in accordance with this **Condition 5.7** for any Zero Coupon Period:

- (a) if **Actual/Actual** is specified for such Note in the applicable Final Terms, the actual number of days from (and including) the first Closing Date of the applicable Series and Class of Notes to (but excluding) the date fixed for redemption (the **Zero Coupon Period**) or, as the case may be, the date upon which such Note becomes due and payable divided by 365 (or, if any portion of the Zero Coupon Period falls in one or more leap years, the sum of (A) the actual number of days in the Zero Coupon Period falling in a leap year divided by 366 and (B) the actual number of days in the Zero Coupon Period falling in a non-leap year divided by 365); or

- (b) if **30/360** is specified for such Note in the applicable Final Terms, the number of days (calculated on the basis of a 360-day year consisting of 12 months of 30 days each) during the Zero Coupon Period divided by 360.

## **5.8 Mandatory Transfer of Remarketable Notes**

- (a) The Remarketable Notes shall, subject to paragraph (c) below, be transferred in accordance with paragraph (b) below on each relevant Mandatory Transfer Date prior to the occurrence of a Mandatory Transfer Termination Event (as confirmed by the Remarketing Agent or Tender Agent by the provision of a Conditional Purchaser Confirmation to the Issuer and the Principal Paying Agent) in exchange for payment of the Mandatory Transfer Price, and the Issuer will procure payment of the Mandatory Transfer Price to the Holders of the Remarketable Notes on the relevant Mandatory Transfer Date, provided that the Issuer shall not be liable for the failure to make payment of the Mandatory Transfer Price to the extent that such failure is a result of the failure of the Remarketing Agent or the Conditional Purchaser to perform its obligations under the relevant agreements.
- (b) Subject to paragraphs (a) above and (c) below, all the Noteholders' interests in the Remarketable Notes shall be transferred on the relevant Mandatory Transfer Date to the account of the Remarketing Agent on behalf of the relevant purchasers or as otherwise notified by or on behalf of the Remarketing Agent prior to such date or, if Definitive Notes are then issued with respect to the Remarketable Notes, the Remarketable Notes will be registered in the name of the Remarketing Agent or as otherwise notified by or on behalf of the Remarketing Agent by the Registrar and the Register will be amended accordingly with effect from the relevant Mandatory Transfer Date.
- (c) Any Holder of Remarketable Note may exercise his right to retain such Note through the facilities of DTC at any time prior to the commencement of the Remarketing Period that ends immediately before the relevant Mandatory Transfer Date.

## **6. Payments**

### **6.1 Payment of Interest and Principal**

Payments of principal shall be made by cheque in the Specified Currency, drawn on a Designated Bank, or, upon application by a Holder of the relevant Note, to the Specified Office of the Principal Paying Agent not later than the fifth Business Day before the Record Date (as defined in **Condition 6.7**), by transfer to a Designated Account maintained by the payee with a Designated Bank and (in the case of final redemption) upon surrender (or, in the case of part payment only, endorsement) of the relevant Note at the Specified Office of any Paying Agent.

Payments of interest shall be made by cheque in the Specified Currency drawn on a Designated Bank, or, upon application by a Holder of the relevant Note, to the Specified Office of the Principal Paying Agent not later than the fifth Business Day before the Record Date (as defined in **Condition 6.7**), by transfer to a Designated Account maintained by the payee with a Designated Bank and (in the case of interest payable on final redemption) upon surrender (or, in the case of part payment only, endorsement) of the relevant Note at the Specified Office of any Paying Agent.

### **6.2 Laws and Regulations**

Payments of principal and interest in respect of the Notes are subject in all cases to any fiscal or other laws and regulations applicable thereto. Noteholders will not be charged commissions or expenses on payments.

### **6.3 Payment of Interest following a failure to pay Principal**

If payment of principal is improperly withheld or refused on or in respect of any Note or part thereof, the interest which continues to accrue in respect of such Note in accordance with **Condition 4** will be paid in accordance with this **Condition 6**.

### **6.4 Change of Agents**

The initial Principal Paying Agent, the Registrar, the Transfer Agent and the initial Paying Agents are listed in these Conditions. The Issuer reserves the right, subject to the prior written approval of the Note Trustee, at any time to vary or terminate the appointment of the Principal Paying Agent, the Registrar, the Transfer Agent and the US Paying Agent and to appoint additional or other Paying Agents. The Issuer will at all times maintain a Paying Agent with a Specified Office in London and a US Paying Agent and a Registrar. Except where otherwise provided in the Note Trust Deed, the

Issuer will cause at least 30 days' notice of any change in or addition to the Paying Agents, the Transfer Agent or the Registrar or their Specified Offices to be given in accordance with **Condition 14** and will notify the Rating Agencies of such change or addition. For as long as any Note is outstanding, the Issuer will endeavour to maintain a Paying Agent in a member state of the European Union that will not be obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive.

#### **6.5 No payment on non-Business Day**

Where payment is to be made by transfer to a Designated Account, payment instructions (for value the due date or, if the due date is not a Business Day, for value the next succeeding Business Day) will be initiated and, where payment is to be made by cheque, the cheque will be mailed (a) (in the case of payments of principal and interest payable on redemption) on the later of the due date for payment and the day on which the relevant Note is surrendered (or, in the case of part payment only, endorsed) at the Specified Office of a Paying Agent and (b) (in the case of payments of interest payable other than on redemption) on the due date for payment. A Holder of a Note shall not be entitled to any interest or other payment in respect of any delay in payment resulting from (i) the due date for a payment not being a Business Day or (ii) a cheque mailed in accordance with this **Condition 6.5** arriving after the due date for payment or being lost in the mail.

#### **6.6 Partial Payment**

If a Paying Agent makes a partial payment in respect of any Note, the Issuer shall procure and the Registrar will ensure that the amount and date of such payment are noted on the Register and, in the case of partial payment upon presentation of a Note, that a statement indicating the amount and date of such payment is endorsed on the relevant Note.

#### **6.7 Record Date**

Each payment in respect of a Note will be made to the persons shown as the Holder in the Register at the opening of business in the place of the Registrar's Specified Office on the fifteenth day before the due date for such payment (the **Record Date**). Where payment in respect of a Note is to be made by cheque, the cheque will be mailed to the address shown as the address of the Holder in the Register at the opening of business on the relevant Record Date.

#### **6.8 Payment of Interest**

Subject as provided otherwise in these Conditions, if interest is not paid in respect of a Note of any Class on the date when due and payable (other than because the due date is not a Business Day) or by reason of non-compliance with **Condition 6.1**, then such unpaid interest shall itself bear interest at the Rate of Interest applicable from time to time to such Note until such interest and interest thereon are available for payment and notice thereof has been duly given in accordance with **Condition 14**.

#### **7. Prescription**

Claims against the Issuer for payment of interest and principal on redemption shall be prescribed and become void if the relevant Notes are not surrendered for payment within a period of 10 years from the relevant date in respect thereof. After the date on which a payment under a Note becomes void in its entirety, no claim may be made in respect thereof. In this **Condition 7**, the **relevant date**, in respect of a payment under a Note, is the date on which the payment in respect thereof first becomes due or (if the full amount of the monies payable in respect of those payments under all the Notes due on or before that date has not been duly received by the Principal Paying Agent, the US Paying Agent or the Note Trustee (as the case may be) on or prior to such date) the date on which, the full amount of such monies having been so received and notice to that effect is duly given to Noteholders in accordance with **Condition 14**.

#### **8. Taxation**

All payments in respect of the Notes will be made without withholding or deduction for, or on account of, any present or future taxes, duties or charges of whatsoever nature unless the Issuer or any relevant Paying Agent is required by applicable law to make any payment in respect of the Notes subject to any such withholding or deduction. In that event, the Issuer or such Paying Agent shall make such payment after such withholding or deduction has been made and shall account to the relevant authorities for the amount so required to be withheld or deducted. No Paying Agent nor the

Issuer will be obliged to make any additional payments to Noteholders in respect of such withholding or deduction.

## 9. Events of Default

### 9.1 Class A Noteholders

The Note Trustee in its absolute discretion may (and, if so requested in writing by the Holders of not less than 25 per cent. in aggregate Principal Amount Outstanding of the Class A Notes (which, for this purpose and for the purpose of any Extraordinary Resolution referred to in this **Condition 9.1**, means the Class A Notes of all Series constituted by the Note Trust Deed) or if so directed by or pursuant to an Extraordinary Resolution passed at a meeting of the Holders of the Class A Notes, shall), subject in each case to being indemnified and/or secured to its satisfaction, give notice (a **Class A Note Acceleration Notice**) to the Issuer, the Issuer Security Trustee and the Funding 1 Security Trustee of a Note Event of Default (as defined below) declaring (in writing) the Class A Notes and all other Notes to be due and repayable (and they shall forthwith become due and repayable) at any time after the happening of any of the following events, which is continuing or unwaived:

- (a) default being made for a period of three Business Days in the payment of any amount of principal of or interest on the Class A Notes of any Series when and as the same ought to be paid in accordance with these Conditions; or
- (b) the Issuer failing duly to perform or observe any other obligation binding upon it under the Class A Notes of any Series, the Note Trust Deed, the Issuer Deed of Charge or any other Transaction Document and, in any such case (except where the Note Trustee certifies that, in its sole opinion, such failure is incapable of remedy, in which case no notice will be required), such failure is continuing unremedied for a period of 20 days following the service by the Note Trustee on the Issuer of notice requiring the same to be remedied and the Note Trustee has certified that the failure to perform or observe is materially prejudicial to the interests of the Holders of the Class A Notes; or
- (c) the Issuer, otherwise than for the purposes of such amalgamation or reconstruction as is referred to in **subparagraph (d) below**, ceases or threatens to cease to carry on its business or a substantial part of its business or the Issuer is deemed unable to pay its debts within the meaning of section 123(1)(a), (b), (c) or (d) of the Insolvency Act 1986 (as amended, modified or re-enacted) or becomes unable to pay its debts as they fall due or the value of its assets falls to less than the amount of its liabilities (taking into account for both these purposes its contingent and prospective liabilities) or otherwise becomes insolvent; or
- (d) an order being made or an effective resolution being passed for the winding-up of the Issuer except a winding-up for the purposes of or pursuant to an amalgamation, restructuring or merger the terms of which have previously been approved by the Note Trustee in writing or by an Extraordinary Resolution of the Holders of the Class A Notes; or
- (e) proceedings being otherwise initiated against the Issuer under any applicable liquidation, insolvency, composition, reorganisation or other similar laws (including, but not limited to, presentation of a petition for an administration order, the filing of documents with the court for an administration or the service of a notice of intention to appoint an administrator) and (except in the case of presentation of a petition for an administration order) such proceedings are not, in the sole opinion of the Note Trustee, being disputed in good faith with a reasonable prospect of success, or an administration order being granted or the appointment of an administrator takes effect or an administrative receiver or other receiver, liquidator or other similar official being appointed in relation to the Issuer or in relation to the whole or any substantial part of the undertaking or assets of the Issuer, or an encumbrancer taking possession of the whole or any substantial part of the undertaking or assets of the Issuer, or a distress, execution, diligence or other process being levied or enforced upon or sued out against the whole or any substantial part of the undertaking or assets of the Issuer and such possession or process (as the case may be) not being discharged or not otherwise ceasing to apply within 30 days, or the Issuer initiating or consenting to the foregoing proceedings relating to itself under applicable liquidation, insolvency, composition, reorganisation or other similar laws or making a conveyance or assignment for the benefit of its creditors generally or a composition or

similar arrangement with the creditors or takes steps with a view to obtaining a moratorium in respect of its indebtedness, including without limitation, the filing of documents with the court; or

- (f) if an Intercompany Loan Acceleration Notice is served under the Intercompany Loan Agreement while the Class A Notes of any Series are outstanding.

## 9.2 Class B Noteholders

This **Condition 9.2** shall have no effect if, and for as long as, any Class A Notes of any Series are outstanding. Subject thereto, for so long as any Class B Notes of any Series are outstanding, the Note Trustee in its absolute discretion may (and, if so requested in writing by the Holders of not less than 25 per cent. in aggregate Principal Amount Outstanding of the Class B Notes (which, for this purpose and for the purpose of any Extraordinary Resolution referred to in this **Condition 9.2**, means the Class B Notes of all Series constituted by the Note Trust Deed) or if so directed by or pursuant to an Extraordinary Resolution passed at a meeting of the Holders of the Class B Notes, shall), subject in each case to it being indemnified and/or secured to its satisfaction, give notice (a **Class B Note Acceleration Notice**) to the Issuer, the Issuer Security Trustee and the Funding 1 Security Trustee of a Note Event of Default (as defined below) and declaring (in writing) the Class B Notes and all other Notes to be due and repayable (and they shall forthwith become due and repayable) at any time after the happening of any of the following events:

- (a) default being made for a period of three Business Days in the payment of any amount of principal of or interest on the Class B Notes of any Series when and as the same ought to be paid in accordance with these Conditions; or
- (b) the occurrence of any of the events in **Condition 11(b)**, **(c)**, **(d)**, **(e)** or **(f)** provided that the references in **Condition 11(b)**, **Condition 11(d)** and **Condition 11(f)** to Class A Notes shall be read as references to Class B Notes.

## 9.3 Class M Noteholders

This **Condition 9.3** shall have no effect if, and for as long as, any Class A Notes or Class B Notes of any Series are outstanding. Subject thereto, for so long as any Class M Notes of any Series are outstanding, the Note Trustee in its absolute discretion may (and, if so requested in writing by the Holders of not less than 25 per cent. in aggregate Principal Amount Outstanding of the Class M Notes (which, for this purpose and for the purpose of any Extraordinary Resolution referred to in this **Condition 9.3**, means the Class M Notes of all Series constituted by the Note Trust Deed) or if so directed by or pursuant to an Extraordinary Resolution passed at a meeting of the Holders of the Class M Notes, shall), subject in each case to it being indemnified and/or secured to its satisfaction, give notice (a **Class M Note Acceleration Notice**) to the Issuer, the Issuer Security Trustee and the Funding 1 Security Trustee of a Note Event of Default (as defined below) and declaring (in writing) the Class M Notes and all other Notes to be due and repayable (and they shall forthwith become due and repayable) at any time after the happening of any of the following events:

- (a) default being made for a period of three Business Days in the payment of any amount of principal of or interest on the Class M Notes of any Series when and as the same ought to be paid in accordance with these Conditions; or
- (b) the occurrence of any of the events in **Condition 11(b)**, **(c)**, **(d)**, **(e)** or **(f)** provided that the references in **Condition 11(b)**, **Condition 11(d)** and **Condition 11(f)** to Class A Notes shall be read as references to Class M Notes.

## 9.4 Class C Noteholders

This **Condition 9.4** shall have no effect if, and for as long as, any Class A Notes, Class B Notes or Class M Notes of any Series are outstanding. Subject thereto, for so long as any Class C Notes of any Series are outstanding, the Note Trustee in its absolute discretion may (and, if so requested in writing by the Holders of not less than 25 per cent. in aggregate Principal Amount Outstanding of the Class C Notes (which, for this purpose and for the purpose of any Extraordinary Resolution referred to in this **Condition 9.4**, means the Class C Notes of all Series constituted by the Note Trust Deed) or if so directed by or pursuant to an Extraordinary Resolution passed at a meeting of the Holders of the Class C Notes, shall), subject in each case to it being indemnified and/or secured to its satisfaction, give notice (a **Class C Note Acceleration Notice**) to the Issuer, the Issuer Security Trustee and the Funding 1 Security Trustee of a Note Event of Default (as defined below) and declaring (in writing)



the Class C Notes and all other Notes to be due and repayable (and they shall forthwith become due and repayable) at any time after the happening of any of the following events:

- (a) default being made for a period of three Business Days in the payment of any amount of principal of or interest on the Class C Notes of any Series when and as the same ought to be paid in accordance with these Conditions; or
- (b) the occurrence of any of the events in **Condition 11(b), (c), (d), (e) or (f)** provided that the references in **Condition 11(b), Condition 11(d) and Condition 11(f)** to Class A Notes shall be read as references to Class C Notes.

## 9.5 Class D Noteholders

This **Condition 9.5** shall have no effect if, and for as long as, any Class A Notes, Class B Notes, Class M Notes or Class C Notes of any Series are outstanding. Subject thereto, for so long as any Class D Notes of any Series are outstanding, the Note Trustee in its absolute discretion may (and, if so requested in writing by the Holders of not less than 25 per cent. in aggregate Principal Amount Outstanding of the Class D Notes (which, for this purpose and for the purpose of any Extraordinary Resolution referred to in this **Condition 9.5**, means the Class D Notes of all Series constituted by the Note Trust Deed) or if so directed by or pursuant to an Extraordinary Resolution passed at a meeting of the Holders of the Class D Notes, shall), subject in each case to it being indemnified and/or secured to its satisfaction, give notice (a **Class D Note Acceleration Notice**) to the Issuer, the Issuer Security Trustee and the Funding 1 Security Trustee of a Note Event of Default (as defined below) and declaring (in writing) the Class D Notes to be due and repayable (and they shall forthwith become due and repayable) at any time after the happening of any of the following events:

- (a) default being made for a period of three Business Days in the payment of any amount of principal of or interest on the Class D Notes of any Series when and as the same ought to be paid in accordance with these Conditions; or
- (b) the occurrence of any of the events in **Condition 11(b), (c), (d), (e) or (f)** provided that the references in **Condition 11(b), Condition 11(d) and Condition 11(f)** to Class A Notes shall be read as references to Class D Notes.

## 9.6 Following Service of a Note Acceleration Notice

In these Conditions, a **Note Acceleration Notice** means any of a Class A Note Acceleration Notice, a Class B Note Acceleration Notice, a Class M Note Acceleration Notice, a Class C Note Acceleration Notice or a Class D Note Acceleration Notice. For the avoidance of doubt, upon any Note Acceleration Notice being given by the Note Trustee in accordance with **Condition 9.1, 9.2, 9.3, 9.4 or 9.5**, all Notes shall immediately become due, without further action, notice or formality at their Principal Amount Outstanding together with accrued interest (or, in the case of a Zero Coupon Note, at its Redemption Amount, calculated in accordance with **Condition 5.7**).

## 10. Enforcement of Notes

### 10.1 Enforcement

The Note Trustee may, at its discretion and without notice at any time and from time to time, take such steps and institute such proceedings against the Issuer or any other person as it may think fit to enforce the provisions of the Notes, the Trust Deed (including these Conditions) or any of the other Transaction Documents to which it is a party and the Note Trustee may, at its discretion without notice, at any time after the Issuer Security has become enforceable (including after the service of a Note Acceleration Notice in accordance with **Condition 9**), instruct the Issuer Security Trustee to take such steps as it may think fit to enforce the Issuer Security. The Note Trustee shall not be bound to take such steps or institute such proceedings or give such instructions unless:

- (a) (subject in all cases to restrictions contained in the Note Trust Deed to protect the interests of any higher ranking Class of Noteholders) it shall have been so directed by an Extraordinary Resolution of the Class A Noteholders, the Class B Noteholders, the Class M Noteholders, the Class C Noteholders or the Class D Noteholders (which, for this purpose, means the Holders of all Series of the Class A Notes, the Class B Notes, the Class M Notes, the Class C Notes or the Class D Notes (as applicable)) or so requested in writing by the Holders of at least one quarter in aggregate Principal Amount Outstanding of the Class A Notes, Class B Notes, Class M Notes, Class C Notes or Class D Notes (as applicable) of all Series; and

- (b) it shall have been indemnified and/or secured to its satisfaction.

The Issuer Security Trustee shall not, and shall not be bound to, take such steps or take any such other action unless it is so directed by the Note Trustee and indemnified and/or secured to its satisfaction.

Amounts available for distribution after enforcement of the Issuer Security shall be distributed in accordance with the terms of the Issuer Deed of Charge.

No Noteholder may institute any proceedings against the Issuer to enforce its rights under or in respect of the Notes, the Note Trust Deed or the Issuer Deed of Charge. Notwithstanding the foregoing and notwithstanding any other provision of the Note Trust Deed, the right of any Noteholder to receive payment of principal and of interest on its Notes on or after the due date for such principal or interest, or to institute suit for the enforcement of payment of that principal or interest, may not be impaired or affected without the consent of that Noteholder.

## 10.2 Post-enforcement Call Option

In the event that the Issuer Security is enforced and realised to the maximum possible extent as certified by the Issuer Security Trustee and the Issuer Security Trustee determines that the proceeds of such enforcement, after distribution of such proceeds to the persons entitled thereto ranking in priority to the Notes under the Issuer Deed of Charge and to the Noteholders (to the extent entitled thereto), are insufficient to pay in full all principal and interest and other amounts whatsoever due in respect of the Notes and all other claims ranking *pari passu* therewith, then the Noteholders are required, at the request of the Post-Enforcement Call Option Holder, for the consideration of one penny per Note of each Series and Class, to transfer or (as the case may be) procure transfer of all (but not some only) of the Notes to the Post-Enforcement Call Option Holder pursuant to the option granted to it by the Note Trustee (as agent for the Noteholders) under the terms of the Post-Enforcement Call Option Agreement. Immediately upon such transfer, no such former Noteholder shall have any further interest in the Notes. Each of the Noteholders acknowledges that the Note Trustee has the authority and the power to bind the Noteholders in accordance with the terms and conditions set out in the Post-Enforcement Call Option Agreement and each Noteholder, by subscribing for or purchasing Notes, agrees to be so bound. The Note Trustee shall give notice of the exercise of such option to the Noteholders in accordance with **Condition 14**.

## 11. Meetings of Noteholders, Modifications and Waiver

### 11.1 Meetings of Noteholders

The Note Trust Deed contains provisions for convening meetings of Noteholders of any Series and Class to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of any provision of these Conditions or the provisions of any of the Transaction Documents.

#### (a) Class A Notes

In respect of the Class A Notes, the Note Trust Deed provides that, subject to **Condition 11.2**:

- (i) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of one class only of the Class A Notes shall be deemed to have been duly passed if passed at a meeting of the Holders of that class of the Class A Notes;
- (ii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class A Notes but does not give rise to a conflict of interest between the Holders of any such two or more classes of Class A Notes shall be deemed to have been duly passed if passed at a single meeting of the Holders of such two or more classes of Class A Notes; and
- (iii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class A Notes and gives or may give rise to a conflict of interest between the Holders of any such two or more classes of Class A Notes shall be deemed to have been duly passed only if, in lieu of being passed at a single meeting of the Holders of such two or more classes of Class A Notes, it shall be passed at separate meetings of the Holders of each of such two or more classes of Class A Notes.

#### (b) Class B Notes

In respect of the Class B Notes, the Note Trust Deed provides that, subject to **Condition 11.2**:

- (i) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of one class only of the Class B Notes shall be deemed to have been duly passed if passed at a meeting of the Holders of that class of the Class B Notes;
- (ii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class B Notes but does not give rise to a conflict of interest between the Holders of any such two or more classes of Class B Notes shall be deemed to have been duly passed if passed at a single meeting of the Holders of such two or more classes of Class B Notes; and
- (iii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class B Notes and gives or may give rise to a conflict of interest between the Holders of any such two or more classes of Class B Notes shall be deemed to have been duly passed only if, in lieu of being passed at a single meeting of the Holders of such two or more classes of Class B Notes, it shall be passed at separate meetings of the Holders of each of such two or more classes of Class B Notes.

(c) **Class M Notes**

In respect of the Class M Notes, the Note Trust Deed provides that, subject to **Condition 11.2**:

- (i) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of one class only of the Class M Notes shall be deemed to have been duly passed if passed at a meeting of the Holders of that class of the Class M Notes;
- (ii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class M Notes but does not give rise to a conflict of interest between the Holders of any such two or more classes of Class M Notes shall be deemed to have been duly passed if passed at a single meeting of the Holders of such two or more classes of Class M Notes; and
- (iii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class M Notes and gives or may give rise to a conflict of interest between the Holders of any such two or more classes of Class M Notes shall be deemed to have been duly passed only if, in lieu of being passed at a single meeting of the Holders of such two or more classes of Class M Notes, it shall be passed at separate meetings of the Holders of each of such two or more classes of Class M Notes.

(d) **Class C Notes**

In respect of the Class C Notes, the Note Trust Deed provides that, subject to **Condition 11.2**:

- (i) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of one class only of the Class C Notes shall be deemed to have been duly passed if passed at a meeting of the Holders of that class of the Class C Notes;
- (ii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class C Notes but does not give rise to a conflict of interest between the Holders of any such two or more classes of Class C Notes shall be deemed to have been duly passed if passed at a single meeting of the Holders of such two or more classes of Class C Notes; and
- (iii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class C Notes and gives or may give rise to a conflict of interest between the Holders of any such two or more classes of Class C Notes shall be deemed to have been duly passed only if, in lieu of being passed at a single meeting of the Holders of such two or more classes of Class C Notes, it shall be passed at separate meetings of the Holders of each of such two or more classes of Class C Notes.

(e) **Class D Notes**

In respect of the Class D Notes, the Note Trust Deed provides that, subject to **Condition 11.2**:

- (i) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of one class only of the Class D Notes shall be deemed to have been duly passed if passed at a meeting of the Holders of that class of the Class D Notes;
- (ii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class D Notes but does not give rise to a conflict of interest between the Holders of any such two or more classes of Class D Notes shall be deemed to have been duly passed if passed at a single meeting of the Holders of such two or more classes of Class D Notes; and
- (iii) a resolution which, in the sole opinion of the Note Trustee, affects the interests of the Holders of any two or more classes of the Class D Notes and gives or may give rise to a conflict of interest between the Holders of any such two or more classes of Class D Notes shall be deemed to have been duly passed only if, in lieu of being passed at a single meeting of the Holders of such two or more classes of Class D Notes, it shall be passed at separate meetings of the Holders of each of such two or more classes of Class D Notes.

The quorum for any meeting of the Holders of any Series and Class of Notes or of any Class of Notes of more than one Series convened to consider a resolution (except for the purpose of passing an Extraordinary Resolution or a Programme Resolution) will be one or more persons holding or representing not less than one-twentieth of the aggregate Principal Amount Outstanding of such Series and Class of Notes or such Class of Notes of more than one Series or, at any adjourned meeting, one or more persons being or representing Noteholders of such Series and Class of Notes or such Class of Notes of more than one Series, whatever the aggregate Principal Amount Outstanding of the relevant Notes so held or represented. A **resolution** means a resolution (excluding an Extraordinary Resolution or a Programme Resolution) passed at a meeting of Noteholders duly convened and held in accordance with the provisions of the Note Trust Deed by a simple majority of the persons voting thereat upon a show of hands or, if a poll is duly demanded, by a simple majority of the votes cast on such poll.

Subject as provided in the following paragraph, the quorum at any meeting of the Holders of any Series and Class of Notes or of any Class of Notes of more than one Series convened to consider an Extraordinary Resolution will be one or more persons holding or representing not less than 50 per cent. of the aggregate Principal Amount Outstanding of such Series and Class of Notes or such Class of Notes of more than one Series or, at any adjourned meeting, one or more persons being or representing Noteholders of such Series and Class of Notes or such Class of Notes of more than one Series of Notes, whatever the aggregate Principal Amount Outstanding of the relevant Notes so held or represented.

The quorum at any meeting of Noteholders for passing an Extraordinary Resolution which includes the sanctioning of a modification which would have the effect of altering the amount, rate or timing of payments of principal on any Series and Class of the Notes or any Class of Notes of more than one Series or the rate, the day or the timing of payments on, or the currency of payment of, such Series and Class of Notes or such Class of Notes of more than one Series or altering the priority of payments to the extent it affects such Series and Class of Notes or such Class of Notes of more than one Series or altering the quorum or majority required in relation to any resolution (each a **Basic Terms Modification**, as more fully defined in the Note Trust Deed) shall be one or more persons holding or representing not less than 75 per cent. of the aggregate Principal Amount Outstanding of the relevant Series and Class of Notes or of the relevant Class of Notes of more than one Series or, at any adjourned and reconvened meeting, not less than 25 per cent. of the aggregate Principal Amount Outstanding of the relevant Series and Class of Notes or of the Class of Notes of more than one Series.

An Extraordinary Resolution passed at any meeting of Noteholders shall be binding on all of the Noteholders of the relevant Series and Class or of the Class of Notes of more than one Series whether or not they are present or represented at the meeting.

In connection with any meeting of Noteholders where the relevant Series and Class Notes (or any of them) are not denominated in Sterling, the Principal Amount Outstanding of any Note not denominated in Sterling shall be converted into Sterling at the relevant Specified Currency Exchange Rate.

A resolution signed by or on behalf of all the Noteholders of the relevant Series and Class or of the relevant Class of more than one Series who for the time being are entitled to receive notice of a meeting under the Note Trust Deed shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Holders of such Series and Class of Notes or of the relevant Class of more than one Series.

## 11.2 Programme Resolution

Notwithstanding the provisions of **Condition 11.1**, any Extraordinary Resolution of the Noteholders of any Class to direct the Note Trustee to give a Note Acceleration Notice pursuant to **Condition 9** or take any enforcement action or instruct the Issuer Security Trustee to enforce the Issuer Security pursuant to and **Condition 10** (a **Programme Resolution**) shall only be capable of being passed at a single meeting of the Noteholders of all Series of such Class of Notes. The quorum at any such meeting for passing a Programme Resolution shall be one or more persons holding or representing not less than 50 per cent. of the aggregate Principal Amount Outstanding of the Notes of such Class or, at any adjourned and reconvened meeting, one or more persons being or representing Noteholders of such Class of Notes, whatever the aggregate Principal Amount Outstanding of such Class of Notes so held or represented by them.

A Programme Resolution passed at any meeting of all Series of any Class of Notes shall be binding on all Noteholders of all Series of that Class of Notes, whether or not they are present or represented at the meeting.

## 11.3 Limitations on Noteholders

Subject as provided in **Condition 11.4**:

- (a) an Extraordinary Resolution of the Class A Noteholders of any Series shall be binding on all Class B Noteholders, all Class M Noteholders, all Class C Noteholders and all Class D Noteholders, in each case of that Series or of any other Series;
- (b) no Extraordinary Resolution of the Class B Noteholders of any Series shall take effect for any purpose while any Class A Notes, of that Series or of any other Series, remain outstanding unless it shall have been sanctioned by an Extraordinary Resolution of the Class A Noteholders of each Series or the Note Trustee is of the opinion that it would not be materially prejudicial to the interests of the Class A Noteholders of any Series and, subject hereto and to **Condition 11.4**, an Extraordinary Resolution of the Class B Noteholders of any Series will be binding on the Class M Noteholders, the Class C Noteholders and the Class D Noteholders in each case of that or any other Series irrespective of the effect upon them;
- (c) no Extraordinary Resolution of the Class M Noteholders of any Series shall take effect for any purpose while any Class A Notes or Class B Notes, in each case of that Series or of any other Series remain outstanding unless it shall have been sanctioned by an Extraordinary Resolution of the Class A Noteholders and an Extraordinary Resolution of the Class B Noteholders, in each case of each Series, or the Note Trustee is of the opinion that it would not be materially prejudicial to the respective interests of the Class A Noteholders of any Series or the Class B Noteholders of any Series and, subject hereto and to **Condition 11.4**, an Extraordinary Resolution of the Class M Noteholders of any Series will be binding on the Class C Noteholders and the Class D Noteholders, in each case, of that or of any other Series irrespective of the effect upon them;
- (d) no Extraordinary Resolution of the Class C Noteholders of any Series shall take effect for any purpose while any Class A Notes, Class B Notes or Class M Notes, in each case of that Series or of any other Series, remain outstanding unless it shall have been sanctioned by an Extraordinary Resolution of the Class A Noteholders, an Extraordinary Resolution of the Class B Noteholders and an Extraordinary Resolution of the Class M Noteholders, in each case of each Series, or the Note Trustee is of the opinion that it would not be materially prejudicial to the respective interests of the Class A Noteholders of any Series, the Class B Noteholders of any Series or the Class M Noteholders of any Series and, subject hereto and to **Condition 11.4**, an Extraordinary Resolution of the Class C Noteholders of any Series will be binding on the Class D Noteholders of that or any other Series irrespective of the effect upon them; and

- (e) no Extraordinary Resolution of Class D Noteholders of any Series shall take effect for any purpose while any Class A Notes, Class B Notes, Class M Notes or Class C Notes, in each case of that Series or of any other Series, remain outstanding unless it shall have been sanctioned by an Extraordinary Resolution of the Class A Noteholders, an Extraordinary Resolution of the Class B Noteholders, an Extraordinary Resolution of the Class M Noteholders and an Extraordinary Resolution of the Class C Noteholders, in each case of each Series, or the Note Trustee is of the opinion that it would not be materially prejudicial to the respective interests of the Class A Noteholders of any Series, the Class B Noteholders of any Series, the Class M Noteholders of any Series or the Class C Noteholders of any Series.

#### **11.4 Approval of Modifications and Waivers by Noteholders**

No Extraordinary Resolution of the Noteholders of any one or more Series of Class A Notes to sanction a modification of, or any waiver or authorisation of any breach or proposed breach of, any of the provisions of the Transaction Documents or the Conditions of the Notes shall take effect unless it has been sanctioned by an Extraordinary Resolution of the Class B Noteholders, an Extraordinary Resolution of the Class M Noteholders, an Extraordinary Resolution of the Class C Noteholders and an Extraordinary Resolution of the Class D Noteholders, in each case of each Series, or the Note Trustee is of the opinion that it would not be materially prejudicial to the respective interests of the Class B Noteholders of any Series, the Class M Noteholders of any Series, the Class C Noteholders of any Series and the Class D Noteholders of any Series.

No Extraordinary Resolution of the Noteholders of any one or more Series of Class B Notes to sanction a modification of, or any waiver or authorisation of any breach or proposed breach of, any of the provisions of the Transaction Documents or the Conditions of the Notes shall take effect unless it has been sanctioned by an Extraordinary Resolution of the Class M Noteholders, an Extraordinary Resolution of the Class C Noteholders and an Extraordinary Resolution of the Class D Noteholders, in each case of each Series, or the Note Trustee is of the opinion that it would not be materially prejudicial to the respective interests of the Class M Noteholders of any Series, the Class C Noteholders of any Series and the Class D Noteholders of any Series.

No Extraordinary Resolution of the Noteholders of any one or more Series of Class M Notes to sanction a modification of, or any waiver or authorisation of any breach or proposed breach of, any of the provisions of the Transaction Documents or the Conditions of the Notes shall take effect unless it has been sanctioned by an Extraordinary Resolution of the Class C Noteholders and an Extraordinary Resolution of the Class D Noteholders, in each case of each Series, or the Note Trustee is of the opinion that it would not be materially prejudicial to the respective interests of the Class C Noteholders of any Series and the Class D Noteholders of any Series.

No Extraordinary Resolution of the Noteholders of any one or more Series of Class C Notes to sanction a modification of, or any waiver or authorisation of any breach or proposed breach of, any of the provisions of the Transaction Documents or the Conditions of the Notes shall take effect unless it has been sanctioned by an Extraordinary Resolution of the Class D Noteholders of each Series or the Note Trustee is of the opinion that it would not be materially prejudicial to the interests of the Class D Noteholders of any Series.

#### **11.5 Modifications and Determinations by Note Trustee**

The Note Trustee, may, without the consent of the Noteholders:

- (a) agree to any modification (other than a Basic Terms Modification) of, or to the waiver or authorisation of any breach or proposed breach of, the Conditions or any of the Transaction Documents which is not, in the opinion of the Note Trustee, materially prejudicial to the interests of the Noteholders of any Series and Class of Notes; or
- (b) determine that any Note Event of Default shall not be treated as such provided that it is not, in the opinion of the Note Trustee, materially prejudicial to the interests of the Holders of the most senior Class of Notes then outstanding; or
- (c) agree to any modification (including a Basic Terms Modification) of these Conditions or any of the Transaction Documents which, in the sole opinion of the Note Trustee, is of a formal, minor or technical nature or is to correct a manifest error or is to comply with the mandatory provisions of law; or

- (d) agree to any modification of any of these Conditions or any Transaction Documents, as expressly provided for in the Transaction Documents.

For the avoidance of doubt, the Note Trustee shall be entitled to assume, without further investigation or inquiry, that such modification, waiver or authorisation, will not be materially prejudicial to the interests of the Noteholders if each of the Rating Agencies rating the relevant Series and Class of Notes has confirmed in writing that the then current ratings of the applicable Series and Class of Notes would not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified by such modification, waiver or authorisation. Any such modification, waiver, authorisation or determination shall be binding on the Noteholders and, unless the Note Trustee agrees otherwise, any such modification shall be notified to the Noteholders and the Rating Agencies in accordance with **Condition 14** as soon as practicable thereafter.

#### **11.6 Redenomination**

The Note Trustee may agree, without the consent of the Holders of the Sterling Notes on or after the Specified Date (as defined below), to such modifications to the Sterling Notes and the Note Trust Deed in respect of redenomination of such Notes in euro and associated reconventioning, renominatisation and related matters in respect of such Notes as may be proposed by the Issuer (and confirmed by an independent financial institution approved by the Note Trustee to be in conformity with then applicable market conventions) and to provide for redemption at the euro equivalent of the sterling principal amount of the Sterling Notes. For these purposes, **Specified Date** means the date on which the United Kingdom participates in the third stage of European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended by the Treaty on European Union, or otherwise participates in European Economic and Monetary Union in a manner with an effect similar to such third stage.

Any such modification shall be binding on the Holders of the Sterling Notes and, unless the Note Trustee agrees otherwise, any such modification shall be notified to such Noteholders in accordance with **Condition 14** as soon as practicable thereafter.

#### **11.7 Exercise of Note Trustee's Functions**

Where the Note Trustee is required, in connection with the exercise of its powers, trusts, authorities, duties and discretions under these Conditions or any Transaction Document, to have regard to the interests of the Noteholders of any Class, it shall have regard to the interests of such Noteholders as a Class and, in particular but without prejudice to the generality of the foregoing, the Note Trustee shall not have regard to, or be in any way liable for, the consequences of such exercise for individual Noteholders resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory. In connection with any such exercise, the Note Trustee shall not be entitled to require, and no Noteholder shall be entitled to claim, from the Issuer or any other person, any indemnification or payment in respect of any tax consequence of any such exercise upon individual Noteholders.

#### **12. Indemnification of The Note Trustee and the Issuer Security Trustee**

The Note Trust Deed and the Issuer Deed of Charge set out certain provisions for the benefit of the Note Trustee and the Issuer Security Trustee. The following is a summary of such provisions and is subject to the more detailed provisions of the Note Trust Deed and the Issuer Deed of Charge.

The Transaction Documents contain provisions governing the responsibility (and relief from responsibility) of the Note Trustee and the Issuer Security Trustee and providing for their indemnification in certain circumstances, including, among others, provisions relieving the Issuer Security Trustee from taking enforcement proceedings or enforcing the Issuer Security unless indemnified to its satisfaction. The Note Trustee and the Issuer Security Trustee are also entitled to be paid their costs and expenses in priority to any interest payments to Noteholders.

