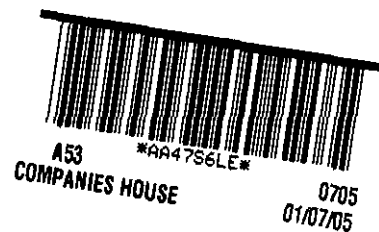


Company No. 3149607

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS' REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2004



BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS' REPORT AND FINANCIAL STATEMENTS

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BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS AND COMPANY INFORMATION

DIRECTORS

J.H. Lloyd
I.G. Stewart

SECRETARY

S. Mayer

REGISTERED OFFICE

Premier House
City Road
CHESTER
CH88 3AN

AUDITORS

KPMG Audit Plc
1 The Embankment
Neville Street
LEEDS
LS1 4DW

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC DIRECTORS' REPORT

The directors present their report and the audited financial statements for the year ended 31 December 2004.

PRINCIPAL ACTIVITY AND BUSINESS REVIEW

The principal activity of the Company is to finance mortgage lending. In 1997 the Company issued £105.6m floating rate loan notes. The interest payable on the loan notes is set at 60% of the three-month LIBOR rate for sterling deposits less 0.30% per annum. The loan notes are secured on the mortgage portfolio. The capital appreciation arising on the sale of a mortgage holder's property is shared between the mortgage holder and the Company as set out in the original loan agreement. The Company pays its entire share of the appreciation to bondholders and the swap provider. No changes in the business of the Company are anticipated. Movements in the mortgage book are disclosed in the notes to the financial statements.

RESULTS FOR THE YEAR TO 31 DECEMBER 2004

No new mortgages were acquired or generated by the Company in the period and no new loan notes were issued.

The profit after taxation for the year amounted to £307,863 (2003: £322,269). An interim dividend of £130,225 was paid (2003: £139,864). The directors recommend a final dividend payment of £162,539 (2003: £150,177).

SUPPLIER PAYMENT POLICY

It is the Company's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the Company and its suppliers. The Company did not, at any time during the year, obtain or seek to obtain credit from any of its suppliers. On this basis no calculation has been made for the average number of days credit taken at the year end.

FINANCIAL INSTRUMENTS

The Company's financial instruments, other than derivatives, comprise mortgage loans, funds on deposit and loan notes. The main purpose of these financial instruments is to raise finance for the Company's operations.

Interest rate risk exists where assets and liabilities have interest rates set under a different basis or which reset at a different time. The Company has entered into an interest rate derivative with an external swap provider to manage the interest rate risk on its operations and sources of finance. The purpose of the interest rate swap is to reduce the interest rate risk on the Company's non-trading assets and liabilities by paying over a portion of capital appreciation on the mortgage loans in return for a fixed interest receipt. The swap is accounted for on an accruals basis.

It is, and has been throughout the year under review, the Company's policy that no trading in financial instruments is undertaken.

DIRECTORS AND THEIR INTERESTS

The directors who served during the year were as follows:

I.G. Stewart
J.H. Lloyd

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.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS' REPORT (continued)

DIRECTORS AND THEIR INTERESTS (CONTINUED)

The beneficial interests of the directors and their immediate families in HBOS plc shares are set out below. References to "HBOS plc shares" are to ordinary shares of 25p each in HBOS plc.

	At 31.12.03 HBOS plc shares	At 31.12.04 HBOS plc shares
J. H. Lloyd	10,921	10,934
I.G. Stewart	8,146	13,390

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 31.12.04
J.H. Lloyd	March 2003	1,264

LONG-TERM INCENTIVE PLAN - HBOS SCHEME AND FORMER HALIFAX SCHEME

Details of the 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 2004.

	Grant effective from	At 31.12.03	Granted (G) or lapsed (L) in year	Added as a result of performance	Dividend reinvestment shares	Released in year	At 31.12.04
I.G. Stewart	January 2001	3,931	-	4,444	513	8,888	-

Shares granted under these plans can crystallise at any level between 0% and 200% of the conditional award noted in the above table, dependent upon performance. The performance period for the January 2001 grant ended on 31 December 2003 and, in the light of performance outcome, grants were released at 200% of the conditional award. On maturity, dividend reinvestment shares equivalent to approximately 26% of the original conditional grant were also released to participants in accordance with the rules of the plan.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS' REPORT (continued)

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 precondition. Details of the options outstanding under these plans are set out below.

