Arkle Funding (No.1) Limited

Annual Report and Accounts

Period ended 11 May 2007

Company number 05941595

DIRECTORS' REPORT

The Directors have pleasure in presenting their first report for Arkle Funding (No 1) Ltd for the period from incorporation to 11 May 2007

Principal activities

The principal activity of Arkle Funding (No 1) Ltd (the "Company") is to acquire an interest in a portfolio of mortgage loans and to enter into financial arrangements with its related parties No future changes in activity are envisaged

The Company was registered as Arkle Funding (No 1) Ltd in England and Wales on 20 September 2006 as a limited company The authorised share capital is £100 comprising of 100 ordinary shares of £1 each, 1 of which has been issued

Results and dividends

Distribution of revenue by the Company is pre-determined under the securitisation transaction documents Under the terms of the securitisation, the Company retains the right to 0 01% of 'issuer available revenue receipts' (as defined within the securitisation transaction documents)

The profit on ordinary activities before tax for the period from incorporation to 11 May 2007 was £14,000 No dividends were paid during the year

Business review and future developments

The company commenced trading on 6th November 2006 when it received £7,015 million as an intercompany loan from Arkle Master Issuer plc following the sale of Notes The loan proceeds were used to purchase an interest in the assets of Arkle Finance Trustee Ltd (the "Trust") The assets of the Trust comprise mortgage loans originated by Cheltenham & Gloucester plc ("C&G plc") and secured on residential properties in England, Wales and Scotland

On the 14th December 2006, the Company received a further intercompany loan following a further issue of Notes by Arkle Master Issuer plc to the value of £3,179 million

The company will continue to receive the proceeds as intercompany loans from Arkle Master Issuer plc following future issuances The Directors anticipate that the company will be profitable over its lifetime

Risks and Uncertainties

The company is exposed to the beneficial interest in a portfolio of mortgage assets The structure of the company is designed to minimise risk and uncertainties at an entity level This is achieved through the fixed to floating and basis rate swaps with C&G plc, certain credit enhancement agreements and on-going linked obligations to Arkle Master Issuer plc

Key Performance Indicators (KPIs)

Given the straightforward nature of the business, the Company's directors are of the opinion that analysis using KPIs is not necessary for an understanding of the development, performance or position of the Company

However, the performance of the Company is monitored by comparing the actual repayments on the intercompany loan to those necessary to repay the issued loan notes, as forecast in the Company's Offering Circular To date, all loan and note repayments have been made in accordance with the forecast

Directors and Directors' interests

The Directors of the Company at the end of the period were as follows

Oliver FJ Pritchard
Vincent M Rapley
Mark Escott

None of the directors had a beneficial interest in the shares of the Company, or of the ultimate holding company, Stanhope Gate Trustees Limited

Daniel J Birtwistle resigned from the Board on the 17 January 2007

During the period, Mark Escott was an employee of Lloyds TSB Bank plc which is a related party of Cheltenham & Gloucester plc

Policy and practice on payment of creditors

The Company follows "The Better Payment Practice Code", published by the Department of Trade and Industry, regarding payments to suppliers A copy of the code and information about it may be obtained from the Department of Trade and Industry, No 1 Victoria Street, London, SW1H 0ET

The Company's policy is to agree terms of payment with suppliers and these normally provide for settlement within 30 days after the date of the invoice, except where other arrangements have been negotiated It is the policy of the Company to abide by the agreed terms of payment, provided the supplier performs according to the terms of the contract

The number of days required to be shown in this report, to comply with the provisions of the Companies Act 1985, is 31

Auditors

PricewaterhouseCoopers LLP were appointed during the period and have indicated their willingness to continue in office

Employees

The Company does not have any employees

Statement of Directors' Responsibilities

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company

The Directors confirm that suitable accounting policies have been used and applied consistently in the year They also confirm that reasonable and prudent judgements and estimates have been made in preparing the financial statements for the period from incorporation to 11 May 2007 and that applicable accounting standards have been followed

