CAPITAL BANK Limited

(Known as Capital 1945 Limited from 20th May, 2008)

ANNUAL REPORT AND ACCOUNTS

FOR THE YEAR ENDED 31 DECEMBER 2007

Company Number 392902

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Registered Office

Charterhall House, Charterhall Drive, Chester, Cheshire, CH88 3AN

Directors' Report

The Directors have pleasure in presenting their Report and Accounts for the year ended 31 December 2007 for CAPITAL BANK Limited ('the Company')

Principal Activities

The Company is dormant and has no principal activity Under the HBOS Group Reorganisation Act 2006, the assets, liabilities, contingent liabilities and business of the Company transferred to Bank of Scotland plc on 17 September 2007 (the "HBOS Group Reorganisation") The HBOS Group Reorganisation is accounted for as a merger with effect from 1 January 2007 as explained in the Accounting Policies on page 4 Consequently all transactions and activities carried out by the Company during the period in 2007 are accounted for in Bank of Scotland plc Previously, the principal activities of the Company were the provision of financial services and following the HBOS Group Reorganisation the Company has relinquished its banking licence

On 5 December 2007, the Company re-registered from a public limited company to a private company

Business Review

The profit before tax for the year ended 31 December 2007 is £nil (2006 £148 million) as the Company has no reportable activity during the year It is intended that the Company remains dormant and is wound up in due course

Directors

The current Directors are H F Baines, Halifax Secretaries Limited and Halifax Directors Limited all of whom were appointed on 5 December 2007

The following Directors resigned on 5 December 2007, J Coyle, P J Cummings, D R Fryatt, J Morris, L Town, and A Webster

Corporate Governance

The Company follows the principles of good governance set out in the Combined Code No separate report on corporate governance is presented here as full details are contained in the Annual Report and Accounts of HBOS plc, the Company's ultimate parent undertaking

Going Concern

The Directors are satisfied that the Company has adequate resources to continue in business for the foreseeable future and consequently the going concern basis continues to be appropriate in preparing the accounts

Auditors

A resolution to re-appoint KPMG Audit Plc as auditors will be put to the members at the forthcoming Annual General Meeting

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they each are aware, there is no relevant audit information of which the Company's auditors were unaware, and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information

On behalf of the Board

For and on behalf of

Halifax Secretaries Limited

Company Secretary

25 FEBRUARY 2008

Statement of Directors' Responsibilities in Respect of the Annual Report and the Financial Statements

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

Company law requires the Directors to prepare financial statements for each financial year Under that law they have elected to prepare the financial statements in accordance with International Financial Reporting Standards ('IFRS') as adopted by the EU

The financial statements are required by law to present fairly the financial position and performance of the Company, the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation

In preparing these financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether they have been prepared in accordance with IFRS as adopted by the EU, and
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company will continue in business

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 1985 They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities

Independent Auditors' Report to the Members of CAPITAL BANK Limited

We have audited the financial statements (the "financial statements") of CAPITAL BANK Limited for the year ended 31 December 2007 which comprise the Income Statement, Balance Sheet, Cash Flow Statement, Statement of Recognised Income and Expense and the related notes These financial statements have been prepared under the accounting policies set out therein

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985 Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the Annual Report, Directors' Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 2

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 We also report to you if, in our opinion, the information given in the Directors' Report is consistent with the financial statements The information given in the Directors' Report includes that specific information presented in the Annual Report that is cross referred from the Business Review section of the Director's Report

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements Our responsibilities do not extend to any other information

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements

Opinion

In our opinion

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Company's affairs as at 31 December 2007 and of its results for the year then ended,
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the Directors' Report is consistent with the financial statements

KPMG Audit plc
Chartered Accountants
Registered Auditor KPMG Audit Plc

Saltire Court

20 Castle Terrace

Edinburgh

28 February 2008

Accounting Policies

Statement of compliance

The financial statements set out on pages 8 to 22 have been prepared in accordance with International Financial Reporting Standards ('IFRS')

The Standards adopted by the Company are those endorsed by the European Union and effective at the date the IFRS financial statements were approved by the Board

The accounts also comply with the relevant provisions of Part VII of the Companies Act 1985, as amended by the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004

Basis of preparation

The financial statements have been prepared under the historical cost basis, except that the following assets and liabilities are stated at their fair values, derivatives, financial instruments held for trading, financial instruments designated at fair value through the income statement, financial instruments classified as available for sale and investment properties

