THE MORTGAGE CORPORATION

(formerly The Mortgage Corporation Limited)

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 1996

TOGETHER WITH DIRECTORS' AND AUDITORS' REPORTS

The company's registered number is: 1759546

THE MORTGAGE CORPORATION

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 1996

The directors present their annual report on the affairs of the company, together with the financial statements and auditors' report for the year ended 31 December 1996.

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The principal activities of the company throughout the year were the provision of mortgage loans secured on residential properties within England, Wales and Scotland and servicing mortgages for fellow subsidiary undertakings.

The company was sold during the year. Full details of changes in ownership are provided in Note 23 to the financial statements.

On 7th August 1996 the company sold part of its mortgage portfolio and the rights to cash flows equating to the future cash flows less 0.1% on the remainder of its mortgage portfolio to Mortgage Trust Limited (see note 24). The company continues to service these mortgages.

On 7th August 1996 the company changed its status from a limited to an unlimited company, undergoing a capital restructure.

The company made a profit on ordinary activities after taxation of £5,947,436 for the year ended 31 December 1996 (1995 Profit: £6,175,342).

The directors recommend the payment of a dividend of £4,184,730.

In order to rationalise costs in 1997 both the company and Mortgage Trust Limited have agreed to operate from the same headquarters based in Epsom.

DIRECTORS AND THEIR INTERESTS

The directors who served during the year are as shown below:

P. Middleton - Chairman - (appointed 10 January 1996, resigned 7 August 1996)
R. G. Baker (appointed 7 August 1996)
M. J. Bracken (appointed 6 August 1996, resigned 7 August 1996)
C. F. Holmes (appointed 6 August 1996, resigned 7 August 1996)
N. Kheraj (resigned 6 August 1996)
P. D. Mullen (resigned 7 August 1996)
M. A. Shanahan (appointed 6 August 1996)
SPV Management Limited (appointed 7 August 1996)
A. J. Ward (appointed 14 November 1996 as alternate director to M. A. Shanahan)

The company is a wholly-owned subsidiary undertaking of Zophonous Limited, of which M. A. Shanahan, R. G. Baker, SPV Management Limited and A. J. Ward (as alternate Director to M. A. Shanahan and R. G. Baker) are directors.

None of the directors had at any time during the year any interests in the shares or contracts of the company which are required to be disclosed under the terms of the Companies Act 1985, other than SPV Management Limited under the terms of a Corporate Services Agreement dated 7 August 1996. SPV Management Limited is contracted to receive fees of £20,000 per annum and received fees of £15,000.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing those financial statements, the directors are required to:

STATEMENT OF DIRECTORS' RESPONSIBILITIES (Continued)

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

EMPLOYEE CONSULTATION

The company places considerable value on the involvement of its employees and has kept them informed by formal and informal meetings on matters affecting them as employees and on the various factors affecting the company.

On 6th August 1996 all staff employment contracts were transfered to Mortgage Trust Limited. These staff were then seconded back to the company.

EMPLOYMENT OF DISABLED PEOPLE

In line with its general policy of equal opportunity in employment practice the company supports the employment of disabled persons wherever possible, by recruitment, by retention of those who become disabled during their employment and generally through training, career development and promotion.

AUDITORS

A resolution to re-appoint the auditors, Coopers & Lybrand, will be proposed at the annual general meeting.

POST BALANCE SHEET EVENT

Subsequent to the year end, on 28th May 1997, the company acquired the entire share capital of certain BES companies, as detailed in note 21.

BY ORDER OF THE BOARD,

Sir William Atkins House
2 Ashley Avenue
Epsom
Surrey
KT18 5AS

23 July 1997

Director on behalf of
SPV Management Limited

Auditors' report to the members of THE MORTGAGE CORPORATION :

We have audited the financial statements on pages 4 to 18.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As described on pages 1 and 2 the company's directors are responsible for the preparation of the financial statements. It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

BASIS OF OPINION

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

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

OPINION

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 December 1996 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Coopers & Lybrand

