Company No. 1997277

THE MORTGAGE BUSINESS plc

ACCOUNTS

FOR THE YEAR ENDED 31 DECEMBER 2006

THE MORTGAGE BUSINESS plc

ACCOUNTS FOR THE YEAR ENDED 31 DECEMBER 2006

CONTENTS

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2006

The Directors present their Report and the audited financial statements for the year ended 31 December 2006

Business Review

The principal activity of the Company is the provision of mortgage loans and associated services

The Company is a subsidiary of CAPITAL BANK plc, itself a subsidiary of HBOS plc

The Company has no employees It uses the services of its immediate parent undertaking for which a management charge is made

Risk Management

The key risks and uncertainties faced by the Company are managed within the framework established for the HBOS group

Credit risk

The Company has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis and are performed on all customers Credit evaluations are continually reviewed and evaluated

There are no significant concentrations of credit risk, except in the UK mortgages market

Liquidity risk

The Company is funded by its immediate parent and, as a result, liquidity risk is managed within the HBOS group

Market risk

The primary market risk faced by the company is interest rate risk

Interest rate risk exists where the company's financial assets and liabilities have interest rates set under different bases or are reset at different times The risk is managed using an earnings at risk methodology

In respect of income earning financial assets and interest bearing financial liabilities, their effective interest rates at the balance sheet date and the periods in which they will reprice is disclosed in note 17

Operational Risk

Operational risk is managed by The Mortgage Business plc's Risk Committee which provides information on risks to the Group Operational Risk team to process within the HBOS Operational Risk Framework The main components of the Group Operational Risk Framework include risk and control assessment, internal loss reporting, capture of risk event information, key risk indicator monitoring and evaluation of external events

continued

THE MORTGAGE BUSINESS plc

DIRECTORS' REPORT (continued)

Performance

The key performance indicators used by management in assessing the performance of the Company are the review of net loans and advances to customers, loans and advances to customers (as detailed on the balance sheet), the interest margin on these outstanding balances and the ratio of impairment losses to loans and advances to customers These are detailed in monthly management accounts which are reviewed by the Directors and discussed below

The Company has conducted its activities throughout the year in a satisfactory manner

The Company's profit before tax for the financial year is £115,555,000 (2005 £145,900,000) This represents a decrease in profit before tax of 20 8%

This is mainly due to the movement in net interest receivable which has decreased by £21,933,000 following increases in redemptions of products with higher margins impacting interest receivable and increases in bank base rate increasing the interest payable in the year The net interest margin has decreased from an average of 1 3% in 2005 to 1 2% in 2006

Impairment losses on loans and advances have increased mainly due to the value of amounts written off during the year and an increase in the collective impairment provision following an increase in loans and advances to customers This is partially offset by a decrease in individual impairment due to impairment releases made during the year The ratio of impairment losses to loans and advances to customers has increased to 0 2% (2005 0 1%)

The profit margin has been positively impacted by a 20% increase in fees and similar charges

The balance sheet has total assets of £9,623,550,000 in 2006 (2005 £8,714,063,000) This movement is due to a full year positive net lending position in 2006 of £925,382 (2005 negative net lending of £599,618)

Future Developments

The company is committed to providing competitively priced secured mortgages and will continue to develop its product offerings to meet the needs of its customers

No significant change in the company's activities is foreseen at the present time

Results and Dividends

The results for the year are shown in the Income Statement on page 10 The Directors paid an interim dividend of £110,250,000 (2005 £136,117,000) during the year

continued

Results

	£000
The accounts of the company show a profit for the financial year of	80,888
2006 interim dividend paid in 2006	(110,250)
	(29,362)
The balance of reserves brought forward at 1 January 2006 was	280,569
Leaving a balance of reserves to be carried forward of	251,207

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

Supplier payment policy

The company's suppliers are paid through HBOS plc's centralised Accounts Payable department

For the forthcoming period HBOS plc's policy for the payment of suppliers will be as follows

- Payment terms will be agreed at the start of the relationship with the supplier and will only be changed by agreement,
- Standard payment terms to suppliers of goods and services will be 30 days from the date of a correct invoice that has been received for satisfactory goods or services which have been ordered and received unless other terms are agreed in a contract,
- Payment will be made in accordance with the agreed terms or in accordance with the law if no agreement has been made, and
- Suppliers will be advised without delay when an invoice is contested and disputes will be settled as quickly as possible

