SCOTTISH WIDOWS PLC

DIRECTORS' REPORT

AND

FINANCIAL STATEMENTS

31 DECEMBER 2011

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Member of Lloyds Banking Group plc

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COMPANY INFORMATION

Board of Directors

Dr N M Bryson (Interim Chairman)

R J M Bulloch*
M Christophers
J Goford
A M Peck
G N Stewart*
T E Strauss*
D J Walkden*

Company Secretary

C M Herd

Actuarial Function

C M Murison

Independent Auditors

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Erskine House
68-73 Queen Street
Edinburgh
EH2 4NH

Registered Office

69 Morrison Street
Edinburgh
EH3 8YF

Company Registration Number

SC199549

* denotes Executive Director

DIRECTORS' REPORT

Principal activities and review of business

The Directors present the audited consolidated financial statements of Scottish Widows plc ("the Company") and its subsidiary undertakings (together referred to as "the Group"). The Company is a limited liability company domiciled and incorporated in the United Kingdom. Details of the most significant subsidiary undertakings are given in note 17.

The principal activity of the Group is the undertaking of ordinary long-term insurance and savings business and associated investment activities in the United Kingdom. The Group also has branches operating within the EU, which write a relatively small amount of business, principally in Germany. The Group offers a wide range of life insurance products such as annuities, pensions, whole life, term life and investment type products through independent financial advisers, the Lloyds Banking Group ("LBG") network and direct sales. The Company also reinsures business with related undertakings and with insurance entities external to the Group. This includes the majority of the pensions linked business, which is reinsured to the Company's subsidiary, Scottish Widows Unit Funds Limited ("SWUF"); its annuity business, which is reinsured to the Company's subsidiary, Scottish Widows Annuities Limited ("SWA"); and new protection business, which is reinsured to the Company's subsidiary, Clerical Medical Investment Group Limited ("CMIG").

Acquisition of Clerical Medical Investment Group Limited

On 1 July 2011, as a result of a restructuring project to integrate and simplify the Insurance Division legal entity structure and improve the capital efficiency within LBG, the Company acquired the entire share capital in CMIG from a fellow subsidiary of LBG for consideration of £1,846m. The principal activity of CMIG is the undertaking of ordinary long-term insurance and savings business and associated investment activities. The acquisition was partly funded by an increase in the Company's share capital of £821m by the Company's immediate parent (see note 26). Full details can be found in note 3.

During the year, the Company entered into an agreement with Scottish Widows Financial Services Holdings ("SWFSH") to sell CMIG to SWFSH at fair value (with a minimum value of zero) should there be an event that reduced CMIG's capital in excess of its regulatory requirement to nil.

German Insurance Business Litigation

CMIG has received a number of claims in the German courts, relating to policies issued by CMIG but sold by independent intermediaries in Germany, principally during the late 1990s and early 2000s. CMIG has won the majority of decisions to date, although a small number of regional district and appeal courts have found against CMIG on specific grounds. CMIG's strategy includes defending claims robustly and appealing against adverse judgments. The ultimate financial effect, which could be material, will only be known once all relevant claims have been resolved. However, consistent with this strategy, and having regard to the costs involved in managing these claims, and the inherent risks of litigation, the Group recognised a provision of £175m. Management believes this represents the most appropriate estimate of the financial impact, based upon a series of assumptions, including the number of claims received, the proportion upheld, and resulting legal and administration costs.

The Group will re-evaluate the assumptions underlying its analysis at each reporting date as more information becomes available. As noted above, there is inherent uncertainty in making estimates; actual results in future periods may differ significantly from the amount provided.

Results and dividend

The result of the Group for the year ended 31 December 2011 is a profit after tax of £282m (2010: £248m) and this has been transferred to reserves. The result reflects the impact of the acquisition of CMIG and its subsidiaries referred to earlier in this report and market conditions over 2011. Significant losses arose in respect of investments held by the Group, these were partially offset by gains. As the majority of assets held by the Group back policyholder liabilities, there was also a consistent change in the value of insurance and investment contract liabilities over the course of 2011. The Directors consider the result for the year to be satisfactory in light of these factors.

During the year, no interim dividends (2010: £210m) were paid. The Directors do not recommend payment of a dividend in respect of the year ended 31 December 2011.

Key performance indicators

Total insurance premiums received from policyholders were £6,948m (2010: £4,726m). Of this, £5,413m (2010: £4,016m) was recognised in the statement of comprehensive income, with the remainder being subject to deposit accounting as set out in accounting policy 1(aa). The increase largely reflects the impact of the acquisition of CMIG and its subsidiaries referred to earlier in this report.

Funds under management, excluding cross holdings, were £89,143m (2010: £48,606m). The increase reflects the inclusion of funds under management by CMIG and its subsidiaries.

The Directors believe that the Company currently has adequate capital resources and will continue to do so in the foreseeable future. Further information on the capital position of the Company is given in note 42. The Directors consider that the above key performance indicators, together with the disclosures contained in the LBG accounts, are appropriate to the principal activity of the Company. In addition, the Directors are of the opinion that the Company's FSA returns' capital resource requirement information and regular actuarial reports, in conjunction with the information presented in the financial statements as a whole, provide the management information necessary for the Directors to understand the development, performance and position of the business of the Company. Along with fellow direct and indirect subsidiaries of the ultimate insurance parent undertaking, the Group is included in the calculation of the Scottish Widows Group capital requirement. This is calculated in accordance with the Insurance Group Directive.

The Company also forms part of LBG. The development, performance and position of the Scottish Widows group companies are presented within LBG's annual report, which does not form part of this report.

Future outlook

The Directors consider that the Group and Company's principal activities will continue unchanged in the foreseeable future.

Principal risks and uncertainties

The management of the business and the execution of the Company's and Group's strategy are subject to a number of risks. The financial risk management objectives and policies of the Company and Group and the exposure to market, insurance, credit, financial soundness and operational risk are set out in note 42.

In addition, the Company and Group are also exposed to financial and prudential regulatory reporting risk, in particular the risk of reputational damage, loss of investor confidence and/or financial loss arising from the adoption of inappropriate accounting policies, ineffective controls over financial reporting or over prudential regulatory reporting and financial reporting fraud. The financial and risk management objectives and policies of the Company and Group in respect of financial and prudential regulatory reporting risk are also set out in note 42.

The Group, like other insurers, is subject to legal proceedings in the normal course of business. Whilst it is not practicable to forecast or determine the final results of all pending or threatened legal proceedings, management does not believe that such proceedings, including litigation, will have a material effect on the results and financial position of the Group except for the German insurance business litigation, for which a provision has been established, as discussed earlier in this report and set out in note 32.

Directors

The names of the current Directors are listed on page 3. Changes in directorships during the year and since the end of the year are as follows:

A G Kane	(resigned 19 May 2011)
K Luscombe	(resigned 25 May 2011)
P D Loney	(resigned 27 September 2011)
R Harris	(appointed 25 August 2011, resigned 29 February 2012)
T E Strauss	(appointed 17 October 2011)
G N Stewart	(appointed 15 December 2011)
D J Walkden	(appointed 1 January 2012)
R J M Bulloch	(appointed 1 January 2012)
Lord A P Leitch	(resigned 29 February 2012)

Particulars of the Directors' emoluments are set out in note 43.

All Directors have the benefit of a contract of indemnity, which is both a Qualifying Third Party Indemnity Provision and a Qualifying Pension Scheme Indemnity Provision. This was in force during the whole of the year. Directors no longer in office but who served on the Board at any time in the year had the benefit of this contract of indemnity during that period of service.

Disclosure of information to auditors

Each person who is a Director at the date of approval of this report confirms that, so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware and each Director has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information. This confirmation is given, and should be interpreted in accordance with, the provisions of the Companies Act 2006.

Employees

The Lloyds Banking Group is committed to providing employment practices and policies which recognise the diversity of the workforce and ensure equality for employees regardless of sex, race, disability, age, sexual orientation or religious belief.

In the UK, the Lloyds Banking Group belongs to the major employer groups campaigning for equality for the above groups of staff, including Employers' Forum on Disability, Employers' Forum on Age and Stonewall. The Lloyds Banking Group is also represented on the Board of Race for Opportunity and the Equal Opportunities Commission. Involvement with these organisations enables Lloyds Banking Group to identify and implement best practice for staff.

Employees are kept closely involved in major changes affecting them through such measures as team meetings, briefings, internal communications and opinion surveys. These meetings, briefings and internal communications also serve to achieve a common awareness of the financial and economic factors that affect the performance of the company. There are well established procedures, including regular meetings with recognised unions, to ensure that the views of employees are taken into account in reaching decisions. Schemes offering share options or the acquisition of shares are available for most staff, to encourage their financial involvement in the Lloyds Banking Group. Further details are set out in note 44.

Charitable and political contributions

During the year, the Group made contributions totalling £8,023 (2010: £12,120) for charitable purposes. These donations were made to a variety of children's and cancer charities. The Group made no political contributions (2010: £nil).

Policy and practice on payment of creditors

The Group follows the "Prompt Payment Code" published by the Department for Business Innovation and Skills ("BIS") regarding the making of payments to suppliers. A copy of the code and information about it may be obtained from the BIS website.

The Group's policy is to agree terms of payment with suppliers and these normally provide for settlement within 30 days after the date of the invoice, except where other arrangements have been negotiated. It is the policy of the Group to abide by agreed terms of payment, provided the supplier performs according to the terms of contract.

The processing of invoices from suppliers and settlement of trade creditors is undertaken by a separate company within the Scottish Widows Group. As the Company owed no amounts to trade creditors at 31 December 2011 (2010: £nil), the number of days shown in this report, to comply with the provisions of the Companies Act 2006, is nil (2010: nil).

Statement of Directors' responsibilities

The Directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors have prepared the Group and Parent Company financial statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union. Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union 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 adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Company's website www.scottishwidows.co.uk. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors, whose names are listed on page 3, confirm that, to the best of their knowledge:

- the Group and Company financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group and Company; and
- the Directors' Report on pages 4 to 7 includes a fair review of the development and performance of the business and the position of the Group and Company, together with a description of the principal risks and uncertainties that it faces.

