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This base prospectus has been delivered to you on the basis that you are a person into whose possession this base prospectus may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located. By accessing the base prospectus, you shall be deemed to have confirmed and represented to us that (a) you have understood and agree to the terms set out herein, (b) you consent to delivery of the base prospectus by electronic transmission, (c) you are either (i) not a US person (within the meaning of Regulation S under the Securities Act) or acting for the account or benefit of a US person and the electronic mail address that you have given to us and to which this e-mail has been delivered is not located in the United States, its territories and possessions (including Puerto Rico, the US Virgin Islands, Guam, American Samoa, Wake Island and the Northern Mariana Islands) or the District of Columbia or (ii) a qualified institutional buyer (as defined in Rule 144A under the Securities Act) and (d) if you are a person in the United Kingdom, then you are a person who (i) has professional experience in matters relating to investments or (ii) is a high net worth entity falling within Article 49(2)(a) to (d) of the Financial Services and Markets Act (Financial Promotion) Order 2005.

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PENDEFORD 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 Gilt-Edged and Fixed Interest Market (being a regulated market for purposes of the Investment Services Directive (93/22/EEC)). 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 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.

Currently, there is no public secondary market for the notes.

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 43 of this base prospectus.

Arranger for the programme



Dealers for the programme

Citigroup

JPMorgan

Morgan Stanley

Base prospectus dated 5 April 2007

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 REGULATIONS 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 HALIFAX PLC (**HALIFAX**), HBOS TREASURY SERVICES PLC (**HBOSTS**), 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 HALIFAX, HBOSTS 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 HALIFAX, HBOSTS, 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 HALIFAX, HBOSTS OR ANY OTHER PARTY TO THE TRANSACTION DOCUMENTS.

The notes of each class sold in reliance on Rule 144A (**Rule 144A**) under the Securities Act 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 of Regulation S under the Securities Act (**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 in the name of (i) a nominee of a common depository (the **common depository**) 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, Halifax, HBOSTS, 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 Halifax, HBOSTS 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, Halifax, HBOSTS, 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 Halifax, HBOSTS 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 (provided that, in the case of any series and class of notes to be admitted to trading on the London Stock Exchange’s Gilt-Edged and Fixed Interest Market or any other regulated market (within the meaning of the Investment Services Directive (Directive 93/22/EEC)) in the European Economic Area, the aggregate principal amount of such notes allotted does not exceed 105 per cent. of the aggregate principal amount of the relevant series and class) or effect transactions with a view to supporting the market price of the notes at a level higher than that which might otherwise prevail. However, there is no assurance that the stabilising manager(s) (or any persons acting on behalf of a stabilising manager(s)) will undertake stabilisation action. 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.

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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, **Halifax** (which term shall mean Halifax plc or, as applicable, the entity expected to succeed to its business pursuant to the HBOS Group Reorganisation Act 2006), the division of Halifax known as Birmingham Midshires (**Birmingham Midshires**) 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 Halifax and/or Birmingham Midshires, 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, Halifax plc will sell 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. From time to time the **seller** (which term shall mean Halifax and the entity which is expected to succeed to its business in accordance with the HBOS Group Reorganisation Act 2006) may, 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, sell further loans and their related security to the mortgages trustee. The **loans** are, as at the date hereof, residential mortgage loans originated by Birmingham Midshires, a division of the seller, 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 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 will distribute 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) will be secured under the Funding 1 deed of charge to be entered into 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 asset will be its rights under the intercompany loan agreement and the Funding 1 deed of charge. Neither the issuing entity nor the noteholders will have any direct interest in the trust property, although the issuing entity will share 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 withdrawn, reduced or 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 will be secured under the issuing entity deed of charge to be 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 reduced, withdrawn or qualified as a result thereof.

