419096

Preferred Holdings Limited

Report and consolidated financial statements

30 November 2005

Registered No 4191096

Directors
W Bilsborough
D Gibb
W Hinshelwood
N Ingram
C Rupp
R Taylor

Secretary
Clifford Chance Secretaries (CCA) Limited
10 Upper Bank Street
London
E14 5JJ

Auditors
Ernst & Young LLP
1 More London Place
London SE1 2AF

Bankers
Barclays Bank PLC
54 Lombard Street
London
EC3V 9EX

National Westminster Bank PLC
1 Princes Street
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EC2R 8PB

Girobank PLC
Bridle Road
Bootle
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GIR 0AA

Registered Office
6 Broadgate
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Directors' report

The directors present their report and the financial statements for the year ended 30 November 2005

Principal activities

The principal activity of the Company is that of a holding company and the Company currently holds the entire share capital of Preferred Group Limited

The principal activity of the Group is the provision of loans secured on properties in the United Kingdom

Future prospects

The directors are confident that the Company is well placed to continue its activities

Going concern

The directors believe that the Group is a going concern and accordingly have prepared the financial statements on this basis

Results and dividends

The results of the Group for the year are shown in the consolidated profit and loss account on page 6 The directors do not recommend the payment of a dividend (30 November 2004 – nil)

Directors and their interests

The directors who held office during the year, and after the year end, were as follows

G Fraser (resigned 9 November 2005)
G Patellis (resigned 9 November 2005)
J Webster (resigned 15 December 2005)
A Attia (resigned 18 May 2006)
W Bilsborough (appointed 9 November 2005)
D Gibb (appointed 17 May 2006)
W Hinshelwood (appointed 17 May 2006)
N Ingram (appointed 9 November 2005)
C Rupp (appointed 9 February 2006)
R Taylor (appointed 9 November 2005)

During the year, none of the directors who held office, nor any of their families, held any beneficial interest in the shares of the Company or of any group company

Policy and practise on payment of creditors

The Company does not follow any stated code on payment practice It is the Group's policy to agree terms of payment with suppliers when agreeing the terms of each transaction and to abide by those terms Standard terms provide for payment of all invoices within 30 days after the date of the invoice, except where different terms have been agreed with the supplier at the outset It is the policy of the Group to abide by the agreed terms of payment There are 15 creditors days of suppliers' invoices outstanding at the year end (30 November 2004 – 15 days)

Events occurring after the balance sheet

On 31 January 2006 the Group disposed of £2,314,541 of assets at net book value to Capstone Mortgage Services Limited This sale formed part of the implementation of a shared service centre within Capstone Mortgage Services Limited to provide support services to the Group and to other Lehman Brothers mortgage businesses in the United Kingdom On 31 January 2006, the entire share capital of Preferred Holdings Limited was acquired by Resetfan Limited

Directors' report

Financial instruments

The Group's financial instruments comprise mortgages, borrowings, cash and liquid resources, and various items (such as trade debtors and trade creditors) that arise directly from its operations

The Group also enters into derivative transactions (principally interest rate swaps, caps and currency swaps) to manage the interest rate and currency risks arising within the securitised mortgage vehicles

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

The main risks arising from the Group's financial instruments are credit risk, interest rate risk, currency risk and liquidity risk The directors review and agree policies for managing each of these risks and they are summarised below These policies have remained unchanged from 2004

Credit risk

Credit risk is principally the risk that borrowers will not be able to meet their obligations as they fall due, allied to the risk that property values will fall to the extent that borrowers' failure to meet obligations is translated into losses

The Group has established detailed, documented credit policies, which are used to define, monitor and control the quality of new lending through analysis of new origination, existing portfolios and the wider marketplace These policies control the approval of new origination sources, the approval of new products, the underwriting criteria development, underwriting and collection mandates and the criteria and processes for arrears collection, litigation and repossession

The ongoing credit risk of the mortgage portfolio (and particularly in respect of accounts in arrears) is closely monitored by the directors

Interest rate risk

Interest rate risk exists where assets and liabilities have interest rates set under different bases or which reset at different times The Group minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of its assets and liabilities are similar Where this is not possible the Group considers the use of derivative financial instruments to mitigate any residual interest rate risk

Foreign exchange risk

Foreign exchange risk exists where loan notes are denominated in a currency which is different to the underlying sterling mortgage loans The Group minimises its exposure to foreign currency risk by ensuring that the currency characteristics of its assets and liabilities are similar, where this is not possible the Group considers the use of derivative financial instruments to mitigate any foreign exchange risk

Liquidity risk

The Group's policy is to manage liquidity risk by matching the timing of the cash receipts from mortgage assets with those of the cash payments due on the sources of financing, which include loan notes, funding facilities and subordinated loans

Auditors

A resolution to reappoint Ernst & Young LLP as auditors will be put to the members at the next Annual General Meeting

Approved by the board of directors and signed on behalf of the board

Director

Date 24 April 2007

Statement of directors' responsibilities in respect of the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and United Kingdom Generally Accepted Accounting Practice regulations

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 Group and of the profit or loss of the Group 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, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group 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 Group and to enable them to ensure that the financial statements comply with the Companies Act 1985 They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

ERNST & YOUNG

Independent auditors' report

to the members of Preferred Holdings Limited

We have audited the Group's financial statements for the year ended 30 November 2005 which comprise the Consolidated Profit and Loss Account, Consolidated Balance Sheet, Company Balance Sheet, the Consolidated Cash Flow Statement and the related notes 1 to 28 These financial statements have been prepared on the basis of the accounting policies set out therein

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985 Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities the Company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards

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 Group 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 United Kingdom 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 Group'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 affairs of the Company and of the Group as at 30 November 2005 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985

Ernst & Young LLP.