HBOS plc complies with the Better Payment Practice Code Information regarding this Code and its purpose can be obtained from the Better Payment Practice Group's website at www payontime co uk

The Company's main trading subsidiary undertakings, Halifax plc and Bank of Scotland, had trade creditors outstanding at 31 December 2006 representing 18 days of purchases for each company The Company itself owed no amounts to trade creditors at 31 December 2006

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THE MORTGAGE BUSINESS plc

DIRECTORS' REPORT (continued)

Directors

The Directors of the company during the year to 31 December 2006 were -

P Charge	(Resigned 3 July 2006)
R J Holmes	(Appointed 19 May 2006)
P A Jenks	
D M Murphy	(Appointed 14 November 2006)
D C Nicholson	(Resigned 15 November 2006)
N C Payne	
N Stockton	
K L Wood	(Appointed 10 February 2006)

Directors' beneficial interests in the ordinary shares of HBOS plc during the year were as follows.

References to "HBOS plc shares" are to ordinary shares of 25p each in HBOS plc

During the year, no Director had any beneficial interest in the share capital of the Company or of any other Group undertaking other than in HBOS plc, the ultimate holding company

The beneficial interests of the Directors and their immediate families in HBOS plc shares are set out below -

	At 31.12.05 or date of appointment if later HBOS plc shares	At 31 12 06 HBOS plc shares
R J Holmes	326	645
P A Jenks	14,785	23,168
N C Payne	1,133	658
N Stockton	1,603	3,535
K L Wood	3,389	4,173

Short-term Incentive Plan - HBOS scheme and former Halifax scheme

Certain Directors have conditional entitlements to shares arising from the annual incentive plan Where the annual incentive for any year was taken in shares and these shares are retained in trust for three years, the following shares will also be transferred to the Directors

	Grant effective from	Shares as at 31.12.06
R J Holmes	April 2005	36
N Stockton	March 2004	95
	April 2005	540
	March 2006	803
K L Wood	March 2004	346
	April 2005	487
	March 2006	583

continued

THE MORTGAGE BUSINESS plc

DIRECTORS' REPORT (continued)

Long-term Incentive Plan - HBOS scheme and former Halifax scheme

Details of shares which have been conditionally awarded to Directors under the plans are set out below The conditions relating to the long-term incentive plan may be found in the HBOS plc Annual Report & Accounts 2006

	Grant Effective from	At 31 12.05 or date of appoint-ment if later	Granted (G) or lapsed (L) in year	Dividend reinvest-ment shares	Added as a result of performance (including on dividend reinvestment shares)	Released in year	At 31.12.06
P A Jenks	January 2003	5,468	-	848	5,242	11,558	-
	January 2004	5,020	-	-	-	-	5,020
	March 2006	-	4,778 (G)	-	-	-	4,778
N Stockton	January 2004	4,194	-	-	-	-	4,194
	January 2005	5,555	-	-	-	-	5,555
	March 2006	-	5,120 (G)	-	-	-	5,120

Shares granted under these plans can crystallise at any level between 0% and 200% of the conditional award noted in the above table, dependant upon performance The performance period for the January 2003 grant ended on 31 December 2005 and, in the light of the performance outcome, grants were released at 183% of the conditional award On maturity, dividend reinvestment shares equivalent to approximately 15 5% of the original conditional grant were also released to participants in accordance with the rules of the plan

Long-term Incentive Plan
HBOS scheme, former Bank of Scotland scheme and former Halifax scheme

Share options granted between 1995 and 2000 under the Bank of Scotland Executive Stock Option Scheme 1995 are subject to performance pre-conditions which have now been satisfied Share options granted under other plans are not subject to a performance pre-condition Details of the options outstanding under these plans are set out below

	Options outstanding At 31.12 05 or date of appointment	Granted (G), lapsed (L) or exercised (E) in year	At 31.12 06
R J Holmes	1,156	-	1,156
P A Jenks	8,691	5,660 (E)	3,031
N C Payne	4,525	2,224 (E)	2,301
N Stockton	3,087	18,000 (G)	21,087
K L Wood	1,343	-	1,343

continued

THE MORTGAGE BUSINESS plc

DIRECTORS' REPORT (continued)