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 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

So far as the directors are aware, there is no relevant audit information of which the Company's auditors are unaware, and the directors have taken all the steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information

Post Balance Sheet Events

On 31 May 2007, the Company received further proceeds in the form of an intercompany loan to the value of £3,024 million from Arkle Master Issuer plc following the sale of Notes, which were used to purchase an interest in the assets of the Trust administered by Arkle Finance Trustee Limited The assets of the Trust comprise mortgage loans originated by Cheltenham & Gloucester plc and secured on residential properties in England, Wales and Scotland

Statement of Going Concern

The Directors are satisfied that the Company has adequate resources to continue to operate for the foreseeable future and is financially sound For this reason, they continue to adopt the going concern basis in preparing the financial statements

By order of the board

Oliver FJ Pritchard
Director
4 March 2008

Registered Office
8th Floor
68 King William Street
London EC4N 7DZ

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF ARKLE FUNDING (NO 1) LIMITED

We have audited the financial statements of Arkle Funding (No 1) Limited for the period ended 11 May 2007, which comprise the Income Statement, the Balance Sheet, the Cash Flow Statement, the Statement of Changes in Equity and the related notes These financial statements have been prepared under the accounting policies set out therein

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 European Union are set out in the Statement of Directors' Responsibilities

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland) This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing

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

Opinion
In our opinion

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the company's affairs as at 11 May 2007 and of its profit and cash flows for the period then ended,

- the financial statements have been properly prepared in accordance with the Companies Act 1985, and

- the information given in the Directors' Report is consistent with the financial statements

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Bristol

10 March 2008

INCOME STATEMENT
FOR THE PERIOD ENDED 11 MAY 2007

	Note	Period from incorporation to 11 May 2007
		£'000
Interest receivable and similar income	3	289,369
Interest payable and similar charges	4	(288,820)
Net interest income		549
Operating expenses	5	(535)
Profit before tax		14
Taxation	6	(4)
Profit for the period attributable to equity shareholders		10

The accompanying notes are an integral part of the Financial Statements
All amounts are on a continuing basis

BALANCE SHEET
AT 11 MAY 2007

	Note	11 May 2007
		£'000
Assets		
Deemed loan to group undertaking	7	10,193,966
Trade and other receivables	8	34,250
Deferred tax		-
Cash and cash equivalents		287,821
Other Debtors		-
Total assets		10,516,037

The accompanying notes are an integral part of the Financial Statements

BALANCE SHEET
AT 11 MAY 2007

	Note	11 May 2007
		£'000
Equity and liabilities		
Loan from related companies	9	10,367,993
Trade and other payables	10	148,030
Current Tax Liability		4
Total liabilities		10,516,027
Called up share capital	11	-
Retained profits	12	10
Shareholders' equity		10
Total equity and liabilities		10,516,037

The Directors approved the accounts on 4 March 2008

Vincent Rapley
Director

The accompanying notes are an integral part of the Financial Statements

STATEMENT OF CHANGES IN EQUITY
FOR THE PERIOD ENDED 11 MAY 2007

	Note	Share capital and premium	Retained profits	Total
		£'000	£'000	£'000
Company				
Balance sheet at incorporation 20 September 2006		0	0	0
Share Capital issued in the period		-	-	-
Profit for the period	12	-	10	10
Balance at 11 May 2007		0	10	10

CASH FLOW STATEMENT
FOR THE PERIOD ENDED 11 MAY 2007

	Note	Period from incorporation to 11 May 2007 £'000
Cash generated from operations		
Profit before tax		14
Changes in operating assets		
Deemed loan due from group undertaking	7	(10,193,966)
Changes in other assets	8	(34,250)
		(10,228,216)
Changes in operating liabilities		
Loans due to group undertaking	9	10,367,993
Changes in other liabilities	10	148,030
		10,516,023
Net cash provided by (used in) operating activities		**287,821**
Cash flows from financing activities		
Issue of share capital		-
Net cash generated by financing activities		-
Change in cash and cash equivalents		287,821
Cash and cash equivalents at incorporation		0
Cash and cash equivalents at end of period		**287,821**