Ernst & Young LLP
Registered Auditor
London

24/04/06

Consolidated profit and loss account

for the year ended 30 November 2005

	Notes	*Year ended 30 November 2005 £000*	*Period ended 30 November 2004 £000*
Interest receivable and similar income	2	44,575	27,151
Interest payable and similar charges	3	(38,885)	(20,980)
Net interest income		5,690	6,171
Income from securitised operations	4	53,538	30,031
Profit on sale of mortgage assets	5	3,600	–
Other operating income	6	14,938	10,970
Operating income		77,766	47,172
Operating expenses		(52,128)	(32,751)
Operating profit		25,638	14,421
Provision for bad and doubtful debts		(847)	(2,355)
Profit on ordinary activities before taxation		24,791	12,066
Taxation	8	(7,620)	(54)
Profit on ordinary activities after taxation	21	17,171	12,012
Retained profit for the year		17,171	12,012

The profit for the year was derived from continuing operations

There were no recognised gains or losses other than the profit for the year, accordingly no statement of recognised gains and losses is given

The notes on pages 10 to 31 form part of these financial statements

Consolidated balance sheet

at 30 November 2005

	Notes	2005 £000	2004 £000
Fixed assets			
Intangible assets	11	6,622	7,047
Tangible assets	12	2,419	2,914
		9,041	9,961
Current assets			
Mortgage loans and other assets - securitised balances	15	1,734,399	1,395,736
Less non recourse borrowings and other liabilities	15	(1,691,391)	(1,383,850)
		43,008	11,886
Mortgage loans - unsecuritised balances	14	501,593	378,637
		544,601	390,523
Debtors	17	51,897	43,440
Cash at bank and in hand		60,636	86,108
Total current assets		657,134	520,071
Creditors amounts falling due within one year	18	(547,122)	(437,917)
Net current assets		110,012	82,154
Total assets less current liabilities		119,053	92,115
Creditors amounts falling due after more than one year	19	(78,782)	(69,015)
Net assets		40,271	23,100
Capital and reserves			
Called up share capital	20	5	5
Share premium	21	490	490
Profit and loss account	21	39,776	22 605
Shareholders' funds	22	40,271	23 100

Included above within mortgages are balances due within one year and after more than one year, the analysis of which is provided in note 16

The notes on pages 10 to 31 form part of these financial statements

These financial statements were approved by the board of directors and were signed on its behalf by

Director

Date 24 April 2007

Company balance sheet

at 30 November 2005

	Notes	2005 £000	2004 £000
Fixed assets			
Investments	13	–	–
		–	–
Current assets			
Debtors	17	368	368
Cash		1	1
Total current assets		369	369
Creditors: amounts falling due within one year	18	(310)	(310)
Net current assets		59	59
Total assets less current liabilities		59	59
Creditors amounts falling due after more than one year		–	–
Net assets		59	59
Capital and reserves			
Called up share capital	20	5	5
Share premium	21	490	490
Profit and loss account	21	(436)	(436)
Equity shareholders' funds	22	59	59

The notes on pages 10 to 31 form part of these financial statements

These financial statements were approved by the board of directors and were signed on its behalf by

Director [signature]

Date 24 April 2007

Consolidated cash flow statement

for the year ended 30 November 2005

	Notes	*Year ended 30 November 2005 £000*	*Period ended 30 November 2004 £000*
Net cash outflow from operating activities	24(a)	126,953	97,679
Returns on investments and servicing of finance	24(b)	(113,910)	(76,397)
Taxation		(2,294)	(4,485)
Capital expenditure and financial investment	24(b)	(536,446)	(527,395)
Cash outflow before use of liquid resources and financing		(525,697)	(510,598)
Financing	24(b)	425,457	767,907
(Decrease)increase in cash in the year		(100,240)	257,309

Reconciliation of net cash flow to movement in net debt (note 24(c))

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
(Decrease)/increase in cash in the year	(100 240)	257,309
Cash inflow from increase in debt financing	(425,299)	(767,737)
Change in net debt arising from cash flows	(525,539)	(510,428)
Net debt at 31 December 2004	(1,549,548)	(1,039,120)
Net debt at 30 November 2005	(2,075,087)	(1,549,548)

Notes to the financial statements

at 30 November 2005

1. Accounting policies

Basis of accounting

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

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiary undertakings made up to 30 November 2005 The acquisition method of accounting has been adopted

Under section 230(4) of the Companies Act 1985 the Company is exempt from the requirement to present its own profit and loss account The amount of profit for the period dealt with in the financial statements of Preferred Holdings Limited is disclosed in note 21

Linked presentation

The Group has sold by securitisation, certain mortgages to other companies on a non-recourse basis In accordance with the requirements of Financial Reporting Standard No 5 "Reporting the Substance of Transactions", these amounts cannot be derecognised and have been disclosed on the face of the balance sheet less any non-recourse finance, using the linked presentation basis

