

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
DIRECTORS' REPORT AND FINANCIAL STATEMENTS
YEAR ENDED 31 DECEMBER 2009

DIRECTORS AND COMPANY INFORMATION

DIRECTORS

I G Stewart
T A Hill

SECRETARY

A Lockwood

REGISTERED OFFICE

Premier House
City Road
CHESTER
CH88 3AN

AUDITORS

PricewaterhouseCoopers LLP
Benson House
33 Wellington Street
Leeds
LS1 4JP

THURSDAY



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COMPANIES HOUSE

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 2009

BOS (Shared Appreciation Mortgages) NO 2 PLC is a company domiciled in the United Kingdom

PRINCIPAL ACTIVITY

The principal activity of BOS (Shared Appreciation Mortgages) NO 2 PLC (the "Company") is to finance mortgage lending. In 1997 the Company issued £105.6m floating rate notes (the "Notes"). The interest payable on the Notes is set at 60% of the three-month LIBOR rate for Sterling deposits less 0.30% per annum until August 2027. Thereafter, the interest rate applicable to the Notes will be 60% of the three-month LIBOR rate for Sterling deposits plus 0.10% per annum until 2072 when the Notes become due. The 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 Note holders and the swap provider.

The activities of the Company are conducted primarily by reference to a series of transaction documents (the "Programme Documentation")

Movements in the mortgage book are disclosed in the notes to the financial statements

Business structure

The Company is a subsidiary undertaking of Bank of Scotland plc ("BOS") and HBOS plc. HBOS plc was acquired by Lloyds Banking Group plc ("LBG"), previously known as Lloyds TSB Group plc, on 16 January 2009.

RESULTS AND DIVIDENDS

No new mortgages were acquired or generated by the Company in the year and no new Notes were issued.

The profit after taxation for the year amounted to £1,369,181 (2008: £392,583 profit). A dividend of £171,000 was paid in the year (2008: £234,000).

BUSINESS REVIEW AND FUTURE DEVELOPMENTS

The Company's business will continue to unwind over the life of the mortgages issued as no further advances will be made. Cash is continuing to be collected.

The principal asset in the Company is a mortgage portfolio which is subject to an annual impairment review. The mortgage portfolio is subject to the economic factors relating to the housing market (see "Credit Risk" below). In 2008 and 2009 the UK experienced a significant reduction in activity in the housing market, together with a growth in mortgage arrears, as the effects of the recession became more widespread. However, this trend has not affected the Company's results as the mortgage loans bear a zero rate of interest. No impairment provision was deemed necessary as at 31 December 2009 or 31 December 2008.

UK interest rates have remained both relatively stable and at historically low levels in 2009, which has impacted on the Company's results due to correspondingly low LIBOR rates. The underlying profits are determined by a margin earned between the interest received on the bank accounts including the Guaranteed Investment Contract account (the "GIC"), income on the swap and the interest paid to the Note holders. This is fixed by the Programme Documentation. The sensitivity of the Company's results to changes in interest rates is assessed in note 16.

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

BUSINESS REVIEW AND FUTURE DEVELOPMENTS (CONT'D)

During January 2009, the balance in the GIC account was transferred back to the Company, in accordance with the terms of the Programme Documentation, as a result of the downgrade in the external GIC provider's credit rating and this balance was placed on a temporary fixed rate deposit with BOS

Following the transfer of this balance, the directors of the Company sought approval from the Trustees and the Note holders to change the terms of the legal documents to allow the GIC balance to be held by a financial institution with a rating of at least A rather than the original requirement for a rating of at least A1 (Standard and Poor's)

As at 31 December 2009, the Trustees had approved the change in the credit rating required for the GIC provider and the directors were waiting for further approval from the Note holders

The Company has seen a significant increase in net interest income due to a reduction in interest payable on the Notes caused by the lower levels for LIBOR

Under International Financial Reporting Standards ("IFRSs") an effective yield adjustment is made on interest receivable and interest payable. The expected life of the mortgages and Notes was extended in 2008 to reflect actual payment experience. The net difference passed through the income statement for the year ended 31 December 2009 was £82,548 profit (31 December 2008 £82,549 profit)

The key performance indicator used by management in assessing the performance of the Company is the monitoring of actual cash flows against planned cash flows on the Notes. The Company's performance is addressed in the quarterly management accounts provided to the directors

POLICY AND PRACTICE ON PAYMENT OF CREDITORS

The majority of the Company's payments are in relation to the Notes and are due quarterly in accordance with the terms of the Notes. Payments are subject to the receipt of principal and appreciation rights received on the underlying mortgage pool. All such payments were made on the due dates

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 owed no amounts to trade creditors at 31 December 2009

DIRECTORS

The directors who served during the year were as follows

I G Stewart	
P A Curran	(Resigned 22 December 2009)
T A Hill	(Appointed 22 December 2009)

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

RISK MANAGEMENT

The majority of the Company's assets and liabilities have been classified as financial instruments in accordance with IAS 32 "Financial Instruments Presentation"

The Company's financial instruments comprise a mortgage portfolio, cash and liquid resources, a derivative contract ("swap"), an embedded derivative, interest-bearing loans and borrowings and various other payables that arise directly from its operations. The principal purpose of these financial instruments is to raise finance for the Company's operations.