Critical Accounting Judgements

The preparation of the financial statements necessarily requires the exercise off judgement both in the application of accounting policies which are set out below and in the selection of assumptions used in the calculation of estimates These judgements are continually reviewed and evaluated based on historical experience and other factors The principal critical judgements made by the Company are as follows

Basis of Accounting

There is no specific accounting policy under IFRS that covers group reconstructions Accordingly the Company has adopted merger accounting with effect from 1 January 2007 in preparing these financial statements This follows the accounting treatment prescribed in the HBOS Group Reorganisation Act 2006 for accounting in the year in which the transfer becomes effective It is also consistent with accounting for group reconstructions under UK generally accepted accounting principals, which the Company has considered in the absence of specific IFRS guidance The comparatives for 2006 are the audited financials for the Company that were published in the Company's last Annual Report and Accounts

New IFRS standards and interpretations

The Company has reviewed the new accounting policies that are effective for accounting periods applicable to the year ending 31 December 2007 including IFRS 7 'Financial Instruments Disclosures' that replaces existing IFRS standards, including IAS 30 Disclosures in the Financial Statements of Banks' and IAS 32 'Financial Instruments Disclosure and Presentation' None of these would have had any effect on the financial statements as the Company is dormant, has no income or expenses and no assets or liabilities and no future activity is planned Accordingly the Company considers the restatement of comparatives to be impracticable

Impairment Losses on Loans and Advances

Impairment loss calculations involve the estimation of future cash flows of loans and advances based on observable data at the balance sheet date and historical loss experience for assets with similar credit risk characteristics These calculations are undertaken on a portfolio basis other than in respect of significant balances, relating principally to larger corporate customers, which are assessed individually In applying the portfolio basis the Company makes use of various statistical modelling techniques which are specific to different portfolio types Significant judgement is applied in selecting and updating these models In calculating individual impairment provisions the Company takes account of a number of relevant considerations including historical experience, future prospects of the customer, value of collateral held and reliability of information Significant judgement is supplied in estimating the impact of these considerations on the expected future cash flows

Subsidiaries

Subsidiaries and special purpose entities are entities controlled by the Company Control is defined as where the Company has power, directly or indirectly, to govern the financial and operating policies of such entities In assessing control, potential voting rights that presently are exercisable or convertible are taken into account These entities have not been consolidated In accordance with the exemption afforded by s228 of the Companies Act 1985, consolidated accounts have not been prepared CAPITAL BANK plc is consolidated within the Bank of Scotland plc group financial statements

Jointly controlled entities

Jointly controlled entities are entities over which the Company has joint control under a contractual arrangement with other parties

The attributable share of results of associates and jointly controlled entities, generally based on audited accounts, are included in the consolidated financial statements using the equity method of accounting The share of any losses is restricted to a level that reflects an obligation to fund such losses

Accounting Policies (continued)

Designation of Financial Instruments

The Company has designated its financial instruments in accordance with IAS 39 'Financial Instruments Recognition and Measurement' as follows

– Non-derivative financial assets where there is no active market and which have fixed or determinable payments are designated as 'loans and receivables'

– Derivative instruments are automatically designated as 'at fair value through the income statement' unless they form part of a hedging relationship

– Instruments that are designated 'on initial recognition to eliminate a mearsurement mismatch or where they contain an embedded derivative which is not separated from the host contract are designated 'at fair value through the income statement'

– No financial assets are designated as 'held to maturity' or held for trading

– All financial assets are classified as 'as available for sale'.

– All financial liabilites are classified as 'at amortised cost'

The resulting treatment of these financial instruments is set out in the accounting policies below

Derivatives

Derivatives are initially recognised at fair value on the date the contract is entered into and are subsequently remeasured at their fair value Where the fair value of a derivative is positive, it is carried as a derivative asset and where negative, as a derivative liability The gain or loss on remeasurement to fair value at the balance sheet date is taken to the income statement The only circumstance where this will not apply is when cash flow hedge accounting is employed

Hedge accounting allows one financial instrument, generally a derivative such as a swap, to be designated as a hedge of another financial instrument such as a loan or deposit or a portfolio of the same At inception of the hedge relationship formal documentation must be drawn up specifying the hedging strategy, the component transactions and the methodology that will be used to measure effectiveness

Monitoring of hedge effectiveness is undertaken on an ongoing basis A hedge is regarded as effective if the change in fair value or cash flows of the hedge and the hedged item are correlated within a range of 80% to 125% either for the period since effectiveness was last tested or cumulatively since inception