Quasi-subsidiaries

Preferred Residential Securities 1 PLC, Preferred Residential Securities 2 PLC, Preferred Residential Securities 3 PLC, Preferred Residential Securities 4 PLC, Preferred Residential Securities 5 PLC and Preferred Residential Securities 6 PLC, Preferred Residential Securities 7 PLC, Preferred Residential Securities 8 PLC, Preferred Residential Securities 05-1 PLC and Preferred Residential Securities 05-2 PLC have been consolidated as quasi-subsidiaries under the linked presentation basis described above

In addition, Preferred Funding One Limited, Preferred Funding Two Limited, Preferred Funding Four Limited and Preferred Mortgages Collections Limited and PRS 5&6 Sub Loan Holdings Ltd have been fully consolidated as quasi-subsidiaries

Mortgage loans

Mortgage loans are stated at cost less provision made to reduce the value of the loans to their estimated recoverable amounts Provisions are made against mortgages when, in the opinion of the Directors, credit risk or economic risk make recovery doubtful

Income and expense recognition

Interest receivable and insurance commissions are accounted for on an accruals basis Fees are credited to income when they have been charged to the borrower's account Receipts and payments of expenses are accounted for on an accruals basis

Provisions

Specific provisions for losses on loans and advances to customers in arrears are made throughout the period and at the period-end on a case-by-case basis (calculated with reference to the probability of the loan defaulting and the value of the security held against the loan) The specific provision for properties in possession is based on the balance outstanding less a discounted valuation of the security held (with adjustments for expenses of sale)

Notes to the financial statements

at 30 November 2005

1. Accounting policies (continued)

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less accumulated depreciation

Depreciation is provided to write off the cost of tangible fixed assets on a straight line basis at the following rates per annum

Office furniture, fixtures and fittings	15%
Office equipment and computer software	25%

Operating leases

Rental costs under operating leases are charged to the profit and loss account on a straight line basis over the period of the lease

Origination costs deferral

Third party introduction fees incurred in originating mortgages are written off over the period in which early redemption charges apply (currently 36 months from the date of completion) or the life of the mortgage loan, whichever is the shorter

Investments

In the Company's financial statements, investments in subsidiary undertakings are stated at cost, less any necessary provision for diminution in value

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transaction or events that result in an obligation to pay more, or a right to pay less tax in the future, have occurred at the balance sheet date

Deferred tax assets are recognised only to the extent that the directors consider it is more likely than not that there will be suitable taxable profits from which the reversal of the underlying timing differences can be deducted Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date

Turnover

The Group's trade and turnover are wholly within the UK and within a single market sector Consequently, no segmental analysis has been prepared

Deferred consideration

Deferred consideration represents further amounts payable on the acquisition of mortgages from Preferred Mortgages Limited, a subsidiary of the company, by the Preferred Residential Securities and Preferred Funding companies The payment of these amounts is conditional on the performance of the acquired mortgages

Notes to the financial statements

at 30 November 2005

1. Accounting policies (continued)

Foreign exchange currency swaps

A currency swap has been entered into, in order to manage the currency rate exposure in relation to non-sterling denominated loan notes of Preferred Residential Securities 6 PLC, Preferred Residential Securities 8 PLC, Preferred Residential Securities 05-1 PLC and Preferred Residential Securities 05-2 PLC The derivative contracts match the expected profile of the run-off of the non-sterling denominated loan notes The net interest paid on the loan notes is recorded on an accruals basis and included within interest payable within the income from securitised operations Any foreign exchange gain or loss arising from the currency swaps in respect of capital and interest repayments is recorded on an accruals basis and is included in interest receivable or payable

Interest rate cap

An interest rate cap has been entered into, in order to manage Preferred Residential Securities 05-1 PLC's interest rate exposure in relation to fixed rate mortgage assets The derivative contracts match the expected profile of the run-off of the fixed rate mortgage assets The net interest received on the mortgage assets are recorded on an accrual basis and included within interest receivable within the profit and loss account Any gain or loss arising from the interest rate cap is included in the interest receivable or payable within the profit and loss account

Pension costs

The Group pays contributions to defined contribution pension schemes that are either personal pension plans or group personal pension schemes Such contributions are charged in the financial statements as they accrue

Finance leases

Assets held under finance leases are capitalised as tangible fixed assets and are depreciated over the shorter of the lease term and their useful lives The capital elements of future lease obligations are recorded as liabilities, while the interest elements are charged to the profit and loss account over the period of the lease

2 Interest receivable and similar income

	Year ended 30 November 2005	*Period ended 30 November 2004*
	£000	*£000*
Mortgage interest	41,839	24,421
Bank interest	2,549	2,081
Other	187	649
	44,575	27,151

Notes to the financial statements

at 30 November 2005

3. Interest payable and similar charges

	Year ended 30 November 2005 £000	Period ended 30 November 2004 £000
Loan facilities	37,855	20,641
Other interest	1,030	339
	38,885	20,980

4. Income from securitised and unsecuritised operations

(a) Securitised operations

Preferred Residential Securities 1 PLC, Preferred Residential Securities 2 PLC, Preferred Residential Securities 3 PLC, Preferred Residential Securities 4 PLC, Preferred Residential Securities 5 PLC, Preferred Residential Securities 6 PLC, Preferred Residential Securities 7 PLC, Preferred Residential Securities 8 PLC, Preferred Residential Securities 05-1 PLC and Preferred Residential Securities 05-2 PLC all hold securitised mortgage assets The summarised profit and loss account for these companies is as follows