Coopers & Lybrand
Chartered Accountants and Registered Auditors
Croydon

24 July 1997

THE MORTGAGE CORPORATION

PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31 DECEMBER 1996

Continuing Operations	Notes	£'000	1996 £'000	1995 £'000 (restated)
Operating Income	2		24,086	33,647
Income from mortgages subject to non-recourse funding:				
Income		4,550		
Expenses		(4,491)		
			59	-
TURNOVER			24,145	33,647
Cost of funding	3		(9,029)	(14,069)
GROSS PROFIT			15,116	19,578
Administrative expenses			(7,647)	(9,531)
Exceptional administration credit/(expense)	4		9,935	(5,017)
			2,288	(14,548)
OPERATING PROFIT			17,404	5,030
Costs of integration	5		(5,128)	-
Interest receivable and similar income			1,107	1,145
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	6		13,383	6,175
Tax on profit on ordinary activities	8		(7,435)	-
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION			5,948	6,175
Dividend	9		(4,184)	-
RETAINED PROFIT FOR THE FINANCIAL YEAR	19		1,764	6,175
RETAINED DEFICIT BROUGHT FORWARD			(67,338)	(73,513)
Capital Restructure			65,574	-
RETAINED PROFIT / (DEFICIT) CARRIED FORWARD			-	(67,338)

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

There were no other recognised gains or losses in the current year (1995 - £Nil).

THE MORTGAGE CORPORATION

BALANCE SHEET - 31 DECEMBER 1996

	Notes	£'000	1996 £'000	1995 £'000 (restated)
FIXED ASSETS				
Tangible assets	10		484	2,610
Properties	11		14,288	14,288
			14,772	16,898
MORTGAGE DEBTORS				
Mortgage debtors	12		-	193,763
Mortgage debtors subject to non-recourse funding	13			
Mortgage debtors		140,712		
less : non-recourse funding		(140,712)		
			-	-
Mortgage debtors securitised	14		856,652	1,113,572
CURRENT ASSETS				
Debtors:				
- due after a year	15		9,891	11,234
- due within a year	15		13,919	15,952
Cash at bank and in hand	16		22,913	10,577
			46,723	37,763
TOTAL ASSETS			918,147	1,361,996
CAPITAL AND RESERVES				
Called-up share capital	17		13,286	67,500
Share premium account	18		-	11,360
Profit and loss account			-	(67,338)
EQUITY SHAREHOLDERS' FUNDS	19		13,286	11,522
PROVISION FOR LIABILITIES AND CHARGES	20		4,309	5,055
CREDITORS:				
- due within a year	21		35,141	184,728
- due after a year	21		865,411	1,160,691
			918,147	1,361,996

The financial statements on pages 4 to 18 were approved by the board of directors on 23 July 1997 and were signed on its behalf by:

Director on behalf of
SPV Management Limited

1. PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies, all of which have been applied consistently throughout the current year and the preceding year, are set out below.

(a) Basis of Accounting

The financial statements are prepared under the historical cost convention and are in accordance with applicable accounting standards.

Under the provisions of Financial Reporting Standard No. 1 (Revised), the company has not prepared a cash flow statement because its ultimate parent undertaking, Seahorse Limited, which is registered in England and Wales as an overseas company, has prepared consolidated financial statements which include the cash flows of the company for the year.

(b) Turnover

Turnover comprises interest, servicing fees, commissions and miscellaneous fee income recognised as it becomes receivable. Interest includes that which is recoverable from the Inland Revenue under MIRAS (mortgage interest relief at source).

(c) Depreciation

Depreciation is provided at rates calculated to write-off the cost of fixed assets on a straight-line basis over their expected useful life, as follows:

Leasehold improvements	Over the life of the lease to a maximum of 20 years
Fixtures, fittings and equipment	4 - 5 years
Computer equipment	3 - 5 years
Motor cars	3 years

(d) Pension Costs

The company accounts for pension costs in accordance with Statement of Standard Accounting Practice 24. For the defined contribution scheme, the charge recorded in the profit and loss account is the amount of contribution payable in respect of the year, plus administration costs incurred by the fund.

Further information on pension costs is provided in note 22b.

(e) Leases

Rentals under operating leases are primarily charged on a straight-line basis to the profit and loss account over the term of the lease. Where the company has vacated or intends to vacate space a provision is established for the estimated net future liability of the space vacated.

(f) Taxation

Corporation tax is provided on taxable profits at the current rate.