Sharesave Plan

Share options granted under these plans are set out below

	At 31 12.05 or date of appointment	Granted (G), lapsed (L) or exercised (E) in year	At 31.12.06
R J Holmes	2,867	443 (G)	
		386 (E)	2,924
N C Payne	1,164	-	1,164
N Stockton	1,585	-	1,585
K L Wood	2,748	-	2,748

Options under these plans were granted using middle market prices shortly before the dates of the grants, discounted by 20%

Full details of the Directors' shareholdings and options are contained in the Register of Directors' Interests which is available for inspection

Mr P Baker was appointed as a director on 15 February 2007

The Articles of Association do not provide for the retirement of Directors by rotation

Audit Information

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

Auditors and General Meeting

KPMG Audit Plc signified their willingness to continue in office and a resolution for their re-appointment was passed at the Annual General Meeting on 15th February 2007

BY ORDER OF THE BOARD

A. Lockwood.

A LOCKWOOD
Secretary

Bridge House
Queens Park Road
Handbridge
Chester
CH4 7AD
15th February 2007

THE MORTGAGE BUSINESS plc

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS

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

Company law requires the directors to prepare company financial statements for each financial year Under that law the directors have elected to prepare the company financial statements in accordance with IFRSs as adopted by the EU

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

In preparing the company financial statements, the directors are required to

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

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

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report and a Business Review

INDEPENDENT AUDITORS' REPORT
TO THE MEMBERS OF THE MORTGAGE BUSINESS PLC

We have audited the financial statements of The Mortgage Business plc for the year ended 31 December 2006 which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement, the 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 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 7

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

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985 We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements

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

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements It also includes an assessment of the significant estimates and 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

continued

INDEPENDENT AUDITORS' REPORT
TO THE MEMBERS OF THE MORTGAGE BUSINESS PLC (continued)

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 2006 and of its profit 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

KPMG Audit Plc
Chartered Accountants
Registered Auditor
MANCHESTER

15 February 2007

THE MORTGAGE BUSINESS plc

INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2006

	Notes	2006 £000	2005 £000
Interest receivable and similar income	2	539,095	558,783
Interest payable and similar charges		(405,481)	(403,236)
Net interest receivable		133,614	155,547
Fee and commission income	3	11,435	9,518
Administrative expenses	4	(8,576)	(7,370)
Impairment losses on loans and advances	10	(20,918)	(11,795)
Profit before tax		115,555	145,900
Income tax expense	5	(34,667)	(43,770)
Profit after tax		80,888	102,130
Attributable to:			
Equity holders		80,888	102,130
Profit for the period		**80,888**	**102,130**

STATEMENT OF RECOGNISED INCOME AND EXPENSE
FOR THE YEAR ENDED 31 DECEMBER 2006

	2006 £000	2005 £000
Change in accounting policy on adoption of IAS 39	-	10,823
Profit for the financial year	80,888	102,130
Total recognised income for the period	**80,888**	**112,953**

The notes on pages 13 to 23 form part of the financial statements

THE MORTGAGE BUSINESS plc

BALANCE SHEET
AS AT 31 DECEMBER 2006

	Notes	2006 £000	2005 £000
Assets			
Deferred tax asset	6	940	1,058
Loans and advances to customers	8	9,309,277	8,466,109
Total non-current assets		9,310,217	8,467,167
Deferred tax asset	6	118	118
Trade and other receivables	7	16	10
Loans and advances to customers	8	313,199	246,768
Total current assets		313,333	246,896
Total assets		**9,623,550**	**8,714,063**
Equity			
Share capital	12	10,000	10,000
Reserves	12	251,207	280,569
Issued capital and reserves attributable to equity holders of the parent		261,207	290,569
Liabilities			
Interest bearing loans and borrowings	14	10,000	10,000
Total non-current liabilities		10,000	10,000
Interest bearing loans and borrowings	14	9,316,461	8,369,131
Trade and other payables	15	35,882	44,363
Total current liabilities		9,352,343	8,413,494
Total liabilities		9,362,343	8,423,494
Total equity and liabilities		**9,623,550**	**8,714,063**