	Year ended 30 November 2005 £000	Period ended 30 November 2004 £000
Interest receivable	130,889	90,417
Interest payable	(78,658)	(57,863)
Other operating income	8,161	3,938
Operating expenses	(5,065)	(2,435)
Provision for bad and doubtful debts	(1,767)	(4,002)
Corporation tax charge	(22)	(24)
	53,538	30,031

(b) Unsecuritised operations

Prior to acquisition by Lehman Brothers Holdings PLC, Preferred Mortgages Limited a subsidiary of the company transferred mortgages on an ongoing basis to Preferred Funding One Limited, Preferred Funding Two Limited, Preferred Funding Three Limited and Preferred Funding Four Limited On acquisition the mortgages and loan facilities within these companies were transferred to Preferred Funding Five Limited

Preferred Funding One Limited, Preferred Funding Two Limited and Preferred Funding Four Limited are wholly owned by a charitable trust and as detailed in note 1, have been consolidated as quasi-subsidiaries Preferred Funding One Limited, Preferred Funding Two Limited and Preferred Funding Four Limited have traded throughout the accounting period

Notes to the financial statements

at 30 November 2005

4. Income from securitised and unsecuritised operations (continued)

(b) Unsecuritised operations (continued)

Preferred Holdings Limited is not obliged to support any losses of Preferred Funding One Limited, Preferred Funding Two Limited and Preferred Funding Four Limited and does not intend to do so The liabilities of Preferred Funding One Limited, Preferred Funding Two Limited and Preferred Funding Four Limited, are only repayable out of funds generated by the mortgage loans and there is no recourse to the Group for any shortfall

Both Preferred Funding Three Limited and Preferred Funding Five Limited are wholly owned subsidiaries of Preferred Mortgages Limited All of above mentioned funding companies carry out the principal activity of financing the provision of residential mortgages

The summarised profit and loss account for Preferred Funding One Limited, Preferred Funding Two Limited and Preferred Funding Four Limited for the year ended 30 November 2005, were as follows

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Interest receivable	1,011	501
Interest payable	(1,111)	–
Net interest income	(100)	501
Other operating income	588	1,326
Operating expenses	(488)	(1,827)
Operating profit	–	–
Taxation	–	–
Profit after taxation	–	–

Operating expenses includes the provision/(write back) of deferred consideration payable to Preferred Mortgages Limited, of which the Company is parent, of £430,701 (30 November 2004 – (£1,247,448))

5. Profit on sale of mortgage assets

During the year Preferred Mortgages Limited sold mortgage assets of £268,236,844 (2004 – £Nil), and recognised a profit of £3,600,000 (2004 – £Nil)

Notes to the financial statements

at 30 November 2005

6. Other operating income

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Commissions and fee income	14,938	10,970

Commissions and fee income includes redemption fee income, insurance commission income and sundry fee income

7. Profit on ordinary activities before taxation

Profit on ordinary activities before taxation is stated after charging

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Auditors' remuneration		
Audit services - audit fees	214	150
- non-audit fees	–	–
Depreciation of tangible fixed assets	2,025	1,005
Amortisation of goodwill	425	390
Operating lease rentals in respect of		
Land and buildings	645	508
Other	285	103

(Included in depreciation above is £49,471 (2004 – £91,999) being depreciation of assets held under finance leases)

Notes to the financial statements

at 30 November 2005

8. Taxation

(a) Tax charge for the year

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
UK corporation tax at 30%	7,902	–
Prior year adjustment	–	180
Total current tax for period (note 8(b))	7,902	180
Deferred taxation		
Origination and reversal of timing differences	(270)	(126)
Adjustment in respect of prior years	(12)	
Total deferred tax (note 8(c))	(282)	(126)
Total current tax	7,620	54

(b) Factors affecting tax charge for the year

The tax assessed on the profit on ordinary activities for the year is higher than the companies rate of corporation tax in the UK, currently 30 6 (2004 – 30%) The differences are explained below

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Profit before taxation	24,791	12,066
Expected tax charge at 30%	7,437	3,620
Expenditure not qualifying for tax relief	67	19
Capital allowances in excess of depreciation	261	71
Non deductible goodwill	128	117
Other timing differences	9	–
Group relief claimed for nil consideration	–	(3,807)
Consolidation adjustments	–	(20)
Underprovision in previous years	–	180
Total current tax	7,902	180

Notes to the financial statements

at 30 November 2005

8. Taxation (continued)

(c) Deferred tax

The deferred tax asset can be analysed as follows

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Capital allowances in excess of depreciation	(282)	(126)

The deferred tax asset can be analysed as follows

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Balance at 1 January	86	(40)
(Debit)/credit to profit and loss account	282	126
	368	86

9. Directors' emoluments

Directors' emoluments are as follows

	Year ended 30 November 2005 £000	*Period ended 30 November 2004 £000*
Salaries	529	673
Other	28	33
Aggregate remuneration	557	706
Remuneration of the Chairman	–	–
Remuneration of the highest paid director	295	437

None of the directors are members of a company pension scheme, (30 November 2004 – none) but during the period, the Group has made contributions to personal pensions plans for the directors totalling £6,249 (30 November 2004 – £6,110)

Notes to the financial statements

at 30 November 2005

9. Directors' emoluments (continued)

Highest paid director

The highest paid director in 2005, was G Patellis (30 November 2004 – D J Pitocco)

	2005	*2004*
	£000	*£000*
Total emoluments	295	437
Contributions to personal pension plan	–	–

10. Employees

The Company does not employ any employees The average number of employees in the Group, including directors, during the year was 368 (30 November 2004 – 271) and they were employed in the following areas of the business

