

SCOTTISH WIDOWS PLC

REPORT OF THE DIRECTORS

AND

ACCOUNTS

31 DECEMBER 2002

Member of Lloyds TSB Group



Scottish Widows plc
Report and Accounts for the Year Ended 31 December 2002

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Company Information

Board of Directors

G J N Gemmell (Chairman)
A A Knight (Deputy Chairman)

M E Fairey
A J Low
J McConville*
W H Main*
A E Moore
N V Moss*
M D Ross*
I D Thompson*

Secretary

C M Herd

Reporting Actuary

A M Eastwood

Auditors

PricewaterhouseCoopers LLP
Erskine House
68-73 Queen Street
Edinburgh
EH2 4NH

Registered Office

69 Morrison Street
Edinburgh
EH3 8YF

Company Registration Number

199549

* denotes Executive Director

Scottish Widows plc
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Directors' Report

Principal Activity and Review of Business

The principal activity of Scottish Widows plc ("the Company") is the undertaking of ordinary long-term insurance business in the United Kingdom. The Directors consider that the Company's activities will continue unchanged in the foreseeable future.

Results and Dividend

The result for the year ended 31 December 2002 is a profit of £15.9m (2001: restated loss of £61.7m) and has been transferred to reserves. The Directors do not recommend the payment of a dividend for the year (2001: £nil).

Directors

The names of the current Directors are listed on page 2. Particulars of the Directors' emoluments and interests in shares are given in note 7 to the accounts. Changes in directorships during the year are as follows:

L M Urquhart	(resigned 12 March 2002)
N V Moss	(appointed 19 June 2002)
N Scott	(resigned 30 June 2002)

On behalf of the Board of Directors



C M Herd
Edinburgh
20 March 2003

Scottish Widows plc
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Report of the Independent Auditors
To the Members of Scottish Widows plc

We have audited the financial statements which comprise the profit and loss account, the balance sheet and related notes which have been prepared under the accounting policies set out in the statement of accounting policies.

Respective Responsibilities of Directors and Auditors

The Directors are responsible for preparing the annual report including, as described below, the financial statements. The United Kingdom Companies Act 1985 requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company as at the end of the year and of the profit or loss for that year. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping accounting records which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the United Kingdom Companies Act 1985. They are also responsible for safeguarding the assets of the Company and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Scottish Widows plc
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Report of the Independent Auditors
To the Members of Scottish Widows plc (continued)

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2002 and of the profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Edinburgh
20 March 2003

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Technical Account – long-term business

	Notes	2002 £m	(restated) 2001 £m
Earned premiums, net of reinsurance			
Gross premiums written	3(a)	4,175.4	3,602.5
Outward reinsurance premiums		(2,175.7)	(1,062.6)
Investment income	4	922.4	789.0
		<u>2,922.1</u>	<u>3,328.9</u>
Claims incurred, net of reinsurance			
Claims paid:			
Gross amount		(2,158.4)	(2,027.0)
Reinsurers' share		367.1	324.6
Change in the provision for claims : gross amount	16(a)	(18.8)	(0.8)
		<u>(1,810.1)</u>	<u>(1,703.2)</u>
Change in other technical provisions, net of reinsurance			
Long-term business provision, net of reinsurance:			
Gross amount	16(a)	900.0	(836.7)
Reinsurers' share	16(b)	652.4	313.5
		<u>1,552.4</u>	<u>(523.2)</u>
Other technical provisions, net of reinsurance			
Technical provisions for linked liabilities	16	(423.7)	(236.8)
		<u>1,128.7</u>	<u>(760.0)</u>
Net operating expenses	5	(354.5)	(375.5)
Investment expenses and charges	4	(1,103.9)	(951.2)
Unrealised losses on investments	4	(1,385.8)	(1,375.1)
Other technical charges, net of reinsurance		-	(6.0)
Tax attributable to the long-term business	8	137.9	297.6
Transfer from the fund for future appropriations	13	98.1	1,479.6
		<u>(2,608.2)</u>	<u>(930.6)</u>
Balance on the Technical Account – long-term business		<u>(367.5)</u>	<u>(64.9)</u>

The notes on pages 10 to 28 form an integral part of these accounts.

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Non-Technical Account

	Notes	2002 £m	(restated) 2001 £m
Balance on long-term business technical account		(367.5)	(64.9)
Tax attributable to balance on the long-term business technical account		(125.0)	(150.0)
Shareholder's pre tax loss from long-term business		<u>(492.5)</u>	<u>(214.9)</u>
Investment income	4	18.2	4.6
Unrealised gains on investments	4	370.7	-
Loss on ordinary activities before taxation		<u>(103.6)</u>	<u>(210.3)</u>
Taxation on loss on ordinary activities	8	119.5	148.6
Retained profit / (loss) for the financial year	13	<u>15.9</u>	<u>(61.7)</u>

There are no gains and losses arising other than those reported in the Technical and Non-technical Accounts. All activities are continuing.

The notes on pages 10 to 28 form an integral part of these accounts.