Deferred taxation is calculated on the liability method at the rate of tax at which the liability is likely to be paid. Deferred taxation is provided to take account of the difference in timing between certain items for financial statement purposes and taxation purposes. Deferred taxation is not provided on timing differences which, in the opinion of management, will probably not reverse.

1. **PRINCIPAL ACCOUNTING POLICIES (Continued)**

(g) **Mortgage Advances**

Mortgage advances comprise loans which are secured by way of a mortgage over freehold and leasehold residential properties located in Great Britain.

Mortgage advances include properties in possession and are stated after deducting a provision for loan losses. The provision is maintained at a level that is considered adequate by management to absorb losses inherent in the loan portfolio of the company. A judgement as to the adequacy of the provision is made at year end and includes anticipated recoveries under mortgage indemnity guarantees and other insurance policies. Should the provision be judged inadequate either because of reductions due to write-offs or because of changes to the size and characteristics of the portfolio, the provision is increased and charged to other operating expenses in the current year.

(h) **Properties**

Properties are recorded at cost less provisions for permanent diminution in value and represent properties which have been sold to non-group companies organised under a business expansion scheme ("BES"). As more fully described in note 21, the company has granted an option which may require the company to repurchase these properties at a future date. Therefore, the company has not accounted for these transactions as a sale, and a corresponding liability is reported in creditors.

The liability is adjusted at each year end based on management's estimate of the future liability that may arise and the movement is charged or credited to the profit and loss account.

(i) **Securitisation of Mortgage Debtors**

During the period 1987 through 1992, the company entered into a series of transactions under which it sold pools of residential mortgages to fellow subsidiaries (referred to as Special Purpose Vehicles - "SPVs") of its immediate parent. Each SPV issued debt, the proceeds of which were used to finance the purchase of mortgages from the company.

The company does not hold any of the issued share capital of the SPVs but has entered into servicing agreements with the SPVs to administer their mortgage portfolios. For certain of these SPVs the company is required to provide liquidity support facilities and limited indemnities against shortfalls arising on the sale of repossessed properties.

Servicing fees are earned by the company from each SPV calculated on excess earnings as defined in the relevant servicing agreements.

(j) **Assets and Liabilities Recognised by The Company**

In order to comply with the requirements of Financial Reporting Standard No. 5 ("FRS No. 5"), the company has separately presented on its balance sheet assets securitised under the arrangements summarised in note 1 (i). The corresponding financing obligations for these assets are classified as floating rate notes and credit facilities within creditors.

This treatment is deemed appropriate because the directors have concluded, on the basis of reasonable assumptions, that the company retains significant interest and control in the performance of assets sold to the SPVs for the purpose of securitisation.

The company has also presented on its balance sheet in a linked presentation format mortgage advances for which it has sold the rights to cash flows equating to the future cash flows less 0.1% to Mortgage Trust Limited.

1. **PRINCIPAL ACCOUNTING POLICIES (Continued)**

(k) **Related Party Disclosures**

Under the provisions of Financial Reporting Standard No. 8 ("FRS No.8"), the company has taken advantage of the exemption provided, for subsidiary undertakings whose voting rights are controlled within the group, from disclosing group related party transactions. The consolidated financial statements of Seahorse Limited, in which these results are included, are publicly available.

(l) **Format of Accounts**

The cost of funding heading within the profit and loss account has been adapted from that prescribed by Schedule 4 to the Companies Act 1985 in view of the nature of the business. Mortgage debtors have been presented separately on the face of the balance sheet rather than included as part of current assets. In the opinion of the directors, this departure from the format of Schedule 4 of the Companies Act 1985 is required to give a true and fair view of the state of the company's affairs since to present mortgage advances as part of current assets would not fairly reflect the liquidity of these assets.

There are changes of presentation from previous years where interest receivable from bank deposits was included within turnover and provisions for mortgage related charges which were included under provisions for liabilities and charges are now presented within debtors. The comparative figures have been restated accordingly.

2. **OPERATING INCOME**

Operating income comprises:

	1996 £'000	1995 £'000 (restated)
Servicing fees	10,840	18,363
Interest income	10,439	13,493
Commission income and miscellaneous fees	1,207	1,791
Premium on sale of assets	1,600	-
	24,086	33,647

All income and the profit on ordinary activities is derived from the company's principal activities relating to mortgage advances offered in Great Britain.