	2005	*2004*
	No	*No*
Sales and marketing	31	24
Administration	337	247
	368	271

The costs incurred in respect of these employees were

	2005	*2004*
	£000	*£000*
Salaries	10,199	7,359
Pension costs	272	193
Social security costs	1,138	808
	11,609	8,360

Pension costs represent contributions made by the Group to the personal pension plans or group personal pension schemes of certain employees

Notes to the financial statements

at 30 November 2005

11. Intangible fixed assets

	Goodwill 2005 £000	*Goodwill 2004 £000*
Cost		
At 1 December 2004 and 30 November 2005	8,498	8,498
Accumulated amortisation		
At 1 December 2004	1,451	1,061
Charge for year	425	390
At 30 November 2005	1,876	1,451
Net book value		
At end of year	6,622	7,047
At start of year	7,047	7,437

12. Tangible fixed assets

Group

	Office equipment £000	*Fixtures and furniture £000*	*Total £000*
Cost			
At 1 December 2004	5,141	720	5,861
Additions	1,302	228	1,530
At 30 November 2005	6,443	948	7,391
Depreciation			
At 1 December 2004	2,616	331	2,947
Charge for the year	1,890	135	2,025
At 30 November 2005	4,506	466	4,972
Net book value			
At 30 November 2005	1,937	482	2,419
At 30 November 2004	2,525	389	2,914

Included in the net amounts for office equipment above are £40,638 (2004 – £197,885) relating to assets held under finance leases

The Company has no tangible fixed assets

Notes to the financial statements

at 30 November 2005

13. Fixed asset investments

Company

	Shares in subsidiary undertakings
	£
Cost	
At 30 November 2004 and 30 November 2005	1
Net book value	
At 30 November 2004 and 30 November 2005	1

Subsidiary undertakings	*Country of registration and operation*	*Activity*	*Portion of ordinary shares held*
Preferred Group Limited	England and Wales	Investment holding company	100%
Preferred Mortgages Limited*	England and Wales	Provision of loans secured on properties	100%
Yellow Brick Road Direct Mortgages Limited*	England and Wales	Dormant	100%
Preferred Home Loans Limited*	England and Wales	Dormant	100%

With the exception of the companies marked with an asterisk, all shareholdings are in the name of Preferred Holdings Limited All subsidiaries have been included in the consolidation

The following information is presented in the financial statements of Preferred Group Limited for the year ended 30 November 2005

	2005
	£000
Aggregate capital and reserves	367
Profit for the year	–

The following information is presented in the consolidated financial statements of Preferred Mortgages Limited, a subsidiary of Preferred Group Limited, for the year ended 30 November 2005

	2005
	£000
Aggregate capital and reserves	48,590
Profit for the year	17,596

Notes to the financial statements

at 30 November 2005

14. Mortgage loans – unsecuritised balances

Group

	Mortgages £000	*Mortgage loss provision £000*	*Total £000*
At beginning of the year	382,470	(3,833)	378,637
Net movement	124,744	(2,008)	122,956
At end of the year	507,434	(5,841)	501,593

The summarised balance sheets as at 30 November 2005 prior to consolidation adjustments for Preferred Funding One Limited, Preferred Funding Two Limited and Preferred Funding Four Limited were as follows

	2005 £000	*2004 £000*
Current assets		
Debtors		
Amounts falling due after one year	6,558	18
Amounts falling due within one year	9,758	7,781
Cash at bank and in hand	4,988	7,348
	21,304	15,147
Creditors amounts falling due within one year	(21,292)	(15,135)
Net assets	12	12
Capital and reserves		
Called up share capital	–	–
Profit and loss account	12	12
	12	12

15. Mortgage loans – securitised balances

(a) Consolidation using linked presentation

During the period the Group securitised £365 9m mortgages within Preferred Residential Securities 05-1 PLC and £299 8m mortgages within Preferred Residential Securities 05-2 PLC, owned by a charitable trust As at 30 November 2005 the Group had securitised mortgages of £1,579 6m within the ten special purpose companies, Preferred Residential Securities 1 PLC, Preferred Residential Securities 2 PLC, Preferred Residential Securities 3 PLC, Preferred Residential Securities 4 PLC, Preferred Residential Securities 5 PLC Preferred Residential Securities 6 PLC, Preferred Residential Securities 7 PLC Preferred Residential Securities 8 PLC, Preferred Residential Securities 05-1 PLC and Preferred Residual Securities 05-2 PLC These special purpose companies are consolidated within the financial statements of the Group on a linked presentation basis, in accordance with FRS5 The consolidated results of those companies are detailed in note 4 All of the companies invest in residential mortgage loans secured by first or second charges

Notes to the financial statements

at 30 November 2005

15. Mortgage loans – securitised balances (continued)

The summary consolidated balance sheet of these ten companies is as follows

	2005 £000	2004 £000
Mortgage loans (note 15(b))	1,579,563	1,169,661
Debtors due within one year	7,276	3,360
Cash at bank	147,560	222,765
Total assets	1,734,399	1,395,736
Mortgage Backed Loan Notes (note 15(c))	1,672,818	1,359,880
Other creditors		
Due within one year	18,573	23,970
Due after one year	–	–
Total liabilities	1,691,391	1,383,850
Net securitised assets	43,008	11,886