A reconciliation of the movement in equity is provided in note 12

The notes on pages 13 to 23 form part of the financial statements

Approved by the Board of Directors on 15th February **2007 and signed on its behalf by**

N Scott

DIRECTOR

THE MORTGAGE BUSINESS plc

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2006

	Note	2006 £000	2005 £000
Cash flows from operating activities			
Profit before tax		115,555	145,900
Increase in impairment		5,087	13,158
Increase/(decrease) in trade and other payables		740	(41,254)
(Increase)/decrease in debtors and trade and other receivables		(914,692)	684,087
Decrease in inter-company accounts with HBOS Group companies		(634,020)	(681,476)
Income taxes paid		(43,770)	(35,505)
Net cash (outflow)/inflow from operating activities		**(1,471,100)**	**84,910**
Cash flows from financing activities			
Dividends paid		(110,250)	(136,117)
Net cash from financing activities		**(110,250)**	**(136,117)**
Net decrease in cash and cash equivalents		(1,581,350)	(51,207)
Cash and cash equivalents at 1 January		(108,139)	(56,932)
Cash and cash equivalents at 31 December	14	**(1,689,489)**	**(108,139)**

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS

1 SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

The 2006 statutory financial statements set out on pages 10 to 12 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ('IFRS')

The standards adopted by the Company are those endorsed by the European Union and effective at the date the IFRS financial statements are 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

(b) Basis of preparation

The financial statements are presented in Sterling, rounded to the nearest thousand They are prepared on the historical cost basis

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources Actual results may differ from these estimates

The estimates and underlying assumptions are reviewed on an ongoing basis Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods

(c) Adopted IFRS not yet applied

IFRS 7 'Financial instruments Disclosure' and the 'Capital disclosure amendment' to IAS 1 'Presentation of financial statements' which are applicable for periods commencing on or after 1 January 2007 have not been applied The application of these standards in 2006 would not have affected the balance sheet, income statement or cash flow statements as they are only concerned with disclosure

(d) Interest receivable and similar income, fee income and mortgage incentive costs

Revenue on financial instruments, including loans and advances, is recognised on an effective interest rate basis This calculation takes into account interest received or paid, fees and commissions paid or received, expected early redemption penalties and premiums and discounts on acquisition or issue 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 instrument at initial recognition

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

1 SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Interest payable and similar charges

Interest payable and similar charges comprise interest payable on borrowings calculated using the interest receivable on funds invested

(f) Loans and advances

Loans and advances held for trading are carried at fair value Gains, losses and related income are taken to net trading income as they arise

Loans and advances designated at fair value through the income statement are carried at fair value Gains, losses and related income are taken to other operating income as they arise, except for those related to insurance and investment business which are taken to net investment income related to insurance and investment business

All other loans and advances are classified as loans and receivables They are initially recognised at fair value plus directly related transaction costs and are subsequently carried on the balance sheet at amortised cost using the effective interest method less provision for impairment

The Company assesses 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

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 methodology based on existing risk conditions or events that have a strong correlation with a tendency to default

The fair value of loans and advances to customers is estimated by discounting anticipated cash flows, including interest, at a current market rate of interest

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

1 SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Loans and advances (continued)

The fair value of floating rate placements and overnight deposits is equal to carrying value The fair value of fixed interest bearing deposits is based on cash flows discounted using current money market interest rates for debts with similar maturity and credit risk characteristics

(g) Taxation

Income tax on the profit or 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 policyholder returns and tax that is payable on shareholders' equity returns This allocation is based on an assessment of the effective rate of tax that is applicable to shareholders' equity 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 Temporary differences in relation to the initial recognition of assets and liabilities that affects neither accounting nor taxable profit are not provided 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

(h) Dividends

Dividends are recognised as a liability in the period in which they are declared

(i) Trade and other payables

Trade and other payables are stated at cost

2 INTEREST RECEIVABLE AND SIMILAR INCOME

Interest income, all of which arose from activities within the United Kingdom, represents finance charges earned on mortgage loan agreements together with income from associated services This has been recognised in accordance with IAS 39 on an effective yield basis

The interest income and profit before tax are attributable to one continuing activity, the provision of mortgage loans and associated services