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

The principal risks arising from the Company's financial instruments are credit risk and interest rate risk. These and other risks which may affect the Company's performance are detailed below. Further analysis of the risks facing the Company on its financial instruments is provided in note 16.

Credit Risk

Credit risk arises on the individual loans within the mortgage loan portfolio which are in turn secured on the underlying UK residential properties. The performance of these loans is therefore influenced by the economic background and the UK housing market. However, the maximum loan-to-value of the original advances was 25% and the credit risk is considered to be low.

The extent to which the Company can meet its obligations to pay interest and ultimately repay the Notes will be dependent upon the receipt of funds earned on its bank deposits, the swap agreement with the external provider, principal receipts on the mortgages and the Letter of Credit issued by BOS (see "Liquidity Risk"). To the extent that this income does not provide sufficient funds to cover the interest due on the Notes or the repayment of the Notes the Company has no claim on the assets of BOS.

The terms of the Mortgage Portfolio Agreement given by BOS in respect of the mortgages require BOS to repurchase any mortgage which is found to be in breach of warranty. BOS will repurchase any mortgages that are found or held not to be valid, binding and enforceable.

Although in such an event the total value of the outstanding loan and any accrued interest will be covered by BOS, the Note holder will not receive the benefit of any future payments of appreciation amounts or partial repayment of appreciation amounts in respect of the mortgages repurchased.

Shared appreciation is subject to the movement in the market value of the property which is dependent upon house price inflation ("HPI"). This may provide a return on the Notes below initial expectations. Any expected increase in value cannot be guaranteed.

Interest rate risk

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 minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of assets and liabilities are similar.

The Company has also 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 assets and liabilities by paying over a portion of capital appreciation on the mortgage loans in return for a fixed interest receipt. The Notes issued by the Company are exposed to cash flow interest rate risk as they carry a floating interest rate that is reset as market rates change.

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

RISK MANAGEMENT (CONTINUED)

Liquidity risk

The Company has an unconditional and irrevocable 364-day revolving Letter of Credit provided by BOS. The Letter of Credit is for a maximum aggregate principal amount of £1,165,000 to assist the Company should it not be able to meet its obligations under the Notes. The reliance on this facility is therefore dependent upon the creditworthiness of BOS. The Company has not drawn on the Letter of Credit since inception.

Operational risk

In accordance with the Programme Documentation the Company is bound to make payments to meet third party expenses.

The Company's operations are subject to periodic review by the Internal Audit function of LBG and is currently implementing processes to comply with the requirements of Sarbanes Oxley as part of the alignment with LBG.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

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 financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. In preparing these financial statements, the directors have also elected to comply with IFRSs, issued by the International Accounting Standards Board (IASB). Under company law the directors must not approve the financial statements unless they are satisfied that they 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 these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable International Financial Reporting Standards (IFRSs) as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements,

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and 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 2006. 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.

EMPLOYEES

The Company has employed no staff during the year ended 31 December 2009 or the previous year.

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

AUDITORS AND AUDIT INFORMATION

Following the resignation of KPMG Audit Plc on 13 May 2009, PricewaterhouseCoopers LLP were appointed as auditors of the Company with effect from the same date by resolution of the members dated 26 May 2009

Pursuant to section 487 of the Companies Act 2006, auditors duly appointed by the members of the company shall, subject to any resolution to the contrary, be deemed to be reappointed for the next financial year and PricewaterhouseCoopers LLP will therefore continue in office

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

This confirmation is given, and should be interpreted, in accordance with the provisions of section 418 of the Companies Act 2006

STATEMENT OF GOING CONCERN

As set out in the statement of compliance of the significant accounting policies section of the notes to the financial statements, 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

By Order of the Board



A Lockwood
Secretary

Premier House
City Road
CHESTER
CH88 3AN

DATE 25 March 2010

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

We have audited the financial statements of BOS (Shared Appreciation Mortgages) NO 2 PLC for the year ended 31 December 2009 which comprise the Statement of comprehensive income, the Balance sheet, the Statement of changes in equity, the Cash flow statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 4, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's member as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, 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.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2009 and of its profit and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

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

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit



Mark Hannam (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors

Benson House
33 Wellington Street
Leeds
LS1 4JP

Date 8 April 2010

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2009

	Notes	2009 £	2008 £
Interest receivable and similar income	2	3,806,638	3,728,306
Interest payable and similar charges	3	(1,468,930)	(3,156,324)
Net interest income		<u>2,337,708</u>	<u>571,982</u>
Net fair value gains and losses on derivatives held for economic hedging	4	(371,239)	58,070
Other operating income	5	3,900	2,870
Operating expenses	6	(68,728)	(76,077)
Profit before tax for the year		<u>1,901,641</u>	<u>556,845</u>
Taxation	7	(532,460)	(164,262)
Profit / Total comprehensive income attributable to equity holders		<u><u>1,369,181</u></u>	<u><u>392,583</u></u>

The profit shown above is derived from continuing operations. The Company operates in a single business segment and all of the Company's activities are in the UK.

There was no income or expense recognised directly in equity in the current year or preceding year.

The notes on pages 12 to 30 form an integral part of these financial statements.