The Company uses three hedge accounting methods

Firstly, fair value hedging measures the change in the fair value of the derivative against the offsetting changes in the fair value of the hedged item in respect of the risk being hedged These changes in fair value are recognised through the income statement If this hedge is highly effective then the net impact on the income statement is minimised

Secondly, cash flow hedging matches the cash flows of hedged items against the corresponding cashflow of the hedging derivative The effective part of any gain or loss on the derivative is recognised directly in equity and the hedged item is accounted for in accordance with the policy for that financial instrument

In circumstances where the hedge relationship proves ineffective or is early settled or terminated then the associated gains and losses that were recognised directly in reserves are reclassified in the income statement in the same period or periods during which the asset acquired or liability assumed affects profit or loss The ineffective part of any gain or loss is recognised immediately in the income statement

Adjustments made to the carrying amount of the hedged item for fair value hedges will be amortised on an effective interest rate basis In respect of cash flow hedges, the amount deferred in reserves will either remain in equity until the designated transaction occurs or, if not expected to occur, be recognised in the income statement

A derivative may be embedded in another financial instrument, known as the host contract Where the economic characteristics and risks of an embedded derivative are not closely related to those of the host contract the embedded derivative is separated from the host and held on balance sheet at fair value Movements in fair value are posted to the income statement, whilst the host contract is accounted for according to the policy for that class of financial instrument

Loans and advances

Loans and advances are held at amortised cost less provision for impairment

The Company will assess impairment individually for financial assets that are significant and individually or collectively for assets that are not significant

Individual impairment is identified at a counterparty specific level following objective evidence that a financial asset is impaired This may be after an interest or principal payment is missed or when a banking covenant is breached The present value of estimated cash flows recoverable is determined after taking into account any security held The amount of any impairment is calculated by comparing the present value of the cash flows discounted at the loan's original effective interest rate with the balance sheet carrying value If impaired, the carrying value is adjusted and the difference charged to the income statement

Accounting Policies (continued)

The written down value of the impaired loan is compounded back to the net realisable balance over time using the original effective interest rate This is reported through interest receivable within the income statement and represents the unwinding of the discount

A write-off is made when all or part of a claim is deemed uncollectible or forgiven Write-offs are charged against previously established provisions for impairment or directly to the income statement

In circumstances where an asset has been individually assessed for impairment and no objective evidence of impairment exists, then it will be subject to a collective assessment

Collective impairment is identified for groups of assets that share similar risk characteristics

Collective impairment is assessed using a methodology based on existing risk conditions or events that have a strong correlation with a tendency to default

Loans and advances to customers include advances that are subject to non-returnable finance arrangements following securitisation of portfolios of mortgages and other advances The principal benefits of these advances were acquired by special purpose securitisation companies that fund their purchase primarily through the issue of floating rate notes These floating rate notes are accounted for through 'Debt securities in issue' on the face of the balance sheet

Finance leases, instalment credit and operating leases

Assets leased to customers that transfer substantially all of the risks and rewards incidental to ownership to the customer are classified as finance leases Together with instalment credit agreements, they are recorded at an amount equal to the net investment in the lease, less any provisions for impairment, within loans and advances to customers

The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income Lease income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return

All other assets leased to customers are classified as operating leases These assets are separately disclosed in the balance sheet and are recorded at cost less aggregate depreciation, which is calculated on a straight-line basis Operating lease rentals are recognised in operating income on a straight-line basis over the lease term Operating lease assets are reviewed for impairment when there is an indication of impairment

Goodwill

The excess of the cost of a business combination over the interest in the net fair value of the identifiable assets, liabilities and contingent liabilities at the date of acquisition, of subsidiary undertakings, associated undertakings (including jointly controlled entities) and other businesses, is capitalised as goodwill

After initial recognition, goodwill is measured at cost less any accumulated impairment losses Goodwill carried in the balance sheet is subject to a bi-annual impairment review by comparing the value in use with the carrying value When this indicates that the carrying value is not recoverable, it is written down through the income statement by the amount of any impaired loss identified

Software

Costs associated with the development of software for internal use, subject to de minimis limits, are capitalised if the software is technically feasible and the Company has both the intent and sufficient resources to complete the development Costs are only capitalised if the asset can be reliably measured, will generate future economic benefits and there is an ability to use or sell the asset

Only costs that are directly attributable to bringing the asset into working condition for its intended use are capitalised These costs include all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in a manner intended by management Other development expenditure, including software research development costs, are recognised in the income statement as an expense as incurred