Scottish Widows plc
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Balance Sheet

	Notes	2002 £m	2001 £m
ASSETS			
Investments			
Land and buildings	9(a)	1,174.1	1,680.9
Investment in Group undertakings	9(b)	1,456.7	633.8
Other financial investments	9(c)	18,086.0	19,299.8
		<u>20,716.8</u>	<u>21,614.5</u>
Assets held to cover linked liabilities	10	970.1	546.4
Reinsurers' share of technical provisions			
Long-term business provision	16(b)	1,416.0	763.6
Technical provisions for linked liabilities	16(b)	3,955.2	3,130.4
		<u>5,371.2</u>	<u>3,894.0</u>
Debtors			
Debtors arising out of direct insurance operations		24.2	40.7
Other debtors	11	393.9	388.0
		<u>418.1</u>	<u>428.7</u>
Other assets			
Cash at bank and in hand		-	292.4
Prepayments and accrued income			
Accrued interest and rent		161.0	124.2
Deferred acquisition costs		527.9	530.8
Other prepayments and accrued income		13.2	10.9
		<u>702.1</u>	<u>665.9</u>
TOTAL ASSETS		<u>28,178.3</u>	<u>27,441.9</u>

The notes on pages 10 to 28 form an integral part of these accounts.

Scottish Widows plc
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Balance Sheet

	Notes	2002 £m	(restated) 2001 £m
LIABILITIES			
Capital and reserves			
Called-up share capital	12	648.9	101.0
Other reserves	13	2,404.9	3,212.9
Profit and loss account	13	580.2	(307.7)
Equity shareholder's funds	14	3,634.0	3,006.2
Subordinated liabilities	15	-	200.0
Fund for future appropriations	13	-	162.1
Technical provisions			
Long-term business provision	16(a)	19,144.7	20,044.7
Claims outstanding	16(a)	78.0	59.2
		19,222.7	20,103.9
Technical provisions for linked liabilities	16(a)	4,925.3	3,676.8
Provisions for other risks and charges	18	22.6	23.6
Creditors			
Creditors arising out of direct insurance operations		31.0	21.2
Amounts owed to credit institutions		37.6	-
Other creditors including taxation and social security	19	300.9	238.4
		369.5	259.6
Accruals and deferred income		4.2	9.7
TOTAL LIABILITIES		28,178.3	27,441.9

The notes on pages 10 to 28 form an integral part of these accounts.

Approved by the Board on 20 March 2003



M D Ross
Chief Executive

Scottish Widows plc
Report and Accounts for the Year Ended 31 December 2002

Notes to the Accounts

1. Basis of preparation

The accounts have been prepared in accordance with section 255 and Schedule 9A of the Companies Act 1985 which covers the disclosures applicable to insurance companies. The accounts are prepared in accordance with the Association of British Insurers' Statement of Recommended Practice (SORP) on Accounting for Insurance Business issued in December 1998. As the company is a wholly owned subsidiary undertaking of Lloyds TSB Group plc, registered in the United Kingdom, the Company has taken advantage of the provisions of the Companies Act 1985 and has not produced consolidated accounts.

The accounts have been prepared in accordance with applicable accounting standards. Compliance with Statement of Standard Accounting Practice 19 "Accounting for Investment Properties" ("SSAP 19") requires departure from the requirements of the Companies Act 1985 relating to depreciation and an explanation of the departure is given in the accounting policy note relating to investments below.

Accounting policies are unchanged from 2001, except that the Company has implemented the requirements of Financial Reporting Standard 19 ("FRS 19") "Deferred Tax". Following its implementation, the Company makes full provision for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Previously provision was only made where it was considered that there was a reasonable probability that a liability or asset would crystallise in the foreseeable future. A prior year adjustment has been made as at 1 January 2001 to reflect the revised policy which has decreased shareholders' funds by £19.1m and decreased the fund for future appropriations by £141.0m. The effect of the restatement on the prior year profit and loss account has been to increase the tax credit by £136.5m and to reduce the change in the fund for future appropriations by £96.8m. The effect of the change in policy on the Company's balance sheet at 31 December 2002 has been to reduce the deferred tax liability by £20.0m (2001: create a deferred tax liability of £23.6m) and thereby increase shareholder's funds by £20.0m. The effect of the change on the profit and loss account for the year ended 31 December 2002 has been to increase the total tax credit by £43.6m and reduce the change in the fund for future appropriations by £44.2m.

2. Accounting policies

a) Financial Reporting Standard 18 "Accounting Policies"

The Company complies with Financial Reporting Standard 18 "Accounting Policies".

b) Premiums

Premiums earned are accounted for in the year in which they fall due.

c) Investment income

Dividends are included as investment income on the date that the shares become quoted ex-dividend. Interest and rent are included on an accruals basis.

d) Realised gains and losses on investments

Realised gains and losses on investments are calculated as the difference between net sales proceeds and the original cost.

