

Corporate Responsibility



The HBOS difference

HBOS is the UK's largest provider of mortgages, savings and new investment products. We have a relationship with two out of every five households in the UK.

About HBOS

HBOS has operations across the UK, Australia, Ireland, Europe and North America with 78% of profits generated in the UK. 22% of profits are generated outside the UK, up from 17% in 2006. The Executive Committee, led by the Chief Executive Andy Hornby

and consisting of all HBOS Executive Directors plus the Company Secretary & Group Counsel and the Group Risk Director, provides advice and support to the Chief Executive.

Full details of HBOS's structure and governance are available on pages 111 to 150 of the Annual Report and Accounts.

Key facts (tables)	2007	2006
Financial		
Profit before tax	£5,474m	£5,706m
Underlying earnings per share	106.1p*	100.5p
Dividend per share	48.9p	41.4p
Cost: income ratio	40.9%	41.0%
Return on Equity	19.7%	20.8%
Economic		
Tax on profit	£1,365m	£1,772m
Wages and salaries	£2,340m	£2,137m
Social security costs	£226m	£228m
Pension costs	£201m	£205m
Social impact		
Number of customers (approx.)	23m	23m
Number of employees	74,087	71,850
Total community investment	£55.2m	£44.2m
Number of times HBOS products appeared in best buy tables	3,912	3,317
Percentage of colleagues satisfied with opportunities to learn (sector average 49%)	67%	65%
Environmental		
UK CO2 emissions (tonnes)	53,577	56,743
Energy use per FTE (kWh)	7,269	7,822
Water consumption (m3) per FTE	8.9	9.2
	*Restated for the Rights Issue	



Included in the Sunday Times Best Green Companies



FTSE4Good
Included in the FTSE4Good Ethical Index.



Highest ranked UK bank in the Dow Jones Sustainability Index.



Included in the Global 100 Most Sustainable Corporations



Ranked Platinum in the Business in the Community Corporate Responsibility Index.



Awarded the Community Mark

Highlights Here are some of the highlights of 2007

Highest ranked UK bank in the Carbon Disclosure Project's Climate Leadership Index

1st
Highest scoring UK bank in the Carbon Disclosure Project

Highest ranked UK bank in the Dow Jones Sustainability Index

1st
Highest scoring UK bank in the Dow Jones Sustainability Index

Achieved more retail best buys than any major bank – over 3,900 appearances in best buy tables.

3,900
appearances in best buy tables

UK's leading savings provider helping over 15 million customers save for the future.

15m
savings customers

We lend £11.5 bn in mortgages in deprived areas of the UK.

£11.5 bn
mortgages in deprived areas

Income multiple of 2.8 across mortgage book, with average loan-to-value of 44%.

44%
average loan to value

First bank to launch a Christmas savings scheme for our social banking customers

1st
bank to launch Christmas Savings Scheme

Invested £55.2m in local communities.

£55.2m
invested in local communities

Reduced UK carbon emissions by 7% since 2006 and over 66% since 2004.

2/3
reduction in CO2 since 2004

One of only 2 UK banks to achieve the Business in the Community CommunityMark

1st
one of the first 21 companies awarded the Community Mark

UK's leading provider of mortgages to first time buyers - 35% of the first time buyers

35%
of first time buyers choose an HBOS mortgage

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Our strategy

What are the issues?

Corporate responsibility (CR) is integrated into our overall strategy, with an emphasis on highly competitive products.

Our Corporate Responsibility approach focuses on best serving the diverse interests of our key stakeholders. Understanding their views and concerns, about how we are growing the business, helps drive our strategy.

- **Shareholders** Creating value; governance; sustainability.
- **Customers** Responsible lending, marketing and advertising; accessibility; value and inclusiveness of products.
- **Colleagues** Remuneration; employment conditions; culture; diversity.
- **Environment** Climate change and carbon reduction; paper management; water management.
- **Community** Economic impact; national and local community programmes; dealing fairly with suppliers.

Our strategy is driven by stakeholder dialogue. The AA1 000 Assurance Standard helps us deliver this.

Strong governance

Our statement of business principles, The Way We Do Business, is our commitment to our stakeholders about the standards we aspire to deliver. We are the only major UK bank to directly underpin our statement with a clear and explicit set of Key Performance Indicators by which we manage our programme and which we report against year on year.

Our principles are also supported by a robust management and governance framework which ensures group-wide application of the principles. The management framework also provides a means of sharing best practice and driving progress throughout our business. This framework is set out on pages 43 to 44.

Our Key Performance Indicators

The Way We Do Business Key Performance Indicators (WWDB KPIs) provide our stakeholders with a clear and concise overview of our progress. Every month the biggest challenges and issues are escalated to HBOS's 50 most senior managers in regular reports. KPIs as a whole are reviewed annually by the HBOS Board and Executive Committee. The KPIs are set out in full on page *

Where can we do better?

What we committed	How we performed	Where we can do better
We will introduce a new comprehensive set of targets for reducing resource use.	We have introduced new three-year targets for energy, paper, water, waste, recycling and emissions	Ensure strong initiatives are in place to deliver against targets



Foreword Peter Cummings Our strategy is about making Corporate Responsibility integral to the way we do business

Our commitment

Over the past 12 months we have been operating in an environment of serious market turbulence. This has not, however, compromised our commitment to Corporate Responsibility. Indeed, it has served as a reminder of the importance of a company's character and behaviour towards customers and colleagues.

As a board, we are proud of the strength of our stakeholder relations, our colleagues' ability and commitment, and our processes for dealing with customers fairly.

Our performance last year

There were a number of highlights in 2007 achieved with the involvement of businesses across HBOS.

Our award winning dormant account campaign has reunited customers with £16.6m in forgotten accounts. We have installed 100 new free to use ATMs in disadvantaged areas and we were the only bank to launch a savings scheme specifically for our social banking customers. We are making this available to 70,000 customers this year.

Our corporate lending deals are subject to robust environmental and social risk assessments. Our profitability allows us to contribute to society in many positive ways, and in 2007 the UK Exchequer received £1.2bn in tax and NI from HBOS. We are one of the largest contributors of tax in the UK.

We provide all our colleagues with ongoing opportunities to learn and HBOS-U, launched in 2006 to help senior managers build on their skills, has been a great success. In 2008 HBOS-U will be extended to all our colleagues throughout the business.

Our approach

When we say we take CR seriously, we mean that it is integrated into the way we do business across the Group.

We put £55.2m back into the community last year. This supported projects ranging from financial inclusion and literacy to helping young people from disadvantaged backgrounds get more involved with sports and the arts.

But CR is more fundamental than this. It means that the Board of HBOS is satisfied that it is doing everything possible to ensure that every aspect of its business conforms to the highest standards of behaviour.

Our aims this year

I am delighted to be championing HBOS's CR strategy on behalf of the business. A number of very important steps are being taken during 2008.

Our Climate Change strategy continues to take centre stage. Paper reduction is an area we will improve and we will launch a green mortgage.

We will significantly improve consistency in the way CR risks and issues are managed in the supply chain. We will implement a rigorous model for managing CR through our supply chain, starting this year with our 50 highest impact suppliers.

I am delighted to be leading this strategy for the Group and I welcome any comments. An enlightened CR strategy must be at the heart of the way we do business.

Peter Cummings
Chief Executive, Corporate



2007 at a glance Here are some of 2007's biggest achievements.

Customers

- HBOS installed 100 new, fee-free ATMs last year in areas of need across Scotland and the North of England.
- £16.6m reunited through our dormant accounts campaign
- Launched the Bank of Scotland Entrepreneur Challenge, providing interest-free funding for the winning companies

Responsible lending

- 8 projects reviewed in line with Equator Principles

Financial inclusion

- Exceeded 15% target for new social bank accounts, opening 19.3% of all new social banking accounts
- 1st major bank to offer a Christmas Savings Account
- 16% of the banking market among ethnic minorities
- Announced two new credit union partnerships with Calderdale Credit Union and Rotherham Credit Union Development Agency (RCUDA)

Investor responsibility

- Insight Investment launched a unique in-depth assessment of how well FTSE 100 companies and Europe's largest companies are responding to climate change risks and opportunities. In a recent survey by FairPensions, Insight scored 83% for its work in the ethical investment sector.

Environment and climate change

- Green Miles successfully reduced growth in travel
- 100% recycled business cards rolled out
- Improved recycling facilities launched in our major employment sites.
- Emissions reduced by over two thirds since 2004.

Community

- HBOS invested £55.2m in communities across the UK in 2007, including support for financial inclusion, sponsorship of sports and arts for young people, and donations through the HBOS Foundation.
- Million £ Challenge HBOS colleagues raised over £3.6m for our Million £ Challenge charities: the British Heart Foundation, WRVS, Family Holiday Association, the RNLI and Age Action.
- Over 70,000 young people benefited last year from HBOS sponsorship of sports and arts projects in our heartlands of Yorkshire and Scotland. An estimated 65% of these young people were from socially disadvantaged areas.

Disclosure

- Became 1st bank to publish standalone, data-led Climate Change and Financial Inclusion Reports

Colleagues

- Colleague advocacy of our climate change programme increased to 56% from 24% in 2004.
- Over 10,000 colleagues volunteered in their communities in 2007.

Competing on value Our aim is to offer better value products and a better deal for customers.

Cost efficiency

HBOS's cost: income ratio 41% is one of the lowest of all the major UK banks. This gives us the ability to offer customers the lowest price, whilst generating the same returns for the business. This strategy has allowed us to challenge our competitors and grow our business both nationally and internationally.

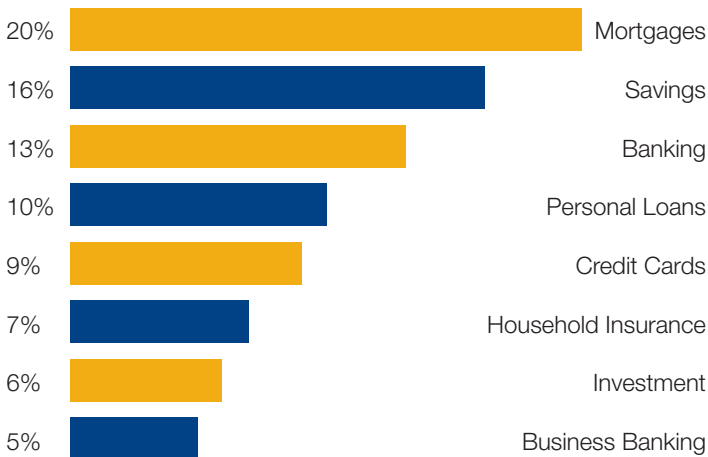
Cost / income ratio



Our products

Last year, we received over 3,900 mentions in the best buy tables, considerably more than any other big bank and an increase of 600 compared with the previous year. We have a relationship with two out of every five households in the UK. More detail can be found in our Annual Report and Accounts as at end 2007.

Estimated UK market shares as at end 2007



Customer Satisfaction

We aim to improve our customer ratings for satisfaction with our service compared to our banking peers. We achieve this by improving the day to day interactions between our colleagues and customers, by streamlining our processes and by introducing new services to meet customer needs. GfK NOP research indicated the proportion of customers who were delighted or completely satisfied with HBOS' service was 59% in 2007 – 3% ahead of the average for the Big Four banks and level with HBOS's 2006 performance (59%)

Mortgages

We are the UK's number one mortgage lender with a one in five share of the mortgage market. This means our mortgage lending stood at £235bn at the end of 2007. We are also the UK's largest single branded estate agent.

We offer a broad range of products to suit the circumstances of the majority of potential borrowers. Products focus predominantly on prime residential mortgages but also cover a range of more specialist needs. We are a major provider of mortgages to first time buyers. See the responsible lending section for more details.

Financial market dislocation

As a result of the dislocation in financial markets, most major lenders have increased their mortgage pricing during 2007 and into 2008. Wholesale money is significantly more expensive than it was prior to the dislocation in financial markets. Since banks and building societies obtain funding for mortgages from both customer deposits and wholesale markets, and such funding is more expensive, increased cost has had to be passed on to new customers by banks and building societies. This increased cost has had to be passed on to new customers by banks and building societies. This is just like any other commodity.

Existing customers are unaffected by changes to mortgage pricing. There are approximately 12 million mortgage customers in the UK. 6 million of these customers are on a variable or tracker rate and have benefited from successive Base Rate cuts. HBOS has passed on each Base Rate cut in full. The other 50 per cent of customers are on fixed rate products and, by definition, are insulated from the ups and downs of official interest rate policy.

Market dynamics

There has been a sharp contraction in the number of lenders actively offering mortgages. This contraction has come about because of the lack of wholesale funding and the very significant increase in its cost.

Lenders have a duty to ensure their mortgage underwriting is prudent and proportionate. It is not appropriate for the company to pick up the significant capacity deficit left by lenders who have departed from the market.

As the UK's largest lender, HBOS provides around one in five of all new mortgages in any one year. The company expects to do the same this year. Customers with a good deposit will continue to get a good deal.

Halifax was awarded Best Overall Lender at the Your Mortgage Awards 2007 for the sixth year running. Responsible lending is core to our strategy and our approach to assessing the amount an individual can afford to borrow is set out in the responsible lending section of this report.

Savings

We are the UK's leading savings provider helping 15 million customers save for the future. We offer a wide range of accounts including ISAs, regular savings accounts, and children's savings accounts.

Individual Savings Accounts (ISAs)

We continue to be the biggest provider of cash ISAs, and have a 21% share of ISA balances. In 2008/09 customers will be able to save even more tax-free, up to £3,600 in a cash ISA within an overall annual tax-free savings limit of £7,200.

Dormant Accounts

HBOS has taken the lead in reuniting customers with money they have left in 'forgotten' accounts. Through our "Funds Reunited" campaign and pro-active contact activity, we have so far reunited £16.6m of dormant balances with their rightful owners.

In 2007, the proactive searches concentrated on higher balance accounts. This year, HBOS is searching for remaining 'lost'

customers, with an average balance of just £273. In addition, we have registered details of unclaimed dormant accounts on the Unclaimed Assets Register.

HBOS's Funds Reunited campaign was congratulated during an Early Day Motion in October 2007, tabled by Christine McAfferty MP and signed by 69 members of Parliament

'this House... congratulates HBOS for launching a major campaign to reunite customers with dormant funds; recognises that this is the first such initiative to be launched by a bank; and calls on other banks and building societies to follow suit'.

The dormant accounts bill will receive its second reading in October. We expect the bill to receive royal assent by the end of the year and the scheme to be introduced in H1 2009. We will continue to do all we can between now and then to reunite customers with their accounts.

Banking

Our market share of new bank accounts, an area traditionally dominated by the Big Four, has continued to increase. This is driven by the value for money accounts we offer:

- We offer a 5.12% AER high interest bearing current account – 50 times more interest than HSBC, Nat West and Barclays that typically offer just 0.1%.
- Our Ultimate Reward Current Account is one of the best value packaged current accounts on the high street- offering up to £800 worth of benefits for a £10 per month fee, including worldwide travel insurance, mobile phone insurance, RAC breakdown cover and 1% extra interest on the Halifax Instant Saver account.
- HBOS received the 'Best Banking Provider' and 'Best Student Banking Provider' awards at the annual Your Money magazine awards.

Online banking

We are now one of the largest online banks in the UK with over 2.5 million customers regularly using the service. We have improved our website to make it easier for customers to manage their accounts, make transfers and set up standing orders. We have once again improved the navigation of the site to help customers find the answers to their questions more easily.