	Options Outstanding at 31.12.03		Granted (G), lapsed (L) or exercised (E) in year	At 31.12.04
I.G. Stewart	6,024	(G)	3,019	9,043
J.H. Lloyd	19,645	(G)	1,964	21,609

SHARESAVE PLAN

Share options granted under these plans are set out below

	At 31.12.03		Granted (G), Lapsed (L) or exercised (E) in year	At 31.12.04
J.H. Lloyd	4,255	(G)	208	
		(E)	1,382	3,081

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

ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs")

The directors intend to prepare the financial statements for the year ending 31 December 2005 in accordance with IFRSs. The main effects of IFRSs for the Company are that dividends accrued at 31 December 2004 will not be reflected until they are paid in 2005; the mortgage portfolio and loan notes will be presented on an amortised cost basis; and the Company's share of the capital appreciation arising on the mortgage portfolio and payable to the bond holders will be reflected as an embedded derivative asset and liability.

RATIFICATION OF PREVIOUS UNAPPROVED DIVIDEND PAYMENTS

Dividend payments of the Company were made between 1 March 1998 and 31 December 2004 without the payments having been formally approved by the directors and/or shareholders of the Company.

The directors believe that neither the Company's shareholders nor its creditors were prejudiced, given that at the time the payments were made the Company had sufficient distributable reserves to make such payments.

The company has therefore obtained from the Company's shareholders, retrospective ratification of all previous unapproved dividend payments.

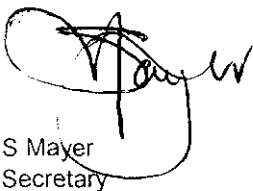
BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS' REPORT (continued)

AUDITORS AND ANNUAL GENERAL MEETING

The Members had previously resolved to re-appoint KPMG Audit Plc as auditors of the Company on 29 July 2003. However since this date KPMG Audit Plc has not been re-appointed as auditor as required under the Companies Act 1985. The Members of the Company have therefore agreed to retrospectively ratify KPMG Audit Plc's re-appointment for the year ended 31 December 2004 at their Annual General Meeting on 22 February 2005.

KPMG Audit Plc were re-appointed as auditors of the Company on 22 February 2005 for the forthcoming financial period. KPMG Audit Plc have signified their willingness to continue in office and a resolution for their re-appointment was passed at the Annual General Meeting on 22 February 2005.

By Order of the Board



S Mayer
Secretary

Premier House
City Road
CHESTER
CH88 3AN

22 February 2005

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
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 for that period. In preparing those 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 applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- 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 have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF
BOS (SHARED APPRECIATION MORTGAGES) NO.2 PLC**

We have audited the financial statements on pages 9 to 14.

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 audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors are responsible for preparing the directors' report and, as described on page 7, the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if 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 transactions with the Company is not disclosed.

BASIS OF AUDIT 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 2004 and of the profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc

KPMG Audit Plc
Registered Auditor
1 The Embankment
Neville Street
LEEDS
LS1 4DW

22 February 2005

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 2004

	Note	2004	2003
		£	£
Interest receivable	2	2,619,185	2,290,074
Interest payable		(2,037,845)	(1,681,727)
Net interest income		581,340	608,347
Fees and commissions receivable		3,510	3,425
Shared appreciation receivable		4,748,513	3,277,747
Shared appreciation payable		(4,748,513)	(3,277,747)
Other income		18	3,050
Operating expenses		(145,064)	(154,438)
Profit on ordinary activities before taxation	3	439,804	460,384
Tax on profit on ordinary activities	4	(131,941)	(138,115)
Profit on ordinary activities after taxation		307,863	322,269
Dividend on equity shares - paid		(130,225)	(139,864)
Dividend on equity shares - proposed		(162,539)	(150,177)
Retained profit for the year		15,099	32,228
Retained profit at the start of the year		779,742	747,514
Retained profit at the end of the year		794,841	779,742

All gains and losses arising during the year and the comparative period have been recognised in the profit and loss account and derive from continuing operations.

The notes on pages 11 to 14 form part of the financial statements.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
BALANCE SHEET AS AT 31 DECEMBER 2004