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Notes to the Accounts (continued)

e) Unrealised gains and losses on investments

Unrealised gains and losses on investments are calculated as the difference between the carrying valuation of investments at the Balance Sheet date and the original cost. Movements in unrealised gains and losses on investments arising in the year are shown in the Technical Account.

f) Claims incurred

Death claims and surrenders are recorded on the basis of notifications received. Maturities and annuity payments are recorded when due. Claims payable include direct costs of settlement. Reinsurance recoveries are accounted for in the same period as their related claims.

g) Commission

Commission is accounted for in the Technical Account in the year in which it falls due to be paid.

h) Bonuses

Bonuses charged to the long-term business Technical Account in a given year comprise:

- New reversionary bonuses declared in respect of that year which are provided within the calculation of the long-term business provision;
- Terminal bonuses paid out to policyholders on maturity and included within claims paid.

i) Deferred acquisition costs

The costs of acquiring new insurance contracts which are incurred during a financial period but which relate to subsequent financial periods, are deferred to the extent that they are recoverable out of future revenue margins. Such costs are disclosed as an asset in the Balance Sheet and are determined in respect of conventional assurance business by means of an adjustment applied to the net premium valuation of the long term business provision, grossing up for tax where appropriate. Deferred acquisition costs in respect of term assurances, linked business and unitised with-profits business are determined explicitly. The rate of change of the deferred acquisition cost asset is consistent with a prudent assessment of the expected pattern of receipt of the future revenue margins over the period the relevant contracts are expected to remain in force.

j) Tax

Tax is charged or credited on all taxable profits or losses arising for the accounting period. The taxation charge in the Non-technical Account is based on the taxable profit for the period. In the long-term business Technical Account, the taxation charge or credit is based on a method of assessing taxation for the long-term fund. Any balance on the long-term business Technical Account that is computed on an after tax basis is grossed up at the effective rate of taxation in the Non-technical Account.

Notes to the Accounts (continued)

k) Deferred Tax

Full provision is made for deferred tax liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that there will be suitable tax profits from which the future reversal of the underlying timing differences can be deducted. Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

l) Long-term reinsurance contracts

Long-term business is ceded to reinsurers under contracts to transfer part or all of one or more of the following risks: mortality, morbidity, investment, persistency and expenses. Such contracts are accounted for as insurance contracts.

m) Valuation of investments

The value of investments at the Balance Sheet date is calculated as follows:

- Freehold and leasehold properties are individually valued by external qualified surveyors on the basis of open market value, account being taken of the cost of disposal. The valuation is carried out on an annual basis. Under the Companies Act 1985, land and buildings are required to be depreciated over their expected useful economic lives. In respect of investment properties, this requirement conflicts with the generally accepted accounting principle set out in SSAP 19, that no depreciation should be provided in respect of such investments. The Directors consider that to depreciate investment properties would not give a true and fair view and accordingly the provisions of SSAP 19 have been adopted. Depreciation is only one of the factors reflected in the annual valuations and the amounts which might otherwise have been shown cannot reasonably be separately identified and quantified;
- Listed securities are stated at middle market value;
- Open ended investment companies ("OEICs") are stated at their quoted price;
- Short-term deposits are included at cost;
- Financial futures and option contracts are valued at market rates ruling at the Balance Sheet date and the gain or loss on these contracts is brought into the Technical Account;
- Subsidiaries are valued at their net asset value based on the most recent information available;
- Other investments are stated at Directors' valuation having prudent regard to the likely realisable value.

n) Foreign currency translation

Assets and liabilities in foreign currencies are translated into sterling at the exchange rates ruling at the Balance Sheet date. Revenue transactions and those relating to the acquisition and realisation of investments have been translated at rates of exchange ruling at the time of the respective transactions.

Notes to the Accounts (continued)

o) Long-term business provision

The long-term business provision for the Company is determined on the basis of recognised actuarial methods and in accordance with the FSA Rules, as modified by the Statement of Recommended Practice on Accounting for Insurance Business, and all relevant guidance from the Institute and Faculty of Actuaries.

For conventional with-profits business, a net premium valuation method is used. For conventional with-profits deferred annuities, the liability valued is the higher of the maturity cash benefit or deferred annuity under any guaranteed annuity option applying, subject to the assumed rate of take-up of such options. For other classes, the methods used involve estimating future policy cashflows over the duration of the in-force book of policies, and discounting these cashflows back to the valuation date allowing for the probabilities of occurrence. Assumptions are made in respect of all material factors affecting future cashflows, including future interest rates, mortality and costs. All assumptions are set with a margin for prudence.

The principal assumptions made are the interest rates used to discount the cashflows and the mortality assumptions. These are disclosed in Note 17 to the Accounts. These, and other, assumptions are set as described below.

Interest rates

The higher the assumed rates of interest used to discount the cashflows when valuing the liabilities, the lower the value placed on the liabilities. The rates used are chosen in accordance with the relevant FSA Rules (as set out in the Interim Prudential Sourcebook for Insurers IPRU(INS)). These limit the rates of interest that can be used by reference to a number of factors including the dividend and earnings yields on equities, rental income, and redemption yields on fixed interest assets at the valuation date. When appropriate an adjustment is made to the interest rates used to value conventional with-profits business to allow for future bonuses.

Bonus Rates

The long-term business provision includes explicit provision for declared bonuses added up to and including the reporting date. In addition, explicit allowance for future regular bonus is made in the case of unitised with-profits business, the assumed rates being consistent with the valuation interest rate assumptions.