ABI Customer Impact Scheme

Along with other members of the Association of British Insurers (ABI) Customer Impact Scheme, we ensure that customers' needs are at the core of the way we do business by:

- Developing and promoting products and services which meet the needs of our customers.
- Providing customers with clear information and good service when they buy our products.
- Maintaining appropriate and effective relationships with our customers and providing them with a good service after they have bought a product.
- We deliver these commitments through the Way We Do Business. Beyond the main KPIs detailed in this report, further detail of our participation in the ABI scheme can be found at http://www.hbosplc.com/community/includes/Customer_Impact_Scheme.pdf

Credit cards

Our credit card offering is one of the most competitive on the market and is a best buy. We offer one of the best introductory offers available (0% for 12 months with a One Card) and have one of the lowest APRs around.

Charity credit cards

In 2007 customers using Halifax and Bank of Scotland credit cards helped raise over £933,500 for charities including Cancer Research UK, the RSPCA and SSPCA. The first time a customer uses a Halifax or Bank of Scotland credit card, their chosen charity receives a £20 donation from HBOS. After this, for every £100 the customer spends on the card, HBOS makes a further donation of 25p. HBOS entered the Guinness Book of Records in 2000 as the world's most successful charity card provider.

Home Insurance

Halifax Home Insurance (HHI) is now the third largest home insurer in the UK. We currently have a market share of 7%.

Value for money

By launching its 'Beat and Freeze' offer in May 2007, HHI gave new customers the opportunity to beat renewal quotes and freeze premiums for three years, providing certainty in a market place where premiums are rising following major weather events. HHI was ranked number one for its share of new home insurance policies by GfK in October 2007, up from fifth at the beginning of the year.

Fast response

A record 10,500 insurance claims were received in one day following severe storms in the UK in January 2007 compared to an average of 4,000. Overall, we registered 20,000 extra claims over a five day period with an average call answer rate of 2.25 minutes.

When devastating floods hit many parts of the UK last summer, Halifax Home Insurance was quick to respond, ensuring customers received face to face practical help from our teams of Personal Claims Consultants.

During the flooding, Halifax Home Insurance redeployed call handlers from other areas of the business to ensure there were enough fully trained people to manage call volumes. Halifax also established a dedicated team of flood claim handlers who regularly called customers to update them on the progress of their claim. The team of Personal Claims Consultants were able to take fully qualified building contractors to visit customers' homes, assess the damage and ensure repair work was underway as soon as possible.

Halifax Home Insurance's fast response to the flooding has meant that over half of customers who were forced out of their homes by the flooding were back in their homes in time for Christmas.

Investments

Halifax is still the only high street bank to offer a range of investment products and funds with no initial or exit charges – just a simple annual management charge. Other high street banks have initial charges as high as 4.5%, with annual charges the same as or slightly higher than Halifax.

ISA Provider	No upfront charges applied on all funds	Annual management charge	Average saving in charges with Halifax compared against major Big Four banks
Halifax	✓	✓	£171.25
RBS / Natwest	✗	✓	
Barclays	✗	✓	
Lloyds TSB	✗	✓	
HSBC	✗	✓	

* Source: Aequos Database (Defaqto), 25th February 2008 applied to an investment of over £4,000. Average saving is based on average initial and annual management charges across all the funds of all the other banks in the table.

Halifax came top against 31 Association of British Insurers (ABI) members in the 2007 Customer Impact Scheme survey when it came to ‘really caring about its customers’, ‘treating customers fairly’ and being ‘easy to do business with’.

Business banking

Bank of Scotland Business Banking provides a full range of products and services for small businesses with an annual turnover of up to £1 million. We bank over 170,000 SMEs across the UK, including over a third of all Scottish SMEs. We aim to attract new customers with innovative and value added products alongside first-class customer service levels.

With the launch of the Total Business Account, we became the first British bank to bring consumer pricing to the business banking

market offering base rate on credit balances – almost double the interest paid out by the Big Four banks.

For business customers switching to HBOS we offer free transactions and no overdraft arrangement fees for the first 12 months. Small business customers of the Big Four have saved nearly £7.5million on charges by switching to Bank of Scotland Business Banking over the course of 2007.

Bank of Scotland scooped two prestigious awards at this year’s Business Moneyfacts awards for the second consecutive year, including Best Overall Business Bank and Best Computer Bank. Bank of Scotland also won the Best Direct Business Bank award at the Your Money awards.

Addressing Climate Change

Halifax Web Saver Carbon Label

In collaboration with the Carbon Trust, Halifax was the first bank in Europe to carbon label a banking product – the Halifax Web Saver, one of the group’s most popular savings products with more than 1.1 million accounts. Halifax Web Saver’s Carbon Label shows people how much CO2 each account produces and commits Halifax to reducing these emissions within two years.

The carbon footprint calculated includes carbon emissions both from opening the account and the annual use of the account. To reduce the emissions produced by each account, we will be concentrating on improving the energy efficiency of ATM facilities, reducing the amount of paper we send to customers in relation to their accounts and improving how we deal with queries from customers.

The Smart Card

In association with smart cars we recently launched a ‘greener’ credit card. In addition to standard features such as a competitive interest rate and introductory 0% rate, the first time the card is used £20 is donated to the Woodland Trust. This donation is used to restore 100m2 of ancient woodland in the UK- an area equivalent to over 25 smart cars parked next to each other. In addition the plastic used in producing the credit card is carbon neutral, and customers are encouraged to switch to paperless statements when they receive the card.

Championing consumer interests

We are the only bank to proactively campaign and produce research on each of the following issues:

Empty homes

We are the only major bank to highlight the issue with an annual survey. Our latest report, published in December 2007 announced that there are nearly 290,000 private homes in England that had been empty for more than six months. House prices in areas with a high number of empty homes are on average 17% lower than average prices in the region. Likewise, average weekly earnings in areas with a high number of empty homes are, on average, 10% below regional averages, and 17% lower than English average earnings.

Inheritance tax

We have lobbied for the inheritance tax threshold to account for the significant rise in house prices over the last 12 years. In 2007 increases were announced to the IHT threshold. However, the increases do not fully account for the rise in house prices and we continue to campaign on this point.

Stamp duty

The threshold for stamp duty on homes has also not risen in line with house prices. Home buyers in 29% of Local Authorities (LAs) have a stamp duty bill equivalent to more than 20% of average annual gross earnings, compared to only 5% of LAs five years ago. We call on all political parties to raise the stamp duty thresholds to account fully for the rise in house prices over the past decade and to commit to raise the threshold in line with house price inflation in the future.

Public sector workers

To highlight the difficulties faced by key workers trying to buy a house Halifax publishes research on affordability for key public sector workers- nurses, teachers, police officers, fire fighters and paramedics. In 2007 we published research showing 70% of towns are now unaffordable for key public sector workers, up from 65% in 2006. In 2002 the average house price was unaffordable for all key workers in only 36% of towns.

Halifax House Price Index

The Halifax House Price Index is the UK's longest running house price series covering the whole country. As the UK's largest mortgage lender, the data provides a robust and representative sample of the entire UK market.

What do our stakeholders think?

Bank of Scotland named Best Computer Business Banking provider 2007 Moneyfacts Awards.

Bank of Scotland named Best Overall Business Bank 2007 Moneyfacts Awards.

Birmingham Midshires Solutions named Best Variable Rate Buy-To-Let Mortgage Provider 2007 Moneyfacts Awards.

"An Excellent Current Account from The Halifax" Halifax Ultimate Reward Current Account – Why we like it, Learnmoney.co.uk, February 2007.

HBOS named Best Banking Provider and Best Student Banking Provider at the 2007 Your Money magazine awards.

What we committed	How we performed	Where we can do better
We will introduce green products to help customers manage their environmental impacts, including a Green Mortgage in the second half of 2008. Work will start on this during 2007.	A Green Loan was piloted in 2007. The Green Mortgage has been developed and will be launched in Q4 2008	Launch the Green Mortgage in Q4 2008.
We will provide more help for people in rural communities by launching a new mobile branch service in Aberdeenshire to provide banking services to almost 20 local communities.	A new mobile branch was launched by First Minister Alex Salmond in Inverurie. The service operates five days a week, providing banking services to almost 20 local communities	Continue to review our branch network and expand our presence in the South of England.

Responsible lending Responsible lending is an important part of our strategy.

Our Strategy

Tighter market conditions have made our approach to lending even more important. However, our affordability calculation has always focused on lending appropriately to each individual customer.

Affordability

Our affordability model

Our affordability model for mortgages and other secured lending factors in an individual's total credit commitments, spending patterns and a conservative interest rate assumption. The average income multiple across our mortgage lending of 2.5 is little changed for over 15 years now. The average Loan to value across the book is just 44%.

The mortgage market has changed as a consequence of the liquidity crunch and we have changed with it. We are actively rewarding prudence in uncertain market conditions. It is a very simple concept – a better deal is offered in exchange for a bigger upfront commitment from the customer. In general someone putting down a 25% deposit will be able to get a better rate.

Our approach to unsecured lending (such as credit cards and personal loans) is very similar, with customers' ability to pay, credit references and other lending commitments taken into account.

Affordability in context

In the previous section we explained that the increased cost of borrowing has meant that lenders have had to increase their mortgage rates. It is important to keep this in context.

Affordability is still better than the late 1980s, early 1990s. The vast majority of borrowers are unaffected by the re-pricing of mortgages that has taken place this year. Existing customers on variable products have benefited from base rate cuts, while only a minority of all borrowers are coming off fixed rate deals in 2008.

The overwhelming majority of borrowers coming off fixed rate deals are expected to be able to absorb the increase in payments.

We do agree with the bank of England's assessment that approximately 5% of all households are very stretched as a result of a whole range of things – rising council tax, higher food prices, increased mortgage costs, etc. As we have always done, we try to

help those households that are our customers to manage their way through this difficult period.

Helping People On To The Housing Ladder

First time Buyers

Rising house prices have made it increasingly difficult for first time buyers (FTBs) to get onto the housing ladder. The number of first time buyers is at its lowest level since 1980.

HBOS research shows that the average house is now unaffordable for first time buyers in nearly all UK towns (96% in 2007 compared with just 30% in 2002).

HBOS is committed to helping first time buyers onto the housing ladder. We also have a dedicated mortgage offer for first time buyers. We are one of only two of the top ten lenders to do so.

We have a dedicated website, <http://buyingyourfirsthome.co.uk/>, to help first time buyers select a mortgage and pick their rate based on the additional services they need.

The Group continues to help more first time buyers than any other organisation. Our market share of the FTB market has increased from 22 per cent to 35 per cent, a 50 per cent increase, since the current market uncertainty began last summer.

In April 2008, Halifax became the first lender for many months to launch a number of new products aimed specifically at FTBs. These products build on the existing package of FTB support offered by Halifax.

Affordable housing schemes

HBOS has worked closely with the Government on affordable housing schemes and continues to do so. In particular we have been involved in the following:

We provide thousands of mortgages supporting shared ownership schemes for key workers, first time buyers and people on lower incomes.

Support for Housing Associations and Registered Social Landlords
HBOS is one of the largest lenders to social landlords in the country, with over £4.8bn committed to Registered Social Landlords

Open Market Homebuy

We were one of only four lenders working with the Government to deliver the original Open Market Home Buy scheme for first time buyers. Halifax was asked to provide an arrangement that included an equity stake. This has been replaced by the Government with a new scheme (see below) which we take part in.

Mychoicehomebuy

The borrower arranges an equity loan from one of the Housing Associations in the CHASE group. We will then recognise this stake and, subject to standard lending criteria, issue a mortgage offer based on the proportion of the property against which they are borrowing.

Mortgage Lending in Deprived Areas

Last year, HBOS published details of its mainstream mortgage lending in deprived areas for the first time.

In 2007 our mortgage lending in deprived areas was £11.5bn, 4.9% of our mortgage lending. Lending to customers living in deprived parts of the country can act as a catalyst for economic and social regeneration as well as being a key measure of financial inclusion.

A tailored approach

Personal Loans and credit

We offer customers market leading deals on personal loans and credit cards to help them make the most of these facilities. Our new credit card launched in 2008 offers 0% on balance transfers and new purchases for ten months. Our personal loan offers a three month break before repayments start to help customers

organise their finances. Interest rates are tailored to personal circumstances.

Corporate Lending

Lending to Housing Associations

Housing Associations are social businesses where any profit made is redistributed into the business. Many housing associations are registered under charitable rules, designed to provide homes at affordable rents. This creates access to housing for people who can't otherwise afford it. Our support helps housing associations provide rented accommodation or shared ownership schemes. The latter can help people onto the housing ladder.

We are one of the largest lenders to housing associations in the country.

	No of Customers- November 2007	Amount committed
England	150	£4,506m
Scotland	62	£289m
Wales	9	£95m
Total	221	£4,889m

Yorkshire Scotland Rest of UK Total

	Yorkshire	Scotland	Rest of UK	Total
Total Mortgages (£m)	17,030	18,343	198,786	234,159
Mortgages in Deprived Areas (£m)	785	134	10,647	11,566

Banking small businesses in deprived areas: a year on

We acknowledged the need to improve our support for small businesses in deprived areas and we have made good progress.

We currently have 6,785 business accounts in deprived areas, an increase of nearly 300 accounts since last year.

4.08% of our business banking accounts are held in deprived areas; compared to an industry average of 4.8%. However, we lend more money to businesses in deprived areas than the industry average. Businesses in deprived areas benefited from 4.14% of our total lending in 2007, compared to an industry average of 3.78%.

SME Funding Options

We offer SMEs a full range of funding options for their business. These range from the innovative 'business banking offset' loan (which uses the interest from a business current account to reduce the loan term or repayments) to asset finance and competitive overdrafts.

SMEs often struggle to collect invoiced payments for goods and services. This can be one of the main causes of financial difficulty for small companies. We offer SMEs a cash flow finance scheme where we manage the collection of invoices on behalf of SMEs. This allows small companies to improve their cash flow and spend time managing their business, rather than chasing payments.

Environmental and social issues in lending to business

We have detailed processes to manage environmental and social risks in our corporate lending. All corporate lending deals are subject to an environmental and social risk review, with higher risk projects subject to closer and more senior scrutiny. Colleagues are provided with tools with which to assess the risk and we have put in place stronger reporting and monitoring systems. This framework has been supported by in depth training on the Equator Principles for 40 specialists across our Corporate division.

Environmental policy

Our Corporate division's new environmental policy covers both direct impacts and the indirect impacts arising through our business activity. The policy helps ensure consistency in the way environmental risks are assessed as part of the credit process within the Corporate division.

The policy is supported by an Environmental Procedures Guide and

Lenders Guide to Environmental Risk Management. These guides integrate environmental issues into our credit applications and ensure the ongoing management of environmental risks.

10 'Carbon catalysts' have been appointed in Corporate's Specialised Industry Finance team to help further improve carbon performance in the division.

Equator Principles

Project finance is a relatively small part of our Corporate business, representing under a 10th of Corporate lending. We have nonetheless adopted the Equator Principles to demonstrate commitment to addressing the environmental and social impacts of our business operations. This year we provide detailed data on our Equator risk reviews for the first time.

Number of projects receiving EP review at marketing stage/appraisal and fully funded or executed:

One EP project has been progressed, a category C infrastructure project in Europe.

EP Category (A- high risk, B- medium risk, C- low risk)	Projects reviewed	Projects fully funded or executed	Projects not progressed	Projects work in progress
A	0	0	0	0
B	0	0	0	0
C	2	1	1	0
Pre- categorisation	1	0	0	1
Transaction reviewed but outside scope of EP	5	0	5	0
TOTAL PROJECTS REVIEWED	8	1	6	1

	Number in deprived areas (HBOS)		Percentage in deprived areas (HBOS)		Industry average: % in deprived areas	
	2006	2007	2006	2007	2006	2007
Business banking accounts	6,500	6,785	3.82%	4.08%	4.84%	4.80%
Accounts in credit	5,386	5,203	3.69%	3.74%	4.85%	4.94%
Accounts with an overdraft limit	1,332	1,839	3.73%	4.52%	3.68%	3.39%
Business deposit accounts	2,262	2,231	3.51%	3.64%	4.68%	4.65%
Loans	208	288	2.32%	3.04%	4.16%	3.53%

Support For Customers In Financial Difficulty

The Banking code and the Business Banking Code

HBOS follows the Banking Code and the Business Banking Code, which set out standards for banks and building societies to follow in dealing with individual and business customers.