The Group is not obliged to support any losses of the securitisation companies and does not intend to do so The providers of finance have given notice in writing that they will seek repayment of the finance, both principal and interest, only to the extent that sufficient funds are generated by the securitised assets and they will not seek any form of recourse from the Group

The priority and amount of claims on the proceeds generated by the assets are determined in accordance with a strict priority of payments The Group is entitled to additional deferred consideration and/or residual income, in addition to the non-recourse consideration already received, depending upon the performance of the securitised assets

(b) Analysis of securitised mortgage balances

	Mortgages £000	*Mortgage loss provision £000*	*Total £000*
Group			
At beginning of the year	1,177,416	(7,805)	1,169,611
Net movement	413,211	(3,259)	409,952
At end of the year	1,590,627	(11,064)	1,579,563

Notes to the financial statements

at 30 November 2005

15. Mortgage loans – securitised balances (continued)

(c) Analysis of non recourse borrowings

	2005	*2004*
	£000	*£000*
Capital value of borrowings	1,672,818	1,359,880
Interest payable on borrowings	15,581	16,690
	1,688,399	1,376,570

16. Mortgage loans: amounts falling due within one and after one year

	Group	*Group*
	2005	*2004*
	£000	*£000*
Securitised mortgages	1,579,563	1,169,611
Non-securitised mortgages	501,593	378,637
	2,081,156	1,548,248
Amounts falling due within one year	419,691	373,195
Amounts falling due after one year	1,661,465	1,175,053
	2,081,156	1,548,248

17. Debtors: amounts falling due within one year

Group

	2005	*2004*
	£000	*£000*
Deferred origination costs	22,783	19,441
Deferred taxation	368	86
Corporation tax	–	3,466
Other debtors	26,457	19,944
Prepayments and accrued income	2,289	503
	51,897	43,440

Company

	2005	*2004*
	£000	*£000*
Amounts owed by related companies	368	368

Notes to the financial statements

at 30 November 2005

18. Creditors: amounts falling due within one year

Group

	2005	*2004*
	£000	*£000*
Loan facility	483,107	397,847
Loan finance	41,820	28,747
Bank overdraft	2,337	2,774
Social security and other taxes	266	224
Trade creditors	92	420
Other creditors	6,894	4,268
Corporation tax	2,181	–
Accruals and deferred income	6,006	3,479
Amounts owed to parent company	4,397	–
Finance lease	22	158
	547,122	437,917

Company

	2005	*2004*
	£000	*£000*
Amounts owed to related companies	315	301
Accruals and deferred income	(5)	9
	310	310

19. Creditors: amounts falling due after more than one year

	2005	*2004*
	£000	*£000*
Finance lease	18	40
Parent company loan	41,591	41,591
Residual Finance Companies Loan	37,173	27,384
	78,782	69,015

Notes to the financial statements

at 30 November 2005

20. Called up share capital

		2005	2004
		£	£
Authorised			
50,000	Deferred shares of 1p each	500	500
50,000	Ordinary shares of 10p each	5,000	5,000
124,963	A ordinary shares of 1p each	–	–
32,215	B ordinary shares of 1p each	–	–
10,001	C ordinary shares of 1p each	–	–
1,291	D ordinary shares of 10p each	–	–
450,000	X Ordinary shares of 1p each	4,500	4,500
		10,000	10,000

		2005	2004
		£	£
Issued			
16,868	Deferred shares of 1p each	169	169
30,638	Ordinary shares of 10p each	3,193	3,193
124,963	A ordinary shares of 1p each	–	–
27,214	B ordinary shares of 1p each	–	–
7,001	C ordinary shares of 1p each	–	–
1,291	D ordinary shares of 10p each	–	–
159,178	X Ordinary shares of 1p each	1,592	1,592
		4,954	4,954

On 5 May 2004, the existing issued and authorised share capital was redenominated whereby the Class A ordinary shares of 1p, the Class B ordinary shares of 1p and the Class C ordinary shares of 1p were each redenominated to Class X ordinary shares of 1p each Similarly, the Class D ordinary shares of 10p were denominated as ordinary shares of 10p each

On 5 May 2004, a resolution was passed to increase the Company's authorised share capital from £5,665 to £10,000

On 31 January 2006, the entire share capital of Preferred Holdings Limited was acquired by Resetfan Limited On 1 December 2006 ownership of Resetfan Limited was transferred to Mable Commercial Funding Limited

Notes to the financial statements

at 30 November 2005

21. Statement of movement on reserves

Group

	Share premium account £000	*Profit and loss account £000*	*Total £000*
Balance at 1 December 2004	490	22,605	23,095
Retained profit for the year	–	17,171	17,171
Balance at 30 November 2005	490	39,776	40,266

Company

	Share premium account £000	*Profit and loss account £000*	*Total £000*
Balance at 1 December 2004	490	(436)	54
Retained profit for the year	–	–	–
Balance at 30 November 2005	490	(436)	54

22. Reconciliation of movements in shareholders' funds

Group

	2005 £000	*2004 £000*
Profit for the financial year	17,171	12,012
Issue of shares (share premium)	–	–
Net addition to shareholders' funds	17,171	12,012
Opening shareholders' funds	23,100	11,088
Closing shareholders' funds	40,271	23,100

Notes to the financial statements

at 30 November 2005

22. Reconciliation of movements in shareholders' funds (continued)

Company

	2005 £000	2004 £000
Profit/(loss) for the financial year	–	(8)
Issue of shares (share premium)	–	–
Net increase/(decrease) to shareholders' funds	–	(8)
Opening shareholders' funds	59	67
Closing shareholders' funds	59	59