NOTES TO THE ACCOUNTS

1 ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below

These financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRS')

The financial information has been prepared under the historical cost convention, as modified by the revaluation of the financial assets and financial liabilities as appropriate under IFRS

Revenue recognition

Interest income and expense are recognised in the income statement for all interest–bearing financial instruments, including loans and advances, using the effective interest method The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability When calculating the effective interest rate, the future cash flows are estimated after considering all the contractual terms of the instrument but not future credit losses The calculation includes all amounts paid or received by the Group that are an integral part of the overall return, direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument and all other premiums or discounts

Taxation

Current tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements Deferred tax is determined using tax rates that have been enacted or announced by the balance sheet date that are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled

Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised Deferred tax is provided on temporary differences arising from investments in subsidiaries and associates and it is probable that the difference will not reverse in the foreseeable future Income tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which those profits arise The tax effects of losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised

Deferred and current tax assets and liabilities are offset when they arise in the same tax reporting group and where there is both a legal right of offset and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and on demand deposits

Recognition of Financial Assets and Liabilities

Under IFRS, if a transferor retains substantially all the risks and rewards associated with the transferred assets, the transaction is accounted for as a financing transaction, notwithstanding that it is a sale transaction from a legal perspective The Directors of the Company have concluded that C&G plc has retained substantially all the risks and rewards of the pool of mortgage loans and as a consequence, the Company does not recognise the mortgage loans on its balance sheet but rather a deemed loan due from C&G plc

The initial amount of the loan due from C&G plc corresponds to the consideration paid by the Company to obtain the mortgage loans less the subordinated loan granted by the Originator The Company recognises principal and interest cashflows from the underlying pool of mortgage loans only to the extent that it is entitled to retain such cashflows Cashflows attributable to C&G plc are not recognised by the Company

The fixed-to-floating interest rate swaps and basis swaps entered into by the Company and C&G plc are not recognised separately as financial derivative instruments, as the amounts payable under the swaps reflect interest flows from the mortgage loans which are not recognised by the Company for accounting purpose Instead, the deemed loan to C&G plc is recognised with an effective interest rate which reflects the amount received under the swap receiving leg

All underlying cashflows are UK based

Impairment of financial assets

At each balance sheet date the Company assesses whether, as a result of one or more events occurring after initial recognition, there is objective evidence that a financial asset or group of financial assets has become impaired Evidence of impairment may include indications that the counterparty is experiencing significant financial difficulty, default or delinquency in interest or principal payments

Dividends

Dividends on ordinary shares are recognised in equity in the period in which they are paid

2 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Company makes assumptions and estimates that affect the reported amounts of assets and liabilities Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances The accounting policies deemed critical to the Company's results and financial position, based upon materiality and significant judgments and estimates, are discussed below

Effective interest method – expected life assumptions

Fees, costs and interest are accounted for on a level yield basis over the expected life of the loan, to either maturity or a market-based re-pricing event Management makes assumptions regarding the expected life of the loan, taking into account expectations of future behaviour

3 INTEREST RECEIVABLE AND SIMILAR INCOME

	Period from incorporation to 11 May 2007
	£'000
Interest receivable on Deemed loan	283,991
Bank interest receivable	5,378
	289,369

4. INTEREST PAYABLE AND SIMILAR CHARGES

	Period from incorporation to 11 May 2007
	£'000
Interest payable on Deemed loan	279,978
Interest payable on start up loan	5,895
Amortisation of issue costs	2,947
	288,820

5 OPERATING EXPENSES

	Period from incorporation to 11 May 2007
	£'000
Audit Fees	29
Administration charges	506
	535

The company has no employees The Directors' emoluments are paid in the form of a management charge A management fee for administration services is charged by Cheltenham & Gloucester plc