These codes include a commitment to treat customers all customers fairly and reasonably, give clear information on products and services and deal with cases of financial difficulty sympathetically and positively. The former has recently been strengthened and now includes a commitment to proactively review whether a customer is potentially vulnerable

What does HBOS do to help customers in difficulty?

When a borrower is experiencing financial difficulty we recommend that they seek independent advice, through such agencies as Citizens Advice. There is a range of possible arrangements we come to with borrowers to help them manage their difficulties including:

- Extending the term of the mortgage
- Changing the date on which payment is expected (e.g. to better time with salary payments)
- Switching between interest only and capital loans
- Payment arrangements (for example reducing or suspending payments for a period to get through a temporary period of hardship such as a job loss).
- Treating arrears as part of the original debt and repaying them over the remaining period of the loan.
- Repossession is always the last resort (it is very costly for providers) and only ever the result of a long process in which we work very closely with the borrower and the courts

The HBOS Money Management Unit

HBOS has a specific team, the Money Management Unit, to identify borrowers in distress, in some cases before they even realise it themselves.

We seek to identify customers up to nine months in advance of any problems. Every customer who calls is offered a financial 'healthcheck' over the phone to explore ways of cutting expenditure such as utility bills, mobile phone etc, maximising their income and helping them to budget more effectively.

Money Management offers bespoke help as well as working in partnership with a range of organisations to provide customers external expertise, offering specialist advice and debt solutions. Feedback from both the Banking Code Standards Board and the FSA has been very positive.

Money Management are expanding the channels through which customers can access the service – the branch network and regional contact centres already have the ability to transfer a customer seeking help directly. Halifax and Bank of Scotland websites now clearly signpost customers looking for help in managing their money to the team and an online budget calculator is available.

What Do Our Stakeholders Think

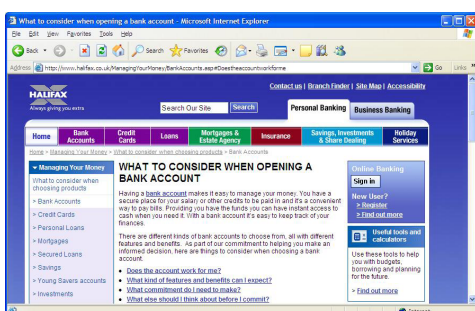
Halifax named 'Best Overall Lender' for the 6th year running in the 2007 Your Mortgage Awards

HBOS finalist in 'Most Responsible Customer Acquisition Strategy' in 2008 Credit Card Awards'

Bank of Scotland named 'Best overall Business Bank' in the Business Moneyfacts Awards 2008



Halifax online guide to bank accounts



Where We Can Do Better

What we recommended	How we delivered	Where we can do better
Develop and grow the money management unit	<p>We have expanded the channels through which customers can access the unit to include the website and branch network.</p> <p>Outbound call volumes are increasing – 20,000 were made in January 2008 alone.</p>	<p>We will look at opportunities to include secured as well as unsecured financial commitments in our 'horizon scanning' of our customers' financial health.</p> <p>We will look at opportunities to expand the range of possible solutions offered to customers in financial difficulty</p>
Increase our provision of clear easy to understand information	We have introduced 'managing your money' pages on our web site and worked with the FSA to pilot the Moneymade clear guides.	We will introduce summary boxes on bank account statements
Report the number of projects reviewed according to the Equator Principles and expand Equator Principles training	Equator principles data is reported in this report and in our Climate Change report.	Broaden our wider reporting on social and environmental risk in our lending portfolio

Financial Inclusion

Financial Inclusion has long been integral to our business strategy. It is about driving business growth as well as ensuring we deliver key social responsibilities.

Our Strategy

We are the only bank to produce a separate financial inclusion report containing detailed data and information on our programme. Our latest report can be viewed at http://www.hbosplc.com/community/financial_inclusion.asp. We have a number of specific inclusion and financial literacy objectives. These include:

- Increasing participation in personal banking
- Increasing participation in savings and asset ownership (such as housing)
- Increasing the availability of small amounts of credit

On The High Street

Unlike some banks we have expanded our network over the last few years. By the end of December 2007, 19 new branches were already open for business. The new branches will be concentrated in the South as we expand our presence outside our heartlands in Scotland and the North.

Mobile branches

In 2007 Bank of Scotland opened a new mobile branch in Inverurie, taking the number of mobile branches in the fleet to seven. The mobile branches provide a full banking service to some of the most remote areas in Scotland. Covering a variety of villages as well as schools, retirement homes, community groups and worksites, the vans also visit the homes of disabled customers.

Telephones

In 2007 we expanded dedicated customer telephone lines to enable customers in all our UK branches to call their local branch directly. The initiative was a big success, with x calls made directly to branches in 2007.

Parents

Halifax was voted Most Parent Friendly Bank for the fourth year running in the 2007 Tommy's Parent Friendly Awards. The awards credit companies that are taking parents' needs into

consideration and helping to make their lives less stressful. In the same awards, Halifax was named Best Children's Savings Account Provider for the second year running.

Disabled customers

HBOS is committed to providing easy access to our branches, with over 95% of branches being accessible to disabled users with features such as ramps, lifts and modified counters for wheelchair users, and induction loops for customers with hearing impairments. Upgrading the remaining branches is difficult due to planning constraints and building unsuitability – however we will investigate all reasonable steps to meet a customer's access needs. We also offer visually impaired customers the option to receive communications in Braille, audio or large format.

Diverse customers

We recently conducted a review of our retail banking provision for customers from different nationalities and ethnic groups. Our share of the market among ethnic minorities is 16%. We publish product information in more languages than ever before, including Gujarati, Hindi, Punjabi, Urdu and Welsh. Posters in Polish, Punjabi and Welsh have been trialled in branches in communities where a high concentration of residents speak these languages. In 2008 we will begin new local recruitment initiatives to further reflect customer needs in local communities.

Social Banking

Social banking accounts offer basic money transmission facilities such as direct debits and standing orders but do not provide an overdraft credit facility. HBOS was the first bank to offer a social banking service to its customers, through the Cardcash account, first launched in 1983.

Bank Accounts	HBoS All No. Accts Dec-07	HBoS Deprived Areas % of all Dec-07	HBoS Deprived Areas No. Accts - Dec-07
Current Accounts	5,800,129	5,800,129	3.97%
Social Bank Accounts			
Cardcash	3,389,628	3,389,628	7.44%
EasyCash	281,972	281,972	10.96%
Total Social Bank Accounts	3,671,600	3,671,600	7.72%
Total Bank Accounts	9,471,729	9,471,729	5.42%

Our share of new business

In 2007, we became the only major high street bank to publish a target for our share of new social banking accounts - 15%. We exceeded this, opening over 19% of new accounts. We believe this is the highest share of new business taken by any high street bank.

Social banking in deprived areas

10.96% of our Easycash accounts are held by customers living in the 5% most deprived areas of the UK. As a whole HBOS has over 510,000 account holders in deprived areas.

Scotland and Yorkshire account for 16.9% of the UK's population and 23.6% of our social banking accounts (14.4 % of our social banking accounts are held by customers in Scotland and 9.2% in Yorkshire). The table below illustrates the number of our social banking accounts held in deprived areas according to geographical and Financial ACORN categorisation.

	Yorkshire	Scotland	Rest of UK	Total
Total Bank Accounts	954,292	1,656,428	6,861,009	9,471,729
Total Social Bank Accounts	337,216	530,398	2,803,986	3,671,600
Social Bank Accounts in Financial Acorn groups I,J,K	168,281	281,401	1,224,680	1,674,362
Social Bank Accounts in Deprived Areas	23,206	11,162	248,874	283,242

The ACORN classification is a means of classifying areas according to Census characteristics and in order of affluence. ACORN groups I,J and K are the most deprived.

Easycash

Social bank accounts do not have overdraft facilities. However, in 2007 HBOS's social banking account, Easycash was improved via the introduction of a 'buffer zone', meaning that customers will not incur charges if direct debits or standing orders take customers beyond their balance by up to £10.

Our Easycash customers also receive a Visa Electron debit card. The Visa Electron can be used to pay for goods in shops and online, and can only be used if there are sufficient funds in the account, so there is no risk of going into overdraft. Not all banks provide this facility.

Post Office access

The Post Office is a competitor in offering its own financial products such as insurance, credit cards and loans. However, to help our social banking customer access their money easily we pay a premium to the Post Office to allow our Easycash Social Banking customers to access their accounts over Post Office counters. All Easycash customers have this facility.

Of the 100 new free ATMs we have installed across our Yorkshire and Scottish heartlands, we have installed machines in 9 Post Offices-including one at threat of closure, contributing to their ongoing sustainability by attracting customers to the Post Offices. The Post Office has an ATM agreement with Bank of Ireland, which limits our ability to work further with the Post Office on ATMs.

Post Office Card Account (POCA)

The POCA is a basic account currently run by the Post Office that allows state benefits to be paid directly into individual accounts. Unlike social banking accounts the POCA does not allow deposits or direct debits, but account holders can withdraw their benefits over the counter at any Post Office branch. HBOS has invested significantly in POCA which is scheduled to run until 2010.

Simplifying our social banking offering

Since 2005, we have made Cardcash available only to 16 and 17 year olds as our "Youth Account". All HBOS social bank account openings since have been Easycash accounts. We are now simplifying our account structure even further.

During the first half of 2008, 200,000 Cardcash customers were moved to an Easycash account. These customers will have the same facilities as Cardcash with the added benefit of Post Office access. They will also benefit from a £10 buffer zone. On average, these customers will have an income of around £350 per month and may live in an area identified by the Government as one of social exclusion.

The remaining (and larger) group of Cardcash customers are those for whom a Halifax Current Account is appropriate. The Halifax Current Account provides customers with a fully featured bank account. If they wish, customers may apply for an overdraft. This will be provided if appropriate

We have written to all of our Cardcash customers, explaining what the changes mean. In every case, customers will get a better deal. Customers will keep the same sort code and account number and they will not need to make any changes to salary payments, direct debits or standing orders.

Savings and asset ownership

Regular saving enhances long-term independence and opportunity by providing a pool of assets to draw on during periods of financial difficulty. It provides individuals with a way of taking personal responsibility for their future finances and increases familiarity with banking.

As the UK's largest liquid savings provider, we aim to make savings as accessible as possible to those who have not previously had access

Promoting savings to social banking customers

In May 2007 Halifax became the first major UK bank to offer a tailor

made Christmas Savings Account. The account was offered to 10,000 social banking customers. It could be opened with just £5 and funded with a minimum of £5 per month.

In April 2008, the account was offered to 70,000 customers. It will be offered to a further 70,000 customers each year. Once again, customers will have the peace of mind that the Halifax stands behind this product. Customers' savings balances will also be protected in full under the Financial Services Compensation Scheme. At the end of the savings period, i.e. October, customers will be able to take their savings in the form of either cash or high street vouchers. The account will allow payments up until 31 October. No withdrawals will be allowed before maturity on this date. If customers do wish to withdraw their money, their funds will be returned to the customers' Easycash account.

	Yorkshire	Scotland	Rest of UK	Total
Number of social banking customers in deprived areas holding a savings account 2007	7,333	3,471	60,348	71,152
Proportion of social banking customers in deprived areas holding a savings account 2007	32%	31%	25%	26%

The Saving Gateway

Halifax is the only financial institution to have piloted the Saving Gateway with the Government. The Saving Gateway pilots, which drew to a close last year, aimed to encourage saving by those on low incomes by providing matched funding from the Treasury. 23,000 accounts were opened.

The independent evaluation of the pilots, published in May 2007 found that the pilots had encouraged saving among those on low incomes and is in consultation on further rollout. In the budget 2008, the government confirmed the Gateway will be rolled out nationally from 2010. The budget report highlighted HBOS's role in piloting the initiative. We welcome the government's announcement. We aim to participate, subject to a panel of providers being identified.

Credit and micro finance

We work with a broad range of organisations, including Credit Unions, Community Development Finance Institutions (CDFIs), social enterprises and charities who provide small levels of credit to individuals or small organisations. Our total lending to these organisations stood at £110m in 2007.

Credit Unions

One of our major commitments in 2007 was to develop and implement a group wide approach to Credit Unions. We are some way into this now. We lend to 30 credit unions. We have established unique agreements with two Credit Unions, Calderdale Credit Union and Rotherham Credit Union Development Agency (RCUDA). For the next five years, free of charge, these Credit

Unions will be using our award-winning iSITE facility to set up hundreds of accounts for their members. This technology should help build the capacity of the CUs and the services they are able to provide local communities.

Case study

RCUDA: supports four local Credit Unions in South Yorkshire and has assumed lead responsibility for inaugural Financial Inclusion Strategy for Rotherham. There are 260,000 residents in the Borough of Rotherham.

Calderdale Credit Union: operates within Calderdale in West Yorkshire and has a population of 193,400. Almost half the local people live in Halifax. Other towns are Brighouse, Elland, Hebden Bridge, Sowerby Bridge and Todmorden.

Community Development Finance Institutions

We are the largest lender to CDFIs in the UK. Our total lending to this sector stands at £6.85m. The CDFI sector is new and emerging in the UK. Already it has financed around 10,000 businesses, created 10,000 jobs and sustained 85,000 more. CDFIs aim to improve the lives of financially excluded individuals and help develop and sustain grassroots regeneration. In the case of the voluntary and community sector, these institutions can be a valuable source of financial support for developing income generating activities.

What we recommended	How we performed	Where we can do better
We will maintain and build upon our position as the biggest provider of social banking accounts in the UK - aiming to grow our share of new accounts to 15% in 2007.	We opened over 19% of new social banking accounts in 2007.	We will maintain our 15% target for new social banking accounts in 2008.
We will develop and implement a Group-wide approach to credit unions and the micro-credit sector.	We have established new relationships with Calderdale and Rotherham Credit Unions, working to provide them with award-winning client banking service iSite.	We will seek to build on our work with credit unions where possible.
We will lead on disclosure through our annual financial inclusion report.	We remain the only major UK bank to produce an annual, data-driven financial inclusion report disclosing lending in deprived areas and to the voluntary sector	We will continue to provide leading disclosure on our lending in deprived areas and to the voluntary sector.

Financial understanding and literacy Responsible lending is underscored by consumers' ability to understand what they are buying .

Ensuring our literature is clear

In 2005 HBOS became the first card issuer to provide summary boxes on credit card statements, a move praised at the time by the Treasury Select Committee as being 'essential in ensuring consumers are kept informed'.

Summary boxes précis key product information that customers should understand when they purchase a product. We have since extended the use of summary boxes to include credit card cheques, payment protection insurance, marketing literature and estate agency contracts.

Helping our customers understand our products

We work very closely with the FSA and Government to help improve financial capability cross the whole of the UK.

Through our Halifax and Bank of Scotland websites we support consumer understanding. Our Managing Your Money pages give help and guidance to consumers, for example, explaining financial jargon and providing easy to use online calculators.

This approach is mirrored in our front of house branch literature. We are the only major UK bank to work with the FSA to pilot their MoneyMadeClear guides, making these available through selected branches to test whether consumers will use them.

The range of guides for each branch has been carefully selected in consultation with the branch team to reflect the customer base in that area, and have been displayed in Money Made Clear branded stands in prominent positions in the branches.

Support via the FSA levy

The FSA financial capability strategy is financed through a levy on the financial sector. The portion of this levy which is dedicated to financial capability was around £10m in 2006, increasing to £17m in

2007/8. Around £69m will be spent over the remaining three years of the FSA's current programme.