The Note Trustee and the Issuer Security Trustee and their related companies are entitled to enter into business transactions with the Issuer, Bank of Scotland, the Issuer Cash Manager and/or the related companies of any of them and to act as note trustee or security trustee for the holders of any new notes other than the Notes and/or any other person who is a party to any Transaction Document or whose obligations are comprised in the Issuer Security and/or any of its subsidiary or associated companies without accounting for any profit resulting therefrom.

Neither the Note Trustee nor the Issuer Security Trustee will be responsible for any loss, expense or liability which may be suffered as a result of any assets comprised in the Issuer Security, or any deeds or documents of title thereto, being uninsured or inadequately insured or being held by clearing organisations or their operators or by intermediaries such as banks, brokers or other similar persons on behalf of the Note Trustee or the Issuer Security Trustee, as applicable.

Furthermore, the Note Trustee and the Issuer Security Trustee will be relieved of liability for making searches or other inquiries in relation to the assets comprising the Issuer Security. The Note Trustee and the Issuer Security Trustee do not have any responsibility in relation to the legality and the enforceability of the trust arrangements and the related Issuer Security. Neither the Note Trustee nor the Issuer Security Trustee will be obliged to take any action that might result in its incurring personal liabilities. Neither the Note Trustee nor the Issuer Security Trustee is obliged to monitor or investigate the performance of any other person under the Transaction Documents and is entitled to assume, until it has actual knowledge to the contrary, that all such persons are properly performing their duties, unless it receives express notice to the contrary.

Neither the Note Trustee nor the Issuer Security Trustee will be responsible for any deficiency that may arise because it is liable to tax in respect of the proceeds of any Issuer Security.

### **13. Replacement of Notes**

If Definitive Notes are lost, stolen, mutilated, defaced or destroyed, the Noteholder can replace them at the Specified Office of any Paying Agent subject to all applicable laws and stock exchange requirements. The Noteholder will be required both to pay the expenses of producing a replacement and to comply with the Issuer's, the Registrar's and the Paying Agent's reasonable requests for evidence and indemnity.

If a Global Note is lost, stolen, mutilated, defaced or destroyed, the Issuer will deliver a replacement Global Note to the registered Holder upon receipt of satisfactory evidence and surrender of any defaced or mutilated Global Note. A replacement will only be made upon payment of the expenses for a replacement and compliance with the Issuer's, Registrar's and Paying Agents' reasonable requests as to evidence and indemnity.

Defaced or mutilated Notes must be surrendered before replacements will be issued.

### **14. Notice to Noteholders**

#### **14.1 Publication of Notice**

Any notice to Noteholders shall be validly given if such notice is:

- (a) sent to them by first class mail (or its equivalent) or (if posted to a non-UK address) by airmail at the respective addresses on the Register; and
- (b) published in The Financial Times; and
- (c) for so long as amounts are outstanding on the Rule 144A Notes, in a daily newspaper of general circulation in New York (which is expected to be The New York Times);

or, if any of such newspapers set out above shall cease to be published or timely publication therein shall not be practicable, in a leading English language daily newspaper having general circulation in the United Kingdom or the United States (as applicable) provided that if, at any time, the Issuer procures that the information concerned in such notice shall be published on the Relevant Screen, publication in the newspapers set out above or such other newspaper or newspapers shall not be required with respect to such information.

#### **14.2 Date of publication**

Any notices so published shall be deemed to have been given on the fourth day after the date of posting or, as the case may be, on the date of such publication or, if published more than once on different dates, on the first date on which publication shall have been made in the newspaper or newspapers in which (or on the Relevant Screen on which) publication is required.

#### **14.3 Global Notes**

While the Notes are represented by Global Notes, any notice to Noteholders will be validly given if such notice is provided in accordance with **Condition 14.1** or (at the option of the Issuer) if delivered



to DTC (in the case of the Notes held by Cede & Co., as nominee for DTC) or Euroclear and/or Clearstream, Luxembourg (in the case of the Notes held by a nominee of the common depositary) or (if specified in the applicable Final Terms) if delivered through any **Alternative Clearing System** specified therein. Any notice delivered to the DTC and/or Euroclear and/or Clearstream, Luxembourg and/or such Alternative Clearing System will be deemed to be given on the day of such delivery.

#### **14.4 Note Trustee's Discretion to Select Alternative Method**

The Note Trustee shall be at liberty to sanction some other method of giving notice to the Noteholders having regard to market practice then prevailing and to the requirements of the stock exchanges on which the Notes are then admitted for trading and provided that notice of such other method is given to the Noteholders in such manner as the Note Trustee shall require.

#### **15. Note Issues**

The Issuer shall be at liberty from time to time, without the consent of the Noteholders, to create and issue Notes, upon the Issuer obtaining written confirmation from each of the Rating Agencies that its then current ratings of the outstanding Notes will not be downgraded, withdrawn or (in the case of S&P and Moody's) qualified because of the new issue.

#### **16. Rating Agencies**

If:

- (a) a confirmation of rating or other response by a Rating Agency is a condition to any action or step under any Transaction Document (other than pursuant to **Condition 15**); and
- (b) a written request for such confirmation or response is delivered to each Rating Agency by the Issuer (copied to the Note Trustee and/or the Issuer Security Trustee and/or the Funding 1 Security Trustee, as applicable) and either one or more Rating Agency (each a **Non-Responsive Rating Agency**) indicates that it does not consider such confirmation or response necessary in the circumstances; and
- (c) at least one Rating Agency gives such a confirmation or response based on the same facts,

then such condition shall be deemed to be modified with respect to the facts set out in the request referred to in (b) so that there shall be no requirement for the confirmation or response from the Non-Responsive Rating Agency.

The Note Trustee and/or the Issuer Security Trustee and/or the Funding 1 Security Trustee, as applicable, shall be entitled to treat as conclusive a certificate by any director, officer or employee of the Issuer, Funding 1, the seller, any investment bank or financial adviser acting in relation to the Notes as to any matter referred to in (b) in the absence of manifest error or the Note Trustee and/or the Issuer Security Trustee and/or the Funding 1 Security Trustee, as applicable, having facts contradicting such certificates specifically drawn to his attention and the Note Trustee and/or the Issuer Security Trustee and/or the Funding 1 Security Trustee, as applicable, shall not be responsible for any loss, liability, costs, damages, expenses or inconvenience that may be caused as a result.

#### **17. Governing Law and Jurisdiction**

The Transaction Documents and the Notes are governed by English law unless specifically stated to the contrary. Certain provisions in the Transaction Documents relating to property situated in Scotland are governed by Scots law. Unless specifically stated to the contrary:

- (a) the courts of England are to have exclusive jurisdiction to settle any disputes which may arise out of or in connection with the Notes and the Transaction Documents; and
- (b) the Issuer and the other parties to the Transaction Documents irrevocably submit to the exclusive jurisdiction of the courts of England.

#### **18. Contracts (Rights of Third Parties) Act 1999**

No person shall have any right to enforce any term or condition of the Notes under the Contracts (Rights of Third Parties) Act 1999, but this shall not affect any right or remedy of a third party which exists or is available apart from that Act.

## 19. Definitions

Unless otherwise defined in these Conditions or unless the context otherwise requires, in these Conditions the following words shall have the following meanings and any other capitalised terms used in these Conditions shall have the meanings ascribed to them or incorporated in the Note Trust Deed or set out in the Master Definitions and Construction Schedule or the Issuer Master Definitions and Construction Schedule (each as defined below). These Conditions shall be construed in accordance with the interpretation provisions set out in the Master Definitions and Construction Schedule and the Issuer Master Definitions and Construction Schedule.

**A Loan Tranches** means the Loan Tranches made by the Issuer to Funding 1 under the Intercompany Loan Agreement from the proceeds of issue of the Class M Notes of any Series;

**AA Loan Tranches** means the Loan Tranches made by the Issuer to Funding 1 under the Intercompany Loan Agreement from the proceeds of the issue of the Class B Notes of any Series;

**AAA Loan Tranches** means the Loan Tranches made by the Issuer to Funding 1 under the Intercompany Loan Agreement from the proceeds of issue of the Class A Notes of any Series;

**Accrual Yield** means, in respect of any Series and Class of Notes, the yield specified as such for such Notes in the applicable Final Terms;

**Additional Business Centre** means, in respect of any Series and Class of Notes, each place specified as such for such Notes in the applicable Final Terms;

**Agents** means the Paying Agents, the Transfer Agent, the Registrar, the Exchange Agent and the Agent Bank;

**Agent Bank** means Deutsche Bank AG, London Branch in its capacity as agent bank at its Specified Office or such other person for the time being acting as agent bank under the Paying Agent and Agent Bank Agreement;

**BB Loan Tranche** means the Loan Tranches made by the Issuer to Funding 1 under the Intercompany Loan Agreement from the proceeds of issue of the Class D Notes of any Series;

**BBB Loan Tranches** means the Loan Tranches made by the Issuer to Funding 1 under the Intercompany Loan Agreement from the proceeds of issue of the Class C Notes of any Series;

**Broken Amount** means, in respect of any Series and Class of Notes, the amount specified as such (if any) for such Notes in the applicable Final Terms;

**Call Option Date** means, in respect of any Series and Class of Notes, the date specified as such in the applicable Final Terms, being the Interest Payment Date on which the Issuer is entitled to redeem such Notes pursuant to Condition 5.4(a);

**Class** or **class** means, in relation to the Class A Notes, the Class B Notes, the Class M Notes, the Class C Notes and the Class D Notes and the holders thereof, each single class (or each sub-class) thereof as the context requires and except where otherwise specified, and the respective holders thereof;

**Class A Noteholders** means the Holders of the Class A Notes;

**Class A Notes** means Notes of any Series designated as such (or a sub-class of such) in the applicable Final Terms;

**Class B Noteholders** means the Holders of the Class B Notes;

**Class B Notes** means Notes of any Series designated as such (or a sub-class of such) in the applicable Final Terms;

**Class C Noteholders** means the Holders of the Class C Notes;

**Class C Notes** means Notes of any Series designated as such (or a sub-class of such) in the applicable Final Terms;

**Class D Noteholders** means the Holders of the Class D Notes;

**Class D Notes** means Notes of any Series designated as such (or a sub-class of such) in the applicable Final Terms;

**Class M Noteholders** means the Holders of the Class M Notes;

**Class M Notes** means Notes of any Series designated as such (or a sub-class of such) in the applicable Final Terms;

**Clearstream, Luxembourg** means Clearstream Banking, société anonyme;

**Closing Date** means, in relation to any Series and Class of Notes, the date specified as such for such Notes in the applicable Final Terms;

**Conditional Purchaser** means, in respect of any Series and Class of Remarketable Notes, the person specified as such for such Remarketable Notes in the applicable Final Terms;

**Conditional Purchaser Confirmation** means, in respect of any Series and Class of Remarketable Notes, the confirmation given by the Remarketing Agent or the Tender Agent to the Issuer and the Principal Paying Agent that the Conditional Purchaser has purchased an interest in or has had transferred to it or on its behalf an interest in all such Remarketable Notes;

**Definitive Notes** means the note certificates representing the Notes while in definitive form;

**Designated Account** means the account (which, in the case of a payment in Japanese Yen to a non-resident of Japan, shall be a non-resident account) maintained by a Holder with a Designated Bank and identified as such in the Register;

**Designated Bank** means (in the case of payment in a Specified Currency other than euro) a bank in the principal financial centre of the country of such Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively) and (in the case of a payment in euro) any bank which processes payments in euro;

**Determination Date** means, in respect of any Series and Class of Notes, the date(s) specified as such (if any) for such Notes in the applicable Final Terms;

**Determination Period** as defined in **Condition 4.1**;

**Distribution Compliance Period** means, in relation to any Series and Class of Reg S Notes, 40 days after the later of the commencement of the offering of such Reg S Notes and the relevant Closing Date;

**Dollars, US\$, US Dollars or \$** means the lawful currency for the time being of the United States of America;

**DTC** means The Depository Trust Company;

**EURIBOR** means the Euro-zone inter-bank offered rate;

**Euro, euro or €** means the currency of the member states of the European Union that adopt the single currency in accordance with the Treaty of Rome of 25 March 1957, establishing the European Community, as amended from time to time;

**Euroclear** means Euroclear Bank S.A./N.V, as operator of the Euroclear System:

**Exchange Agent** means Deutsche Bank Trust Company Americas in its capacity as exchange agent at its Specified Office or such other person for the time being acting as exchange agent under the Paying Agent and Agent Bank Agreement;

**Extraordinary Resolution** means a resolution passed at a meeting of the Noteholders of a particular Class and Series or of a Class of Notes of more than one Series duly convened and held in accordance with the provisions of the Note Trust Deed by a majority consisting of not less than three-fourths of the persons voting thereat upon a show of hands or if a poll is duly demanded by a majority consisting of not less than three-fourths of the votes cast on such poll;

**Final Maturity Date** means, in respect of any Series and Class of Notes, the date specified as such for such Notes in the applicable Final Terms;

**Final Terms** means, in relation to any Issuance of Notes, the final terms issued in relation to all Series and Classes of Notes comprising such Issuance giving details of, *inter alia*, the amount and price of all such Series and Class of Notes;

**Fixed Coupon Amount** means, in respect of any Series and Class of Notes, the amount specified as such (if any) for such Notes in the applicable Final Terms;

**Funding 1** means Pendeford Funding (No. 1) Limited;

**Global Notes** means the Rule 144A Global Notes and the Reg S Global Notes;

**Holder** has the meaning indicated in **Condition 1.2**;

**Interest Commencement Date** means, in respect of any Series and Class of Notes, the Closing Date of such Series and Class of Notes or such other date as may be specified as such for such Notes in the applicable Final Terms;

**Interest Payment Date** means, in respect of a Series and Class of Notes (other than Money Market Notes), the Quarterly Interest Payment Dates and (in the case of Money Market Notes) the Monthly Interest Payment Dates, subject, in each case, to the Conditions of the Notes;

**Interest Period** means the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date;

**ISDA Definitions** means the 2000 ISDA Definitions, as published by the International Swaps and Derivatives Association, Inc. and as amended and updated as at the Closing Date of the relevant Series and Class of Notes;

**Issuance** means all Series and Classes of Notes comprising the Notes issued on a particular Closing Date;

**Issuer** means Pendeford Master Issuer plc;

**Issuer Deed of Charge** means the deed of charge entered into on the Programme Date, as supplemented and/or amended from time to time, between, among others, the Issuer and the Issuer Security Trustee and each deed of accession or supplement entered into in connection therewith;

**Issuer Master Definitions and Construction Schedule** means the master definitions and construction schedule dated the Programme Date, as amended and/or restated from time to time, setting out, among other things, definitions which apply to the Transaction Documents to which Issuer is a party;

**Issuer Secured Creditors** means the Issuer Security Trustee (and any receiver appointed under the Issuer Deed of Charge), the Note Trustee, the Issuer Swap Providers, the Corporate Services Provider, the Issuer Account Bank, the Issuer Cash Manager, the Paying Agents, the Agent Bank, the Transfer Agent, the Exchange Agent, the Registrar, the Issuer Start-up Loan Provider, the Issuer Subordinated Loan Provider and the Noteholders and any new Issuer Secured Creditor who accedes to the Issuer Deed of Charge from time to time under a deed of accession or a supplemental deed;

**Issuer Security** means the security created by the Issuer pursuant to the Issuer Deed of Charge;

**Issuer Security Trustee** means Deutsche Bank Trust Company Americas and its successors or any other security trustee under the Issuer Deed of Charge;

**Issuer Swap Providers** means the institutions identified in respect of each Issuer Swap Agreement in the applicable Final Terms related to the relevant Series and Class of Notes;

**LIBOR** means the London inter-bank offered rate;

**Listed Notes** means each Series and Class of Notes which is admitted to the official list maintained by the UK Listing Authority and admitted to trading on the London Stock Exchange's Regulated Market;

**Loan Tranches** means the AAA Loan Tranches, the AA Loan Tranches, the A Loan Tranches, the BBB Loan Tranches and the BB Loan Tranches and loan tranches of any other designated credit rating, being the advances made by the Issuer to Funding 1, pursuant to the Intercompany Loan

Agreement, each being funded from proceeds received by the Issuer from the issue of a Series and Class of Notes;

**London Stock Exchange** means London Stock Exchange plc;

**Manager** means the entities specified as such in the applicable Final Terms;

**Mandatory Transfer Date** means, in respect of any Series and Class of Remarketable Notes, the Interest Payment Date specified as such for such Remarketable Notes in the applicable Final Terms;

**Mandatory Transfer Price** means, in respect of any Series and Class of Remarketable Notes, the Principal Amount Outstanding of such Remarketable Notes on the relevant Mandatory Transfer Date following the application of Note Principal Payments on such date;

**Mandatory Transfer Termination Event** shall occur, in respect of any Series and Class of Remarketable Notes, if the Conditional Purchaser has purchased an interest in all such Remarketable Notes;

**Margin** means, in respect of any Series and Class of Notes, the amount specified as such for such Notes in the applicable Final Terms and, in the case of Remarketable Notes, shall include the Reset Margin;

**Master Definitions and Construction Schedule** means the master definitions and construction schedule dated the Programme Date, as amended and/or restated from time to time, setting out, among other things, definitions which apply to the Transaction Documents to which Funding 1 is a party;

**Maximum Rate of Interest** means, in respect of any Series and Class of Notes, the rate of interest specified as such for such Notes in the applicable Final Terms;

**Maximum Reset Margin** means, in respect of any Series and Class of Remarketable Notes, the amount specified as such for such Remarketable Notes in the applicable Final Terms;

**Minimum Rate of Interest** means, in respect of any Series and Class of Notes, the rate of interest specified as such for such Notes in the applicable Final Terms;

**Money Market Notes** means Notes which will be “Eligible Securities” within the meaning of Rule 2a-7 under the Investment Company Act;

**Monthly Date** means the 12th day of each calendar month;

**Monthly Interest Payment Dates** means, in respect of any Money Market Notes, each Monthly Date specified in the applicable Final Terms for the payment of interest and/or principal until the occurrence of a Pass-Through Trigger Event and, following such occurrence, the Quarterly Interest Payment Dates specified in the applicable Final Terms for payment of interest and/or principal subject, in each case, to the appropriate Business Day Convention, if any, specified in the applicable Final Terms;

**Note Acceleration Notice** has the meaning given in **Condition 9.6**;

**Note Determination Date** means the date two Business Days prior to each Interest Payment Date;

**Note Event of Default** means the occurrence of an event specified in **Condition 9**;

**Note Principal Payment** has the meaning given in **Condition 5.3**;

**Note Trust Deed** means the note trust deed entered into on the Programme Date, as supplemented and/or amended from time to time, between the Issuer and the Note Trustee, and each supplemental deed entered into in connection therewith;

**Note Trustee** means Deutsche Trustee Company Limited and its successors or any further or other note trustee under the Note Trust Deed, as trustee for the Noteholders;

**Noteholders** means the Holders for the time being of the Notes;

**Notes** means the Class A Notes, the Class B Notes, the Class C Notes, the Class D Notes and/or the Class M Notes;

**Pass-Through Trigger Event** means any of the following events:

- (a) a Trigger Event; or
- (b) the service of a Note Acceleration Notice by the Note Trustee on the Issuer; or
- (c) the service of an Intercompany Loan Acceleration Notice by the Issuer Security Trustee on Funding 1;

**Paying Agent and Agent Bank Agreement** means the paying agent and agent bank agreement entered into on the Programme Date as amended and/or restated from time to time between, among others, the Issuer, the Paying Agents, the Transfer Agent, the Registrar, the Exchange Agent, the Agent Bank and the Issuer Security Trustee;

**Paying Agents** means the Principal Paying Agent and the US Paying Agent, together with any further or other paying agents for the time being appointed under the Paying Agent and Agent Bank Agreement;

**Post-Enforcement Call Option Holder or PECO** means Pendeford PECO Limited; **Principal Amount Outstanding** has the meaning given in **Condition 5.3**;

**Principal Paying Agent** means Deutsche Bank AG, London Branch in its capacity as principal paying agent at its Specified Office or such other person for the time being acting as principal paying agent under the Paying Agent and Agent Bank Agreement;

**Programme Date** means the date of the first issuance of Notes by the Issuer, 12 April 2007;

**Quarter Dates** means the 12th day of February, May, August and November;

**Quarterly Interest Payment Dates** means, in respect of a Series and Class of Notes (other than Money Market Notes), each Quarterly Date specified in the Final Terms for the payment of interest and/or principal, subject to the appropriate Business Day Convention, if any, specified in the applicable Final Terms;

**Rate of Interest and Rates of Interest** means, in respect of any Series and Class of Notes, the rate or rates (expressed as a percentage per annum) of interest payable in respect of such Notes specified in the applicable Final Terms or calculated and determined in accordance with the applicable Final Terms;

**Rating Agencies** means Standard & Poor's Rating Services, a division of The McGraw-Hill Companies Inc., Moody's Investors Service Limited and Fitch Ratings Ltd.;

**Reference Price** means, in respect of any Series and Class of Notes, the price specified as such for such Notes in the applicable Final Terms;

**Reference Rate** means, in respect of any Series and Class of Notes, the rate specified as such for such Notes in the applicable Final Terms;

**Regulation S** means Regulation S under the United States Securities Act of 1933, as amended;

**Reg S Global Notes** means the note certificates representing the Reg S Notes while in global form;

**Reg S Notes** means each Series and Class of Notes that are sold outside the United States to non-US persons in reliance on Regulation S;

**Register** means the register of Noteholders kept by the Registrar and which records the identity of each Noteholder and the number of Notes that each Noteholder owns;

**Registrar** means Deutsche Bank Trust Company Americas in its capacity as registrar at its Specified Office or such other person for the time being acting as registrar under the Paying Agent and Agent Bank Agreement;

**Relevant Screen** means a page of the Reuters service or Bloomberg service (or any other medium for electronic display of data as may be previously approved in writing by the Note Trustee and has been notified to Noteholders in the manner set out in **Condition 14**);

**Relevant Screen Page** means, in respect of any Series and Class of Notes, the screen page specified as such for such Notes in the applicable Final Terms (or such replacement page on the relevant service which displays the information);

**Remarketing Agent** means, in respect of any Series and Class of Remarketable Notes, the Remarketing Agent specified in the applicable Final Terms or such other agent appointed to act as remarketing agent under the terms of the relevant Remarketing Agreement;

**Remarketing Agreement** means, in respect of any Series and Class of Remarketable Notes, the agreement between the Issuer and the Remarketing Agent pursuant to which the Remarketing Agent agrees to use reasonable efforts to identify third party purchasers for such Remarketable Notes on each Mandatory Transfer Date prior to the occurrence of a Mandatory Transfer Termination Event;

**Remarketable Notes** means any Series and Class of Notes identified as such in the applicable Final Terms;

**Reset Margin** means, in respect of any Series and Class of Remarketable Notes, (i) for each Reset Period, a percentage not exceeding the Maximum Reset Margin determined by the Remarketing Agent in accordance with the Remarketing Agreement or (ii) if the Remarketing Agreement has been terminated, the Maximum Reset Margin;

**Reset Period** means, in respect of any Series and Class of Remarketable Notes, the period commencing on the first Mandatory Transfer Date specified in the applicable Final Terms up to (but excluding) the next Mandatory Transfer Date and thereafter the period from (and including) each Mandatory Transfer Date up to (but excluding) the next Mandatory Transfer Date;

**Rule 144A Global Notes** means the note certificates representing the Rule 144A Notes while in global form;

**Rule 144A Notes** means each Series and Class of Notes which are sold in the United States only to QIBs within the meaning of Rule 144A under the Securities Act;

**Securitisation Tax Regime** means the permanent regime for the taxation of securitisation companies established pursuant to the Finance Act 2005 and the regulations made thereunder, in each case as amended from time to time;

**Series** means, subject to **Condition 15**, in relation to the Notes, all Notes (of any Class) issued on a given day and designated as such;

**Series and Class** means, a particular Class of Notes of a given Series or, where such Class of such Series comprises more than one sub-class, **Series and Class** means any sub-class of such Class;

**Specified Currency** means, in respect of any Series and Class of Notes, the currency or currencies specified as such for such Notes in the applicable Final Terms;

**Specified Currency Exchange Rate** means, in relation to a Series and Class of Notes, the exchange rate specified in the Issuer Swap Agreement relating to such Series and Class of Notes or, if the Issuer Swap Agreement has been terminated, the applicable spot rate;

**Specified Date** has the meaning indicated in **Condition 11.6**;

**Specified Denomination** means, in respect of any Series and Class of Notes, the denomination specified as such for such Notes in the applicable Final Terms which shall be a minimum of \$100,000 (in the case of Dollar Note), £50,000 (in the case of each Sterling Note, provided in respect of Sterling Notes issued with a maturity of less than 366 days, £100,000) and €50,000 (in the case of each Euro Note), provided that no Note shall be issued with a denomination of less than €50,000 (or its equivalent in the relevant Specified Currency);

**Specified Office** means, as the context may require, in relation to any of the Agents, the office specified against the name of such Agent in the Paying Agent and Agent Bank Agreement or such other specified office as may be notified to the Issuer and the Note Trustee pursuant to the Paying Agent and Agency Bank Agreement;

**Step-up Date** means the Interest Payment Date on which the Rates of Interest on the relevant Series and Class of Notes increases by a pre-determined amount as specified for such Notes in the applicable Final Terms;

**sterling, pounds sterling** or **£** means the lawful currency for the time being of the United Kingdom of Great Britain and Northern Ireland;

**Sterling Notes** means each Series and Class of Notes denominated in sterling;

**sub-unit** means, with respect to any currency other than sterling, the lowest amount of such currency that is available as legal tender in the country of such currency and, with respect to sterling, one pence;

**Tender Agent** means, in respect of any Series and Class of Remarketable Notes, the Tender Agent specified for such Remarketable Notes in the applicable Final Terms;

**Transfer Agent** means Deutsche Bank Trust Company Americas in its capacity as transfer agent at its Specified Office or such other person for the time being acting as transfer agent under the Paying Agent and Agent Bank Agreement; and

**US Paying Agent** means Deutsche Bank Trust Company Americas, acting in its capacity as US paying agent or such other person for the time being acting as US paying agent under the Paying Agent and Agent Bank Agreement.



## **Material legal aspects of the loans**

The following discussion is a summary of the material legal aspects of English and Scottish residential property loans and mortgages. It is not an exhaustive analysis of the relevant law.

### **English Loans**

#### *General*

There are two parties to a mortgage. The first party is the mortgagor, who is the borrower and homeowner. The mortgagor grants the mortgage over its property. The second party is the mortgagee, who is the lender. Each English loan will be secured by an English mortgage which has a first ranking priority over all other mortgages secured on the property and over all unsecured creditors of the borrower. Borrowers may create a subsequent mortgage or other secured interest over the relevant property without the consent of the seller, though such other mortgage or interest will rank below the seller's mortgage in priority.

#### *Nature of property as security*

There are two forms of title to land in England and Wales: registered and unregistered. Both systems of title can include both freehold and leasehold land.

#### *Registered title*

Title to registered land is registered at the Land Registry. Each parcel of land is given a unique title number. Prior to 13 October 2003 title to the land was established by a land certificate or (in the case of land which is subject to a mortgage or charge) charge certificate containing official copies of the entries on the register relating to that land, however, pursuant to the Land Registration Act 2002 which came into force on 13 October 2003 the provision of land certificates and charge certificates has now been abolished. Title to land is now established by reference to entries on the registers held by the Land Registry.

There are four classes of registered title. The most common is title absolute. A person registered with title absolute owns the land free from all interests other than those entered on the register and those classified as unregistered interests which override first registration and unregistered interests which override registered dispositions.

Title information documents provided by the Land Registry will reveal the present owner of the land, together with any legal charges and other interests affecting the land. However, the Land Registration Act 2002 provides that some interests in the land will bind the land even though they are not capable of registration at the Land Registry such as unregistered interests which override first registration and unregistered interests which override registered dispositions. The title information documents will also contain a plan indicating the location of the land. However, this plan is not conclusive as to matters such as the location of boundaries.

#### *Unregistered title*

All land in England and Wales is now subject to compulsory registration on the happening of any of a number of trigger events, which includes the granting of a first legal mortgage. However, a small proportion of land in England and Wales (typically where the land has been in the same ownership for a number of years) is still unregistered. Title to unregistered land is proved by establishing a chain of documentary evidence to title going back at least 15 years. Where the land is affected by third party rights, some of those rights can be proved by documentary evidence or by proof of continuous exercise of the rights for a prescribed period and do not require registration. However, other rights would have to be registered at the Central Land Charges Registry in order to be effective against a subsequent purchaser of the land.

#### *Taking security over land*

Where land is registered, a mortgagee must register its mortgage at the Land Registry in order to secure priority over any subsequent mortgagee. Prior to registration, the mortgage will take effect only as an equitable mortgage or charge. Priority of mortgages over registered land is governed by the date of registration of the mortgage rather than date of creation. However, a prospective mortgagee is able to obtain a priority period within which to register his mortgage. If the mortgagee submits a proper application for registration during this period, its interest will take priority over any application for registration of another interest which is received by the Land Registry during this priority period.

In the system of unregistered land, the mortgagee protects its interest by retaining possession of the title deeds to the property. Without the title deeds to the property, the borrower is unable to establish the necessary chain of ownership, and is therefore effectively prevented from dealing with its land without the consent of the mortgagee.

Priority of mortgages over unregistered land is governed first by the possession of title deeds, and in relation to subsequent mortgages by the registration of a land charge.

### *The seller as mortgagee*

The sale of the English mortgages by the seller to the mortgages trustee will take effect in equity only. The mortgages trustee will not apply to the Land Registry or the Central Land Charges Registry to register or record its equitable interest in the mortgages. The consequences of this are explained in “**Risk factors – There may be risks associated with the fact that the mortgages trustee has no legal title to the loans and their related security, which may adversely affect payments on the notes**” above.

### *Enforcement of mortgages*

If a borrower defaults under an English loan, the English mortgage conditions provide that all monies under the English loan will become immediately due and payable. The seller or its successors or assigns would then be entitled to recover all outstanding principal, interest and fees under the covenant of the borrower contained in the English mortgage conditions to pay or repay those amounts. In addition, the seller or its successors or assigns may enforce its English mortgage in relation to the defaulted loan. Enforcement may occur in a number of ways, including the following:

- The mortgagee may enter into possession of the property. If it does so, it does so in its own right and not as agent of the mortgagor, and so may be personally liable for mismanagement of the property and to third parties as occupier of the property.
- The mortgagee may lease the property to third parties.
- The mortgagee may foreclose on the property. Under foreclosure procedures, the mortgagor’s title to the property is extinguished so that the mortgagee becomes the owner of the property. The remedy is, because of procedural constraints, rarely used.
- The mortgagee may sell the property, subject to various duties to ensure that the mortgagee exercises proper care in relation to the sale. This power of sale arises under the Law of Property Act 1925. The purchaser of a property sold pursuant to a mortgagee’s power of sale becomes the owner of the property.

A court order under section 126 of the CCA is necessary to enforce a land mortgage in certain circumstances as described under “**Risk factors – If Birmingham Midshires’ interpretation of certain technical rules under the CCA were held to be incorrect by a court or the Ombudsman or was challenged by a significant number of borrowers, or borrowers exercise rights of set-off insofar as available under the CCA, there could be material disruption in the income from the mortgages trust**” above.

## **Scottish loans**

### *General*

A standard security is the only means of creating a fixed charge over heritable or long leasehold property in Scotland. Its form must comply with the requirements of the Conveyancing and Feudal Reform (Scotland) Act 1970 (the **1970 Act**). There are two parties to a standard security. The first party is the grantor, who is the borrower and homeowner. The grantor grants the standard security over its property (and is generally the only party to execute the standard security). The second party is the grantee of the standard security, who is the lender and is called the heritable creditor. Each Scottish loan will be secured by a standard security which has a first ranking priority over all other standard securities secured on the property and over all unsecured creditors of the borrower. Borrowers may create a subsequent standard security over the relevant property without the consent of the seller. Upon intimation to the seller (in its capacity as trustee for the mortgages trustee pursuant to the relevant Scottish declaration of trust) of any subsequent standard security the prior ranking of the seller’s standard security shall be restricted to security for advances made prior to such intimation and advances made subsequent to such intimation which the seller or the mortgages trustee is obliged to advance, and interest and expenses in respect thereof.

The 1970 Act automatically imports a statutory set of **Standard Conditions** into all standard securities, although the majority of these may be varied by agreement between the parties. The seller, along with most lenders in the residential mortgage market in Scotland, has elected to vary the Standard Conditions by means of its own set of Scottish mortgage conditions, the terms of which are imported into each standard security. The main provisions

of the Standard Conditions which cannot be varied by agreement relate to redemption and enforcement, and in particular the notice and other procedures that are required to be carried out prior to the exercise of the heritable creditor's rights on a default by the borrower.

#### *Nature of property as security*

While title to all land in Scotland is registered there are currently two possible forms of registration, namely the Land Register and Sasine Register. Both systems of registration can include both heritable (the Scottish equivalent to freehold) and long leasehold land.

#### *Land Register*

This system of registration was established by the Land Registration (Scotland) Act 1979 and now applies to the whole of Scotland. Any sale of land (including a long leasehold interest in land) the title to which has not been registered in the Land Register or the occurrence of certain other events in relation thereto (but not the granting of a standard security alone) trigger its registration in the Land Register, when it is given a unique title number. Title to the land and the existence of a standard security over it are established by the entries on the Land Register relating to that land. Prior to 22 January 2007, the holder of the title received a land certificate containing official copies of the relevant entries on the Land Register. Similarly, the holder of any standard security over the land in question received a charge certificate containing official copies of the entries relating to that security. However, in terms of the Automated Registration of Title to Land (Electronic Communications) (Scotland) Order 2006 and the Land Registration (Scotland) Rules 2006, with effect from 22 January 2007 such land and charge certificates will only be issued to the relevant title or security holder if so requested at the time of the relevant registration and will otherwise be available in electronic form only. A person registered in the Land Register owns the land free from all interests other than those entered on the Register, those classified as overriding interests and any other interests implied by law.

The relevant Land Register entries and land certificates (whether in paper or electronic form) will reveal the present owners of the land, together with any standard securities and other interests (other than certain overriding interests and any other interests implied by law) affecting the land. They will also contain a plan indicating the location and extent of the land. While this plan is not in all circumstances conclusive as to the extent of the land, it cannot be amended if this would be to the prejudice of a proprietor in possession of the land, unless the statutory indemnity in respect of such amendments has been expressly excluded in the relevant Land Register entries and land certificate.

#### *Sasine Register*

Title to all land in Scotland where no event has yet occurred to trigger registration in the Land Register is recorded in the General Register of Sasines. Title to such land is proved by establishing a chain of documentary evidence of title going back at least ten years. Where the land is affected by third party rights, some of those rights can be proved by documentary evidence or by proof of continuous exercise of the rights for a prescribed period and do not require registration. However, other rights (including standard securities) would have to be recorded in the Sasine Register in order to be effective against a subsequent purchaser of the land.

#### *Taking security over land*

A heritable creditor must register its standard security in the Land Register or the Sasine Register (as applicable) in order to perfect its security and secure priority over any subsequent standard security. Until such registration occurs, a standard security will not be effective against a subsequent purchaser or the heritable creditor under another standard security over the property. Priority of standard securities is (subject to express agreement to the contrary between the security holders) governed by their date of registration rather than their date of execution. There is no equivalent in Scotland to the priority period system which operates in relation to registered land in England and Wales.

#### *The seller as heritable creditor*

The sale of the Scottish mortgages by the seller to the mortgages trustee has been given effect by a number of declarations of trust by the seller and any further sale of Scottish mortgages in the future will be given effect by further declarations of trust, by which the beneficial interest in the Scottish mortgages has been or will be transferred to the mortgages trustee. Such beneficial interest (as opposed to the legal title) cannot be registered in the Land Register or Sasine Register. The consequences of this are explained in "**Risk factors – There may be risks associated with the fact that the mortgages trustee has no legal title to the loans and their related security, which may adversely affect the payments on the notes**" above.

#### *Enforcement of mortgages*

If a borrower defaults under a Scottish loan, the Scottish mortgage conditions provide that all monies under the Scottish loan will become immediately due and payable. The seller or its successors or assignees would then be entitled to recover all outstanding principal, interest and fees under the obligation of the borrower contained in the Scottish mortgage conditions to pay or repay those amounts. In addition, the seller or its successors or assignees may enforce its standard security in relation to the defaulted Scottish loan. Enforcement may occur in a number of ways, including the following (all of which arise under the 1970 Act):

- The heritable creditor may enter into possession of the property. If it does so, it does so in its own right and not as agent of the borrower, and so may be personally liable for mismanagement of the property and to third parties as occupier of the property.
- The heritable creditor may grant a lease of the property of up to seven years (or longer with the court's permission) to third parties.
- The heritable creditor may sell the property, subject to various duties to ensure that the sale price is the best that can reasonably be obtained. The purchaser of a property sold pursuant to a heritable creditor's power of sale becomes the owner of the property.
- The heritable creditor may, in the event that a sale cannot be achieved, foreclose on the property. Under foreclosure procedures the borrower's title to the property is extinguished so that the heritable creditor becomes the owner of the property. However, this remedy is rarely used.

In contrast to the position in England and Wales, the heritable creditor has no power to appoint a receiver under the standard security.

A court order under section 126 of the CCA is necessary to enforce a standard security in certain circumstances as described under "**Risk factors – If Birmingham Midshires' interpretation of certain technical rules under the CCA were held to be incorrect by a court or the Ombudsman or was challenged by a significant number of borrowers, or borrowers exercise rights of set-off insofar as available under the CCA, there could be material disruption in the income from the mortgages trust**" above.

### **Borrower's right of redemption**

Under Section 11 of the Land Tenure Reform (Scotland) Act 1974 the grantor of any standard security over residential property has an absolute right, on giving appropriate notice, to redeem that standard security once it has subsisted for a period of 20 years, subject only to the payment of certain sums specified in Section 11 of that Act. These specified sums consist essentially of the principal monies advanced by the lender, interest thereon and expenses incurred by the lender in relation to that standard security.

## United Kingdom taxation

*The following applies only to persons who are the beneficial owners of notes and is a summary of the issuing entity's understanding of current law and practice in the United Kingdom relating only to United Kingdom withholding tax treatment of payments of principal and interest in respect of notes. It does not deal with any other United Kingdom taxation implications of acquiring, holding or disposing of notes. The United Kingdom tax treatment of prospective noteholders depends on their individual circumstances and may be subject to change in the future. Prospective noteholders who may be subject to tax in a jurisdiction other than the United Kingdom or who may be unsure as to their tax position should seek their own professional advice.*

### **Payment of interest on the notes**

Payments of interest on the notes may be made without deduction of or withholding on account of United Kingdom income tax provided that the notes are and continue to be listed on a "recognised stock exchange" within the meaning of section 1005 of the Income Tax Act 2007. The London Stock Exchange is a recognised stock exchange. Securities will be treated as listed on the London Stock Exchange if they are included on the Official List (within the meaning of and in accordance with the provisions of Part 6 of the Financial Services and Markets Act 2000) and admitted to trading on the London Stock Exchange. Provided, therefore, that the notes are and remain so listed, interest on the notes will be payable without withholding or deduction on account of United Kingdom tax.