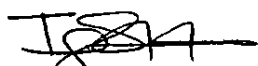
BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
BALANCE SHEET AS AT 31 DECEMBER 2009

	Notes	2009 £	2008 £
Assets			
Mortgage portfolio	8	14,129,109	15,082,385
Shared appreciation rights receivable	9	112,110,507	131,769,549
Total non-current assets		126,239,616	146,851,934
Cash and cash equivalents	10	36,417,833	36,283,837
Total current assets		36,417,833	36,283,837
Total assets		162,657,449	183,135,771
Equity			
Called up share capital	11	50,001	50,001
Retained earnings		3,046,918	1,848,737
Total equity		3,096,919	1,898,738
Liabilities			
Interest-bearing loans and borrowings	12	47,635,242	50,618,797
Shared appreciation rights payable	13	92,592,997	108,651,577
Deferred tax liability	14	151,183	170,080
Total non-current liabilities		140,379,422	159,440,454
Interest-bearing loans and borrowings	12	(16,020)	96,219
Other payables	15	631,341	277,748
Derivative liability		18,012,964	21,242,188
Bank overdraft	10	1,466	2,506
Current tax liability	7	551,357	177,918
Total current liabilities		19,181,108	21,796,579
Total liabilities		159,560,530	181,237,033
Total equity and liabilities		162,657,449	183,135,771

These financial statements were approved by the Board of Directors on

25 March 2010

and were signed on its behalf by


 Ian Gordon Stewart

Director

The notes on pages 12 to 30 form an integral part of these financial statements

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2009

	Share Capital £	Retained Profits £	Total £
Balance at 1 Jan 2009	50,001	1,848,737	1,898,738
Profit for the year	-	1,369,181	1,369,181
Dividends paid in the year	-	(171,000)	(171,000)
Balance at 31 Dec 2009	50,001	3,046,918	3,096,919

	Share Capital £	Retained Profits £	Total £
Balance at 1 Jan 2008	50,001	1,690,154	1,740,155
Profit for the year	-	392,583	392,583
Dividends paid in the year	-	(234,000)	(234,000)
Balance at 31 Dec 2008	50,001	1,848,737	1,898,738

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2009

Direct Method		2009	2008
	Notes	£	£
Operating Activities			Restated
Inter-company fees paid		(46,296)	(48,624)
Audit fees paid		(3,220)	(3,020)
Administration expenses		(15,378)	(21,375)
Tax paid		(177,918)	(299,223)
Net cash from operating activities		(242,812)	(372,242)
Investing Activities			
Repayments on mortgage portfolio		1,637,269	148,356
Shared appreciation rights received		5,732,168	3,643,596
Net cash flows from investing activities		7,369,437	3,791,952
Financing Activities			
Bank interest received		2,396,116	2,337,386
Premium interest received		371,821	385,620
Repayment of borrowings		(3,893,844)	(1,841,693)
Interest paid on borrowings		(602,628)	(2,277,296)
Shared appreciation rights paid		(5,451,285)	(3,477,096)
Dividends paid		(171,000)	(234,000)
Net cash from financing activities		(7,350,820)	(5,107,079)
Net decrease in cash and cash equivalents		(224,195)	(1,687,369)
Cash and cash equivalents at 1 January		42,747,484	44,434,853
Cash and cash equivalents at 31 December	10	42,523,289	42,747,484

The comparative 2008 cash flow statement has been restated using the direct method to be consistent with the presentation adopted by other companies within the LBG Group

As explained in the accounting policies in note 1, cash is distributed in accordance with the Programme Documentation

The notes on pages 12 to 30 form an integral part of these financial statements

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009

1. SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

The financial statements for the year ended 31 December 2009 have been prepared in accordance with International Financial Reporting Standards (IFRSs) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) as adopted by the European Union. The standards applied by the Company are those endorsed by the European Union and effective at the date the financial statements are approved by the Board. However the Company has not utilised the "carve-out" provisions in respect of full fair value and portfolio hedging of core deposits in IAS39 'Financial Instruments: Recognition and Measurement' as adopted by the European Union. Consequently, the financial statements comply with International Financial Reporting Standards.

The following new IFRS pronouncements, relevant to the Company, became effective in 2009 and have been adopted in these financial statements although they have no material impact on any part of the statements:

- IAS 1 (revised), 'Presentation of financial statements',
- Amendments to IFRS 7 'Financial Instruments: Disclosures – Improving Disclosures about Financial Instruments',
- IFRS 8 'Operating Segments'

The accounting policies set out below have been applied consistently in respect of the financial years ended 31 December 2009 and 31 December 2008.

The financial statements also comply with the relevant provisions of Part XV of the Companies Act 2006.

The financial statements are presented in sterling which is the Company's functional and presentation currency and have been prepared on the historical cost basis (except that derivative financial instruments are stated at their fair value).

The Company is reliant on funding provided by BOS plc. Notwithstanding the improvement in market liquidity during 2009, the Company's ultimate parent company, Lloyds Banking Group plc, continues to be reliant on UK Government sponsored measures to maintain its wholesale funding position. The directors are satisfied that it is the intention of Lloyds Banking Group plc that its subsidiaries including the Company will continue to receive funding in the future and, accordingly, the financial statements have been prepared on a going concern basis.

(b) Revenue recognition

Interest receivable and similar income have been calculated 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 over the expected life of the financial instrument. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability.

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Segment Reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

The directors of the Company consider that the entity has only one geographical and one business segment and therefore is not required to produce additional segmental disclosure.