Capitalised development expenditure and purchased software is stated at cost less accumulated amortisation and impairment losses Once the software is ready for use, the capitalised costs are amortised over their expected lives, generally four years Capitalised software is assessed for impairment where there is an indication of impairment Where impairment exists, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss recognised in the income statement The depreciation charge for the asset is then adjusted to reflect the asset's revised carrying amount

Subsequent expenditure is only capitalised when it increases the future economic benefits embodied in the specific asset to which it relates

Property and equipment

Property and equipment is stated at cost less accumulated depreciation and impairment losses

Accounting Policies (continued)

Freehold land is not depreciated Freehold and leasehold property, other than freehold investment property, is stated at cost and depreciated over 50 years or the length of the lease term if shorter Improvements to leasehold properties with unexpired lease terms of 50 years or less are stated at cost and are depreciated in equal instalments over the lesser of the remaining life of the lease or eight years Premiums are amortised over the period of the lease

The cost of equipment, which includes fixtures and fittings, vehicles and computer hardware, less estimated residual value, is written off in equal instalments over the expected lives of the assets, generally between three and fifteen years

Subsequent costs are included in the asset's carrying amount, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably

Property and equipment is assessed for impairment where there is an indication of impairment Where impairment exists, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss recognised in the income statement The depreciation charge for the asset is then adjusted to reflect the asset's revised carrying amount

Taxation

Income tax on the profit and loss for the year comprises current and deferred tax Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity The tax charge is analysed between tax that is payable in respect of policyholders' returns and tax that is payable on equity holder returns This allocation is based on an assessment of the effective rate of tax that is applicable to equity holders for the year

Deferred tax is provided using the Balance Sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes The following temporary differences are not provided goodwill not deductible for tax purposes, the initial recognition of assets and liabilities that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates at the balance sheet date

Other borrowed funds

Other borrowed funds comprise preference shares that are classified as debt and subordinated liabilities, all of which are held at amortised cost

Preference shares are classified as debt where they are redeemable on a specific date or at the option of the shareholders or if dividend payments are not discretionary Dividends on preference shares classified as debt are recognised in the income statement through interest payable Subordinated liabilities consist of dated and undated loan capital The interest payable is recognised in the income statement through interest payable

Collateral and netting

Assets and liabilities are shown net where there is a legal right of offset and there is an intention and ability to settle on a net basis The Company nets loans, deposits and derivative transactions where it enters into master agreements with counterparties where there is an intention and ability to settle net

Foreign currencies

The financial statements are presented in Sterling which is the Company's functional and presentation currency

Foreign currency transactions are translated into Sterling at the exchange rate prevailing at the date of the transaction

Cash and cash equivalents

Cash and cash equivalents are held for the purpose of meeting short term cash commitments rather than investing or other purposes Cash and cash equivalents consist of cash and balances with central banks that are freely available and non-equity investments with a maturity of three months or less from the date of acquisition

Effective interest rate

Revenue on financial instruments classified as loans and receivables, available for sale, or financial liabilities at amortised cost, is recognised on an effective interest rate basis This calculation takes into account interest received or paid, fees and commissions paid or received that are integral to the yield as well as incremental transaction costs The effective interest rate is the rate that discounts the expected future cash flows over the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or liability at initial recognition

Income Statement

For the year ended 31 December 2007

	Notes	2007 £ million	2006 £ million
Interest receivable		-	1,057
Interest payable		-	(921)
Net interest income		-	136
Dividend income from subsidiary undertakings		-	207
Fees and commission income		-	17
Fees and commission expense		-	(8)
Net trading income or expense		-	2
Other operating income		-	15
Net operating income			369
Administrative expenses	1	-	(149)
Depreciation and amortisation			
Property and equipment	11	-	(9)
Operating lease assets	12	-	(1)
Intangible assets other than goodwill		-	
Operating expenses			(159)
Impairment losses on loans and advances	6	-	(62)
Operating profit		-	148
Non-operating income		-	
Profit before taxation		-	148
Tax credit on profit	3	-	7
Profit after taxation		-	155
Attributable to			
Shareholders		-	155

The accounting policies on pages 4 to 7 and the notes on pages 12 to 22 form part of these accounts