Helping our colleagues

Last year, HBOS established a Colleague Financial Awareness team who deliver a programme of financial education seminars for colleagues. Each seminar was specially designed to deal with a different aspect of financial planning and provides an opportunity for colleagues to ask experts questions relating to their own individual circumstances.

Helping vulnerable people through the HBOS Foundation

When people are in a vulnerable position they may prefer to get money advice from organisations with whom they are already very familiar. Money advice and financial literacy have therefore been key themes of the HBOS Foundation since it was formed in 2002 investing nearly £3 million in financial literacy projects with partners such as National Debtline, NCH and RNID.

The HBOS Foundation is a registered charity that makes grants to charities. The projects supported are aimed at some of the most vulnerable people in society who may be excluded from mainstream financial literacy support, like single mothers, children leaving care, refugees, the elderly, ex-offenders and the homeless.

In addition to cash grants, the Foundation offers the expertise of HBOS colleagues. For example, the Foundation is working with the charity 'Refuge' to develop a money advice programme for victims of domestic violence. This is delivered alongside other educational programmes that focus on building independence and cover subjects such as careers and education.

More information on the work of the HBOS Foundation is provided in the community section of this report.

What we recommended	How we performed	Where we can do better
We will launch a major financial literacy programme aimed at people at risk of financial exclusion in deprived areas	We are funding a number of new financial literacy programmes aimed at helping vulnerable group, including working with the Terence Higgins Trust, Citizens Advice & YouthNet, Age Concern, FISY and the Refugee Council.	We will develop innovative programmes aimed at additional vulnerable groups such as under-supported young people.
We will lobby the Government and the money advice charities for a clearer and more streamlined approach to money advice.	We responded to the call for evidence for the Thoresen Review on Generic Financial Advice.	We will continue our dialogue with both Government and money advice agendas.

Investor responsibility

On behalf of our clients we engage with companies on environmental, social and governance risk to ensure the £109bn of clients' funds we manage are invested responsibly.

Our strategy

Insight Investment, HBOS's asset management business, has a strong track record of engaging with companies to upgrade their governance and management practices. Our investment process, on behalf of our clients, explicitly takes into account issues such as board structure, climate change, human rights, and good governance.

The single most important motivation for Insight's commitment to responsible investment is to protect and enhance our clients' financial returns. We firmly believe that poor governance practices and mismanagement of social and environmental risks can have significant impacts on companies' financial performance and, thus, investment returns. Conversely, companies with good governance practices, good stakeholder relationships and proactive management of social and environmental risks should be better long-term investments.

Integration

Corporate governance and corporate responsibility issues into our investment decisions. This includes research into sector specific issues including nanotechnology, consumer health, water management, alternative energy, and waste management.

Governance activism, engagement and voting

We engaged with 285 companies in total during 2007.

We engaged with companies 138 times on corporate governance issues such as succession planning, strategy, financing and incentives. We also covered many other governance issues in our wider meetings with companies, and carried out our commitment to vote on all resolutions at Annual General Meetings and Extraordinary General Meetings. During the year, we voted on a total of 8,884 resolutions at 911 company meetings.

Summary of voting activity 2006

We engaged a total of 348 times with companies on 12 different topics relating to corporate responsibility – ranging from climate change to human rights, chemicals and obesity.

All engagement on corporate responsibility and corporate governance issues, 2007.

Corporate governance

Annual General Meeting (AGM)	2
Capital structure	14
Directors' remuneration	65
Chairmen meetings	54
Take-overs	3
Sub-total	138

Corporate responsibility	
Access to medicines	1
Climate change	139
Corporate responsibility, strategy, governance, reporting and management	38
Customer-related risks	30
Doing business in difficult countries	24
Health and safety	1
Human rights	6
New and emerging technologies	22
Principles for Responsible Investment	24
Responsible alcohol retailing	9
Supply-chain issues	28
Sustainable homes	26
Sub-total	348
Total	486

UN Principles for Responsible Investment

Insight has been a member of the UN Principles for Responsible Investment (PRI) since its launch in 2006. Early in 2007, we completed the member questionnaire to assess compliance with the Principles; the summary results are available on the PRI website. Insight's summary and commentary on the findings of this first assessment are available at:

http://www.insightinvestment.com/Documents/responsibility/briefings/insights_pri_capability_one_year_on.pdf.

In July 2007, we attended the first annual members' meeting where we presented our work on investment integration, and, later in the year, we joined the Assessment Working Group, the body that guides the development of the member assessment questionnaire and the process for evaluating the responses and publishing the results. We also posted to, and used, the Engagement Clearinghouse during the year.

Case study

Biofuels

High fuel prices, energy security fears and concerns about climate change have focused global attention on biofuels. Tax breaks and subsidies to make them more competitive helped the sector to grow rapidly. By mid- to late-2006, however, there were signs of trouble: biofuels ignited a fierce 'food versus fuel' debate; some biofuels were implicated in causing significant environmental damage; and the CO2 'footprints' of some biofuels were determined to be not as small as once purported.

Throughout 2007, we closely tracked developments in the sector including changes in regulation, feedstock prices, capacity and production volume, and end-product prices. We believe the longer-term prospects for 'first-generation' biofuels remain uncertain. Thus, we sought to identify potential investment opportunities along the value chain, as well as those exposed to alternative and second-generation biofuels. For example, we added to our holdings in Novozymes, a producer of enzymes used in the conversion of grains such as corn, barley, wheat and rye into bioethanol. The company is also at the forefront of research into enzymes suitable for the production of bioethanol from cellulosic feedstocks – a 'second-generation' biofuel that looks to be five to ten years from commercialisation.

Case study

Light-emitting diodes (LEDs)

The global lighting industry is going experiencing a significant structural change, due in large part to concerns about climate change. Conventional incandescent light bulbs (which are extremely energy inefficient) are being replaced with more 'environmentally friendly' alternatives, namely compact fluorescent lights (CFLs) and light-emitting diodes (LEDs). This shift is being driven by both voluntary Initiatives and regulation.

In 2007, we researched the global CFL and LED markets, to keep abreast of global regulatory changes and voluntary corporate initiatives that might affect them, and to identify companies involved with these technologies.

While CFLs are benefiting from the initial switchover, LEDs are poised to significantly benefit from general lighting applications in the near future, as well as from mobile phone, automobile, traffic signal and signage, and liquid crystal display (LCD) applications in the near and mid terms.

As a result of our analysis, the RI team identified approximately 50 stocks with some level of exposure to the LED theme and further identified the most highly leveraged to it (with over 50% of their revenues LED-related).

Case study

Brixton plc: Bonuses for executive directors

In April 2007, the Chairman of Brixton's Remuneration Committee wrote to us to highlight the Remuneration Committee's decision to provide two executive directors with a bonus in excess of the normal 100% of salary maximum.

Following our review of the company's Remuneration Report, we concluded that bonus payments were above the normal limit. Our view was that shareholders would normally only expect maximum bonuses to be paid for exceptional

performance. However, the company did not achieve exceptional performance during the year.

Insight and other investors discussed the additional bonuses at a meeting held at the ABI. We accepted the argument that recruitment and retention of executives within the property market was difficult in view of competition for talent from outside the quoted company arena. While we were not happy with the company's approach, we decided to support the proposal, although 9% of shareholders voted against it.

Our approach

A founding signatory and member of the steering committee of the United Nations Principles for Responsible Investment, Insight delivers on its responsible investment commitments by:

- Incorporating environmental, social and governance issues into investment analysis and decision-making processes.
- Being active owners and incorporating ESG issues into ownership policies and practices.
- Seeking appropriate disclosure on ESG issues by the entities in which we invest.
- Promoting acceptance and implementation of the Principles within the investment industry.
- Working together to enhance our effectiveness in implementing the Principles.
- Reporting on our activities and progress towards implementing the Principles.

Governance activism, engagement and voting

During 2007, Insight played an active role in important national and international initiatives that promote responsible investment; in 2007 we participated actively in 16 such initiatives, including the UN Principles for Responsible Investment, the Association of British Insurers (ABI), the UK Social Investment Forum (UKSIF) and the Institutional Investors Group on Climate Change (IIGCC); We raised corporate governance issues on 138 occasions, and environmental and social issues on 348 occasions;

Where we can do better

What we recommended	How we performed	Where we can do better
Deepen investment research with a particular emphasis on analysing large UK and European companies' management of climate change related risks.	Insight has conducted wide-ranging research from the impact of aviation on the EU ETS to the extent to which UK water companies have considered climate change risks. Insight made over 75 stock related to ESG issues researched.	Continue to deepen investment research into management of ESG risks
Strengthen engagement with a focus on encouraging companies to achieve and maintain high standards of corporate governance and corporate responsibility.	Insight engaged with 285 companies on 17 corporate responsibility and corporate governance issues.	Continue to encourage companies to maintain high standards of corporate governance and corporate responsibility
Promote increased disclosure on environmental, social and governance risk and stronger goals in collaborative initiatives	Insight publishes detailed data on its engagement and voting practices on its investor responsibility website	Continue to promote increased disclosure on ESG risks.



Risk and regulation The principles based regulation governing the UK financial services sector is a strong driver for us to ensure our products and services are transparent and ultimately help consumers choose the right financial services for their needs.

Climate change research

Climate change is a major focus of our work. The specific investment research we conducted in 2007 on climate change, energy policy and related issues included:

- An updated analysis of the exposure of European electricity utilities to climate change-related regulation for the period 2008-2012 and beyond 2012.
- An analysis of energy supply/demand balances in the major European electricity markets and the potential tensions between climate change and energy policy at the national and European levels.
- An assessment of the implications of including aviation in the EU ETS.
- An initial analysis of the EU's proposals for reducing GHG emissions from motor vehicles. Our focus was implications for the manufacturers' R&D and capital costs and the potential penalties they will incur if they do not reduce emissions in line with EU targets.
- A review of the implications of the US Energy Independence and Security Act of 2007 – intended to decrease the US's dependence on foreign oil and reduce its CO2 emissions – which provides strong incentives for biofuels, proposes better fuel efficiency for cars and light trucks, increases the energy efficiency of light bulbs and sets improved energy efficiency standards for electrical appliances and consumer electronic products.
- An assessment of the extent to which UK water utilities have considered climate-change-related issues (such as resource protection, flooding, demand management, leakage and greenhouse gas emissions) and how the UK water sector's regulator, Ofwat, expects water companies to address climate change as part of their long-term asset management planning and how it will take climate change risks into account in the next Price Review in 2009.

Treating customers fairly

We aim to ensure that our product life cycle, from product conception, through marketing, sales and after sales including complaints handling, captures the essence of principles based regulation.

Our customer contract sets out principles governing how we interact with our customers. Senior managers take responsibility for embedding them in every aspect of our business. The contract also includes an annual review of our products to ensure they still meet the needs of our customers as well as shareholders.

HBOS has been at the forefront of moves to simplify customer communications by providing clear summary boxes on credit card statements, marketing literature and estate agency agreements. These summary boxes provide a clear and balanced summary of features, benefits, risks and commitments of our products.

OFT review of fees and charges

The vast majority of banking customers never incur charges and bank for free. Arranging an overdraft, or increasing a limit, in advance can be done 24 hours a day, online or over the phone, and need take no more than five minutes.

However in 2007 the major high street banks and Office of Fair Trading jointly entered into a High Court test case to obtain a firm legal position on unarranged overdraft charges. In April 2008 the Court issued its judgement that the fees are not penalties, but that they are assessable in UK law for fairness.

The Court has not yet ruled on whether the charges are fair or not- this will be decided at a future hearing. HBOS believes the fees customers pay for unarranged overdrafts are fair and that the charges will therefore be upheld by the Court at the next phase.

Protecting customers' assets

Face to face transactions have seen a further reduction of x% in fraud losses on top of the 43% reduction last years. However, internet and international fraud attacks have increased as fraudsters seek different points of attack. We are working hard to tackle the problem, and there are also steps customers can take to help protect themselves.

Card fraud

HBOS reimburses customers who, through no fault of their own, fall victim to card fraud. Chip and PIN is a good safeguard, but fraudsters are moving towards using stolen card data in ATMs in countries which have not yet implemented technology such as Chip and PIN.

We have increased our defences to protect customers, and there are simple steps customers can take to help reduce the risk – always shield the keypad when entering a PIN, never write down a PIN number, and make sure to keep the card in view when paying for goods and services.

Phishing

Phishing attacks, where fraudsters set up fake websites to trick customers into giving away credit card or bank account details, continue to grow. To respond to such threats HBOS has a specialist Internet Attack Centre tackling online attacks and we are constantly working to ensure that the security of our online banking service remains at the forefront of the industry.

Boiler room scams

'Boiler room scams' involve unlicensed brokers targeting investors by cold-calling or mailing them and using high pressure sales techniques to recommend the purchase of shares. These shares commonly turn out to be worthless or are unlisted. While rare, these frauds can be very costly – HBOS continues to work with the City of London Police and the FSA to disrupt and prosecute those involved.

Identity theft

Identity (ID) theft is when a criminal uses another person's personal information to take on that person's identity. They may then buy expensive goods on credit, take out loans, obtain state benefits and even obtain false passports.

We have rigorous credit reference and application processes to help prevent ID theft in the first place, and if a customer does fall victim we have processes to put things right.

Anti-money laundering (AML)

We observe high standards of customer identification and verification, in line with Joint Money Laundering Steering Group guidance. Our Group AML policy is updated annually to reflect developments in legislation and guidance. We have recently been heavily engaged in the consultation process for the Draft Money Laundering Regulations 2007.

Whistleblowing

We have a policy and a helpline to support colleagues who are concerned about possible unacceptable behaviour or practices at work. By raising concerns, colleagues can help HBOS to protect its reputation and deal with inappropriate behaviours. In addition to the Whistleblowing Policy, colleagues are advised to refer to our Grievance and Harassment policies to ensure they report any concerns in the most appropriate way. All cases are treated seriously and sensitively and appropriate follow-up action is taken.

People strategy **Achieving success**

Our colleagues

Our strategy

We aim to have the strongest leadership teams in the sector and we are very clear about the high expectations of both what our leaders deliver and how they do this. Our strategy is underpinned by our core values of dignity and respect. We provide all our colleagues with ongoing opportunities to learn and to develop their careers and we constantly evaluate our efforts to create a positive working environment that reflects the diversity of our colleagues. We keep all aspects of our reward systems under continuous review to ensure they deliver the right reinforcement in respect of recruitment, retention and motivation. Through our Colleague Opinion Survey we track our leadership and capability indices as well as employer and product advocacy.

Our leadership

To be successful we need to develop colleagues who can Lead, Shape, Build and Deliver. These elements form our Leadership Commitment which drives our approach to hiring, performance management, reward, succession planning and development. The Way We Do Business, our statement of business principles, is integrated into the Leadership Commitment. This helps ensure that our commitments to stakeholders are part of the core competencies against which the performance of all colleagues is measured. Since 2006, 25% of senior manager bonus has been based on personal performance against this commitment.

HBOS-U

In 2006 we launched HBOS-U, our corporate university, to help senior managers understand their responsibilities. In 2007, HBOS-U became fully operational. The HBOS-U brand built great traction in the business.

Key highlights from the year include:

- The Leadership Commitment Conference series: over 430 colleagues attended Leadership Commitment Conferences, 98% of which rated the events as 'excellent' (57%) or 'good' (41%).
- The Leadership Exchange Programme: the Programme was updated and provided opportunities for 52 colleagues to 'exchange' roles to gain insights into their leadership styles and

further their understanding of other parts of the business.

- We launched 'Management Update', a monthly e-magazine, providing business focused articles directly to the mailboxes of our senior managers. Around 70% of senior managers now regularly make use of this resource.
- Over 1,300 colleagues attended an HBOS-U event, representing 41% of the target audience. Based on this success, in 2008 HBOS-U is being extended to all colleagues.