On behalf of the Board of Directors

C M Herd
Company Secretary
29 March 2012

INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF SCOTTISH WIDOWS PLC

We have audited the Group and parent Company financial statements (the "financial statements") of Scottish Widows plc for the year ended 31 December 2011 which comprise the Consolidated Statement of Comprehensive Income, the Group and Company Balance Sheets, the Group and Company Statements of Cash Flows, the Group and Company Statements of Changes in Equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Respective responsibilities of directors and auditors
As explained more fully in the Directors' Responsibilities Statement set out on page 6, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements
In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 December 2011 and of the Group's profit and Group's and parent Company's cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matter prescribed by the Companies Act 2006
In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception
We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

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

Karyn Lamont

Karyn Lamont (Senior Statutory Auditor)
For and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Edinburgh
29 March 2012

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2011

	Notes	2011 £ m	2010 £ m
		Group	*Group*
Revenue			
Gross earned premiums	4	5,413	4,016
Premiums ceded to reinsurers		(224)	(217)
Premiums net of reinsurance		5,189	3,799
Fee and commission income	5	378	324
Investment income	6	3,006	2,186
Net (losses)/ gains on assets and liabilities at fair value though income	7	(2,276)	3,607
Other income	8	244	222
Total revenue		6,541	10,138
Expenses			
Gross claims and benefits paid		6,154	4,134
Claims recoveries from reinsurers		(74)	(92)
		6,080	4,042
Change in insurance contract and participating investment contract liabilities		(459)	3,796
Change in non-participating investment contract liabilities		(359)	1,437
Change in reinsurers' share of liabilities		68	(356)
Change in unallocated surplus		(366)	(3)
		(1,116)	4,874
Net (loss)/ profit attributable to external interests in mutual investment funds		(324)	161
Operating expenses	9	1,234	589
Expenses for asset management services received		139	76
Finance costs	12	137	65
		1,186	891
Total expenses		6,150	9,807
Profit before tax		391	331
Taxation (charge)/credit	13	(109)	(82)
Profit for the year		282	249
Other comprehensive income			
Amortisation of actuarial losses	33	-	(1)
Movement in net investment hedges, net of tax		(3)	-
Currency translation differences, net of tax		3	-
Total comprehensive income for the year		282	248
Total comprehensive income for the year attributable to :			
- equity holder of the Company		282	248
		282	248

The notes set out on pages 13 to 88 are an integral part of these financial statements.

BALANCE SHEETS AS AT 31 DECEMBER 2011

	Notes	2011 £ m	2011 £ m	2010 £ m	2010 £ m
		Group	*Company*	*Group*	*Company*
ASSETS					
Retirement benefit surplus	33	115	-	88	-
Intangible assets including insurance intangible assets	14	2,633	-	263	-
Deferred costs	15	1,072	450	1,002	475
Deferred tax assets	16	485	716	325	627
Investment in subsidiaries	17	-	8,046	-	1,892
Property and equipment	18	100	19	102	20
Investment properties	19	4,397	1,402	2,603	1,464
Assets arising from reinsurance contracts held	20	4,720	33,017	2,824	31,116
Current tax receivables	16	238	20	198	139
Investment in joint ventures	21	76	51	61	34
Prepayments		281	30	54	31
Financial assets:					
Derivative financial instruments	22	1,390	225	314	177
Loans and receivables	23	19,077	1,180	2,124	1,749
Investments at fair value through income	24	89,849	16,629	57,405	23,518
Cash at bank		989	48	505	42
Total assets		125,422	61,833	67,868	61,284
EQUITY AND LIABILITIES					
Capital and reserves attributable to Group's equity shareholder					
Share capital	26	1,470	1,470	649	649
Other reserves	27	1,254	1,254	1,254	1,254
Retained earnings		3,565	1,646	1,663	1,350
Total equity		6,289	4,370	3,566	3,253
Liabilities					
Insurance contract and participating investment contract liabilities	29	69,718	38,896	40,202	38,066
Unallocated surplus	30	298	239	325	325
		70,016	39,135	40,527	38,391
Future profits on non-participating business in the With Profits Fund	31	(45)	(45)	(86)	(86)
Retirement benefit obligations	33	27	-	26	-
Deferred tax liabilities	16	968	187	410	247
Current tax payables	16	163	-	93	-
Provisions for other liabilities and charges	32	172	-	5	-
Accruals and deferred income	34	251	1,355	257	1,227
Financial liabilities:					
Subordinated debt	35	1,875	1,424	1,410	1,410
Non-participating investment contract liabilities	36	26,374	13,686	16,226	13,852
Derivative financial instruments	22	1,162	628	453	334
Other financial liabilities	37	2,235	1,089	3,131	2,652
External interests in mutual investment funds		15,928	-	1,839	-
Borrowings	38	7	4	11	4
Total liabilities		119,133	57,463	64,302	58,031
Total liabilities and equity		125,422	61,833	67,868	61,284

The notes set out on pages 13 to 88 are an integral part of these financial statements.

Approved by the Board on 29 March 2012

G N Stewart
Director

STATEMENTS OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2011

	Notes	2011 £m		2010 £ m	
		Group	*Company*	*Group*	*Company*
Cash flows from operating activities					
Profit before tax		391	257	331	133
Adjusted for:					
Depreciation of property and equipment	18	9	1	11	1
Amortisation and impairment of intangible assets	14	200	-	74	-
Finance costs		137	99	65	64
Dividends received				-	(40)
Actuarial losses	33	-	-	(1)	-
Net decrease/(increase) in operating assets and liabilities	39	15,820	765	315	178
Taxation paid		(63)	8	(74)	(72)
Net cash flows from operating activities		16,494	1,130	721	264
Cash flows from investing activities					
Acquisition of subsidiary	3	(772)	(1,846)	-	-
Purchase of property and equipment	18	(6)	-	(5)	-
Additions to intangible assets	14	(63)	-	(56)	-
Dividends received		-	-	-	40
Net cash flows from investing activities		(841)	(1,846)	(61)	40
Cash flows from financing activities					
Proceeds from issue of share capital	26	821	821	-	-
Dividends paid	40	-	-	(210)	(210)
Finance costs paid		(137)	(99)	(65)	(64)
Net cash flows from financing activities		684	722	(275)	(274)
Net increase/(decrease) in cash and cash equivalents		16,337	6	385	30
Cash and cash equivalents at the beginning of the year		494	38	109	8
Net cash and cash equivalents at the end of the year	25	16,831	44	494	38

The notes set out on pages 13 to 88 are an integral part of these financial statements.

STATEMENTS OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2011

Group

	Notes	Issued share capital £ m	Retained earnings £ m	Other reserves £ m	Total attributable to owner of the parent £m
Balance as at 1 January 2010		649	1,625	1,254	3,528
Profit for the year		-	249	-	249
Other comprehensive income					
Amortisation of actuarial losses	33	-	(1)	-	(1)
Dividends paid	40	-	(210)	-	(210)
Balance as at 31 December 2010		649	1,663	1,254	3,566
Increase in ordinary share capital	26	821	-	-	821
Profit for the year		-	282	-	282
Other comprehensive income					
Movement in net investment hedges, net of tax		-	(3)	-	(3)
Other movements	3	-	1,620	-	1,620
Currency translation, net of tax		-	3	-	3
Balance as at 31 December 2011		1,470	3,565	1,254	6,289

Company

	Notes	Issued share capital £ m	Retained earnings £ m	Other reserves £ m	Total attributable to owner of the parent £ m
Balance at 1 January 2010		649	1,436	1,254	3,339
Profit for the year		-	125	-	125
Other comprehensive income					
Amortisation of actuarial losses	33	-	(1)	-	(1)
Dividends paid	40	-	(210)	-	(210)
Balance as at 31 December 2010		649	1,350	1,254	3,253
Increase in share capital	26	821	-	-	821
Profit for the year		-	296	-	296
Balance as at 31 December 2011		1,470	1,646	1,254	4,370

Not all of the above amounts can be distributed to the equity holder since the Company is required to meet regulatory capital requirements. Further details are given in note 42.

The notes set out on pages 12 to 88 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011

1. Accounting policies

Summary of significant accounting policies

The Group has identified the accounting policies that are most significant to its business operations and the understanding of its results.

The financial statements comprise the statement of comprehensive income, the balance sheets, the statements of cash flows, the statements of changes in equity and the related notes. The preparation of the financial statements necessitates the use of estimates and assumptions in applying the accounting policies set out on pages 13 to 28. The accounting policies which relate to insurance contract and participating investment contract liabilities (policy w), intangible assets (policy i), deferred costs (policy j), retirement benefit obligations (policy x), taxation (policy u), the ascertainment of fair values of financial assets and financial liabilities (policy r), the determination of impairment losses (policy t) and the calculation of provisions for liabilities and charges (policy y) are those which involve the most complex or subjective decisions or assessments. These estimates and assumptions affect the reported amounts of assets and liabilities, contingent or otherwise, at the reporting date, as well as affecting the reported income and expenses for the year.

In each case, the determination of these assumptions is fundamental to the financial results and position of the Group and Company, and requires management to make complex judgments based on information and financial data that may change in future periods. Although the estimates are based on management's best knowledge of current facts as at the reporting date, the actual outcome may differ from those estimates.

The significant accounting policies adopted in the preparation of the financial statements, which have been consistently applied to all periods presented in these financial statements unless stated otherwise, are set out below.

(a) Basis of preparation

The financial statements of the Group and Company have been prepared:

(1) in accordance with the International Accounting Standards ("IASs") and IFRSs issued by the International Accounting Standards Board and the Standards and Interpretations ("SICs") and International Financial Reporting Interpretations ("IFRICs") issued by its IFRS Interpretations Committee, as endorsed by the European Union;

(2) in accordance with those parts of the Companies Act 2006 applicable to companies reporting under IFRSs;

(3) in respect of the Group's and Company's With Profits Fund liabilities, in accordance with Financial Reporting Standard ("FRS") 27 "Life Assurance" issued by the United Kingdom Accounting Standards Board; and

(4) under the historical cost convention, as modified by the revaluation of investment properties and certain financial assets and financial liabilities at fair value through income, as set out in the relevant accounting policies.

The Directors are satisfied that the Group and Company have adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements of the Group and Company have been prepared on a going concern basis.

In accordance with IAS 1 "Presentation of Financial Statements", assets and liabilities in the balance sheet are presented in accordance with management's estimated order of liquidity. Analysis of the assets and liabilities of the Group and Company into amounts expected to be received or settled within 12 months after the reporting date (current) and more than 12 months after the reporting date (non-current) is presented in the notes.

The Group has taken advantage of the provisions of section 408 of the Companies Act 2006 and has not disclosed a statement of comprehensive income and related notes in respect of the Company.

In previous years the Group has included annual management charges on non-participating investment contracts within change in non-participating investment contract liabilities. In light of developing industry practice, these amounts (2011: £141 million; 2010: £95 million) are now included within fee and commission income.

Standards and interpretations effective in 2011

A number of standards, amendments to and interpretations of published standards which have the potential to impact on the Group's operations have been issued and are mandatory for accounting periods beginning on or after 1 January 2011. Their relevance to the Group's operations is assessed at note 48.

Details of standards and interpretations in issue but which have not been adopted early are set out at note 49.

(b) Basis of consolidation

The assets, liabilities and results of Group undertakings (including special purpose entities) are included in the financial statements on the basis of financial statements made up to the reporting date. Group undertakings include all entities over which the Group has the ability to control the financial and operating policies, which is generally where the Group has a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Group undertakings are fully consolidated from the date on which the ability to exercise control is transferred to the Group and cease to be consolidated from the date on which the ability to exercise control ceases. Mutual investment funds are consolidated where the Group, partly through its long term funds, has a controlling interest, which is generally where the Group has a shareholding of more than one half of the voting rights and the ability to control the Authorised Corporate Director of the mutual investment fund. Amounts payable to external unit holders in respect of mutual investment funds which are consolidated are reported within liabilities as external interests in mutual investment funds.

Intragroup transactions, balances and gains and losses on transactions between Group companies have been eliminated.