Balance Sheet

As at 31 December 2007

	Notes	31 December 2007 £ million	31 December 2006 £ million
Assets			
Derivative assets	4	-	8
Loans and advances to banks		-	1,995
Loans and advances to customers	5	-	19,114
Investment securities	7	-	7
Interests in jointly controlled entities	8	-	5
Interests in subsidiary undertakings	9	-	50
Property and equipment	11	-	49
Operating lease assets	12	-	5
Current tax assets		-	34
Other assets		-	86
Prepayments and accrued income		-	17
Total assets		-	21,370
Liabilities			
Deposits by banks		-	19,848
Customer accounts		-	6
Derivative liabilities	4	-	16
Deferred tax liabilities	13	-	1
Other liabilities	14	-	4
Accruals and deferred income		-	205
Other provisions		-	1
Other borrowed funds	15	-	724
Total liabilities		-	20,805
Shareholders' equity			
Issued share capital	16	70	70
Share premium		3	3
Statutory reserve		(73)	-
Retained earnings		-	492
Shareholders' equity	17	-	565
Total liabilities and shareholders equity			21 370

Approved by the Board on 28 FEBRUARY 2008 and signed on its behalf by

For and on behalf of

Halifax Directors Limited

Director

The accounting policies on pages 4 to 7 and the notes on pages 12 to 22 form part of these accounts

Statement of Recognised Income and Expense

For the year ended 31 December 2007

	31 December 2007	31 December 2006
	£ million	£ million
Profit after taxation	-	155
Total recognised income and expense	-	155
Attributable to		
Shareholders	-	155

The accounting policies on pages 4 to 7 and the notes on pages 12 to 22 form part of these accounts

Cash Flow Statement

For the year ended 31 December 2007

	31 December 2007 £ million	31 December 2006 £ million
Profit before tax	-	148
Adjustments for		
Impairment losses on loans and advances	-	62
Depreciation and amortisation	-	10
Interest on other borrowed funds	-	33
Other non-cash items	-	(1)
Net change in operating assets and liabilities	-	1,231
Cash flows from operating activities	-	1 483
Cash flows from investing activities	-	-
Cash flows from financing activities	-	(288)
Net (decrease)/ increase in cash and cash equivalents	-	1,195
Opening cash and cash equivalents	**1,855**	660
Transfer under HBOS Group Reorganisation	**(1,855)**	-
Closing cash and cash equivalents	-	1,855

Analysis of cash and cash equivalents

	31 December 2007 £ million	31 December 2006 £ million
Cash and balances at central banks		
Loans and advances to other banks – repayable in less than 3 months	-	1,855
Closing cash and cash equivalents	-	1 855

Investing activities	31 December 2007 £ million	31 December 2006 £ million
Sale of operating lease assets	-	(1)
Purchase of property and equipment	-	(9)
Sale of property and equipment	-	10
Cash flows from investment activities	-	-

Financing activities	31 December 2007 £ million	31 December 2006 £ million
Equity dividends paid	-	(200)
Interest on other borrowed funds relating to servicing of finance	-	(33)
Repayment of subordinated loan capital	-	(55)
Cash flows from financing activities	-	(288)

The accounting policies on pages 4 to 7 and the notes on pages 12 to 22 form part of these accounts

Notes to the Accounts

1 Administrative expenses and colleagues

HBOS refers to its employees as colleagues Most UK based colleagues are contractually employed by HBOS plc, the ultimate parent company All expenses related to the employment of colleagues for whom the Company gains the benefit of their employment are recharged by HBOS to the Company The average number of colleagues recharged during the year was

	2007 Number	2006 Number
Full time	-	2 993
Part time	-	631
	-	3,624

No Directors received emoluments for qualifying services to CAPITAL BANK Limited in the year ended 31 December 2007

	2007 £ million	2006 £ million
Administrative expenses include		
Staff costs	-	73
Accommodation, repairs and maintenance	-	9
Technology	-	5
Marketing and communication	-	26

2 Auditors' remuneration

In respect of the Company, statutory audit fees were £nil (2006 £48,000) and other fees were £nil (2006 £nil) All fees are within the UK

3 Taxation

	2007 £ million	2006 £ million
Current tax- Corporation tax credit at 30 per cent (2006 – 30 per cent)	-	20
Deferred taxation (Note 13)	-	(13)
Total income tax on profit	-	7
The above tax credit is made up as follows		
Tax on shareholder returns	-	7

No tax was assessed for the year In 2006 the tax assessed is lower than the standard rate of corporation tax in the UK (30%) The difference is explained below

	2007 £ million	2006 £ million
Profit before taxation	-	148
Profit multiplied by the standard rate of corporation tax in the UK of 30% (2006 30%)	-	(44)
Effects of		
Income / expenses not taxable / deductible for tax purposes	-	57
Adjustments in respect of previous periods	-	(6)
Total income tax on profit	-	7