Union partnership

Last year, we signed a groundbreaking Partnership Agreement with our partner unions ACCORD and Unite. Over the next five years we will seek to increase membership to approximately 70% of UK colleagues. We believe this ambition makes us unique in the UK financial sector.

Our agreement supports the development and implementation of good employee relations throughout the business. Our approach to partnership is to progressively embed the concept of working collaboratively with our partner unions throughout the HBOS culture. This is supported by a focused communications strategy.

We ensure that our partner unions are involved at an early stage in any change management process as we believe that the subsequent outcomes will be of greater benefit to our business. We actively encourage HBOS colleagues to become union members. By doing so, we believe that our unions will be truly representative of HBOS colleagues.

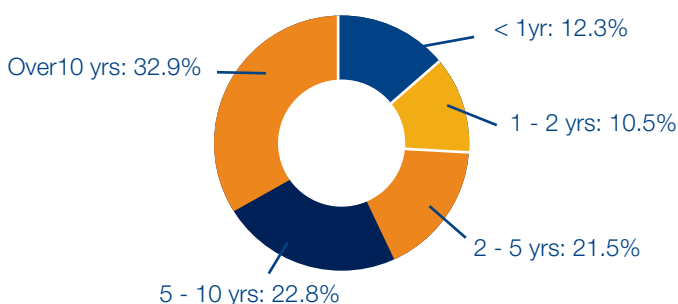
We are currently working with our partner unions on the design and delivery of workshops to develop managers' and union representatives' skills. We believe there are significant business benefits in ensuring that employee relations issues are managed - and resolved - within the workplace.

Reward and recognition

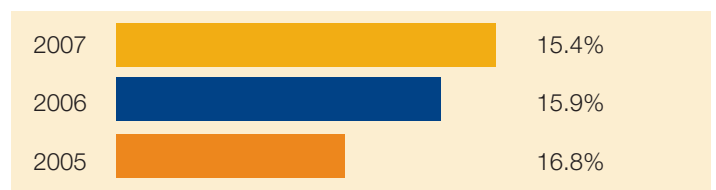
Sharing in success

Our Total Reward strategy aligns performance with rewards. Colleagues are encouraged to share in the success of HBOS through share ownership. HBOS's financial performance during 2007 means that over £200m was shared by colleagues this year through maturities under our unique range of share ownership plans. Colleagues also benefited from over £300m in cash bonuses.

Length of service



Colleague turnover rates



Clear communication

As in previous years, Chief Executive Andy Hornby issued all colleagues with their own personalised statement, itemising the full value within their reward package and including elements such as share plans and pensions. All of our reward communications are printed on materials which are recycled or from sustainable sources.

Flexible and every day benefits

Colleagues can access a range of valuable benefits and discounts online, in order to help them secure maximum value by matching their reward packages to their personal circumstances. 'Flex' gives colleagues a wide range of options to purchase, via their regular salary, benefits such as childcare, health cover and bicycles with the added bonus of these benefits provided at reduced cost. Take up of benefits through Flex increased by over 16% in 2007.

HBOS car provision for colleagues

In 2007, HBOS reduced the range of vehicles for our essential car users (4,000 colleagues) by half and we now supply only diesel or hybrid vehicles to help reduce our carbon emissions.

Our wholly owned fleet business, Lex, has partnered with a global vehicle manufacturer to share and learn about best practice. Initiatives include improving how we incentivise and enable colleagues to drive 'smarter' more efficient vehicles, such as attractive purchase options as well as full servicing and business travel enabled insurance so colleagues who are not company car drivers are appropriately covered on business travel.

Fair pay and rewards

HBOS regularly monitors its pay and reward provision across the business, including the delivery of a detailed pay and bonus review every year, in addition to a formal Equal Pay Audit every three years, to ensure that colleagues are rewarded fairly in line with our Diversity commitments.

Colleague financial education

Last year, HBOS established a Colleague Financial Awareness team to deliver a programme of financial education seminars for colleagues. The seminars, designed in collaboration with the FSA, deal with financial planning and provide an opportunity for colleagues to ask experts questions relating to their own individual circumstances. Themes range from helping colleagues to maximise the benefits of their HBOS "Total Reward" package, helping

colleagues onto the housing ladder or to move on up, including colleague mortgage offerings and other products and services, share plan awareness and benefits, saving and investment.

By the end of 2007, over 5,000 colleagues had attended financial education seminars. To date, the seminars have taken place at our major employment sites. In 2008, the objective is to develop electronic learning materials for the benefit of colleagues in smaller locations. All colleagues already have access to on-line calculators to support pension and share plan decisions, and these will be supplemented by a broader range of learning materials to mirror the content in the seminar programme.

Diversity

A commitment to diversity and inclusion helps us attract, develop and retain the best talent.

In January 2006 the HBOS Board agreed a new Diversity Strategy. The key areas agreed in the strategy are Leadership, Awareness, Getting the Basics Right and Disability. It advocates an approach whereby diversity is integrated into everything we do; diversity and inclusion now form part of our business planning process.

During 2007, we introduced many new initiatives to embed the strategy across the business. To support the integration of diversity and inclusion into the business planning process, we developed new management objectives. These were presented to the HBOS Forum, consisting of the top 1000 leaders in HBOS, by our chief executive, Andy Hornby, in November 2007. They ensure that all HBOS businesses measure and monitor progress against diversity and inclusion objectives year on year.

Leadership

Our Diversity Steering Group is chaired by Andy Hornby. Members of the group comprise senior leaders across HBOS. The steering group is there to shape and direct the diversity agenda as well as act as advocates for driving the diversity agenda forward and challenge the business to remove any barriers to progress.

Peter Cummings, Chief Executive of Corporate, represents HBOS at the Employers Forum on Disability President's group. Lord Dennis Stevenson, HBOS Chairman, is the Patron of the Employers Forum on Age and the Employers Forum on Belief.

Female managers at Level 4 and above



Managers from ethnic minorities at Level 4 (senior manager) and above



Workforce statistics

We monitor and measure workforce trends, to help us understand what impact our strategy is having and where our focus should rest. We monitor representational trends and responses to diversity and inclusion questions that form part of our monthly and annual Colleague Opinion Surveys. We review the Colleague Opinion Survey by a range of diversity strands, levels and business areas to identify perception gaps between minority and majority colleagues, including sexual orientation, religion and belief. This information has helped for our thinking and action planning and is one area which is monitored year upon year for progress and identifies areas for future focus.

2007 workforce statistics

- 61.4% of all colleagues were female.
- Almost 60% were aged between 26 and 45.
- 7.2% of colleagues were from an ethnic minority, compared to 7% in 2006 and 6.3% in 2005.
- Approximately 1.7% of our colleagues stated they had some form of disability.

Age diversity

HBOS recognises the value of age diversity. A result of the implementation of the Equality in Employment (Age) Regulations, as well as ensuring we have age friendly policies, we took the decision in 2006 to remove our contractual retirement age and implement a flexible retirement scheme. Colleagues are able to continue working full-or part- time, whilst taking advantage of their pension benefits. These changes have proved very popular.

Education and awareness

Diversity training is mandatory for all HBOS colleagues and is delivered through our e-learning tool, 'Diversity at Work'. Recruiting managers are required to complete the Disability Confident E-Learning module, as well as Diversity at Work, on an annual basis to help build diversity and disability competence.

In 2007, we:

- Introduced a Diversity Upskilling Programme that includes Lunchbite sessions covering diversity, cultural awareness, dignity and respect, disability, colleague wellbeing and flexible working. In 2007, we delivered over 100 sessions across the business.
- Began working in partnership with our unions Unite and Accord on the development of a more in-depth Dignity at Work module.

- Delivered our 150 diversity sessions in Corporate division.
- Introduced Corporate Knowledge for all colleagues in the Corporate division with a mandatory session reinforcing our values.

Disability

In 2007, we launched a Disability Confident e-learning tool, and an online guide for line managers in managing colleagues with disabilities.

Disability Confident has been rolled out across the business, initially for use by HR colleagues, line managers and colleagues involved in recruitment and selection activities. Our online guide, the 'Workplace Adjustment Site', provides practical support and tools to enable colleagues with disabilities to carry out their jobs effectively.

Case study

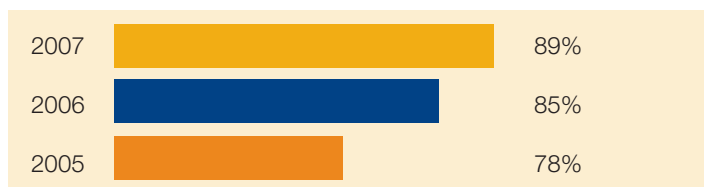
HBOS Australia Corporate Responsibility Seal of Approval
HBOS Australia has introduced a novel concept to help grow colleague awareness of corporate responsibility.

The HBOS Australia Corporate Responsibility Seal of Approval is awarded to those initiatives and projects that meet the corporate responsibility standards governing the company's activities in the marketplace, workplace, environment and community.

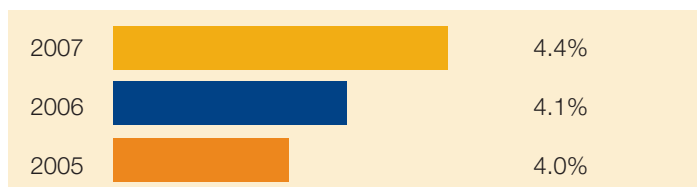
The Seal of Approval has proven to be an effective tool in helping to communicate the successes of HBOS Australia's Corporate Responsibility program.

Since its introduction in May 2008, the Seal of Approval has been awarded to departments for initiatives such as providing financial education books at discount prices and helping customers in financial difficulties (BankWest Retail), investment in the community (HBOSA Foundation), recycling uniforms and driving improved travel information (HBOSA Procurement) and promoting video conferencing to help cut costs and emissions (HBOSA IT).

% colleagues that understand the importance of equal opportunities and diversity in their work



HBOS workforce aged 56 and above



Flexible working

In 2007, we conducted a major review of our flexible working policies. The Flexible Working Project, sponsored by Andy Hornby, aims to embed a flexible working culture across the business and ensure that all colleagues are able to operate some form of flexible working. To drive the Project forward, over 100 interviews were conducted with colleagues to gather feedback and ideas to develop a range of actions and pilots. We subsequently launched flexible working pilots in our Retail and Corporate divisions, and developed a Flexible Working intranet site. We are working closely with our union partners on the development of the flexible working project to incorporate stakeholder feedback at every stage.

Health and safety

The health, safety and welfare of colleagues, customers and contractors are key business objectives at HBOS. We are committed to achieving high standards of health and safety across all of our businesses. Our Health and Safety policy is available on our Corporate Responsibility website.

In April 2008, HBOS was awarded a gold award for its health and safety standards - for the third year running. The accolade, from the Royal Society for the Prevention of Accidents (ROSPA), recognises high standards in the management of health and safety.

Our approach is based on the Health and Safety Executive (HSE) best practice allowing the Group to demonstrate a structured and consistent approach. Our approach to health and safety is guided by stakeholder dialogue within HBOS and externally to ensure appropriate consultation and effective implementation.

KPI 2007 performance

Year on year reduction in the number of recorded accidents across the Group

Group Accidents - 4% increase in the Group Incident rate
Total accidents involving injury (colleagues only) - 1223

Reduce the number of slip, trip and fall accidents (the most common injury causing accident in HBOS) by 10% from 2004 levels by end of 2009

STF - 10% reduction in the Group Incidence rate for slip, trip and fall accidents
Total Slips, Trips and Falls (including Members of Public) - 467

Reduce the number of RIDDOR (reportable accidents) events across the Group by 6% from 2004 levels by end of 2008

Riddor - 5.4% increase in the Group Incidence rate
Total RIDDOR (colleagues only) - 122

Colleague Opinion Survey

- In 2007 almost 60,000 colleagues (more than 88% of colleagues) took part – the biggest return for HBOS and Ipsos MORI.
- 89% of colleagues said they understood the importance of equal opportunities and diversity in their work, an increase of 4% from the 2006 survey.
- 79% agree that HBOS is committed to improving equal opportunities and diversity throughout the business, an increase of 5% since the 2006 survey.
- 86% of colleagues felt that their line manager treated them fairly, with dignity and respect, ahead of the industry norm of 79%.
- 70% of colleagues were satisfied with their job.

External benchmarking and awards

Opportunity Now

HBOS is a Gold standard performer in Opportunity Now

Race for Opportunity

HBOS was ranked 5th out of 70 private sector companies

Stonewall Workplace and Equality Index

HBOS featured in the top 100 for the fourth year running, and climbed from 77th position in 2006 to 43rd position in 2007.

Employers Forum on Disability

The Employers Forum on Disability Standard Benchmark rated HBOS Silver status with a score of 79%. HBOS ranked 14th out of 116 organisations.

A Cranfield University Report on Female Directors placed HBOS 5th in the FTSE Top 100 for female representation at Board level.

What we recommended	How we performed	Where we can do better
Launch the Disability Confident tool across the HBOS Group in support of our ongoing disability strategy.	Disability Confident has been rolled out across the business.	Work in partnership with our unions Unite and Accord on the development of an in-depth Dignity at Work e-learning module.
Conduct a major review in 2007 of how we can extend the reach of flexible working opportunities within the business.	The review was completed in 2007, resulting in flexible working pilots in Retail and Corporate divisions and a dedicated intranet site.	Work closely with the unions on the development of the Flexible Working Project sponsored by Andy Hornby.
Improve colleague advocacy of HBOS's environmental strategy.	Colleague advocacy of our environmental programme has grown from 24% in 2004 to 56% by the end of Q1 2008.	Drive colleague advocacy for our environmental programme higher.

Climate change and environment

Protecting our future

Emissions Controlling our energy use and travel.

Paper use Controlling our use of paper.

Resource use Controlling water and waste.

Market solutions Innovative products and services.

Governance Ensuring strong management.



Environment Reducing our use of resources is better for the environment and better for the bottom line.

Our strategy

HBOS's biggest environmental challenges are responding to climate change and managing our use of resources. Reducing our use of resources such as travel, energy use and paper is a clear environmental imperative, and can result in significant cost savings.

Managing our carbon emissions is also an investment in the future sustainability of our business model. We are committed to managing the risks posed to HBOS by climate change and grasping the opportunities that it presents.

Our impact

Our UK estate

Our UK estate comprises 2,200 buildings (including 1,100 bank branches) occupied by over 66,000 colleagues. As well as investing in environmental efficiencies, to deliver these, we are engaging our colleagues to advocate our strategy.

We assess the environmental impact of operating our buildings using the Building Research Establishment Ecopoints system. This shows that energy consumption accounts for around 70% of our direct impact on the environment, followed by paper consumption and business travel. The production of general office waste produced by colleagues while they work, such as food packaging and plastics, together with water consumption, accounts for less than 1% of HBOS's direct impacts.

Our international operations

We have a growing international presence across Australia, Ireland, Europe and North America. In 2007 our international operations have started to introduce a wider range of environmental targets and initiatives to reduce resource use. This programme will continue to develop during 2008 and we will report on progress next year.

Our targets

We have set new 3 year targets for our major impact areas with annual checkpoints to assess progress towards the overall target.