Mortality and Morbidity

The mortality and morbidity assumptions are set with regard to the Company's actual experience where this provides a reliable basis, and relevant industry data otherwise.

Expenses

Allowance is made for future policy costs on either an explicit or an implicit basis. Where an implicit margin is used, the adequacy of that margin is tested.

Expense loadings are determined by reference to an internal analysis of expense levels. An allowance is made for expense inflation from the valuation date.

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Notes to the Accounts (continued)

p) Fund for future appropriations

The fund for future appropriations comprises amounts which have yet to be allocated to either participating policyholders or shareholders. Transfers between the fund for future appropriations and the long-term business Technical Account represent the changes in these unallocated amounts between Balance Sheet dates.

q) Cash flow statement

A cash flow statement has not been provided as the Company has taken advantage of the exemption contained in Financial Reporting Standard No 1 (Revised) "Cash Flow Statements" as consolidated accounts, in which the Company is included, are available (see note 25).

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Report and Accounts for the Year Ended 31 December 2002

Notes to the Accounts (continued)

3. Segmental analysis

All premiums relate to continuing operations and to direct business.

(a) Gross premiums written	2002 £m	2001 £m
Individual premiums	3,887.2	3,431.8
Premiums under group contracts	288.2	170.7
Total	<u>4,175.4</u>	<u>3,602.5</u>
Regular premiums	1,084.2	955.9
Single premiums	3,091.2	2,646.6
Total	<u>4,175.4</u>	<u>3,602.5</u>
Premiums from non profit contracts	782.8	389.0
Premiums from with profits contracts	1,274.1	2,063.4
Premiums from linked contracts	2,118.5	1,150.1
Total	<u>4,175.4</u>	<u>3,602.5</u>
Premiums from life business	1,953.5	2,084.5
Premiums from annuity business	597.5	341.2
Premiums from pensions business	1,620.5	1,172.8
Permanent Health Insurance	3.9	4.0
Total	<u>4,175.4</u>	<u>3,602.5</u>
(b) Gross new business premiums		
Individual premiums	3,209.6	2,730.0
Premiums under group contracts	167.9	198.7
Total	<u>3,377.5</u>	<u>2,928.7</u>
Regular premiums	286.3	282.1
Single premiums	3,091.2	2,646.6
Total	<u>3,377.5</u>	<u>2,928.7</u>
Premiums from non profit contracts	654.6	278.2
Premiums from with profits contracts	773.5	1,573.8
Premiums from linked contracts	1,949.4	1,076.7
Total	<u>3,377.5</u>	<u>2,928.7</u>
Premiums from life business	1,531.4	1,656.3
Premiums from annuity business	597.5	341.2
Premiums from pensions business	1,241.5	927.4
Permanent Health Insurance	7.1	3.8
Total	<u>3,377.5</u>	<u>2,928.7</u>

Where regular premiums are received other than annually, the regular new business premiums are included on an annualised basis.

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Report and Accounts for the Year Ended 31 December 2002

Notes to the Accounts (continued)

(c) Business segment analysis

In the opinion of the Directors the company operates in a single business segment, that being the provision of long-term insurance.

(d) Geographical analysis

With the exception of £79.2m (2001: £109.9m) premiums written in Jersey, all other premiums were written in the United Kingdom.

(e) Reinsurance balance

The outward reinsurance balance amounted to a debit to the long-term business Technical Account of £265.6m at 31 December 2002 (2001: £143.5m).

4. Total investment return

Technical Account long-term business	2002 £m	2001 £m
(i) Investment income:		
Income from Group undertakings	3.5	3.5
Income from land and buildings	55.8	108.2
Income from investments		
- listed	699.6	579.9
- other	163.5	97.4
	<u>922.4</u>	<u>789.0</u>
(ii) Unrealised losses on investments	(1,385.8)	(1,375.1)
(iii) Investment management expenses, including interest		
Investment management expenses	(13.8)	(17.0)
Interest paid	(5.5)	(4.4)
Losses on the realisation of investments	(1,084.6)	(929.8)
	<u>(1,103.9)</u>	<u>(951.2)</u>
Net investment return included in the long-term business Technical Account	<u>(1,567.3)</u>	<u>(1,537.3)</u>
Non-technical Account	2002 £m	2001 £m
(i) Investment income:		
Income from investments		
- listed	14.5	-
- other	3.7	4.6
	<u>18.2</u>	<u>4.6</u>
(ii) Unrealised gains on investments	370.7	-
Net investment return included in the Non-technical Account	<u>388.9</u>	<u>4.6</u>

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Notes to the Accounts (continued)

5. Net operating expenses

	2002	2001
	£m	£m
Acquisition costs	348.9	303.9
Change in deferred acquisition costs	2.9	52.9
Administrative expenses	68.5	55.2
Reinsurance commissions	(65.8)	(36.5)
	<u>354.5</u>	<u>375.5</u>

- (a) The administration of the Company is undertaken by Scottish Widows Services Limited. A recharge is levied from this undertaking to the Company in respect of those costs incurred on behalf of the Company.
- (b) The Company had no direct employees during the year (2001: nil). The employee costs, including pension costs, are included in the recharge from Scottish Widows Services Limited noted above. The pension scheme operated is primarily a defined benefit scheme, however it is not possible to separately identify the amount of any surpluses or deficits in the scheme which relates to the Company. Details of the pension scheme can be found in the accounts of Scottish Widows Services Limited.
- (c) Included within acquisition costs and administrative expenses are total commissions paid by the Company of £118.1m (2001: £97.7m).
- (d) Included within administration expenses are costs of £23.1m (2001: £18.1m) that relate to the costs of integrating the long-term insurance businesses of Scottish Widows and Lloyds TSB.
- (e) The investment management for the Company is provided by Scottish Widows Investment Partnership Limited and fees are included within investment management expenses.