All the financial statements included are uniformly prepared in conformity with IFRSs and the Group's accounting policies and have adopted consistent accounting policies as at 31 December 2011.

Minority interests in the net assets of consolidated subsidiaries (other than in investments in mutual investment funds, which are presented as liabilities) are identified separately from the Group's equity. Minority interest consists of the amount of those interests at the date of the original business combination and the minority interest share of changes in equity since that date. Losses applicable to the minority interest share in the subsidiary's equity are allocated against the interests of the Group once all previous minority interest in previous positive changes in equity has been extinguished, except to the extent that the minority has a binding obligation and is able to make additional investment to cover the losses.

(c) Product classification

The Group issues contracts that transfer insurance risk or financial risk or both.

Insurance contracts

Insurance contracts are those contracts which transfer significant insurance risk. Such contracts may also transfer financial risk. As a general guideline, the Group defines as significant insurance risk the possibility of having to pay benefits on the occurrence of an insured event which are significantly more than the benefits payable if the insured event were not to occur. Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly over time.

Investment contracts

Any long term contracts not considered to be insurance contracts under IFRSs because they do not transfer significant insurance risk are classified as investment contracts. Such contracts are further analysed between those with and without a discretionary participation feature ("DPF"). Contracts containing a DPF are referred to as participating investment contracts and those without a DPF as non-participating investment contracts.

A DPF is a contractual right that gives investors the right to receive, as a supplement to guaranteed benefits, additional discretionary benefits or bonuses that are likely to be a significant portion of the total contractual benefits, through participation in the surplus arising from the assets held in the fund. The Group has the discretion within the constraints of the terms and conditions of the instrument to allocate part of this surplus to the policyholders and part to the Group's shareholder. Participating investment contracts are accounted for in the same manner as insurance contracts in accordance with the requirements of IFRS 4 "Insurance Contracts".

Non-participating investment contracts are contracts that neither transfer significant insurance risk nor contain a DPF.

Hybrid contracts

For certain investment contracts within Scottish Widows heritage, the contract can be partly invested in units which contain a DPF and partly in units without. Where switching levels for similar contracts are deemed to be significant, new investment contracts which contain an option to switch into investment contracts with DPF have been classified as participating investment contracts. Where the switching levels are not deemed to be significant, a new contract is split, with units containing a DPF being allocated as a participating investment contract and the units without a DPF as a non-participating investment contract. Investment contracts which were in force when IFRS was implemented in 2005 were classified according to the switching levels observed at the time and retain their original classification.

For certain investment contracts within Clerical Medical heritage, the contract can be partly invested in units which contain a participating feature and partly without. Where the contract is split, part is allocated as a non-participating investment contract and part as a participating investment contract.

(d) Financial assets and financial liabilities

Management determines the classification of its financial assets and financial liabilities at initial recognition. Management's policies for the recognition of specific financial assets and financial liabilities, as identified on the balance sheet, are set out under the relevant accounting policies.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all of the risks and rewards of ownership. Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled or expires.

All financial assets and financial liabilities are designated at fair value through income, with the exception of certain loans and receivables, borrowings and other financial liabilities which are stated at amortised cost (as described in policies (q), (ac) and (ae)) and derivatives (policy p). The classification depends on the purpose for which the financial assets and financial liabilities were acquired. Certain financial assets and financial liabilities, whose default accounting treatment would be to record these balances at amortised cost, are instead designated at fair value through income as they are held to match insurance and investment contract liabilities linked to the changes in fair value of these assets and liabilities, thereby reducing measurement inconsistencies, and reflecting the fact that these are managed and their performance evaluated on a fair value basis. Information on these balances is provided internally on a fair value basis to the Group's key management. The Group's investment strategy is to invest in equity and debt securities, investment property, derivatives and cash and to evaluate the Group's investments with reference to their fair values.

Fair value methodology

All financial instruments carried at fair value are categorised into a "fair value hierarchy" as follows:

(i) Level 1

Valued using quoted prices (unadjusted) in active markets for identical assets and liabilities to those being valued. An active market is one in which similar arm's length transactions in the instrument occur with both sufficient frequency and volume to provide pricing information on an ongoing basis. Examples include listed equities, listed debt securities, Open Ended Investment Companies ("OEICs") and unit trusts traded in active markets and exchange traded derivatives such as futures.

(ii) Level 2

Valued using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices). If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. Level 2 inputs include the following:

- Quoted prices for similar (but not identical) instruments in active markets;
- Quoted prices for identical or similar instruments in markets that are not active, where prices are not current, or price quotations vary substantially either over time or among market makers;
- Inputs other than quoted prices that are observable for the instrument (for example, interest rates and yield curves observable at commonly quoted intervals and default rates);
- Inputs that are derived principally from, or corroborated by, observable market data by correlation or other means.

Examples of these are securities measured using discounted cash flow models based on market observable swap yields, and listed debt or equity securities in a market that is inactive.

(iii) Level 3

Valued using inputs for the asset or liability are not based on observable market data (unobservable inputs). Unobservable inputs may have been used to measure fair value where observable inputs are not available. This approach allows for situations in which there is little, if any, market activity for the asset or liability at the measurement date (or market information for the inputs to any valuation models). Unobservable inputs reflect the assumptions the Group considers that market participants would use in pricing the asset or liability, for example private equity investments held by the Group and Company.

Where estimates are used, these are based on a combination of independent third-party evidence and internally developed models, calibrated to market observable data where possible.

Further analysis of the Group's and Company's instruments held at fair value is set out at note 42.

The Group's management, through a fair value pricing committee, review information on the fair value of the Group's financial assets and financial liabilities and the sensitivities to these values on a regular basis.

No assets are classified as held-to-maturity or available-for-sale. Derivative assets (other than a derivative which is a designated and effective hedging instrument) are classified as held for trading. With the exception of derivative liabilities, no liabilities are classified as held for trading. Further information on derivatives is set out at policy (p).

Transaction costs incidental to the acquisition of a financial asset are expensed through the statement of comprehensive income, within net gains and losses on assets and liabilities at fair value through income. On disposal, those transaction costs become realised and are expensed through the statement of comprehensive income, within net gains/ (losses) on assets and liabilities at fair value through income.

Financial assets and financial liabilities are offset and the net amount reported in the balance sheet only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

(e) Revenue recognition

Premium income

Premiums received in respect of life insurance contracts and participating investment contracts are recognised as revenue when they become payable by the policyholder and are shown before deduction of commission. Premiums ceded to reinsurers are recognised when the related gross premiums are recognised. Gross and ceded premiums are recorded through the relevant lines in the statement of comprehensive income.

Fee and commission income

The Group receives ongoing investment management fees which are recognised as revenue as the services are provided.

The Group also receives initial investment management fees in the form of an adjustment, or charge, to the amount invested. These fees are in respect of services rendered in conjunction with the issue and management of investment contracts where the Group actively manages the consideration received from its customers to fund a return that is based on the investment profile that the customer selected on origination of the contract. These services comprise an indeterminate number of acts over the lives of the individual contracts and, therefore, the Group defers these fees and recognises them on a straight-line basis over the estimated lives of the contracts unless there is evidence to support an alternative recognition basis. Where an alternative recognition basis is applied, this is calculated by reference to experience information in respect of the period over which income from contracts is earned. The income is recognised through the statement of comprehensive income, within fee and commission income. The liability is recognised in the balance sheet within accruals and deferred income until recognition criteria are met.

Net gains and losses on assets and liabilities at fair value through income

Net gains and losses on assets and liabilities at fair value through income includes both realised and unrealised gains and losses. Movements are recognised in the statement of comprehensive income in the period in which they arise.

Investment income

Interest income for all interest-bearing financial instruments is recognised in the statement of comprehensive income as it accrues, within investment income.

Dividends receivable in respect of listed shares and OEICs are recognised on the date that these are quoted ex-dividend; other dividend income is recognised when received. All dividends received are recognised through the statement of comprehensive income, within investment income.

Rental income in respect of investment properties is recognised on a straight line basis over the term of the lease. The cost of incentives are recognised as a reduction of total income over the term of the lease on a straight line basis.

Other income

Other income recognised in the statement of comprehensive income comprises recharges of costs incurred in respect of several subsidiaries of the Lloyds Banking Group which are not consolidated in these financial statements. Income is recognised as the related expenses are incurred.

(f) Expense recognition

Claims

Claims are recorded as an expense on the earlier of the maturity date or the date on which the claim is notified. Claims recoveries from reinsurers are recognised when the related claims are recognised. Claims and claims recoveries are recognised through the relevant lines in the statement of comprehensive income. Claims handling costs and interest on late claims are also included in claims.

Operating expenses

Commission paid in respect of the business written by the Group is recognised through the statement of comprehensive income, within operating expenses. Where certain criteria are met, commission and other acquisition costs may be deferred. The circumstances under which such costs are deferred are set out at policy (j).

Other operating expenses are recognised in the statement of comprehensive income as incurred, within operating expenses.

Expenses for asset management services received

Expenses for asset management services received are recognised in the statement of comprehensive income as they accrue, within expenses for asset management services received.

Finance costs

Interest expense for all interest-bearing financial instruments is recognised in the statement of comprehensive income as it accrues, within finance costs.

(g) Leases

Assets leased to or from third parties, including properties leased to tenants, are classified as finance leases if the lease agreements transfer substantially all the risks and rewards of ownership to the lessee; all other leases are classified as operating leases. Operating lease rental income and expenditure are recognised on a straight-line basis over the life of the leases through the statement of comprehensive income, within investment income and operating expenses respectively.

Properties leased out to tenants under operating leases are included in investment properties in the balance sheet.

(h) Share-based payments

Employees of the Group participate in a number of equity-settled, share-based compensation plans operated by LBG. The value of the employee services received in exchange for equity instruments granted under these plans is recognised as an expense over the vesting period of the instruments. This expense to the Lloyds Banking Group, of which an element is recharged to the Group, is determined by reference to the fair value of the number of equity instruments that are expected to vest. The fair value of equity instruments granted is based on market prices, if available, at the date of grant. In the absence of market prices, the fair value of the instruments at the date of grant is estimated using an appropriate valuation technique, such as a Black-Scholes option pricing model. The determination of fair values excludes the impact of any non-market vesting conditions, which are included in the assumptions used to estimate the number of options that are expected to vest. At each reporting date, this estimate is reassessed and, if necessary, revised. Any revision of the original estimate is recognised in the statement of comprehensive income over the remaining vesting period, within operating expenses.

(i) Intangible assets including insurance intangible assets

(i) Acquired value of in-force business

Insurance and investment contracts acquired in business combinations are measured at fair value at the time of acquisition. This measurement includes the recognition of an acquired value of in-force ("acquired VIF") asset which reflects the present value of future cash flows expected from the business acquired. The asset is shown gross of attributable tax and a corresponding deferred tax liability has been established. Amortisation of the acquired VIF balance and related tax is carried out on a best estimate basis over the estimated life of the contracts. The amortisation charge for the year is recognised through the statement of comprehensive income, within operating expenses. The carrying value of the acquired VIF balance is tested for impairment at each reporting date. Such an asset is not recognised in respect of future profits on contracts written in the normal course of business, which are recognised in accordance with revenue recognition policy (e).