CO2 emissions

HBOS's target is to reduce CO2 emissions by 5% within 3 years:

2008	At least 1% less than 2007
2009	At least 3% less than 2007
2010	5% less than 2007

HBOS's target is to reduce energy use per FTE in major employment sites and the retail branch network by 10% within 3 years:

2008	At least 3% per FTE less than 2007
2009	At least 6% per FTE less than 2007
2010	10 % per FTE less than 2007

Waste Generation

HBOS's target is to reduce waste generated per FTE by 5% within 3 years:

2008	At least 1.5% per FTE less than 2007
2009	At least 3% per FTE less than 2007
2010	At least 5% per FTE less than 2007

Paper Use

HBOS's target is to reduce total paper use by 10% within 3 years:

2008	At least 3% less than 2007
2009	At least 6% less than 2007
2010	10% less than 2007

Water Use

HBOS's target is to reduce total water use by 2% within 3 years:

2008	At least 0.5% less than 2007
2009	At least 1% less than 2007
2010	2% less than 2007

Recycling

HBOS's target is to increase recycling by 6.60% within 3 years:

2008	54% of total waste recycled
2009	57% of total waste recycled
2010	60% of total waste recycled

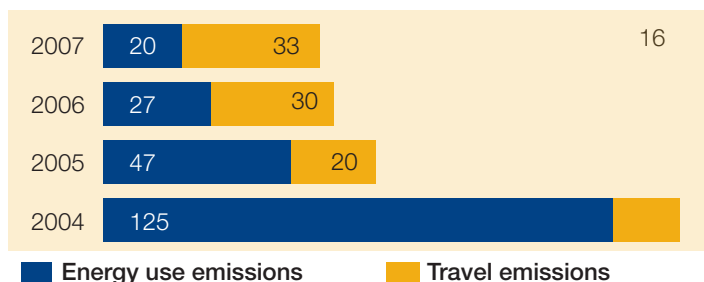
Where do our carbon emissions come from?

Banking is a low carbon sector- our carbon footprint consists of our energy use (electricity and gas) and business travel. Since 2004 we have reduced our UK emissions by over two thirds, from 163,000 tonnes in 2004 to around 53,500 tonnes in 2007. This has been achieved through the use of 100% renewable electricity, energy efficiency schemes, and the Green Miles initiative.

HBOS offsets all UK emissions through only 100% Kyoto compliant carbon credits and is carbon neutral in the UK.

New standards for voluntary credits (VERs) are developing and maturing such as the Voluntary Carbon Standard (VCS). We will consider the merits of purchasing high quality VERs in this context. Our approach will also be considered in the light of developments to DEFRA's reporting framework. We may choose not to offset next year as a result (see page 7).

HBOS carbon emissions 2004 - 2007 (thousand tonnes CO2)



Carbon neutrality

HBOS's UK operations are carbon neutral. HBOS is the only bank to offset emissions using only 100% Kyoto compliant carbon credits. HBOS's carbon credits support renewable electricity generation in Brazil and India.

Energy generated CO2 emissions

HBOS was the first major UK bank to purchase 100% renewable electricity for its entire UK estate. 100% renewable energy produces no carbon emissions. Remaining energy related emissions arise from use of natural gas in boilers across some of our estate.

Controlling our use of energy

In 2002, HBOS set itself a stretching target of reducing its consumption of energy by 17.5% per FTE by the end of 2007. By the end of 2007 we had achieved a reduction of 12.8% per FTE, slightly behind our target. This is due to the dual-running of sites during a move to a new environmentally friendlier building in Bristol. We have set new targets for the next three years which are set out in the following pages.

Long-life lightbulbs (compact fluorescent lamps)

Over 80% of light bulbs across HBOS's estate are long-life, low energy bulbs. The remaining light fittings will be upgraded over the next four years as part of our building refurbishment programme.

Green Miles

Green Miles was rolled out across the UK in 2007 to reduce growth in travel. The scheme incentivises travel reduction by sharing the savings made with the HBOS Foundation's Charity of the Year. In 2007 Green Miles raised £500,000 for the British Heart Foundation and saved over 5m miles.

Business travel generated emissions

Business travel now accounts for over 50% of our UK carbon emissions- 33,874 tonnes. Of this, 48.4% is road, 47.2% air and 4.2% rail. Last year we launched a new programme, Green Miles designed to reduce travel growth, saving money and controlling our impact on climate change.

A greener car fleet

We offer only diesel or hybrid vehicles to 'essential' company car users and we have been steadily reducing the average CO2 emissions of the fleet for many years. The average CO2 emissions across the HBOS fleet have reduced from 165.5g/km in 2006 to 163.8g/km in 2007.

Bristol Harbourside

Our flagship south west headquarters, Bristol Harbourside, was completed at the end of 2007. Built from sustainable materials and kitted out with cutting edge energy efficiency technology, the building received the highest possible building rating, 'Excellent', in the Building Research Establishment's Environmental Assessment Method ('BREEAM') environmental rating.

Managing paper use

HBOS directly consumed approximately 17,664 tonnes of paper in 2007. Equivalent figures for 2006 and 2005 were 17,329 tonnes and 16,440 tonnes respectively. This increase is despite moving to double-sided printing, cutting down on internal reports, and encouraging customers to move to paper free communications. Our new target was set as result of this trend.

In addition to providing paper recycling facilities in major employment sites, we recycle all our confidential paper waste across our entire estate.

We have also increased the amount of recycled paper we use, moving to 100% recycled paper for business cards and compliment slips.

In 2008 HBOS will launch a new paper strategy seeking to further increase the amount of 100% recycled paper we use, reduce the amount of paper we use and increase the amount of paper we recycle.

Paper-free banking

Over 1.7 million banking customers are now registered for the Halifax and Bank of Scotland online paper-free service. More than 65% of HBOS online customers use paper-free. By registering for the service, customers can:

- Find statements and letters quickly and easily – they are stored securely online for two years.
- Save statements into money management software like Microsoft Money.
- Print statements whenever they need a hard copy.
- Save paper and help the environment.
- Cut out the clutter and reduce paperwork.

Managing resource use (waste and water)

Waste and recycling

Our target for waste was to increase recycling to 60% of all general waste by the end of 2007. We fell short of this target, recycling 51.48% of all waste during 2007. We have set new checkpoints towards 60% over the next three years, alongside new plans to achieve them.

Improved recycling schemes have been introduced in all our major employment sites to allow recycling of paper, printer cartridges,

cans and plastic bottles and cups. In the branch network all confidential paper and a large amount of non-confidential paper is recycled. However, we know there is more we can do here.

Water use

HBOS committed to reduce water use by 10% between 2002 -2007. By the end of 2007 we experienced a 1.5% increase per FTE against the 2002 baseline- substantially worse than our target despite water saving devices having been fitted in over 95% of cisterns in our buildings. Partly this is due to dual-running of sites as we move to improved, more environmentally friendly buildings but we know we need to do better across the estate.

Our new target is to reduce total water use by 2% within 3 years.

Helping our customers

The increasing regulation and emerging fiscal mechanisms designed to tackle climate change are creating opportunities for banks to develop services which will help address climate change and environmental degradation.

Carbon labelling

In 2007 HBOS became the first major bank in Europe to carbon label a financial services product. HBOS has carbon labelled the Halifax Web Saver account, one of the group's most popular savings products with more than 1.1 million accounts.

HBOS worked with Carbon Trust, tasked by the UK government to tackle climate change, to calculate the greenhouse gas emissions generated by Web Saver. In turn, the Trust is working with DEFRA and BSI British Standards to develop a single standard to measure the embodied greenhouse gas emissions from products and services.

What carbon labelling means for Web Saver customers

A logo has been added to the Halifax Web Saver online site. This shows existing and potential customers how much carbon their account produces. The carbon calculation covers all greenhouse gas emissions from the initial application to customers' transactions.

Web Saver is an on-line product so each account will generate relatively low carbon emissions. Halifax has committed to reducing these emissions within two years. If a reduction is not achieved, the label will be withdrawn.

Our lending decisions

Lending is one of the key areas where we can have a significant positive impact on managing Climate Change. Bank of Scotland Corporate is a top 10 lender (in Europe) to renewable energy projects. We continue to explore the commercial opportunities to finance solar tidal energy and off shore wind projects. Clearly, this commercial UK activity on our part sends an important message to the renewable energy community.

Our purchasing decisions

Environmental issues continue to be built into our procurement practices and colleagues are actively encouraged to work with suppliers to minimise our environmental impact. All our paper comes from sustainably managed sources and we have moved to 100% recycled paper for business cards and compliment slips. We have expanded SpendWise our online stationery buying tool, reducing the use of paper in our ordering process.

Leadership in investment

Insight Investment, HBOS's asset management business led the process of developing the Investor Statement on Climate Change. Insight has an active approach to investor responsibility including publishing briefings, offering a specific screening service to investors and providing funds such as the Evergreen Fund that has a 20% weighting towards investment in companies that develop environmentally beneficial products. The investor responsibility section of this report contains more detail.

Governance

The HBOS Environmental Policy

HBOS has an Environmental Management System based on ISO 14001. We have not however sought external ISO14001 certification as, based on the advice of external consultants, we have decided that certification would not add value to our environmental programme. This approach was once again reviewed during 2007 and will be reviewed again in 2008.

Corporate Environmental Objectives linked to our significant impacts are published alongside our Environmental Policy Statement on Groupnet (the HBOS intranet) and on our external

website. Management and performance targets addressing HBOS's significant operational environmental impacts are set following audits and the management review conducted annually by independent external consultants. Performance against targets is reported in the annual report to the Board on the Environmental Strategy, our annual Climate Change report and here, in our Corporate Responsibility Report.

Training and education

Internal environmental communications and training are delivered to colleagues via a range of media including, for example, group-wide and divisional intranets and e-magazines, divisional hard copy magazines, presentations, seminars and workshops, to raise our colleagues' awareness of environmental issues and how they can address these at work and at home. We gauge our colleagues' views on the effectiveness of our environmental programme in monthly and annual Colleague Opinion Surveys conducted by MORI.

What do our stakeholders think?

Colleague advocacy

In three years, colleague advocacy of our environmental programme has increased from 24% to 56% – a substantial improvement, but our target is to increase this to 70% so much remains to be done.

Following the launch of the new Climate Change Strategy last year, over 400 colleagues sent feedback on the programme, making the programme the most successful internal communication campaign HBOS has delivered.

Stronger external metrics

HBOS is now the UK leader in the main external metrics. HBOS is the highest scoring UK bank in the Dow Jones Sustainability Index, Carbon Disclosure Project Climate Leadership Index and Business in the Community CR Index. We are the only UK bank to have featured in the Global 100 Most Sustainable Corporations index every year since its launch at the World Economic Forum in Davos in January 2005.

Where we can do better

What we committed	How we performed	Where we can do better
Offset UK emissions through Certified Emissions Reductions delivered in developing countries.	HBOS offset all UK emissions including energy use and business travel by purchasing 100% Kyoto compliant Certified Emissions Reductions	Meet new targets for carbon emissions and continue to offset using only 100% Kyoto compliant carbon credits
Roll out Green Miles across the UK.	Green Miles was rolled out across the UK saving over 5m miles and raising £500,000 for HBOS Charity of the Year	Expand Green Miles to include road mileage in addition to rail and air
Be the first bank to rate the energy efficiency of all HBOS buildings on a scale of A-G and display a rating, just like the stickers on new fridges and washing machines.	EnergyTrack was launched in 2007, setting out the energy, waste and water performance of each building.	Improve the performance of HBOS buildings using the information generated for EnergyTrack
Launch a Green Mortgage during 2008.	The Green Mortgage was developed during 2007 and into 2008. It will be launched as planned in 2008.	Launch the Green Mortgage in 2008.
Implement new recycling facilities for all waste paper across our entire branch network, to supplement facilities already in place in our offices and call centres.	HBOS's entire branch network now has recycling facilities for waste paper	

Community Benefiting society

Economic impact Our main contribution to society is as a tax payer, employer and generator of wealth.

Investment Our economic contribution is supported by a comprehensive programme of investment in communities, financial inclusion, micro-finance and community giving.



Community HBOS is a significant generator of wealth across the UK.

Our strategy

We are the only major bank to express community contribution in terms of our overall economic impact. Our economic contribution to the community is large and growing. Our community investment strategy centres around two key areas:

- Our economic contribution as a tax payer, an employer, and a generator of wealth.
- Our active investment in many communities: financial inclusion, micro-finance and community giving.

Our economic impact

Tax contributions

We are one of the largest payers of tax in the UK. The UK Exchequer received a total of almost £1.7bn in tax and National Insurance from HBOS and its colleagues in 2007. That equates to £3,150 a minute in tax or the annual salary bill of 46,500 secondary school teachers for a year. We are the fifth largest payer of tax in the UK, as measured by the PwC One Hundred Group Survey of the UK's 100 top firms. We accounted for almost 2% of all UK corporation tax paid in 2007.

Employment

HBOS employs over 69,000 people in the UK and over 74,000 worldwide. Through directly employed staff and the indirect jobs created at suppliers, HBOS supports 105,000 full-time equivalent jobs in the UK.

In 2007, colleagues were awarded £80m in free shares and a total of £270m in cash bonuses. HBOS colleagues across the UK have now received £218m in free shares since our Free Shares scheme began in 2005. More about our approach to employment is set out in the Colleague Strategy chapter.

Wealth generation

In 2007, 79% of HBOS's private shareholders were also HBOS customers. HBOS has over 2m private shareholders, the biggest private shareholder base in the UK. HBOS small shareholders account for more than 7% (£5.66bn) of the total value of all the shares held by private individuals in the FTSE 100 companies. Each small shareholder received, on average, £183 in 2007. Last year, HBOS paid out dividends totalling £1.8bn.

HBOS accounts for £8.1bn or almost 1% (0.7%) of the UK's GDP, according to the annual survey from the DTI. The DTI measure total sales less costs of bought in goods and services. When the earnings and turnover of overseas subsidiaries of UK companies are stripped out, we calculate that HBOS is a top five corporate generator of wealth in the UK.

Purchasing goods and services

HBOS spent over £3bn on goods and services in 2007. The Procurement Minimum Standards, approved by the Board and the Best Practice Manual identify the process for awarding and evaluating Group-wide contracts with key suppliers, including Corporate Responsibility. Suppliers in Scotland and Yorkshire benefited from 22% of our total spend in 2007.

Community investment

HBOS	Procurement spend 2007	Procurement spend 2006	Procurement spend 2001
Total	£3.05bn	£2.92bn	£2.2bn
Of which Scotland-based suppliers	£532m	£755m	£204m
Yorkshire-based suppliers	£149m	£178m	£189m

HBOS invested £55.2m in communities across the UK in 2007, including support for financial inclusion, sponsorship of sports and arts for young people, and donations through the HBOS Foundation. This was an increase of £1m compared to 2006 and represents 1.3% of our UK pre-tax profit.

Investment in the community (£m)

2007	55.2
2006	44.2
2005	43.1

Our approach

We believe we can achieve the greatest impact by focusing on issues that are consistent with our business and inspire our colleagues. We keep costs down by integrating our efforts into our business wherever possible. Our input is also designed to lever additional funding for our chosen projects from other stakeholders, in turn making projects more sustainable. This was most recently demonstrated through the financial support which the Scottish Government has committed to our work with the Midnight league. Over the last five years, Halifax and Bank of Scotland have invested approximately £250m in thousands of local community initiatives and charities.

Financial inclusion

Our financial inclusion strategy is driven by both commercial opportunity and a recognition that it is right to work towards bringing more consumers, especially those on lower incomes, into the financial system. A full picture of our financial inclusion activity is set out in the financial inclusion section of this report and in our Financial Inclusion Report. No other bank produces one.

We recognise that an effective way of bringing people into the banking may be to work with partners from the non-profit sector who have close relationships with individuals who are currently excluded.

Micro-Finance

HBOS is helping to pioneer UK focused micro-finance projects for financially excluded people. HBOS is already one of the biggest lenders to Community Development Finance Institutions in the UK, and we made a commitment in 2007 to expand our work with credit unions and increase our investment in this sector. We already lend to over 30 credit unions on a commercial basis. This year, we have launched new initiatives with Calderdale Credit Union (CU) and RCUDA CU in Rotherham. Each CU will be given free access to our iSITE technology, so they can manage hundreds of new accounts for people wanting small amounts of credit.