6. Auditors' remuneration

	2002	2001
	£m	£m
Remuneration paid to PricewaterhouseCoopers		
- as auditors	0.6	0.5
- for other services	1.1	2.1

7. Directors' emoluments and interests

- (a) Directors' emoluments

An apportionment of Directors' emoluments has been made to the Company as follows:

	2002	2001
	£000	£000
Aggregate emoluments	1,279	1,075
Sums paid to third parties for Directors' services	112	88
	<u>1,391</u>	<u>1,163</u>

Retirement benefits are accruing to 5 Executive Directors (2001: 5) under defined benefit schemes.

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Notes to the Accounts (continued)

7. Directors' emoluments and interests (continued)

(b) Highest paid Director

An apportionment of emoluments of the highest paid Director has been made as follows:

	2002	2001
	£000	£000
Aggregate emoluments	<u>411</u>	<u>324</u>
Defined benefits pension scheme accrued benefit at 31 December	<u>274</u>	<u>245</u>

(c) Directors' interests

M E Fairey, G J N Gemmell, A E Moore and M D Ross are also Directors of the Company's ultimate parent company, Lloyds TSB Group plc, and their interests can be found in the accounts of that company.

A A Knight, A J Low, I D Thompson, J McConville, W H Main and N V Moss are also Directors of the Company's intermediate parent company, Scottish Widows Group Limited, and their interests are disclosed in the accounts of that company.

None of the Directors who held office during the year ended 31 December 2002 had any interest in the shares of the Company (2001: none).

8. Taxation on loss on ordinary activities

The Technical Account and Non-technical Account are liable to United Kingdom Corporation Tax on the basis applicable to insurance companies as follows:

Technical Account long-term business

	2002	(restated)
	£m	2001
		£m
UK corporation tax:		
Current tax on profits for the year	(73.4)	(131.6)
Adjustments in respect of prior periods	(66.0)	(3.2)
Double tax relief	(1.4)	(2.2)
	<u>(140.8)</u>	<u>(137.0)</u>
Foreign tax:		
Current tax on profits for the year	3.9	5.4
	<u>(136.9)</u>	<u>(131.6)</u>
Current tax charge		
	<u>(136.9)</u>	<u>(131.6)</u>
Deferred taxation	(1.0)	(166.0)
	<u>(137.9)</u>	<u>(297.6)</u>

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Notes to the Accounts (continued)

8. Taxation on loss on ordinary activities (continued)

Non-technical Account	2002 £m	2001 £m
Tax credit attributable to balance on the long-term business Technical Account	(125.0)	(150.0)
Tax attributable to income arising in the Non-technical Account	5.5	1.4
	<u>(119.5)</u>	<u>(148.6)</u>

The calculation of tax for the year is based on a UK corporation tax rate of 30% (2001: 30%).

A reconciliation of the current tax credit for the year for the Non-technical Account to the credit that would result from applying the standard UK corporation tax rate to the loss before tax is given below:

	2002 £m	(restated) 2001 £m
Loss on ordinary activities before taxation	<u>(103.6)</u>	<u>(210.3)</u>
Loss on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2001: 30%)	(31.1)	(63.1)
Effects of:		
Non-taxable unrealised gains	(111.2)	-
Differences in effective rate on technical account	22.8	(85.5)
Current tax credit	<u>(119.5)</u>	<u>(148.6)</u>

9(a) Land and buildings

	Current value 2002 £m	Cost 2002 £m	Current value 2001 £m	Cost 2001 £m
Freehold occupied by the Company	25.5	27.3	27.3	27.3
Freehold	997.2	939.6	1,452.1	1,399.5
Long leasehold	151.4	130.8	201.5	185.6
	<u>1,174.1</u>	<u>1,097.7</u>	<u>1,680.9</u>	<u>1,612.4</u>

The Company's properties are valued individually at 31 December each year by independent professional valuers and are included in the accounts at these valuations. The valuations are carried out by Messrs Jones Lang LaSalle on an open market basis less an allowance for expenses of sale.