(ii) Software development costs

Acquired computer software licences are capitalised on the basis of the cost incurred to acquire and to bring to use the specific software. These costs are amortised on a straight-line basis over the expected useful life of the software, not exceeding a period of five years.

Costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets, subject to de minimis limits. Direct costs include the software development team's employee costs and an appropriate portion of relevant overheads. All other costs associated with developing or maintaining computer software programmes are recognised through the statement of comprehensive income as an expense as incurred, within operating expenses.

Computer software development costs recognised as assets are amortised using the straight-line method over their expected useful lives, not exceeding a period of five years. Subsequent expenditure is only capitalised when it increases the expected future economic benefits of the specific asset to which it relates.

The amortisation charge for the year in respect of software licences and software development costs is recognised through the statement of comprehensive income, within operating expenses. The carrying value of the assets is tested for impairment at each reporting date. Further information on the Group's impairment policy is set out at policy (t).

(j) Deferred costs

(i) Deferred acquisition costs

The costs of acquiring new insurance contracts and participating investment contracts (excluding those assessed on a 'realistic basis' in accordance with FRS 27), 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. The deferred acquisition cost asset is amortised over the lifetime of the related contracts based on the pattern of margins arising from these contracts unless there is evidence to support an alternative recognition basis. Where an alternative recognition basis is applied, this is calculated by reference to experience information in respect of the period over which income from contracts is earned. The amortisation charge for the year is recognised through the statement of comprehensive income, within operating expenses. The carrying value of the asset is tested for impairment at each reporting date. Further information on the Group's impairment policy is set out at policy (t).

(ii) Deferred origination costs

Costs which are directly attributable and incremental to securing new non-participating investment contracts are capitalised. This asset is subsequently amortised over the estimated contractual lifetime of each policy on a straight-line basis unless there is evidence to support an alternative recognition basis. Where an alternative recognition basis is applied, this is calculated by reference to experience information in respect of the period over which income from contracts is earned. The amortisation charge for the year is recognised through the statement of comprehensive income, within operating expenses. The carrying value of the asset is tested for impairment at each reporting date. Further information on the Group's impairment policy is set out at policy (t).

(k) Investment in subsidiaries

The Company owns a variety of subsidiaries as set out in note 17. Certain subsidiaries trade with a view to making a profit, and the risks and rewards of owning those subsidiaries primarily rest with the shareholder of the Company. These subsidiaries are held initially at cost, being the fair value of the consideration given to acquire the holding, then subsequently at cost subject to impairment. Further information on the Group's impairment policy is set out at policy (t).

Certain subsidiaries, including holdings in mutual investment funds, are held primarily as vehicles through which specific investments are held as part of the actively managed investment portfolios. These subsidiaries hold assets which are designated at fair value through income in accordance with IAS 39 "Financial Instruments: Recognition and Measurement" and primarily match policyholder liabilities. Accordingly, subsidiaries which are managed as part of policyholder investment funds are carried at fair value and changes in their fair value are reflected in the statement of comprehensive income, within net gains and losses on assets and liabilities at fair value through income.

In addition, ownership of one subsidiary is split between the policyholder and the shareholder of the Company. Such subsidiaries are held initially at cost, being the fair value of the consideration given to acquire the holding, then subsequently at cost subject to impairment. Further information on the Group's impairment policy is set out at policy (t).

(l) Property and equipment

All property (other than investment property) and equipment is stated at cost less accumulated depreciation and any impairment in value. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Subsequent costs are included in an asset's carrying value only when it is probable that future economic benefits related to the asset will flow to the Group and such costs can be measured reliably.

Depreciation of property and equipment is calculated on a straight-line basis to allocate the difference between the cost and the estimated residual value over the estimated useful lives of these assets. The depreciation charge is recognised through the statement of comprehensive income, within operating expenses.

The periods generally applicable are:

- Buildings 40 years
- Fixtures and fittings 15 years
- Furnishings 10 years
- Computer equipment 3 years
- Other equipment 5 years

Land is considered to have an indefinite useful life and is therefore not depreciated.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In the event that an asset's carrying amount is determined to be greater than the recoverable amount, it is written down immediately. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

(m) Investment properties

Investment properties comprise freehold and long leasehold land and buildings, which are held either to earn rental income or for capital appreciation, or both, are initially measured at cost, being the fair value of the consideration given, including directly attributable transaction costs. Subsequently, on a periodic basis and at each reporting date, such properties are carried at fair value as assessed by qualified external appraisers who have recent experience in the relevant location and the category of properties being valued. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, alternative valuation methods such as discounted cash flow analysis or recent prices in less active markets are used. Investment property being redeveloped for continuing use as investment property, or for which the market has become less active, continues to be measured at fair value.

Gains or losses arising from changes in the fair values of investment properties are recognised in the statement of comprehensive income in the period in which they arise, within net gains and losses on assets and liabilities at fair value through income.

(n) Reinsurance

The Group cedes reinsurance in the normal course of business. Where the reinsurance contract transfers significant insurance risk to the reinsurer, the assets arising from reinsurance contracts held are classified as insurance contracts. Where the reinsurance contract does not transfer significant insurance risk to the reinsurer for the assets arising from reinsurance contracts held are classified as a financial asset designated as fair value through income.

Assets arising from reinsurance contracts held – classified as insurance contracts

These assets are recognised within assets arising from reinsurance contracts held. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the underlying contracts and in accordance with the terms of each reinsurance contract. These balances are subject to an annual impairment review. Further information on the Group's impairment policy is set out at policy (t).

Premiums ceded and claims reimbursed are recognised when due and disclosed separately on the face of the statement of comprehensive income. Changes in these assets are recognised on the face of the statement of comprehensive income, through change in assets arising from reinsurance contracts held.

Assets arising from reinsurance contracts held – at fair value through income

Amounts due from reinsurers in respect of contracts that do not transfer significant insurance risk to the reinsurer are designated as fair value through income as this ensures consistency of valuation with the underlying liabilities. These contracts, whilst legally reinsurance contracts, do not meet the definition of a reinsurance contract under IFRSs. Where this is the case, the amounts recoverable have been recognised as a financial asset within assets arising from reinsurance contracts held. Changes in these assets are recognised on the face of the statement of comprehensive income, through change in assets arising from reinsurance contracts held. These balances are subject to an annual impairment review. Further information on the Group's impairment policy is set out at policy (t).

(o) Investment in joint ventures

Joint ventures are entities where the Group has joint control with another party. All joint ventures are held within investment linked insurance funds of the Group and are designated at fair value through income in accordance with IAS 39. Accordingly, the measurement requirements of IAS 31 "Interests in Joint Ventures" do not apply. Changes in the fair value of the investments are recognised in the statement of comprehensive income, within net gains and losses on assets and

liabilities at fair value through income, in accordance with IAS 39. The value of such investments has been separately disclosed within the financial statements.

(p) Derivative financial instruments

Classification

Derivative financial instruments, including embedded derivatives, are held for trading, with the exception of derivatives which are designated as effective hedging instruments, which are held at fair value through income. Derivatives held for trading are used for the purposes of efficient portfolio management or to match contractual liabilities.

Recognition

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value.

Measurement

The best evidence of the fair value of a derivative at initial recognition is the transaction price unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument.

Fair values are obtained from quoted market prices in active markets, including recent market transactions. For over-the-counter ("OTC") derivatives, the value is derived from a hierarchy of valuation sources, as follows:

- primary source – an independent valuation source
- secondary source – generally, this would be the counterparty valuation
- tertiary source – generally, this would be the fund manager valuation

Data from a primary source will initially be used in valuing derivatives. However, tolerance checks are also performed between valuations derived from different sources in order to validate the calculated valuations, detect any potential discrepancies and, if appropriate, select a secondary or tertiary price for use in the valuation instead. If, as a result of this process, a value other than one obtained from a primary valuation source were to be used to value a derivative, this would be approved by the Insurance Investments Strategy Committee.

For exchange traded contracts, the value is based on the quoted bid or ask price at close of business where the contract is an asset held or liability issued. Where the contract is an asset to be acquired or liability held, the value is based on the quoted ask price at close of business.

Changes in the fair value of derivatives are recognised in the statement of comprehensive income, through net gains and losses on assets and liabilities at fair value through income.

Hedge accounting

In limited circumstances, derivatives are designated as fair value hedges. Hedge accounting allows one instrument, generally a derivative such as a swap, to be designated as a hedge of another instrument such as a loan.

Derivatives may only be designated as hedging instruments provided certain strict criteria are met. At the inception of a hedge, its terms must be clearly documented and there must be an expectation that the derivative will be highly effective in offsetting changes in the fair value of the hedged risk. The hedge documentation must also specify the methodology that will be used to measure effectiveness. Changes in the fair value of derivatives that are designated as fair value hedges are recorded in the statement of comprehensive income, through net gains and losses on assets and liabilities at fair value through income, together with the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

The effectiveness of the hedging relationship must be tested throughout its life. A hedge is regarded as highly effective if the change in fair value of the hedge instrument and the hedge item are negatively correlated within a range of 80% to 125%, either for the period since effectiveness was last tested or for the period since inception. Where the hedge is highly effective, the net impact on the statement of comprehensive income is minimised. If, at a reporting date, it is concluded that the hedge is no longer highly effective in achieving its objective, the hedge relationship is terminated. Should this happen, changes in the fair value of the hedged item are no longer recognised in the statement of comprehensive income and the adjustment that has been made to the carrying amount of the hedged item is amortised to the statement of comprehensive income over the period to maturity of the hedged item.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the statement of comprehensive income, together with the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, changes in the fair value of the hedged item attributable to the hedged risk are no longer recognised in the statement of comprehensive income. The cumulative

adjustment that has been made to the carrying amount of the hedged item is amortised to the statement of comprehensive income using the effective interest method over the period to maturity.

Changes in the fair value of derivatives that qualify as a net investment hedge on foreign operations are taken to other comprehensive income when the hedge is deemed to be effective. The ineffective portion of any net investment hedge is recognised in the statement of comprehensive income immediately.

The fair values of derivative instruments used for hedging purposes are disclosed in note 22.

All derivatives are presented as assets when their fair value is positive and as liabilities when their fair value is negative.

(q) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Loans and receivables are initially recognised at fair value less directly attributable transaction costs and subsequently measured at amortised cost, subject to impairment. In practice, the carrying value of these balances equates to the fair value due to the short-term nature of the amounts included within loans and receivables.

A charge for impairment in respect of loans and receivables would be made in the statement of comprehensive income when there is objective evidence that the Group will not be able to collect all amounts due according to their original terms. The impairment charge would be recognised through administration expenses in that part of the statement of comprehensive income. Receivables arising from insurance contracts are also classified in this category and are reviewed for impairment as part of the impairment review of loans and receivables. Such amounts are reflected through the statement of comprehensive income, within gross premiums written and claims recoveries from reinsurers. Further information on the Group's impairment policy is set out at policy (t).

(r) Investments at fair value through income

Investments at fair value through income comprise debt and equity securities.

Classification

A financial asset is classified in this category at inception if acquired principally for the purpose of selling in the short-term, if it forms part of a portfolio of financial assets in which there is evidence of short-term profit-taking, or if designated as such.