3. **COST OF FUNDING**

Cost of funding comprises:

	1996 £'000	1995 £'000
Interest on intercompany borrowings	6,613	10,476
Interest on bank loans and other	1,722	2,196
Interest on subordinated loan	694	1,397
	9,029	14,069

With the exception of interest on subordinated loan, interest expense relates to short-term borrowings. The subordinated loan was repaid on 6th August 1996.

4. EXCEPTIONAL ADMINISTRATION CREDIT / (EXPENSE)

	1996 £'000	1995 £'000 (restated)
Release of loan loss provisions	7,000	-
Compound interest provision	2,935	(5,017)
	9,935	(5,017)

5. COSTS OF INTEGRATION

	1996 £'000	1995 £'000
Severance payments paid and accrued	1,084	-
Severance related professional fees	115	-
Provision for costs of vacated property	2,230	-
Write down of leasehold improvements	1,699	-
	5,128	-

6. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

Profit on ordinary activities before taxation is stated after charging (crediting):

	1996 £'000	1995 £'000
Provisions for loan losses	(4,704)	(3,443)
Staff costs (note 7)	4,854	5,123
Depreciation	518	603
Exceptional depreciation (note 5)	1,699	-
Hire of equipment - operating leases	22	45
Hire of other assets - operating leases	1,571	1,501
Auditors' remuneration - audit	11	37
Auditors' remuneration - non audit	-	4

7. STAFF COSTS

Particulars of employees including executive directors are shown below:

Employee costs during the year amounted to:

	1996 £'000	1995 £'000
Wages and salaries	4,256	4,473
Social security costs	336	363
Other pension costs (note 22b)	262	287
	4,854	5,123

The average monthly number of persons employed by the company during 1996 was 174 (1995 - 191). On 6th August 1996 the contracts of employment of 180 employees were transfered to Mortgage Trust Limited. These employees have been seconded back to the company under a secondment agreement and have continued to be paid by the company (see note 24). The disclosure of these employees and their remuneration has been included above.

7. **STAFF COSTS (Continued)**

Directors' remuneration in respect of directors of the company was as follows:

	1996 £'000	1995 £'000
Fees	2	-
Other emoluments (including pension contributions and benefits in kind)	170	159
	172	159

The directors' remuneration shown above (excluding pensions and pension contributions) included:

	1996 £'000	1995 £'000
Chairman	-	-
Highest paid director	170	159

Directors received emoluments (excluding pensions and pension contributions) in the following ranges:

	1996	1995
£ 0 - £ 5,000	8	3
£ 155,001 - £ 160,000	-	1
£ 165,001 - £ 170,000	1	-

8. **TAX ON PROFIT ON ORDINARY ACTIVITIES**

The tax charge is based on the profit for the year and comprises:

	1996 £'000	1995 £'000
UK Corporation tax at 33% (1995 : 33%)	5,213	-
Underprovision of current taxation in respect of prior years	2,222	-
	7,435	-

Prior to the change of ownership of the company, some of the taxable profits of the company were covered by group relief and some of the taxable losses of the company were surrendered to other group companies, both for nil consideration. Since the change of ownership, group relief received by the company has been paid for, for a consideration amounting to 33% of the losses surrendered.

Included in the tax charge for the year is a provision for taxation on the exceptional items in notes 4 and 5 of £2.883 million.

9 **DIVIDEND PAYABLE**

	1996 £'000	1995 £'000
Ordinary final dividend proposed of £0.315p per share	4,184	-

10. TANGIBLE FIXED ASSETS

The movement in the year was as follows:

	Computer Equipment	Motor Cars	Leasehold Improvements	Fixtures, Fittings & Equipment	Total
	£'000	£'000	£'000	£'000	£'000
COST-					
Beginning of year	3,259	205	2,683	2,136	8,283
Additions	76	-	71	-	147
Disposals	(6)	(103)	-	-	(109)
End of year	3,329	102	2,754	2,136	8,321
DEPRECIATION-					
Beginning of year	2,861	83	731	1,998	5,673
Charge	256	25	1,883	53	2,217
Disposals	-	(53)	-	-	(53)
End of year	3,117	55	2,614	2,051	7,837
NET BOOK VALUE					
Beginning of year	398	122	1,952	138	2,610
End of year	212	47	140	85	484