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Notes to the Accounts (continued)

9(b) Investment in Group undertakings

	Current value 2002 £m	Cost 2002 £m	Current value 2001 £m	Cost 2001 £m
Shares	1,334.2	996.9	536.2	473.3
Loans	122.5	248.7	97.6	175.8
	<u>1,456.7</u>	<u>1,245.6</u>	<u>633.8</u>	<u>649.1</u>

9(c) Other financial investments

	Current Value 2002 £m	Cost 2002 £m	Current Value 2001 £m	Cost 2001 £m
Shares and other variable yield securities and units in unit trusts	10,201.7	13,167.3	12,397.4	13,836.0
Debt securities and other fixed income securities	7,873.3	7,497.4	5,361.5	5,258.3
Other loans	7.2	7.2	9.4	9.4
Deposits with credit institutions	3.8	3.8	1,531.5	1,531.5
	<u>18,086.0</u>	<u>20,675.7</u>	<u>19,299.8</u>	<u>20,635.2</u>

The market value above includes the following value of investments listed on a recognised stock exchange:

	Current Value 2002 £m	Current Value 2001 £m
Shares and other variable yield securities and units in unit trusts	8,275.7	11,399.6
Debt securities and other fixed income securities	7,293.1	4,882.6
	<u>15,568.8</u>	<u>16,282.2</u>

10. Assets held to cover linked liabilities

	Current Value 2002 £m	Cost 2002 £m	Current Value 2001 £m	Cost 2001 £m
Assets held to cover linked liabilities	<u>970.1</u>	<u>1,022.4</u>	<u>546.4</u>	<u>566.8</u>

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Notes to the Accounts (continued)

11. Other debtors

	2002	2001
	£m	£m
Amounts due from Group undertakings	169.1	266.1
Other debtors	224.8	121.9
	<u>393.9</u>	<u>388.0</u>

12. Called up share capital

	2002	2001
	£000	£000
Authorised		
648,929,000 (2001: 101,080,000) Ordinary Shares of £1 each	<u>648,929</u>	<u>101,080</u>
Allotted, called up and fully paid		
648,929,000 (2001: 101,080,000) Ordinary Shares of £1 each	<u>648,929</u>	<u>101,080</u>

During the year the share capital of the Company was increased through the creation of 547,849,000 ordinary shares with a par value of £1 each. Of those shares, 140,000,000 were subsequently allotted to the Company's immediate parent undertaking in exchange for cash, and 407,849,000 were allotted to the same undertaking in exchange for the acquisition of Lloyds TSB Life Assurance Company Limited.

13. Reserves

	Other reserves £m	Profit and loss account reserves £m	Fund for future appropriations £m
Balance at 1 January 2001 reported in prior year annual report	3,212.9	(226.9)	1,782.7
Prior year restatement (note 1)	-	(19.1)	(141.0)
Movement for the year recorded in the profit and loss account	-	(61.7)	(1,479.6)
Balance at 31 December 2001	<u>3,212.9</u>	<u>(307.7)</u>	<u>162.1</u>
Movement for the year recorded in the profit and loss account	-	15.9	(98.1)
Other movements	(808.0)	872.0	(64.0)
Balance at 31 December 2002	<u>2,404.9</u>	<u>580.2</u>	<u>-</u>

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Notes to the Accounts (continued)

14. Reconciliation of movements in Shareholder's Funds

	2002 £m	(restated) 2001 £m
Balance at 1 January reported in prior year annual report	-	2,987.0
Prior year restatement (note 1)	-	(19.1)
	3,006.2	2,967.9
Net proceeds of issue of ordinary share capital	547.9	100.0
Profit / (loss) for the financial year	15.9	(61.7)
Transfer from the fund for future appropriations	64.0	-
Balance at 31 December	<u>3,634.0</u>	<u>3,006.2</u>

15. Subordinated liabilities

During the prior year the Company entered into a loan arrangement with a fellow Group company, which during the current year has been subsequently repaid. The loan was made available for a maximum of five years and there was no interest payable on the amount outstanding. In the event of the Company's insolvency, repayment of the loan would have been subordinate to amounts owed to the Company's other creditors, including those liabilities incurred through writing long-term insurance policies.

16. Technical provisions

	Long-term business provision £m	Claims outstanding £m	Technical provision for linked liabilities £m
(a) Gross technical provisions			
Balance at 1 January 2002	20,044.7	59.2	3,676.8
Movement for the year	(900.0)	18.8	1,248.5
Balance at 31 December 2002	<u>19,144.7</u>	<u>78.0</u>	<u>4,925.3</u>
(b) Reinsurers' share			
Balance at 1 January 2002	763.6	-	3,130.4
Movement for the year	652.4	-	824.8
Balance at 31 December 2002	<u>1,416.0</u>	<u>-</u>	<u>3,955.2</u>
(c) Net technical provisions			
Balance at 31 December 2002	<u>17,728.7</u>	<u>78.0</u>	<u>970.1</u>
Balance at 1 January 2002	<u>19,281.1</u>	<u>59.2</u>	<u>546.4</u>

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Notes to the Accounts (continued)

17. Long-term business provision

- (a) The principal assumptions underlying the calculation of the long-term business provision were as follows:

Class of business	2002 Interest Rate (Net) %	2001 Interest Rate (Net) %
Life unitised with-profits		
Flexible Investment and With Profits Bond	3.50	2.25
Flexible Options Bond - Growth Fund	3.25	n/a
Flexible Options Bond - Income Fund	3.75	n/a
Other Assurances	3.50	2.25
Other Life		
Conventional With-Profits	3.75	2.50
Conventional Non-Profit	3.40	3.25
Deferred annuities		
Group pensionplaner – pre/post retirement	4.25	4.25
Unitised with-profits	4.00	3.25
Conventional with-profits individual		
Pre retirement	4.45	3.50
Post retirement	4.45	4.20
Pension Annuities in payment		
Participating	4.75	4.75
Non participating	5.00	5.00
Unitised with-profits	4.50	3.25