Interest on the notes may also be paid without withholding or deduction on account of United Kingdom tax where interest on the notes is paid by a company and, at the time the payment is made, the issuing entity reasonably believes (and any person by or through whom interest on the notes is paid reasonably believes) that the beneficial owner is within the charge to United Kingdom corporation tax as regards the payment of interest, provided that HM Revenue and Customs has not given a direction (in circumstances where it has reasonable grounds to believe that the above exemption is not available in respect of such payment of interest at the time the payment is made) that the interest should be paid under deduction of tax.

Interest on the notes may also be paid without withholding or deduction on account of United Kingdom tax where the maturity of the notes is less than 365 days and those notes do not form part of a scheme or arrangement of borrowing intended to be capable of remaining outstanding for more than 364 days.

In other cases, an amount must generally be withheld from payments of interest on the notes on account of United Kingdom income tax at the basic rate (currently 20 per cent.). However, where an applicable double tax treaty provides for a lower rate of withholding tax (or for no tax to be withheld) in relation to interest paid to a noteholder, HM Revenue and Customs can issue a notice to the issuing entity to pay interest to the noteholder without deduction of tax (or for interest to be paid with tax deducted at the rate provided for in the relevant double tax treaty).

Noteholders may wish to note that in certain circumstances, HM Revenue and Customs has power to obtain information (including the name and address of the beneficial owner of the interest) from any person in the United Kingdom who either pays or credits interest to or receives interest for the benefit of a noteholder. HM Revenue and Customs also has power, in certain circumstances, to obtain information from any person in the United Kingdom who pays amounts payable on the redemption of notes which are deeply discounted securities for the purposes of the Income Tax (Trading and Other Income) Act 2005 to, or receives such amounts for the benefit of, another person, although HM Revenue and Customs published practice indicates that HM Revenue and Customs will not exercise the power referred to above to require this information in respect of notes which are deeply discounted securities where such amounts are paid on or before 5 April 2009. Such information may include the name and address of the beneficial owner of the amount payable on redemption. Any information obtained may, in certain circumstances, be exchanged by HM Revenue and Customs with the tax authorities of the jurisdiction in which the noteholder is resident for tax purposes.

### **EU Savings Directive**

Under EC Council Directive 2003/48/EC on the taxation of savings income (the **EU Savings Directive**), a Member State is required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State. However, for a transitional period, Belgium, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A number of non-EU countries and territories including Switzerland have agreed to adopt similar measures (a withholding system in the case of Switzerland).

For additional disclosure in relation to the EU Savings Directive in relation to Jersey, see “**Material Jersey (Channel Islands) tax considerations**” below.

## United States federal income taxation

### General

**To ensure compliance with IRS Circular 230, investors are hereby notified that: (a) any discussion of federal tax issues contained or referred to in this prospectus or any applicable final terms is not intended or written to be used, and cannot be used, by investors for the purpose of avoiding penalties that may be imposed on them under the Internal Revenue Code of 1986, as amended; (b) such discussion is written to support the promotion or marketing of the transactions or matters addressed herein; and (c) prospective investors should seek advice based on their particular circumstances from an independent tax adviser.**

The following section discusses the material US federal income tax consequences of the purchase, ownership and disposition of the Rule 144A notes, subject to the qualifications set forth in the applicable final terms. In general, the discussion assumes that a holder acquires the Rule 144A notes at original issuance and holds the Rule 144A notes as capital assets. It does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to purchase the Rule 144A notes. In particular, it does not discuss special tax considerations that may apply to certain types of taxpayers, including, without limitation, the following: (i) financial institutions; (ii) insurance companies; (iii) dealers or traders in stocks, securities, notional principal contracts or currencies; (iv) regulated investment companies; (v) real estate investment trusts, (vi) persons that will hold the Rule 144A notes as part of a “hedging” or “conversion” transaction or as a position in a “straddle” for US federal income tax purposes; (vii) persons that own (or are deemed to own) 10 per cent. or more of the voting shares of the issuing entity; (viii) persons who hold Rule 144A notes through partnerships or other pass-through entities; and (ix) persons that have a “functional currency” other than the US dollar, and (x) certain US expatriates and former long-term residents of the United States. This discussion does not address alternative minimum tax consequences, nor does it describe any tax consequences arising under the laws of any taxing jurisdiction other than the US federal government. In addition, please consult the applicable final terms in the event the Rule 144A notes are denominated in a currency other than the US dollar.

This discussion is based on the US Internal Revenue Code of 1986, as amended (the **Code**), US Treasury regulations promulgated thereunder and judicial and administrative interpretations thereof, in each case as in effect or available on the effective date of the registration statement. All of the foregoing are subject to change, and any change may apply retroactively and could affect the tax consequences described below.

As described below, upon issuance of the Rule 144A notes, Allen & Overy LLP, US federal income tax advisers to the issuing entity (**US tax counsel**) have delivered and will deliver an opinion that the mortgages trustee acting as trustee of the mortgages trust, Funding 1 and the issuing entity will not be subject to US federal income tax as a result of their contemplated activities. As described further under “– **Characterisation of the Rule 144A notes**” below, unless otherwise indicated in the applicable final terms, upon issuance of the Rule 144A notes, US tax counsel will deliver an opinion that, although there is no authority on the treatment of instruments substantially similar to the Rule 144A notes, the class A Rule 144A notes, the class B Rule 144A notes and the class M Rule 144A notes, when issued, will be treated as debt for US federal income tax purposes and the class C Rule 144A notes, when issued, should be treated as debt for US federal income tax purposes.

An opinion of US tax counsel is not binding on the US Internal Revenue Service (the **IRS**) or the courts, and no rulings will be sought from the IRS on any of the issues discussed in this section and there can be no assurance that the IRS or courts will agree with the conclusions expressed herein. **Accordingly, investors are encouraged to consult their own tax advisers as to the personal US federal income tax consequences to the investor of the purchase, ownership and disposition of the Rule 144A notes, including the possible application of state, local, non-US or other tax laws, and other US tax issues affecting the transaction.**

As used in this section, the term **United States holder** means a beneficial owner of Rule 144A notes that is for US federal income tax purposes: (i) a citizen or individual resident of the United States; (ii) a corporation (or other entity treated as a corporation), created or organised in or under the laws of the United States or any state thereof (including the District of Columbia); (iii) any estate, the income of which is subject to US federal income tax regardless of the source of its income; or (iv) any trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more US persons have the authority to control all substantial decisions of the trust. A **Non-United States holder** is a beneficial owner of Rule 144A notes that is not a United States Holder. If a partnership holds Rule 144A notes, the tax treatment of a partner will generally depend upon the status of the partner and upon the activities of the partnership. Partners of partnerships holding Rule 144A notes are encouraged to consult their own tax advisers regarding the personal tax consequences to them.

## **Tax status of the issuing entity, Funding 1, mortgages trustee and mortgages trust.**

Under the transaction documents, each of the issuing entity, Funding 1 and the mortgages trustee acting in its capacity as trustee of the mortgages trust covenants not to engage in any activities in the United States (directly or through agents), not to derive any income from sources within the United States as determined under US federal income tax principles, and not to hold any property if doing so would cause it to be engaged or deemed to be engaged in a trade or business within the United States as determined under US federal income tax principles. US tax counsel is of the opinion that, assuming compliance with the transaction documents, none of the issuing entity, Funding 1 or the mortgages trustee acting in its capacity as trustee of the mortgages trust will be subject to US federal income tax. See “**United States federal income taxation – General**” for further information regarding this opinion. No election will be made to treat the issuing entity, Funding 1 or the mortgages trustee or any of their assets as a REMIC (a type of securitisation vehicle having a special tax status under the Code).

## **Characterisation of the Rule 144A notes**

Although there is no authority regarding the treatment of instruments that are substantially similar to the Rule 144A notes, unless otherwise indicated in the applicable final terms, upon issuance of the Rule 144A notes, US tax counsel will deliver an opinion that the class A Rule 144A notes, the class B Rule 144A notes and the class M Rule 144A notes, when issued, will be treated as debt for US federal income tax purposes and the class C Rule 144A notes, when issued, should be treated as debt for US federal income tax purposes (see “– **Alternative Characterisation of the Rule 144A notes**” below and see “**United States federal income taxation – General**” above for further information regarding this opinion). The issuing entity intends to treat the Rule 144A notes as indebtedness of the issuing entity for all purposes, including US tax purposes.

The Rule 144A notes will not be qualifying real property loans in the hands of domestic savings and loan associations, real estate investment trusts, or REMICs under sections 7701(a)(19)(C), 856(c) or 860G(a)(3) of the Code, respectively.

## **Taxation of United States holders of the Rule 144A notes**

### *Qualified Stated Interest and Original Issue Discount*

The issuing entity intends to treat interest on the Rule 144A notes as **qualified stated interest** under US Treasury regulations relating to original issue discount (hereafter the **OID regulations**). As a consequence, discount on the Rule 144A notes arising from an issuance at less than par will only be required to be accrued under the OID regulations if such discount exceeds a statutorily defined *de minimis* amount. Qualified stated interest, which generally must be unconditionally payable at least annually, is taxed under a holder’s normal method of accounting as ordinary interest income. *De minimis* original issue discount (**OID**) is included in income on a *pro rata* basis as principal payments are made on the Rule 144A notes.

It is possible that interest on the Rule 144A notes that are class B notes, class M notes or class C notes could be treated as OID because such interest is subject to deferral in certain limited circumstances. A United States holder of a Rule 144A note issued with OID must include OID in income over the term of such Rule 144A note under a constant yield method that takes into account the compounding of interest. Under the Code, OID is calculated and accrued using prepayment assumptions where payments on a debt instrument may be accelerated by reason of prepayments of other obligations securing such debt instrument. Moreover, the legislative history to the provisions provides that the same prepayment assumptions used to price a debt instrument be used to calculate OID, as well as to accrue market discount and amortise premium. Here, prepayment of the loans is not expected to alter the scheduled principal payments on the Rule 144A notes that are class B notes, class M notes or class C notes and accordingly, the issuing entity intends to assume that such Rule 144A notes will have their principal repaid according to the schedule for purposes of accruing any OID. No representation is made that the loans will pay on the basis of such prepayment assumption or in accordance with any other prepayment scenario.

Rule 144A notes with a term of one year or less (**short-term obligations**), such as the money market notes, will be treated as having been issued with OID.

In general, United States holders who report income for US federal income tax purposes under the accrual method are required to accrue OID on short-term obligations on a straight-line basis unless an election is made to accrue the OID under a constant yield method (based on daily compounding). A United States holder who is an individual or other cash method holder is not required to accrue such OID unless such holder elects to do so. If such an election is not made, any gain recognised by such holder on the sale, exchange or maturity of such short term obligations will be ordinary income to the extent of the holder’s rateable share of OID accrued on a straight-line basis, or upon election under the constant yield method (based on daily compounding), through the date of the sale, exchange or maturity.



As an alternative to the above treatments, United States holders may elect to include in gross income all interest with respect to the Rule 144A notes, including stated interest, acquisition discount, OID, *de minimis* OID, market discount, *de minimis* market discount, and unstated interest, as adjusted by any amortisable bond premium or acquisition premium, using the constant yield method described above.

Interest income on the Rule 144A notes will be treated as foreign source income for US federal income tax purposes, which may be relevant in calculating a United States holder's foreign tax credit limitation for US federal income tax purposes. The limitation on foreign taxes eligible for the US foreign tax credit is calculated separately with respect to specific classes of income. The foreign tax credit rules are complex, and United States holders are encouraged to consult their own tax advisers regarding the availability of a foreign tax credit and the application of the limitation in their particular circumstances.

#### *Sales and retirement*

In general, a United States holder of a Rule 144A note will have a basis in such Rule 144A note equal to the cost of the Rule 144A note to such holder, increased by the amount of any OID included in the United States holder's income with respect to such Rule 144A note and reduced by any payments thereon other than payments of qualified stated interest. Upon a sale or exchange of the Rule 144A note, a United States holder will generally recognise gain or loss equal to the difference between the amount realised (less any accrued interest, which would be taxable as such) and the holder's tax basis in the Rule 144A note. Any gain or loss recognised by a United States holder will generally be US source gain or loss for foreign tax credit limitation purposes. Such gain or loss will be long-term capital gain or loss if the United States holder has held the Rule 144A note for more than one year at the time of disposition. **Prospective investors are encouraged to consult their own tax advisers regarding the treatment of capital gains (which may be taxed at lower rates than ordinary income for taxpayers who are individuals, trusts or estates that hold the Rule 144A notes for more than one year) and capital losses (the deductibility of which is subject to limitations).**

#### *Tax Treatment of Tax-Exempt U.S. Holders*

U.S. Holders which are tax-exempt entities (**Tax-Exempt U.S. Holders**) will not be subject to the tax on unrelated business taxable income (**UBTI**) with respect to interest and capital gains income derived from an investment in the Rule 144A notes. However, a Tax-Exempt U.S. Holder which incurs acquisition indebtedness (as defined in Section 514(c) of the Code) with respect to the Rule 144A notes may be subject to the tax on UBTI with respect to income from the notes to the extent that the Rule 144A notes constitute debt-financed property (as defined in Section 514(b) of the Code) of the Tax-Exempt U.S. Holder.

Tax-Exempt U.S. Holders should consult their own tax advisors regarding an investment in the Rule 144A notes.

#### *Taxation of Non-United States holders of the Rule 144A notes*

Subject to the backup withholding rules discussed below, a Non-United States holder generally should not be subject to US federal income or withholding tax on any payments on a Rule 144A note and gain from the sale, redemption or other disposition of a Rule 144A note unless: (i) that payment and/or gain is effectively connected with the conduct by that Non-United States holder of a trade or business in the United States; (ii) in the case of any gain realised on the sale or exchange of an offered note by an individual Non-United States holder, that holder is present in the United States for 183 days or more in the taxable year of the sale, exchange or retirement and certain other conditions are met; or (iii) the Non-United States holder is subject to tax pursuant to provisions of the Code applicable to certain expatriates. **Non-United States holders are encouraged to consult their own tax advisers regarding the US federal income and other tax consequences to them of owning Rule 144A notes.**

#### *Alternative characterisation of the Rule 144A notes*

The proper characterisation of the arrangement involving the issuing entity and the holders of the Rule 144A notes is not clear because there is no authority on transactions comparable to that contemplated herein. The issuing entity intends to treat the Rule 144A notes as debt for all Rule 144A federal income tax purposes. Prospective investors are encouraged to consult their own tax advisers regarding the personal tax consequences with respect to the potential impact of an alternative characterisation of the Rule 144A notes for Rule 144A federal income tax purposes.

One possible alternative characterisation is that the IRS could assert that the class C Rule 144A notes or any other class of Rule 144A notes should be treated as equity in the issuing entity for US federal income tax purposes because the issuing entity may not have substantial equity. If the class C Rule 144A notes or any other class of notes were treated as equity, United States holders of such Rule 144A notes would be treated as owning equity in a passive foreign investment company (**PFIC**) which, depending on the level of ownership of such United States

holders and certain other factors, might also constitute an interest in a controlled foreign corporation (**CFC**) for such United States holder. A Rule 144A note that is treated as an equity interest in a PFIC or CFC rather than a debt instrument for US federal income tax purposes would have certain timing and character consequences to a United States holders and could require certain elections and disclosures that would need to be made shortly after acquisition to mitigate potentially adverse US tax consequences.

If a United States holder were treated as owning an equity interest in a PFIC, unless a United States holder makes a **QEF election** or **mark to market election**, a United States holder will be subject to a special tax regime (i) in respect of gains realised on the sale or other disposition of the relevant notes, and (ii) in respect of distributions on the relevant notes held for more than one taxable year to the extent those distributions constitute excess distributions. Although not free from doubt, the PFIC rules should not apply to gain realised in respect of any notes disposed of during the same taxable year in which such notes are acquired. An excess distribution generally includes dividends or other distributions received from a PFIC in any taxable year to the extent the amount of such distributions exceeds 125 per cent. of the average distributions for the three preceding years (or, if shorter, the investor's holding period). For Rule 144A notes that pay interest at a floating rate, it is possible that a US holder will receive excess distributions as a result of fluctuations in the rate of USD-LIBOR over the term of Rule 144A notes. In general, under the PFIC rules, a United States holder will be required to allocate such excess distributions and any gain realised on a sale of its notes to each day during the United States holder's holding period for the Rule 144A notes, and will be taxable at the highest rate of taxation applicable to the notes for the year to which the excess distribution or gain is allocable (without regard to the United States holder's other items of income and loss for such taxable year) (the **deferred tax**). The deferred tax (other than the tax on amounts allocable to the year of disposition or receipt of the distribution) will then be increased by an interest charge computed by reference to the rate generally applicable to underpayments of tax (which interest charge generally will be a non-deductible interest expense for individual taxpayers). The issuing entity does not intend to provide information that would enable a holder of a note to make a QEF election, and the mark to market election will only be available during any period in which the notes are traded on a qualifying exchange or market and certain other trading requirements are met. The issuing entity encourages persons considering the purchase or ownership of 10 per cent., or more of any class of Rule 144A notes (or combination of classes) that is treated as equity for US federal income tax purposes to consult their own tax advisors regarding the US tax consequences resulting from such an acquisition under the special rules applicable to CFCs under the Code.

### **Backup withholding and information reporting**

Backup withholding and information reporting requirements may apply to certain payments on the Rule 144A notes and proceeds of the sale or redemption of the Rule 144A notes to United States holders. The issuing entity, its agent, a broker, or any paying agent, as the case may be, may be required to withhold tax from any payment that is subject to backup withholding if the United States holder fails to furnish the United States holder's taxpayer identification number (usually on IRS Form W-9), to certify that such United States holder is not subject to backup withholding, or to otherwise comply with the applicable requirements of the backup withholding rules. Certain United States holders (including, among others, corporations) are not subject to the backup withholding and information reporting requirements. Non-United States holders may be required to comply with applicable certification procedures (usually on IRS Form W-8BEN) to establish that they are not United States holders in order to avoid the application of such information reporting requirements and backup withholding.

Payments of principal or interest made to or through a foreign office of a custodian, nominee or other agent acting on behalf of a beneficial owner of a Rule 144A note generally will not be subject to backup withholding. However, if such custodian, nominee or other agent is (i) a United States person (as defined in section 7701(a)(30) of the Code), (ii) a controlled foreign corporation (as defined in section 957(a) of the Code), (iii) a foreign person 50 per cent. or more of whose gross income is effectively connected with a US trade or business for a specified three-year period, or (iv) a foreign partnership if (A) at any time during its tax year, one or more of its partners are United States persons (as defined in applicable Treasury regulations) who in the aggregate hold more than 50 per cent. of the income or capital interest in the partnership or (B) at any time during its taxable year, it is engaged in a US trade or business (each of (i) through (iv), a **US connected holder**), such custodian, nominee or other agent may be subject to certain information reporting requirements with respect to such payment unless it has in its records documentary evidence that the beneficial owner is not a United States holder and certain conditions are met or the beneficial owner otherwise establishes an exemption. Principal and interest paid by the US office of a custodian, nominee or agent will be subject to both backup withholding and information reporting unless the beneficial owner certifies its non-US status under penalties of perjury or otherwise establishes an exemption. Payments of proceeds on the sale of an offered note made to or through a foreign office of a broker will not be subject to backup withholding. However, if such broker is a US connected holder, information reporting will be required unless the broker has in its records documentary evidence that the beneficial owner is not a United States holder and certain conditions are met or the beneficial owner otherwise establishes an exemption. Payments of proceeds on the sale of an offered note made to or through the US office

of a broker will be subject to backup withholding and information reporting unless the beneficial owner certifies, under penalties of perjury, that it is not a US holder or otherwise establishes an exemption.

Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules will be refunded or credited against the United States holder's US federal income tax liability, provided that the required information is furnished to the IRS. **Holders of Rule 144A notes are encouraged to consult their tax advisers as to their qualification for exemption from backup withholding and the procedure for obtaining an exemption.**

#### **IRS disclosure reporting requirements**

US Treasury Regulations (the **disclosure regulations**) meant to require the reporting of certain tax shelter transactions (**reportable transactions**) could be interpreted to cover transactions generally not regarded as tax shelters. Under the disclosure regulations it may be possible that certain transactions with respect to the Rule 144A notes may be characterised as reportable transactions requiring a United States holder to disclose such transactions, such as sales, exchanges, retirements or other taxable dispositions of Rule 144A notes that result in losses that exceed certain thresholds and other specified conditions are met. **Accordingly, investors are encouraged to consult with their own tax advisers to determine the tax return obligations, if any, with respect to an Investment in the Rule 144A notes, including any requirement to file IRS Form 8886 (Reportable Transaction Statement).**

## **Material Jersey (Channel Islands) tax considerations**

### **Tax status of the mortgages trustee and the mortgages trust**

It is the opinion of Mourant du Feu & Jeune, Jersey (Channel Islands) tax counsel to the issuing entity, that the mortgages trustee is resident in Jersey for taxation purposes and is liable to income tax in Jersey at a rate of 20 per cent. in respect of the profits it makes from acting as trustee of the mortgages trust. The mortgages trustee is not liable for any income tax in Jersey in respect of any income it receives in its capacity as mortgages trustee on behalf of the beneficiaries of the mortgages trust.

Legislation has been adopted by the States of Jersey which, on and from 1 January 2009, introduces a standard rate of corporate tax of 0% applicable to all companies (other than any "financial services company" (as defined therein) and certain specified Jersey utility companies). As at the date of this Prospectus the mortgages trustee is neither a "financial services company" nor such a specified utility company.

### **EU Savings Directive**

As part of an agreement reached in connection with the EU Savings Directive on the taxation of savings income in the form of interest payments, in line with steps taken by other relevant third countries, Jersey introduced, with effect from 1 July 2005, a retention tax system in respect of payments of interest, or other similar income, made to an individual beneficial owner resident in an EU Member State by a paying agent established in Jersey. The retention tax system applies for a transitional period prior to the implementation of a system of automatic communication to EU Member States of information regarding such payments. During this transitional period, such an individual beneficial owner resident in an EU Member State is entitled to request a paying agent not to retain tax from such payments but instead to apply a system by which the details of such payments are communicated to the tax authorities of the EU Member State in which the beneficial owner is resident.

## ERISA considerations

The Rule 144A notes are eligible for purchase by employee benefit plans and other plans subject to the US Employee Retirement Income Security Act of 1974, as amended (**ERISA**), and/or the provisions of Section 4975 of the Code and by governmental, certain church and non-US plans that are subject to state, local or other federal law of the United States or foreign law that is substantially similar to Title I of ERISA or Section 4975 of the Code, subject to consideration of the issues described in this section. ERISA imposes certain requirements on **employee benefit plans** (as defined in Section 3(3) of ERISA) subject to Title I.6 ERISA, including entities such as collective investment funds and separate accounts whose underlying assets include the assets of such plans (collectively, **ERISA Plans**) and on those persons who are fiduciaries with respect to ERISA Plans. Investments by ERISA Plans are subject to ERISA's general fiduciary requirements, including the requirements of investment prudence and diversification and the requirement that an ERISA Plan's investments be made in accordance with the documents governing the Plan. The prudence of a particular investment must be determined by the responsible fiduciary of an ERISA Plan by taking into account the ERISA Plan's particular circumstances and all of the facts and circumstances of the investment including, but not limited to, the matters discussed under "**Risk factors**" above and the fact that in the future there may be no market in which such fiduciary will be able to sell or otherwise dispose of the Rule 144A notes.

Section 406 of ERISA and Section 4975 of the Code prohibit certain transactions involving the assets of an ERISA Plan (as well as those plans that are not subject to ERISA but which are subject to Section 4975 of the Code, such as individual retirement accounts (together with ERISA Plans, the **Plans**)) and certain persons (referred to as **parties in interest** or **disqualified persons**) having certain relationships to such Plans, unless a statutory or administrative exemption is applicable to the transaction. A party in interest or disqualified person who engages in a prohibited transaction may be subject to excise taxes and other penalties and liabilities under ERISA and the Code.

The seller, the issuing entity, the servicer, the mortgages trustee, Funding 1 or any other party to the transactions contemplated by the transaction documents may be parties in interest or disqualified persons with respect to many Plans. Prohibited transactions within the meaning of Section 406 of ERISA or Section 4975 of the Code may arise if any of the Rule 144A notes is acquired or held by a Plan with respect to which the issuing entity, the servicer, the mortgages trustee, Funding 1 or any other party to such transactions is a party in interest or a disqualified person. Certain exemptions from the prohibited transaction provisions of Section 406 of ERISA and Section 4975 of the Code may be applicable, however, depending in part on the type of Plan fiduciary making the decision to acquire any such notes and the circumstances under which such decision is made. Included among these exemptions are Section 408(b)(17) of ERISA (relating to certain transactions between a plan and a non-fiduciary service provider), Prohibited Transaction Class Exemption (**PTCE**) 91-38 (relating to investments by bank collective investment funds), PTCE 84-14 (relating to transactions effected by a **qualified professional asset manager**), PTCE 95-60 (relating to transactions involving insurance company general accounts), PTCE 90-1 (relating to investments by insurance company pooled separate accounts) and PTCE 96-23 (relating to transactions determined by in-house asset managers). Prospective investors should consult with their advisors regarding the application of these exemptions. There can be no assurance that any of these class exemptions or any other exemption will be available with respect to any particular transaction involving any such notes.

Non-US plans, governmental plans and certain church plans, while not subject to the fiduciary responsibility provisions of ERISA or the provisions of Section 4975 of the Code, may nevertheless be subject to other laws or regulations that are substantially similar to the foregoing provisions of ERISA and the Code (**similar laws**).

Unless otherwise stated in the Final Terms, each purchaser and subsequent transferee of any Rule 144A note will be deemed by such purchase or acquisition of any such note to have represented and warranted, on each day from the date on which the purchaser or transferee acquires such note through and including the date on which the purchaser or transferee disposes of such note, either that (A) it is not a Plan or an entity whose underlying assets include the assets of any Plan or a governmental, church or non-US plan which is subject to similar law or (B) its purchase, holding and disposition of such note will not result in a non-exempt prohibited transaction under section 406 of ERISA or section 4975 of the Code (or, in the case of a governmental, church or non-US plan a violation of any similar law).

Unless otherwise stated in the Final Terms, each purchaser and subsequent transferee of any Reg S notes will be deemed by such purchase or acquisition of any such note to have represented, warranted and agreed upon such purchase or acquisition that it is not and, for so long as it holds such note, it will not be, an employee benefit plan, Plan or disqualified person.

In addition, the US Department of Labor has promulgated a regulation, 29 C.F.R. Section 2510.3-101, as modified by Section 3(42) of ERISA (the **Plan Asset Regulation**), describing what constitutes the assets of a Plan with respect to the Plan's investment in an entity for purposes of certain provisions of ERISA, including the

fiduciary responsibility provisions of Title I of ERISA, and section 4975 of the Code. Under the Plan Asset Regulation, if a Plan invests in an equity interest of an entity that is neither a publicly-offered security nor a security issued by an investment company registered under the Investment Company Act, the Plan's assets include both the equity interest and an undivided interest in each of the entity's underlying assets, unless one of the exceptions to such treatment described in the Plan Asset Regulation applies. Under the Plan Asset Regulation, a security which is in debt form may be considered an equity interest if it has substantial equity features. If the issuing entity were deemed under the Plan Asset Regulation to hold plan assets by reason of a Plan's investment in any of the Rule 144A notes, such plan assets would include an undivided interest in the assets held by the issuing entity and transactions by the issuing entity would be subject to the fiduciary responsibility provisions of Title I of ERISA and the prohibited transaction provisions of ERISA and Section 4975 of the Code. The Plan Asset Regulation provides, however, that if equity participation in any entity by Benefit Plan Investors is not significant, then the "look-through" rule will not apply to such entity. The term **Benefit Plan Investors** is defined in the Plan Asset Regulation, as modified by Section 3(42) of ERISA, to include (1) any employee benefit plan (as defined in Section 3(3) of ERISA), subject to Title I of ERISA, (2) any plan described in Section 4975(e)(1) of the Code, and (3) any entity whose underlying assets include "plan assets" by reason of any such plan's investment in the entity. Equity participation by Benefit Plan Investors in any entity is significant if, immediately after the most recent acquisition of any equity interest in the entity, 25 per cent. or more of the value of any class of equity interests in the entity (excluding the value of any interests held by certain persons, other than Benefit Plan Investors) exercising control over the assets of the entity or providing investment advice to the entity for a fee or any affiliates of such persons is held by Benefit Plan Investors. The look-through rule will not apply to the underlying assets of the issuing entity if less than 25 per cent. of the value of each class of its equity interests are held by Benefit Plan Investors. Several rules apply in calculating this percentage under the Plan Asset Regulation. First, a proportionate rule applies to investments by one entity in another entity. Under this rule, if more than 25 per cent. of an investor's equity interests are held by Benefit Plan Investors, only a proportionate amount of its investment counts towards the 25 per cent. threshold (but if less than 25 per cent. of an investor's equity interests are held by Benefit Plan Investors, none of the investor's investment counts). Second, an entity must determine whether the 25 per cent. threshold has been reached each time an investor acquires an equity interest in the entity. The Department of Labor has taken the position in this regard that a redemption of an equity interest by an investor constitutes the acquisition of an equity interest by the remaining investors (through an increase in their percentage ownership of the remaining equity interests). Third, for this purpose, the value of any equity interests held by a person (other than a Benefit Plan Investor) who has discretionary authority or control with respect to the assets of an entity or any person who provides investment advice for a fee (direct or indirect) with respect to such assets, or any affiliate of such a person, is disregarded.

There is little pertinent authority in this area and securities may change character from debt to equity over time due to changing circumstances. Fiduciaries of Plans considering the purchase of notes should consult their counsel in this regard. As noted above, it is expected that the Class A notes, the Class B notes and the Class C notes, when issued, will be treated as debt for US federal income tax purposes and, thus, will not constitute "equity interests". Although there is less certainty that the Class C notes will be treated as debt for US federal income tax purposes, no measures will be taken to restrict investment in the Class C notes by Benefit Plan Investors.

Any insurance company proposing to purchase any of the Rule 144A notes using the assets of its general account should consider the extent to which such investment would be subject to the requirements of ERISA in light of the US Supreme Court's decision in *John Hancock Mutual Life Insurance Co. v. Harris Trust and Savings Bank* and under any subsequent guidance that may become available relating to that decision. In particular, such an insurance company should consider the retroactive and prospective exemptive relief granted by the Department of Labor for transactions involving insurance company general accounts in PTCE 95-60, 60 Fed. Reg. 35925 (12 July 1995), the enactment of Section 401(c) of ERISA by the Small Business Job Protection Act of 1996 (including, without limitation, the expiration of any relief granted thereunder) and the Insurance Company General Account Regulations, 65 Fed. Reg. No. 3 (5 January 2000) (codified at 29 C.F.R. pt. 2550) that became generally applicable on 5 July 2001.

Each Plan fiduciary who is responsible for making the investment decisions whether to purchase or commit to purchase and to hold any of the Rule 144A notes should determine whether, under the documents and instruments governing the Plan, an investment in such notes is appropriate for the Plan, taking into account the overall investment policy of the Plan and the composition of the Plan's investment portfolio and liquidity needs in view of the Plan's benefit obligations. Any Plan, governmental, church or non-US plan proposing to invest in such notes should consult with its counsel to confirm that such investment will not result in a non-exempt prohibited transaction and will satisfy the other requirements of ERISA and the Code (or, in the case of a governmental, church or non-US plan, any similar law).

The sale of any Rule 144A notes to a Plan is in no respect a representation by the seller, the issuing entity, the servicer, the mortgages trustee, Funding 1 or any other party to the transactions that such an investment meets all

relevant legal requirements with respect to investments by Plans generally or any particular Plan, or that such an investment is appropriate for Plans generally or any particular Plan.

### **Enforcement of foreign judgments in England and Wales**

The issuing entity is a UK public limited company incorporated with limited liability in England and Wales and its executive offices and administrative activities are located outside the United States. Any final and conclusive judgment of any United States federal or state court having jurisdiction recognised by England or Wales in respect of an obligation of the issuing entity in respect of the notes which is for a fixed sum of money and which has not been stayed or satisfied in full, would be enforceable by action against the issuing entity in the courts of England and Wales without a re-examination of the merits of the issues determined by the proceedings in that United States federal or state court, as applicable, unless:

- the proceedings in that United States federal or state court, as applicable, involved a denial of the principles of natural or substantial justice;
- the judgment is contrary to the public policy of England or Wales;
- the judgment was obtained by fraud or duress or was based on a clear mistake of fact;
- the judgment is of a public nature (for example, a penal or revenue judgment);
- there has been a prior judgment in another court between the same parties concerning the same issues as are dealt with in the judgment of the United States federal or state court, as applicable;
- enforcement would breach section 5 of the Protection of Trading Interests Act 1980; or
- enforcement proceedings are not instituted within six years after the date of the judgment.

A judgment by a court may be given in some cases only in sterling. The issuing entity expressly submits to the non-exclusive jurisdiction of the courts of England for the purpose of any suit, action or proceedings arising out of this offering.

All of the directors and executive officers of the issuing entity reside outside the United States. Substantially all or a substantial portion of the assets of all or many of those persons are located outside the United States. As a result, it may not be possible for holders of the notes to effect service of process within the United States upon those persons or to enforce against them judgments obtained in United States courts predicated upon the civil liability provisions of federal securities laws of the United States. Based on the restrictions referred to in this section, there is doubt as to the enforceability in England and Wales, in original actions or in actions for enforcement of judgments of United States courts, of civil liabilities predicated upon the federal securities laws of the United States.



### **United States legal investment considerations**

None of the notes constitute or will constitute **mortgage related securities** under the United States Secondary Mortgage Market Enhancement Act of 1984, as amended.

No representation is made as to the proper characterisation of the notes for legal investment purposes, financial institutional regulatory purposes, or other purposes, or as to the ability of particular investors to purchase the notes under applicable legal investment restrictions. These uncertainties may adversely affect the liquidity of the notes. Accordingly, all institutions whose investment activities are subject to legal investment laws and regulations, regulatory capital requirements or review by regulatory authorities should consult with their legal advisors in determining whether and to what extent the notes constitute legal investments or are subject to investment, capital or other restrictions.

Any money market notes of the issuing entity (as detailed in the final terms) are and will be “Eligible Securities” within the meaning of Rule 2a-7 under the Investment Company Act. Money market notes designated as remarketable notes in the relevant final terms will be sold subject to Condition 5.8, which provides for mandatory transfer on each Note mandatory transfer date in respect of the period up to and including the first mandatory transfer date. Thereafter, if a remarketing termination event has not occurred, it is expected that the remarketable notes will be “Eligible Securities” within the meaning of Rule 2a-7 in respect of the period up to and including the next following mandatory transfer date if the eligibility requirements of Rule 2a-7 remain unchanged.

## Remarketing Arrangements

### The remarketing agreement

If money market notes are designated as remarketable notes in the relevant final terms, the issuing entity will enter into an agreement (the **remarketing agreement**) pursuant to which it will appoint the remarketing agent specified in the final terms to act as its agent and to use its reasonable efforts to identify third party purchasers for such remarketable notes on each mandatory transfer date prior to the occurrence of a mandatory transfer termination event. Any amounts paid to the remarketing agent by any third party or the conditional purchaser for the remarketable notes as part of the mandatory transfer will be held by the remarketing agent as fiduciary for the relevant purchaser.

To facilitate the transfer of interests in the remarketable notes as part of the mandatory transfer, the remarketing agent may appoint a tender agent (the **tender agent**) specified in the final terms for the purpose of arranging delivery and payment by and to holders of the remarketable notes on the relevant mandatory transfer date. No further action will be required by such noteholders for the transfer of the remarketable notes to or for the account of the remarketing agent.

Prior to each mandatory transfer date prior to the occurrence of a mandatory transfer termination event, subject to the occurrence of a remarketing termination event (as defined below) then outstanding, the remarketing agent will approach potential investors with a view to procuring purchasers for the remarketable notes on the relevant mandatory transfer date. The remarketing agent will seek bids from investors for the margin to apply to the remarketable notes from the relevant mandatory transfer date. If there is one or more third parties willing to purchase in aggregate all the outstanding remarketable notes of the relevant series and class, the margin on all the remarketable notes of that series and class will be reset to an amount (not greater than the maximum reset margin) (the **reset margin**) being the lowest margin at which all such remarketable notes will be purchased by third parties as determined by the remarketing agent, if all of such remarketable notes cannot be placed with third parties, the margin will be reset to the maximum reset margin. The conditional purchaser will be obliged to purchase any such remarketable notes not otherwise purchased by third parties. If a remarketing termination event occurs, the reset margin will equal the maximum reset margin.

The issuing entity may terminate the remarketing agreement in certain circumstances, including where the remarketing agent becomes insolvent, no longer has the requisite authority or ability to act in accordance with the terms of the remarketing agreement or a material breach of warranty or covenant remains outstanding under the remarketing agreement.

The remarketing agent will have the right to terminate the remarketing agreement and will have no further obligations thereunder in certain circumstances, including where a note event of default has occurred and is continuing, there has been an event beyond the control of the remarketing agent or the issuing entity as a result of which the remarketing agent is unable to perform its obligations under the remarketing agreement or which in the reasonable opinion of the remarketing agent represents a material market change affecting the relevant remarketable note, the issuing entity is in material breach of any representations and warranties given by it in the conditional purchase agreement as at the closing date of the relevant remarketable notes, the requirements of Rule 2a-7 under the Investment Company Act in respect of the eligibility of such remarketable notes have changed since the closing date of such notes or a mandatory transfer termination event occurs. The occurrence of any of these events or a termination by the issuing entity pursuant to the previous paragraph where an alternative remarketing agent has not yet been appointed upon delivery of a notice from the remarketing agent to the issuing entity and the principal paying agent giving notice of termination is a remarketing termination event. The occurrence of a **remarketing termination event** does not affect the obligations of the conditional purchaser under the conditional purchase agreement (unless there has been a mandatory transfer termination event or a note event of default that is continuing).

A mandatory transfer termination event will occur if the conditional purchaser has purchased all the relevant remarketable notes under the terms of a mandatory transfer and the remarketing agent has confirmed such purchase or the tender agent has confirmed the interest in such remarketable notes has been transferred to the name or account of, or on behalf of, the conditional purchaser (either being a conditional purchaser confirmation), the confirmation in either case being given in writing to the issuing entity and the principal paying agent. If a conditional purchaser confirmation has been given with respect to any remarketable notes, the issuing entity will not be obliged to procure any subsequent purchasers of such remarketable notes and the remarketing agent will not be obliged to further remarket such notes.