11. PROPERTIES

	1996 £'000	1995 £'000
Cost		
At beginning and end of year	14,879	14,879
Provisions		
At beginning and end of year	591	591
Net Book Value		
At beginning and end of year	14,288	14,288

12. MORTGAGE DEBTORS

Mortgage debtors comprise:

	1996 £'000	1995 £'000
Completed advances	-	197,588
Provisions for loan losses	-	(3,825)
	-	193,763

Mortgage debtors are all due to be repaid after more than one year. The rights to cash flows equating to the future cash flows less 0.1% of these debtors were sold to a Mortgage Trust Limited on 7th August 1996. That company is holding the provisions for loan losses on these mortgages.

13. **MORTGAGE DEBTORS SUBJECT TO NON-RECOURSE FUNDING**

	1996 £'000	1995 £'000
Mortgage debtors	136,879	-
Investments	3,833	-
	140,712	-
less : non-recourse funding	(140,712)	-
	-	-

On 7th August 1996, the company sold the cash flows equating to the future cash flows less 0.1% on a mortgage portfolio of £146.8m to Mortgage Trust Limited (see note 24). Investments represent redemption proceeds on mortgage debtors.

In accordance with Financial Reporting Standard Number 5 "Reporting the substance of transactions", these mortgages have been included in these financial statements using linked presentation, whereby the non-recourse funding is shown deducted from the mortgage debtors.

The directors confirm that:

(a) The company is not obliged to support any losses of its independent providers of finance, nor does it intend to do so: and

(b) The providers of finance have agreed in writing that they will only seek repayment of finance, as to both principal and interest, to the extent sufficient funds are generated by or attached to the mortgages they have financed and they will not seek recourse in any other form.

The company has no option or obligation to purchase the mortgages concerned.

14. **ASSETS SECURITISED**

	1996 £'000	1995 £'000 (restated)
Mortgage debtors	839,712	1,082,948
Investments	25,699	44,384
	865,411	1,127,332
Provisions for mortgage related charges	(8,759)	(13,760)
	856,652	1,113,572

Investments represent redemption proceeds on mortgage debtors. The total of mortgage debtors and investments secure the credit facilities and floating rate notes reported in creditors (see note 21).

Provisions for mortgage related charges primarily consist of shortfalls on the sale of repossessed properties and associated insurance claims by fellow subsidiary undertakings, as well as other liabilities relating to its fellow subsidiary undertakings.

Other net assets of the SPVs including capitalised issue costs of £2,073,067 (1995 - £4,752,820), from which the company will not obtain economic benefit, have been excluded from the financial statements of the company.

15. DEBTORS

The following are included in the net book value of debtors:

	1996 £'000	1995 £'000
Amounts due after more than one year:		
Due from group undertakings	8,845	11,234
ACT recoverable	1,046	-
	9,891	11,234
Amounts falling due within one year:		
Due from group undertakings	10,869	9,196
Prepayments and accrued income	2,956	4,158
Other debtors	94	2,598
	13,919	15,952
Total debtors	23,810	27,186

Amounts due from group undertakings due after more than one year are in respect of subordinated loans which are currently non-interest bearing. The loans may be repaid in whole or in part provided the subsidiaries have sufficient assets to meet their other obligations and liabilities. The balance shown is after a provision of £581,122 (1995 - £269,744) for uncollectable amounts.

16. CASH AT BANK AND IN HAND

Cash at bank and in hand at 31 December 1996 includes segregated funds of £10,128,502 (1995 - £10,245,426) which have been established to meet potential claims by fellow subsidiary undertakings for losses on current and future repossessed properties (see note 20).

17. CALLED-UP SHARE CAPITAL

	1996 £'000	1995 £'000
Authorised:		
170,000,000 ordinary £1 shares	170,000	170,000
30,000,000 non-redeemable preference shares of £1 each	30,000	30,000
	200,000	200,000
Allotted, called-up and fully paid ordinary £1 shares	13,286	67,500

On 7th August 1996 the company changed its status from a limited to an unlimited company. The balances on share capital and share premium were partially used to eliminate negative retained earnings.