(d) Financial instruments

The Company's financial instruments comprise a mortgage portfolio, cash and liquid resources, a derivative contract ("swap"), an embedded derivative, interest-bearing loans and borrowings and various other payables that arise directly from its operations.

The main purpose of these financial instruments is to raise finance for the Company's operations. These financial instruments are classified in accordance with the principles of IAS 39 as described below.

(d)(i) Mortgage portfolio

The Company's mortgage portfolio comprises mortgage loans with no fixed maturity date. The individual mortgage loans terminate on the earlier of the date of sale of the property or the death of the mortgage account holder.

Under IAS 39, the mortgage portfolio is classified within "loans and receivables". The initial measurement is at fair value (excluding amounts for the shared appreciation referred to in (d)(iv) below). Subsequent measurement is at amortised cost with revenue being recognised using the effective interest method. The discount arising on initial recognition is being amortised over the expected life of the mortgages.

At each reporting period end, the Company assesses whether there is any objective evidence that mortgage loans within the portfolio are impaired. The directors do not consider that a provision for impaired assets is currently required.

(d)(ii) Cash and cash equivalents

The Company holds bank accounts with BOS. These accounts are held in the Company's name and meet the definition of cash and cash equivalents. The use of certain accounts is restricted by a detailed priority of payments set out in the Programme Documentation. As the cash can only be used to meet certain specific liabilities and is not available to be used with discretion, it is viewed as restricted cash.

These bank accounts are classified within "loans and receivables" in accordance with IAS 39. The initial measurement is at fair value. Subsequent measurement is at amortised cost with revenue being recognised using the effective interest method. The discount arising on initial recognition is being amortised over the expected life of the mortgages and Notes.

The Cash Flow Statement has been restated using the direct method of preparation.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d) Financial instruments (continued)

(d)(iii) Interest-bearing loans and borrowings

The Company's interest-bearing loans and borrowings comprise mortgage-backed floating rate notes that have been issued in the capital market

Interest-bearing loans and borrowings are recognised initially at fair value less directly related incremental transaction costs. Subsequent to initial recognition, interest-bearing loans and borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

(d)(iv) Embedded derivatives

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host instrument, and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivative recognised in the income statement. Depending on the classification of the host instrument, the host is then measured in accordance with IAS 39.

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 the Note holders and the swap provider.

The economic characteristics and risks of the shared appreciation rights receivable and payable are not viewed as being closely related to those arising on the mortgages and Notes, respectively. The shared appreciation rights receivable and payable have therefore been valued separately from the mortgages and Notes using discounted cash flow techniques and taking account of current HPI. There is uncertainty regarding the timing of any future shared appreciation receipts and the directors do not consider that it is practical to include an estimate of future HPI in these valuations.

The resulting fair value movements of these embedded derivatives are recorded in net fair value gains and losses on derivatives held for economic hedging in the income statement and the embedded derivatives are shown separately on the face of the balance sheet. The host instruments are valued at amortised cost, as noted above in (d)(i) and (d)(iii).

(d)(v) Derivatives

IAS 39 requires all derivative financial instruments to be recognised initially at fair value on the balance sheet and to be re-measured to fair value at subsequent reporting dates. Where the value of the derivative is positive, it is carried as a derivative asset and where negative, as a derivative liability. The gain or loss on re-measurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged.

The Company uses a derivative financial instrument to hedge its exposure to interest rate risk arising from operational, financing and investment activities. In accordance with its treasury policy, the Company does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d) Financial instruments (continued)

(d)(v) Derivatives

The gain or loss on re-measurement of the interest rate swap to fair value has been recognised immediately in net fair value gains and losses on derivatives held for economic hedging in the income statement

Amounts receivable on the interest rate swap are accounted for on an accruals basis within interest receivable in the income statement. The shared appreciation payable is recorded in other operating income.

The fair value of interest rate swaps is the estimated amount that the Company would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

(e) Critical Accounting Judgements and Estimates

The preparation of the financial statements necessarily requires the exercise of judgement both in the application of accounting policies and in the selection of assumptions used in the calculation of estimates. These judgements are reviewed on an ongoing basis and are continually evaluated based on historical experience and other factors. The most significantly affected components of the financial statements and associated critical judgements are as follows:

Effective Interest Rate Method

The effective interest rate is calculated on initial recognition of the financial asset or liability, estimating the future cash flows after considering all the contractual terms of the instrument but not future credit losses. The calculation includes all amounts expected to be paid or received by the Company including expected early redemption fees and related penalties and premiums and discounts that are an integral part of the overall return. Direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument are also taken into account in the calculation. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

For the purpose of the effective yield calculation on the Notes, an average expected life has been calculated based on prepayment expectations for the mortgages. This is revised on a regular basis in light of actual redemption experience.

Fair Value Calculations

Fair value is defined as the value at which assets, liabilities or positions could be closed out or sold in a transaction with a willing and knowledgeable counterparty.

The value of the embedded derivative has been calculated by discounting future cash flows at an appropriate market rate. The valuation method is consistent with commonly used market techniques. All inputs into the valuation models are obtained from observable market data. No assumption for future HPI has been included as this is not considered to be practical.