	Note	2004	2003
		£	£
Fixed assets investments			
Mortgage portfolio	5	32,413,391	34,044,969
Deposit account	6	48,793,551	51,096,786
		<u>81,206,942</u>	<u>85,141,755</u>
Current assets			
Amount due from group undertakings		923,391	825,478
Deferred expenditure		130,650	205,770
Interest receivable		246,138	219,175
Cash at bank and in hand		616,151	276,101
		<u>1,916,330</u>	<u>1,526,524</u>
Creditors: amounts falling due within one year			
Corporation tax payable		(131,941)	(138,115)
Accruals and deferred income		(737,035)	(455,591)
Proposed dividend		(162,539)	(150,177)
		<u>(1,031,515)</u>	<u>(743,883)</u>
Net current assets		<u>884,815</u>	<u>782,641</u>
Total assets less current liabilities		<u>82,091,757</u>	<u>85,924,396</u>
Creditors: amounts falling due after more than one year			
Floating rate loan notes	7	(81,246,915)	(85,094,653)
Net assets		<u>844,842</u>	<u>829,743</u>
Capital and reserves			
Called up share capital	8	50,001	50,001
Profit and loss account		794,841	779,742
Shareholders' funds (including non-equity share)	9	<u>844,842</u>	<u>829,743</u>

The notes on pages 11 to 14 form part of the financial statements.

The financial statements were approved by the Board of directors on 22 February 2005

and were signed on its behalf by:  Director
 Ian Gordon Stewart

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS

1. ACCOUNTING POLICIES

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's financial statements.

BASIS OF PREPARATION

The financial statements have been prepared in accordance with applicable accounting standards and have been drawn up under the historical cost convention and on a going concern basis.

INTEREST RECEIVABLE AND PAYABLE

Interest receivable comprises interest arising on cash deposits held in the Guaranteed Investment Contract (GIC) account. No interest is receivable from the customers during the life of the mortgages. Interest payable comprises amounts payable to bondholders at a fixed margin below the three-month LIBOR rate for sterling deposits. All interest receivable and payable is accrued on a daily basis.

SHARED APPRECIATION

The capital appreciation arising on the sale of a mortgage holder's property is shared between the mortgage holder and the Company as set out in the original loan agreement. The Company pays its share of the appreciation to the bondholders and a third party swap provider as part of a swap agreement.

TAXATION

The charge for taxation takes into account all timing differences in the accounting and taxation treatment of certain items.

DEFERRED TAX

Deferred tax is recognised at the standard rate of corporation tax, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date (except as otherwise required by FRS 19), based on the corporation tax rate expected when the timing differences reverse.

VAT

Value added tax is not recoverable by the Company and is included with its related costs.

FEES AND COMMISSIONS

Arrangement fees and commissions receivable for the continuing service of loans and advances are recognised on the basis of work done. Other fees are recognised when receivable.

DEFERRED EXPENDITURE

Issue costs, in respect of the floating rate loan notes, have been deferred and are being charged to the profit and loss account over a ten year period, being the estimated life of the mortgages.

FINANCIAL INSTRUMENTS

The Company's financial instruments comprise mortgage loans, funds on deposit, loan notes and an interest rate swap. It is, and has been throughout the year under review, the Company's policy that no trading in financial instruments is undertaken. The purpose of the interest rate swap is to reduce the interest rate risk on the Company's non-trading assets and liabilities by paying over a portion of the capital appreciation on the mortgage loans in return for a fixed interest receipt. The swap is accounted for on an accruals basis.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS (continued)

1. ACCOUNTING POLICIES (CONTINUED)

CASH FLOW STATEMENT

The Company is exempt from preparing a Cash Flow Statement under paragraph 5 (a) of FRS 1 (revised 1996), "Cash flow statements" as it is a wholly-owned subsidiary and its results are consolidated within the financial statements of HBOS plc.

2. INTEREST RECEIVABLE

Interest receivable includes amounts receivable from group undertakings of £38,283 (2003: £23,167).

3. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

The profit on ordinary activities before taxation is stated after charging:

	2004 £	2003 £
Auditor's remuneration for audit services	<u>2,000</u>	<u>2,291</u>

The Company has no employees and none of the Directors receive any emoluments from the Company.

4. TAX ON PROFIT ON ORDINARY ACTIVITIES

	2004 £	2003 £
The charge for the year based on a corporation tax rate of 30% (2003: 30%) comprises:		
UK Corporation tax	<u>131,941</u>	<u>138,115</u>

The actual tax charge for the years ended 31 December 2004 and 2003 is equal to the standard rate of corporation tax in the UK (30%).

5. MORTGAGE PORTFOLIO

	2004 £	2003 £
At 1 January	34,044,969	35,373,650
Fees capitalised	4,265	2,745
Mortgage redemptions in year	<u>(1,635,843)</u>	<u>(1,331,426)</u>
At 31 December	<u>32,413,391</u>	<u>34,044,969</u>

The mortgage loans advanced by the Company have no fixed maturity date but would terminate on the earlier of, the sale of the property, or the death of the mortgage account holder.