Recognition

Purchases and sales of financial assets are recognised on the trade date, i.e. the date the Group commits to purchase the asset from, or deliver the asset to, the counterparty. Investments are initially recognised at cost, being the fair value of the consideration given, and are subsequently remeasured at fair value.

Measurement

The fair values of investments are based on current bid prices. If the market for a financial asset is not active, and also for unlisted securities, the Group establishes fair value by using valuation techniques. These include the use of similar arm's length transactions and reference to other instruments that are substantially the same, making maximum use of market inputs and relying as little as possible on entity-specific inputs. The following paragraphs detail the valuation techniques specific to quoted equity and debt securities.

For equity investments that are quoted and actively traded in organised financial markets, fair value is determined by reference to Stock Exchange quoted market bid prices at the final pricing point on the reporting date. Prices are provided by vendors such as Reuters or Bloomberg or by direct reference to the Stock Exchange.

For quoted debt security investments, bid prices at the final pricing point on the reporting date are obtained from index providers who obtain prices from a number of leading brokers, investment banks and market makers. Where no independent price is available, a valuation technique is used to determine fair value. The technique uses a spread over a comparable term gilt as the best estimate of fair value. Spreads are calculated by reference to the wider market movement in credit spreads, the way in which the security is structured, other assets issued by the issuer or other assets with similar characteristics.

The fair value of holdings in OEICs and Unit Trusts is determined as the last published price applicable to the OEIC sub-fund or the Unit Trust at the reporting date.

For corporate bonds, the Group's management perform a comparison of information received from the index provider used against other available price sources on a monthly basis to ensure that prices can be supported by market data.

In addition to the measurement policies, investment asset prices are reviewed weekly to identify those assets where the price has not moved for at least six days. This review provides an initial indication that the market for each identified asset may be inactive. These assets are then reviewed by management who may identify an alternative price source for assets which in their view are still actively traded. On conclusion that a particular asset is illiquid, management will identify an alternative valuation technique by deciding whether an appropriate price can be obtained from a recognised independent broker. Where this is the case, the broker will be approved as a price source for the asset. A price will then be obtained from the broker on a monthly basis. A review of all illiquid assets and prices obtained or calculated is conducted by the Fair Value Pricing Committee on a monthly basis.

For equity investments such as private equity, fair value is determined by reference to the most recent valuation, adjusted for any cash movements or other relevant information since the last valuation point, which is likely to be up to one quarter prior to the reporting date.

In order to ensure that a fair value is recognised for unquoted or illiquid debt securities, the primary price source is an external broker valuation. If available, a further external broker valuation is sought as a secondary valuation source in order to validate the primary source. A formal review is then carried out which challenges the external valuation and includes consideration of the impact of any relevant movements in underlying variables such as:

- underlying movements in the relevant markets, for example credit spreads;
- how current transactions are being priced in the market;
- how the security is structured; and
- any supporting quantitative analysis as appropriate, for example with reference to Bloomberg or internal models.

Property investments through special purpose vehicles

The Group invests in a number of investment properties through holdings in special purpose vehicles ("SPVs"). Some of these SPVs are consolidated. Unconsolidated SPVs are initially recognised at cost, being the fair value of the consideration given. After initial recognition, such assets are accounted for and measured at fair value, which equates to the relevant proportion of the published net asset value of the company. This valuation is based on open market valuations of the properties held by the SPVs, as provided at the reporting date by independent valuers.

(s) Cash and cash equivalents

Cash and cash equivalents includes cash at bank, short-term highly liquid investments with original maturities of three months or less (excluding such investments as otherwise meet this definition but which are held for investment purposes rather than for the purposes of meeting short-term cash commitments) and bank overdrafts where a legal right of set off exists.

(t) Impairment

Financial assets

The carrying value of all financial assets held at amortised cost is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. The identification of impairment and the determination of recoverable amounts is an inherently uncertain process involving various assumptions and factors, including the financial condition of the counterparty, expected future cash flows, observable fair prices and expected net selling prices.

In order to determine whether financial assets are impaired, all financial assets for which the fair value has fallen below the carrying value (assessed using cost price and the factors above), either by a significant amount or for a prolonged period of time, are individually reviewed. A distinction is made between negative revaluations due to general market fluctuations and due to issuer-specific developments. The impairment review focuses on issuer-specific developments regarding financial condition and future prospects.

Non-financial assets

Assets that have an indefinite useful life, for example land, are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its estimated recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows.

If there is objective evidence that an impairment loss has occurred, the amount of the loss is charged to the relevant line in the statement of comprehensive income in the period in which it occurs. Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

Impairment process

Objective evidence that an asset or group of assets is impaired includes observable data that comes to the attention of the Group and Company about the following events:

(i) significant financial difficulty of the issuer or debtor;
(ii) a breach of contract;
(iii) the disappearance of an active market for that asset because of financial difficulties; or
(iv) observable data indicating that there is a measurable decrease in the estimated future cash flow from a group of assets since the initial recognition of those assets, even where the decrease cannot yet be identified with the individual assets of the Group or Company, including:
- adverse changes in the payment status of issuers or debtors; or
- national or local economic conditions that correlate with defaults on the assets in the Group or Company.

The Group first assesses whether objective evidence of impairment exists individually for assets that are individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed asset, whether significant or not, it includes the asset in a group of assets with similar credit risk characteristics and collectively assesses them for impairment. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the issuer's ability to pay all amounts due under the contractual terms of the debt instrument being evaluated. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

(u) Taxes

Tax on the profit or loss for the year is recognised in the statement of comprehensive income within taxation and comprises current and deferred tax.

Current tax

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at the reporting date, together with adjustments to estimates made in prior years.

Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that, at the time of the transaction affects neither accounting nor taxable profit or loss, it is not accounted for. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date.

Deferred income tax assets are only recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences, carry-forward of unused tax assets and unused tax losses can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the deferred income tax asset to be utilised. Deferred tax assets and liabilities held outwith the policyholder liabilities are undiscounted.

Allocation of tax charge between shareholder and policyholders

The tax expense in the statement of comprehensive income is analysed between policyholder and shareholder tax. This allocation is based on an assessment of the rates of tax which will be applied to the returns under current UK tax rules.

(v) Share capital

Shares are classified as equity when there is no obligation to transfer cash or other assets. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax.

Dividends payable

Dividends payable on ordinary shares are recognised in equity in the period in which they are approved.

(w) Insurance contracts and participating investment contracts

The Group issues life insurance contracts to protect customers from the consequences of events (such as death, critical illness or disability) that would affect the ability of the customer or their dependants to maintain their current level of income and also issues pension and annuity contracts. Guaranteed claims paid on occurrence of the specified insured event are either fixed or linked to the extent of the economic loss suffered by the policyholder.

Insurance contracts or participating investment contracts in the Group's With Profits Funds

Liabilities of the Group's With Profits Funds, including guarantees and options embedded within products written by the funds, are accounted for under the "realistic" method in accordance with the requirements of FRS 27. However, in contrast to the approach used for the FSA's realistic capital regime, projected transfers out of the funds into other funds of the Group are not treated as insurance liabilities, but are recorded in unallocated surplus. Changes in the value of these liabilities are recognised in the statement of comprehensive income, through change in insurance contract and participating investment contract liabilities. Liabilities for non-participating policies are included based on the traditional regulatory assessment. The value of future profits on those policies partially offsets the corresponding liability so that the net position is in line with FRS 27.

Insurance contracts or participating investment contracts which are not unit-linked or in the Group's With Profits Funds

The liability is calculated by estimating the future cash flows over the duration of in-force policies and discounting them back to the valuation date, allowing for probabilities of occurrence. The liability will vary with movements in interest rates and with the cost of life assurance and annuity benefits where future mortality is uncertain. Assumptions are made in respect of all material factors affecting future cash flows, including future interest rates, mortality and costs. Changes in the value of these liabilities are recognised in the statement of comprehensive income, through change in insurance contract and participating investment contract liabilities.

Life insurance contracts or participating investment contracts which are unit-linked

Allocated premiums in respect of unit-linked contracts that are either life insurance contracts or participating investment contracts are recognised as liabilities. These liabilities are increased or reduced by the change in the unit prices and are reduced by policy administration fees, mortality and surrender charges and any withdrawals. Where the mortality charges deducted in each period from the policyholders as a group are not considered adequate to cover the expected total death benefit claims in excess of the contract account balances in each period, additional liabilities are established for these claims. Income consists of fees deducted for mortality, policy administration and surrender charges. Interest or changes in the unit prices credited to the account balances incurred in the period are charged as expenses in the statement of comprehensive income, through changes in insurance contract and participating investment contract liabilities. Benefit claims in excess of the account balances incurred in the period are charged as expenses in the statement of comprehensive income, through gross claims and benefits paid.

Unallocated surplus

Any amounts in the With Profits Funds not yet determined as being due to policyholders or the equity holder and projected transfers out of the funds to other funds of the Group are recognised as an unallocated surplus which is shown separately from the other insurance liabilities.

Bonuses

Bonuses in a given year comprise:

- Unit price increases and new reversionary bonuses declared in respect of that year which are provided within the calculation of insurance and investment contract liabilities;
- Terminal and interim bonuses paid out to policyholders on maturity and included within claims paid.

Receivables and payables

Receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders.

(x) Retirement benefit obligations

The majority of individuals employed by the Group are members of the Scottish Widows Retirement Benefit Scheme ("SRBS"). A less significant number of employees are members of other pension schemes (Lloyds Banking Group Pension Schemes Nos 1 and 2) administered by the Lloyds Banking Group (the "Lloyds Schemes"). All schemes are funded through payments to trustee-administered funds, determined by periodic actuarial calculations.

The Group contributes to both the defined benefit and defined contribution elements of the pension schemes in question. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, dependent on one or more factors such as age, years of service and salary. A defined contribution plan is a pension plan under which the Group pays fixed contributions; there is no legal or constructive obligation to pay further contributions.

Scottish Widows Retirement Benefit Scheme

A full actuarial valuation of this defined benefit scheme is carried out every three years with interim reviews in the intervening years; the valuation is updated to 31 December each year by a qualified actuary. For the purposes of these annual updates scheme assets are included at their fair value and scheme liabilities are measured on an actuarial basis using the projected unit credit method adjusted for unrecognised actuarial gains and losses. The actuary is an employee of the Company.

The amount recognised in the balance sheet in respect of the defined benefit element of the pension scheme is the present value of the defined benefit obligation at the reporting date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs, all as adjusted to exclude the portion of the pension scheme transactions and balances relating to employees of the Scottish Widows Investment Partnership Group Limited ("SWIP Group"), which are presented in the SWIP Group financial statements. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates equivalent to the market yields at the reporting date on high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity that are approximate to the terms of the related pension asset/liability.

A surplus is only recognised to the extent that it is recoverable through a contractual right to make reduced contributions in the future or to receive a refund from the scheme.

The Group's statement of comprehensive income includes the current service cost of providing pension benefits, the expected return on the scheme's assets and the interest cost on the scheme's liabilities. The current service cost is recognised within operating expenses and the expected return and interest cost are recognised within other income.