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Taxation

Income tax recognised in the Income Statement comprises both current and deferred tax. Current income 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 substantially enacted by the balance sheet date which are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

The Company's tax charge for 2009 is calculated on an IFRS basis and disclosed in accordance with IAS 12.

(g) Fees and commissions

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.

(h) VAT

Value Added Tax is not recoverable by the Company and is included with its related costs.

(i) Dividends

Dividends on the equity shares of the Company are recognised in the year in which they are paid.

(j) Related parties

In accordance with the provisions of IAS 24 "Related Party Disclosures", the Company has disclosed details of transactions with its related parties.

(k) Other payables

Other payables are stated at cost or at amortised cost if deemed to be a financial liability.

2. INTEREST RECEIVABLE AND SIMILAR INCOME

	2009 £	2008 £
Mortgage interest from customers	679,470	679,470
Bank interest from BOS	2,626,553	58,862
Bank interest	500,615	2,989,974
	3,806,638	3,728,306

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

3 INTEREST PAYABLE AND SIMILAR CHARGES

	2009 £	2008 £
Interest payable on Notes	1,446,542	3,133,936
Amortisation of issue costs	22,388	22,388
	1,468,930	3,156,324

4. NET FAIR VALUE GAINS AND LOSSES ON DERIVATIVES HELD FOR ECONOMIC HEDGING

	2009 £	2008 £
Fair value movement on shared appreciation rights receivable	(19,659,042)	(38,587,512)
Fair value movement on shared appreciation rights payable	16,058,580	32,044,169
Fair value movement on interest rate derivative	3,229,223	6,601,413
	(371,239)	58,070

5. OTHER OPERATING INCOME

	2009 £	2008 £
Fees and commissions receivable	3,900	2,710
Shared appreciation receivable	5,732,168	3,643,596
Shared appreciation payable	(5,732,168)	(3,643,596)
Other income	-	160
	3,900	2,870

6. OPERATING EXPENSES

	2009 £	2008 £
Inter-company fees	46,181	48,461
Administration fees	19,327	24,357
Audit fees	3,220	3,259
	68,728	76,077

Audit fees relate to the statutory audit. There are no fees payable to the auditors and their associates for services other than the statutory audit.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

7. TAXATION

	2009	2008
	£	£
Current Tax		
Corporation tax charge for the year at a rate of 28% (2008 28.5%)	551,357	177,918
Corporation tax charge in respect of earlier periods	-	16,376
	<u>551,357</u>	<u>194,294</u>
Deferred Tax		
Deferred tax credit in respect of earlier periods	-	(11,134)
Deferred tax change in tax rate – charge	-	337
Deferred tax credit for the year at a rate of 28% (2008 28.5%)	(18,897)	(19,235)
	<u>532,460</u>	<u>164,262</u>
Total tax charge in income statement	<u>532,460</u>	<u>164,262</u>
Reconciliation of effective tax rate	2009	2008
	£	£
Profit before tax	1,901,641	556,845
	<u>1,901,641</u>	<u>556,845</u>
Profit before tax multiplied by the standard rate of corporation tax in the UK of 28% (2008 28.5%)	532,460	158,683
Effects of		
Corporation tax prior year	-	16,376
Deferred tax credit in respect of earlier periods	-	(11,134)
Deferred tax change in tax rate – charge	-	337
	<u>532,460</u>	<u>164,262</u>
Total tax charge in income statement	<u>532,460</u>	<u>164,262</u>

The current tax liability of £551,357 (2008 £177,918 liability) represents the net amount of income tax payable in respect of the current year

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

8. MORTGAGE PORTFOLIO

	2009 £	2008 £
At 1 January	15,082,385	15,182,033
Mortgage redemptions in the year	(1,632,746)	(779,118)
Amortisation of discount	679,470	679,470
At 31 December	14,129,109	15,082,385

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

9. SHARED APPRECIATION RIGHTS RECEIVABLE

The right for the Company to receive a share of the capital appreciation arising on the individual mortgages, as set out in the original loan agreements, is classified as an embedded derivative, in accordance with the principles of IAS 39. The embedded derivative has been valued separately from the host contract using discounted cash flow techniques. No estimate has been made of the effect of future HPI as the directors consider that this is impractical.

The Company is contractually obliged to pay to the Note holders or the swap provider any amounts received from mortgage customers for the shared appreciation. A corresponding embedded derivative liability has therefore been recognised in the balance sheet (note 13).

10. CASH AND CASH EQUIVALENTS

	2009 £	2008 £
Bank accounts	42,494,084	42,596,680
Accrued interest	30,671	153,310
Unamortised discount	(6,106,922)	(6,466,153)
Bank overdraft	36,417,833	36,283,837
	(1,466)	(2,506)
	36,416,367	36,281,331
Unamortised discount	6,106,922	6,466,153
Cash and cash equivalents per Cash Flow statement	42,523,289	42,747,484

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

10. CASH AND CASH EQUIVALENTS

Until January 2009, the Company held the GIC bank account with an external provider. The Company was contractually entitled to a LIBOR related return on this account. However, following the downgrade in the external bank provider's credit rating at the end of December 2008, the GIC account, together with other accounts with the same external provider, were transferred to BOS.

The equivalent GIC balance has been placed on deposit with BOS at 31 December 2009, with the intention to transfer to an appropriate GIC account once the Note holders have approved changes to the Programme Documentation with regard to the rating requirements for the new GIC provider.