The fair value of the mortgage loans at 31 December 2004 amounted to £178m (2003: £153m). This includes the value of house price inflation that would be receivable from borrowers if the loans were terminated at the period end. This appreciation in property values would be payable to bondholders and the swap provider.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS (continued)

6. DEPOSIT ACCOUNT

This account represents a cash balance held with a third party under a guaranteed investment contract. The Company earns a LIBOR related return on the account, which is recorded as interest income in the profit and loss account. Withdrawals from this deposit account are restricted to certain circumstances, primarily in relation to the redemption of the loan notes.

7. FLOATING RATE LOAN NOTES

	2004 £	2003 £
At 1 January	85,094,653	88,700,737
Loan note redemptions	<u>(3,847,738)</u>	<u>(3,606,084)</u>
At 31 December	<u>81,246,915</u>	<u>85,094,653</u>

The asset backed floating rate loan notes are due in 2072. The interest rate applicable on the loan notes up to and including the interest period ending in the quarter to 31 August 2027 is 60 per cent of LIBOR for three-month sterling deposits less 0.30% per annum. Thereafter, the interest rate applicable to the loan notes will be 60 per cent of LIBOR for three-month sterling deposits plus 0.10% per annum. The loan notes carry, in addition to interest, rights to receive certain amounts calculated by reference to the value of shared appreciation proceeds received from redeemed mortgages. The loan notes are subject to mandatory part redemption from time to time based on the level of redeemed mortgages and can be redeemed in full, in certain circumstances, at the option of the Company. The loan notes are secured on the mortgage portfolio, the guaranteed investment contract and certain other assets of the Company.

The fair value of the loan notes at 31 December 2004 amounted to £178m (2003: £153m). This includes the value of house price inflation that would be payable to bondholders and the swap provider on redemption of the mortgage loans.

8. SHARE CAPITAL

	2004 £	2003 £
Authorised		
50,000 ordinary shares of £1 each	<u>50,000</u>	<u>50,000</u>
1 deferred share of £1	<u>1</u>	<u>1</u>
Allotted, called up and fully paid		
50,000 ordinary shares of £1 each	<u>50,000</u>	<u>50,000</u>
1 deferred share of £1	<u>1</u>	<u>1</u>

The deferred share carries no entitlement to any dividend or to any share in any surplus assets of the Company on a winding-up, other than the right to be repaid the amount of any paid up share capital thereon. The right to be repaid any paid up share capital in the deferred share shall be deferred until after all paid up share capital has been first repaid on all other classes of issued share capital in the Company.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS (continued)

8. SHARE CAPITAL (CONTINUED)

The deferred share carries the right to receive notice of all general meetings of the Company but does not carry the right to attend, speak or vote at a general meeting unless a resolution is to be proposed abrogating, varying or modifying any of the rights or privileges of the holder of the deferred share, or for the winding up or administration of the Company under the Insolvency Act 1986, or for the entry by the Company with any other party into a merger, reconstruction, scheme of arrangement or amalgamation of or affecting the Company, in any of which cases such holder shall have the right to attend such general meeting and shall be entitled to speak and vote. Whenever the holder of the deferred share is entitled to vote at a general meeting, such holder shall have one vote and on a poll such number of votes as is equal to 34 per cent of the number of votes attached to all other issued shares of the Company.

9. RECONCILIATION OF SHAREHOLDERS' FUNDS

	2004 £	2003 £
Opening shareholders' funds	829,743	797,515
Profit attributable to shareholders	15,099	32,228
Closing shareholders' funds	<u>844,842</u>	<u>829,743</u>

Included in shareholders' funds is £1 of non-equity interests.

10. FINANCIAL AND DERIVATIVE INSTRUMENTS

The Company's financial instruments comprise mortgages, funds on deposit, loan notes and an interest rate swap.

The fair value of the mortgages and the loan notes are disclosed in the relevant note on these financial instruments. The carrying value of the funds on deposit approximates to fair value.

The interest rate swap which matures on 28 February 2040, was entered into on 28 February 1999 with a UK Financial Institution. As at 31 December 2004 the replacement cost of the contract is £nil and its fair value is a liability of £14,606,045 (2003: £13,873,010). There are no significant amounts recognised in these financial statements in relation to this swap.

11. RELATED PARTY TRANSACTIONS

The Company has taken advantage of the exemption covered by paragraph 3 (c) of FRS 8, "Related party disclosures", not to disclose transactions with entities that are part of the HBOS plc Group.

12. PARENT UNDERTAKINGS

HBOS plc is the ultimate parent undertaking of BOS (Shared Appreciation Mortgages) NO. 2 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.