Actuarial gains and losses arising from experience adjustments and changes in the actuarial assumptions are not recognised unless the cumulative unrecognised gain or loss at the end of the previous reporting period exceeds the greater of 10 per cent of the scheme assets or liabilities (the "corridor approach"). In these circumstances, the excess is charged or credited to income over the employees' expected average remaining working lives.

Past service costs are recognised immediately through income, within operating expenses, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the "vesting period"). In this case, the past service costs are amortised on a straight-line basis over the vesting period.

The effect of material changes to the terms of the scheme which reduce benefits are recognised through the statement of total comprehensive income when the curtailments occur.

For the defined contribution element of the scheme, the Group pays fixed contributions. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised in the statement of comprehensive income as an employee benefit expense when they are due, within operating expenses.

Scottish Widows plc share of Lloyds Banking Group defined benefit pension scheme deficit

A small number of employees are members of certain Lloyds Banking Group pension schemes. Accordingly, defined benefit pension scheme accounting, as set out above, has been applied to reflect the Group's share of those schemes' deficits.

Full actuarial valuations of these group-wide schemes are carried out every three years, with interim reviews in the intervening years which are updated by qualified independent actuaries. Scheme assets are included at their fair value. Scheme liabilities are measured on an actuarial basis using the projected unit credit method, adjusted for unrecognised actuarial gains and losses, and are discounted using rates equivalent to the market yields at the reporting date on high-quality corporate bonds that have terms to maturity approximating to the terms of the related pension liability.

The Group's share of the resulting net surplus or deficit, determined on the basis of the Group's cash contributions into the schemes for employee members (calculated in accordance with the rules of each scheme) is included in the consolidated balance sheet. The Group's statement of comprehensive income includes the Group's share of the current service cost of providing pension benefits, the expected return on the schemes' assets, net of expected administration costs, and the interest cost on the schemes' liabilities, which is again determined on the basis of the Group's cash contributions into the schemes for employee members. These amounts are recognised in the same way as the respective amounts in relation to the SRBS. The Group's share of actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions is not recognised unless the cumulative unrecognised gain or loss at the end of the previous reporting period exceeds the greater of 10 per cent of each scheme's assets or liabilities. In these circumstances, the excess is charged or credited to the statement of comprehensive income over the employees' expected average remaining working lives. Past service costs are charged immediately to the statement of comprehensive income, within operating expenses, unless the changes are conditional on the employees remaining in service for a specified period of time. In this case, the past service costs are amortised on a straight-line basis over the vesting period. The effect of material changes to the terms of the scheme which reduce benefits are recognised through the statement of total comprehensive income when the curtailments occur.

Other schemes

Contributions made by the Group to defined contribution schemes are recognised in the statement of comprehensive income as an employee benefit expense when they are due, within operating expenses.

(y) Provisions for other liabilities and charges

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, when it is probable that the obligation will result in an outflow of resources to settle the obligation and when a reliable estimate of the amount of the obligation can be made. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessment of the time value of money and, where appropriate, the risks specific to the liability.

The Group recognises a provision for onerous contracts when the expected benefits to be derived from contracts are less than the unavoidable costs of meeting the obligations under the contracts.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are not recognised in the financial statements but are disclosed unless the likelihood of possible obligations arising is remote.

(z) Subordinated liabilities

Subordinated liabilities comprise dated and undated loan capital and are carried at amortised cost. The undated subordinated liabilities are adjusted for hedged interest rate risk. Changes in the resulting fair value of the undated subordinated debt are accounted for as set out at policy (p). Interest payable is recognised in the statement of comprehensive income, through finance costs.

The subordinated guaranteed bonds are classified as a liability on the basis of the existence of a capital disqualification event considered to be a genuine settlement provision in the context of current uncertainty surrounding the direction of future regulatory rule developments.

(aa) Non-participating investment contracts

The Group's non-participating investment contracts are primarily unit-linked. These contracts are accounted for as financial liabilities whose value is contractually linked to the fair values of financial assets within the Group's unitised investment funds. The value of the unit-linked financial liabilities is determined using current unit prices multiplied by the number of units attributed to the contract holders at the reporting date. Their value is never less than the amount payable on surrender, discounted for the required notice period where applicable.

Interest or changes in the unit prices credited to the account balances incurred in the period are charged as expenses in the statement of comprehensive income, through changes in non-participating investment contract liabilities.

Deposits and withdrawals are not accounted for through the statement of comprehensive income but are accounted for directly in the balance sheet as adjustments to the non-participating investment contract liability.

(ab) Liability adequacy test

At each reporting date, liability adequacy tests are performed to ensure the adequacy of the insurance contracts and participating investment contract liabilities net of related deferred costs and acquired VIF. In performing these tests, current best estimates of future contractual cash flows, claims handling and policy administration expenses, as well as investment income from assets backing such liabilities, are used. Any deficiency is immediately charged to the statement of comprehensive income, initially by writing off the relevant assets and subsequently by establishing a provision for losses arising from the liability adequacy tests.

(ac) Other financial liabilities

Other financial liabilities are initially recognised at fair value less directly attributable transaction costs and subsequently measured at amortised cost. In practice, the carrying value of these balances equates to the fair value due to the short-term nature of the amounts included within other financial liabilities.

(ad) External interests in mutual investment funds

External interests in mutual investment funds which are accounted for by the Group as investments in subsidiaries as set out at policy (k) above are initially recognised, and subsequently stated, at fair value. The fair value of holdings in these funds is determined at the valuation point applicable to the OEIC sub-fund or the Unit Trust at the reporting date as set out under policy (r) above. Changes in the fair value of this balance are recognised in the statement of comprehensive income, through net profit attributable to external interests in mutual investment funds

(ae) Borrowings

Borrowings are recognised initially at fair value, being the issue proceeds net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the statement of comprehensive income through finance costs over the period of the borrowings using the effective interest rate applicable to the instrument. In practice, due to the nature of these balances, being bank overdrafts, the carrying value equates to the fair value of these liabilities as the borrowings are repayable on demand.

(af) Foreign currency translation

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in pounds sterling, (rounded to the nearest million ("£m")), which is the Group's presentational and functional currency.

Assets and liabilities denominated in foreign currencies are translated into sterling at the exchange rates ruling at the reporting 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. Any exchange differences are dealt with in that part of the statement of comprehensive income in which the underlying transaction is reported.

The results and financial position of the Group's foreign operations that have a functional currency different from the presentational currency are translated into the presentational currency as follows. The assets and liabilities of foreign operations are translated into sterling at foreign exchange rates ruling at the balance sheet date. The income and expenses of foreign operations are translated into sterling at average exchange rates, unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions in which case income and expenses are translated at the dates of the transactions. Foreign exchange differences arising on the translation of foreign operations are recognised in other comprehensive income.

(ag) Collateral

The Group receives or pledges collateral in the form of cash or securities in respect of derivative transactions it undertakes. The Group also receives collateral in the form of securities in respect of stock lending agreements and repurchase agreements. Collateral received is recognised as an asset on the balance sheet when the risks and rewards of ownership are substantially transferred to the Group. A corresponding liability for repayment of collateral is recognised in financial liabilities. Collateral received that is not recognised on the balance sheet is legally segregated from the assets of the Group. Collateral pledged continues to be recognised as an asset on the balance sheet unless the risks and rewards have been substantially transferred to the counterparty.

2. Critical accounting estimates and judgments in applying accounting policies

The Group's management makes estimates and judgments that affect the reported amount of assets and liabilities. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

(a) Insurance contract and participating investment contract liabilities

The estimation of the ultimate liability arising from insurance contracts and participating investment contracts which are not unit-linked is the Group's most critical accounting estimate.

In accordance with FRS 27, the liabilities of the Group's With Profits Funds are calculated using stochastic simulation models which values liabilities on a basis consistent with tradable market option contracts (a "market-consistent" basis). The liabilities are sensitive to both investment market conditions and changes to a number of non-economic assumptions, such as the level of take-up of options inherent in the contracts, mortality rates and lapses prior to dates at which a guarantee would apply.

For insurance contracts outside the With Profits Funds, the liabilities are calculated using a projection of future cash flows after making prudent assumptions about matters such as investment return, expenses, credit default and mortality. Discount rates used to value the liabilities are set with reference to the risk adjusted yields on the underlying assets. The most critical non-economic assumptions are mortality rates in respect of annuity business written and levels of future expenses. Such assumptions are based on recent actual experience, supplemented by industry information where appropriate. No critical accounting estimates apply for participating investment contracts as the contract liabilities arising outside of the With Profits Funds are almost entirely current unit values

At each reporting date, the estimates and assumptions referred to above are reassessed for adequacy and changes will be reflected in adjustments to the liability, through the statement of comprehensive income. Further information on these assumptions is given in note 41.

Sensitivities regarding changes to key assumptions in calculating insurance and participating investment contract liabilities are given in note 41.

(b) Intangible assets including intangible insurance assets

Acquired value of in-force business

Following the acquisition of Scottish Widows Unit Trust Managers Limited ("SWUTM") in 2006 and the acquisition of CMIG in 2011, the Group holds assets representing the acquired VIF of each transaction.

The asset arising on the acquisition of SWUTM was calculated by projecting the future surpluses and other cash flows attributable to the Group arising from business written, excluding the value of future investment risk margins, discounted at an appropriate rate. The key assumptions used in estimating future surpluses related to lapse rates and expenses. The assumptions were determined on a best-estimate basis and, as above, were based on recent actual experience and industry information where appropriate.

The asset arising on the acquisition of CMIG is calculated in the context of predecessor accounting as set out in note 3.

Amortisation of these balances and the related deferred tax is carried out on a best estimate basis over the estimated life of the contracts. The amortisation charge for the year is recognised through the statement of comprehensive income, within operating expenses. The carrying value of this asset is tested for impairment at each reporting date. Further information on this asset is given in note 14.

(c) Deferred costs

For insurance contracts and participating investment contracts (excluding those assessed on a 'realistic basis' in accordance with FRS 27), acquisition costs 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. All other costs are recognised as expenses when incurred. The calculation of the deferred acquisition cost asset and its pattern of amortisation requires estimation of both the expected pattern of receipt of future revenue margins and the period that the business is expected to remain in force. Further information on this asset is given in note 15.

The recognition of costs and income in respect of non-participating investment contracts is governed by IAS 18 "Revenue". Under this standard, directly attributable and incremental costs to securing new business are capitalised and are then subsequently amortised over the period of the provision of the investment management services. Estimation is required of the period that the business is expected to remain in force and prudent assumptions are required for contracts which do not have a fixed maturity date.

(d) Accruals and deferred income

For non-participating investment contracts, the recognition of income is governed by IAS 18. Income received for services to be provided in future periods is deferred and recognised in the statement of comprehensive income as the service is provided. As above, estimation is required of the period that the business is expected to remain in force and prudent assumptions are required for contracts which do not have a fixed maturity date. Further information on this liability is given in note 34.

(e) Retirement benefit obligations

The majority of the Company's employees are members of the SRBS, although some employees are members of certain LBG Schemes. All schemes provide defined benefits and/or defined contribution benefits to the members of those schemes.