Notes to the Accounts (continued)

4 Derivatives

The Company used derivative instruments to hedge and reduce the interest rate exposures that are inherent in any banking business The hedge accounting strategy adopted by the Company is to utilise a macro cashflow hedge approach The remaining derivatives held by the Company are held for economic hedging purposes but do not meet the criteria for hedge accounting As such, the gain or loss arising from the change in fair value is taken to the income statement Where a derivative does not qualify for hedge accounting it is classified below as held for trading The Company has entered into derivative contracts as noted below

2006	Fair Value	
	Asset	Liability
	£ million	£ million
Derivatives held for trading		
Exchange rate related contracts		
Forward rate agreements	1	-
Cross currency swaps	1	-
Equity/index and commodity related contracts		
Options and swaps	-	10
Total derivatives held for trading	2	10
Derivatives held for hedging		
Derivatives designated as cash flow hedges		
Forward rate agreements	6	6
Total derivatives held for hedging	6	6
Total derivatives	8	16

5 Loans and advances to customers

	2007	2006
	£ million	£million
Gross loans and advances to customers	-	19,243
Impairment losses on loans and advances to customers (Note 6)	-	(129)
Net loans and advances to customers	-	19,114

Included in the above are loans to subsidiaries of £nil (2006 £11,647m) and jointly controlled entities of £nil (2006 £2,637m)

Loans and advances to customers designated as loans and receivables are measured at amortised cost on the balance sheet The fair value of loans and advances to customers is disclosed in Note 20

Gross loans and advances to customers are further analysed as follows

	2007	2006
	£ million	£million
Neither past due nor impaired	-	18,871
Past due up to 3 months but not impaired	-	97
Impaired loans	-	275
Gross loans and advances to customers	-	19,243

Notes to the Accounts (continued)

5 Loans and advances to customers (continued)

The Company's lending exposure before the deduction of impairment provisions and before taking account of collateral is analysed below

	2007 £ million	2006 £ million
Agriculture forestry and fishing	-	68
Manufacturing industry	-	139
Construction and property	-	189
Hotels, restaurants and wholesale and retail trade	-	415
Transport, storage and communication	-	142
Financial	-	14,392
Other services	-	614
Other personal lending	-	3,114
Overseas residents	-	170
	-	19 243

Loans and advances to customers include finance leases of £nil (2006 £3,477 million) analysed as follows

	2007 £ million	2006 £ million
Gross investment in finance receivables		
Within one year	-	1,916
Between one and five years	-	1 972
More than five years	-	84
	-	3,972
Less unearned finance income	-	(495)
Present value of minimum lease payments	-	3,477
Analysed as		
Within one year	-	1,683
Between one and five years	-	1,720
More than five years	-	74
Finance lease receivables	-	3,477

At 31 December 2007 the impairment provision relating to minimum lease payments receivable amounted to £nil (2006 £34m)

6 Impairment losses on loans and advances

	2007 £ million	2006 £ million
At 1 January 2007	129	150
Transfer to BOS plc under HBOS Group Reorganisation	(129)	-
New impairment provisions less releases	-	72
Amounts written off	-	(89)
Discount unwind on impaired loans and advances to customers	-	(4)
Cumulative provisions as at 31 December 2007	-	129
New impairment provisions less releases	-	72
Recoveries of amounts previously written off	-	(10)
Net charge to income statement	-	62

Notes to the Accounts (continued)

7 Investment securities

	2007		2006	
	Loans and receivables	Total	Loans and receivables	Total
	£ million	£ million	£ million	£ million
Investment securities				
Unlisted debt securities	-	-	7	7
Total investment securities	-	-	7	7

8 Interests in jointly controlled entities

	2007	2006
Interests in jointly controlled entities	£ million	£ million
At 1 January	5	5
Transfer to BOS plc under HBOS Group Reorganisation	(5)	-
At 31 December	-	5

9 Interests in subsidiary undertakings

	2007	2006
	£ million	£ million
At cost at 1 January	50	50
Transfer to BOS plc under HBOS Group Reorganisation	(50)	-
At cost at 31 December	-	50

10 Other intangible assets

Software	2007	2006
	£ million	£ million
Cost		
At 1 January	4	4
Transfer to BOS plc under HBOS Group Reorganisation	(4)	-
At 31 December	-	4
Amortisation		
At 1 January	4	3
Transfer to BOS plc under HBOS Group Reorganisation	(4)	-
Amortisation charge in year	-	1
At 31 December	-	4
Carrying value at 31 December	-	-