Sponsorship

HBOS's award winning sponsorship programme invests £4m a year in sport and the arts to make a tangible difference to the lives of young people in the communities where we live and work. Over 70,000 young people benefited last year from HBOS sponsorship of sports and arts projects in our heartlands of Yorkshire and Scotland. An estimated 65% of these young people were from socially disadvantaged areas.

Case study

UNLOCK

HBOS plc is working in partnership with UNLOCK, the National Association of Reformed Offenders, to deliver social banking provision to low category former offenders. The pilot programme, launched in Cookham Wood and Coldingley prisons, opened basic bank accounts for prisoners approaching release. Social banking accounts provide a foundation for former offenders to rebuild their lives, making it easier for them to secure accommodation and employment.

Having opened accounts for 99% of applicants, the success of the pilots has led to plans to expand the programme from two prisons to four by the end of 2008 and integration into business as usual. Separately, the HBOS Foundation, a registered charity funded by HBOS plc, is supporting UNLOCK with a grant of £164,137 over three years. The funding has enabled UNLOCK to deliver a capacity building project 'UNLOCKing Financial Capability'. The course covers basic banking and money management skills to help people prepare to enter the banking system.

The UNLOCKing Social Banking programme aims to benefit up to 480 low category prisoners each year. The UNLOCKing Financial Capability programme aims to benefit around 5000 prisoners per year. Both programmes aim to leave sustainable systems in place so these benefits continue after the end of the project.

Says Chris Bath, Director of Projects at UNLOCK: "HBOS were quite simply the only bank brave enough to pilot the concept of pre-release banking with UNLOCK. By engaging with a financially excluded group that no other bank would even consider at the time, HBOS's pioneering attitude to financial exclusion has not just helped those in our project, it is fundamentally changing the industry's attitudes and practices. Where they have led, others are now following."

% of colleagues who would speak highly about the way HBOS supports charities and local communities



Sport	Number of young people
Schools Football	10,000
Soccer One	2,400
Midnightleague	10,000
Scottish Athletics	3,500
Yorkshire Athletics	430
Badminton	10,700
Total	37,030
Arts	
Children's Theatre Festival	11,600
The July Project	5,000
Northern Ballet Theatre	780
Scottish Ballet	1,500
Glasgow Book Festival	10,000
Northern Orchestral Enterprises	600
Connecting to Music	1,150
National Galleries	7,350
Total	37,980
Total young people	75,010

Sport

Bank of Scotland's Community Football is the most comprehensive grassroots football programme in Scotland. Bank of Scotland has cemented its commitment to grassroots football with a £1.5m investment over three years, enabling 140,000 schoolchildren to play and develop their skills. In December 2007, this commitment gained recognition from the Scottish Government when over £1m of Cash:Back funding was secured by the Scottish Football Association to support our sponsored community football programmes.

The Midnightleague is a 5-a-side community football programme which we run in partnership with the Scottish Football Association. The Midnightleague aims to keep young people off the streets, reduce crime levels and anti-social behaviour. The programme provides football training and skills late on weekday and weekend evenings, a time recognised by local police as a peak for disruptive behaviour. By working with police forces, local authorities and

football coaches we have extended the programme to all 32 local authorities in Scotland, helping over 10,000 young people to take part.

Arts

Our Connecting to Music programme, run in partnership with the Edinburgh International Festival, introduces young people to classical music using a series of practical workshops. More than 1,000 primary school children took part in 2007. Over 7,000 young people took part in an extensive education programme linked to our sponsorship of the Andy Warhol exhibition at the National Galleries of Scotland. The NGS Education Centre was turned into The Factory for the period of the exhibition with a wide variety of activities for children led by visual arts specialists including collage, printmaking and film. The Children's International Theatre Festival attracts world class theatre from across the globe to perform, entertain and educate more than 11,000 young people and their families throughout Scotland.

This year saw the launch of the Halifax sponsored July Project, a partnership with Square Chapel and Eureka, the museum for children. The July Project is a two week cultural festival in Halifax and Calderdale and in its first year involved around 5,000 young people.

HBOS Foundation

The HBOS Foundation is now one of the largest corporate fundraisers in the UK. Funded by HBOS, the Foundation drives volunteering and charitable work for the Group. In 2007, HBOS donated £8m to the Foundation. Unlike other foundations, HBOS finances all its staff, office and marketing costs, meaning that 100% of funds raised go to charitable causes. During the year, the Foundation donated almost £11m to charity, including contributions raised by colleagues and customers.

National and regional grants

The Foundation is funding a new educational programme, believed to be the most comprehensive of its kind in the UK, with the Sutton Trust in Yorkshire. The programme, delivered by Leeds University, aims to widen participation by under-privileged young people in higher education. The Foundation also distributed £2.8m in national and regional grants to financial literacy and money advice projects and to develop and support communities.

Fundraising

The HBOS Foundation's flagship programme is the Million £ Challenge. This programme raises money for the charities voted for by HBOS colleagues. In 2007, HBOS colleagues in the UK and Ireland, supported by matched funding from the Foundation, raised over £3.6m for the Million £ Challenge charities. They were: British Heart Foundation, WRVS, Family Holiday Association, RNLI and Age Action. The matched funding scheme raised £2.1m for a wide range of other charities.

The Million £ Challenge charity of the year for 2008 is CLIC Sargent. The two shortlisted charities, Age Concern and Diabetes UK, also stand to benefit – all funds raised above the £1m are split evenly between the three charities. The Foundation has set a target for 2008 to raise £4 million for the Million £ Challenge Charities.

Colleague volunteering

Volunteering has continued to grow. In 2007 over 10,000 HBOS colleagues volunteered, compared to over 7,000 in 2006. £21.3m has been raised via the Foundation, through volunteering, in the last five years.

Case study

Social inclusion Reach for Excellence

The HBOS Foundation is funding a new educational programme, believed to be the most comprehensive of its kind in the UK, with the Sutton Trust in Yorkshire. The programme, delivered by Leeds University, aims to widen participation by under-privileged young people in higher education. The programme will benefit 360 sixteen to eighteen year-olds over a three year period across HBOS's Yorkshire heartland. It will target young people who are plausible candidates for university and are from non-professional backgrounds with little family history of higher education, are in receipt of the Educational Maintenance Allowance or are in schools with low rates of progression to higher education.

Case study

Financial literacy

The Refugee Council

The HBOS Foundation is donating £100,000 over two years to the Refugee Council to support the development of a pilot to deliver financial literacy training courses for refugees and asylum seekers.

Financial literacy skills are essential for asylum seekers and refugees in becoming fully integrated in communities and accessing basic human needs. The Refugee Council has undertaken work to build their clients' personal financial literacy skills; however the organisation has not developed a standardised approach in this important area. The Foundation's grant will help to develop training to increase financial literacy of refugees and asylum seekers.

HBOS Foundation governance

The HBOS Foundation is a registered charity funded by HBOS plc. All the Foundation's staff, office and administration costs are paid by HBOS, as well as considerable support on marketing and promotion and funding of £8m per year.

The Foundation is governed by the Trustees, the Chairman of which is Phil Hodkinson, HBOS Finance Director. Full details of the HBOS Foundation's activity and governance can be found in the HBOS Foundation Annual Review at www.hbosfoundation.org/downloads/hbos-foundation-annual-report-2006.doc

Case study

Volunteering

Teamtime

Teamtime was the largest ever volunteering project undertaken by HBOS colleagues – over 750 colleagues took part in 2007. It provided an opportunity for HBOS colleagues to engage in environmental and conservation volunteering projects with the British Trust for Conservation Volunteers (BTCV).

Teamtime projects took place in nine areas across the UK, including Bristol, Chester, Leeds, Calderdale, Edinburgh, London, Cardiff, Glasgow and Wolverhampton, all of which are major HBOS employment centres. Through Teamtime, colleagues were able to contribute positively to the communities they live and work in. Each project was individually designed by BTCV to take into account local community needs to ensure long term sustainability.

HBOS Foundation targets	2007 Target	2007 Achieved
Fundraising	£5m	£5.86m
Volunteering	9000 colleagues	10,120
Community Action Plan	£1,000,000	£1,033,819
Calderdale/Edinburgh	£600,000	£580,415
National investment	£1,430,000	£1,189,911
Fundraising Costs	£850,000	£799,781

Case study

HBOS Australia Foundation

From its inception in 2005 to the end of 2007, the HBOS Australia Foundation has donated more than A\$2.3 million to charitable causes.

HBOS Australia donates A\$1 million to the Foundation each year and pays all overheads and operating costs. In 2007, colleagues raised nearly A\$250,000 for charity partners through workplace giving and fundraising activities.

Volunteering has also been successful with 800 colleagues assisting a charitable cause, including mentoring high school students, participating in reading programs for primary school children, and undertaking gardening and maintenance at facilities for the disabled.

What do our stakeholders think?

- Percentage of colleagues who speak highly about the way HBOS supports charities and local communities – 81% (86% in 2006, 79% in 2005).
- Percentage of colleagues who speak highly about the way HBOS supports colleague volunteering – 71% (71% in 2006, 67% in 2005).

Where we can do better

What we recommended	How we performed	Where we can do better
The HBOS Foundation and educational charity the Sutton Trust will launch a £1m initiative to help over 350 16-18 years olds from non-privileged backgrounds across Yorkshire gain a place at a top university.	In 2007 the HBOS Foundation funded "The Reach for Excellence programme" working with The Sutton Trust and Leeds University to develop a joint education programme in Yorkshire.	The HBOS Foundation is donating £410,000 over three years to the Rainer Foundation to fund the development and delivery of financial literacy training to key workers and volunteer mentors. We will aim to raise £4m for charities through the HBOS Foundation's Million £ Challenge in 2008.



Management Responsible business.

Managing corporate responsibility A comprehensive governance framework supports our corporate responsibility programme to ensure we manage our responsibilities effectively

Stakeholder dialogue Our programme is informed by dialogue with a wide range of stakeholders



Managing corporate responsibility

HBOS's focus on corporate responsibility is driven by the Board. We aspire to the highest standards of corporate governance as a means of driving the performance of the business.

Our strategy

Good governance helps ensure stakeholders have confidence that HBOS has processes in place to ensure the business is managed appropriately. HBOS has a strong framework of governance supporting decision-making. This framework integrates environmental, social and reputational considerations, including the impact on all our stakeholders, into our decision-making.

What this means in practice

Corporate governance

Good corporate governance is about running the company well. It involves putting in place an effective internal framework of authority and accountability that promotes success whilst managing and mitigating risk. We aim to challenge and refresh our approach to corporate governance to keep it live, well embedded and at the forefront of best practice development. Detail of the Group's governance arrangements, including the composition of the Board and internal controls, are set out on pages 111–150 of the Annual Report and Accounts 2007, available at the following link: http://www.hbosplc.com/investors/results/ARA_2007/downloads/HBOS_ARAreduce.pdf

Our CR governance

Ultimate responsibility for Corporate Responsibility lies with the Board. Each member has responsibility for the Way We Do Business and for implementing Group CR policies within their divisions.

The Board as a whole reviews the Way We Do Business Strategy and KPIs, the HBOS Environment Strategy and the HBOS Community Strategy annually.

Specialist CR committees and groups

The Board directs strategy for specific issues and implementation to committees and teams across HBOS. These committees comprise senior HBOS executives from across the Group to drive performance throughout every division.

Formal Board responsibility for CR lies with Peter Cummings, Chief Executive of Corporate.

Financial Inclusion and Capability Committee

Chaired by Jo Dawson, Chief Executive of Retail Distribution,

Insurance and Investment, the Financial Inclusion Committee focuses on products, services and initiatives designed to increase financial inclusion and capability. Initially established to focus on financial inclusion, its remit has been broadened to drive the Group's financial capability strategy.

Climate Change Action Group

Chaired by Chief Operating Officer, Philip Gore-Randall, the Climate Change Group is comprised of senior leaders from across HBOS's divisions. Formed to develop products and services to meet the growing consumer demand for 'green' products, the Climate Change Action Group acts as a central coordination point for HBOS's response to Climate Change.

HBOS Communications Group

Chaired by Andy Hornby, HBOS's Chief Executive, the HBOS Communications Group (HCG) is primarily responsible for reviewing strategies and issues affecting the standing of the Group's brands. It sets standards product development, marketing and other issues of major reputational impact. Corporate responsibility issues are frequently tabled to the HCG for senior guidance.

Diversity Leadership Group

The Diversity Leadership Group drives HBOS' Equality and Diversity strategy. Chaired by Andy Hornby, the Leadership Group acts as a central coordination body for HBOS' approach to diversity.

CR responsibilities and teams

Most of our Corporate Responsibility activity takes place in the business itself – through our lending decisions or the management of our property estate. A small CR team coordinates HBOS's CR programme on behalf of the Board. Group Communications facilitates committees and supports the Board in the development and implementation of new strategy. The Corporate Responsibility team reports to General Manager, Communications Shane O'Riordain, who reports directly to Andy Hornby, HBOS Chief Executive.

HBOS's Corporate Division has its own Head of Corporate Responsibility, reporting to Chief Executive of Corporate Peter Cummings. Corporate also has a network of 100 CR champions, five CR forums and a divisional CR Group chaired by Peter Cummings that meets quarterly.

Policies and procedures

HBOS has a set of detailed policies and procedures supporting the Way We Do Business. Reviewed annually, these Group policies set out our minimum requirements for the integration of Corporate Responsibility principles into our business-as-usual activities. For example, our Human Rights Policy incorporates the International Labour Organisation’s Declaration of Principles and Rights at work, as well as the UN declaration of Human Rights.

Clear and regular reporting

HBOS sets out clearly the strategy of each of our five divisions and provides Key Performance Indicators (KPIs) for each in our Annual Report, available at the following link: http://www.hbosplc.com/investors/results/ARA_2007/downloads/HBOS_ARAreduce.pdf

HBOS is the only major UK bank to produce a standalone, data-driven climate change report and financial inclusion report. These reports are available for download at our website at http://www.hbosplc.com/community/corporate_responsibility_home.asp.

HBOS is also the only major UK bank to directly support its statement of principles with a detailed set of KPIs. These can be found on at the back of this report.

An external verification process

Reviews are carried out of HBOS’s activity and reporting by bodies such as external auditors, diversity specialists, health and safety strategic partners, community investment specialists and HBOS Foundation Trustees. Our Corporate Responsibility programme is reviewed annually by independent consultants and an independent assurance is carried out on this annual CR report.

Corporate Responsibility performance is reviewed against peers through a wide range of benchmarking reviews, including Dow Jones Sustainability Index, FTSE4Good and Business in the Community.

Where we can do better

What we recommended	How we performed	Where we can do better
Expand environmental data capture to include non-UK businesses.	We now publish environmental data from our global businesses in our annual climate change report.	Continue to improve the quality and scope of our environmental data.

Case study

2007 Australian Corporate Responsibility Index
 In May 2008, the 2007 Australian Corporate Responsibility Index ranked HBOS as a world leader in corporate responsibility with a score of 98.64 per cent.

This was the first time HBOS had taken part in the Australian Index, following a global submission from HBOSplc.

HBOS was ranked first in community management, fourth in both marketplace and workplace management and eighth in environmental management.

Two of Australia’s oldest and most prestigious newspapers, The Sydney Morning Herald and Melbourne Age published the results in a special lift-out business report, which reached more than 1.5 million readers.

HBOS’s participation in the 2007 Australian Index highlights the company’s commitment to corporate responsibility in Australia.

Stakeholder dialogue Stakeholder dialogue is another way of saying that we respond to the people who are important to us. Dialogue helps define our strategy and shape our programme.

Our strategy

Our approach to stakeholder dialogue is aligned with the AA1000 Assurance Standard: completeness, materiality and responsiveness. This means we ensure we have clearly identified who our stakeholders are and understand their views and concerns; that we assess the relative importance of the issues in determining our strategy and the content of our reports; and that we respond to challenges and concerns.