The risks associated with the LBG Schemes are shared among various entities under the common control of LBG. The appropriate share of the deficit associated with these schemes has been added to the retirement benefit obligations of SWS, which is included within these consolidated financial statements. Further information on these liabilities is given in note 33.

(f) Taxation

The Company recognises current and deferred tax assets in line with IAS 12 "Income Taxes". In recognising these assets, management takes into account the likely impact of tax issues that are subject to ongoing discussion with HM Revenue and Customs and other tax authorities. With regard to the Group's and Company's deferred tax assets, a significant feature is the management judgment applied in determining the timing, sensitivities and probability of them reversing. This judgment is based on tax forecasts reflecting new business assumptions, sensitivities and proposed management actions. Further information in relation to the Group's and Company's current and deferred tax assets is set out at notes 13 and 16.

3. Business combinations

On 1 July 2011, in order to improve the capital efficiency within LBG, the Company acquired the entire share capital in CMIG from a fellow subsidiary of LBG giving the Company control of CMIG and its subsidiaries. On the basis that this is an intra-group transaction, the acquisition is outside the scope of IFRS 3 "Business Combinations" in accordance with paragraph 2(c) for a combination of entities under common control. As a result there is currently no specific guidance in IFRS for the accounting treatment or disclosure of the transaction and so management have applied IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors" in developing an appropriate policy. The result of this is that management has decided to use the principles of predecessor accounting, meaning that the acquirer does not restate acquired assets or liabilities to fair value but instead incorporates predecessor carrying values. These predecessor values have been incorporated for CMIG from 1 July 2011, the date of acquisition. The carrying value of the assets and liabilities reflect the carrying value as applied by LBG as at 1 July 2011. The principal activity of CMIG and its subsidiaries is the undertaking of ordinary long-term insurance and savings business and associated investment activities.

A consideration of £1,846m was paid. The consideration was based on valuation techniques consistent with those used for similar transactions in the insurance industry between independent third parties.

The following net assets were acquired:

	£m
Intangible assets including intangible insurance assets	2,507
Deferred tax assets	202
Investment properties	2,002
Assets arising from reinsurance contracts held	341
Current tax receivables	102
Financial assets:	
Derivative financial instruments	661
Loans and receivables	1,102
Investments at fair value through income	46,778
Cash and cash equivalents	1,074
Total assets acquired	54,769
Insurance contract and participating investment contract liabilities	(30,053)
Unallocated surplus	(338)
Deferred tax liabilities	(633)
Current tax payables	(55)
Provisions for other liabilities and charges	(3)
Accruals and deferred income	(287)
Financial liabilities:	
Subordinated debt	(454)
Non-participating investment contract liabilities	(12,084)
Derivative financial instruments	(175)
Other financial liabilities	(1,235)
External interests in mutual investment funds	(5,987)
Total liabilities acquired	(51,304)
Net assets acquired	3,465

Under the principles of predecessor accounting, the difference between the consideration paid and the net assets acquired has been taken to reserves as shown in the Statement of Changes in Equity. In addition, the difference between the predecessor carrying values and the carrying value as applied by LBG has led to the recognition of an insurance intangible asset (see note 14).

The amount of premiums written net of reinsurance and profit after tax of CMIG and its subsidiaries included in the Consolidated Statement of Comprehensive Income for the year ending 31 December 2011 is £729m and £250m respectively.

4. Segmental analysis

In the opinion of the Directors, the Group operates in a single business segment, being the provision of long-term insurance and investment contracts, and therefore there are no specific disclosure requirements under IFRS 8 "Operating Segments".

The table below provides a summary of the gross premiums written within the single business segment:

	2011 £ m	2010 £ m
Regular premiums	2,400	1,792
Single premiums	3,013	2,224
Total	5,413	4,016

5. Fee and commission income

	2011 £ m	2010 £ m
Fund management and policy administration fees	357	326
Change in deferred income	16	(2)
Fee income from reinsured business	5	-
Total	378	324

In previous years the Group has included annual management charges on non-participating investment contracts within change in non-participating investment contract liabilities. In light of developing industry practice, these amounts (2011: £185m; 2010: £125m) are now included within fee and commission income.

6. Investment income

	2011 £ m	2010 £ m
Investments at fair value through income		
Interest income on investments	1,475	1,201
Interest income on deposits	93	21
Dividend income	1,103	734
Interest receivable on swap	21	20
Financial instruments at amortised cost		
Interest income on intercompany loans	27	24
Rental income on investment properties	245	176
Stocklending income	7	7
Fund manager rebates received	42	47
Derivative fee income	(93)	(47)
Foreign currency translation differences	75	-
Other	11	3
Total	3,006	2,186

7. Net (losses)/gains on assets and liabilities at fair value through income

	2011 £ m	2010 £ m
Derivative financial instruments at fair value through income	(619)	148
Investments at fair value through income		
Equity securities	(4,528)	2,694
Debt securities	3,181	867
Investment properties at fair value through income	(67)	202
Foreign exchange	(244)	(3)
Fair value hedge adjustment in respect of swap	25	20
Fair value hedge adjustment for change in value of subordinated debt	(24)	(25)
Total	(2,276)	3,907

The fair value hedge adjustments in the above table reflect gains and losses arising in respect of undated subordinated debt issued by the Company which forms part of a hedge relationship. Further information in respect of this subordinated debt is set out at note 35.

8. Other income

Included within the Group is a service company which incurs costs on behalf of several subsidiary undertakings of the Lloyds Banking Group which are not consolidated into these financial statements. The costs recharged to those entities are recorded as other income.

9. Operating expenses

	2011 £ m	2010 £ m
Acquisition and origination costs in respect of insurance and investment contracts	243	223
Expenses for administration	686	359
	929	582
Provision in relation to German insurance business litigation	175	-
Amortisation of software development costs	25	23
Change in deferred costs	(70)	(67)
Amortisation of acquired VIF	175	51
Total	1,234	589

10. Staff costs and other employee related costs

	2011 £ m	2010 £ m
Wages and salaries	254	207
Social security costs	20	17
Other pension costs – defined contribution plan	4	4
Other pension costs – defined benefit plan	18	18
Curtailment gain	-	(76)
Total	296	170

The average number of employees directly employed by the Insurance Division, analysed into business functions, is as follows:

	2011	2010
Client service	2,067	1,352
Marketing and sales	701	661
Other support services	853	818
Banking	211	198
Total	3,832	3,029

The costs of certain employees in the above table are recharged to companies outside the Group.

11. Auditors' remuneration

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Fees payable for the audit of the statutory accounts for the Company	0.9	0.9	0.7	0.7
Fees payable for the audit of Lloyds Banking Group reporting returns	1.1	0.6	2.1	0.7
Fees payable for other services:				
Audit of Scottish Widows Group subsidiaries pursuant to legislation	0.9	-	1.0	-
Other services provided pursuant to legislation	0.6	0.1	0.6	0.1
Total audit fees	3.5	1.6	4.4	1.5
Other services audit related	0.7	-	1.0	-
Total audit and audit related fees	4.2	1.6	5.4	1.5
Services relating to taxation	0.1	0.1	0.3	0.3
Other services	0.4	0.4	0.2	0.2
Total non audit fees	0.5	0.5	0.5	0.5
Total	4.7	2.1	5.9	2.0

During the year, the Group incurred audit fees in respect of its pension schemes of £28,050 (2010: £27,000).

12. Finance costs

	2011 £ m	2010 £ m
Interest on borrowings	10	2
Interest on repos	13	10
Interest on swaps	5	-
Interest on subordinated debt	109	53
Total	137	65

13. Taxation

(a) Current year tax charge/(credit)

	2011 £ m	2010 £ m
Current tax:		
UK corporation tax	164	39
Overseas tax	2	10
Adjustment in respect of prior years	(27)	(52)
Total current tax	139	(3)
Deferred tax:		
Origination/(reversal) of temporary differences	(57)	140
Adjustment in respect of prior years	27	(55)
Total deferred tax	(30)	85
Total income tax charge/(credit)	109	82

The policyholder tax credit or charge is included in income tax credit. Policyholder tax is a charge of £234m (2010: charge of £116m), including a prior year tax charge of £51m (2010: credit of £2m).

(b) Reconciliation of tax charge/(credit)

	2011 £ m	2010 £ m
Profit before tax	391	331
Tax at 26.5% (2010: 28%)	104	93
Effects of:		
Income tax at other than standard rate	(33)	66
Disallowable Expenses	4	0
Non-deductible policyholder tax	190	83
Adjustment to tax charge in respect of prior years	(51)	(107)
Deferred Tax not previously recognised	53	-
Overseas tax	14	9
Change in tax rate	(64)	(21)
Unallocated Surplus	(70)	-
Group relief received for less than full value	(34)	(54)
Other	(4)	13
Total	109	82

The standard rate of Corporation Tax in the UK changed from 28% to 26% with effect from 1 April 2011. Accordingly, the company's profits for this accounting period are taxed at an effective rate of 26.5%

The Finance Act 2011 has reduced the rate of corporation tax from 26% to 25% with effect from 1 April 2012. The impact of this reduction in tax rate, which is applicable to the calculation of deferred tax assets and liabilities at the reporting date, is reflected in the above table.

14. Intangible assets including intangible insurance assets

		2011 £ m	2010 £ m
		Group	*Group*
Acquired VIF	(a)	2,483	153
Software development costs	(b)	150	110
Total		2,633	263

(a) Acquired VIF

	2011 £ m	2010 £ m
	Group	*Group*
Cost		
At 1 January	371	371
Additions	2,505	-
At 31 December	2,876	371
Accumulated amortisation and impairment		
At 1 January	218	167
Amortisation during the year	175	51
At 31 December	393	218
Carrying amount		
At 31 December	2,483	153

Following completion of the annual impairment review in respect of these assets for 2011, no impairment charge has been required.

Of the above total, £2,184m (2010: £102m) is expected to be recovered more than one year after the reporting date.

(b) Software development costs

	2011 £ m	2010 £ m
	Group	*Group*
Cost		
At 1 January	224	168
Adjustment on acquisition	6	-
Additions	63	56
At 31 December	293	224
Accumulated amortisation		
At 1 January	114	91
Adjustment on acquisition	4	-
Amortisation charge for the year	25	23
At 31 December	143	114
Carrying amount		
At 31 December	150	110

Of the above total, £120m (2010: £86m) is expected to be recovered more than one year after the reporting date.

15. Deferred costs

		2011 £ m	2011 £ m	2010 £ m	2010 £ m
		Group	*Company*	*Group*	*Company*
Deferred acquisition costs	(a)	804	246	694	240
Deferred origination costs	(b)	268	204	308	235
Total		1,072	450	1,002	475

(a) Deferred acquisition costs

	2011 £ m	2011 £ m	2010 £ m	2010 £ m
	Group	*Company*	*Group*	*Company*
At 1 January	694	240	601	214
Amounts incurred during the year	209	42	151	49
Amortisation during the year	(99)	(36)	(58)	(23)
At 31 December	804	246	694	240

Of the above total, £712m for Group and £219m for Company (2010: £627m for Group and £209m for Company) is expected to be recovered more than one year after the reporting date.