## Subscription and sale

Any dealer(s) appointed from time to time (together, the **dealers**) in accordance with the programme agreement dated the programme date (as amended from time to time) shall agree with the issuing entity a basis upon which such dealers or any of them may from time to time agree to purchase notes. The issuing entity may pay the dealers a selling commission and a management and underwriting fee from time to time in connection with the sale of any notes. In the programme agreement, the issuing entity has agreed to reimburse and indemnify the dealers for certain of their expenses and liabilities in connection with the establishment and any future update of the programme and the issue of the notes under the programme. The dealers are entitled to be released and discharged from their obligations in relation to any agreement to issue and purchase notes under the programme agreement in certain circumstances prior to the payment to the issuing entity.

Some of the dealers are expected to make offers and sales of notes both inside and outside the United States through their respective selling agents. Any offers or sales in the United States will be conducted by broker dealers registered with the SEC.

### United Kingdom

Each dealer has represented and agreed, and each further dealer appointed under the programme agreement will be required to represent and agree, that:

- in relation to any notes which have a maturity of less than one year, (i) it is a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business and (ii) it has not offered or sold and will not offer or sell any notes other than to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or as agent) for the purposes of their businesses or who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses where the issue of the notes would otherwise constitute a contravention of Section 19 of the FSMA by the issuing entity;
- it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of section 21 of the FSMA) received by it in connection with the issue or sale of any notes in circumstances in which section 21(1) of the FSMA does not apply to the issuing entity; and
- it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the notes in, from or otherwise involving the United Kingdom.

### United States

Each dealer has acknowledged, and each dealer appointed under the programme agreement will be required to acknowledge, that the notes have not been and will not be registered under the Securities Act or any state securities laws, and may not be offered or sold within the United States or to, or for the account or benefit of, US persons except in accordance with Regulation S or in certain transactions exempt from the registration requirements of the Securities Act and applicable state securities laws. In addition, the notes cannot be resold in the United States or to US persons unless they are subsequently registered or an exemption from registration is available. Each dealer has agreed, and each further dealer appointed under the programme agreement will be required to agree, that with respect to the relevant Reg S notes for which it has subscribed that it will not offer, sell or deliver the Reg S notes (a) as part of their distribution at any time or (b) otherwise until 40 days after the later of the commencement of the offering of the Reg S notes and the relevant closing date (the **distribution compliance period**) within the United States or to, or for the account or benefit of, US persons except in accordance with Regulation S and that it will have sent to each distributor, dealer or person receiving a selling commission, fee or other remuneration that purchases Reg S notes from it during the distribution compliance period (other than resales pursuant to Rule 144A) a confirmation or other notice setting forth the restrictions on offers and sales of the Reg S notes within the United States or to, or for the account or benefit of, US persons. Terms used in this paragraph have the meanings given to them by Regulation S.

In addition, until the expiration of 40 days after commencement of the offering in respect of any series and class of notes, an offer or sale of the notes within the United States by any dealer, whether or not participating in the offering, may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in compliance with Rule 144A or pursuant to another exemption from the registration requirements under the Securities Act.

The dealers may directly or through their respective US broker-dealer affiliates arrange for the offer and resale of Rule 144A notes within the United States only to QIBs in reliance to Rule 144A and each purchaser of Rule 144A notes is hereby notified that the sellers may be relying on the exemption from the registration requirements of the Securities Act provided by Rule 144A. To the extent that the issuing entity is not subject to or does not comply with the reporting requirements of Section 13 or 15(d) of the Exchange Act or the information furnishing requirements of Rule 12g3-2(b) thereunder, the issuing entity has agreed to furnish to holders of Rule 144A notes and to prospective purchasers designated by such holders, upon request, such information as may be required by Rule 144A(d)(4).

Each dealer has represented and agreed and each dealer appointed under the programme agreement will be required to represent and agree that it has not (and will not), nor has (nor will) any person acting on its behalf: (a) made offers or sales of any security or solicited offers to buy, or otherwise negotiated in respect of any security, under circumstances that would require the registration of the notes under the Securities Act; or (b) engaged in any form of general solicitation or general advertising (within the meaning of Rule 502(c) under the Securities Act) in connection with any offer or sale of notes in the United States.

Each dealer has acknowledged that the Reg S notes are not designed for, and may not be purchased or held by, any “employee benefit plan” as defined in Section 3(3) of ERISA, which is subject to Title I thereto, any “plan” as defined in Section 4975 of the Code or by any person any of the assets of which are, or are deemed for purposes of ERISA or Section 4975 of the Code to be, assets of such an “employee benefit plan” or “plan” and each purchaser of a such note will be deemed to have represented, warranted and agreed that it is not, and for so long as it holds such note will not be, such an “employee benefit plan”, “plan” or person.

### **Republic of Italy**

The offering of the notes has not been registered pursuant to the Italian securities legislation and, accordingly, no notes may be offered, sold or delivered, nor may copies of this prospectus or of any other document relating to the notes be distributed in the Republic of Italy, except:

- (a) to qualified investors (*investitori qualificati*), as defined in Article 100 of Legislative Decree No. 58 of 24 February 1988, as amended (the **Financial Services Act**) which includes natural persons and small and medium-sized enterprises as defined by Directive 2303/71/EU of 4 November 2003 and Article 31, second paragraph, of CONSOB (the **Italian Securities Exchange Commission**) Regulation No. 11522 of 1 July 1988, as amended (Regulation No. 11522) by CONSOB; or
- (b) in circumstances which are exempted from the rules on solicitation of investments pursuant to Article 100 of the Financial Services Act and Article 33, first paragraph, of CONSOB Regulation No. 11971 of 14 May 1999, as amended (Regulation No. 11971).

Any offer, sale or delivery of the notes or distribution of copies of this base prospectus or any other document relating to the notes in the Republic of Italy under (a) or (b) above must be:

- (i) made by an investment firm, bank or financial intermediary permitted to conduct such activities in the Republic of Italy in accordance with the Financial Services Act, Regulation No. 11522 and Legislative Decree No. 385 of 1 September 1993, as amended (the Banking Act); and
- (ii) in compliance with any other applicable laws and regulations or requirement imposed by CONSOB.

### **General**

Except for the listing of the listed notes during a period of 12 months from the date of this base prospectus on the Official List of the UK Listing Authority, the admission to trading of the listed notes on the London Stock Exchange’s Regulated Market, no action is being taken by the issuing entity or the dealers in any jurisdiction which would or is intended to permit a public offering of the notes or the possession, circulation or distribution of this base prospectus or any other material relating to the issuing entity or the notes in any country or jurisdiction where action for that purpose is required.

This base prospectus does not constitute, and may not be used for the purposes of, an offer or solicitation in or from any jurisdiction where such an offer or solicitation is not authorised. Accordingly, notes may not be offered or sold, directly or indirectly, and neither this base prospectus nor any other prospectus, form of application, advertisement or other offering material in connection with the notes may be distributed in or from or published in any country or jurisdiction except under circumstances which will result in compliance with applicable laws and regulations of any such country or jurisdiction.

The dealers have represented and agreed, and each dealer appointed under the programme agreement will be required to represent and agree, that they have complied, and will comply, with all applicable laws and regulations in force in any jurisdiction in which they purchase, offer, sell or deliver the notes or possess them or distribute this base prospectus or any part thereof, and the issuing entity shall have no responsibility for such activities by the dealers. Furthermore, the dealers, and each dealer appointed under the programme agreement, will not directly or indirectly offer, sell or deliver any of the notes or distribute or publish this base prospectus or any prospectus, form of application, offering document, advertisement or other offering material in connection with the notes except under circumstances that will, to the best of their knowledge and belief, result in compliance with all applicable laws and regulations, and all offers, sales and deliveries of the notes by them will be made on the same terms.

Neither the issuing entity nor the dealers represent that the notes may at any time lawfully be sold in compliance with any application, registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, or assume any responsibility for facilitating such sale.

With regard to any issuance of notes, the relevant dealers will be required to comply with such other additional or modified restrictions (if any) as the issuing entity and the dealers shall agree.

The dealers have and each dealer appointed under the programme agreement will be required to, unless prohibited by applicable law, furnish to each person to whom they offer or sell notes, a copy of this base prospectus as then amended or supplemented or, unless delivery of this base prospectus is required by applicable law, inform each such person that a copy will be made available upon request. The dealers are not authorised to give any information or to make any representation not contained in this base prospectus in connection with the offer and sale of notes to which this base prospectus relates.

This base prospectus may be used by the dealers for offers and sales related to market making transactions in the notes. All or any one of the dealers may act as principal or agent in these transactions. Other than in the case of sales being made to Bank of Scotland and/or any other member of the HBOS Group, these sales will be made at prices relating to prevailing market prices at the time of sale. None of the dealers has any obligation to make a market in the notes, and any market making may be discontinued at any time without notice.

Bank of Scotland and/or any other member of the HBOS Group may purchase any of the notes from time to time as specified in the applicable final terms.

## Transfer restrictions and investor representations

### Offers and sales by the initial purchasers

The notes (including interests therein represented by a Rule 144A global note, a Rule 144A definitive note or a book-entry interest and interests therein represented by a Reg S global note or a Reg S definitive note or a book-entry interest) have not been and will not be registered under the Securities Act or any state securities laws, and may not be offered or sold in the United States or to, or for the account or benefit of US persons (as defined in Regulation S under the Securities Act (**US persons**)) except pursuant to an effective registration statement or in accordance with an applicable exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and any other applicable laws. Accordingly, the notes (and any interests therein) are being offered and sold: (1) in the United States only to a limited number of “qualified institutional buyers” within the meaning of Rule 144A under the Securities Act (**QIBs**) in transactions exempt from the registration requirements of the Securities Act and in accordance with any state securities laws; and (2) outside the United States to non-US persons in compliance with Regulation S under the Securities Act.

The global notes held by a nominee of the common depositary only may be transferred only to another common depositary for Euroclear and Clearstream, Luxembourg and the global notes held by Cede & Co., as nominee for DTC only, may be transferred only to another custodian for DTC or DTC’s nominee.

On or prior to the expiration of the distribution compliance period, no sale or transfer of interests in Reg S global notes to US persons shall be permitted unless such resale or transfer is made pursuant to Rule 144A as provided below.

### Investor representations and restrictions on resale

Each purchaser of the notes (which term for the purposes of this section is and will be deemed to include any interests in the notes, including book-entry interests) is and will be deemed to have represented and agreed as follows (terms used below that are defined in Rule 144A or Regulation S have the meanings given to them in Rule 144A or Regulation S):

1. either (A) it is a QIB, is aware that any sale to it may be being made in reliance on Rule 144A and is acquiring such notes for its own account or as a fiduciary or agent for other QIBs for investment purposes and not for distribution in violation of the Securities Act, and it is able to bear the economic risk of an investment in the notes and has such knowledge and experience in financial and business matters as to be capable of evaluating the merits and risks of purchasing the notes, or (B) it is outside the United States, is not a US person and is acquiring such notes for its own account or as a fiduciary or agent for other non-US persons in an offshore transaction (as defined in Regulation S, an **offshore transaction**) pursuant to an exemption from registration provided by Regulation S;
2. such notes are being offered only in a transaction that does not require registration under the Securities Act and, in the case of the Rule 144A notes, if such purchaser decides to resell or otherwise transfer such notes, then it agrees that it will resell or transfer such notes only (i) to the issuing entity, (ii) so long as such notes are eligible for resale pursuant to Rule 144A, to a person whom the seller reasonably believes is a QIB acquiring the notes for its own account or as a fiduciary or agent for others (which others must also be QIBs) to whom notice is given that the resale or other transfer is being made in reliance on Rule 144A, (iii) pursuant to an exemption from registration provided by Rule 144 under the Securities Act (if available), (iv) to a purchaser acquiring the notes in an offshore transaction pursuant to an exemption from registration in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act or (v) pursuant to an effective registration statement under the Securities Act, in each case in accordance with any applicable securities laws of any state or other jurisdiction of the United States; provided, that the agreement of such purchaser is subject to any requirement of law that the disposition of the purchaser’s property shall at all times be and remain within its control;
3. in the case of a purchase of Rule 144A notes unless and until the relevant legend set out below has been removed from the Rule 144A notes, such purchaser shall notify each transferee of Rule 144A notes (as applicable) from it that (i) such notes have not been registered under the Securities Act, (ii) the holder of such notes is subject to the restrictions on the resale or other transfer thereof described above, (iii) such transferee shall be deemed to have represented (a) as to its status as a QIB or a purchaser acquiring the notes in an offshore transaction (as the case may be), (b) if such transferee is a QIB, that such transferee is acquiring the notes for its own account or as a fiduciary or agent for others (which others also must be QIBs), (c) if such purchaser is acquiring the notes in an offshore transaction, that such transfer is made pursuant to an exemption from registration in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act, and (d) that such transferee is not an

underwriter within the meaning of Section 2(11) of the Securities Act, and (iv) such transferee shall be deemed to have agreed to notify its subsequent transferees as to the foregoing; and

4. with respect to purchasers of the Reg S notes, and unless otherwise stated in the Final Terms, no part of the assets to be used to purchase such notes to be purchased by it constitutes assets of any employee benefit plan or other plan (including an individual retirement account) subject to Title I of ERISA or Section 4975 of the Code;
5. with respect to purchasers of the Rule 144A notes, and unless otherwise stated in the Final Terms, either (A) no part of the assets to be used to purchase such notes to be purchased by it constitutes assets of any employee benefit plan or other plan (including an individual retirement account) subject to Title I of ERISA or Section 4975 of the Code or, in the case of a governmental, church or non-US plan, any federal, state or valid law that is similar to the prohibited transaction provisions of Title I of ERISA or Section 4975 of the Code (**similar law**) or (B) all or part of the assets to be used to purchase such notes to be purchased by it constitute assets of one or more employee benefit plans or other plans (including an individual retirement account) subject to Title I of ERISA, Section 4975 of the Code or any similar law and the use of such assets to purchase such notes will not constitute, cause or result in the occurrence of a non-exempt prohibited transaction under ERISA, Section 4975 of the Code or any similar law;
6. The notes sold in reliance on Regulation S will bear a legend substantially to the following effect:

“THIS NOTE HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933, AS AMENDED (THE **SECURITIES ACT**) OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES AND, AS A MATTER OF US LAW, PRIOR TO THE DATE THAT IS 40 DAYS AFTER THE LATER OF THE COMMENCEMENT OF THE OFFERING OF THE NOTES AND THE CLOSING OF THE OFFERING OF THE NOTES, MAY NOT BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED IN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, A US PERSON (AS DEFINED IN REGULATION S UNDER THE SECURITIES ACT) EXCEPT PURSUANT TO AN EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAWS OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES.”

7. The notes sold in reliance on Rule 144A will bear a legend substantially in the following effect:

“THIS NOTE HAS NOT BEEN REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933, AS AMENDED (THE **SECURITIES ACT**), OR ANY STATE SECURITIES LAWS, AND, AS A MATTER OF US LAW, MAY NOT BE OFFERED OR SOLD IN VIOLATION OF THE SECURITIES ACT OR SUCH STATE LAWS. THE HOLDER HEREOF, BY PURCHASING OR ACCEPTING THIS NOTE AGREES FOR THE BENEFIT OF THE ISSUER AND THE RELEVANT DEALERS AND/OR MANAGERS THAT IT WILL RESELL, PLEDGE OR OTHERWISE TRANSFER THIS NOTE, AS A MATTER OF US LAW, ONLY (A) (1) SO LONG AS THIS NOTE IS ELIGIBLE FOR RESALE PURSUANT TO RULE 144A UNDER THE SECURITIES ACT (**RULE 144A**), TO A PERSON WHOM THE SELLER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER, AS DEFINED IN RULE 144A (A **QUALIFIED INSTITUTIONAL BUYER**), THAT IS ACQUIRING THIS NOTE FOR ITS OWN ACCOUNT OR AS A FIDUCIARY OR AGENT FOR OTHERS (WHICH OTHERS MUST BE QUALIFIED INSTITUTIONAL BUYERS) TO WHOM NOTICE IS GIVEN THAT THE RESALE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A, (2) PURSUANT TO AN EXEMPTION FROM REGISTRATION IN ACCORDANCE WITH RULE 144 UNDER THE SECURITIES ACT (IF AVAILABLE), (3) TO A PERSON WHO IS NOT A US PERSON (AS DEFINED IN REGULATION S UNDER THE SECURITIES ACT), AND WHO IS NOT ACQUIRING THE NOTE FOR THE ACCOUNT OR BENEFIT OF A U.S. PERSON, OUTSIDE THE UNITED STATES IN ACCORDANCE WITH RULE 903 OR RULE 904 OF REGULATION S UNDER THE SECURITIES ACT OR (4) PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT, IN EACH CASE IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAWS OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES; AND (B) TO A PURCHASER WITH RESPECT TO WHOM (X) NO PART OF THE ASSETS USED TO PURCHASE THIS NOTE CONSTITUTES ASSETS OF ANY EMPLOYEE BENEFIT PLAN OR OTHER PLAN (INCLUDING AN INDIVIDUAL RETIREMENT ACCOUNT) SUBJECT TO TITLE I OF ERISA OR SECTION 4975 OF THE CODE OR, IN THE CASE OF A GOVERNMENTAL, CHURCH OR NON-US PLAN, ANY FEDERAL, STATE OR VALID LAW THAT IS SIMILAR TO THE

PROHIBITED TRANSACTION PROVISIONS OF TITLE I OF ERISA OR SECTION 4975 OF THE CODE (**SIMILAR LAW**), OR (Y) PART OR ALL OF THE ASSETS USED TO PURCHASE THIS NOTE CONSTITUTE ASSETS OF AN EMPLOYEE BENEFIT PLAN OR OTHER PLAN (INCLUDING AN INDIVIDUAL RETIREMENT ACCOUNT) SUBJECT TO TITLE I OF ERISA OR SECTION 4975 OF THE CODE IF AND ONLY IF THE USE OF SUCH ASSETS WILL NOT CONSTITUTE, CAUSE OR RESULT IN THE OCCURRENCE OF A NON-EXEMPT PROHIBITED TRANSACTION UNDER ERISA, SECTION 4975 OF THE CODE OR ANY SIMILAR LAW, PROVIDED THAT THE AGREEMENT OF THE HOLDER HEREOF IS SUBJECT TO ANY REQUIREMENT OF LAW THAT THE DISPOSITION OF THE PURCHASER'S PROPERTY SHALL AT ALL TIMES BE AND REMAIN WITHIN ITS CONTROL. THIS NOTE AND RELATED DOCUMENTATION MAY BE AMENDED OR SUPPLEMENTED FROM TIME TO TIME TO MODIFY THE RESTRICTIONS ON AND PROCEDURES UNDERTAKEN OR REPRESENTED BY THE HOLDER, FOR RESALES AND OTHER TRANSFERS OF THIS NOTE TO REFLECT ANY CHANGE IN APPLICABLE LAW OR REGULATION (OR THE INTERPRETATION THEREOF) OR IN PRACTICES RELATING TO RESALES OR OTHER TRANSFERS OR RESTRICTED SECURITIES GENERALLY. THE HOLDER OF THIS NOTE AND ANY BENEFICIAL OWNER OF ANY INTEREST THEREIN SHALL BE DEEMED, BY ITS ACCEPTANCE OR PURCHASE HEREOF, TO HAVE AGREED TO ANY SUCH AMENDMENT OR SUPPLEMENT (EACH OF WHICH SHALL BE CONCLUSIVE AND BINDING ON THE HOLDER HEREOF AND ALL FUTURE HOLDERS OF THIS NOTE AND ANY NOTES ISSUED IN EXCHANGE OR SUBSTITUTION HERE FOR, WHETHER OR NOT ANY NOTATION THEREOF IS MADE HEREON) AND AGREES TO TRANSFER THIS NOTE ONLY IN ACCORDANCE WITH ANY SUCH AMENDMENT OR SUPPLEMENT IN ACCORDANCE WITH APPLICABLE LAW IN EFFECT AT THE DATE OF SUCH TRANSFER." PROSPECTIVE PURCHASERS ARE HEREBY NOTIFIED THAT THE SELLER OF THIS SECURITY MAY BE RELYING ON THE EXEMPTION FROM THE PROVISIONS OF SECTION 5 OF THE SECURITIES ACT PROVIDED BY RULE 144A."

8. the notes will be represented by a global note and that transfers thereof or any interest therein are restricted herein;
9. with respect to any foreign purchaser claiming an exemption from United States income or withholding tax, such purchaser has delivered to the paying agent a true and complete IRS Form W-8BEN, W-8ECI or W-8IMY (or applicable successor forms) indicating such exemption;
10. the purchaser acknowledges that transfers of the offered notes or any interest therein will otherwise be subject in all respects to the restrictions applicable thereto contained in the note trust deed.

The issuing entity and others will rely upon the truth and accuracy of the foregoing acknowledgments, representations or agreements and agrees that if any of such acknowledgments, representations or agreements made by it are no longer accurate, it shall promptly notify the issuing entity; and if it is acquiring any note as a fiduciary or agent for one or more accounts it represents that it has sole investment discretion with respect to each such account and that it has full power to make the foregoing acknowledgments, representations and agreements on behalf of each account.

**Because of the foregoing restrictions, purchasers of notes are advised to consult legal counsel prior to making any offer, resale, pledge or transfer of such securities offered and sold.**



### **Reports to noteholders**

The cash manager and the issuing entity cash manager on behalf of Funding 1 and the issuing entity respectively have prepared and will prepare a report on the portfolio, the notes, the intercompany loan, the Funding 1 cash accumulation ledger, Funding 1 reserve funds, the Funding 1 principal deficiency ledger and the occurrence of any material events. The financial information contained in these reports will not be prepared in accordance with generally accepted accounting principles of any jurisdiction. These monthly and annual reports are and will be sent by the cash manager and the issuing entity cash manager on behalf of Funding 1 and the issuing entity, respectively, to Deutsche Bank Trust Company Americas, in its capacity as US paying agent and Deutsche Bank AG, London Branch, in its capacity as principal paying agent, to be made available to noteholders upon request (subject to such noteholders providing satisfactory evidence of their holding). No reports will be sent to noteholders by the cash manager or the issuing entity cash manager.

Pursuant to the servicing agreement, the servicer provides to beneficial owners of the notes on a monthly basis a report containing information about the loans in the mortgages trust if they have furnished the servicer with the beneficial ownership certification described in the servicing agreement.

### Certain relationships

There are no business relationships, agreements, arrangements, transactions or understandings that are entered into outside the ordinary course of business or are on terms other than would be obtained in an arm's length transaction with an unrelated third party, apart from the issuance of the notes, between Funding 1 or the issuing entity on the one hand and the servicer, the note trustee, the Funding 1 security trustee, the issuing entity security trustee, the mortgages trustee, the seller, the Funding 1 swap provider, any issuing entity swap provider or any affiliates of such parties, that currently exist or that existed during the past two years and that would be material to the notes.

Pursuant to the transaction documents, there are numerous relationships involving or relating to the notes or the portfolio between Bank of Scotland (which is the seller, the servicer, the cash manager, the issuing entity cash manager, the Funding 1 swap provider, the issuing entity subordinated loan provider and the issuing entity start-up loan provider), Funding 1 or the issuing entity on the one hand and the servicer (see "**The servicing agreement**" above), the note trustee, the Funding 1 security trustee and the issuing entity security trustee (see "**Description of the note trust deed**", "**Security for Funding 1's obligations – Appointment, powers, responsibilities and liabilities of the Funding 1 security trustee**" and "**Security for the issuing entity's obligations – Appointment, powers, responsibilities and liabilities of the issuing entity security trustee**" above), the mortgages trustee (see "**The mortgages trust deed**" above), the seller (see "**Sale of the loans and their related security**" above), the Funding 1 swap provider (see "**The swap agreements – The Funding 1 swap**" above), each issuing entity swap provider (see "**The swap agreements – The issuing entity swaps**" above), or any affiliates of such parties (Bank of Scotland, is the account bank and the issuing entity account bank: see "**The intercompany loan agreement – Funding 1's bank accounts**" above and "**Cash management for issuing entity – The issuing entity's bank accounts**" above), that currently exists or that existed during the past two years and that would be material to the notes. The material terms of these relationships are disclosed in the sections referred to above. See "**Fees**" above for a summary of fee amounts relating to certain of the foregoing relationships.

## **Listing and general information**

### **Authorisation**

The initial issuance of notes under the programme has been authorised by resolution of the board of directors of the issuing entity passed on 3 April 2007.

### **Listing of notes**

Application has been made to the FSA in its capacity as competent authority under the FSMA (the **UK Listing Authority**) for the notes issued during the period of 12 months from the date of this prospectus (other than any notes which are unlisted or listed on any other exchange) to be admitted to the official list (the **Official List**) maintained by the UK Listing Authority. Application will also be made to the London Stock Exchange for such notes to be admitted to trading on the London Stock Exchange's Regulated Market. Admission to the Official List together with admission to the London Stock Exchange's Regulated Market (being a regulated market for the purposes of the Markets in Financial Instruments Directive) constitute official listing on the London Stock Exchange.

It is expected that each series and class of notes which is to be admitted to the Official List and to trading on the London Stock Exchange's Regulated Market will be admitted separately, as and when issued, subject only to the issue of a global note or notes initially representing the notes of each series and class and to making the final terms relating to the series and class of notes available to the public in accordance with the EU Directive 2003/71/EC (the Prospectus Directive) and associated UK and EU implementing legislation. Prior to listing, however, dealings will be permitted by the London Stock Exchange in accordance with its rules.

This prospectus has been prepared in compliance with the prospectus rules made under Part VI of the FSMA.

The issuing entity accepts responsibility for the information contained in this prospectus. To the best of the knowledge of the issuing entity (who has taken all reasonable care to ensure that such is the case) the information contained in this prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information. The issuing entity accepts responsibility accordingly.

### **Clearing and settlement**

It is expected that the notes will be accepted for clearance through DTC and/or Clearstream, Luxembourg and Euroclear as specified in the applicable final terms. The appropriate ISINS and, as applicable, CUSIP numbers and common codes for each series and class of notes will be specified in the applicable final terms.

### **Litigation**

Currently, none of the issuing entity, Funding 1, the post-enforcement call option holder, Holdings or the mortgages trustee is or has been involved since 21 February 2007 (in the case of the issuing entity, Funding 1, the post-enforcement call option holder, Holdings (being the date of its incorporation)) or 12 February 2007 (in the case of the mortgages trustee (being the date of its incorporation)) in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which the issuing entity, Funding 1, the post-enforcement call option holder, Holdings or the mortgages trustee, as applicable, is aware) which may have, or have had in the recent past, a significant effect on the financial position or profitability of the issuing entity, Funding 1, the post-enforcement call option holder, Holdings or the mortgages trustee.

There are currently no legal or arbitration proceedings pending (or known by Bank of Scotland to be contemplated by governmental authorities) against Bank of Scotland or in which any property of Bank of Scotland is the subject, that is material to holders of the notes.

### **Accounts**

No statutory or non-statutory accounts within the meaning of the Companies Act 1985 in respect of any financial year of the issuing entity have been prepared. So long as the notes are listed on the Official List of the UK Listing Authority and are trading on the London Stock Exchange's Regulated Market, the most recently published audited annual accounts of the issuing entity from time to time shall be available at the specified office of the principal paying agent in London. The issuing entity does not publish interim accounts.

Since the date of its incorporation, the issuing entity has not entered into any contracts or arrangements not being in the ordinary course of business.

### **Significant or material change**

Since 21 February 2007 (the date of incorporation of the post-enforcement call option holder and Holdings) and 12 February 2007 (the date of incorporation of the mortgages trustee), there has been (1) no material adverse change in the financial position or prospects of the post-enforcement call option holder, Holdings or the mortgages trustee and (2) no significant change in the financial or trading position of the post-enforcement call option holder, Holdings or the mortgages trustee.

Since 31 December 2007 (the end of the last financial period of the issuing entity and Funding 1), there has been (1) no material adverse change in the financial position or prospects of the issuing entity or Funding 1 and (2) no significant change in the financial or trading position of the issuing entity or Funding 1.

### **Documents available**

From the date of this base prospectus and for so long as any series and class of notes issued by the issuing entity is listed on the London Stock Exchange's Regulated Market, copies of the following documents may, when published, be inspected at the registered office of the issuing entity and from the specified office of the principal paying agent during usual business hours, on any weekday (public holidays excepted):

- (A) the memorandum and articles of association of each of the issuing entity, Funding 1, Holdings, mortgages trustee and the post-enforcement call option holder;
- (B) a copy of this base prospectus and the accompanying final terms;
- (C) any future offering circulars, prospectuses, final terms, information memoranda and supplements including final terms (as applicable) (save that a final terms relating to an unlisted series and class of notes will be available for inspection only by the dealers and/or managers, as specified in the final terms or, upon proof satisfactory to the principal paying agent or the registrar, as the case may be, as to the identity of the holder of any note to which the final terms relates) to the prospectus and any other documents incorporated therein or therein by reference;
- (D) each of the following documents:
  - the bank account agreement;
  - the cash management agreement;
  - the corporate services agreement;
  - each deed of accession to the Funding 1 deed of charge;
  - each deed of accession to the issuing entity deed of charge;
  - the Funding 1 deed of charge;
  - the Funding 1 guaranteed investment contract;
  - the Funding 1 swap agreement;
  - the issuing entity bank account agreement;
  - the issuing entity cash management agreement;
  - the issuing entity deed of charge;
  - the issuing entity master definitions and constructions schedule;

- each issuing entity start-up loan agreement;
- each issuing entity subordinated loan agreement;
- each issuing entity swap agreement;
- the intercompany loan agreement;
- the master definitions and construction schedule;
- the mortgage sale agreement;
- the mortgages trust deed;
- the mortgages trustee corporate services agreement;
- the mortgages trustee guaranteed investment contract;
- the note trust deed;
- the paying agent and agent bank agreement;
- the programme agreement;
- each Scottish declaration of trust;
- the servicing agreement;
- each subscription agreement; and
- any other deeds of accession or supplemental deeds relating to any such documents.

The issuing entity confirms that the assets backing the issue of notes, taken together with the other arrangements entered into by the issuing entity on the programme date and entered or to be entered in to by the issuing entity on each relevant closing date (including those described in “**Credit Structure**” above), have characteristics that demonstrate capacity to produce funds to service any payments due and payable on the notes. However, investors are advised that this confirmation is based on the information available to the issuing entity on the date of this prospectus and may be affected by the future performance of such assets backing the issue of the notes. Consequently, investors are advised to review carefully any disclosure in this prospectus and the accompanying final terms together with any amendments and supplements thereto.

## Glossary

Principal terms used in this base prospectus are defined as follows:

\$, US\$, US dollars and dollars	the lawful currency of the United States of America
€, euro and Euro	the single currency introduced at the third stage of European Economic and Monetary Union pursuant to the Treaty establishing the European Communities, as amended from time to time
£, pounds and sterling	the lawful currency for the time being of the United Kingdom of Great Britain and Northern Ireland
1999 Regulations	the Unfair Terms in Consumer Contracts Regulations 1999, as amended
A loan tranches	the loan tranches made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of issue of any series of class M notes
A principal deficiency sub-ledger	a sub-ledger on the Funding 1 principal deficiency ledger which specifically records any principal deficiency in respect of any A loan tranches
AA loan tranches	the loan tranches made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of issue of any series of class B notes
AA principal deficiency sub-ledger	a sub-ledger on the Funding 1 principal deficiency ledger which specifically records any principal deficiency in respect of any AA loan tranches
AAA loan tranches	the loan tranches made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of issue of any series of class A notes
AAA principal deficiency sub-ledger	a sub-ledger on the Funding 1 principal deficiency ledger which specifically records any principal deficiency in respect of any AAA loan tranches
account bank	Bank of Scotland
accrual yield	in respect of any series and class of notes, the yield specified as such for such notes in the applicable final terms
accrued interest	in respect of loans on a given date, the interest which has accrued from the last payment date up to that date, but which is not currently payable
additional business centre	has the meaning given to that term in the applicable final terms
additional interest	has the meaning given to that term in Condition 4.4
adjusted Funding 1 general reserve fund level	the sum of:  (a) the amount standing to the credit of the Funding 1 general reserve fund; and  (b) the amount (if any) then to be credited in accordance with item (A) of the relevant Funding 1 pre-enforcement principal priority of payments
advance date	in relation to an issuing entity subordinated loan, means the date on which such issuing entity subordinated loan is advanced by the issuing entity subordinated loan provider as, as the case may be, a new issuing entity subordinated loan provider
agent bank	Deutsche Bank AG, London Branch
agents	means the paying agents, the transfer agent, the registrar, the exchange

	agent and the agent bank
alternative clearing system	in relation to an issuance of notes, has the meaning given to that term in the applicable final terms
annualised CPR	the result of the calculation $1 - ((1 - M)^{12})$  where M is expressed as a percentage and determined as at the most recent normal calculation date as indicated in the definition of “anticipated cash accumulation period” (see “ <b>The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1</b> ” above)
anticipated cash accumulation period	on any normal calculation date, the anticipated number of months required by Funding 1 to accumulate sufficient principal receipts to pay the relevant accumulation amount in relation to the relevant cash accumulation loan tranche, as described further in “ <b>The mortgages trust – Cash management of trust property – distribution of principal receipts to Funding 1</b> ” above
applicable final terms	in relation to a series and class of notes, the final terms (or the relevant provisions thereof) attached to or endorsed on such notes
arranger	Bank of Scotland Treasury
arrear of interest	in respect of a given date, interest and expenses which are due and payable and remain unpaid on that date
asset trigger event	an asset trigger event will occur when losses on the loans in the portfolio (after application of Funding 1 available principal receipts to meet deficiencies in Funding 1 revenue receipts or to fund the Funding 1 liquidity reserve fund) reach a level causing an amount is debited to the principal deficiency sub-ledger to the AAA principal deficiency sub-ledger of Funding 1, unless such debit is made when (a) the aggregate principal amount outstanding of each of the AA loan tranches, the A loan tranches, the BBB loan tranches, the BB loan tranches is equal to zero; and (b) the sum of the amount standing to the credit of the Funding 1 general reserve ledger and the Funding 1 revenue ledger together with amounts determined and due to be credited to the Funding 1 revenue ledger prior to the immediately following Funding 1 interest payment date after such debit is made, is greater than the amount necessary to pay the items in paragraphs (A) to (F) of the Funding 1 pre-enforcement revenue priority of payments on the immediately following Funding 1 interest payment date after such debit is made.
authorised investments means:	(a) sterling gilt-edged securities; and  (b) sterling demand or time deposits, certificates of deposit and short-term debt obligations (including commercial paper) provided that in all cases such investments have a maturity date of 90 days or less and mature on or before the next following quarterly interest payment date and the short-term unsecured, unguaranteed and unsubordinated debt obligations of the issuing or guaranteeing entity or the entity with which the demand or time deposits are made (being an authorised person under the FSMA) are rated at least equal to F1+ by Fitch, P-1 by Moody’s and A-1+ by Standard & Poor’s and such entity's long-term unsecured, unguaranteed and unsubordinated debt obligations are rated AA- by Fitch (if such obligations have a long-term rating) or which are otherwise acceptable to the rating agencies to maintain the then current ratings of the notes
AVM	automated valuation model
bank account agreement	the agreement entered into on the programme date between (among others) the account bank, the mortgages trustee and Funding 1 (as the same may be amended, restated, novated, replaced or supplemented from time to time), which governs (among other things) the operation of the mortgages trustee GIC account, the Funding 1 GIC account and the Funding 1

	transaction account
Bank of Scotland	Bank of Scotland plc, incorporated in Scotland, which was, prior to its registration under the Companies Act 1985 on the reorganisation date in accordance with the HBOS Group Reorganisation Act 2006, The Governor and Company of the Bank of Scotland
basic terms modification	has the meaning given to that term in Condition 11.1
BB loan tranches	the loan tranches made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of issue of any series of class D notes
BBB principal deficiency sub-ledger	a sub-ledger on the Funding 1 principal deficiency ledger which specifically records any principal deficiency in respect of any BBB loan tranches
BBB loan tranches	the loan tranches made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of issue of any series of class C notes
BBB principal deficiency sub-ledger	a sub-ledger on the Funding 1 principal deficiency ledger which specifically records any principal deficiency in respect of any BBB loan tranches
beneficiaries	Funding 1 and the seller as beneficiaries of the mortgages trust
Benefit Plan Investors	has the meaning given to that term on page 274
BERR	the Department for Business, Enterprise and Regulatory Reform (formerly the Department of Trade and Industry)
Birmingham Midshires	a brand under which Bank of Scotland (previously Halifax) originates residential mortgage loans
book-entry interests	has the meaning given to that term on page iii
booking fee	a fee payable by the borrower in respect of applications for certain types of loans
borrower	in relation to a loan, the individual or individuals specified as such in the relevant mortgage together with the individual or individuals (if any) from time to time assuming an obligation to repay such loan or any part of it
Bank of Scotland Treasury	Bank of Scotland plc, Treasury Division (formerly known as HBOS Treasury Services plc)
broken amount	in respect of any series and class of notes, the amount specified as such (if any) for such notes in the applicable final terms
bullet accumulation liability	means on any Funding 1 interest payment date prior to any payment under item (C) of the priority of payments described in “ <b>Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes</b> ” above the aggregate of the relevant accumulation amounts at that time of all bullet loan tranches which are within a cash accumulation period
bullet accumulation shortfall	means at any time the amount by which the cash accumulation ledger amount is less than the bullet accumulation liability
bullet loan tranche	any rated loan tranche which is scheduled to be repaid in full in one instalment on one Funding 1 interest payment date, namely those loan tranches designated as a ‘bullet loan tranches’ in the applicable loan tranche supplement and final terms.  The bullet loan tranches are and will be deemed to be pass through loan



	tranches on the earlier to occur of a pass through trigger event and the step up date (if any) in relation to such loan tranche
bullet redemption date	the date for redemption of any series and class of bullet redemption notes, which will be the interest payment date specified as such for such series and class of notes in the applicable final terms, subject to the terms and conditions of the notes
bullet redemption notes	any series and class of notes which is scheduled to be repaid in full on one bullet redemption date. Bullet redemption notes will be deemed to be pass-through notes in certain circumstances
bullet repayment date	the Funding 1 interest payment date specified for repayment of any loan tranche supplement, which will be specified as such for such loan tranche in the applicable loan tranche supplement and final terms
business day	a day that is a London business day, a New York business day and a TARGET business day and (in the case of the notes) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in any additional business centre specified in the applicable final terms and in the principal financial centre of the country of the relevant specified currency
calculation date	the date on which the mortgages trust is terminated and first day of each month or, if not a London business day, the next succeeding London business day or any other day on which Funding 1 or the seller acquires a further interest in the trust property (otherwise than due to capitalised interest) and/or the mortgages trustee acquires new loans from the seller
calculation period	the period from (and including) one calculation date, to (but excluding) the next calculation date and in respect of the first calculation date following the programme date, the period from (and including) the programme date to (but excluding) the first calculation date following the programme date
calculation period swap provider amount	has the meaning given to that term on page 166
calendar year	a year from the beginning of 1 January to the end of the next following 31 December
called notes	has the meaning given to that term in Condition 5.6
call option date	in respect of any series and class of notes, the date specified as such in the applicable final terms (if any), being the interest payment date on which the issuing entity is entitled to redeem such notes pursuant to Condition 5.4(a)
capitalised	means, in respect of a fee or other amount, added to the principal balance of a loan
capitalised arrears	in relation to a loan at any date (being, the determination date), the amount (if any) at such date of any arrears of interest which have been capitalised and added, in the accounts of the mortgages trustee, to the principal amount outstanding in respect of such loan
capitalised expenses	the amount of any expense, charge, fee, premium or payment (excluding, however, any arrears of interest) capitalised and added to the principal amount outstanding in respect of a loan in accordance with the relevant mortgage terms (including, for the avoidance of doubt, any high loan-to-value fee)
capitalised interest	if a borrower takes a payment holiday or makes an underpayment (in either case as permitted under the terms of the loan), then the outstanding principal balance of the loan will increase by the amount of interest that would have been paid on the relevant loan if not for such payment holiday