The following mortality assumptions (for the main classes of business) are based on the actual experience of the portfolio as well as relevant industry statistics:

Assurances (excluding term assurances)	End-2002	End-2001
Conventional With-Profits & Non Profit Assurances (excluding Term Assurances)		
Males		
Smoker	130% AM92 ult	160% AM80 ult minus 3 years
Non-smoker	65% AM92 ult	80% AM80 ult minus 3 years
Unknown	80% AM92 ult	100% AM80 ult minus 3 years
Females		
Smoker	130% AF92 ult	160% AF80 ult minus 3 years
Non-smoker	65% AF92 ult	80% AF80 ult minus 3 years
Unknown	80% AF92 ult	100% AF80 ult minus 3 years
Unitised Assurances		
Males	55% AM92 ult	As above for Conventional Assurances.
Females	55% AF92 ult	

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Notes to the Accounts (continued)

17. Long-term business provision (continued)

Term	End-2002		End-2001
Assurances			
Sold through LTSB Branch Network	Males		
	Smoker	208% TM92(5) select	As above for Conventional Assurances, but with no age deduction.
	Non-smoker	113% TM92(5) select	
	Unknown	135% TM92(5) select	
	Females		
	Smoker	198% TF92(5) select	As above for Conventional Assurances, but with no age deduction.
	Non-smoker	88% TF92(5) select	
	Unknown	145% TF92(5) select	
	Plus, for AIDS,		
	Males	33.3% of AIDSR6A for calendar year 1998	
Females	10.0% of AIDSR6A for calendar year 1993		
Other Sales			
Males			
Smoker	A varying percentage* between 65% and 155% of TM92 ult	As above for Conventional Assurances.	
Non-smoker	A varying percentage* between 55% and 65% of TM92 ult		
Unknown	A varying percentage* between 55% and 65% of TM92 ult		
Females			
Smoker	A varying percentage* between 55% and 130% of TF92 ult	As above for Conventional Assurances.	
Non-smoker	A varying percentage* between 55% and 80% of TF92 ult		
Unknown	A varying percentage* between 55% and 80% of TF92 ult		
*In both cases with % adjustment for age chosen to be a good fit to recent internal experience.			
Plus, for AIDS,			
Males	33.3% of AIDSR6A for calendar year 1998		
Females	10.0% of AIDSR6A for calendar year 1993		

Annuitants		End-2002	End-2001
Purchased (whole life)	Males	85% IMA92 ult mc	85% IMA92 ult **
	Females	100% IFA92 ult mc	90% IFA92 ult **
Purchased (term)		Valued as annuities certain	Valued as annuities certain
Self-employed / personal pensions	Males	90% RMV92 ult mc	80% RMV92 ult **
	Females	90% RFV92 ult mc	75% RFV92 ult **
Executive Pensions	Males	95% PMA92 ult mc	85% PMA92 ult **
	Females	105% PFA92 ult mc	90% PFA92 ult **
Group scheme annuities	Males	100% PMA92 ult mc	85% PMA92 ult **
	Females	130% PFA92 ult mc	115% PFA92 ult **
Deferred annuities in deferment	Males	70% AM92 ult *	A67/70 minus 9 years (individual), 7 years (group)
	Females	70% AF92 ult *	A67/70 minus 12 years (individual), 10 years (group)

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Notes to the Accounts (continued)

17. Long-term business provision (continued)

With regard to the above tables:

'mc' denotes that explicit provision for future mortality improvement is made by applying the CMI 'Medium Cohort' projection factors to the 1992 base tables (adjusted as above).

* For deferred annuities in deferment an explicit provision for future improvement has been made by assuming mortality in deferment reduces at a rate of 4% pa from the valuation date through deferment.

** For annuities in payment at end-2001 an explicit allowance was made for future improvement in annuitant mortality by applying standard CMIR7 improvement to the 1999 base tables.

Other Assumptions

It is assumed that the take-up rate for guaranteed annuity rates is 95%. This assumption is prudent relative to an analysis of experience in 2002. In the end-2001 valuation a rate of 100% was assumed.

(b) Cost of bonuses

The cost of bonuses declared for the period, including terminal bonuses, totalled £559m (2001: £888m).

18. Provisions for other risks and charges

	2002	(restated)
	£m	2001
		£m
Deferred tax		
Deferred acquisition costs	66.5	68.6
Unrealised capital gains	-	55.4
Pension losses	(20.0)	(22.3)
Other timing differences	(23.9)	(78.1)
	<u>22.6</u>	<u>23.6</u>

Changes in the provisions are as follows:

Balance at 1 January	23.6	189.6
Deferred tax credit recognised in the year	(1.0)	(166.0)
Balance at 31 December	<u>22.6</u>	<u>23.6</u>

- (a) There are realised and unrealised capital losses of approximately £537m and £330m as at 31 December 2002. The deferred tax assets (undiscounted) not recognised on the Balance Sheet are approximately £118m and £73m respectively. These assets will become realised as and when capital gains arise in future periods.