Notes to the Accounts (continued)

11 Property and equipment

	Property £ million	Equipment £ million	2007 Total £ million
Cost			
At 1 January 2007	58	80	138
Transfer to BOS plc under HBOS Group Reorganisation	(58)	(80)	(138)
At 31 December 2007	-	-	-
Depreciation			
At 1 January 2007	22	67	89
Transfer to BOS plc under HBOS Group Reorganisation	(22)	(67)	(89)
At 31 December 2007	-	-	-
Carrying value at 31 December 2007	-	-	-

	Property £ million	Equipment £ million	2006 Total £ million
Cost			
At 1 January 2006	51	74	125
Inter-company transfer	6	7	13
Additions	1	1	2
Disposals		(2)	(2)
At 31 December 2006	58	80	138
Depreciation			
At 1 January 2006	18	57	75
Depreciation for year	2	7	9
Disposals		(2)	(2)
Inter-company transfer	2	5	7
At 31 December 2006	22	67	89
Carrying value at 31 December 2006	36	13	49

Notes to the Accounts (continued)

12 Operating lease assets

Assets leased to customers include the following amounts in respect of operating lease assets

			2007
	Cost	Depreciation	Carrying Value
	£ million	£ million	£ million
At 1 January 2007	8	(3)	5
Transfer to BOS plc under HBOS Group Reorganisation	(8)	3	(5)
At 31 December 2007	-	-	-

			2006
	Cost	Depreciation	Carrying Value
	£ million	£ million	£ million
At 1 January 2006	9	(2)	7
Disposals	(1)	-	(1)
Depreciation charge for the year	-	(1)	(1)
At 31 December 2006	8	(3)	5

Future minimum lease payments under non-cancellable leases are expected to be received in the following periods,

	2007	2006
	£ million	£ million
1 year or less	-	-
Later than 1 year and not later than five years	-	5
	-	5

13 Deferred tax

	2007	2006
	£ million	£ million
Deferred tax liabilities	-	(21)
Deferred tax assets	-	20
Net position	-	(1)

	2007	2006
	£ million	£ million
At 1 January 2007	(1)	10
Transfer to BOS plc under HBOS Group Reorganisation	1	-
Charge to income for the year (Note 3)	-	(13)
Charges to equity	-	2
At 31 December 2007	-	(1)

Notes to the Accounts (continued)

13 Deferred tax (continued)

Analysed as follows

Deferred tax liabilities			**2007**
	Capital Allowances	**Other**	**Total**
	£ million	**£ million**	**£ million**
At 1 January 2007	**(10)**	**(11)**	**(21)**
Transfer to BOS plc under HBOS Group Reorganisation	**10**	**11**	**21**
At 31 December 2007	**-**	**-**	**-**

			2007
Deferred tax assets	**Provisions**	**Other**	**Total**
	£ million	**£ million**	**£ million**
At 1 January 2007	**18**	**2**	**20**
Transfer to BOS plc under HBOS Group Reorganisation	**(18)**	**(2)**	**(20)**
At 31 December 2007	**-**	**-**	**-**

14 Other liabilities

	2007	2006
	£ million	£ million
Other liabilities	**-**	4

Notes to the Accounts (continued)

15 Other borrowed funds

	2007 £ million	2006 £ million
Preference shares	-	136
Subordinated liabilities		
Dated	-	423
Undated	-	165
Total	-	724

Preference shares

	2007 £ million	2006 £ million
9 3/8% Non-cumulative Irredeemable Preference shares	-	136

Subordinated liabilities

	2007 £ million	2006 £ million
Dated		
£66 million floating rate notes dated seven years from 31 December 2002 extended by one year upon each anniversary thereafter unless notice is given to repay	-	66
£30 million floating rate notes 2007	-	30
£79 million floating rate notes 2007	-	79
£60 million floating rate notes 2009	-	60
£14 million floating rate notes 2009	-	14
£14 million floating rate notes 2009	-	14
£80 million floating rate notes dated five years from the 1 January following the notice of demand for repayment	-	80
£80 million floating rate notes 2009	-	80
	-	423
Undated		
£165 million floating rate notes	-	165

Notes to the Accounts (continued)

16 Share capital

The authorised share capital of the Company comprises 440 million (2006 440 million) ordinary shares of 25p each

Ordinary stock 25p each	Total £ million
Issued, allotted, called up and fully paid	
At 1 January 2006 and 1 January 2007	70
At 31 December 2006 and 31 December 2007	**70**