6. TAXATION

Analysis of charge in period

	Period from incorporation to 11 May 2007 £'000
UK corporation tax	
Current tax on profits for the period	4
Current year deferred tax	-
	4

The charge for tax on the profit for the period from incorporation to 11 May 2007 is based on a UK corporation tax rate of 30 per cent

Factors affecting tax charge for the period

	Period from incorporation to 11 May 2007 £'000
Tax charge at UK corporation tax rate of 30%	4
Deferred tax timing differences	-
Total tax charge	4

7 DEEMED LOAN DUE FROM GROUP UNDERTAKING

	As at 11 May 2007 £'000
Deemed loan due from C&G	10,193,966
All unsubordinated	

The terms of this loan are aligned to the bonds issued by Arkle Master Issuer plc

During the period, a beneficial interest of £10,193,966,000 in mortgage assets originated by C&G plc was acquired in accordance with the accounting policy set out in Note 1 This has been accounted for as a deemed loan

8 TRADE AND OTHER RECEIVABLES

	As at 11 May 2007 £'000
Due from C&G plc	33,800
Due from related party	450
All unsubordinated	34,250

9. LOAN FROM RELATED COMPANIES

	As at 11 May 2007 £'000
Loan due to Arkle Master Issuer plc	10,187,913
Loan due to C&G plc	180,080
	10,367,993

The terms of the loan due to Arkle Master Issuer plc are aligned to the bonds issued by Arkle Master Issuer plc

10 TRADE AND OTHER PAYABLES

	As at 11 May 2007 £'000
Interest payable on loan from group undertaking	147,676
Other amounts owed to group undertakings	308
Other payables	46
	148,030

11 CALLED UP SHARE CAPITAL

	2007 £
Authorised ordinary shares of £1 each	100
Issued and fully paid ordinary shares of £1 each	1

The Company was registered as Arkle Funding (No 1) Limited in England and Wales on 20 September 2006 as a limited company, with authorised share capital of £100 comprising 100 ordinary shares of £1 each One share was issued and fully paid up

12 RETAINED PROFITS

	2007 £'000
Profit for the period from incorporation	10
At 11 May 2007	10

13. RELATED PARTY TRANSACTIONS

A number of transactions are entered into with related parties as part of the Company's normal business

The related parties are Arkle Master Issuer plc, Cheltenham & Gloucester plc and Lloyds TSB Bank plc by virtue of their various roles and inputs into securitisation arrangements to which Arkle Funding (No 1) Ltd is a party

These transactions include a loan from Arkle Master Issuer, a loan from Cheltenham & Gloucester plc, a banking relationship with Lloyds TSB Bank plc, a cash management fee of £978,000 payable to Cheltenham & Gloucester plc and Arkle Master Issuer plc and management expenses borne by the company in respect of Arkle Master Issuer plc and other associated companies

14 FUTURE DEVELOPMENTS

The following pronouncements will be relevant to the Company but were not effective at 11 May 2007 and have not been applied in preparing these financial statements

Pronouncement	Nature of Change	Effective Date
IFRS 7 Financial Instruments Disclosures	Consolidates the current financial instruments disclosures into a single standard and requires more detailed qualitative and quantitative disclosures about exposure to risks arising from financial instruments	Annual periods beginning on or after 1 January 2007
Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures	Introduces additional disclosures of the objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital, and compliance with capital requirements	Annual periods beginning on or after 1 January 2007

15 PARENT COMPANIES

The immediate parent company is Arkle Holdings Limited for which Stanhope Gate Trustees Limited holds the shares in trust for the benefit of certain discretionary objects (which do not include Lloyds TSB Bank or any entity connected with Lloyds TSB Bank) For accounting purposes, the Company's ultimate parent and controlling party is Lloyds TSB Group plc The Company's results are included within the consolidated financial statements of Lloyds TSB Group plc Copies of the group accounts may be obtained from the Company Secretary's Office, Lloyds TSB Group plc, 25 Gresham Street, London EC2V 7HN

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Registered in England No 05941595