All income is accounted for on an effective yield basis. The use of the accounts is restricted by a detailed priority of payments set out in the Programme Documentation. As the cash can only be used to meet certain specific liabilities and is not available to be used with discretion, it is viewed as restricted cash. The accounts are held in the Company's name and meet the definition of cash and cash equivalents.

11 SHARE CAPITAL

	2009	2008
	£	£
Authorised		
50,000 ordinary shares of £1 each	50,000	50,000
1 deferred share of £1	1	1
Allotted, called up and fully paid		
50,000 ordinary shares of £1 each	50,000	50,000
1 deferred share of £1	1	1

The Company is a directly held subsidiary undertaking of BOS.

The £1 deferred share is held by Deutsche Trustee Company Limited (formerly Bankers Trustee Company Limited).

The holder of the ordinary shares is entitled to receive dividends as declared from time to time.

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
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

11. 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% of the number of votes attached to all other issued shares of the Company.

Capital disclosures

The Company is not subject to externally imposed capital requirements in either the current year or the prior year other than the minimum share capital required by the Companies Act with which it complies. The Company manages its ordinary share capital in order that there is sufficient capital, in the opinion of the directors, to support the transactions and level of business undertaken by the Company.

12. INTEREST-BEARING LOANS AND BORROWINGS

This note provides information about the contractual terms of the Company's interest-bearing loans and borrowings. For more information about the Company's exposure to interest rate risk and the fair value of its financial instruments, see note 16.

	2009	2008
	£	£
Non-current liabilities		
Notes	47,993,454	50,999,397
Deferred issue costs	(358,212)	(380,600)
	47,635,242	50,618,797
Current liabilities		
Accrued interest payable to Note holders	6,368	118,607
Deferred issue costs	(22,388)	(22,388)
	(16,020)	96,219

The mortgage-backed floating rate Notes are due in 2072. The interest rate applicable on the Notes up to and including the interest period ending in the quarter to 31 August 2027 is 60% of the three-month LIBOR rate for Sterling deposits less 0.30% per annum. Thereafter, the interest rate applicable to the Notes will be 60% of the three-month LIBOR rate for Sterling deposits plus 0.10% per annum until 2072 when the Notes become due.

The 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 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 Notes are secured on the mortgage portfolio, the bank accounts and certain other assets of the Company.

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

13. SHARED APPRECIATION RIGHTS PAYABLE

The Company is contractually obliged to pay to the Note holders and swap provider any amounts received from mortgage customers for the shared appreciation arising on the sale of the property. An embedded derivative liability has therefore been recognised in the balance sheet for the same value as the embedded derivative asset (note 9).

14. DEFERRED TAX LIABILITY

	2009	2008
	£	£
At 1 January	170,080	200,112
Credit for year	(18,897)	(19,235)
Credit in respect of previous periods	-	(11,134)
Change in Tax Rate – charge	-	337
At 31 December	151,183	170,080

The deferred tax liability was recognised for the fair value adjustments that arose on transition to IFRS and is being released to the income statement over a period of ten years from adoption.

15. OTHER PAYABLES

	2009	2008
	£	£
Shared appreciation payable	447,383	166,500
Note redemptions payable	113,252	45,000
Accruals and deferred income	66,779	62,206
Amounts owed to BOS	3,927	4,042
	631,341	277,748

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

16. FINANCIAL INSTRUMENTS

The majority of the Company's assets and liabilities have been classified as financial instruments in accordance with IAS 32 "Financial Instruments Presentation"

The Company's financial instruments comprise a mortgage portfolio, cash and liquid resources, a derivative contract ("swap"), an embedded derivative, interest-bearing loans and borrowings and various other payables that arise directly from its operations

The principal risks arising from the Company's financial instruments are credit risk, liquidity risk and interest rate risk. Further detailed analysis of the risks facing the Company in relation to its financial instruments is provided below

As noted in the Directors' Business Review, the activities of the Company are conducted primarily by reference to a series of transaction documents (the "Programme Documentation"). The structure was established as a means of raising finance for BOS and no business activities are undertaken by the Company beyond those set out in the Programme Documentation

The Company's exposure to risk on its financial instruments and the management of such risk is largely determined at the inception of the securitisation transaction. The Company's activities and the role of each party to the transaction is clearly defined and documented

16(a) Credit risk

Credit risk is the risk of financial loss arising from a customer's failure to settle financial obligations as they fall due

Credit risk arises on the individual loans within the mortgage portfolio which are in turn secured on the underlying UK residential properties. The performance of these loans is therefore influenced by the economic background and the UK housing market. Mortgage loans are no longer offered by the Company but the maximum loan-to-value of the original advances was 25% and the credit risk is considered to be low

The extent to which the Company can meet its obligations to pay interest and ultimately repay the Notes will be dependent upon the receipt of funds earned on the bank deposits, the swap agreement with the external provider, principal receipts on the mortgages and the Letter of Credit issued by BOS (see "Liquidity Risk"). To the extent that this income does not provide sufficient funds to cover the interest due on the Notes or the repayment of the Notes the Company has no claim on the assets of BOS

The terms of the Mortgage Portfolio Agreement given by BOS in respect of the mortgages require BOS to repurchase any mortgage which is found to be in breach of warranty. BOS will repurchase any mortgages that are found or held not to be valid, binding and enforceable