17 Reconciliation of shareholders equity

2007	Issued share capital £ million	Share premium £ million	Retained earnings £ million	Statutory reserve £ million	Total £ million
At 1 January 2007	70	3	492	-	565
Transfer of reserves under HBOS Group Reorganisation	-	-	(492)	(73)	(565)
At 31 December 2007	70	3	-	(73)	-

2006	Issued share capital £ million	Share premium £ million	Retained earnings £ million	Total £ million
At 1 January 2006	70	3	534	607
Profit after tax	-	-	155	155
Total recognised income and expense	70	3	689	762
Equity element of share plan tax deductions	-	-	3	3
Dividends paid in 2006 (Note 18)	-	-	(200)	(200)
At 31 December 2006	70	3	492	565

Notes to the Accounts (continued)

18 Dividends

	2007	2006
	£ million	£ million
2006 Interim dividend	-	200
	-	200

19 Commitments and contingencies

The contract amounts noted below indicate the volume of business outstanding at the balance sheet date in respect of contingent liabilities and commitments undertaken for customers They do not reflect the underlying credit and other risks, which are significantly lower, as some facilities will not be drawn down and some facilities that are drawn down will be supported by collateral

	2007	2006
	£ million	£ million
Commitments		
Up to and including 1 year	-	316
Over 1 year	-	51
	-	367

20 Fair value of financial instruments

The fair values of financial instruments are based on market prices where available, or are estimated using other valuation techniques Where they are short term in nature or reprice frequently, fair value is equivalent to the carrying value The classification adopted by the Company is shown in the following table

2006	At fair value through the income statement		Loans and receivables	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	£ million	£ million	£ million	£ million
Assets				
Derivative assets	8	8		
Loans and advances to banks			1,995	1,995
Loans and advances to customers			19,114	19,120
Investment securities			7	7
Other assets			6	6
Total financial assets	8	8	21,122	21,128

2006	At fair value through the income statement		At amortised cost	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	£ million	£ million	£ million	£ million
Liabilities				
Deposits by banks			19,848	19,848
Customer accounts			6	6
Derivative liabilities	16	16		
Other borrowed funds			724	803
Other liabilities			5	5
Total financial liabilities	16	16	20,583	20 662

Notes to the Accounts (continued)

21 Risk relating to financial instruments

The assets and liabilities of the Company as at 31 December 2006 transferred to the Bank of Scotland plc on 1 January 2006 As a consequence all the risks and rewards attaching to the financial assets and liabilities of the Company transferred to the Bank of Scotland plc on that date Accordingly, the market risks attaching to the Company's financial assets and liabilities as at 31 December 2006 from future changes in market rates are for the account of Bank of Scotland plc and not the Company Similarly, the exposure to credit and liquidity risks, in the form of exposures to future credit defaults of financial assets and undrawn commitments and the future payments of the entity's financial liabilities at 31 December 2006, are for the account of Bank of Scotland plc and not the Company

22 Related party transactions

The ultimate parent of the Company is HBOS plc The assets, liabilities, contingent liabilities and business of the Company transferred to Bank of Scotland plc on 17 September 2007 under the HBOS Group Reorganisation Act 2006 Banking transactions are entered into with other entities in the HBOS Group in the normal course of business These include loans, deposits and foreign currency transactions The net interest income received during the year was £nil (2006 - £660 million) Loans and advances to banks comprise balances owed by related parties of £nil (2006 - £2,015 million) and deposits by banks comprise amounts owed to related parties of £nil (2006 - £19,848 million) Disclosed within loans and advances to customers are balances owed to the Company by related parties of £nil (2006 - £14,284 million) During 2006 property and equipment was transferred into CAPITAL BANK Limited from Governor and Company of Bank of Scotland at net book value of £2 million As detailed in Note 1 HBOS plc is the principal employer of colleagues and staff and other costs amounting to £nil (2006 £78m) were recharged to the Company

23 Transactions with key management personnel

The Directors of the Company are considered to be the key management personnel There were no transactions during 2007 or 2006 between CAPITAL BANK Limited and key management personnel

24 Ultimate parent undertaking

Bank of Scotland plc heads the smallest group into which the accounts of the Company are consolidated The accounts of the Bank of Scotland plc may be obtained from its head office at The Mound, Edinburgh EH1 1YZ

HBOS plc is the ultimate parent undertaking of CAPITAL BANK Limited and heads the largest group into which the accounts of the Company are consolidated The consolidated accounts of HBOS plc may be obtained from its head office at The Mound, Edinburgh EH1 1YZ