Who do we engage with?

Our key stakeholders are those who are impacted significantly by the business or who might impact on it. On these criteria our most important stakeholders include:

Key stakeholders:

- Shareholders Over 2.2m shareholders.
- Customers 23 million customers; 80% of our private shareholders are also HBOS customers.
- Colleagues 74,000 Group-wide.
- Suppliers Around 21,500 suppliers.
- Society and environment Consumer groups, NGOs, politicians and regulators.

Since last year, 25% of each colleague's bonus has depended on personal performance, measured against the HBOS leadership framework. This includes stakeholder dialogue.

Dialogue with shareholders

Our dedicated Shareholder Services and Investor Relations teams are responsible for dialogue with private and institutional shareholders.

In 2007 Investor Relations had over 700 contacts with analysts and institutional investors.

The Investor Relations team has primary, day-to-day responsibility for managing communications with institutional shareholders through a combination of briefings to analysts and institutional shareholders (both at the interim and year end results and throughout the year), site visits and individual discussions between institutional shareholders and Board members and key senior executives. Regular dialogue with shareholders helps to ensure that our strategy is understood and that any queries or other issues are addressed in a constructive way.

Having pioneered online voting for shareholders in 2002, HBOS has seen the number of shareholders using this facility grow year on year. We have actively promoted online voting in mailings for our 2007 Annual General Meeting.

In December 2007 HBOS held a dinner with key Socially Responsible Investment analysts to discuss our approach climate change and other key issues. Phil Hodkinson, then Finance Director before retiring in 2008, led detailed dialogue on our activity.

Dialogue with customers

Understanding our customer opinion is one of the most important elements of our dialogue.

We undertake regular (monthly and quarterly) detailed customer research on service and products to ensure high standards are maintained as well as ad hoc research in response to particular business needs or specific customer needs.

In addition to direct customer contact we engage with stakeholder groups representing specific customer groups or specific customer issues.

Our Customer Contract includes an annual product review to ensure we are meeting needs.

Dialogue with colleagues

Regular dialogue with colleagues is encouraged through monthly and annual colleague opinion surveys, online 'Ask Andy Hornby' sessions, roadshows, and intranet sites.

Our internal communications channels include one-way communications, such as frequent HBOS Today newsletters and intranet communications, central feedback channels coordinated by Group Communications and multi-lateral discussions with business leaders – both in person at roadshows and regular intranet discussions. We benchmark ourselves against other high-performing organisations and obtain honest feedback MORI conducts monthly and annual Colleague Opinion Surveys. These surveys allow attitudes and trends to be identified in teams as few as 25 people, but individual responses cannot be identified to help ensure honest feedback. The results are published and plans drawn up for improvement.

We have good relationships with the finance sector trade unions, Unite and ACCORD, and we support colleagues' right to join for all UK colleagues in levels 1-5. We believe around half our UK colleagues are union members. We regularly engage with both unions to ensure they are able to contribute to our strategy and ensure we consult with them when making decisions that might affect large numbers of colleagues, such as pay, reward, pensions and job evaluations.

Dialogue with consumer groups, government and regulators
We maintain a regular and open dialogue with the FSA and Financial Ombudsman Service to ensure we are fully aware of, and involved in, the latest consumer and regulatory issues.

Contact with consumer advocates helps to improve the service we provide to our customers. It can give us new perspectives on how we operate, complementing direct feedback from our customers and market research. We frequently engage in dialogue with such groups.

Assessing the issues

The assessment process and prioritising our efforts and resources requires judgement. We evaluate issues against the following criteria:

- Key points raised by our stakeholders.
- How directly an issue affects our core business.
- Financial impact.
- Reputational impact.

Key issues raised by stakeholders:

- Climate change and renewable energy
- Social banking
- Financial capability
- Fees and charges
- Free ATMs

How do we respond?

Below are two case studies showing how HBOS responded to some of these issues during 2007.

Free ATMs

In 2006, we agreed to launch 100 new free ATMs in deprived areas to meet HM Treasury's wish to increase ATM provision in those areas. The ATMs provide customers with free access to cash in communities that have previously had access only to ATMs from fee-charging providers or no access to ATMs at all. We consulted extensively with local stakeholders through 2006 and 2007 on ATM sites, and HBOS has now installed all 100 ATMs.

Fees and charges

A number of stakeholders have raised the issue of unauthorised overdraft fees. In 2007 the major high street banks (including HBOS) and the Office of Fair Trading jointly entered into a High Court test case to obtain a firm legal position on unarranged overdraft charges. In April 2008 the Court issued its judgement that the fees are not penalties, but that they are assessable in UK law for fairness. The Court has not yet ruled on whether the charges are fair or not- this will be decided at a future hearing.

What we recommended	How we performed	Where we can do better
Launch communications campaign to improve dialogue with colleagues on environmental issues.	We launched a major colleague communication campaign including a CO2 calculator, dedicated electronic newsletters and intranet news stories.	Continue to implement a detailed communications campaign on climate change and environmental issues.
Increase engagement with suppliers through suppliers workshops.	HBOS held a major workshop bringing together key suppliers.	Implement a new supplier management framework integrating CR issues into supplier reviews.

Key Performance Indicators

WWDB Principle	KPI	Definition and unit of measurement	2004	2005	2006	2007
Shareholders We will promote the interests of our shareholders by seeking to increase the value of their shares and dividends, and through sound corporate governance"	Return on equity	% post-tax return on mean equity"	19.6%	19.6%	20.8%	19.7%
	Performance of shares versus sector (based on total shareholder return)	% by which the HBOS total shareholder return (TSR) exceeded the weighted average of the comparator group over the performance period	22.9%	22.8%	14.21%	-8.0%
We will communicate with shareholders regularly and in doing so will seek to be clear, comprehensive and balanced	Total number of contacts with investors	Number of meetings held by Investor Relations.	311	323	528	719
Customers We will be honest, fair, professional and open in our dealings with our customers and endeavour to help them at all times"	Customer satisfaction	Proportion of customers who were 'delighted' or 'completely satisfied' with service from HBOS.	53%	53%	59%	59%
We are committed to providing them with value for money products and services, designed and promote in a simple and transparent way, and made as widely available as possible	Independent research on best buys	Number of times an HBOS product was featured in best buy tables	1,666	2,671	3,317	3,912
When things go wrong, as they sometimes do, we will resolve problems as quickly and fairly as we can.	% of customers agreeing that they were satisfied with the way in which their complaint was handled	% who were satisfied with HBOS as identified in 'Service Tracker' research	39%	40%	40%	47%
Colleagues We will create a safe working environment which encourages openness, honesty and mutual respect, and where colleagues can constructively challenge and ask questions."	% colleagues agreeing people are open and honest with each other	% HBOS overall that agree in Colleague Opinion Survey	52%	49%	57%	58%
	% colleagues agreeing it is safe to speak up and challenge the way things are done	% HBOS overall that agree in Colleague Opinion Survey	59%	56%	63%	64%
We will offer equal opportunities for all	% colleagues satisfied that HBOS is committed to improving equal opportunities and diversity throughout the business	% HBOS overall that agree in Colleague Opinion Survey	-	35%	74%	79%
	% colleagues satisfied that HBOS treats colleagues with dignity and respect	% HBOS overall that agree in Colleague Opinion Survey	-	57%	69%	72%

WWDB Principle	KPI	Definition and unit of measurement	2004	2005	2006	2007	
We will offer equal opportunities for all (cont.)	Colleague satisfaction with total reward and benefits	% HBOS overall that agree in Colleague Opinion Survey	59%	58%	64%	66%	
	% colleagues agreeing good performance is fairly rewarded	% HBOS overall that agree in Colleague Opinion Survey	51%	49%	58%	59%	
We will provide the opportunity for all colleagues to develop their skills and knowledge, and to enjoy fulfilling careers.	% colleagues satisfied with opportunities to learn	% HBOS overall satisfied in the Colleague Opinion Survey	53%	56%	65%	67%	
	% colleagues satisfied with coaching and development received from line manager	% HBOS overall always/usually applies in the Colleague Opinion Survey	61%	63%	67%	68%	
Suppliers We will deal openly, fairly and honestly with all our suppliers and business partners. We will not demand of them standards that we do not apply to ourselves, but we will seek to understand their approach before doing business with them	% suppliers paid within agreed timescale as at 31st December	Trade creditors outstanding	15	13	18	20	
Society Our main contribution to Society is the value we can add through our success in business” We will seek to be a positive influence on those social and environmental issues which, having listened responsibly to our shareholders, customers, colleagues and suppliers, we think are important.	Taxation paid	On profit on ordinary activities (£m)	1,272	1,546	1,772	895	
	Dividends paid	Underlying profit attributable to ordinary shareholders based on IFRS (£m)	3,118	3,230	3,879	1,747	
	Annual community spend	HBOS plus HBOS Foundation investment in communities, charities and the sports and arts, (£m)	36.3	43.14	44.16	55.19	
	Total UK greenhouse gas emissions	tonnes CO2 tonnes		162,956	66,811	56,743	53,577
		tonnes CO2/m2					
		tonnes CO2/FTE					
	Waste	Total waste (tonnes)		14,127	13,861	20,590	17,944
% general office waste recycled			45.43	48.8	46.9	51.5	
	Total kg/FTE		248.08	243.3	353.6	302.1	

WWDB Principle	KPI	Definition and unit of measurement	2004	2005	2006	2007
We will seek to be a positive influence on those social and environmental issues which, having listened responsibly to our shareholders, customers, colleagues and suppliers, we think are important. (cont.)	Business travel	car tonnes CO2/FTE	0.161	0.247	0.273	0.269
		train tonnes CO2/FTE	0.005	0.005	0.011	0.024
		plane tonnes CO2/FTE	0.111	0.104	0.234	0.270
		Total CO2/FTE	0.278	0.355	0.518	0.563
	Number of companies Insight Investment engages with per year on corporate governance and corporate responsibility		-	-	228	285
	Annual Financial Inclusion Report				Planned for 2007	Yes
We will observe the laws and regulations of all countries in which we operate, not just in the letter but in the spirit. We will not countenance bribery, corruption or the concealment of conflicts of interest.	Regulatory fines or reprimands.	Number of fines and reprimands	Fines: 4	0	0	0
Community We will contribute to the development of the community outside of our direct business interests by making charitable donations to initiatives relating to financial literacy and money advice, and by providing opportunities for colleagues to support the development of the communities in which they live and work"	Funds raised by colleagues	Total – including £1m Challenge and matched funding (£m)	3.5	3.97	4.62	5.70
	% colleagues who speak highly about the way that HBOS supports volunteering opportunities for colleagues	% HBOS overall that agree in Colleague Opinion Survey	50%	67%	73%	71%
We will measure our progress against this statement and report this regularly to shareholders, customers, colleagues and suppliers	Presence of HBOS in corporate responsibility indices					
	Dow Jones		Yes	Yes	Yes	Yes
	FTSE4Good		Yes	Yes	Yes	Yes
	BITC CR Index		Yes	Yes	Yes	Yes
Wherever possible, we will independently benchmark or verify that WWDB continues to meet stakeholder expectations	Annual independent verification of CR activity		Yes	Yes	Yes	Yes

Independent assurance

Independent Assurance Statement

WSP Environmental (WSP) was commissioned by HBOS plc to conduct independent external assurance of the HBOS Corporate Responsibility Report 2008. The aim of this statement is to provide assurance to stakeholders that the information provided by HBOS in their Corporate Responsibility Report 2008 is appropriate to the nature and activities of HBOS business operations as well as accurate, reliable, objective and has been validated by an independent third party.

Responsibility of WSP

WSP's obligation is to HBOS stakeholders and readers of this statement. WSP is responsible exclusively for the contents of this statement and providing assurance over the scope of data and statements contained in the HBOS Corporate Responsibility Report 2008. WSP has not been involved in the development of the HBOS Corporate Responsibility strategy or preparation of any of the material included in the Corporate Responsibility Report for 2008.

Scope of our assurance

WSP undertook a review of the scope and final content of the HBOS Corporate Responsibility Report 2008 in accordance with the principles of the international AA1000 Assurance Standard which cover:

- Materiality: The CR reporting information includes detail that is material to HBOS stakeholders and is considered by senior management in strategic development.
- Completeness: The CR reporting information indicates comprehensive coverage of CR issues facing HBOS and the systems and management in place.
- Responsiveness to stakeholder concerns: Engagement with stakeholders is clearly stated in the report, with evidence of continuing development in this area on climate change.

Our assurance procedures included:

- Testing on a sample basis;
- Validation processes on data collation methods;
- Validation of Corporate Responsibility practices;
- Validation of performance and non-financial data, including interviews with key personnel.

HBOS provided access to records and data required and WSP is confident that no material information has been withheld.

Excluded from our work are sustainability statements made outside the HBOS Corporate Responsibility Report 2008, statements of commitment or intention and statements of opinion, belief or aspiration. In addition to this statement, an internal management report was produced for HBOS.

Commentary- key highlights

This report, the sixth HBOS Corporate Responsibility Report, demonstrates continuing progress for HBOS in managing and reporting on its CR issues. Highlights for 2008 include:

- Our assurance noted that HBOS has been recognised for their corporate responsibility achievements, reflected in the number of awards received and retained in 2007, as well as their performance in the carbon disclosure project.
- The HBOS Climate Change Action Plan has led to a number of improvements in resource use, recycling and emission reductions and a number of further targets have been set in these areas for the period up until 2010.
- During 2007 HBOS has supported local communities. A total of £55.2 million in total was invested into communities through; volunteering, sponsorship programmes, and grants to provide financial literacy.
- We recognise a committed approach by HBOS on responsible lending through the 'Business Banking Offset Loan' to SMEs and through a Money Management Unit which is designed to identify and assist "borrowers in distress".
- HBOS include reporting on financial inclusion and social banking targets. We noted HBOS exceeded their aim for new social bank accounts by 4.3% and have created a number of links and partnerships with credit unions.



WSP's global corporate services team supports clients in managing and improving their Corporate Responsibility performance including environmental, social and ethical issues.

We work with clients across the industrial, commercial and public sectors, including leading FTSE 100 and Fortune 500 companies as well as innovative small-medium size enterprises. Our global team comprises industry practitioners, consultants and practical specialists working in WSP's offices across the world. Many staff are registered with the Institute of Environmental Management and Assessment (IEMA) as qualified auditors.

Areas for ongoing improvement

The following is a summary of the key areas for comment and improvement, highlighted within the scope of the assurance:

Procurement and the supply chain are briefly mentioned within the report; the main achievements to date are related to the procurement of paper and business cards and engaging with companies on supply chain issues. HBOS should consider extending its reach and influence to their suppliers to encourage environmental compliance and best practice. The commitment HBOS has made to implement a "rigorous model" to help manage the environmental impacts within the supply chain in 2008 will provide a good basis for this.

HBOS ran a number of feedback sessions in 2007 for staff. Areas covered included financial awareness and the HBOS climate change strategy. Following these seminars it is important that HBOS continue to monitor feedback and ensure it is communicated in the most effective and accurate manner.

Key Performance Indicators (KPIs) reflect the changing priorities in the HBOS

Corporate Responsibility agenda, HBOS should however continue to review and update KPIs as appropriate and in line with the GRI.

HBOS could consider developing a more structured approach to the collection of data as the year progresses through the provision of a data library. This will assist with a more streamlined approach to final reporting at the end of the year.

Our assurance opinion

Based on our assurance our opinion is that the HBOS Corporate Responsibility Report

2008 provides a detailed and accurate representation of their activities for the period 1 January 2007 to 31 December 2007.

Prepared by :

Emma Bollan
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August 2008

Reviewed by:

David Symons
Director
August 2008