18. SHARE PREMIUM ACCOUNT

	1996 £'000	1995 £'000
Beginning of the year	11,360	11,360
Capital restructure	(11,360)	-
End of the year	-	11,360

19. RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

	1996 £'000	1995 £'000
Profit for the year	5,948	6,175
Dividend	(4,184)	-
	1,764	6,175
Opening shareholders' funds	11,522	5,347
Closing shareholders' funds	13,286	11,522

20. PROVISION FOR LIABILITIES AND CHARGES

The provision for liabilities and charges comprises:

	1996 £'000	1995 £'000 (restated)
Provisions for mortgage related charges:		
Beginning of the year	3,779	-
Charge for the year	-	6,399
Utilised for the year	(2,643)	(2,620)
End of the year	1,136	3,779
Lease costs		
Beginning of the year	1,276	1,923-
Charge for the year	2,230	-
Utilised for the year	(333)	(647)
End of the year	3,173	1,276
	4,309	5,055

Provisions for mortgage related charges include provisions for the reversal of compound interest and provisions for uninsured losses on future repossessed properties, the related mortgages being owned by fellow subsidiary undertakings.

Lease costs represent a provision for the estimated future payments on vacated premises let by and sublet by the company. The estimated future payments are net of income from sub-leasing the vacant space.

21. CREDITORS

The following are included in creditors:

	1996 £'000	1995 £'000
Amounts falling due within one year:		
Bank overdrafts	212	403
Due to group undertakings	-	178,265
UK corporation tax payable	4,044	-
ACT Payable	1,046	-
Other taxation and social security	198	360
Other creditors and accruals	25,457	5,700
Ordinary dividend payable	4,184	-
	35,141	184,728
Amounts falling due after more than one year:		
Floating rate notes	865,411	1,111,333
Credit facilities	-	16,000
Other creditors	-	18,358
Due to group undertaking	-	15,000
	865,411	1,160,691
	900,552	1,345,419

Floating rate notes and credit facilities represent the financing obligations of fellow subsidiaries, which fall due after 5 years, whose securitised assets have been separately presented on the balance sheet of the company.

Other creditors due within one year (1995 after more than one year) includes amounts provided through three business expansion schemes ("BES"). Under the terms of the transaction, the company sold repossessed properties to three BES companies, who in turn marketed them as rental properties. In connection with the sale, the company granted an option to each of the BES companies. The option, if exercised, would require the company to repurchase the properties at such a price that will enable the BES companies to make a distribution on a winding up of £1.37 for each £1 invested by their shareholders. Therefore, the company has not accounted for the transaction as a sale. The option was exercisable at any time between 1 June 1997 and 10 July 1997.

Subsequent to the year end, on 28th May 1997, in relation to the above options, the company acquired the entire share capital of the three BES companies: Cavendish Homes No.1 plc, Cavendish Homes No.2 plc and Cavendish Homes No.3 plc for a consideration of £20,652,750 (including stamp duty of £102,750). Subsequent to their acquisition, on 25th June 1997 the BES companies exercised their options, resulting in the company acquiring the BES properties from them for a consideration of £18,484,052. On 26th June 1997, Mortgage Trust Limited then exercised its call option (see note 24(v)), and acquired these properties from the company for a consideration of £14,916,900, being their market value at that time.

22. GUARANTEES AND OTHER FINANCIAL COMMITMENTS

(a) Lease Commitments

The company has entered into operating leases in respect of equipment, the payments for which extend over a period not exceeding 3 years. The total annual rental for 1996 was £21,594 (1995 - £44,943).

In addition, the company leases certain land and buildings on short and long term leases. The annual rental on these leases for 1996 was £1,571,128 (1995 - £1,501,128). The rents payable under these leases are subject to re-negotiation at various intervals specified in the leases. The leases also require the company to pay insurance, maintenance and repairs of the properties.

The minimum annual rentals under non-cancellable leases are as follows:

	1996 £'000		1995 £'000	
	Property	Equipment	Property	Equipment
Operating Leases which expire:-				
within 1 year	-	-	-	-
within 2 - 5 years	-	41	-	12
after 5 years	1,571	-	1,501	-
	1,571	41	1,501	12

The minimum annual rental payment of £1,571,128 will be reduced by £617,100 through the sub letting of vacated space in 1997.

(b) Pension Arrangements

Eligible employees of the company participate in The Mortgage Corporation Pension Plan ("the Plan"). The Plan is a funded pension scheme providing defined contribution benefits and insured death benefits.