Although in such an event the total value of the outstanding loan and any accrued interest will be covered by BOS, the Note holder will not receive the benefit of any future payments of appreciation amounts or partial repayment of appreciation amounts in respect of the mortgages repurchased

In terms of the shared appreciation, in accordance with the Programme Documentation, amounts received by the Company from the borrower are required to be paid over to the Note holders and swap provider

Credit risk also exists on the derivative contract with an external provider that the Company has entered into to manage the interest rate risk arising on its operations and sources of finance (see 16(b) below). The swap counterparty, UBS, is a regulated financial institution with a rating of A or above (2008 A rating or above)

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

16 FINANCIAL INSTRUMENTS (CONTINUED)

16(a) Credit risk (continued)

All loans in the mortgage portfolio pay a zero rate of interest. As a result, there are no arrears of interest, properties in possession or bad debts within the Company and therefore no impairment provision is considered to be necessary at 31 December 2009 or 31 December 2008.

The maximum exposure to credit risk arising on the Company's financial assets at the reporting date is disclosed in the table below.

	Note	Carrying Amount 2009 £	Maximum Exposure 2009 £	Carrying Amount 2008 £	Maximum Exposure 2008 £
Assets held at amortised cost.					
Mortgage portfolio	8	14,129,109	25,680,101	15,082,385	27,312,847
Cash and cash equivalents	10	36,417,833	42,524,755	36,283,837	42,749,990
Assets held at fair value.					
Shared appreciation rights receivable	9	112,110,507	112,110,507	131,769,549	131,769,549
Total Assets		162,657,449	180,315,363	183,135,771	201,832,386

At the balance sheet date all financial assets subject to credit risk were neither past due nor impaired. A financial asset is "past due" if a counterparty has failed to make a payment when contractually due.

16(b) Interest rate risk

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 minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of assets and liabilities are similar, where this is not possible the Company uses a derivative financial instrument to mitigate interest rate risk. The Notes issued by the Company are exposed to cash flow interest rate risk as the Notes carry a floating interest rate that is reset as market rates change.

The Company has entered into an interest rate swap with an external swap provider, UBS, 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 assets and liabilities by paying over a portion of capital appreciation on the mortgage loans in return for a fixed interest receipt.

The main impact on profit is due to variable rate movements on interest payable on the Notes and movements on the derivative.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

16. FINANCIAL INSTRUMENTS (CONTINUED)

16(b) Interest rate risk (continued)

At 31 December 2009, if interest rates had been 100 basis points higher or lower with all other variables held constant (2008 100 basis points spread), the net effect on the Company's income statement would be as shown in the table below. For 2009 due to the historically low interest rates and potential for rates to fluctuate in the future, a 100 basis point shift in interest rates is deemed to be an appropriate sensitivity measure.

	-100bps 2009 £	Per Income Statement 2009 £	+100bps 2009 £
Profit before tax for the year	2,452,654	1,901,641	1,348,205
	-100bps 2008 £	Actual 2008 £	+100bps 2008 £
Profit before tax for the year	771,634	556,845	342,056

16(c) Liquidity Risk

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at an unacceptably high cost.

The extent to which the Company can meet its obligations to pay interest and ultimately repay the Notes will be dependent upon the receipt of funds earned on the bank deposits, the swap agreement with the external provider, principal receipts on the mortgages and the Letter of Credit issued by BOS.

The Company has an unconditional and irrevocable 364-day revolving Letter of Credit provided by BOS. The Letter of Credit is for a maximum aggregate principal amount of £1,165,000 to assist the Company should it not be able to meet its obligations under the Notes. The reliance on this facility is therefore dependent upon the creditworthiness of BOS, which currently has a rating of A (2008 A rating).

The Company has not drawn on the Letter of Credit since inception.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

16. FINANCIAL INSTRUMENTS (CONTINUED)

16(c) Liquidity Risk (continued)

The liquidity tables reflect the undiscounted cash payments which will fall due if the structure continues until the earliest contractual maturity date as set out in the Programme Documentation. The Note repayment profile mirrors the repayment of the mortgages, and based on current modelling assumptions, it is not anticipated that any mortgages will still be outstanding beyond the step-up date of August 2027.

2009	Carrying amount	Contractual repayment value	Not later than one month	Later than one month but not later than three months	Later than three months but not later than one year	Later than one year and not later than five years	Later than five years
	£	£	£	£	£	£	£
Principal							
Notes	47,993,454	64,361,310	-	-	-	-	64,361,310
Derivative liability (swap)	18,012,964	13,136,190	-	(88,588)	(270,687)	(1,438,086)	14,933,551
Shared appreciation payable	92,592,997	97,587,551	-	-	-	-	97,587,551
Other payables	631,341	631,341	9,342	621,999	-	-	-
Interest payable							
Interest payable on Notes	6,368	766,857	-	10,646	32,529	172,818	550,864
	<u>159,237,124</u>	<u>176,483,249</u>	<u>9,342</u>	<u>544,057</u>	<u>(238,158)</u>	<u>(1,265,268)</u>	<u>177,433,276</u>
2008	Carrying amount	Contractual repayment value	Not later than one month	Later than one month but not later than three months	Later than three months but not later than one year	Later than one year and not later than five years	Later than five years
	£	£	£	£	£	£	£
Principal							
Notes	50,999,397	68,255,151	-	-	-	-	68,255,151
Derivative liability (swap)	21,242,188	15,981,001	(32,476)	(61,809)	(288,094)	(1,529,519)	17,892,899
Shared appreciation payable	108,651,577	115,589,861	-	-	-	-	115,589,861
Other payables	277,748	277,748	8,017	269,731	-	-	-
Interest payable							
Interest payable on Notes	118,607	26,196,818	-	351,995	1,044,506	5,589,828	19,210,489
	<u>181,289,517</u>	<u>226,300,579</u>	<u>(24,459)</u>	<u>559,917</u>	<u>756,412</u>	<u>4,060,309</u>	<u>220,948,400</u>