	or underpayment
capped rate loan	a loan which allows the borrower to pay interest by reference to the standard variable rate or another variable rate, which is subject to a maximum level for a fixed period of time
cash accumulation ledger amount	means at any time the amount standing to the credit of the Funding 1 cash accumulation ledger at that time immediately prior to any drawing to be applied on that Funding 1 interest payment date and prior to any payment under item (H) of the priority of payments described in “ <b>Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes</b> ” above
cash accumulation liability	means on any Funding 1 interest payment date prior to any payment under item (C) of the priority of payments described in “ <b>Cashflows – Distribution of Funding 1 available principal receipts – Repayment of loan tranches before a trigger event and before intercompany loan acceleration or acceleration of all notes</b> ” above, the sum of: <p>(a) the bullet accumulation liability at that time; and</p> <p>(b) the aggregate of each relevant accumulation amount at that time of all of the scheduled amortisation instalments which are within a cash accumulation period</p>
cash accumulation loan tranche	a bullet loan tranche or scheduled amortisation instalment which is within a cash accumulation period
cash accumulation period	the period beginning on the earlier of: <p>(a) the commencement of the anticipated cash accumulation period relating to the relevant accumulation amount; and</p> <p>(b) unless otherwise specified in the applicable final terms, in respect of an original bullet loan tranche, six months prior to the scheduled repayment date of that original bullet loan tranche and, in respect of an original scheduled amortisation instalment, three months prior to the scheduled repayment date of that original scheduled amortisation instalment, and ending when Funding 1 has fully repaid that original bullet loan tranche or original scheduled amortisation instalment, as applicable</p>
cash accumulation requirement	has the meaning given to that term on page 109
cash accumulation shortfall	means, at any time, the amount that the cash accumulation ledger amount is less than the cash accumulation liability
cash management agreement	the cash management agreement entered into on the programme date between the cash manager, the mortgages trustee, Funding 1 and the Funding 1 security trustee (as the same may be amended, restated, novated, replaced or supplemented from time to time), as described further in “ <b>Cash management for the mortgages trustee and Funding 1</b> ” above
cash manager	Bank of Scotland (as successor to Halifax acting, pursuant to the HBOS Group Reorganisation Act 2006), pursuant to the cash management agreement, as agent for the mortgages trustee, Funding 1 and the Funding 1 security trustee, among others, to manage all cash transactions and maintain certain ledgers on behalf of the mortgages trustee, Funding 1 and the Funding 1 security trustee (among others)
CCA	the Consumer Credit Act 1974, as amended
CCA 2006	the Consumer Credit Act 2006, as may be amended
CFC	has the meaning given to that term on page 269

class	each single class (or sub-class) of the class A notes, the class B notes, the class M notes, the class C notes and the class D notes or their respective holders thereof as the context requires and except where otherwise specified
class A noteholders	the holders of the class A notes
class A notes	the notes of a series designated as such (or a sub-class of such) in the applicable final terms
class A rule 144A notes	each series and class of class A notes which are sold in the United States to QIBs in reliance on Rule 144A
class B noteholders	the holders of the class B notes
class B notes	the notes of a series designated as such (or a sub-class of such) in the applicable final terms
class B rule 144A notes	each series and class of class B notes which are sold in the United States to QIBs in reliance on Rule 144A
class C noteholders	the holders of the class C notes
class C notes	the notes of a series designated as such (or a sub-class of such) in the applicable final terms
class C rule 144A notes	each series and class of class C notes which are sold in the United States to QIBs in reliance on Rule 144A
class D noteholders	the holders of the class D notes
class D notes	the notes of a series designated as such (or a sub-class of such) in the applicable final terms
class M noteholders	the holders of the class M notes
class M notes	the notes of a series designated as such (or a sub-class of such) in the applicable final terms
class M rule 144A notes	each series and class of class M notes which are sold in the United States to QIBs in reliance on Rule 144A
clearing agency	an agency registered under the provisions of section 17A of the United States Securities Exchange Act of 1934, as amended
clearing corporation	a corporation within the meaning of the New York Uniform Commercial Code
Clearstream, Luxembourg	Clearstream Banking, société anonyme
closing date	in respect of the first issuance of notes under the programme, the programme date and, in respect of every other issuance of notes under the programme (which may comprise one or more series and one or more classes of notes), the date on which such issuance of notes is issued, as indicated in the applicable final terms
CML	the Council of Mortgage Lenders and any successor organisation thereto
CML Code	the Mortgage Code issued by the CML
Code	United States Internal Revenue Code of 1986, as amended
collection account	any collection account in the name of the servicer which is from time to time used for the purpose of collecting, directly or indirectly, monies due in respect of the loans and/or the related security forming part of the trust property

common depositary	has the meaning given to that term on page iii
conditional purchase agreement	has the meaning given to that term on page 13
conditional purchaser	in respect of any series and class of remarketable notes, the conditional purchaser specified in the applicable final terms
conditional purchaser confirmation	in respect of any series and class of remarketable notes, the confirmation given by the remarketing agent or the tender agent to the issuing entity and the principal paying agent that the conditional purchaser has purchased an interest in or has had transferred to it or on its behalf an interest in all such remarketable notes
conditions	the terms and conditions of the notes, and “condition” shall be construed accordingly
Consumer Credit Directive	has the meaning given to that term on page 54
controlling beneficiary deed	the controlling beneficiary deed entered into on the programme date between (amongst others) Funding 1, the Funding 1 security trustee and the seller (as the same may be amended, restated, novated, replaced or supplemented from time to time)
core terms	the terms which define the main subject matter of the contract
corporate services agreement	an agreement entered into on the programme date between (among others) Holdings, the issuing entity, Funding 1, Halifax (to which Bank of Scotland has succeeded), the corporate services provider, the UK share trustee and the Funding 1 security trustee (as the same may be amended, restated, novated, replaced or supplemented from time to time), which governs the provision of corporate services by the corporate services provider to the issuing entity, Funding 1, PECO and Holdings
corporate services provider	in respect of the issuing entity, Funding 1, Holdings and PECO, means Structured Finance Management Limited or such other person or persons for the time being acting as corporate services provider to the issuing entity, Funding 1, Holdings and PECO under the corporate services agreement
crystallise	when a floating charge becomes a fixed charge
current seller share	the amount of trust property beneficially owned by the seller from time to time, calculated in accordance with the mortgages trust deed
cut-off date	has the meaning given to that term in the applicable final terms
dealers	Any dealer or dealers appointed from time to time in accordance with the programme agreement.
deferred interest	has the meaning given to that term in Condition 4.4
definitive notes	notes in definitive registered form
designated account	has the meaning given to that term in Condition 19
designated bank	has the meaning given to that term in Condition 19
designated loan tranche ratings	has the meaning given to that term on page 116
detached	a house not joined to another house
determination date	in respect of a series and class of notes, the date(s) specified as such in the applicable final terms
determination period	has the meaning given to that term in Condition 4.1
diligence	the process (under Scots law) by which a creditor attaches the property of a

	debtor to implement or secure a court decree or judgment
discount loan	loans which allow the borrower to pay interest at a specified discount to the standard variable rate
distribution compliance period	has the meaning given to that term on page 180
distribution date	the date which is two London business days after each calculation date, being the date that the mortgages trustee will distribute mortgages trust available principal receipts and mortgages trust available revenue receipts to Funding 1 and the seller
DTC	The Depository Trust Company
early repayment charge or early repayment fee	any fee which a borrower is required to pay in the event that he or she is in default or his or her loan becomes repayable for any other mandatory reason or he or she repays all or any part of the relevant loan before a specified date
eligible securities	has the meaning given to that term in Rule 2a-7 under the Investment Company Act
employee benefit plans	has the meaning given to that term on page 273
English loan	a loan secured by an English mortgage
English mortgage	a mortgage secured over a property in England or Wales
English mortgage conditions	the mortgage conditions applicable to English loans
Enterprise Act	the Enterprise Act 2002
ERISA	the US Employee Retirement Income Security Act of 1974, as amended
ERISA plans	has the meaning given to that term on page 273
EU Savings Directive	EC Council Directive 2003/48/EC
EURIBOR	the Euro-Zone Interbank offered rate and, in the case of the Rule 144A notes, the Euro-Zone Interbank offered rate as determined by the agent bank in accordance with the paying agent and agent bank agreement
Euroclear	Euroclear Bank S.A./N.V.
excess swap collateral	an amount equal to the value of the collateral (or the applicable part of any collateral) provided by an issuing entity swap provider to the issuing entity in respect of that issuing entity swap provider's obligations to transfer collateral to the issuing entity under the relevant issuing entity swap agreement which is in excess of that issuing entity swap provider's liability under the relevant issuing entity swap agreement as at the date of termination of the relevant issuing entity swap agreement or which it is otherwise entitled to have returned to it under the terms of the relevant issuing entity swap agreement
Exchange Act	The United States Exchange Act of 1934, as amended
exchange agent	Deutsche Bank Trust Company Americas
extraordinary resolution	a resolution passed at a meeting of the noteholders of a particular class and series or a class of notes of one or more series duly convened and held in accordance with the provisions of the note trust deed by a majority consisting of not less than three-fourths of the persons voting thereat upon a show of hands or, if a poll is duly demanded, by a majority consisting of not less than three-fourths of the votes cast on such poll
final maturity date	in respect of a series and class of notes, means the interest payment date falling in the month indicated for such series and class of notes in the

	applicable final terms
final repayment date	in relation to a loan tranche, the date specified as such in the related loan tranche supplement and (if applicable) final terms
final terms	in relation to any issuance of notes, the final terms issued in relation to all series and classes of notes comprising such issuance giving details of, <i>inter alia</i> , the amount and price of such series and class of notes
Fitch	Fitch Ratings Ltd. and any successor to its ratings business
fixed coupon amount	in respect of any series and class of notes, the amount specified as such (if any) for such notes in the applicable final terms
fixed rate loan	has the meaning given to that term on page 76
fixed rate note	a note, the interest basis of which is specified in the applicable final terms as being fixed rate
fixed security	a form of security which means that the chargor is not allowed to deal with the assets subject to the charge without the consent of the chargee
flexible loan	a type of loan product that typically incorporates features that give the borrower options to, among other things, make further drawings on the loan account and/or to overpay or underpay interest and principal in a given month
floating charge	a form of charge which is not attached to specific assets but which “floats” over a class of them and which allows the chargor to deal with those assets in the every day course of its business, up until the point that the floating security is enforced, at which point it crystallises into a fixed security
floating rate note	a note, the interest basis of which is specified in the applicable final terms as being floating rate
Framework	the regulatory capital framework described in the Basel Committee on Banking Supervision’s publication, International Convergence of Capital Measurement and Capital Standards: a Revised Framework (Comprehensive Version)
FSA	the Financial Services Authority
FSMA	the Financial Services and Markets Act 2000, as amended
Funding 1	Pendeford Funding (No. 1) Limited
Funding 1 available principal receipts	has the meaning given to that term on page 143
Funding 1 available revenue receipts	has the meaning given to that term on page 135
Funding 1 cash accumulation ledger	a ledger maintained by the cash manager to record the amount accumulated by Funding 1 from time to time to pay the relevant accumulation amounts
Funding 1 deed of charge	the deed of charge entered into on the programme date between Funding 1, the Funding 1 security trustee and the Funding 1 secured creditors (as the same may be amended, supplemented, novated, replaced or supplemented from time to time), including any deeds of accession or supplements thereto in connection with an issuance of notes and/or the advance of a subordinated loan
Funding 1 general reserve fund	at any time the amount standing to the credit of the Funding 1 general reserve ledger at that time, which may be used in certain circumstances by Funding 1 to meet any deficit in revenue (provided that it shall not be available to make payments with respect to subordinated loan tranches) or

	to repay certain amounts of principal in respect of the rated loan tranches, as described further in “ <b>Credit structure – Funding 1 general reserve fund</b> ” above
Funding 1 general reserve fund	the lesser of:  threshold  (a) the Funding 1 reserve required amount; and  (b) if agreed with the rating agencies on the most recent closing date, the highest amount which the adjusted Funding 1 general reserve fund level has been at since the most recent closing date
Funding 1 general reserve ledger	a ledger maintained by the cash manager to record the amount credited to the Funding 1 general reserve fund from the proceeds of a portion of each start-up loan tranche and other withdrawals and deposits in respect of the Funding 1 general reserve fund
Funding 1 GIC account	the account in the name of Funding 1 maintained with the Funding 1 GIC provider pursuant to the terms of the bank account agreement and the Funding 1 guaranteed investment contract or such additional or replacement account as may for the time being be in place
Funding 1 GIC provider	Bank of Scotland
Funding 1 guaranteed investment contract	the guaranteed investment contract entered into on the programme date between Funding 1 and the Funding 1 GIC provider under which the Funding 1 GIC provider agrees to pay Funding 1 a guaranteed rate of interest on the balance of the Funding 1 GIC account, as described further in “ <b>Credit structure – Mortgages trustee GIC account/Funding 1 GIC account</b> ” above
Funding 1 interest payment date	in respect of a loan tranche, the quarterly date specified in the loan tranche supplement and (if applicable) final terms for payment of interest and/or principal subject to the appropriate Business Day Convention, if any, specified in relation to a loan tranche in the applicable loan tranche supplement
Funding 1 issuing entities	(as the context may require) Pendeford Master Issuer plc and/or any other issuing entities issuing new notes and entering into new intercompany loan agreements with Funding 1 from time to time
Funding 1 issuing entity security trustees	the issuing entity security trustee and/or any other security trustee in respect of the security granted by a Funding 1 issuing entity other than the issuing entity
Funding 1 liquidity reserve fund	a liquidity reserve fund established on the occurrence of certain ratings downgrades of the seller to meet interest and principal shortfalls (in limited circumstances) on the rated loan tranches
Funding 1 liquidity reserve fund required amount	on any Funding 1 interest payment date, an amount equal to the excess (if any) of 3 per cent. of the aggregate outstanding balance of the notes on that Funding 1 interest payment date (taking into account any principal repayments to be made by the issuing entity on that date) over the aggregate of amounts standing to the credit of the Funding 1 general reserve fund on that Funding 1 interest payment date (taking into account any amount credited to the Funding 1 general reserve ledger on that date)
Funding 1 liquidity reserve ledger	a ledger maintained by the cash manager to record the withdrawals and deposits in respect of the Funding 1 liquidity reserve fund
Funding 1 notes	the notes issued by any Funding 1 issuing entities, and includes (where the context requires) the notes of the issuing entity
Funding 1 post-enforcement	the order in which, following service of an intercompany loan acceleration

priority of payments	notice, the Funding 1 security trustee will apply the amounts received following service of an intercompany loan acceleration notice, as set out in <b>“Cashflows – Distribution of Funding 1 principal receipts and Funding 1 revenue receipts following intercompany loan acceleration”</b> above
Funding 1 pre-enforcement principal priority of payments	the order in which, prior to service of an intercompany loan acceleration notice, the cash manager will apply the Funding 1 available principal receipts as set out in <b>“Cashflows – Distribution of Funding 1 available principal receipts”</b> above
Funding 1 pre-enforcement revenue priority of payments	the order in which, prior to service of an intercompany loan acceleration notice, the cash manager will apply the Funding 1 available revenue receipts as set out in <b>“Cashflows – Distribution of Funding 1 available revenue receipts before intercompany loan acceleration”</b> above
Funding 1 principal deficiency ledger	the ledger of such name established and maintained by the cash manager, comprising on the programme date six sub-ledgers, the AAA principal deficiency sub-ledger, the AA principal deficiency sub-ledger, the A principal deficiency sub-ledger, the BBB principal deficiency sub-ledger, the BB principal deficiency sub-ledger and the subordinated loan principal deficiency sub-ledger and which records any deficiency of principal (following a loss on a loan allocated to Funding 1 or the application of Funding available principal receipts to meet any deficiency in Funding 1 available revenue receipts or to fund the Funding 1 liquidity reserve fund up to the Funding 1 liquidity reserve fund required amount) in respect of payments due under the intercompany loan agreement
Funding 1 principal ledger	a ledger maintained by the cash manager to record the amount of principal receipts received by Funding 1 from the mortgages trustee on each distribution date
Funding 1 principal receipts	the principal receipts paid by the mortgages trustee to Funding 1 on each distribution date
Funding 1 priority of payments	as the context requires, any of the Funding 1 pre-enforcement revenue priority of payments, the Funding 1 pre-enforcement principal priority of payments or the Funding 1 post-enforcement priority of payments
Funding 1 reserve funds	the Funding 1 general reserve fund and the Funding 1 liquidity reserve fund
Funding 1 reserve principal payment	<p>(a) prior to the occurrence of a trigger event:</p> <p>(i) repayments of principal which are then due and payable in respect of the original bullet loan tranches; and</p> <p>(ii) repayments of principal in respect of original scheduled amortisation loan tranches on their respective final repayment dates only; and</p> <p>(b) on or after the occurrence of a trigger event, repayments of principal in respect of original bullet loan tranches and original scheduled amortisation loan tranches on their respective final repayment dates only,</p> <p>in each case prior to the service of an intercompany loan acceleration notice on Funding 1</p>
Funding 1 reserve required amount	as at any date, the amount specified in the most recent final terms
Funding 1 revenue ledger	a ledger maintained by the cash manager to record all amounts received by Funding 1 from the mortgages trustee on each distribution date other than principal receipts, together with interest received by Funding 1 on its authorised investments or pursuant to the bank account agreement



Funding 1 secured creditors	the Funding 1 security trustee, the Funding 1 swap provider, the cash manager, the account bank, the seller, the corporate services provider, the Funding 1 GIC provider, the issuing entity and any other entity that accedes to the terms of the Funding 1 deed of charge from time to time
Funding 1 security	the security created under the Funding 1 deed of charge
Funding 1 security trustee	Deutsche Bank Trust Company Americas
Funding 1 share	the Funding 1 share of the trust property from time to time, as calculated in accordance with the mortgages trust deed on each calculation date
Funding 1 share percentage	the Funding 1 share percentage of the trust property from time to time, as calculated in accordance with the mortgages trust deed on each calculation date
Funding 1 swap	the swap documented under the Funding 1 swap agreement which enables Funding 1 to hedge against the possible variance between the standard variable rate payable on the standard variable rate loans, the fixed rates of interest payable on the fixed rate loans and the rates of interest payable on the tracker rate loans and the LIBOR-based rates for sterling deposits payable in respect of any outstanding loan tranches, as described further in “ <b>The swap agreements – The Funding 1 swap</b> ” above
Funding 1 swap agreement	the ISDA master agreement and schedule thereto entered into on the programme date between Funding 1, the Funding 1 swap provider and the Funding 1 security trustee and any confirmation documented thereunder from time to time between Funding 1, the Funding 1 swap provider and the Funding 1 security trustee (as each of the same may be amended, restated, novated or supplemented from time to time)
Funding 1 swap excluded termination amount	<p>in relation to the Funding 1 swap agreement an amount equal to:</p> <p>(a) the amount of any termination payment due and payable to the Funding 1 swap provider as a result of a Funding 1 swap provider default or following a Funding 1 swap provider downgrade termination event;</p> <p>less</p> <p>(b) the amount, if any, received by Funding 1 from a replacement swap provider upon entry by Funding 1 into an agreement with such replacement swap provider to replace the Funding 1 swap agreement which has terminated as a result of such Funding 1 swap provider default or following the occurrence of such Funding 1 swap provider downgrade termination event</p>
Funding 1 swap provider	Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006), pursuant to the Funding 1 swap agreement
Funding 1 swap provider default	the occurrence of an event of default (as defined in the Funding 1 swap agreement) where the Funding 1 swap provider is the defaulting party (as defined in the Funding 1 swap agreement)
Funding 1 swap provider downgrade termination event	the occurrence of an additional termination event following the failure by the Funding 1 swap provider to comply with the requirements of the ratings downgrade provisions set out in the Funding 1 swap agreement
Funding 1 transaction account	the account in the name of Funding 1 maintained with the account bank pursuant to the bank account agreement or such additional or replacement account as may for the time being be in place
Funding 1 transaction documents	the transaction documents to which Funding 1 is a party
Funding security trustees	the Funding 1 security trustee and/or any other security trustee in respect of the security granted by a new beneficiary

further advance	an advance made following a request from an existing borrower for a further amount to be lent to him or her under his or her mortgage, where Birmingham Midshires has a discretion as to whether to accept that request
global notes	the notes in registered global form
Halifax	Halifax plc, whose business was transferred to Bank of Scotland in accordance with the HBOS Group Reorganisation Act 2006 on the reorganisation date
HBOS	HBOS plc
HBOS group	HBOS plc and its subsidiaries from time to time
high loan-to-value fee or high LTV fee	a fee incurred by a borrower as a result of taking out a loan with an LTV ratio in excess of a certain percentage specified in the offer
holder	has the meaning given to that term in Condition 1.2
Holdings	Pendeford Holdings Limited
Hometrack	Hometrack Data Systems Limited
in arrears	in respect of a mortgage account, occurs when one or more monthly payments in respect of a mortgage account have become due and unpaid by a borrower
industry CPR	a constant repayment rate which is calculated by dividing the amount of scheduled and unscheduled repayments of mortgages made by building societies in a quarter by the quarterly balance of mortgages outstanding for building societies in the United Kingdom
initial loans	the loans sold by the seller to the mortgages trustee on the programme date pursuant to the terms of the mortgage sale agreement
initial portfolio	means all the initial loans comprising the portfolio on the programme date
Insolvency Act	the Insolvency Act 1986 (as amended)
insolvency event	<p>in respect of the seller, the servicer, the cash manager or the issuing entity cash manager (each, for the purposes of this definition, a relevant entity) means:</p> <p>(a) an order is made or an effective resolution passed for the winding up of the relevant entity;</p> <p>(b) the relevant entity ceases or threatens to cease to carry on its business or stops payment or threatens to stop payment of its debts or is deemed unable to pay its debts within the meaning of section 123(1)(a), (b), (c) or (d) of the Insolvency Act or becomes unable to pay its debts as they fall due or the value of its assets falls to less than the amounts of its liabilities (taking into account, for both these purposes, contingent and prospective liabilities) or otherwise becomes insolvent; or</p> <p>(c) proceedings (including, but not limited to, presentation of an application for an administration order, the filing of documents with the court for the appointment of an administrator or the service of a notice of intention to appoint an administrator) are initiated against the relevant entity under any applicable liquidation, administration reorganisation (other than a reorganisation where the relevant entity is solvent) or other similar laws, save where such proceedings are being contested in good faith; or an administrative or other receiver, administrator or other similar official is appointed in relation to the whole or any substantial part of the undertaking or assets of the relevant entity or the appointment of an administrator takes effect; or distress, execution or diligence or other process is enforced upon the whole or any substantial part of the undertaking or assets of the relevant entity and in any of the foregoing</p>

	cases it is not discharged within 15 London business days; or if the relevant entity initiates or consents to judicial proceedings relating to itself under any applicable liquidation, administration, insolvency, reorganisation or other similar laws or makes a conveyance or assignment for the benefit of its creditors generally or takes steps with a view to obtaining a moratorium in respect of any indebtedness
intercompany loan	the aggregate of the loan tranches made available to Funding 1 pursuant to the intercompany loan agreement
intercompany loan acceleration notice	an acceleration notice served by the issuing entity security trustee on Funding 1 following an intercompany loan event of default
intercompany loan agreement	the intercompany loan agreement entered into on the programme date between (among others) Funding 1, the issuing entity, the issuing entity security trustee and the Funding 1 security trustee (as the same may be amended, restated, novated, replaced or supplemented from time to time) which governs the advance of loan tranches by the issuing entity to Funding 1 as further described in “ <b>The Intercompany loan agreement</b> ”
intercompany loan event of default	an event of default under the intercompany loan agreement
intercompany loan ledger	a ledger maintained by the cash manager on behalf of Funding 1 to record payments of interest and repayments of principal made on each of the loan tranches under the intercompany loan agreement
interest amount	has the meaning given to that term in Condition 4.2(b)
interest commencement date	<p>(a) in relation to a series and class of notes, the relevant closing date of such series and class notes or such other date as may be specified as such in the applicable final terms; and</p> <p>(b) in relation to an issuing entity subordinated loan or an issuing entity start-up loan (as applicable), the relevant advance date of such issuing entity subordinated loan or issuing entity start-up loan (as applicable) or such other date as may be specified as such on the applicable issuing entity subordinated loan agreement or issuing entity start-up loan agreement (as applicable)</p> <p>(c) in respect of a loan tranche, the relevant closing date of the related series and class of notes or the relevant advance date of the related issuing entity subordinated loan or issuing entity start-up loan (as applicable) or such other date as may be specified as such in the applicable loan tranche supplement</p>
interest payment date	in respect of a series and class of notes (other than money market notes), the quarterly interest payment dates specified in the applicable final terms and (in the case of the money market notes) the monthly interest payment dates specified in the applicable final terms, subject (in each case) to the terms and conditions of the notes
interest period	<p>(a) in relation to a series and class of notes (i) with respect to the first interest payment date, the period from (and including) the applicable interest commencement date to (but excluding) such first interest payment date and (ii) thereafter, with respect to each interest payment date, the period from and including the preceding interest payment date to (but excluding) that interest payment date;</p> <p>(b) in relation to an issuing entity subordinated loan or an issuing entity start-up loan, (i) with respect to the first interest payment date, the period from (and including) the applicable interest commencement date to (but excluding) such first interest payment date and (ii) thereafter, with respect to each interest payment date, the period from and including the preceding interest payment date to (but excluding) that interest payment date;</p> <p>(c) in respect of a loan tranche, (i) with respect to the first Funding 1</p>

	interest payment date, the period from (and including) the applicable interest commencement date to (but excluding) such first Funding 1 interest payment date and (ii) thereafter, the period from (and including) the preceding Funding 1 interest payment date to (but excluding) that Funding 1 interest payment date
Investment Company Act	the United States Investment Company Act of 1940, as amended
investment plan	in respect of an interest-only loan, a repayment mechanism selected by the borrower and intended to provide sufficient funds to redeem the full principal of a loan at maturity
IRS	United States Internal Revenue Service
ISA	an individual savings account within the Individual Savings Account Regulations 1998 (as amended) and which shelters investments in the account from income tax and capital gains tax
ISDA definitions	has the meaning given to that term in Condition 19
issuance	in respect of the notes, means all series and classes of notes issued on the same closing date
issuing entities	the issuing entity and other Funding 1 issuing entities (if applicable)
issuing entity	Pendeford Master Issuer plc
issuing entity account bank	Bank of Scotland
issuing entity bank accounts	the issuing entity transaction account and any other account opened and maintained by the issuing entity from time to time with the issuing entity account bank pursuant to the transaction documents
issuing entity bank account agreement	the agreement entered into on the programme date between the issuing entity account bank, the issuing entity, the issuing entity cash manager and the issuing entity security trustee (as the same may be amended, restated, supplemented, replaced and/or novated from time to time) which governs the operation of issuing entity bank accounts
issuing entity capitalisation loan	the loan from Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006) to the issuing entity pursuant to the issuing entity capitalisation loan agreement
issuing entity capitalisation loan agreement	the agreement dated 9 March 2007, pursuant to which Halifax (to which Bank of Scotland has succeeded) agreed to make a loan facility available to Holdings, the proceeds of the initial advance under which were used by Holdings to purchase shares in the issuing entity
issuing entity cash management agreement	the issuing entity cash management agreement entered into on the programme date between the issuing entity cash manager, the issuing entity and the issuing entity security trustee (as the same may be amended, restated, novated, replaced or supplemented from time to time), as described further in “ <b>Cash management for the issuing entity</b> ” above
issuing entity cash manager	Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006) acting, pursuant to the issuing entity cash management agreement, as agent for the issuing entity and the issuing entity security trustee to manage all cash transactions and maintain certain ledgers on behalf of the issuing entity
issuing entity deed of charge	the deed of charge entered into on the programme date between, among others, the issuing entity and the issuing entity security trustee (as the same may be amended, restated, novated, replaced or supplemented from time to time), under which the issuing entity charges the issuing entity security in favour of the issuing entity security trustee for the benefit of the issuing entity secured creditors, as described further in “ <b>Security for the issuing</b>

	<b>entity’s obligations”</b> above
issuing entity expense ledger	a ledger which records payments of certain fees received from Funding 1 under the intercompany loan agreement and payments out in accordance with the issuing entity pre-enforcement revenue priority of payments
issuing entity fee	has the meaning given to that term on page 118
issuing entity note trustees	the note trustee and/or any other note trustee for the holders of new notes issued by the issuing entity
issuing entity post-enforcement priority of payments	the order in which, following service of a note acceleration notice on the issuing entity and the service of an intercompany loan acceleration notice on Funding 1, the issuing entity security trustee will apply the amounts received or recovered by the issuing entity security trustee, as set out in <b>“Cashflows – Distribution of issuing entity principal receipts and issuing entity revenue receipts following note acceleration and intercompany loan acceleration”</b> above
issuing entity pre-enforcement principal priority of payments	the order in which, prior to service of a note acceleration notice on the issuing entity, the issuing entity cash manager will apply the issuing entity principal receipts on each quarterly interest payment date, as set out in <b>“Cashflows – Distribution of issuing entity principal receipts before note acceleration”</b> above
issuing entity pre-enforcement revenue priority of payments	the order in which, prior to service of a note acceleration notice on the issuing entity, the issuing entity cash manager will apply the issuing entity revenue receipts on each quarterly interest payment date, as set out in <b>“Cashflows – Distribution of issuing entity revenue receipts before note acceleration”</b> above
issuing entity principal ledger	a ledger maintained by the issuing entity cash manager to record all Funding 1 available principal receipts received by the issuing entity from Funding 1 constituting principal repayments on a loan tranche (other than a start-up loan tranche)
issuing entity principal receipts	has the meaning given to that term on page 150
issuing entity priority of payments	the issuing entity pre-enforcement revenue priority of payments, the issuing entity pre-enforcement principal priority of payments or the issuing entity post-enforcement priority of payments, as the case may be
issuing entity revenue ledger	a ledger maintained by the issuing entity cash manager to record issuing entity revenue receipts (excluding certain issuing entity fees to be paid by Funding 1 on each Funding 1 interest payment date under the terms of the intercompany loan agreement (other than in respect of any non-subordinated termination payment due by the issuing entity in respect of any issuing entity swap), which will be credited to the issuing entity expense ledger, but including principal repayments to be made by Funding 1 of any start-up loan tranche) received and paid out by the issuing entity
issuing entity revenue receipts	an amount equal to the sum of: <ul style="list-style-type: none"> <li>(a) interest to be paid by Funding 1 on the relevant Funding 1 interest payment date in respect of the loan tranches under the intercompany loan agreement;</li> <li>(b) principal to be repaid by Funding 1 on the relevant Funding 1 interest payment date in respect of start-up loan tranches under the intercompany loan agreement;</li> <li>(c) issuing entity fees to be paid by Funding 1 on the relevant Funding 1 interest payment date under the terms of the intercompany loan agreement;</li> <li>(d) interest payable on the issuing entity bank accounts and any authorised investments which will be received on or before the relevant quarterly</li> </ul>

interest payment date;

(e) other net income of the issuing entity including amounts received or to be received under the issuing entity swap agreements on or before the relevant quarterly interest payment date (including any amount received by the issuing entity in consideration of it entering into a replacement issuing entity swap agreement but excluding (i) the return or transfer of any excess swap collateral as set out under any issuing entity swap agreement and (ii) in respect of each issuing entity swap provider, prior to the designation of an early termination date under the relevant issuing entity swap agreement and the resulting application of the collateral by way of netting or set-off, an amount equal to the value of all collateral (other than excess swap collateral) provided by such issuing entity swap provider to the issuing entity pursuant to the relevant issuing entity swap agreement (and any interest or distributions in respect thereof)); and

(f) any additional amount the issuing entity receives from any taxing authority on account of amounts paid to that taxing authority for and on account of tax by an issuing entity swap provider under an issuing entity swap agreement

issuing entity secured creditors	the issuing entity security trustee, the note trustee, noteholders, the issuing entity swap providers, the issuing entity account bank, the paying agents, the registrar, the transfer agent, the agent bank, the exchange agent, the corporate services provider, the issuing entity cash manager, the issuing entity start-up loan provider, and any new issuing entity secured creditor who accedes to the issuing entity deed of charge from time to time under a deed of accession or a supplemental deed
issuing entity security	security created by the issuing entity pursuant to the issuing entity deed of charge in favour of the issuing entity secured creditors
issuing entity security trustee	Deutsche Bank Trust Company Americas
issuing entity start-up loan	a loan advanced by the issuing entity start-up loan provider to the issuing entity on the programme date pursuant to the issuing entity start-up loan agreement, or, as applicable, by the issuing entity start-up loan provider or a new issuing entity start-up loan provider on a future closing date pursuant to an issuing entity start-up loan agreement
issuing entity start-up loan agreements	The agreement entered into on the programme date between, among others, the issuing entity and the issuing entity start-up loan provider pursuant to which the issuing entity start-up loan provider advanced the first issuing entity start-up loan to the issuing entity and each other agreement entered into following the programme date between, among others, the issuing entity, the issuing entity start-up loan provider or a new issuing entity start-up loan provider pursuant to which it will advance a further issuing entity start-up loan to the issuing entity
issuing entity start-up loan provider	Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006), in its capacity as provider of the first issuing entity start-up loan advanced to the issuing entity on the programme date and any further issuing entity start-up loans it may advance to the issuing entity on future closing dates
issuing entity sub-ledgers	ledgers maintained by the issuing entity cash manager to record payments of interest and repayments of principal on each series and class of notes and payments of issuing entity fees in respect of any early termination payment due by the issuing entity in respect of a corresponding issuing entity swap (other than in respect of any subordinated termination payment by the issuing entity in respect of such issuing entity swap) and payments of interest and repayments of principal on each issuing entity subordinated loan and on each issuing entity start-up loan

issuing entity subordinated loan	the loan advanced or to be advanced by the issuing entity subordinated loan provider or a new issuing entity subordinated loan provider to the issuing entity pursuant to an issuing entity subordinated loan agreement
issuing entity subordinated loan agreement	the agreement entered into between, among others, the issuing entity and the issuing entity subordinated loan provider pursuant to which the issuing entity subordinated loan provider will advance the first issuing entity subordinated loan to the issuing entity and each other agreement entered into following the programme date between, among others, the issuing entity and the issuing entity subordinated loan provider or a new issuing entity subordinated loan provider pursuant to which it will advance a further issuing entity subordinated loan to the issuing entity
issuing entity subordinated loan provider	Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006), in its capacity as provider of the issuing entity subordinated loan advanced to the issuing entity on the programme date and any further subordinated loans it may advance to the issuing entity on future closing dates
issuing entity swap agreements	in respect of a series and class of notes, the ISDA Master Agreement, schedules and confirmations relating to the relevant issuing entity swaps to be entered into on or before the relevant closing date in respect of such series and class of notes between the issuing entity, the relevant issuing entity swap provider and the issuing entity security trustee (as amended, restated, supplemented, replaced and/or novated from time to time)
issuing entity swap excluded termination amount	<p>in relation to an issuing entity swap agreement an amount equal to:</p> <p>(a) the amount of any termination payment due and payable to the relevant issuing entity swap provider as a result of an issuing entity swap provider default or following an issuing entity swap provider downgrade termination event, less</p> <p>(b) the amount, if any, received by issuing entity from a replacement swap provider upon entry by issuing entity into an agreement with such replacement swap provider to replace such issuing entity swap agreement which has been terminated as a result of such issuing entity swap provider default or following the occurrence of such issuing entity swap provider downgrade termination event</p>
issuing entity swap provider	in respect of a series and class of notes, any swap provider identified as such in the applicable final terms
issuing entity swap provider default	the occurrence of an event of default (as defined in the relevant issuing entity swap agreement) where the relevant issuing entity swap provider is the defaulting party (as defined in the relevant issuing entity swap agreement)
issuing entity swap provider downgrade termination event	the occurrence of an additional termination event following the failure by any of the issuing entity swap providers to comply with the requirements of the ratings downgrade provisions set out in the relevant issuing entity swap agreement
issuing entity swaps	in respect of a series and class of notes, the currency and/or interest rate swaps entered into by the issuing entity from time to time under the relevant issuing entity swap agreement, as identified in the applicable final terms
issuing entity transaction account	the day to day bank account of the issuing entity, held with the issuing entity account bank as at the programme date pursuant to the terms of the issuing entity bank account agreement
issuing entity transaction documents	the transaction documents to which the issuing entity is a party