The assets of the Plan are held separately from those of the company and are administered by a trustee.

Total costs relating to the Plan for 1996 were £261,934 (1995 - £286,702).

23. CHANGES IN OWNERSHIP AND ULTIMATE PARENT COMPANY

On 6 August 1996 the company was acquired by FNBS Cayman Limited (later re-named Hippocampus Limited), registered in the Cayman Islands, which at that time was a 100% subsidiary of First National Building Society, registered in the Republic of Ireland.

As part of a group reorganisation within First National Building Society, on 7 August 1996 the company was acquired by FNBS Cayman Holdings Limited (later re-named Zophonus Limited), incorporated in the Cayman Islands and registered in England and Wales as an overseas company, a 100% subsidiary of First National Building Society. Subsequent to this transaction on 7 August 1996 Zophonus Limited was acquired by SeaHorse Limited, registered in the Cayman Islands. The shares in SeaHorse Limited are held under a Declaration of Trust for charitable purposes, the charitable trust being registered in the Cayman Islands, and the directors regard this Cayman Trust as the ultimate parent undertaking.

23. **CHANGES IN OWNERSHIP AND ULTIMATE PARENT COMPANY (Continued)**

The largest and smallest group into which the company is consolidated is that of Seahorse Limited. Copies of the consolidated financial statements may be obtained from The Secretary, Sir William Atkins House, 2 Ashley Avenue, Epsom, Surrey, KT18 5AS.

Prior to 6 August 1996, the company was a wholly owned subsidiary of Salomon Brothers Europe Limited, registered in England and Wales, a 100% subsidiary of Salomon Inc, incorporated in the State of Delaware, USA.

24. **RELATED PARTY TRANSACTIONS**

The company has identified the following transactions which are required to be disclosed under the terms of Financial Reporting Standard Number 8 "Related Party Transactions" ("FRS 8").

(a) **Transactions with Senior Management**

At the balance sheet date the company had entered into one secured loan totalling £89,000 with a senior manager of the Company.

This is at a commercial interest rate.

(b) **Transactions with Mortgage Trust Limited. ("MTL")**

On 7th August 1996, the company entered into the following transactions with MTL, a company under common control, as defined by FRS 8:

(i) A mortgage sale agreement with MTL under which the company sold a mortgage portfolio of £40.2 million for consideration of £41.3 million. Under the terms of this agreement, the company continues to administer the mortgage assets on behalf of MTL and earnt fees of £17,639 in the period to 31st December 1996.

(ii) An agreement with MTL under which the company sold cash flows equating to the future cash flows less 0.1% on a mortgage portfolio of £146.8 million for consideration of £150.8 million. The company earnt fees of £59,242 in the period to 31st December 1996.

(iii) A secondment agreement under which the company agreed to second back from MTL a number of the company's employees (see note 7). MTL has not charged any costs to the company for services of the secondees during the year as all costs of these staff were paid directly by the company.

(iv) A consultancy agreement, under which MTL can provide consultancy services to the company at the latter's request. During the year MTL provided no such consultancy services.

(v) MTL purchased for consideration of £1, an option to buy certain properties from the company at their market value. Their current book value at 31 December 1996 was £14.3 million. This option is exercisable before 31 August 1997. Subsequent to the year end on 26th June 1997, MTL exercised its call option, and acquired these properties from the company for a consideration of £14,916,900, being their market value at that time.

(vi) MTL purchased for consideration of £1 an option to buy the equitable title for the mortgages noted in (ii) above. This option is exercisable within 21 years from 7th August 1996.

(vii) MTL acquired the cash flows relating to servicer loans of £5.875 million for which it paid £5.288 million.

24. **RELATED PARTY TRANSACTIONS (Continued)**

(c) **Transactions with Salomon Brothers Europe Ltd. and other Salomon owned companies ("Salomon's")**

(i) The company had net borrowings from Salomons of £193,265,000 at the beginning of the year. On 6th August the net borrowings of £185,419,000 were repaid to Salomons.

(ii) Included within the profit and loss account are £234,000 of investment income and £6,613,000 of interest payable on inter company borrowings relating to the above loans.

(iii) Included within the profit and loss account are £170,000 of directors emoluments which were recharged from Salomon's for the services of one of the directors of the company.