Structural diagram of the programme

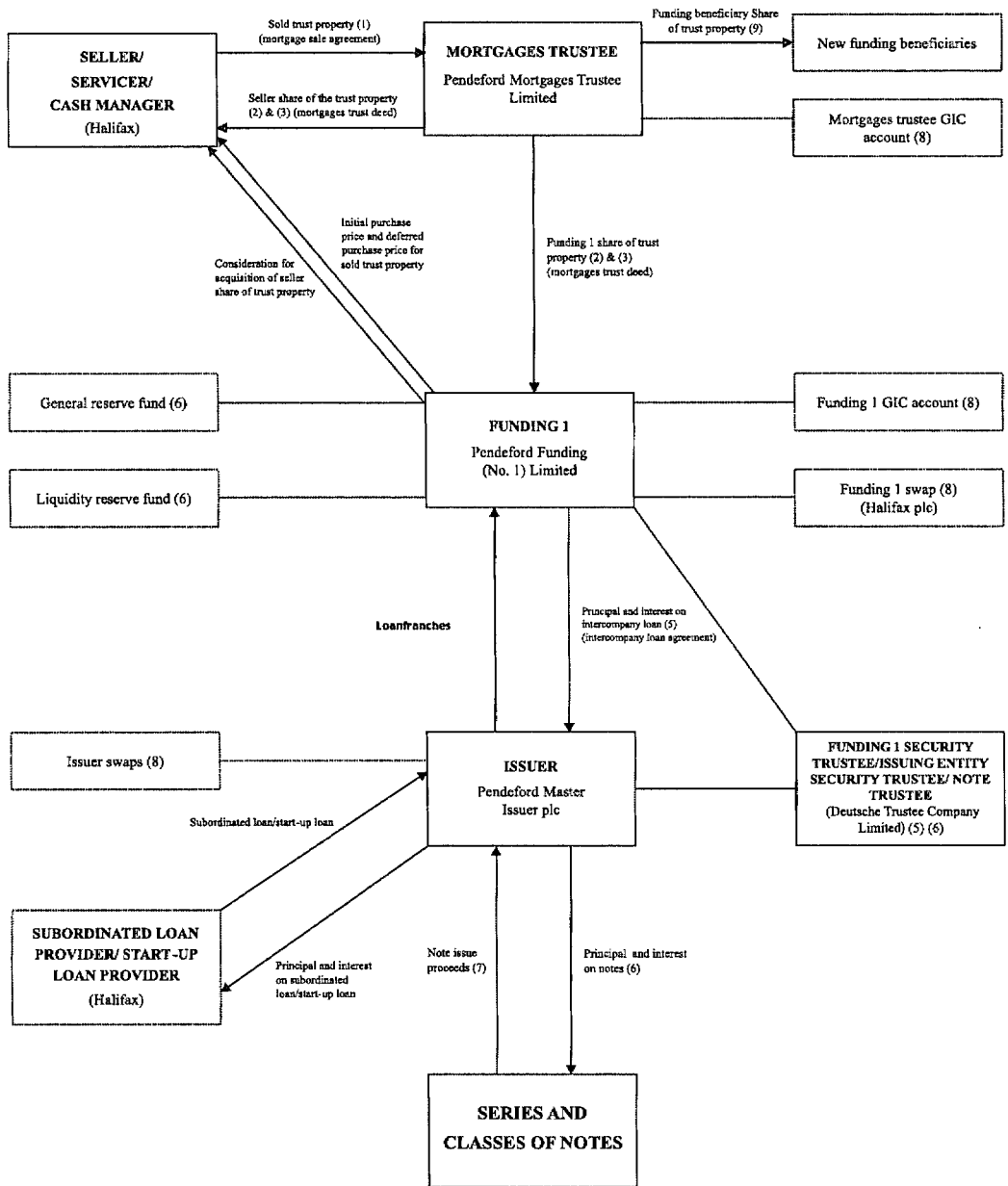
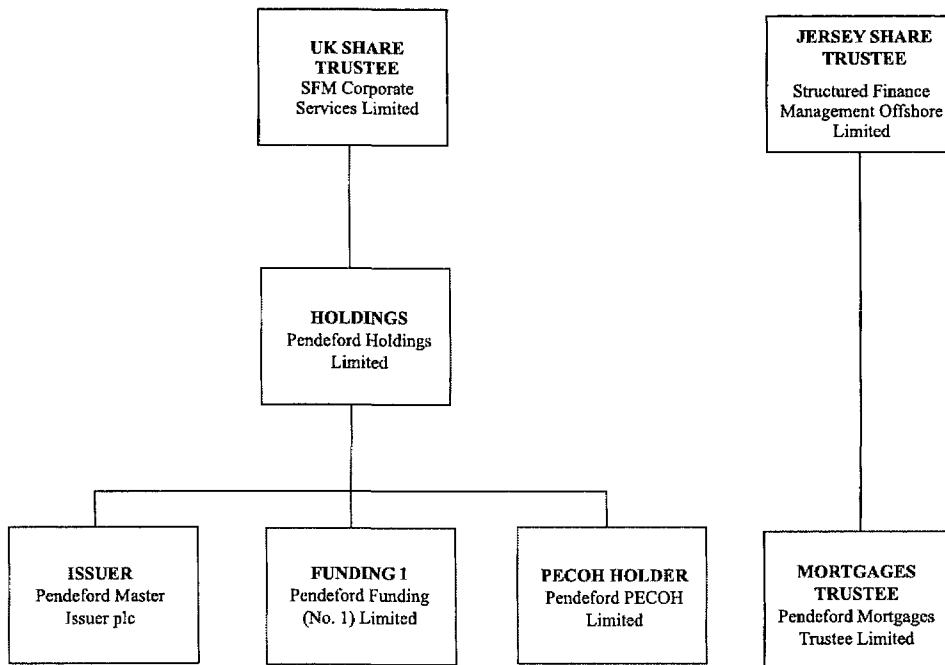