BOS (SHARED APPRECIATION MORTGAGES) NO 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

16. FINANCIAL INSTRUMENTS (CONTINUED)

16(d) Fair values

The fair values of the Company's principal financial instruments, together with the carrying amounts shown in the balance sheet are as follows

	Note	Carrying amount 2009 £	Fair value 2009 £	Carrying amount 2008 £	Fair value 2008 £
Loans and Receivables at amortised cost					
Mortgage portfolio	8	14,129,109	4,321,126	15,082,385	5,919,438
Financial liabilities at amortised cost					
Interest-bearing loans and borrowings	12	(47,619,222)	(42,158,646)	(50,715,016)	(46,178,582)

The embedded derivatives for shared appreciation receivable and payable are recognised in the balance sheet at fair value

The following comments summarise the main methods and assumptions used in estimating the fair value of financial instruments

The fair value of the mortgage portfolio, interest-bearing loans and borrowings, shared appreciation rights receivable, shared appreciation rights payable and the derivative swap have been calculated by discounting future cash flows at an appropriate market rate. The valuation method is consistent with commonly used market techniques. All significant inputs into the valuation models are obtained from observable market data.

For this reason, in accordance with "IFRS 7 Financial Instruments Disclosures", the fair value measurement for the shared appreciation is deemed to be Level 2 in the Fair Value Hierarchy. The change in fair value that has been calculated using this valuation technique has been recognised in the income statement for the year ended 31 December 2009.

The cash and cash equivalents and other payables are recognised on an amortised cost basis that is considered to be a close approximation to fair value.

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

17. RELATED PARTIES

The Company is a subsidiary undertaking of BOS, HBOS and ultimately LBG. The Company receives bank interest from BOS, its immediate parent undertaking. BOS administers the mortgage portfolio on behalf of the Company, for which quarterly service fees are paid. In 2009, a dividend of £171,000 (2008: £234,000) was paid to BOS. The Company's transactions with related parties are summarised below:

	Lloyds Banking Group plc and subsidiaries 2009 £	HBOS plc and subsidiaries 2008 £
Income Statement		
Interest receivable and similar income	2,626,553	58,862
Operating expenses	(46,181)	(48,461)
Balance Sheet		
Equity		
Dividends paid	(171,000)	(234,000)
Assets		
Cash and cash equivalents	42,524,755	1,428,104
Liabilities		
Other payables	(3,927)	(4,042)
Bank overdraft	(1,466)	(2,506)

BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)

18. ACCOUNTING PRONOUNCEMENTS EFFECTIVE AFTER 2009

The following pronouncements will be relevant to the Company but were not effective at 31 December 2009 and have not been applied in preparing these financial statements. The full impact of these accounting changes is being assessed by the Company. The initial view is that none of these pronouncements are expected to cause any material adjustments to reported numbers in the financial statements.

Pronouncement	Nature of change	IASB effective date
<i>Amendment to IAS 39 Financial Instruments Recognition and Measurement – Eligible Hedged Items</i>	Clarifies how the principles underlying hedge accounting should be applied in particular situations	Annual periods beginning on or after 1 July 2009
Improvements to IFRSs (issued April 2009)	Sets out minor amendments to IFRS standards as part of annual improvements process	Dealt with on a standard by standard basis but not earlier than annual periods beginning on or after 1 January 2010
<i>IFRS 9 Financial Instruments Classification and Measurement</i>	Simplifies the way entities will classify financial assets and reduces the number of classification categories to two, fair value and amortised cost. The existing available-for-sale and held-to-maturity categories have been eliminated. Classification will be made on the basis of the objectives of entity's business model for managing the assets and the characteristics of the contractual cash flows.	Annual periods beginning on or after 1 January 2013
<i>IAS24 Related Party Disclosures</i>	Simplifies the definition of a related party and provides a partial exemption from the disclosure requirements for government related entities	Annual periods beginning on or after 1 January 2011

**BOS (SHARED APPRECIATION MORTGAGES) NO. 2 PLC
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2009 (CONTINUED)**

19. PARENT UNDERTAKINGS

The Company's immediate parent company is BOS plc. The company regarded by the directors as the ultimate parent company is Lloyds Banking Group plc, a limited liability company incorporated and domiciled in Scotland, which is also the parent undertaking of the largest group of undertakings for which group accounts are drawn up and of which the Company is a member. BOS plc is the parent undertaking of the smallest such group of undertakings. Copies of the group accounts of both companies may be obtained from Group Secretariat, Lloyds Banking Group plc, The Mound, Edinburgh, EH1 1YZ.