Jersey share trustee	Structured Finance Management Offshore Limited
lending criteria	the criteria applicable to the granting of an offer of a mortgage to a borrower, as may be amended from time to time and as further described in “ <b>The loans – Underwriting – Lending criteria</b> ” above
LIBOR	the London Interbank Offered Rate for deposits in the relevant currency and, in the case of the Rule 144A notes, the London Interbank Offered Rate for deposits in the relevant currency as determined by the agent bank in accordance with the paying agent and agent bank agreement
liquidity reserve fund rating event	the seller’s long-term, unsecured, unsubordinated and unguaranteed debt obligations are rated below A3 by Moody’s (Moody’s confirms that its then current ratings of the notes will not be downgraded, withdrawn or qualified as a consequence of such rating of the seller)
listed notes	means each series and class of notes which is admitted to the official list maintained by the UK Listing Authority and admitted to trading on the London Stock Exchange’s Regulated Market
loan	each loan referenced by its loan identifier number and comprising the aggregate of all principal sums, interest, costs, charges, expenses and other monies (including all further advances) due or owing with respect to that loan under the relevant mortgage conditions by a borrower on the security of a mortgage from time to time outstanding or, as the context may require, the borrower’s obligations in respect of the same
loan tranches	the AAA loan tranches, the AA loan tranches, the A loan tranches, the BBB loan tranches, the BB loan tranches, the subordinated loan tranches and the start-up loan tranches and such other loan tranches as shall be introduced from time to time (subject to certain conditions), being the advances made by the issuing entity to Funding 1 pursuant to the intercompany loan agreement, each being funded from proceeds received by the issuing entity from the issue of a series and class of notes, the borrowing by the issuing entity of an issuing entity subordinated loan or, as applicable, the borrowing by the issuing entity of an issuing entity start-up loan
loan tranche supplement	in relation to any loan tranche, the document between, amongst others, Funding 1 and the issuing entity recording the principal terms of such loan tranche
London business day	a day (other than a Saturday or Sunday) on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London
London Stock Exchange	the London Stock Exchange plc
loss amount	<p>the amount of any costs, expenses, losses or other claims suffered or incurred by, as applicable, the mortgages trustee and/or Funding 1 in connection with any recovery of interest on the loans to which the seller, the mortgages trustee or Funding 1 was not entitled or could not enforce as a result of any determination by any court or other competent authority or any ombudsman in respect of any loan and its related security that:</p> <p>(a) any term which relates to the recovery of interest under the standard documentation applicable to that loan and its related security is unfair; or</p> <p>(b) (if variable margins are introduced in respect of tracker rate loans in the future) the variable margin above the Bank of England repo rate under any tracker rate loan must be set by the seller; or</p> <p>(c) the interest payable under any loan is to be set by reference to an interest rate other than that set or purported to be set by either the servicer or the mortgages trustee as a result of the seller having more than one</p>



	standard variable rate
losses	the realised principal losses experienced on the loans in the portfolio
losses ledger	the ledger of such name created and maintained by the cash manager pursuant to the cash management agreement to record the losses on the portfolio
LTV ratio or loan-to-value ratio	the ratio of the outstanding balance of a loan to the value of the mortgaged property securing that loan
LTV test	a test which assigns a credit enhancement value (i) to each loan in the portfolio based on its current LTV ratio and (ii) calculated to include any related unsecured portion of a mortgage loan in respect of the Mortgage Plus product based on its current LTV ratio. The weighted average credit enhancement value for the portfolio is then determined
managers	the entities specified as such in the applicable final terms
mandatory transfer	has the meaning given to that term on page 13
mandatory transfer date	has the meaning given to that term in Condition 13
mandatory transfer price	has the meaning given to that term in Condition 13
mandatory transfer termination event	has the meaning given to that term in Condition 257
margin	in relation to each series and class of floating rate notes, has the meaning given in the applicable final terms
master definitions and construction schedule	the master definitions and construction schedules, as amended from time to time, containing definitions used in the transaction documents
MCOB	the FSA Mortgages and Home Finance: Conduct of Business Sourcebook
MH/CP documentation	any affidavit, declaration, consent or renunciation granted in terms of the Matrimonial Homes (Family Protection) (Scotland) Act 1981 and/or (as applicable) the Civil Partnership Act 2004 in connection with a Scottish mortgage or the property secured thereby
minimum seller share	an amount included in the current seller share which is calculated in accordance with the mortgages trust deed, as further described under “ <b>The mortgages trust</b> ” above
money market notes	has the meaning given to that term on page 257
monthly CPR	has the meaning given to that term on page 109
monthly interest payment date	means, in respect of any money market notes, each monthly date specified as such in the applicable final terms for the payment of interest and/or principal until the occurrence of a pass-through trigger event and, following such occurrence, the quarterly interest payment dates as specified in the applicable final terms for payment of interest and/or principal subject, in each case, to the appropriate Business Day Convention, if any, specified in the applicable final terms
Moody’s	Moody’s Investors Service Limited and any successor to its ratings business
mortgage	the legal charge or standard security securing a loan
mortgage account	all loans secured on the same property are incorporated in the same mortgage account
mortgage conditions	the terms and conditions applicable to the loans as contained in the seller’s Mortgage Conditions booklets for England and Wales or Scotland

		applicable from time to time
Mortgage Plus loans		has the meaning given to that term on page 80
mortgage related securities		as defined in the United States Secondary Mortgage Market Enhancement Act 1984, as amended
mortgage sale agreement		the mortgage sale agreement entered into on the programme date among the seller, the mortgages trustee, Funding 1 and the Funding 1 security trustee in relation to the sale of loans to the mortgages trustee from time to time (as the same may be amended, restated, novated, replaced or supplemented from time to time), as further described in “ <b>Sale of the loans and their related security</b> ” above
mortgage terms		all the terms and conditions applicable to a loan, including without limitation the applicable mortgage conditions and offer conditions
mortgages trust		the bare trust of the trust property held by the mortgages trustee as to both capital and income on trust absolutely for Funding 1 (as to the Funding 1 share) and the seller (as to the seller share), so that each has an undivided beneficial interest in the trust property
mortgages trust available principal receipts		principal receipts on the loans on the relevant calculation date as described further in “ <b>The mortgages trust – Cash management of trust property – revenue receipts</b> ” above
mortgages trust available revenue receipts		an amount equal to: <ul style="list-style-type: none"> <li>(a) revenue receipts on the loans on the relevant calculation date (but excluding principal receipts);</li> <li>(b) plus interest payable to the mortgages trustee on the mortgages trustee GIC account;</li> <li>(c) less third party amounts, as described further in “<b>The mortgages trust – Cash management of trust property – revenue receipts</b>” above</li> </ul>
mortgages trust deed		the mortgages trust deed dated the programme date, between (among others) the mortgages trustee, Funding 1 and the seller (as the same may be amended, restated, novated, replaced or supplemented from time to time) as, further described in “ <b>The mortgages trust</b> ” above
mortgages trustee		Pendeford Mortgages Trustee Limited
mortgages trustee corporate services agreement		the agreement entered into on the programme date between the mortgages trustee corporate services provider, the mortgages trustee and the Funding 1 security trustee (as the same may be amended, restated, novated, replaced or supplemented from time to time), which governs the provision of corporate services by the corporate services provider to the mortgages trustee
mortgages trustee corporate services provider		Structured Finance Management Offshore Limited or such other person or persons for the time being acting as corporate services provider to the mortgages trustee under the mortgages trustee corporate services agreement
mortgages trustee GIC account		the account in the name of the mortgages trustee maintained with the mortgages trustee GIC provider pursuant to the terms of the bank account agreement and the mortgages trustee guaranteed investment contract or such additional or replacement account as may for the time being be in place
mortgages trustee GIC provider		Bank of Scotland
mortgages trustee guaranteed		the guaranteed investment contract entered into on the programme date between the mortgages trustee and the mortgages trustee GIC provider

investment contract	under which the mortgages trustee GIC provider agrees to pay the mortgages trustee a guaranteed rate of interest on the balance of the mortgages trustee GIC account (as the same may be amended, restated, varied or supplemented from time to time), as described further in “ <b>Credit structure – Mortgages trustee GIC account/Funding 1 GIC account</b> ” above
new Funding 1 issuing entity	an entity that issues securities and lends the proceeds thereof to Funding 1
new funding beneficiary	an entity that has acceded to the mortgages trust deed as a beneficiary of the mortgages trust
new intercompany loan	a loan under a new intercompany loan agreement
new intercompany loan agreement	each agreement entered into between, on the one hand, Funding 1 or a new funding beneficiary and, on the other hand, the issuing entity or a new issuing entity pursuant to which the issuing entity or such new issuing entity will advance funds to Funding 1 or such new funding beneficiary in connection with the mortgages trust using the proceeds of new notes
new issuing entity	an entity that issues securities and lends the proceeds thereof to Funding 1 or a new funding beneficiary
new issuing entity start-up loan provider	any entity that advances an issuing entity start-up loan to the issuing entity on a closing date (excluding the programme date) other than the issuing entity start-up loan provider
new issuing entity subordinated loan provider	any entity that advances an issuing entity subordinated loan to the issuing entity on an advance date other than the issuing entity subordinated loan provider
new loans	loans which the seller sells, from time to time after the programme date, to the mortgages trustee pursuant to the terms of the mortgage sale agreement
new portfolio	<p>the portfolio of loans and their related security (other than any loan and its related security which has been redeemed in full on or before the relevant sale date), particulars of which are set out in the relevant new portfolio notice or in a document stored upon electronic media (including, but not limited to, a CD-ROM), and all right, title, interest and benefit of the seller in and to:</p> <p>(a) all payments of principal and interest (including, for the avoidance of doubt, all accrued interest, arrears of interest, capitalised interest, capitalised expenses and capitalised arrears) and other sums due or to become due in respect of such loans and their related security including, without limitation, the right to demand, sue for, recover and give receipts for all principal monies, interest and costs and the right to sue on all covenants and any undertakings made or expressed to be made in favour of the seller under the applicable mortgage terms;</p> <p>(b) subject where applicable to the subsisting rights of redemption of borrowers, all deeds of consent, deeds of postponement, MH/CP documentation and all third party guarantees and any other collateral security for the repayment of the relevant new loans secured by the relevant new mortgages;</p> <p>(c) the right to exercise all the powers of the seller in relation thereto;</p> <p>(d) all the estate and interest in the relevant properties vested in the seller;</p> <p>(e) each relevant Certificate of Title and Valuation Report and any right of action of the seller against any solicitor, licensed conveyancer, qualified conveyancer, valuer, registrar or registry or other person in connection with any report, valuation, opinion, certificate or other statement of fact or opinion given or received in connection with all or part of any loan and its related security or affecting the decision of the seller to make or offer to</p>

	make all or part of the relevant loan;
	(f) all right, title and interest of the seller (including, without limitation, the proceeds of all claims) to which the seller is entitled under the relevant buildings policies and any relevant properties in possession cover; and
	(g) all proceeds from the enforcement of such loans and their related security
new seller	has the meaning given to that term on page 6
New York business day	a day (other than a Saturday or a Sunday) on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the city of New York
N(M)	the meaning given to that term on page 52
non-asset trigger event	the occurrence of any of the following on a calculation date: <ul style="list-style-type: none"> <li>(a) an insolvency event occurs in relation to the seller on or before that calculation date;</li> <li>(b) the seller's role as servicer under the servicing agreement is terminated and a new servicer is not appointed within 60 days;</li> <li>(c) as at the calculation date immediately preceding the relevant calculation date, the seller share was less than the minimum seller share and this has not been remedied by the relevant calculation date; or</li> <li>(d) as at the calculation date immediately preceding the relevant calculation date, the aggregate outstanding principal balance of loans comprising the trust property was less than the required loan balance amount specified in the most recent final terms and this has not been remedied by the relevant calculation date.</li> </ul>
Non-United States holder	a beneficial owner of Rule 144A notes that is not a United States holder
normal calculation date	the first day (or, if not a London business day, the next succeeding London business day) of each month
note acceleration notice	an acceleration notice served by the note trustee on the issuing entity following a note event of default declaring all the notes to be immediately due and payable
note event of default	an event of default under the provisions of Condition 9 under " <b>Terms and conditions of the notes</b> " above
note principal payment	the amount of each principal payment payable on each series and class of notes
note trust deed	the deed entered into on the programme date governing the notes (as the same may be amended, restated, novated, replaced or supplemented from time to time), as further described in " <b>Description of the note trust deed</b> " above
note trustee	Deutsche Trustee Company Limited
noteholders	the holders of the class A notes, the class B notes, the class M notes, the class C notes (as the same may be amended, restated, novated or supplemented from time to time), the class D notes (and any other class of notes that may be issued from time to time, subject to certain conditions)
notes	all of the class A notes, the class B notes, the class M notes, the class C notes and the class D notes (and any other class of notes that may be issued from time to time, subject to certain conditions)

offer conditions	the terms and conditions applicable to a specific loan as set out in the relevant offer letter to the borrower
official list	the official list of the United Kingdom Listing Authority
offshore transaction	has the meaning given to that term on page 282
OFT	the Office of Fair Trading
OID	has the meaning given to that term on page 268
Ombudsman	the Financial Ombudsman Service under the FSMA
original bullet loan tranche	a loan tranche which at any time has been a bullet loan tranche (even if such bullet loan tranche has subsequently become a pass-through loan tranche)
original pass-through loan tranche	a loan tranche which at the time it was advanced was a pass-through loan tranche
original scheduled amortisation instalment	that part of a loan tranche which at any time has been a scheduled amortisation instalment (even if that part of that loan tranche has subsequently become a pass-through loan tranche)
original scheduled amortisation loan tranche	a loan tranche which at any time has been a scheduled amortisation loan tranche (even if such loan tranche has subsequently become a pass-through loan tranche)
outstanding amount	following enforcement of a loan, the amount outstanding on the payment of that loan after deducting money received under the applicable mortgage indemnity guarantee policy
outstanding principal balance	in relation to a loan, as at any date (the determination date), the aggregate principal balance of the loan as at the determination date including (but avoiding double counting) the initial advance, any further advance, any flexible loan drawing, capitalised expenses, capitalised arrears and capitalised interest in each case relating to such loan (including, without limitation, that which results from an increase in the principal amount due under a flexible loan due to the borrower making flexible loan drawings and/or taking payment holidays or making underpayments) less any prepayment, repayment or payment of the foregoing made on or prior to the determination date plus accrued interest on such loan as at the determination date
overpayment	a payment made by a borrower in an amount greater than the monthly payment then due on the loan
pass-through loan tranche	a rated loan tranche which has no scheduled repayment date other than the final repayment date, namely those loan tranches designated as 'pass-through' loan tranches in the applicable loan tranche supplement and final terms
pass-through notes	any series and class of notes which has no specified redemption dates other than the final maturity date. In addition, on the earlier to occur of a pass-through trigger event and the step-up date (if any) in relation to any series and class of bullet redemption notes or scheduled redemption notes, such notes will be deemed to be pass-through notes
pass-through repayment restrictions	has the meaning given to that term on page 146
pass-through trigger event	any of the following events:  (a) the occurrence of a trigger event;  (b) the service of a note acceleration notice by the note trustee on the

	issuing entity; or
	(c) the service of an intercompany loan acceleration notice by the issuing entity security trustee on Funding 1
paying agent and agent bank agreement	the agreement entered into on the programme date which sets out the appointment of the paying agents, the registrar, the transfer agent, the exchange agent and the agent bank for the notes (as amended, restated, supplemented, replaced and/or novated from time to time)
paying agents	the principal paying agent and the US paying agent
payment holiday	a period during which a borrower may suspend payments under a loan without penalty
permitted redemption dates	in respect of a series and class of notes, the interest payment date on which those notes may be redeemed by the issuing entity, subject to the terms and conditions of the notes
PFIC	has the meaning given to that term on page 269
Plans	has the meaning given to that term on page 273
pool factor	has the meaning given to that term in condition 5.3
portable loan	a loan (other than a variable rate loan) that incorporates a portability facility, which allows the borrower to transfer the loan balance at the same interest rate and subject to all the existing terms and conditions to a new property
portfolio	at any time the loans and their related security sold to the mortgages trustee and held by the mortgages trustee on trust for the beneficiaries
post-enforcement call option	the call option granted to the post-enforcement call option holder in respect of the notes under the post-enforcement call option agreement
post-enforcement call option agreement	the post-enforcement call option agreement entered into on the programme date among the issuing entity, the post-enforcement call option holder, the note trustee and the issuing entity security trustee pursuant to which the note trustee (on behalf of the noteholders) grants to the post-enforcement call option holder the post-enforcement call option (as the same may be amended, restated, novated, replaced or supplemented from time to time)
post-enforcement call option holder	Pendeford PECO Limited
prime loan	a loan categorised as such by Birmingham Midshires
principal amount outstanding	in relation to the notes, has the meaning given to that term in Condition 5.3
principal deficiency sub-ledger	the AAA principal deficiency sub-ledger, the AA principal deficiency sub-ledger, the A principal deficiency sub-ledger, the BBB principal deficiency sub-ledger, the BB principal deficiency sub-ledger or the subordinated loan principal deficiency sub-ledger, as the case may be
principal ledger	the ledger of such name maintained by the cash manager on behalf of the mortgages trustee pursuant to the cash management agreement to record principal receipts on the loans and payments of principal from the mortgages trustee GIC account to Funding 1 and the seller on each distribution date. Together the principal ledger and the revenue ledger reflect the aggregate of all amounts of cash standing to the credit of the mortgages trustee GIC account
principal paying agent	Deutsche Bank AG, London Branch
principal receipts	all principal amounts received from borrowers in respect of the loans or otherwise paid or recovered in respect of the loans and their related

	security representing monthly repayments of principal, prepayments of principal, redemption proceeds and amounts recovered on enforcement representing principal (but excluding principal received or treated as received in respect of a loan subsequent to the completion of enforcement procedures and certain early repayment fees)
product period	has the meaning given to that term on page 76
product switch	a variation to the financial terms and conditions of a loan other than: <ul style="list-style-type: none"> <li>(a) any variation agreed with a borrower to control or manage arrears on the loan;</li> <li>(b) any variation in the maturity date of the loan unless, while any loan tranche under the intercompany loan agreement is outstanding, it is extended beyond May 2057 or such later date specified in the most recent final terms;</li> <li>(c) any variation imposed by statute; or</li> <li>(d) any variation in the frequency with which the interest payable in respect of the loan is charged</li> </ul>
programme	has the meaning given to that term on page i
programme agreement	the agreement entered into on the programme date between, amongst others, the issuing entity, Funding 1, the mortgages trustee and the dealers named therein (or deemed named therein) (as the same may be amended, restated, novated, replaced or supplemented from time to time)
programme date	the date of the first issuance of notes, 12 April 2007
programme resolution	has the meaning given to that term in Condition 11.2
properties in possession cover	such buildings insurance policies as may be issued from time to time to the seller when a property is taken into possession and any endorsements or extensions thereto from time to time or any such similar alternative policy or policies as may in future be issued in favour of the seller
prospectus directive	Prospectus Directive (Directive 2003/71/EC)
prospectus rules	has the meaning given to that term on page 1
purchase option	has the meaning given to that term in Condition 5.6
QIB	“qualified institutional buyer” within the meaning of Rule 144A under the Securities Act
qualified institutional buyer	has the same meaning as QIB
qualified stated interest	has the meaning given to that term on page 268
qualifying body	has the meaning given to that term on page 55
quarterly CPR	on any date means the average of the three most recent CPRs, where CPR is, on any normal calculation date, the annualised principal repayment rate of all the loans comprised in the trust property during the previous calculation period calculated as follows: $1 - ((1 - R)^{12})$ <p>where R equals the result (expressed as a percentage) of the total principal receipts received during the period of one month ending on that normal calculation date divided by the aggregate outstanding principal balance of the loans comprised in the trust property as at the first day of that period</p>
quarterly interest payment date	means, in respect of a series and class of notes (other than money market notes), each quarterly date specified in the applicable final terms for the

	payment of interest and/or principal subject to the appropriate Business Day Convention, if any, specified in the applicable final terms
rate of interest	in respect of any series and class of notes, the rate or rates (expressed as a percentage per annum) of interest payable in respect of such notes specified in the applicable final terms or calculated and determined in accordance with the applicable final terms
rated loan tranche	a loan tranche that corresponds to a series and class of notes
rating	rating assigned by the rating agencies to the notes
rating agencies	each of Fitch, Moody's and Standard & Poor's and any further or replacement rating agency appointed by the issuing entity with the approval of the note trustee to give a credit rating to any series and class of notes
ratings confirmation	has the meaning given to that term on page 41
reasonable, prudent mortgage lender	a reasonably prudent prime residential mortgage lender lending to borrowers in England, Wales and Scotland who generally satisfy the lending criteria of traditional sources of residential mortgage capital
receiver	a receiver appointed by the issuing entity security trustee or the Funding 1 security trustee (as applicable) pursuant to the issuing entity deed of charge or the Funding 1 deed of charge (as applicable)
record date	has the meaning given to that term in Condition 6.7
redemption amount	has the meaning given to that term in Condition 5.
reference rate	in respect of any series and class of notes, the rate specified as such for such notes in the applicable final terms
Reg S global notes	has the meaning given to that term in Condition 19
Reg S notes	each series and class of notes that are sold outside the United States to non-US persons in reliance on Regulation S
register	the register of noteholders kept by the registrar and which records the identity of each noteholder and the number of notes that each noteholder owns
registrar	Deutsche Bank Trust Company Americas
regulated mortgage contract	has the meaning given to that term on page 52
Regulation S	Regulation S under the Securities Act
reinstatement	in relation to a property that has been damaged, repairing or rebuilding that property to the condition that it was in prior to the occurrence of the damage
related security	in relation to a loan, the security for the repayment of that loan including the relevant mortgage and all other matters applicable thereto acquired as part of the portfolio sold to the mortgages trustee
relevant accumulation amount	the amount of funds to be accumulated over a cash accumulation period in order to repay a bullet loan tranche or a scheduled amortisation instalment on its scheduled repayment date whether or not actually repaid on that scheduled repayment date
relevant calculation date	has the meaning given to that term on page 104
relevant closing date	in respect of a series and class of notes, the closing date specified in the applicable final terms



relevant screen page	in respect of any series and class of notes, the screen page specified as such for such notes in the applicable final terms (or such replacement page on the relevant service which displays the information)
relevant share calculation date	the calculation date at the start of the most recently completed calculation period
remarketing agent	has the meaning given to that term on page 13
remarketing termination event	has the meaning given to that term on page 278
reorganisation date	17 September 2007
repayment requirement	has the meaning given to that term on page 110
repayment tests	Rules (1) and (2) under “ <b>Cashflows – Distribution of Funding 1 available principal receipts</b> ” above
resolution	has the meaning given to such term in Condition 11.1
required subordinated loan tranche principal amount outstanding	has the meaning given to such term on page 163
revenue ledger	the ledger(s) of such name created and maintained by the cash manager on behalf of the mortgages trustee pursuant to the cash management agreement to record revenue receipts on the loans and interest from the mortgages trustee GIC account and payments of revenue receipts from the mortgages trustee GIC account to Funding 1 and the seller on each distribution date. The revenue ledger and the principal ledger together reflect the aggregate of all amounts of cash standing to the credit of the mortgages trustee GIC account
revenue receipts	amounts received by the mortgages trustee in the mortgages trustee GIC account in respect of the loans other than principal receipts
right-to-buy loan	a loan made to a borrower in connection with the purchase by such borrower of properties from local authorities or certain other landlords under right-to-buy schemes
Rule 144A	Rule 144A under the Securities Act
Rule 144A global note	has the meaning given to that term in Condition 19
Rule 144A notes	each series and class of notes which are sold in the United States only to QIBs
sale date	the date on which any new loans are sold to the mortgages trustee in accordance with the terms of the mortgage sale agreement
scheduled amortisation instalment	in respect of each rated loan tranche that is a scheduled amortisation loan tranche and in respect of the corresponding series and class of scheduled redemption notes, the instalment amounts specified as applying to such loan tranche and related series and class of notes in the applicable loan tranche supplement and final terms
scheduled amortisation loan tranche	any rated loan tranche that is scheduled to be repaid in more than one instalment on more than one Funding 1 interest payment date, namely those rated loan tranches designated as a scheduled amortisation loan tranches in the applicable loan tranche supplement and final terms.  the scheduled amortisation loan tranches will be deemed to be pass through loan tranches on the earlier to occur of a pass through trigger event and the step up date (if any) in relation to such rated loan tranche
scheduled amortisation repayment restrictions	has the meaning given to that term on page 147

scheduled redemption dates	in respect of a series and class of notes, the interest payment dates, if any, specified in the applicable final terms, for the payment of principal, subject to the terms and conditions of the notes
scheduled redemption notes	any series and class of notes scheduled to be repaid in full in two or more instalments on scheduled redemption dates. Scheduled redemption notes will be deemed to be pass-through notes in certain circumstances
scheduled repayment dates	in respect of a loan tranche, the Funding 1 interest payment dates specified as such in the applicable loan tranche supplement and final terms, for the repayment of the scheduled amortisation instalments
Scottish declarations of trust	the declarations of trust granted and to be granted by the seller in favour of the mortgages trustee pursuant to the mortgage sale agreement transferring the beneficial interest in Scottish loans to the mortgages trustee
Scottish loan	a loan secured by a Scottish mortgage
Scottish mortgage	a mortgage secured over a property in Scotland
Scottish mortgage conditions	the mortgage conditions applicable to Scottish loans
screen rate determination	has the meaning given to that term in Condition 4.2(b)
SEC	The United States Securities and Exchange Commission
Securities Act	United States Securities Act of 1933, as amended
securitisation tax regime	has the meaning given to that term on pages 14 and 57
self-certification loans	has the meaning given to that term on page 78
seller	initially Halifax and since the reorganisation date Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006)
seller's policy	the originating, underwriting, administration, arrears and enforcement policy applied by Birmingham Midshires from time to time to loans and their related security owned solely by the seller
seller rating downgrade	means the seller's long-term, unsecured, unsubordinated and unguaranteed debt obligations are rated below A3 by Moody's (unless Moody's confirms that its then current ratings of the notes will not be downgraded, withdrawn or qualified as a consequence of such rating of the seller)
seller share	the seller share of the trust property from time to time, as calculated in accordance with the mortgages trust deed on each calculation date
seller share percentage	the seller share percentage of the trust property from time to time, as calculated in accordance with the mortgages trust deed on each calculation date
semi-detached	a house joined to another house on one side only
series	has the meaning given to that term in Condition 19
servicer	Bank of Scotland (as successor to Halifax pursuant to the HBOS Group Reorganisation Act 2006), or such other person as may from time to time be appointed as servicer of the portfolio pursuant to the servicing agreement
servicer termination event	has the meaning given to that term on page 91
servicing agreement	the agreement entered into on the programme date between the servicer, the mortgages trustee, the seller, the Funding 1 security trustee and Funding 1 (as the same may be amended, restated, supplemented, replaced or novated from time to time), under which the servicer agrees to

	administer the loans and their related security comprised in the portfolio, as described further in “ <b>The servicing agreement</b> ” above
shortfall	the deficiency of Funding 1 available revenue receipts on a Funding 1 interest payment date over the amounts due by Funding 1 under the Funding 1 pre-enforcement revenue priority of payments
short-term obligations	has the meaning given to that term on page 268
specified currency	has the meaning given to that term in Condition 19
specified currency exchange rate	has the meaning given to that term in Condition 19
specified denomination	has the meaning given to that term in Condition 19
specified office	has the meaning given to that term in Condition 19
staff loan	a loan advanced to an employee of the seller
Standard & Poor’s or S&P	Standard & Poor’s Rating Services, a division of The McGraw-Hill Companies, Inc. and any successor to its ratings business
standard variable rate	the variable mortgage rate set by Birmingham Midshires which applies both to loans beneficially owned by Birmingham Midshires on Birmingham Midshires’ residential mortgage book and those sold to the mortgages trustee
standard variable rate loan	a loan where the interest rate payable by the borrower varies in accordance with the standard variable rate
start-up loan tranche	a loan tranche made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of the advance by the issuing entity start-up loan provider or a new issuing entity start-up loan provider to the issuing entity of an issuing entity start-up loan
step-up date	(i) in relation to a rated loan tranche, the Funding 1 interest payment date on which the interest rate on the relevant loan tranche under the intercompany loan agreement increases by a pre-determined amount and (ii) in relation to a series and class of the notes, the interest payment date on which the interest rate on the relevant series and class of notes increases by a pre-determined amount as specified in the applicable final terms
sterling notes	each series and class of notes denominated in sterling
sub-unit	with respect to any currency other than sterling, the lowest amount of such currency that is available as legal tender in the country of such currency and, with respect to sterling, one pence
sub-prime loan	a loan categorised as such by Birmingham Midshires
subordinated loan principal deficiency sub-ledger	a sub-ledger on the Funding 1 principal deficiency ledger which specifically records any principal deficiency in respect of the subordinated loan tranches
subordinated loan tranche	a loan tranche made by the issuing entity to Funding 1 under the intercompany loan agreement from the proceeds of the advance by the issuing entity subordinated loan provider or a new issuing entity subordinated loan provider to the issuing entity of an issuing entity subordinated loan
subscription agreement	an agreement supplemental to the programme agreement in or substantially in the form set out in the programme agreement or such other form as may be agreed between the issuing entity and the relevant dealer(s) and/or any new dealer(s) and/or manager(s) appointed to the programme and/or in respect of the relevant issuance of notes

swap agreements	the Funding 1 swap agreement and the issuing entity swap agreements and a <b>swap agreement</b> means any one of them
swap early termination event	a circumstance in which a swap agreement can be terminated prior to its scheduled termination date
swap providers	the Funding 1 swap provider and the issuing entity swap providers and a <b>swap provider</b> means any one of them
TARGET business day	a day on which the Trans-European Automated Real-time Gross settlement Express Transfer (TARGET and TARGET 2) System is open
TARGET system	has the meaning given to that term in Condition 4.2(a)
tender agent	in respect of any series and class of remarketable notes, the tender agent specified in the applicable final terms
terraced	a house in a row of houses built in one block in a uniform style
third party amounts	includes: <ul style="list-style-type: none"> <li>(a) amounts under a direct debit which are repaid to the bank making the payment if such bank is unable to recoup that amount itself from its customer's account;</li> <li>(b) payments by borrowers of any fees and other charges which are due to the seller; or</li> <li>(c) recoveries in respect of amounts deducted from loans as described in paragraphs (1) to (4) in "<b>The mortgages trust – Funding 1 share</b>" above, which shall belong to and be paid to Funding 1 and/or the seller as described therein</li> </ul>
tracker rate	the rate of interest applicable to a tracker rate loan (before applying any cap or minimum rate)
tracker rate loan	a loan where interest is linked to a variable interest rate other than the standard variable rates. The rate on tracker rate loans is currently set at a margin by reference to rates set by the Bank of England
transaction documents	the documents listed in (D) under " <b>Listing and general information – documents available</b> " and any other documents designated as such by the Funding 1 security trustee or the issuing entity security trustee
transfer agent	Deutsche Bank Trust Company Americas
transfer date	the date that a portable loan is transferred to a new property
trigger event	an asset trigger event and/or a non-asset trigger event
trust property	has the meaning given to that term on page 1
UK Listing Authority	the FSA in its capacity as competent authority under Part VI of the FSMA
UK share trustee	SFM Corporate Services Limited
underpayment	in the case of flexible loans, a payment made by a borrower in an amount less than the monthly payment then due on the loan being a sum not exceeding the aggregate of any previous overpayments
United States holder	a beneficial owner of Rule 144A notes who is for US federal income tax purposes: <ul style="list-style-type: none"> <li>(a) a citizen or resident of the United States;</li> <li>(b) a corporation (or other entity treated as a corporation) or partnership created or organised in or under the laws of the United States or any state</li> </ul>

thereof (including the District of Columbia);

(c) any estate, the income of which is subject to US federal income tax regardless of the source of its income; or

(d) any trust if (i) a court within the United States is able to exercise primary supervision over the administration of the trust and (ii) one or more US persons have the authority to control all substantial decisions of the trust

US person	has the meaning given to that term in Regulations S
US paying agent	Deutsche Bank Trust Company Americas
US tax counsel	has the meaning given to that term on page 267
UTCCR	the Unfair Terms in Consumer Contracts Regulations 1999 as amended together with (insofar as applicable) the Unfair Terms in Consumer Contracts Regulations 1994
valuation	a methodology for determining the value of a property which would meet the standards of a reasonable, prudent mortgage lender
valuation fee	a fee incurred by borrowers as a result of the seller or servicer obtaining a valuation of the property
VAT	value added tax imposed by the Value Added Tax Act 1994 and legislation and regulations supplemental thereto and any other tax of a similar fiscal nature whether imposed in the United Kingdom (instead of or in addition to value added tax) or elsewhere from time to time
WAFF	has the meaning given to that term on page 95
WALS	has the meaning given to that term on page 95
withholding tax	a tax levied under UK law, as further described in “ <b>United Kingdom taxation – Payment of interest on the notes</b> ” above
zero coupon note	has the meaning given to that term on page 11

## **Index of Appendices**

The following appendices contain the text of the auditors' reports on each of the issuing entity and Funding 1, received by the directors of the issuing entity and Funding 2 respectively from the auditors to the issuing entity and Funding 1, being, in each case, KPMG Audit Plc. The information contained in the appendices constitutes an integral part of the base prospectus. The first statutory accounts of each of the issuing entity and Funding 1 have been prepared and were drawn up to 31st December 2007. KPMG Audit Plc has made reports under Section 235 of the Companies Act 1985 in respect of the each of these statutory accounts. The accounting reference date for each of the issuing entity and Funding 1 will be the last day of December and the next statutory accounts for each of the issuing entity and Funding 1 will be drawn up to 31st December 2008 and annually on the last day of December thereafter.

### **Index of Appendices**

Appendix A	Financial statements of Pendeford Master Issuer PLC
Appendix B	Financial statements of Pendeford Funding (No. 1) Limited

**ANNEX A**

**Registered Number 6121308**

**PENDEFORD MASTER ISSUER PLC  
DIRECTORS' REPORT AND FINANCIAL STATEMENTS  
FOR THE PERIOD FROM INCORPORATION TO 31 DECEMBER 2007**

**PENDEFORD MASTER ISSUER PLC**  
**DIRECTORS' REPORT AND FINANCIAL STATEMENTS**  
**CONTENTS**

	<b>Page</b>
Directors and Company Information	2
Directors' Report	3-7
Statement of Directors' Responsibilities	8
Independent Auditors' Report to the Members of Pendeford Master Issuer PLC	9-10
Income Statement	11
Balance Sheet	12
Cash Flow Statement	13
Notes to the Financial Statements	14-33



**PENDEFORD MASTER ISSUER PLC  
DIRECTORS AND COMPANY INFORMATION**

**DIRECTORS**

David Balai (appointed 21 February 2007)  
SFM Directors Limited (appointed 21 February 2007)  
SFM Directors (No. 2) Limited (appointed 21 February 2007)

**SECRETARY**

SFM Corporate Services Limited (appointed 21 February 2007)

**REGISTERED OFFICE**

35 Great St. Helen's  
LONDON  
EC3A 6AP

**AUDITORS**

KPMG Audit Plc  
1 The Embankment  
Neville Street  
LEEDS  
LS1 4DW

## **PENDEFORD MASTER ISSUER PLC DIRECTORS' REPORT**

The directors present their report and the audited financial statements for the period ended 31 December 2007.

### **INCORPORATION**

Pendeford Master Issuer PLC (the "Company") was incorporated in England and Wales on 21 February 2007 as a public limited company under the Companies Act 1985. The Company began trading on 12 April 2007.

### **ACCOUNTING REFERENCE DATE**

It was resolved on 21 February 2007 that the first accounting reference date of the Company be amended from 29 February 2008 to 31 December 2007. These are the first statutory financial statements prepared for the Company and cover the period from incorporation to 31 December 2007.

### **BUSINESS REVIEW**

#### **Principal activity**

The principal activity of the Company is to issue publicly listed floating and fixed rate notes denominated in US Dollars, Euros and Sterling in the international capital markets (the "Notes"), and to enter into certain related financial arrangements in order to fund the activities of the Pendeford Holdings Limited Group by means of inter-company loans.

The activities of the Company and the Pendeford Holdings Limited Group (see below) are conducted primarily by reference to a series of securitisation transaction documents (the "Programme Documentation"). The securitisation structure has been established as a means of raising finance for Bank of Scotland plc ("BOS"), a subsidiary undertaking of HBOS plc.

On 17 September 2007 the HBOS Group Reorganisation Act 2006 took effect. This brought together four of HBOS plc's main UK banking businesses (Halifax plc, The Governor and Company of the Bank of Scotland, Capital Bank plc and HBOS Treasury Services plc) into a single legal entity, Bank of Scotland plc.

The principal activity of the Company is unaffected by the reorganisation of HBOS plc. BOS now provides cash manager services defined under the Programme Documentation.

#### **Business structure**

The Company is a wholly-owned subsidiary of Pendeford Holdings Limited, a company registered in England and Wales. The shares of Pendeford Holdings Limited are held on a discretionary trust basis by SFM Corporate Services Limited.

**PENDEFORD MASTER ISSUER PLC  
DIRECTORS' REPORT (CONT'D)**

**BUSINESS REVIEW (CONT'D)**

**Business structure (Cont'd)**

At 31 December 2007 the Pendeford Holdings Limited Group (the "Group"), comprised Pendeford Holdings Limited, Pendeford Funding (No 1) Limited ("Funding 1"), Pendeford PECO Limited, and the Company.

Pendeford Holdings Limited holds 49,998, £1 ordinary shares partly paid to £0.25 and 2 £1 ordinary shares, which are fully paid. These shares comprise the entire issued share capital of the Company.

**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". Detailed analysis of the risks facing the Company in relation to its financial instruments and the management of such risks is provided in note 11.

Other risks which may affect the Company's performance are detailed below.

**Operational risks**

In order to meet its obligations to the Noteholders, the Company has entered into contracts with a number of third parties who have agreed to provide operational support to the Company in accordance with the Programme Documentation.

Structured Finance Management Limited has been appointed to provide corporate services in accordance with a corporate services agreement. Other third parties who have agreed to provide services with respect to the Notes include the paying agents, issuing entity swap providers and the agent bank. BOS has been appointed to act as account bank and cash manager on behalf of the Company.

Expenses due to these and other third parties for services provided are paid on behalf of the Company by Funding 1 in priority to other expenses payable by Funding 1 and are paid out of available receipts.

The Company's operations are subject to periodic review by the Internal Audit function of HBOS plc.

**Business risks**

The principal business risks of the Company are reflected in a number of asset and non asset trigger events in the Programme Documentation. The occurrence of trigger events would lead to the early redemption of the Notes in accordance with the established priorities. There have been no such trigger events since inception of the Programme.

**PENDEFORD MASTER ISSUER PLC**  
**DIRECTORS' REPORT (CONT'D)**

**PERFORMANCE**

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. The Company's performance is addressed in the quarterly management accounts provided to the directors and the monthly Trustee Reports issued to investors.

On 12 April 2007 the Company issued £2.5bn of Notes. On the same day, the resultant funds were passed to Funding 1 under the inter-company loan agreement to enable that company to purchase a beneficial interest in the assets held by Pendeford Mortgages Limited (the "Trust").

At the time of issue each series and class of Notes is assigned a credit rating which reflects the likelihood of full and timely payment to the Noteholders of interest on each interest payment date and the payment of principal on the final maturity date. A rating may be subject to revision, suspension or withdrawal at any time by the rating agencies if the Company's circumstances change.

Any change in the credit rating assigned to a Note would be used as an indicator as to the performance of the Company. No downgrade in credit ratings has been applied to the Company's Notes in the period under review.

The Company has made all necessary payments in accordance with the scheduled repayment dates for the period ended 31 December 2007.

The fair value of the Inter-company loan has been stated to take account of the market yields implied by the Note Valuations (see Note 13 (d) Fair Values). However, the underlying mortgage assets within the Trust have performed in line with expectations and, therefore, no impairment is considered necessary.

Profits for the Company are pre-determined under the Programme Documentation. Under the terms of the securitisation the Company retains the right to a profit before tax of up to £5,000 per annum from available revenue receipts from Funding 1. This is reflected in the income statement net of any movements in fair value gains and losses on derivatives.

The Company's tax charge is based on the tax regime for securitisation companies. All fair value adjustments on derivative contracts are ignored for taxation purposes.