Diagram of ownership structure of special purpose vehicles



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.
- Halifax, which will organise and initiate 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 any of the entities in the diagrams above. As a result, neither any issuance of notes under the programme nor any such advance will be directly linked to the credit of Halifax, and Halifax has no obligation to support such transaction financially, although Halifax 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 “**Birmingham Midshires, Halifax plc and the HBOS group**” 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**” below.

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 will issue the notes and borrow subordinated loans and start-up loans and 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

Halifax plc is a bank incorporated in England and Wales as a public limited company. **Birmingham Midshires** is a division of Halifax plc. See "**Birmingham Midshires, Halifax plc and the HBOS group**" below.

Birmingham Midshires originated all of the loans in the initial portfolio and the **seller** (which term shall include Halifax plc and the entity which is expected to succeed to its business in accordance with the HBOS Group Reorganisation Act 2006, as further described in "**Birmingham Midshires, Halifax plc and the HBOS group**" below) will, on the programme date and from time to time, sell those loans 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 Halifax will sell the loans to the mortgages trustee, it 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, as the **servicer**, will perform 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. Halifax may not resign as servicer unless a successor servicer has been appointed. In addition, Halifax 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 will be the **Funding 1 swap provider** as described under "**The swap agreements – The Funding 1 swap**" below.

Halifax will also be appointed as 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 will also be appointed as 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.

Halifax plc 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 Halifax.

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

Halifax 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 Halifax.

The issuing entity account bank and the account bank

Bank of Scotland will be appointed 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 will be the note trustee. Deutsche Bank Trust Company Americas will act as issuing entity security trustee and Funding 1 security trustee. The note trustee will act as trustee for the noteholders under the note trust deed. The issuing entity security trustee will act as trustee for the issuing entity secured creditors under the issuing entity deed of charge. The Funding 1 security trustee will act 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 will be the principal paying agent and the agent bank. Deutsche Bank Trust Company Americas will be the US paying agent, the registrar, the transfer agent and the exchange agent. The paying agents will make payments on the notes to noteholders, the agent bank will calculate the interest rate on the notes and the registrar will maintain 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, qualification or withdrawal 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 withdrawn, qualified or reduced 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 on each interest payment date under those notes 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 Gilt-Edged and Fixed Interest 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 and each sterling-denominated note will be issued in minimum denominations of £50,000 and in integral multiples of £1,000 in excess thereof, 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 144 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, Halifax, HBOSTS, 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); or
- upon implementation by the HBOS group of the necessary arrangements, strategies, processes and mechanisms for it to comply with The Prudential Sourcebook for Banks, Building Societies and Investment Firms Instrument 2006 relating to the EU Capital Requirements Directive (see Condition 5.6).