23. Operating lease commitments

The charge payable in the next year in respect of operating leases is as follows

	2005 £000	2004 £000
Land and buildings		
Leases terminating between 1 and 2 years	598	–
Leases terminating between 2 and 5 years	47	597
Leases terminating after more than 5 years	–	47
Other		
Leases terminating in less than 12 months	6	5
Leases terminating between 1 and 2 years	16	8
Leases terminating between 2 and 5 years	–	22

24. Cash flow statement

(a) Reconciliation of operating profit to net cash inflow from operating activities

	2005 £000	2004 £000
Operating profit after provision	24,791	12,066
Depreciation of fixed assets	2,025	1,005
Interest – loan facilities	37,855	20,641
Interest – mortgage backed loan notes	75,025	55,417
Interest – other	1,030	339
Amortisation of goodwill	425	390
Origination costs	(3,342)	(5,097)
Finance lease	(158)	(170)
Loan loss provision	2,008	2,355
Other debtors	(12,175)	(13 241)
Other creditors	(531)	23,974
Net cash inflow from operating activities	126 953	97,679

Notes to the financial statements

at 30 November 2005

24. Cash flow statement (continued)

(b) Analysis of cash flows for headings netted in the cash flow statement

	2005 £000	2004 £000
Returns on investments and servicing of finance		
Interest paid on mortgage backed floating rate notes	(75,025)	(55,417)
Interest paid on loan facilities and other interest	(38,885)	(20,980)
	(113,910)	(76,397)
Capital expenditure and financial investment		
Payments to acquire tangible fixed assets	1,530	1,462
Payments to acquire mortgages	534,916	525,933
	536,446	527,395
Financing		
Issue of ordinary shares	–	–
Issue of loan notes	312,938	817,899
Increase/(decrease) in bank facility	85,260	(107,676)
Increase in loan finance	22,862	39,184
Increase in loan from parent company	4,397	18,500
	425,457	767,907

(c) Analysis of net debt

	2004 £000	Cash flow £000	2005 £000
Cash in hand	308,873	(100,677)	208,196
Bank overdraft	(2,774)	437	(2,337)
	306,099	(100,240)	205,859
Parent company loan	(41,591)	(4,397)	(45,988)
Non recourse facilities	(1,359,880)	(312,938)	(1,672,818)
Other loan facilities	(454,176)	(107,964)	(562,140)
	(1,549,548)	(525,539)	(2,075,087)

Notes to the financial statements

at 30 November 2005

25. Financial instruments

As explained on page 3 the Group uses financial instruments in its normal course of business The following numerical analysis gives an indication of the significance of these instruments to the Group

(a) Interest rate risk profile of financial liabilities

	Total £000	*Total variable rate £000*	*Total fixed rate £000*	*Weighted average interest rate %*	*Weighted average time for which rate is fixed Years*
30 November 2005					
Interest rate and currency profile	2,321,602	2,321,602	–	–	–
30 November 2004					
Interest rate and currency profile	1,858,238	1,858,238	–	–	–

(b) Interest rate risk profile of financial assets

	Total £000	*Total variable rate £000*	*Total fixed rate £000*	*Weighted average interest rate %*	*Weighted average time for which rate is fixed Years*
30 November 2005					
Interest rate and currency profile	2,303,504	2,115,274	188,230	7 19	1 89
30 November 2004					
Interest rate and currency profile	1,868,759	1,858,739	10,020	7 14	1 46

All financial assets are denominated in pounds sterling

The rates of interest receivable and payable on variable rate financial instruments are set with reference to the London Interbank Offered Rate

Notes to the financial statements

at 30 November 2005

25. Financial instruments (continued)

(c) Foreign currency risk

With the exception of the mortgage backed loan notes in Preferred Residential Securities 6 PLC, Preferred Residential Securities 8 PLC, Preferred Residential Securities 05-1 PLC and Preferred Residential Securities 05-2 PLC all financial instruments are denominated in sterling The mortgage backed loan notes were issued in the following tranches in Preferred Residential Securities 6 PLC

GBP denominated mortgage backed loan notes due 2035 – Class A1 (Notional GBP 232,000,000)
EUR denominated mortgage backed loan notes due 2035 – Class A2 (Notional EUR 50,000,000)
GBP denominated mortgage backed loan notes due 2035 – Class M1 (Notional GBP 27,500,000)
EUR denominated mortgage backed loan notes due 2035 – Class M2 (Notional EUR 8,000,000)

The mortgage backed loan notes were issued in the following tranches in Preferred Residential Securities 8 PLC

GBP denominated mortgage backed loan notes due 2042 with detachable coupons due 2007 - Class A1a1 (Notional GBP 181,000,000)
GBP denominated mortgage backed loan notes due 2042 with detachable coupons due 2007 - Class A1a2 (Notional GBP 100,000,000)
USD denominated mortgage backed loan notes due 2042 – Class A1b (Notional USD 100,000,000)
EUR denominated mortgage backed loan notes due 2042 – Class A1e (Notional EUR 100,000,000)
GBP denominated mortgage backed loan notes due 2042 – Class B1a (Notional GBP 18,500,000)
EUR denominated mortgage backed loan notes due 2042 – Class B1c (Notional EUR 8,500,000)
GBP denominated mortgage backed loan notes due 2042 – Class C1a (Notional GBP 5,900,000)
EUR denominated mortgage backed loan notes due 2042 – Class C1c (Notional EUR 5,000,000)
GBP denominated mortgage backed loan notes due 2042 – Class D1a (Notional GBP 16,200,000)
EUR denominated mortgage backed loan notes due 2042 – Class D1e (Notional EUR 5,000,000)
GBP denominated mortgage backed loan notes due 2042 – Class E (Notional GBP 4,600,000)