The cash flows of the Company with regards to tax liabilities are not impacted by the current accounting policies.

**OTHER INFORMATION**

The Company has employed no staff during the period ended 31 December 2007.

**PENDEFORD MASTER ISSUER PLC**  
**DIRECTORS' REPORT (CONT'D)**

**RESULTS AND DIVIDENDS**

The results for the period are set out on page 11. The loss after taxation for the period, prepared using International Financial Reporting Standards ("IFRSs"), as adopted by the European Union (the "EU"), amounted to £179,000 and will be transferred to reserves. The directors do not recommend the payment of a dividend.

As required under IFRSs, the loss for the period includes a fair value loss on financial instruments of £229,000 which reflects the current market value of the derivatives.

**FUTURE DEVELOPMENTS**

The directors expect that the Company will continue to meet the scheduled repayment dates for the Notes during 2008, based on the relatively low levels of arrears experienced to date on the mortgage loan portfolio which provides the cash to pay the inter-company loans. No changes in business activity are envisaged.

**SUPPLIER PAYMENT POLICY**

It is the Company's policy that payments made to suppliers are made in accordance with those terms and conditions agreed between the Company and its suppliers.

The Company owed no amounts to trade creditors at 31 December 2007.

**DIRECTORS**

The directors who served during the period from incorporation to the end of the period and subsequently were as follows:

David Balai  
SFM Directors Limited  
SFM Directors (No.2) Limited

David Balai, SFM Directors Limited and SFM Directors (No.2) Limited are also directors of Pendeford Holdings Limited.

**GOING CONCERN**

The directors are satisfied that the Company 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 negative reserves are as a result of fair value adjustments made in accordance with IFRSs and are expected to reverse in the future. There was no impact on the cash resources of the Company during the period as a result of these valuation adjustments.

**PENDEFORD MASTER ISSUER PLC  
DIRECTORS' REPORT (CONT'D)**

**AUDIT INFORMATION**

The directors who held office at the date of approval of this Directors' Report confirm that, so far as they each are aware, there is no relevant audit information of which the Company's auditors are unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

**AUDITORS**

The Company's first auditors were appointed by the directors on 21 February 2007. A resolution to re-appoint KPMG Audit Plc as auditors will be presented by the members at the forthcoming Annual General Meeting of the Company.

By Order of the Board

.....

, Director  
SFM Corporate Services Limited Secretary

35 Great St. Helen's  
LONDON  
EC3A 6AP

March 2008

**PENDEFORD MASTER ISSUER PLC**  
**STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE DIRECTORS' REPORT**  
**AND THE FINANCIAL STATEMENTS**

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 Company financial statements for each financial period. Under that law the directors have elected to prepare the Company financial statements in accordance with IFRSs as adopted by the EU.

The Company financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position of the Company and the performance for that period; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing the Company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Directors' Report and a Business Review.

**INDEPENDENT AUDITORS' REPORT  
TO THE MEMBERS OF PENDEFORD MASTER ISSUER PLC**

We have audited the financial statements of Pendeford Master Issuer PLC for the period ended 31 December 2007 which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out therein.

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

**Respective responsibilities of directors and auditors**

The directors' responsibilities for preparing the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 8.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

**Basis of audit opinion**

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

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



## **INDEPENDENT AUDITORS' REPORT**

### **TO THE MEMBERS OF PENDEFORD MASTER ISSUER PLC (CONT'D)**

#### **Opinion**

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Company's affairs as at 31 December 2007 and of its loss for the period then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

#### **KPMG Audit Plc**

Chartered Accountants  
Registered Auditor

1 The Embankment  
Neville Street  
LEEDS  
LS1 4DW

March 2008

**PENDEFORD MASTER ISSUER PLC**  
**INCOME STATEMENT**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007**

	<b>Note</b>	<b>2007 £000</b>
Interest receivable and similar income	2	114,397
Interest payable and similar charges	3	(114,396)
		1
<b>Net interest income</b>		1
Net fair value losses on derivatives		(229)
Income from Group undertaking	4	4
		(224)
<b>Loss before tax for the period</b>		(224)
Income tax credit	5	45
		(179)
<b>Loss after tax for the period</b>		(179)
		(179)
<b>Loss attributable to equity holders</b>		(179)

The loss 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 statement of recognised income and expense has been omitted from the financial statements for the period ended 31 December 2007 as there was no income or expense recognised directly in equity in the period.

Notes 1 to 13 form part of these financial statements.

**PENDEFORD MASTER ISSUER PLC**  
**BALANCE SHEET AS AT 31 DECEMBER 2007**

	Note	2007 £000
<b>Assets</b>		
Loans to Group undertaking	6	2,163,184
Deferred tax asset	7	46
<b>Total non-current assets</b>		2,163,230
Loans to Group undertaking	6	428,440
Derivative asset		67,128
Cash and cash equivalents	8	18
<b>Total current assets</b>		495,586
<b>Total assets</b>		2,658,816
<b>Equity</b>		
Issued capital		13
Retained earnings		(179)
<b>Total equity</b>	9	(166)
<b>Liabilities</b>		
Interest-bearing loans and borrowings	10	2,202,284
<b>Total non-current liabilities</b>		2,202,284
Interest-bearing loans and borrowings	10	430,555
Derivative liability		26,142
Current tax liability	5	1
<b>Total current liabilities</b>		456,698
<b>Total liabilities</b>		2,658,982
<b>Total equity and liabilities</b>		2,658,816

These financial statements were approved by the Board of Directors on March 2008 and were signed on its behalf by:

per pro  
SFM Directors Limited  
as Director

Notes 1 to 13 form part of these financial statements.

**PENDEFORD MASTER ISSUER PLC**  
**CASH FLOW STATEMENT**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007**

<b>Indirect method</b>	<b>Note</b>	<b>2007</b> <b>£000</b>
<b>Cash flows from operating activities</b>		
Loss before tax for period		(224)
<i>Adjustments for:</i>		
Interest receivable on inter-company loans	2	(114,396)
Bank interest	2	(1)
Interest payable on Notes	3	94,538
Swap interest payable	3	16,620
Start up loan interest payable	3	3,238
Net fair value losses on derivatives		229
		4
<b>Operating profit before changes in working capital and provisions</b>		
		4
<b>Cash generated from the operations</b>		
Income taxes paid		-
		4
<b>Net cash from operating activities</b>		
		4
<b>Cash flows from investing activities</b>		
Inter-company loans		(2,573,400)
Inter-company loans repaid		3,916
Interest received on inter-company loans		92,257
		(2,477,227)
<b>Net cash flows from investing activities</b>		
		(2,477,227)
<b>Cash flows from financing activities</b>		
Proceeds from the issue of share capital		13
Notes proceeds		2,507,600
Start up loan		65,800
Repayment of start up loan		(3,916)
Interest paid on Notes		(78,147)
Swap interest paid		(11,476)
Interest paid on start up loan		(2,633)
		2,477,241
<b>Net cash from financing activities</b>		
		2,477,241
<b>Net increase in cash and cash equivalents</b>		
Cash and cash equivalents at incorporation		-
		18
<b>Cash and cash equivalents at 31 December</b>	<b>8</b>	<b>18</b>

As explained in the accounting policies in note 1, the use of cash is restricted in accordance with the Programme Documentation.

Notes 1 to 13 form part of these financial statements.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007**

**1. SIGNIFICANT ACCOUNTING POLICIES**

Pendeford Master Issuer PLC is a company domiciled in England.

**(a) Statement of compliance**

The financial statements for the period ended 31 December 2007 have been prepared in accordance with International Financial Reporting Standards (IFRSs) and its interpretations as endorsed by the EU and effective at 31 December 2007.

The accounting policies set out below have been applied in respect of the financial period ended 31 December 2007. IFRS 7 "Financial Instruments: Disclosures" became effective for all accounting periods ending on or after 1 January 2007. The principles in this standard complement the principles for recognising, measuring and presenting financial assets and liabilities in IAS 32 "Financial Instruments: Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement".

Adoption of the Capital disclosure amendment to IAS 1 "Presentation of Financial Statements" became mandatory for all accounting periods ending on or after 1 January 2007. The adoption of this amendment has had no quantitative impact on the financial data presented in the financial statements. Additional disclosure is presented in the total equity note.

The financial statements also comply with the relevant provisions of Part VII of the Companies Act 1985, as amended by the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004.

**(b) Basis of preparation**

The financial statements are presented in Sterling and rounded to the nearest thousand.

The financial statements have been prepared on the historical cost basis (except that derivative financial instruments are stated at their fair value), and on a going concern basis.

This is the first period of account for the Company and, therefore, there are no prior period comparatives included within the financial statements.

The preparation of the financial statements necessarily requires the exercise of judgement both in the application of accounting policies which are set out in the sections below and in the selection of assumptions used in the calculation of estimates. These estimates and judgements are reviewed on an ongoing basis and are continually evaluated based on historical experience and other factors. However, actual results may differ from these estimates. The most significantly affected components of the financial statements and associated critical judgements are as follows:

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(b) Basis of preparation (cont'd)**

Effective Interest Rate – In calculating the effective interest rate of financial instruments the Company takes into account interest received or paid, fees and commissions paid or received, expected early redemptions and related penalties and premiums and discounts on acquisition or issue that are integral to the yield as well as incremental transaction costs.

For the purpose of the effective yield calculation, it has been assumed that the average expected life of the Notes in issue will end at the date of the first step-up in interest rates, based on the payment experience to date. This may not be the case in practice.

The swaps which have been purchased to hedge interest rate and currency risks arising on the Notes have been valued by discounting future cash flows. The valuation method is consistent with commonly used market techniques. All inputs into valuation models adopted by the Company are obtained from observable market data.

**(c) Financial instruments**

The Company's financial instruments principally comprise loans to Funding 1, cash and liquid resources, derivatives and interest-bearing borrowings that arise directly from its operations. The main purpose of these financial instruments is to raise finance for BOS. The Company issues publicly listed floating and fixed notes in the international capital markets. These financial instruments are classified in accordance with the principles of IAS 39 as described below.

**(c)(i) Loans to Group undertaking**

The loans to Funding 1 are 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 loans are 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 loans will be significantly reduced.

**(c)(ii) Cash and cash equivalents**

The Company holds bank deposits. These accounts are held in the Company's name and meet the definition of cash and cash equivalents but their use 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 recorded using the effective interest method.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(c)(iii) Derivative financial instruments**

IAS 39 requires all derivative financial instruments to be recognised initially at fair value on the balance sheet and to be remeasured 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 gain or loss on remeasurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged. Where a fair value hedge is documented, the fair value movements of the swap may be offset in the income statement against the fair value movements for the risk being hedged on the hedged item.

The Company uses derivative financial instruments to hedge its exposure to interest rate risk and currency risk arising from operational, financing and investment activities. In accordance with its treasury policy, the Company 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.

The Company's interest rate and currency swaps have been designated as fair value hedges of the Notes and formal hedge documentation has been established at inception in compliance with IAS 39.

The subsequent gain or loss on remeasurement of the swaps to fair value has been recognised immediately in net fair value gains and losses on derivatives in the income statement, together with the fair value hedge adjustment to the Notes. Interest receivable or payable on the interest rate and currency swaps is accounted for on an accruals basis within interest receivable or payable in the income statement.

The fair value of interest rate and currency swaps is the estimated amount that the Company would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

**(c)(iv) Interest-bearing borrowings**

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing 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.

**(c)(v) 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.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(c)(vi) Foreign currency**

Assets and liabilities are translated at the rates of exchange ruling on the balance sheet date. The retranslation amounts on currency swaps and the associated Notes are charged or credited to net fair value gains and losses on derivatives.

**(c)(vii) Offsetting of financial assets and liabilities**

A financial asset and a financial liability is offset and the net amount is reported in the balance sheet if the Company has a legally enforceable right to set-off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

**(d) Impairment**

The carrying amounts of the Company's assets other than deferred tax assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated. An impairment loss is recognised in the income statement whenever the carrying amount of the asset exceeds its recoverable amount.

**(e) Value added tax**

Value added tax is not recoverable by the Company and is included with its related cost.

**(f) Income tax**

Income tax on the profit or loss for the period comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Temporary differences arising from the initial recognition of assets and liabilities that affects neither accounting nor taxable profit are not provided for. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates at the balance sheet date.

The Company's tax charge is based on the tax regime for securitisation companies. All fair value adjustments on derivative contracts are ignored for taxation purposes.

Under special rules issued by HM Revenue & Customs for securitisation companies, the Company's charge for taxation for 2007 was based on its taxable profits calculated on a UK GAAP basis but disclosed in accordance with IAS 12 "Income Taxes".

**(g) Related parties**

In accordance with the provisions of IAS 24 "Related Party Disclosures", the Company has disclosed details of transactions with its related parties, including those with Group companies.



**PENDEFORD MASTER ISSUER PLC  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(h) Other payables**

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

**(i) Income from Group undertaking**

Under the terms of the inter-company agreement with Funding 1, the Company has the right to receive a fee for the provision of the inter-company loans. This fee includes an amount up to £5,000 per annum, together with an amount equivalent to payments made to certain third party suppliers for ongoing expenses.

**(j) New accounting standards and interpretations**

The following standards and interpretations have been adopted by the EU but are not effective for the period ended 31 December 2007 and have not been applied in preparing the financial statements:

IFRS 8 "Operating Segments" which is applicable for periods commencing on or after 1 January 2009. The application of this standard in 2007 would not have had any financial impact as it is only concerned with disclosure.

The following standards and interpretations have not yet been adopted by the EU, are not effective for the period ended 31 December 2007 and have not been applied in preparing the financial statements:

IAS 1 "Presentation of Financial Statements" which is effective for periods commencing on or after 1 January 2009. The application of this revised standard in 2007 would not have had a material impact on the financial statements.

**2. INTEREST RECEIVABLE AND SIMILAR INCOME**

	<b>2007 £000</b>
Interest on inter-company loans	114,396
Bank interest	1
	114,397

Interest receivable on the inter-company loans and bank deposits is calculated using the effective interest method.

As the inter-company loans in total are not regarded as impaired, the interest received on impaired assets is £ nil.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**3. INTEREST PAYABLE AND SIMILAR CHARGES**

	<b>2007</b> <b>£000</b>
On Notes:	
<b>Issue 2007-1</b>	
Series 1 Class A Floating Rate Notes 2008	15,359
Series 1 Class B Floating Rate Notes 2059	281
Series 1 Class C Floating Rate Notes 2059	291
Series 2 Class A Floating Rate Notes 2016	11,088
Series 3 Class A Floating Rate Notes 2016	29,395
Series 3 Class B Floating Rate Notes 2059	3,614
Series 3 Class C Floating Rate Notes 2059	3,773
Series 4 Class A Floating Rate Notes 2037	16,824
Series 4 Class B Floating Rate Notes 2059	281
Series 4 Class C Floating Rate Notes 2059	295
Series 5 Class A Floating Rate Notes 2022	13,337
	94,538
Swap interest payable	16,620
Start up loan interest	3,238
	114,396

Interest payable on the Notes is calculated using the effective interest method.

**4. ANALYSIS OF INCOME STATEMENT**

	<b>2007</b> <b>£000</b>
Income from Group undertaking	4

Under the terms of the inter-company agreement with Funding 1, the Company has the right to receive a fee for the provision of the inter-company loans. This fee includes an amount up to £5,000 of the interest receivable on the inter-company loans, together with an amount equivalent to payments made to certain third party suppliers for ongoing expenses.

This fee is not included in determining the effective interest rate arising on the inter-company loans that are held at amortised cost.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**5. INCOME TAX EXPENSE**

	<b>2007</b> <b>£000</b>
<b>Current Tax</b>	
Corporation tax charge for the period at a rate of 20%	(1)
<b>Deferred tax</b>	
Deferred tax credit for the period at a rate of 20%	46
	45
Total income tax credit in income statement	45

	<b>2007</b> <b>£000</b>
<b>Reconciliation of effective tax rate</b>	
Loss before tax	224
Loss before tax multiplied by the small company's rate of corporation tax in the UK (20%)	45
Effects of:	
Items not allowable under securitisation tax rules	(46)
Deferred tax provided	46
	45
Total income tax credit in income statement	45

The current tax liability of £1,000 represents the amount of income tax payable in respect of the current period. No payments on account have been made during the period.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**6. LOANS TO GROUP UNDERTAKING**

	<b>2007</b> <b>£000</b>
<b>Inter-company loans</b>	
Acquisitions	2,573,400
Redemptions	(3,916)
	2,569,484
Accrued interest receivable	22,140
	2,591,624
 Analysed as follows:	
Non-current assets	2,163,184
Current assets	428,440
	2,591,624

The inter-company loans to Funding 1 are all denominated in Sterling and are at variable rates of interest, based on LIBOR for three-month Sterling deposits. Such loans have ultimately been secured against a beneficial interest in a mortgage portfolio held in trust on behalf of the Group.

Funding 1's ability to pay amounts due on the inter-company loans will depend mainly upon it receiving sufficient revenue receipts and principal from Pendeford Mortgages Trustee Limited; receiving the required funds from the Funding 1 swap provider; and amounts available in the reserve funds. In the case of a shortfall, holders of the Notes may, subject to what other sources of funds are available to the Company, receive less than the full interest and/or principal than would otherwise be due on the Notes. The repayment of the inter-company loans will coincide with the repayment of the Notes.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**7. DEFERRED TAX ASSET**

	<b>2007</b> <b>£000</b>
Credit to income for the period	46
	<hr/>
Balance carried forward as at 31 December	46
	<hr/> <hr/>

The deferred tax asset of £46,000 represents the amount of deferred tax deductible in respect of the derivative financial instruments and the fair value hedge adjustment of £229,000, which is a temporary timing difference and, therefore, expected to reverse.

There were no unrecognised deferred tax assets or liabilities as at 31 December 2007.

**8. CASH AND CASH EQUIVALENTS**

The Company is contractually entitled to a variable rate of interest on its bank accounts of 0.25 per cent per annum below LIBOR for three-month Sterling deposits.

	<b>2007</b> <b>£000</b>
Cash and cash equivalents in the cash flow statement	18
	<hr/> <hr/>

**PENDEFORD MASTER ISSUER PLC  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**9. TOTAL EQUITY**

**Reconciliation of movement in capital and reserves**

	<b>Share capital</b>	<b>Retained earnings</b>	<b>Total equity</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>
At Incorporation	13	-	13
Total recognised income and expense	-	(179)	(179)
	<hr/>	<hr/>	<hr/>
At 31 December 2007	13	(179)	(166)
	<hr/>	<hr/>	<hr/>

There are 50,000 authorised ordinary shares of £1 each. The issued share capital comprises two ordinary shares of £1 each, which are fully paid up and 49,998 ordinary shares, which are one quarter paid up.

**Capital disclosures**

The Company is not subject to externally imposed capital requirements in the current period other than the minimum share capital required by the Companies Act with which it complies. The Company manages its ordinary share capital in order that there is sufficient capital, in the opinion of the directors, to support the transactions and level of business undertaken by the Company.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**10. INTEREST-BEARING LOANS AND BORROWINGS**

This note provides information about the contractual terms of the Company's interest-bearing loans and borrowings. For more information about the Company's exposure to risk, see note 11.

<b>Non-current liabilities</b>	<b>Note</b>	<b>2007 £000</b>
<b>Issue 2007-1</b>		
Series 1 Class B Floating Rate Notes 2059	(a)	7,270
Series 1 Class C Floating Rate Notes 2059	(a)	7,270
Series 2 Class A Floating Rate Notes 2016	(b)	339,900
Series 3 Class A Floating Rate Notes 2016	(a)	761,810
Series 3 Class B Floating Rate Notes 2059	(c)	81,300
Series 3 Class C Floating Rate Notes 2059	(c)	81,300
Series 4 Class A Floating Rate Notes 2037	(b)	509,850
Series 4 Class B Floating Rate Notes 2059	(c)	6,300
Series 4 Class C Floating Rate Notes 2059	(c)	6,300
Series 5 Class A Floating Rate Notes 2022	(c)	<u>300,000</u>
		2,101,300
Start up loan from BOS	(c)	61,884
Fair value of Notes hedge adjustment		(116)
Fair value of Notes currency adjustment		<u>39,216</u>
		<u>2,202,284</u>
<b>Current liabilities</b>	<b>Note</b>	<b>2007 £000</b>
<b>Issue 2007-1</b>		
Series 1 Class A Floating Rate Notes 2008	(d)	406,300
Interest payable on Notes		16,089
Interest payable on Start up loan		605
Fair Value of Notes hedge adjustment		(22)
Fair Value of Notes currency adjustment		<u>7,583</u>
		<u>430,555</u>

**Notes:**

- (a) Interest is payable at a variable rate based on three-month USD LIBOR.
- (b) Interest is payable at a variable rate based on three-month EURIBOR.
- (c) Interest is payable at a variable rate based on three-month Sterling LIBOR.
- (d) Interest is payable at a variable rate based on one-month USD LIBOR.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**10. INTEREST-BEARING LOANS AND BORROWINGS (CONT'D)**

The Notes are denominated in the following currencies:

	<b>2007</b> <b>£000</b>
US Dollars	1,182,650
Euros	849,750
Sterling	475,200
Fair value of Notes hedge adjustment	(138)
Fair value of Notes currency adjustment	49,799
	2,554,261
	2,554,261

These Notes are the floating rate Notes issued by the Company to fund the Company's operations.

The Notes are ranked in accordance with the rating assigned; a class A Note ranking in priority to a class B Note and each subsequent Note class ranking in priority to the next, subject to the terms and conditions of the Notes, the Issuer cash management agreement and the deed of charge to which the Company is a party. Within each class of Note there is no preference or priority between them unless such an event occurs as to trigger an enforcement of the security of the Notes. In such an event (subject to redemption dates) each Note will rank in priority as set down in the Programme Documentation.

No assurance is given as to the amount (if any) of interest and principal on any of the Notes which may actually be paid on any interest payment date.

The Notes will be obligations of the Company only. The Notes will not be obligations of, or the responsibility of, or guaranteed by, any person other than the Company.

The Company's obligations to Noteholders and to other secured creditors are secured under a deed of charge, which grants security over all of its assets in favour of the security trustee.

The principal assets of the Company are loans made by it to Funding 1, a Group company. This company's obligations in respect of these loans are secured pursuant to a deed of charge which grants security over all its assets, primarily consisting of its beneficial interest in a portfolio of residential mortgage loans, in favour of the security trustee. The security trustee holds this security for the benefit of all secured creditors of Funding 1, including the Company.

Incidental costs of obtaining loan finance represent legal and professional costs incurred to date less amounts written off to the income statement. Under the terms of the Programme Documentation these costs are included and amortised within the accounts of Funding 1.



**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. FINANCIAL INSTRUMENTS**

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 principally comprise loans to Funding 1, cash and liquid resources, derivatives ("swaps") and interest-bearing borrowings (the "Notes") that arise directly from its operations.

The principal risks arising from the Company's financial instruments are credit risk, interest rate risk and currency risk. Further detailed analysis of the risks facing the Company in relation to its financial instruments is provided below.

As noted in the Directors' Business Review, the activities of the Company and the Group are conducted primarily by reference to a series of securitisation transaction documents (the "Programme Documentation"). The securitisation structure has been established as a means of raising finance for BOS, a subsidiary undertaking of HBOS plc and no business activities will be undertaken by the Company beyond those set out in the Programme Documentation.

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 is clearly defined and documented. Cash flow modelling, including multiple stress scenarios, is carried out as part of the structuring of the transaction, and as such is required by the rating agencies. In addition, derivative contracts are entered into as part of the securitisation transaction to hedge all interest rate and currency risk arising in the transaction including the obligations under the Notes. The derivative counterparties are selected as highly rated, regulated financial institutions and this reduces the risk of default and loss for the Company. Additional credit protection is afforded by the requirement for the derivative counterparties to post collateral in the event of a downgrade to a counterparty's credit rating.

Following initial set-up, the directors monitor the Company's performance, reviewing monthly reports on the performance of the Trust property and the quarterly management accounts. Such review is designed to ensure that the terms of the Programme Documentation have been complied with, that no unforeseen risks have arisen and that the Noteholders have been paid on a timely basis.

**11(a) Credit risk**

The ability of the Company to meet its obligations to make principal and interest payments on the Notes and to meet its operating and administrative expenses is dependent on funds being received under the inter-company loans with Funding 1. Funding 1 is only obliged to pay interest and principal to the Company to the extent that it has such amounts available to it. The Company has recourse to the other assets of Funding 1 for any shortfall in receipts due under the inter-company loan agreement.

The inter-company loans are ultimately secured against a beneficial interest in a mortgage portfolio held in trust (the "Trust") on behalf of the Group under the terms of the Programme Documentation.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. FINANCIAL INSTRUMENTS (CONT'D)**

**11(a) Credit risk (cont'd)**

A higher or lower than anticipated rate of prepayment on the mortgage portfolio will have a direct impact on the level of interest and principal received by Funding 1. To minimise the impact of these risks any mortgage loan included in the mortgage portfolio must meet a number of strict criteria as set out in the Programme Documentation.

Credit risk also exists on the derivatives that the Company has entered into to manage the interest rate and currency risk arising on the Notes (see 11(b) below). The swap counterparties are all regulated financial institutions.

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 2007 £000	Maximum exposure 2007 £000
<b>Assets held at amortised cost</b>			
Loans to Group undertaking	6	2,591,624	2,591,624
Cash and cash equivalents	8	18	18
<b>Assets held at fair value</b>			
Derivative asset		67,128	67,128
		2,658,770	2,658,770
		2,658,770	2,658,770

**11(b) Market Risk**

Market risk is defined as the potential loss in value or earnings of an organisation arising from changes in external market factors.

The Company is exposed to market risk which comprises interest rate risk and currency risk which are explained in more detail below:

**11(b)(i) Interest rate risk**

Interest rate risk exists where assets and liabilities have interest rates set under a different basis or which reset at different times. The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of the inter-company loans and the Notes (its principal assets and liabilities) are similar; where this is not possible the Company uses derivative financial instruments to mitigate any residual interest rate risk.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. FINANCIAL INSTRUMENTS (CONT'D)**

**11(b)(i) Interest rate risk (cont'd)**

At 31 December 2007, if LIBOR for three-month Sterling deposits at that date had been 25 basis points higher or lower, with all other variables held constant, the net effect on the Company's net margin would be £ nil due to swaps being in place. This would also apply if LIBOR for one-month/three-month Dollar deposits or three-month Euro deposits moved by 25 basis points higher or lower, with all other variables held constant. There would however be some movement in the net fair value gains and losses on derivatives which would alter profit as shown in the tables below due to the revaluation of the Sterling leg of the swaps:

2007	-25bps £000	Per income statement £000	+25bps £000
Net fair value (losses) and gains on derivatives	(832)	(229)	374
	<hr/>	<hr/>	<hr/>

**11(b)(ii) Currency risk**

The Company has issued certain Notes denominated in US Dollars, and Euros ("Currency Notes"). All the Company's assets and its other liabilities are denominated in Sterling. The Company's policy is to eliminate all exposures arising from movements in exchange rates by the use of cross-currency swaps to hedge payments of interest and principal on the Currency Notes.

At 31 December 2007, if Sterling had weakened or strengthened 25% against the Dollar and the Euro with all other variables held constant, the overall effect on the Company's income statement would have been £ nil due to the operation of the currency swaps. There would be no direct effect on equity.

The effect of currency movements has no bearing on net interest income as the interest received on the inter-company loans is based on balances held in Sterling and the interest paid on the Notes is calculated on balances converted at a historic currency rate. The revaluation of these Notes passes through the net fair value gains and losses on derivatives caption in the income statement but this is offset by an equal retranslation on the derivative and the effect on the income statement is therefore £ nil.

**11(c) Liquidity risk**

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at an unacceptably high cost. The Company's ability to meet payments on the Notes as they fall due is dependent on timely receipt of funds under the inter-company loan agreement which may be delayed due to slow repayment on the mortgage portfolio (see 11(a) Credit risk above).

Under certain conditions related to the debt ratings of the seller (BOS), Funding 1 will be required to establish a Liquidity Reserve Fund. In the event that Funding 1 has insufficient funds available to pay interest and/or principal on the inter-company loans then it is obliged to draw on this Liquidity Reserve Ledger to meet its obligations to the Company.

**PENDEFORD MASTER ISSUER PL**  
**C NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. FINANCIAL INSTRUMENTS (CONT'D)**

**11(c) Liquidity risk (cont'd)**

The liquidity tables reflect the undiscounted cash payments which will fall due if the structure continues until the step-up date as defined in the Programme Documentation. It is anticipated that the interest earned on the inter-company loans will be sufficient to allow repayment of the Notes by the step-up date and thereby avoid the increase in the interest rate margin payable on the Notes. The step-up date is the earliest date on which the Company could be required to repay the liability and commercially the most likely.

<b>2007</b>	<b>Carrying Value</b>	<b>Contractual repayment value</b>	<b>Not later than one month</b>	<b>Later than one month and not later than three months</b>	<b>Later than three months and not later than one year</b>	<b>Later than one year and not later than five years</b>
<b>Principal</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>
Notes	2,554,261	2,554,416	-	413,285	367,107	1,774,024
Swap principal payable		2,032,400	-	420,840	339,900	1,271,660
Swap principal receivable		(2,079,216)	-	(413,285)	(367,107)	(1,298,824)
Start up loans	61,884	61,884	-	751	2,339	58,794
<b>Interest payable</b>						
Interest payable on Notes	16,089	364,750	1,910	29,821	84,283	248,736
Swap Interest payable		273,523	-	32,330	77,489	163,704
Swap interest receivable		(218,038)	(1,910)	(22,157)	(61,108)	(132,863)
Interest payable on start up loans	605	19,810	-	1,124	3,294	15,329
	<u>2,632,839</u>	<u>3,009,529</u>	<u>-</u>	<u>462,709</u>	<u>446,197</u>	<u>2,100,560</u>

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. FINANCIAL INSTRUMENTS (CONT'D)**

**11(d) Fair values**

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

	Note	Carrying amount 2007 £000	Fair value 2007 £000
<b>Loans and receivables:</b>			
Loans to Group undertaking	6	<u>2,591,624</u>	<u>2,575,505</u>
<b>Financial assets at fair value</b>			
Derivative asset		<u>67,128</u>	<u>67,128</u>
<b>Financial liabilities held at amortised cost:</b>			
Interest-bearing loans and borrowings	10	<u>2,591,853</u>	<u>2,575,734</u>
<b>Financial liabilities at fair value:</b>			
Derivative liability		<u>26,142</u>	<u>26,142</u>

The following comments summarise the main methods and assumptions used in estimating the fair value of financial instruments that are reflected in the table above.

The fair values included above have been calculated taking into account current market values. For the Notes, these have been calculated by disclosing the expected cash flows by the prevailing market rates for similar debt. The fair value of the assets has been adjusted to take account of the market yields implied by the Note valuations.

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

The Company has currency swaps in place with a total principal value of £2,032,400,000 hedging the liability to make payments of interest and principal in US Dollars and Euros on the Currency Notes.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. FINANCIAL INSTRUMENTS (CONT'D)**

**11(d) Fair values (cont'd)**

The swaps which have been purchased to hedge interest rate and currency risks arising on the Notes have been valued by discounting future cash flows. The valuation method is consistent with commonly used market techniques. All inputs into valuation models adopted by the Company are obtained from observable market data. The change in fair value that has been calculated using this valuation technique and has been recognised in net fair value gains and losses on derivatives for the period ended 31 December 2007 amounts to a loss of £367,000. The fair value of the swaps is expected to unwind to £ nil over the life of the Notes.

The sensitivity to a 1% change in fair value of the Company's financial assets and liabilities amounts to £2,000 based on a net fair value liability of £211,000.

For the risks that are being hedged and for which documentation exists that complies with the requirements of IAS 39, a fair value hedge adjustment is posted to the Notes. The designated hedged Notes have been fair valued with respect to the designated hedged risk by discounting future cash flows. The amount recognised in net fair value gains and losses on derivatives for the period ended 31 December 2007 amounts to a gain of £138,000.

The hedge effectiveness testing for these swaps is carried out on behalf of the Company by the treasury function of the ultimate controlling party, HBOS plc.

**12. RELATED PARTY TRANSACTIONS**

The Company is a special purpose company with three directors. Two of the Company's three directors are provided by Structured Finance Management Limited, the third director is an employee of HBOS plc.

BOS provides cash management services defined under the Programme Documentation and also provides the Company with start-up loans. Fees for these services together with audit fees are paid on behalf of the Company by Funding 1, a company which is part of the Group. The cash management fee amounted to £453,000 and the audit fees amounted to £5,000 excluding VAT for the period ended 31 December 2007.

Structured Finance Management Limited provides corporate services pursuant to a corporate services agreement with the Company. Structured Finance Management Limited was paid £7,000 for services provided in the period. These fees are paid on behalf of the Company by Funding 1.

During the period, the Company undertook the following transactions with companies within the Group, and with HBOS plc and its subsidiary undertakings including BOS, the mortgage loan administrator and cash manager for the securitisation transactions.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**12. RELATED PARTY TRANSACTIONS (CONT'D)**

	<b>Pendeford Funding (No.1) Limited</b>	<b>HBOS plc and its subsidiary undertakings</b>
<b>At 31 December or for the period then ended</b>	<b>2007 £000</b>	<b>2007 £000</b>
<b>Interest receivable and similar income</b>		
Interest on inter-company loans	111,158	-
Bank Interest	-	1
Interest on Start up loans	3,238	-
Income from Group undertaking	4	-
<b>Interest payable and similar charges</b>		
Interest on start up loans	-	3,238
<b>Non-current assets</b>		
Loans to Group undertaking	2,163,184	-
<b>Current assets</b>		
Loans to Group undertaking	428,440	-
Cash and cash equivalents	5	13
<b>Current liabilities</b>		
Interest payable on start up loan	-	605

All of the above transactions were conducted on a commercial basis.

**13. PARENT UNDERTAKING AND CONTROLLING PARTY**

The Company is a wholly-owned subsidiary of Pendeford Holdings Limited, a company registered in England and Wales. The shares of Pendeford Holdings Limited are held on a discretionary trust basis by SFM Corporate Services Limited.

**PENDEFORD MASTER ISSUER PLC**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. PARENT UNDERTAKING AND CONTROLLING PARTY (CONT'D)**

The Company meets the definition of a special purpose entity under IFRSs. In accordance with the requirements of SIC 12 "Consolidation – Special Purpose Entities", the Company's accounts are consolidated within the group accounts of HBOS plc.

HBOS plc is the ultimate controlling party of the Company under IFRSs and heads the largest group into which the accounts of the Company are consolidated. The consolidated accounts of HBOS plc may be obtained from its head office at The Mound, Edinburgh EH1 1YZ.

BOS heads the smallest group into which the accounts of the Company are consolidated. The accounts of BOS may be obtained from its head office at the Mound, Edinburgh EH1 1YZ.



**ANNEX B**

**Registered Number 6121306**

**PENDEFORD FUNDING (NO. 1) LIMITED  
DIRECTORS' REPORT AND FINANCIAL STATEMENTS  
FOR THE PERIOD FROM INCORPORATION TO 31 DECEMBER 2007**

**PENDEFORD FUNDING (NO. 1) LIMITED  
DIRECTORS' REPORT AND FINANCIAL STATEMENTS**

**CONTENTS**

	<b>Page</b>
Directors and Company Information	2
Directors' Report	3-7
Statement of Directors' Responsibilities	8
Independent Auditors' Report to the Members of Pendeford Funding (No. 1) Limited	9-10
Income Statement	11
Balance Sheet	12
Cash Flow Statement	13
Notes to the Financial Statements	14-35

**PENDEFORD FUNDING (NO. 1) LIMITED  
DIRECTORS AND COMPANY INFORMATION**

**DIRECTORS**

David Balai (Appointed 21 February 2007)  
SFM Directors Limited (Appointed 21 February 2007)  
SFM Directors (No. 2) Limited (Appointed 21 February 2007)

**SECRETARY**

SFM Corporate Services Limited (Appointed 21 February 2007)

**REGISTERED OFFICE**

35 Great St. Helen's  
LONDON  
EC3A 6AP

**AUDITORS**

KPMG Audit Plc  
1 The Embankment  
Neville Street  
LEEDS  
LS1 4DW

## **PENDEFORD FUNDING (NO. 1) LIMITED DIRECTORS' REPORT**

The directors present their report and the audited financial statements for the period ended 31 December 2007.

### **INCORPORATION**

Pendeford Funding (No. 1) Limited (the "Company") was incorporated in England and Wales on 21 February 2007 as a private limited company under the Companies Act 1985. The Company began trading on 12 April 2007.

### **ACCOUNTING REFERENCE DATE**

It was resolved on 21 February 2007 that the first accounting reference date of the Company be amended from 29 February 2008 to 31 December 2007. These are the first statutory financial statements prepared for the Company and cover the period from incorporation to 31 December 2007.

### **BUSINESS REVIEW**

#### **Principal activity**

The principal activity of the Company is to acquire an interest in a portfolio of mortgage loans and to enter into certain financial arrangements in that connection.

The activities of the Company and the Pendeford Holdings Limited Group (see below) are conducted primarily by reference to a series of securitisation transaction documents (the "Programme Documentation"). The securitisation structure has been established as a means of raising finance for Bank of Scotland plc ("BOS"), a subsidiary undertaking of HBOS plc.

On 17 September 2007, the HBOS Group Reorganisation Act 2006 took effect. This brought together four of HBOS plc's main UK banking businesses (Halifax plc, Governor and Company of the Bank of Scotland, Capital Bank plc and HBOS Treasury Services plc) into a single legal entity, Bank of Scotland plc.

The principal activity of the Company is unaffected by the reorganisation of HBOS plc. BOS now provides cash manager and mortgage loan servicing as defined under the Programme Documentation.

#### **Business structure**

The Company is a wholly-owned subsidiary of Pendeford Holdings Limited, a company registered in England and Wales. The shares of Pendeford Holdings Limited are held on a discretionary trust basis by SFM Corporate Services Limited.

At 31 December 2007 the Pendeford Holdings Limited Group, (the "Group"), comprised Pendeford Master Issuer PLC (the "Issuer"), Pendeford Holdings Limited, Pendeford PECOH Limited and the Company.

**PENDEFORD FUNDING (NO. 1) LIMITED  
DIRECTORS' REPORT (CONT'D)**

**BUSINESS REVIEW (CONT'D)**

**Business structure (cont'd)**

The Company invests in beneficial interests of the assets held by Pendeford Mortgages Trustee Limited (the "Trust"). These assets comprise mortgage loans secured on residential property originated by BOS under the Birmingham Midshires brand. The Company receives a share of income from the Trust in proportion to its share of the mortgage assets of the Trust.

**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". Detailed analysis of the risks facing the Company in relation to its financial instruments and the management of such risks is provided in note 13.

Other risks which may affect the Company's performance are detailed below.

**Operational risk**

The Company is bound by the inter-company loan agreement to make payments to meet the third party expenses of the Issuer including fees to parties providing operational support in accordance with the Programme Documentation.