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 or about 12 April 2007 (the **programme date**) the issuing entity and other principal parties to the programme and the related transactions will enter 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 will also have the benefit of derivatives instruments, namely the Funding 1 swap provided by Halifax, 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 will be 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

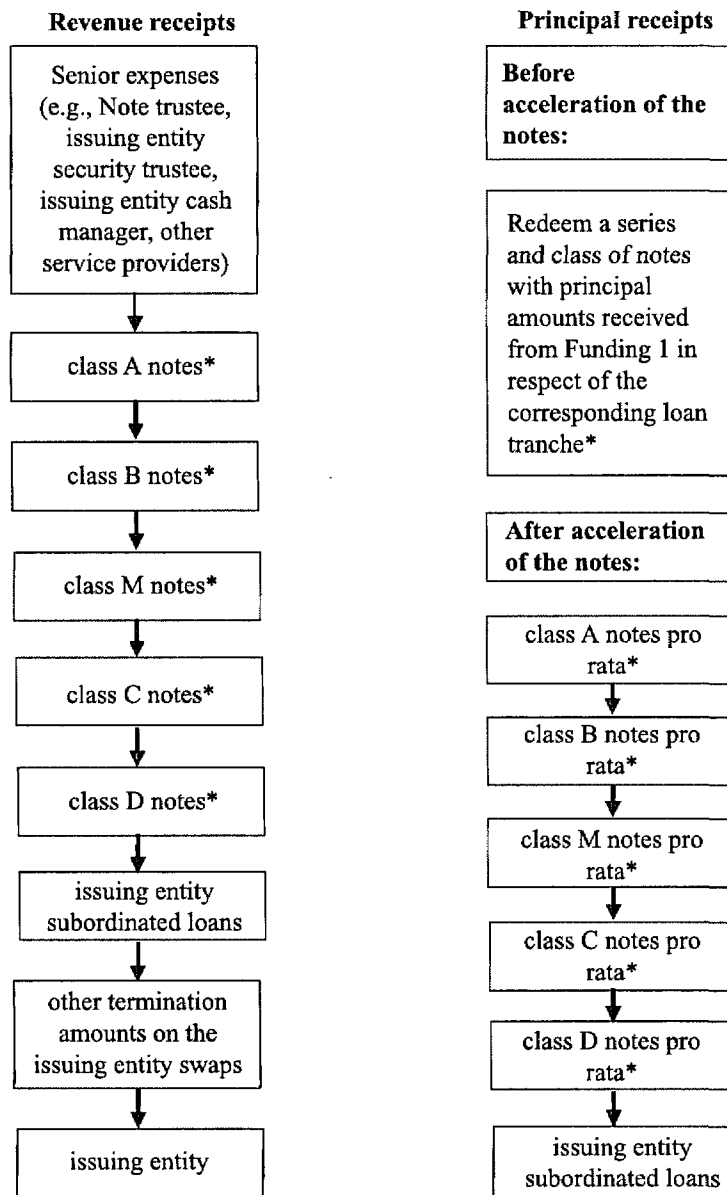
All notes will become immediately due and payable and the issuing entity security trustee will be entitled to enforce the issuing entity security on the service on the issuing entity by the note trustee of a note acceleration notice. The note trustee becomes entitled to serve a note acceleration notice 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 will be 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 will be 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.



* 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 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 programme date, 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 will be included in the portfolio as at the programme date, 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 will sell an initial portfolio to the mortgages trustee on or about the programme date, subject to the terms of the mortgage sale agreement. After the programme date, 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