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Notes to the Accounts (continued)

18. Provisions for other risks and charges (continued)

- (b) In December 2002 the Inland Revenue announced its intention to introduce legislation which may affect the tax treatment of certain transfers from the Company's long term business fund to its shareholder's fund. The precise impact of the proposals is still unclear, however it is possible that these transfers will be subject to a higher tax charge than was previously anticipated.

19. Other creditors including taxation and social security

	2002	2001
	£m	£m
Taxation and social security	37.2	35.4
Amounts due to Group undertakings	82.3	112.5
Other creditors	181.4	90.5
	<u>300.9</u>	<u>238.4</u>

20. Assets attributable to the long-term business funds

The total assets shown on page 8 include £21,872.7m (2001: £22,445.1m) attributable to the long-term business funds of the Company.

21. Subsidiary undertakings

The following are particulars of the Company's principal subsidiaries:

Name	Class of Share or Stock	Percentage held	Country of Registration or Incorporation	Nature of Business
Scottish Widows Annuities Limited	Ordinary	100	Scotland	Life Insurance
Lloyds TSB Life Assurance Company Limited	Ordinary	100	England	Life Insurance
Scottish Widows' Fund and Life Assurance Society	Mutual	Sole member	Scotland	Dormant
Pensions Management (SWF) Limited*	Ordinary	100	Scotland	Life Insurance
Scottish Widows Unit Funds Limited	Ordinary	100	Scotland	Life Insurance
Scottish Widows Services Limited	Ordinary	100	Scotland	Management Services

*Limited by guarantee

The above subsidiaries operate in the United Kingdom. A full list of subsidiaries is available with the Annual Return.

Notes to the Accounts (continued)

22. Derivative contracts

At 31 December 2002 the Company and certain subsidiary undertakings had entered into, in the normal course of business, option contracts, index futures contracts and forward foreign exchange contracts. All such contracts were undertaken for either hedging or efficient portfolio management purposes with the exception of certain contracts used for the purpose of matching contractual liabilities. The use of derivative contracts is monitored against approved limits specified by the Board in relation to total and counterparty exposures, and at all times fulfils the conditions referred to in Rule 4.12 of the Interim Prudential Source Book for Insurers.

23. Contingent liability

After an extensive review of the Company's existing practices, carried out in the light of the judgement of the House of Lords in the guaranteed annuities case *Equitable Life v Hyman*, it was announced that the Company was revising the way it calculates benefits for guaranteed annuity policies with effect from 1 February 2002. As a result of this change, the terminal bonuses for Guaranteed Annuity Option policies were increased.

Under the terms of the transfer of the Scottish Widows' business, a separate memorandum account was created within the With Profits Fund called the Additional Account. This account had a value at 31 December 2002 of approximately £1.5 billion (2001: £1.7 billion) and is available to meet any additional costs of providing guaranteed benefits on transferred policies, including guaranteed annuity option policies. The assets allocated to the Additional Account include certain hedge assets, to provide protection to the With Profits Fund against the consequences of a future fall in interest rates.

The eventual cost of providing the enhanced benefits is dependent upon a number of factors, including in particular:

- The proportion of policyholders with a guaranteed annuity option policy who choose to exercise their options;
- The effect of future interest rate and mortality trends on the cost of annuities; and
- The future investment performance of the With Profits Fund.

Having considered a range of possible outcomes, it is currently expected that the most likely outcome is that the balance in the Additional Account available for this purpose will be sufficient to meet the cost of the enhanced benefits payable to the guaranteed annuity option policyholders, as well as other contingencies. The cost of enhanced benefits, currently estimated to be approximately £1.1 billion (2001: £1.4 billion) on a net present value basis, will be paid out over many years as policies mature. In the event that the amount in the Additional Account proves, over time, to be insufficient, the shortfall will be met by the shareholders of the Company. At this time, no provision is considered necessary for such risk.

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Notes to the Accounts (continued)

24. Related party transactions

Advantage has been taken of the exemption under Financial Reporting Standard 8 not to disclose transactions between entities, 90% or more of whose voting rights are controlled within the Lloyds TSB Group, of which the Company is a member.

No contract of significance existed at any time during the period in which a Director or key manager was materially interested or which requires disclosure as a related party transaction as defined under FRS 8 "Related Party Disclosures".

There were no other material transactions by the Company with related parties for the year ended 31 December 2002.

25. Parent undertaking

The Company's immediate parent undertaking is Scottish Widows Financial Services Holdings Limited, a Company registered in the United Kingdom. Scottish Widows Financial Services Holdings Limited has taken advantage of the provisions of the Companies Act 1985 and has not produced consolidated accounts.

Lloyds TSB Group plc is regarded by the Directors as the ultimate parent company and ultimate controlling party of Scottish Widows plc. Copies of the Lloyds TSB Group plc accounts in which the Company is consolidated can be obtained from the Group Secretary's Department, Lloyds TSB Group plc, 25 Gresham Street, London, EC2V 7HN.