The Company's operations are subject to periodic review by the Internal Audit function of HBOS plc.

**Business risk**

The principal business risks of the Company are set out in a number of asset and non asset trigger events in the Programme Documentation. The occurrence of trigger events would lead to the early redemption of the inter-company loans in accordance with the predetermined priorities.

There have been no such trigger events since inception of the Programme.

In the unlikely event that sufficient funds are not received during a cash accumulation period to redeem the inter-company loans, an amount equal to such a shortfall will be deferred until such funds are received.

Failure to pay the inter-company loan interest and principal to the Issuer will ultimately result in a deterioration of the Issuer's financial position and affect its ability to meet its obligations under the loan notes issued (the "Notes"). To the extent that the income on the loan to originator does not provide sufficient funds to recover the Company's investment in the mortgage portfolio, the Company has no claim on the assets of BOS.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**DIRECTORS' REPORT (CONT'D)**

**PERFORMANCE**

On 12 April 2007 the Company purchased a beneficial interest in the assets of the Trust of £2.5 billion. The purchase was financed by an inter-company loan from the Issuer received on the same day.

Profits for the Company are pre-determined under the Programme Documentation. Under the terms of the securitisation the Company retains the right to a profit before tax of up to £5,000 from available revenue receipts from the beneficial interest in the Trust. This is reflected in the income statement net of any movements in fair value gains and losses on derivatives. Profits in excess of £5,000 accrue to BOS, the originator of the underlying mortgages.

The Company's tax charge is based on the tax regime for securitisation companies. All fair value adjustments on derivative contracts are ignored for taxation purposes.

The cash flows of the Company with regards to tax liabilities are not impacted by the current accounting policies.

Interest receivable and similar income for the period amounted to £118,928,000 following the acquisition of a beneficial interest in the assets of the Trust in April 2007. This is matched by £116,308,000 of interest payable and similar charges.

The principal asset of the Company is a single loan to the originator which is subject to an annual impairment review. The loan represents a beneficial interest in a mortgage loan portfolio and is subject to the economic factors relating to the housing market (see note 13 (a) Credit Risk).

The key performance indicators used by management in assessing the performance of the Company are the monitoring of actual cash flows against planned cash flows on the inter-company loans and the level of arrears on the mortgages in the Trust.

The Company's performance is addressed in the quarterly management accounts provided to the directors and the performance indicators are included within the monthly Trustee Report.

The number and value of loans currently in arrears will have a bearing on the receipt of cash by the Company. Key indicators are as follows:

- At 31 December 2007, 158 accounts were in arrears by three or more months which represents 0.25% of the mortgage pool.
- At 31 December 2007, the number of properties in possession amounted to 4. The balance on these accounts was £0.5m.
- At 31 December 2007, bad debts were £ nil and the Company's share was £ nil.

The fair value of the loan to originator has been adjusted to take account of the market yields implied by the valuation of the borrowings (see Note 13 (d) Fair Values). However, the underlying mortgage assets within the Trust have performed in line with expectations and, therefore, no impairment is considered necessary.

**PENDEFORD FUNDING (NO. 1) LIMITED  
DIRECTORS' REPORT (CONT'D)**

**OTHER INFORMATION**

The Company has employed no staff during the period ended 31 December 2007.

**RESULTS AND DIVIDEND**

The results for the period are set out on page 11. The loss after taxation for the period, prepared using IFRSs, as adopted by the European Union (the "EU"), amounted to £1,517,000 and will be transferred to reserves. The directors do not recommend the payment of a dividend.

The loss for the period includes a net fair value loss on financial instruments of £4,231,000 which reflects the current market value of the derivatives.

**FUTURE DEVELOPMENTS**

The directors expect that the Company will continue to meet the scheduled repayment dates for the inter-company loans during 2008, based on the relatively low levels of arrears experienced to date on the mortgage loan portfolio which provides the cash to pay the inter-company loans. No changes in activity are envisaged.

**SUPPLIER PAYMENT POLICY**

It is the Company's policy that payments made to suppliers are made in accordance with those terms and conditions agreed between the Company and its suppliers.

The Company owed no amounts to trade creditors at 31 December 2007.

**DIRECTORS AND DIRECTORS' INTERESTS**

The directors who served during the period from incorporation to the end of the period and subsequently were as follows:

David Balai

SFM Directors Limited

SFM Directors (No. 2) Limited

David Balai, SFM Directors Limited and SFM Directors (No.2) Limited are also directors of Pendeford Holdings Limited.

**PENDEFORD FUNDING (NO. 1) LIMITED  
DIRECTORS' REPORT (CONT'D)**

**GOING CONCERN**

The directors are satisfied that the Company 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 negative reserves are a result of fair value adjustments made in accordance with IFRSs and are expected to reverse in the future. There was no impact on the cash resources of the Company during the period as a result of these valuation adjustments.

**AUDIT INFORMATION**

The directors who held office at the date of approval of this Directors' Report confirm that, so far as they each are aware, there is no relevant audit information of which the Company's auditors are unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

**AUDITORS**

The Company's first auditors were appointed by the directors on 21 February 2007. In accordance with Companies Act 2006, KPMG Audit plc are deemed to have been reappointed as auditors.

By Order of the Board

, Director  
SFM Corporate Services Limited  
Secretary

35 Great St. Helen's  
LONDON  
EC3A 6AP

March 2008



**PENDEFORD FUNDING (NO. 1) LIMITED**  
**STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE DIRECTORS'**  
**REPORT AND THE FINANCIAL STATEMENTS**

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 Company financial statements for each financial year. Under that law the directors have elected to prepare the Company financial statements in accordance with IFRSs as adopted by the EU.

The Company financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position of the Company and the performance for that period; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing the Company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Directors' Report and a Business Review.

**INDEPENDENT AUDITORS' REPORT  
TO THE MEMBERS OF PENDEFORD FUNDING (NO. 1) LIMITED**

We have audited the financial statements of Pendeford Funding (No. 1) Limited for the period ended 31 December 2007 which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out therein.

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

**Respective responsibilities of directors and auditors**

The directors' responsibilities for preparing the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 8.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

**Basis of audit opinion**

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

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

**INDEPENDENT AUDITORS' REPORT  
TO THE MEMBERS OF PENDEFORD FUNDING (NO. 1) LIMITED (CONT'D)**

**Opinion**

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Company's affairs as at 31 December 2007 and of its loss for the period then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

**KPMG Audit Plc**  
Chartered Accountants  
Registered Auditor

1 The Embankment  
Neville Street  
Leeds  
LS1 4DW

March 2008

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**INCOME STATEMENT**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007**

	<b>Note</b>	<b>2007</b> <b>£000</b>
Interest receivable and similar income	2	118,928
Interest payable and similar charges	3	(116,308)
		2,620
<b>Net interest income</b>		<b>2,620</b>
Net fair value losses on derivatives held for economic hedging		(4,231)
Operating expenses	4	(496)
		(2,107)
<b>Loss before tax for the period</b>		<b>(2,107)</b>
Income tax credit	5	590
		(1,517)
<b>Loss after tax for the period</b>		<b>(1,517)</b>
		(1,517)
<b>Loss attributable to equity holders</b>		<b>(1,517)</b>
		(1,517)

The loss 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 statement of recognised income and expense has been omitted from the financial statements for the period ending 31 December 2007 as there was no income or expense recognised directly in equity in the period.

Notes 1 to 16 form part of these financial statements.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**BALANCE SHEET AS AT 31 DECEMBER 2007**

	Note	2007 £000
<b>Assets</b>		
Loan to originator	6	2,095,003
Deferred tax asset	7	591
		2,095,594
<b>Total non-current assets</b>		
		2,095,594
Loan to originator	6	406,300
Other receivables	8	12,725
Derivative asset		4,185
Cash and cash equivalents	9	492,707
		915,917
<b>Total current assets</b>		
		915,917
<b>Total assets</b>		3,011,511
<b>Equity</b>		
Issued capital		-
Retained earnings		(1,517)
		(1,517)
<b>Total equity</b>		(1,517)
<b>Liabilities</b>		
Interest-bearing loans and borrowings	11	2,164,148
		2,164,148
<b>Total non-current liabilities</b>		
		2,164,148
Interest-bearing loans and borrowings	11	427,930
Other payables	12	420,949
Current tax liability	5	1
		848,880
<b>Total current liabilities</b>		
		848,880
<b>Total liabilities</b>		3,013,028
<b>Total equity and liabilities</b>		3,011,511

These financial statements were approved by the Board of Directors on March 2008 and were signed on its behalf by:

Per pro SFM Directors Limited  
as Director

Notes 1 to 16 form part of these financial statements.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**CASH FLOW STATEMENT**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007**

<b>Indirect method</b>	<b>2007</b>
<b>Note</b>	<b>£000</b>
<b>Cash flows from operating activities</b>	
Profit before tax for the period	(2,107)
<i>Adjustments for:</i>	
Bank interest receivable	2 (14,450)
Swap interest receivable	2 (9,301)
Income from loan to originator	2 (93,058)
Amortisation of discount	2 (2,119)
Interest payable on loans from Group undertakings	3 111,158
Amortisation of issue costs	3 1,912
Interest payable on start-up loans	3 3,238
Net fair value gains and losses on derivatives held for economic hedging	4,231
	<hr/>
<b>Operating loss before changes in working capital and provisions</b>	<b>(496)</b>
Increase in other payables	424,548
	<hr/>
<b>Cash generated from the operations</b>	<b>424,052</b>
Income taxes paid	-
	<hr/>
<b>Net cash from operating activities</b>	<b>424,052</b>
	<hr/>
<b>Cash flows from investing activities</b>	
Swap interest received	6,797
Funds loaned to originator	(2,507,600)
Interest on loan to originator	82,924
	<hr/>
<b>Net cash from investing activities</b>	<b>(2,417,879)</b>
	<hr/>
<b>Cash flows from financing activities</b>	
Bank interest received	14,369
Start up loan receipts	65,800
Repayment of start up loans	(3,916)
Interest paid on start up loan	(2,633)
Loans from Group undertakings	2,507,600
Interest paid on loans from Group undertakings	(89,623)
Payment of issue costs	(5,063)
	<hr/>
<b>Net cash from financing activities</b>	<b>2,486,534</b>
	<hr/>
<b>Net increase in cash and cash equivalents</b>	<b>492,707</b>
Cash and cash equivalents at 21 February	-
	<hr/>
<b>Cash and cash equivalents at 31 December</b>	<b>492,707</b>
	<hr/>

As explained in the accounting policies in note 1, cash is not available to be used with discretion.

Notes 1 to 16 form part of these financial statements.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007**

**1. SIGNIFICANT ACCOUNTING POLICIES**

Pendeford Funding (No. 1) Limited is a company domiciled in England.

**(a) Statement of compliance**

The financial statements for the period ended 31 December 2007 have been prepared in accordance with International Financial Reporting Standards (IFRSs) and its interpretations as endorsed by the EU and effective at 31 December 2007.

The accounting policies set out below have been applied in respect of the financial period ended 31 December 2007. IFRS 7 "Financial Instruments: Disclosures" became effective for all accounting periods ending on or after 1 January 2007. The principles in this standard complement the principles for recognising, measuring and presenting financial assets and liabilities in IAS 32 "Financial Instruments: Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement".

Adoption of the Capital disclosure amendment to IAS 1 "Presentation of Financial Statements" became mandatory for all accounting periods ending on or after 1 January 2007. The adoption of this amendment has had no quantitative impact on the financial data presented in the financial statements. Additional disclosure is presented in the total equity note.

The financial statements also comply with the relevant provisions of Part VII of the Companies Act 1985, as amended by the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004.

**(b) Basis of preparation**

The financial statements are presented in Sterling and rounded to the nearest thousand.

The financial statements have been prepared on the historical cost basis (except that derivative financial instruments are stated at their fair value), and on a going concern basis.

This is the first period of account for the Company and, therefore, there are no prior period comparatives included within the financial statements.

The preparation of the financial statements necessarily requires the exercise of judgement both in the application of accounting policies which are set out in the sections below and in the selection of assumptions used in the calculation of estimates. These estimates and judgements are reviewed on an ongoing basis and are continually evaluated based on historical experience and other factors. However, actual results may differ from these estimates. The most significantly affected components of the financial statements and associated critical judgements are as follows:

Effective Interest Rate – In calculating the effective interest rate of financial instruments the Company takes into account interest received or paid, fees and commissions paid or received, expected early redemptions and related penalties and premiums and discounts on acquisition or issue that are integral to the yield as well as incremental transaction costs.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(b) Basis of preparation (cont'd)**

For the purpose of the effective yield calculation, it has been assumed that the average expected life of the Notes in issue will end at the date of the first step-up in interest rates, based on the payment experience to date. This may not be the case in practice.

The fair value of the interest rate swap is determined by using a discounted cash flow analysis model that is consistent with commonly used market techniques. The fair value calculated using this technique is regularly compared with prices of similar instruments obtained in actual market transactions to ensure reliability. All inputs into valuation models adopted by the Company, including the Sterling zero coupon yield curve used as the discount rate on the swap, are obtained from observable market data.

**(c) Financial instruments**

The Company's financial instruments comprise a loan to BOS, cash and liquid resources, a derivative contract, interest-bearing borrowings and various 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.

**(c)(i) Loan to originator**

In accordance with IAS 39, where a transfer of a financial asset does not qualify for derecognition, the transferee does not recognise the transferred asset as its asset. The transferee derecognises the cash or other consideration paid and recognises a receivable from the transferor. In relation to the mortgage portfolios transferred to the Company, derecognition is considered to be inappropriate for the originator's own financial statements as the originator has retained significant risks and rewards of ownership of that financial asset. The Company's financial statements are, therefore, prepared on the basis that its acquisitions of beneficial interests in mortgage portfolios are recognised as a collateralised non-recourse loan to the originator.

Under the terms of the securitisation the Company retains the right to up to £5,000 per annum from available revenue receipts from the beneficial interest in the mortgage portfolio. This is reflected in the income statement net of any movements on fair value gains and losses on derivatives. Available revenue receipts are defined by the Programme Documentation and include mortgage interest received, interest received on the bank accounts and the amounts standing to the credit of the reserve ledger. Profits in excess of £5,000 accrue to BOS, the originator of the underlying mortgages. Accordingly a creditor ("deferred consideration") for amounts payable to BOS for this residual interest has been recognised at the period-end. The payments of deferred consideration are strictly governed by the priority of payments that sets out how cash can be utilised.



**PENDEFORD FUNDING (NO.1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(c) Financial instruments (cont'd)**

**(c)(i) Loan to originator (cont'd)**

The loan to originator 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 loan to originator is calculated with reference to the interest earned on the beneficial interest in the mortgage portfolio less the residual interest due to BOS as described above. Where cash has been accumulated by the Company to fund the future repayment of its intercompany loans, the Company's share of the interest arising on the beneficial interest in the mortgage portfolio is adjusted.

The loan to originator 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 loan to originator will be significantly reduced. This could occur if the credit quality of the mortgage assets that are pledged as collateral for the loan deteriorated significantly. Currently the directors consider that no impairment exists.

**(c)(ii) Cash and cash equivalents**

The Company holds deposits with the provider of a guaranteed investment contract ("GIC") and a transaction bank account with the same provider. These accounts are held in the Company's name and meet the definition of cash and cash equivalents but their use 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 recorded using the effective interest method.

The Cash Flow Statement has been presented using the indirect method of preparation.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(c) Financial instruments (cont'd)**

**(c)(iii) Derivative financial instruments**

IAS 39 requires all derivative financial instruments to be recognised initially at fair value on the balance sheet and to be remeasured 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 gain or loss on remeasurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged. Where a fair value hedge is documented, the fair value movements of the swap may be offset in the income statement against the fair value movements for the risk being hedged on the hedged item.

The Company uses derivative financial instruments to hedge its exposure to interest rate risk arising from operational, financing and investment activities. In accordance with its treasury policy, the Company 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 loan to originator is managed by means of an interest rate swap with BOS, which requires the Company to pay the effective yield on the beneficial interest in the mortgage portfolio and receive payments based on a rate linked to the three-month Sterling LIBOR.

When the Company commenced trading the fair value of the interest rate swap has been recognised as a derivative asset in the balance sheet with an equal and opposite fair value discount adjustment against the loan to originator. The subsequent gain or loss on remeasurement of the interest rate swap to fair value has been recognised immediately in net fair value gains and losses on derivatives in the income statement. The loan to originator discount adjustment is being amortised to interest receivable over the average expected life of the beneficial interest in the mortgage portfolio.

Interest receivable or payable on the interest rate swap is accounted for on an accruals basis within interest receivable or payable in the income statement.

The fair value of interest rate swaps is the estimated amount that the Company would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

**(c)(iv) Interest-bearing borrowings**

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing 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.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(c)(v) 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.

**(c)(vi) Offsetting of financial assets and liabilities**

A financial asset and a financial liability is offset and the net amount is reported in the balance sheet if the Company has a legally enforceable right to set-off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

**(d) Impairment**

The carrying amounts of the Company's assets other than deferred tax assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated. An impairment loss is recognised in the income statement whenever the carrying amount of the asset exceeds its recoverable amount.

**(e) Value added tax**

Value added tax is not recoverable by the Company and is included with its related cost.

**(f) Income tax**

Income tax on the profit or loss for the period comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Temporary differences arising from the initial recognition of assets and liabilities that affects neither accounting nor taxable profit are not provided for. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates at the balance sheet date.

Under special rules issued by HM Revenue & Customs for securitisation companies, the Company's charge for taxation for 2007 is based on its taxable profits calculated on a UK GAAP basis but disclosed in accordance with IAS 12 "Income Taxes".

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**1. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**(g) Related parties**

In accordance with the provisions of IAS 24 "Related Party Disclosures", the Company has disclosed details of transactions with its related parties, including those with fellow Pendeford Holdings Limited Group companies, and the ultimate controlling party HBOS plc under IFRSs.

**(h) Other payables**

Other payables are stated at cost.

**(i) New accounting standards and interpretations**

The following standards and interpretations have been adopted by the European Union but are not effective for the period ended 31 December 2007 and have not been applied in preparing the financial statements:

IFRS 8 "Operating Segments" which is applicable for periods commencing on or after 1 January 2009. The application of this standard in 2007 would not have had any financial impact as it is only concerned with disclosure.

The following standards and interpretations have not yet been adopted by the European Union, are not effective for the period ended 31 December 2007 and have not been applied in preparing the financial statements:

IAS 1 "Presentation of Financial Statements" which is effective for periods commencing on or after 1 January 2009. The application of this revised standard in 2007 would not have had a material impact on the financial statements.

**PENDEFORD FUNDING (NO. 1) LIMITED  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**2. INTEREST RECEIVABLE AND SIMILAR INCOME**

	<b>2007 £000</b>
Income from loan to originator	93,058
Bank interest	14,450
<b>Income calculated using effective interest method</b>	107,508
Swap interest	9,301
Amortisation of discount on acquisition	2,119
	118,928

Interest from the loan to originator and bank interest is calculated using the effective interest method.

Deferred consideration and bad debt expenses are included as part of the effective yield on the loan to originator. As the loan to originator in total is not regarded as impaired, the interest received on impaired assets is £ nil.

Swap interest receivable arises on a financial instrument that is being accounted for using fair value accounting principles.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**3. INTEREST PAYABLE AND SIMILAR CHARGES**

	<b>2007</b> <b>£000</b>
Interest on loans from Group undertaking	111,158
Amortisation of issue costs	1,912
Start-up loan interest	3,238
	116,308
	116,308

Interest payable is calculated using the effective interest method.

**4. OPERATING EXPENSES**

	<b>2007</b> <b>£000</b>
Cash manager fees	454
SFM Management Limited management fees	13
Fees payable to Group undertakings	4
Audit fees	25
	496
	496

Audit fees relate to the statutory audit and are exclusive of VAT. Fees payable to the auditor and its associates for services other than the statutory audit are not disclosed since the consolidated accounts of HBOS plc, the ultimate controlling party, are required to disclose non-audit fees on a consolidated basis.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**5. INCOME TAX CREDIT RECOGNISED IN THE INCOME STATEMENT**

	<b>2007</b> <b>£000</b>
<b>Current Tax</b>	
Corporation tax charge for the period at a rate of 20%	(1)
<b>Deferred tax</b>	
Deferred tax credit for the period at a rate of 28%	591
	590
Total income tax credit in income statement	590
	<b>2007</b> <b>£000</b>
<b>Reconciliation of effective tax rate</b>	
Loss before tax	(2,107)
Loss before tax multiplied by the current standard rate of corporation tax in the UK (30%)	632
Effects of:	
Items not allowable under securitisation tax rules	633
Deferred tax provided	(633)
Impact of change in future tax rate (28%)	(42)
	590
Total income tax credit in income statement	590

The current tax liability of £1,000 represents the amount of income tax payable in respect of the current period. No payments on account have been made during the period.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**6. LOAN TO ORIGINATOR**

	<b>Loan to originator £000</b>	<b>Fair value hedge adjustment £000</b>	<b>Total £000</b>
Originations	2,507,600	(8,416)	2,499,184
Amortisation	-	2,119	2,119
	<hr/>	<hr/>	<hr/>
At 31 December 2007	2,507,600	(6,297)	2,501,303
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

The balance can be analysed as follows:

Non-current assets	2,095,003
Current assets	406,300
At 31 December 2007	<hr/> 2,501,303

On 12 April 2007 the Company acquired a beneficial interest in a mortgage portfolio from BOS amounting to £2,507,600,000.

The mortgage portfolio, which is accounted for as a loan to originator and in which the Company holds a beneficial interest, is held on trust for the Company and the originator of the mortgage loans by the Trust. The mortgage loans are secured on residential property in England, Wales and Scotland. Mortgages in the pool have to fulfil certain criteria. If they fail to do so they are removed from the pool and the pool is replenished.

Income on the loan to originator, arising on the underlying mortgages, reflects fixed, variable and tracker rates. Deferred consideration is deducted from this income in order to arrive at the effective yield on the loan to originator.



**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**7. DEFERRED TAX**

**Deferred taxation assets**

	<b>2007</b> <b>£000</b>
Credit to income for the period	591
	591
Balance carried forward as at 31 December	591
	591

The deferred tax asset of £591,000 represents the amount of deferred tax deductible in respect of the fair value loss on derivatives of £4,231,000, less amortisation of the discount on the loan to originator of £2,119,000, which are temporary timing differences and, therefore, expected to reverse.

There are no unrecognised deferred taxation assets or liabilities as at 31 December 2007.

**8. OTHER RECEIVABLES**

	<b>2007</b> <b>£000</b>
Amount owed from the Trust	10,134
Interest receivable - Swaps	2,504
Interest receivable – GIC Account	82
Prepayments	5
	12,725
	12,725

The amount owed from the Trust represents cash movements on the Trust GIC account which arise as part of the cash distribution governed by the Programme Documentation.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**9. CASH AND CASH EQUIVALENTS**

The deposit account held by the Company is placed with the provider of a GIC account. Withdrawals from this account are restricted by the detailed priority of payments set out in the Programme Documentation. The Company is contractually entitled to a variable rate of interest of 0.25 per cent per annum below LIBOR for three-month Sterling deposits.

	<b>2007</b>
	<b>£000</b>
Cash and cash equivalents in the cash flow statement.	492,707

**10. TOTAL EQUITY**

	<b>Share capital £000</b>	<b>Retained earnings £000</b>	<b>Total equity £000</b>
Total recognised income and expense	-	(1,517)	(1,517)
At 31 December 2007	-	(1,517)	(1,517)

There are 100 authorised ordinary shares of £1 each. The issued share capital comprises two ordinary shares of £1, which are fully paid.

**Capital disclosures**

The Company is not subject to externally imposed capital requirements in the current period. The Company manages its ordinary share capital in order that there is sufficient capital, in the opinion of the directors, to support the transactions and level of business undertaken by the Company.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**11. INTEREST-BEARING LOANS AND BORROWINGS**

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

	<b>2007</b> <b>£000</b>
<b>Non-current liabilities</b>	
Loans from Group undertakings	2,101,300
Deferred issue costs	(2,640)
Start-up loans	61,884
Deferred consideration	3,604
	2,164,148
<b>Current liabilities</b>	
Loans from Group undertakings	406,300
Deferred issue costs	(510)
Interest payable to Group undertakings	21,535
Interest payable on start-up loans	605
	427,930

Interest payable to Group undertakings and loans from Group undertakings relate to obligations to pay interest and principal amounts due to the Issuer under the inter-company loan agreement.

The inter-company loan agreement provides that the Issuer will lend amounts in Sterling to the Company equivalent to the proceeds of the underlying Notes. The final repayment date of each inter-company loan will be the final maturity date of the corresponding class of Notes.

Interest payable on the loans from Group undertakings is based on LIBOR for three-month Sterling deposits. The Company's obligations under the inter-company loan agreement are secured under a deed of charge by the Company's beneficial interest in the mortgage portfolio held by the Trust.

Current liabilities due within one year are paid when cash is available after other commitments have been fulfilled, in order of priority.

**PENDEFORD FUNDING (NO. 1) LIMITED  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**12. OTHER PAYABLES**

	<b>2007 £000</b>
<b>Current liabilities</b>	
Amount owed to Bank of Scotland plc	420,924
Accruals	25
	420,949
	420,949

The amount owed to BOS represents cash movements on the GIC account which arise as part of the cash distribution governed by the Programme Documentation. The amount will remain a liability until such time as the Notes are redeemed.

Current liabilities due within one year are paid when cash is available after other commitments have been fulfilled, in order of priority.

**13. FINANCIAL INSTRUMENTS**

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 principally comprise a loan to BOS, cash and liquid resources, a derivative contract ("swap") and interest-bearing borrowings that arise directly from its operations.

The principal risks arising from the Company's financial instruments are credit risk and interest rate risk. Further detailed analysis of the risks facing the Company in relation to its financial instruments is provided below.

As noted in the Directors' Business Review, the activities of the Company and the Group are conducted primarily by reference to a series of securitisation transaction documents (the "Programme Documentation"). The securitisation structure has been established as a means of raising finance for BOS and no business activities will be undertaken by the Company beyond those set out in the Programme Documentation.

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 is clearly defined and documented. Cash flow modelling, including multiple stress scenarios, is carried out as part of the structuring of the transaction, and as such is required by the rating agencies. In addition an interest rate swap is entered into with the originator as part of the securitisation transaction to hedge interest rate risk arising in the transaction including the obligations under the inter-company loans. The derivative counterparty is selected as a highly rated, regulated financial institution and this reduces the risk of default and loss for the Company.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. FINANCIAL INSTRUMENTS (CONT'D)**

Following initial set-up, the directors monitor the Company's performance, reviewing monthly reports on the performance of the Trust property and the quarterly management accounts. Such review is designed to ensure that the terms of the Programme Documentation have been complied with, that no unforeseen risks have arisen and that the interest and principal on the inter-company loans have been paid on a timely basis.

**13(a) Credit risk**

Under IFRSs the beneficial interest in the mortgage loan portfolio is classified as a "loan to originator" in the Company's balance sheet.

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. The ability of the Company to pay the inter-company loan interest and principal to the Issuing Company will depend on the amount and timing of the payment of interest and the repayment of principal on the underlying mortgage loans by the borrowers.

In terms of arrears management, the Company has engaged BOS as servicer of the loans in the portfolio to help reduce the risk of loss. The servicer is required to monitor repayments on the mortgage loans in accordance with its usual credit policies. The servicer is also responsible for ensuring mortgage loans in the Trust meet the eligibility criteria set out in the Programme Documentation.

The number and value of loans currently in arrears will have a bearing on the receipt of cash by the Company. Key indicators are as follows:

- At 31 December 2007 158 accounts were in arrears by three or more months which represents 0.25% of the mortgage pool.
- At 31 December 2007 the number of properties in possession amounted to 4. The balance on these accounts was £0.5m.
- At 31 December 2007 bad debts were £ nil and the Company's share was £ nil

However, as a single loan to originator there is no requirement to provide against the individual mortgages. Impairment will only be an issue when mortgage losses exceed the deferred consideration. Until that point, any specific mortgage losses will be netted against the mortgage interest from the Trust, with a corresponding adjustment to deferred consideration. Therefore, there is no effect on the overall yield on the loan to originator. The directors consider that the Company's share of mortgage loans in the Trust will be sufficient to recover the full amount of this loan.

To the extent that the income on the loan to originator does not provide sufficient funds to recover the Company's investment in the mortgage portfolio, the Company has no claim on the assets of BOS. The Company's maximum gross exposure to credit loss is therefore equal to the fair value of its investment in the mortgage portfolio.

**PENDEFORD FUNDING (NO. 1) LIMITED  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. FINANCIAL INSTRUMENTS (CONT'D)**

**13(a) Credit risk (cont'd)**

Sufficient cash has been received from the loan to originator to enable the Company to make all necessary payments on the inter-company loans in accordance with the scheduled repayment dates for the period ended 31 December 2007.

Credit risk also exists on the derivative contract that the Company has entered into to manage the interest rate risk arising on the loan to originator and the inter-company loans (see 13(b) below). The swap counterparty is a regulated financial institution with ratings of AA or higher.

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 2007 £	Maximum exposure 2007 £
<b>Assets held at amortised cost:</b>			
Loan to originator	6	2,499,184	2,499,184
Other receivables	8	12,720	12,720
Cash and cash equivalents	9	492,707	492,707
<b>Assets held at fair value:</b>			
Derivative asset		4,185	4,185
		3,008,796	3,008,796
		3,008,796	3,008,796

**13(b) Market risk**

The Company is exposed to market risk which comprises interest rate risk and is explained in more detail below.

Interest rate risk exists where assets and liabilities have interest rates set under a different basis or which reset at different times. The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of assets and liabilities are similar; where this is not possible the Company uses derivative financial instruments to mitigate interest rate risk. The loan to originator, the inter-company loans and the cash and cash equivalents are exposed to cash flow interest rate risk caused by floating interest rates that are reset periodically.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. FINANCIAL INSTRUMENTS (CONT'D)**

**13(b) Market risk (cont'd)**

An interest rate swap has therefore been entered into with BOS to manage the Company's exposure to interest rate risk associated with the loan to originator and the inter-company loans from the Financing Companies. This interest rate swap is designed to reduce interest rate risk as a result of the possible variance between (a) the weighted average, during an interest period, of (i) the variable rates of interest payable on variable rate loans, (ii) the rates of interest payable on the base rate loans and (iii) the fixed rates of interest payable on the fixed rate loans, and (b) a LIBOR based rate for three-month Sterling deposits.

The Company also has the right to set mortgage rates on the mortgage loans held in the Trust in certain circumstances which are defined in the Programme Documentation to ensure sufficient funds are available to settle payments on the inter-company loans. This right has not been exercised to date.

At 31 December 2007, if interest rates had been 25 basis points higher or lower with all other variables held constant, the net effect on the Company's income statement would be as shown in the table below.

	<b>-25bps</b>	<b>Per income statement</b>	<b>+25bps</b>
	<b>2007</b>	<b>2007</b>	<b>2007</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>
Net fair value losses on derivatives held for economic hedging	(4,846)	(4,231)	(3,616)

Any further impact of an interest rate change on the income statement would be fully offset by a corresponding adjustment to deferred consideration thus having a neutral effect on loss before tax.

**13(c) Liquidity risk**

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at an unacceptably high cost.

The Company's ability to meet payments on the inter-company loans as they fall due is dependent on timely receipt of funds from the loan to originator which may be delayed due to slow repayment on the mortgage portfolio (see 13(a) Credit risk above).

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. FINANCIAL INSTRUMENTS (CONT'D)**

**13(c) Liquidity risk (cont'd)**

The Company's general reserve fund of £55,800,000 was established on the programme date, 12 April 2007. Subject to certain limits and conditions, the Company may apply amounts standing to the credit of this reserve fund in payment of amounts due on the inter-company loans. The Company is only obliged to make payments in respect of the inter-company loans to the extent that it has available revenue and principle receipts available to it. A cash accumulation period is calculated for each bullet loan tranche, which estimates the number of months required to accumulate sufficient principal receipts to repay the loan tranche when due. The minimum accumulation period in respect of any series of notes is at least six months.

The liquidity tables reflect the undiscounted cash payments which will fall due if the structure continues until the earliest contractual maturity date as set out in the Programme Documentation. It is anticipated that the interest earned on the loan to originator will be sufficient to allow early repayment of the inter-company loans and thereby avoid the increase in the interest rate margin payable on the inter-company loans.

2007	Carrying Value	Contractual repayment value	Later than one month 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
	£000	£000	£000	£000	£000
<b>Principal</b>					
Loans from Group undertakings	2,504,450	2,507,600	420,840	339,900	1,746,860
Start-up loans	61,884	61,884	751	2,339	58,794
Deferred consideration	3,604	3,625	-	-	3,625
<b>Interest payable</b>					
Interest payable to Group undertakings	21,535	420,235	39,994	100,664	279,577
Interest payable on start-up loans	605	19,810	1,124	3,294	15,392
	2,592,078	3,013,154	462,709	446,197	2,104,248



**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. FINANCIAL INSTRUMENTS (CONT'D)**

**13(d) Fair values**

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

	Note	Carrying amount 2007 £000	Fair value 2007 £000
<b>Loans and receivables:</b>			
Loan to originator	6	2,499,184	2,483,065
<b>Financial assets at fair value:</b>			
Derivative assets held for economic hedging		4,185	4,185
<b>Financial liabilities held at amortised cost:</b>			
Interest-bearing loans and borrowings	11	2,592,078	2,575,959
Other payables	12	420,949	420,949
		3,013,027	2,996,908
		3,013,027	2,996,908

**Estimation of fair values**

The following comments summarise the main methods and assumptions used in estimating the fair value of financial instruments that are reflected in the table above.

The fair values included above have been calculated taking into account current market values. For interest-bearing loans and borrowings these have been calculated by discounting the expected cashflows by the prevailing market rates for similar debt. The fair values of the assets have been adjusted to take account of the market yields implied by the valuation of the borrowing.

Cash and cash equivalents, other receivables, other payables and interest-bearing loans and borrowings are recognised on an amortised cost basis that is considered to be a close approximation to fair value.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**13. FINANCIAL INSTRUMENTS (CONT'D)**

**13(d) Fair values (cont'd)**

The interest rate swap between the Company and BOS is reflected as a derivative asset in the balance sheet of the Company as at 31 December 2007. The fair value of the interest rate swap is determined by using a discounted cash flow analysis model that is consistent with commonly used market techniques. The fair value calculated using this technique is regularly compared with prices of similar instruments obtained in actual market transactions to ensure reliability. All inputs into valuation models adopted by the Company, including the Sterling zero coupon yield curve used as the discount rate on the swap, are obtained from observable market data. The change in fair value that has been estimated using this valuation technique and has been recognised in the income statement for the period ended 31 December 2007 amounts to a loss of £4,185,000. The fair value of the swap is expected to unwind to £ nil over the life of the transaction.

The sensitivity to a 1% change in fair value of the Company's financial instruments is £21,000 based on a net fair value liability of £2,107,000.

**14. RELATED PARTY TRANSACTIONS**

The Company is a special purpose company with three directors. Two of the Company's three directors are provided by Structured Finance Management Limited, the third director is an employee of HBOS plc (the parent undertaking of BOS, the mortgage loan administrator). The Company pays a corporate services fee to Structured Finance Management Limited in connection with its provision of corporate management services. The fees paid by the Company are on behalf of the Group. The fees payable to Structured Finance Management Limited for providing their services amounted to £13,000. This was paid by the Company. The audit fees amounted to £25,000 excluding VAT for the period ended 31 December 2007, of which £15,000 related to the Company.

During the period, the Company undertook transactions set out below with companies within the Pendeford Holdings Limited Group, the Trust and BOS, the mortgage loan administrator.

The Company pays cash management and mortgage loan servicing fees to BOS in connection with its provision of services defined under the Programme Documentation. BOS is the counterparty to an interest rate swap agreement, on which there is an associated interest benefit for the Company. The interest rate swap is included in the related party note at fair value

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**14. RELATED PARTY TRANSACTIONS (CONT'D)**

<b>At 31 December 2007 or for the period then ended</b>	<b>HBOS plc and Subsidiary Undertakings</b>
	<b>£000</b>
<b>Interest receivable and similar income</b>	
Income from loan to originator	93,058
Bank interest	14,450
Swap interest	9,301
Amortisation of hedge adjustment	2,119
<b>Interest payable and similar charges</b>	
Interest on loans from Group undertakings	111,158
Start-up loan interest	3,238
Net fair value gains and losses on derivatives	4,231
<b>Operating expenses</b>	
Fees payable to Group undertakings	471
Sundry expenses	-
<b>Non-current assets</b>	
Loan to originator	2,080,463
<b>Current Assets</b>	
Loan to originator	420,840
Other receivables	12,720
Derivative asset	4,185
Cash and cash equivalents	492,707
<b>Non-current liabilities</b>	
Interest bearing loans and borrowings:	
Loans from Group undertakings	2,086,760
Start-up loans	61,844
Deferred consideration	3,604
<b>Current liabilities</b>	
Interest bearing loans and borrowings:	
Loans from Group undertakings	420,840
Interest payable to Group undertakings	21,535
Start-up loan interest	605
Other payable BOS	420,924

All of the above transactions were conducted on a commercial basis.

**PENDEFORD FUNDING (NO. 1) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE PERIOD ENDED 31 DECEMBER 2007 (CONT'D)**

**15. PARENT UNDERTAKING AND CONTROLLING PARTY**

The Company is a wholly-owned subsidiary of Pendeford Holdings Limited, a company registered in England and Wales. The shares of Pendeford Holdings Limited are held on a discretionary trust basis by SFM Corporate Services Limited.

The Company meets the definition of a special purpose entity under IFRSs. In accordance with the requirements of SIC 12 "Consolidation – Special Purpose Entities", the Company's accounts are consolidated within the group accounts of HBOS plc.

HBOS plc is the ultimate controlling party of the Company under IFRSs and heads the largest group into which the accounts of the Company are consolidated. The consolidated accounts of HBOS plc may be obtained from its head office at The Mound, Edinburgh EH1 1YZ.

BOS heads the smallest group into which the accounts of the Company are consolidated. The accounts of BOS may be obtained from its head office at The Mound, Edinburgh EH1 1YZ.

**16. TERMINATION PAYMENT GUARANTEE**

Under the Master Inter-company Loan Agreement, the Company is obliged to make a termination payment to the Issuer should one of their currency/interest rate swaps terminate, provided that the Company has sufficient resources to meet all its other obligations in priority. The amount of the termination payment will be based upon the market value of that swap on the date of such termination.

As the termination payment is based upon market value, the maximum amount of potential future payments under this guarantee is unlimited. Whilst this valuation would depend on future interest and foreign exchange rates as applicable, and so cannot be accurately estimated, it is likely that any cost would be substantially less than the principal amounts of the swaps of £2,032,400,000.

No liability for this contingent guarantee has been recognised in the financial statements as the likelihood of the Company having to make any payments under the guarantee is remote. Any payments made by the Company to the Issuer under this guarantee would be made without recourse.

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