As of the programme date, the mortgages trustee will hold the trust property on bare trust for the beneficiaries of the mortgages trust. As of the programme date, the **beneficiaries** of the mortgages trust will be Funding 1 and the seller only. Funding 1 and the seller will each have a joint and undivided beneficial interest in the trust property. Payments of interest and principal arising from the loans in the portfolio will be 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 will consist of the loans in the portfolio and their related security and any income generated by the loans or their related security. The trust property will also include 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 will be 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 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 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 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 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 1s 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 will 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 will enter 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 will be 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 will grant security over all of its assets in favour of the Funding 1 security trustee. As of the programme date, the Funding 1 security trustee will hold that security for the benefit of the Funding 1 secured creditors. Only the Funding 1 security trustee will be 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 will grant security over all of its assets in favour of the issuing entity security trustee. The issuing entity security trustee will hold that security for the benefit of the issuing entity secured creditors, which will, as at the programme date, be 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 will be 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 will enter 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 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 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. See “**Material Jersey (Channel Islands) tax considerations**” below.

ERISA considerations for investors

The Rule 144A notes 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 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
		Ahead of all loan tranches	Each Funding 1 interest payment date
Issuing entity cash management fee	Estimated 0.025 per cent. each year of the principal amount outstanding of the notes	Ahead of all outstanding notes	Each quarterly 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 or about 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 will not represent an obligation or be the responsibility of Halifax, HBOSTS 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 will be 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 will 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 will be 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 will be 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 will be 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 will be 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 will be 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 reduced, withdrawn or 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 reduced, withdrawn or 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 reduced, withdrawn or 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 reduced, withdrawn or 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 programme date, 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 programme date. In particular, new loans may have different payment characteristics from the loans in the portfolio as at the programme date. 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

As at the programme date, each of the loans will be originated in accordance with Birmingham Midshires’ lending criteria at the time of origination. The lending criteria as at the programme date 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 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 initial portfolio of loans does not contain any loans secured on properties valued using an automated valuation model. However, a portion of the balance of the loans added to the portfolio in the future may be originated using an automated valuation model to determine the value of the related 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.

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. The issuing entity cannot guarantee that the value of a mortgaged property will remain at the same level as on the date of origination of the related loan. If the residential property market in the United Kingdom experiences an overall decline in property values, the value of the security created by the mortgage could be significantly reduced and, ultimately, may result in losses to you if the Funding 1 security is required to be enforced.

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 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, qualification or withdrawal 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 reduced, withdrawn or 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 will be 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 will on the programme date make, 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 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**” 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 will take effect in equity only. The sale by the seller to the mortgages trustee of the Scottish mortgages on the programme date will be given effect by a declaration 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 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 (which, when a new entity has succeeded to the business of Halifax in accordance with the HBOS Group Reorganisation Act 2006, may apply also to deposits made by some borrowers with other entities in the HBOS group whose businesses are also succeeded by such entity) 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 will be 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.

Currently, a credit agreement is regulated by the CCA where (a) the borrower is or includes an “individual” as defined in the CCA, (b) 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 licensing of lenders and brokers, 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 is made before 6 April 2007, and if the form to be signed by the borrower is not signed by the borrower personally or omits or misstates 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.

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 the 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. 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**) received the Royal Assent on 30 March 2006. Once implemented, the CCA 2006 will update and augment the CCA.

From 6 April 2007, the "extortionate credit" regime will be replaced by an "unfair relationship" test, which will have retrospective effect in some cases, explicitly imposing 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 to the above legislation for guidance. The FSA principles may also be relevant and apply to the way contract terms are used in practice and not just the way they are drafted. Importantly, the test has retrospective application after a transitional period. Once the debtor alleges that an unfair relationship exists, the burden of proof is on the creditor to prove the contrary.

An alternative dispute resolution scheme for consumer credit matters is to be run by the Ombudsman. From 6 April 2007, the scheme will be mandatory for all businesses licensed under the CCA. The CCA 2006 also introduces an independent Consumer Credit Appeals Tribunal.

The DTI has indicated that, from 6 April 2008, the statutory upper financial limit of £25,000 for CCA regulation will be removed, thereby widening the scope of the CCA's regulation (for example, potentially to most buy-to-let loans over £25,000).

The OFT is to be given far broader powers under the CCA 2006. For instance, it can apply intermediate sanctions, has far greater powers of investigation and can issue indefinite standard licences. The CCA 2006 obliges creditors to comply with more stringent information requirements. The DTI has indicated that, from 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.