The mortgage backed loan notes were issued in the following tranches in Preferred Residential Securities 05-1 PLC

EUR denominated mortgage backed loan notes due 2024 – Class A1a (Notional EUR 181 000,000)
GBP denominated mortgage backed loan notes due 2043 – Class A2c (Notional GBP 218,600,000)
EUR denominated mortgage backed loan notes due 2043 – Class B1a (Notional EUR 7,000,000)
GBP denominated mortgage backed loan notes due 2043 – Class B1c (Notional GBP 22,600,000)
GBP denominated mortgage backed loan notes due 2043 – Class C1c (Notional GBP 10,800,000)
GBP denominated mortgage backed loan notes due 2043 – Class D1c (Notional GBP 15,800,000)
GBP denominated mortgage backed loan notes due 2043 – Class E (Notional GBP 3,400,000)

The mortgage backed loan notes were issued in the following tranches in Preferred Residential Securities 05-2 PLC

USD denominated mortgage backed loan notes due 2028 – Class A1b (Notional USD 70,500,000)
GBP denominated mortgage backed loan notes due 2028 – Class A1c (Notional GBP 50,000,000)
EUR denominated mortgage backed loan notes due 2040 – Class A2a (Notional EUR 100,000,000)
GBP denominated mortgage backed loan notes due with detachable coupons due 2008 – Class A2c (Notional GBP 96,000,000)
EUR denominated mortgage backed loan notes due 2040 – Class B1a (Notional EUR 13,000,000)
GBP denominated mortgage backed loan notes due 2040 – Class B1c (Notional GBP 10,000,000)
EUR denominated mortgage backed loan notes due 2040 – Class C1a (Notional EUR 12,000,000)
GBP denominated mortgage backed loan notes due 2040 – Class C1c (Notional GBP 4,000,000)
GBP denominated mortgage backed loan notes due 2040 – Class D1c (Notional GBP 12,600,000)
GBP denominated mortgage backed loan notes due 2040 – Class DTc (Notional GBP 4,350,000)
GBP denominated mortgage backed loan notes due 2040 – Class E1c (Notional GBP 2,550,000)
GBP denominated mortgage backed loan notes due 2040 – Class ETc (Notional GBP 3,750,000)
GBP denominated mortgage backed loan notes due 2040 – Class FTc (Notional GBP 600,000)

Notes to the financial statements

at 30 November 2005

25. Financial instruments (continued)

(c) Foreign currency risk (continued)

A series of currency swaps has been entered into, in order to manage the Group's currency rate exposure in relation to non-sterling denominated loan notes At 30 November 2005 the notional value of swaps held was £347,179,877 (2004 – £177,037,964) and the unrecognised positive fair value was £707,678 (2004 – £666,537)

The Company has entered into an interest rate cap to hedge against interest rate exposure At 30 November 2005 the notional value of the cap was £112,000,000 (2004 – £nil) and the unrecognised (negative) fair value was £(13,509) (2004 – £nil)

(d) Fair value of financial instruments

	Book value 2005 £000	*Fair value 2005 £000*	*Book value 2004 £000*	*Fair value 2004 £000*
Non-securitised operations				
Cash and deposits	60,636	60,636	86,108	86,108
Mortgage loans	504,682	504,682	382,470	382,470
Loan facilities	491,807	491,807	397,847	397,847
Bank overdraft	2,337	2,337	2,774	2,774
Loan finance	147,968	147,968	56,131	56,131
Parent company loan			41,591	41,591
Loan notes	–	–	–	–
Securitised operations				
Mortgage loans	1,590,626	1,590,626	1,177,416	1,177,416
Cash and deposits	147,560	147,560	222,765	222,765
Mortgage Backed Loan Notes	1,679,490	1,679,490	1,359,880	1,359,880

26 Related party transactions

In accordance with Financial Reporting Standard No 8 "Related Party Transactions" paragraph 3(c), transactions with other group undertakings have not been disclosed in these financial statements

Amounts owed to the shareholders of Preferred Holdings Limited during the year are £41,590,378 (30 November 2004 – £41,590,378) and are included within creditors (note 19)

27 Contingent liability

Upon each loan sale, the Group issues a warranty that all mortgages being sold are compliant with various representations made in the Mortgage Sale Agreement contained in the Offer Circular These representations are made in respect of specific characteristics of the loans being sold such as the level of arrears existing at sale, the ratio of loan to property value and a description of the type of property acting as security for the loans In the event of any mortgages being included in the loan sale that do not meet the criteria specified in the representation made in the Mortgage Sale Agreement contained in the Offer Circular the Group is required to repurchase at par value those mortgages that do not meet the criteria

28. Parent company and ultimate controlling party

The Company's parent company is Lehman Brothers Holdings PLC The largest group in which the results of the Company are consolidated is that headed by Lehman Brothers Holdings Inc , incorporated in the United States of America The consolidated financial statements of this Group are available from 745 Seventh Avenue, New York, USA The smallest group in which they are consolidated is that headed by Lehman Brothers Spain Holdings Limited, registered in England and Wales