The components of interest receivable and similar income are as follows

	2006 £000	2005 £000
Interest on loans	522,755	552,097
IAS 39 impact of interest not recognised on impaired loans	-	(448)
IAS 39 impact of effective yield	16,340	7,134
Interest receivable and similar income	539,095	558,783

3 FEE AND COMMISSION INCOME

The components of fee and commission income are as follows

	2006 £000	2005 £000
Fees and additional charges	10,613	9,021
Insurance commission	822	497
Fee and commission income	11,435	9,518

4 ADMINISTRATIVE EXPENSES

The Company's audit fee of £28,000 (2005 £22,000) will be paid by its immediate parent undertaking

The Company has no employees It uses the services of its immediate parent undertaking for which a management charge, included in administrative expenses, is made

Five directors, Messrs P Charge, R J Holmes, D M Murphy, N C Payne and K L Wood (2005 Five, Messrs M J Bergin, P Charge, W W Dudgeon, D A Parry and N C Payne) were paid an amount by the immediate parent undertaking in respect of their management of the Company totalling £315,530 (2005 £317,434) None of the remaining Directors received remuneration for services as Directors of the Company

5 INCOME TAX EXPENSE

Recognised in the income statement

	2006 £000	2005 £000
Current tax expense	34,549	43,770
Deferred tax expense	118	-
Income tax expense at the standard UK corporation tax rate of 30% (2005 30%)	34,667	43,770

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

6 DEFERRED TAX

Recognised deferred tax assets

Deferred tax assets are attributable to the following	2006 £000	2005 £000
Deferred tax asset brought forward	1,176	5,814
IAS 39 impact on deferred tax asset	-	(4,638)
Release of deferred tax asset	(118)	-
Deferred tax asset carried forward	1,058	1,176

Reconciliation of deferred tax

	2006 £000	2005 £000
Non-current assets		
Deferred tax asset	940	1,058
	940	1,058

	2006 £000	2005 £000
Current assets		
Deferred tax asset	118	118
	118	118

The deferred tax asset brought forward is to be released to the income statement over a period of ten years

7 TRADE AND OTHER RECEIVABLES

	2006 £000	2005 £000
Current assets		
Other debtors	16	10
	16	10

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

8 LOANS AND ADVANCES TO CUSTOMERS

	2006 £000	2005 £000
Non-current assets		
Loans and advances to customers (net of impairment)	9,309,277	8,466,109
	9,309,277	8,466,109

	2006 £000	2005 £000
Current assets		
Loans and advances to customers (net of impairment)	313,199	246,768
	313,199	246,768

9 NON-PERFORMING ASSETS

	2006 £000	2005 £000
Gross non-performing loans and advances	423,683	526,745
Provisions for impairment	(13,486)	(10,200)
Non-performing loans and advances net of impairment	410,197	516,545

10 IMPAIRMENT

	2006 £000
Cumulative provision for impairment as at 1 January	35,425
IAS 39 impact of unwinding of discount	323
New impairment less releases	20,921
Amounts written off	(16,157)
Cumulative provision for impairment as at 31 December	40,512
New impairment less releases	20,921
Recoveries of amounts previously written off	(3)
Net charge to income statement	20,918

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

11 DIVIDENDS

	2006 £000	2005 £000
Amounts recognised as distributions to equity holders in the period		
Interim dividend paid for the year ended 31 December	110,250	136,117

12 RECONCILIATION OF MOVEMENT IN CAPITAL AND RESERVES

	Share Capital £000	Reserves £000	Total £000
Balance at 1 January 2005	10,000	303,733	313,733
Total recognised income and expense	-	112,953	112,953
2005 interim dividend paid in 2005		(136,117)	(136,117)
Balance at 31 December 2005	10,000	280,569	290,569
Balance at 1 January 2006	10,000	280,569	290,569
Total recognised income and expense	-	80,888	80,888
2006 interim dividend paid in 2006	-	(110,250)	(110,250)
Balance at 31 December 2006	10,000	251,207	261,207

	2006 £	2005 £
On issue at 1 January		
Ordinary shares of £1 each	10,000,000	10,000,000
On issue at 31 December – fully paid	10,000,000	10,000,000

13 PARENT UNDERTAKING

HBOS plc is the ultimate parent undertaking of The Mortgage Business plc 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 The Governor and Company of the Bank of Scotland heads the smallest group into which the accounts of the Company are consolidated The accounts of The Governor and Company of the Bank of Scotland may be obtained from its head office at The Mound, Edinburgh, EH1 1YZ

14 INTEREST BEARING LOANS AND BORROWINGS

	2006 £000	2005 £000
Non-current liabilities		
Inter-company accounts with HBOS Group companies	10,000	10,000
	10,000	10,000
Current liabilities		
Inter-company accounts with HBOS Group companies	7,626,972	8,260,992
Bank overdraft at Bank of Scotland	1,689,489	108,139
	9,316,461	8,369,131

The inter-company accounts with HBOS Group companies and the bank overdraft at Bank of Scotland were charged at interest rates of between 4 00% and 6 00% throughout the financial year (2005 4 00% and 5 75%)

15 TRADE AND OTHER PAYABLES

	2006 £000	2005 £000
Tax creditor	34,549	43,770
VAT	3	9
Other creditors	1,330	584
	35,882	44,363

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

16 RELATED PARTY TRANSACTIONS

During the year, in addition to those transactions disclosed separately in the accounts, the Company had the following transactions with related parties

In respect of credit insurance underwritten by companies within the CAPITAL BANK Group, the following related party transactions occurred in the year

	2006 £000	2005 £000
Included within fee and commission income		
Earned commission	822	497

In respect of funding provided by CAPITAL BANK plc, the following related party transactions occurred in the year

	2006 £000	2005 £000
Included within interest payable and similar charges·		
Interest payable to CAPITAL BANK plc	405,481	403,236
Included in creditors at year end		
Closing interest accrual	54	54

In respect of services provided by CAPITAL BANK plc, the following related party transactions occurred in the year

	2006 £000	2005 £000
Included within administrative expenses		
Charges for services provided by CAPITAL BANK plc	8,576	7,370

One director had a mortgage with an outstanding balance of £10,299 at 31 December 2006 The opening balance was £13,578 During the period, interest of £361 was charged and £3,640 was repaid by the director

No amounts have been provided for or written off in the period in respect if this debt

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

17 FINANCIAL INSTRUMENTS

Exposure to credit and interest rate risks arises in the normal course of the Company's business

Credit risk

The Company has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis Credit evaluations are performed on all customers

There are no significant concentrations of credit risk, except in the UK mortgages market

Interest rate risk

In respect of income earning financial assets and interest bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and the periods in which they reprice

Terms and conditions

Mortgage loans are typically at fixed or discounted variable interest rates for an initial period and then revert to the Company's standard variable rate for the remainder of the contractual term, usually around 25 years Early repayment charges apply to certain products, depending upon the length of time the product has been held Mortgage loans are secured against the property

2006	Note	EIR	Less than 1 Year £000	Between 1-2 Years £000	Between 2-5 Years £000	5 years or more £000	**Total £000**
Loans and advances to customers	8	5 6%	313,199	171,792	727,086	8,410,399	**9,622,476**
Interest bearing loans and borrowings	14	4 3%	9,316,461	10,000	-	-	**9,326,461**

2005			Less than 1 Year £000	Between 1-2 Years £000	Between 2-5 Years £000	5 years or more £000	**Total £000**
Loans and advances to customers	8	6 4%	246,768	215,844	995,870	7,254,395	**8,712,877**
Interest bearing loans and borrowings	14	4 8%	8,369,131	10,000	-	-	**8,379,131**

THE MORTGAGE BUSINESS plc

NOTES TO THE FINANCIAL STATEMENTS (continued)

17 FINANCIAL INSTRUMENTS (continued)

Fair values

The fair values together with the carrying amounts shown in the balance sheet are as follows

	Carrying amount 2006 £000	Fair value 2006 £000
Loans and advances to customers	9,622,476	9,613,418
Trade and other receivables	16	16
Trade and other payables	35,882	35,882

Estimation of fair values

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the table

Loans and advances to customers
Fair value is calculated based on discounted expected future principal and interest cash flows

Trade and other receivables/payables
For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value All other receivables/payables are discounted to determine the fair value