(b) Deferred origination costs

	2011 £ m	2011 £ m	2010 £ m	2010 £ m
	Group	*Company*	*Group*	*Company*
At 1 January	308	235	334	262
Amounts incurred during the year	24	7	34	9
Amortisation during the year	(64)	(38)	(60)	(36)
At 31 December	268	204	308	235

Of the above total, £235m for Group and £180m Company (2010: £272m for Group and £208m Company) are expected to be recovered more than one year after the reporting date.

16. Tax assets and liabilities

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Current tax receivables	238	20	198	139
Deferred tax assets	485	716	325	627
Total tax assets	723	736	523	766
Current tax payables	163	-	93	-
Deferred tax liabilities	968	187	410	247
Total tax liabilities	1,131	187	503	247

Deferred tax assets and liabilities included in the above table, except capital losses, are expected to be recovered more than one year after the reporting date.

(a) Recognised deferred tax

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The amounts are as follows:

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Deferred tax assets comprise:				
Pension losses	188	188	181	181
Tax on deferred income	17	344	14	337
Expenses deductible in future periods	242	184	110	108
Unrealised losses on investment assets		-	-	-
Other	38	-	20	1
Total deferred tax assets	485	716	325	627
Deferred tax liabilities comprise:				
Unrealised gains on investment assets	8	5	19	18
Deferred costs	254	112	232	128
Other insurance related items	114	70	100	101
Pension and other post retirement benefit obligations	19	-	11	-
Accelerated capital allowances	6	-	7	-
Deferred tax on acquired VIF	532	-	41	-
Other	35	-	-	-
Total deferred tax liabilities	968	187	410	247
Net deferred tax assets/(liabilities)	(483)	529	(85)	380

The deferred tax balances include an asset of £188m (2010: £181m) in respect of tax losses incurred by the Group in respect of its pension business. These losses are fully recoverable against the expected amount of future pensions profits and thus can be recognised in full under IAS 12. Also included in the deferred tax balance is an asset of £242m (2010: £110m) in respect of expenses incurred by the Group that will be deductible in future periods. Projections indicate that these expenses will be offset against future income and gains.

The deferred tax liability shown above shown in respect of life business capital gains of £5m (2010: £18m) is the net position at a Company level. Additional policyholder provisions may be recognised in respect of capital losses relating to unit linked business and with profit business. In respect of unit linked business, policyholder provisions of £nil (2010: £5m) are included within insurance and participating investment contract liabilities and provisions of £nil (2010: £13m) are included within non-participating investment contract liabilities. In addition, policyholder provisions of £22m (2010: £42m) are included within unallocated surplus in respect of with profit business.

The Finance Act 2011 has reduced the rate of corporation tax from 26% to 25% with effect from 1 April 2012. The impact of this reduction in tax rate, which is applicable to the calculation of deferred tax assets and liabilities at the reporting date, is reflected in the above table.

The tax charge/(credit) in the income statement relating to each of the above items is as follows:

	2011 £ m	2010 £ m
	Group	*Group*
Pension losses	(7)	7
Tax on deferred income	(3)	6
Expenses deductible in future periods	(4)	50
Pensions and post-retirement benefit obligations	8	23
Other deferred tax assets	(7)	(8)
Unrealised gains/losses on investment assets	53	39
Deferred acquisition costs	22	(10)
Other insurance items	12	(6)
Accelerated capital allowances	(1)	-
Acquired value in force	(103)	(16)
Total deferred tax (credit)/charge	(30)	85

(b) Unrecognised deferred tax

Deferred income tax assets are recognised for tax loss carry forwards only to the extent that realisation of the related tax benefit is probable.

The Company has a significant With Profits pension business. The business is subject to UK corporation tax on the basis of a notional return determined by UK taxation authorities. To the extent that the actual return from the business is less than the notional return, tax losses accumulate which may be carried forward and offset against excess returns in future years. The maximum potential value of these losses at 31 December 2011 was £875m (2010: £506m). No asset has been recognised in respect of these losses as it is unlikely that there will be excess returns in future years against which they can be offset.

Deferred tax assets have not been recognised in respect of unrelieved capital losses of £254m (2010: £nil), as there is insufficient certainty as to the availability of future profits .

Deferred tax assets have not been recognised in respect of excess expenses carried forward of £63m (2010: £nil), as there is insufficient certainty as to the availability of future profits.

The Company has a taxable temporary difference of £152m (2010: £152m) in respect of its holding of a structural asset being shares in Scottish Widows Unit Funds Limited. No deferred tax liability is required to be recognised in respect of this taxable temporary difference under IAS 12 as the Company does not intend to dispose of this structural asset.

At the end of 2011 the Group has a deductible temporary difference of £937m (2010:£192m) for which no asset has been recognised as the Group intends to make these losses available to fellow undertakings within the Lloyds Banking Group for no payment.

17. Investment in subsidiaries

	2011 *Company* £ m	2010 *Company* £ m
At 1 January	1,892	1,808
Additions	1,846	60
Revaluations	33	2
Movements in holdings in OEICs at fair value	4,275	22
At 31 December	8,046	1,892

Investments in subsidiaries held at cost are generally recoverable more than one year after the reporting date. Due to the nature of investments in mutual funds including OEICs, there is no fixed term associated with these investments.

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
Pensions Management (S.W.F.) Limited*	Debenture	100	Scotland	Life Insurance
Scottish Widows Unit Funds Limited	Ordinary & Deferred	100	Scotland	Life Insurance
Scottish Widows Services Limited	Ordinary	100	Scotland	Management Services
Scottish Widows Unit Trust Managers Limited	Ordinary	100	England	OEIC Management
Clerical Medical Investment Group Limited	Ordinary	100	England	Life Insurance
Halifax Life Limited 1	Ordinary	100	England	Life Insurance
St Andrew's Life Assurance Plc 1	Ordinary	100	England	Life Insurance

Note: * limited by guarantee
1 indirect holding

The above subsidiaries operate in the United Kingdom and have been included within the consolidated financial statements, along with controlled mutual investment funds and other entities held as part of the actively managed investment portfolios.

During the year, the Company acquired the entire share capital of CMIG. Further details of the acquisition can be found in note 3. During the year, the Company entered into an agreement with Scottish Widows Financial Services Holdings ("SWFSH") to sell CMIG to SWFSH at fair value (with a minimum value of zero) should there be an event that reduced CMIG's capital in excess of its regulatory requirement to nil. This agreement has nil value as at 31 December 2011.

The Company also invests in a number of mutual investment funds including OEICs which have been classified as investments in subsidiaries as described in the accounting policies.

The ability of regulated entities to pay cash dividends to the Company or repay loans or advances is restricted by regulatory solvency requirements as well as Companies Act distributable reserves requirements. The ability of non-regulated entities to pay cash dividends to the Company or repay loans or advances is restricted by Companies Act distributable reserves requirements.

18. Property and equipment

	Group			*Company*
	Land and buildings £ m	Equipment £ m	Total £ m	Land and buildings £ m
Cost				
At 1 January 2010	120	46	166	27
Additions	-	5	5	-
At 31 December 2010	120	51	171	27
Additions	-	6	6	-
Disposals	-	(8)	(8)	-
At 31 December 2011	120	49	169	27
Accumulated depreciation				
At 1 January 2010	26	32	58	6
Depreciation charge for the year	3	8	11	1
At 31 December 2010	29	40	69	7
Depreciation charge for the year	3	6	9	1
Disposals	-	(9)	(9)	-
At 31 December 2011	32	37	69	8
Carrying amount				
At 31 December 2010	91	11	102	20
At 31 December 2011	88	12	100	19

The valuation was undertaken by Jones Lang LaSalle. The above assets are generally recoverable more than one year after the reporting date.

19. Investment properties

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
At 1 January	2,603	1,464	2,309	1,332
Adjustment on acquisition	2,002	-	-	-
Additions – new properties	219	41	116	14
Additions – subsequent expenditure on existing properties	36	14	28	8
Disposals	(396)	(96)	(45)	(41)
Foreign exchange valuation difference	(2)	-	(6)	-
Net gain / (loss) from change in fair values	(65)	(21)	201	151
At 31 December	4,397	1,402	2,603	1,464

Rental income arising from investment properties during the year amounted to £245m (2010: £176m), which is included in investment income. Direct operating expenses (included within operating expenses) arising in respect of such investment properties during the year amounted to £22m (2010: £23m).

Expenditure on investment properties which did not generate rental income was £2m (2010: £1m). The carrying value of investment properties under development is £63m (2010: £5m).

Loans of EUR 94m (£82m) (2010: EUR 94m (£81m)) are secured on certain investment properties held by the Group.

The investment properties are independently valued by Drivers Jonas, Jones Lang LaSalle, DTZ, CB Richard Ellis and Cushman & Wakefield on at least a quarterly basis for the purpose of determining the open market value of the properties.

Due to the nature of the above assets, there is no fixed term associated with these investments.

20. Assets arising from reinsurance contracts held

The Company's assets arising from reinsurance contracts held can be analysed between those classified as insurance contracts and those classified as financial assets designated at fair value through income as follows:

Group	2011 Classified as			2010 Classified as		
	Insurance contracts	Fair value through income	Total	Insurance contracts	Fair value through income	Total
	£ m	£ m	£ m	£ m	£ m	£ m
At 1 January	496	2,328	2,824	408	1,313	1,721
Adjustment on acquisition	265	76	341	-	-	-
Movement recognised through the statement of comprehensive income	21	47	68	88	268	356
Movement recognised directly through the balance sheet	-	1,487	1,487	-	747	747
At 31 December	782	3,938	4,720	496	2,328	2,824
Amounts in respect of insurance and participating investment contract liabilities	782	-	782	496	-	496
Amounts in respect of non-participating investment contract liabilities	-	65	65	-	-	-
Corporate pension reinsurance	-	3,873	3,873	-	2,328	2,328
Total	782	3,938	4,720	496	2,328	2,824

Company	2011 Classified as			2010 Classified as		
	Insurance contracts	Fair value through income	Total	Insurance contracts	Fair value through income	Total
	£ m	£ m	£ m	£ m	£ m	£ m
Amounts backing insurance and participating investment contract liabilities	5,714	12,919	18,633	5,132	13,281	18,413
Amounts backing non-participating investment contract liabilities	-	10,511	10,511	-	10,375	10,375
Corporate pension reinsurance	-	3,873	3,873	-	2,328	2,328
Total	5,714	27,303	33,017	5,132	25,984	31,116

In previous years reinsurance contracts which did not transfer significant insurance risk were classified as insurance contracts where these were held in respect of insurance contract liabilities. In light of developing industry practice, these amounts (2011: £12,919m, 2010: £13,234m) are now classified as financial assets designated at fair value through income in accordance with the underlying reinsurance contracts.

Assets arising from reinsurance contracts held include £3,391m Group and £32,433m Company (2010: £2,823m Group and £30,611m Company) that is expected to be settled more than one year after the reporting date.

21. Investment in joint ventures

The following tables present disclosures required under IAS 31.

Group	2011				
	Assets £ m	Liabilities £ m	Revenues £ m	Profit £ m	Average interest held %
The Great Wigmore Partnership	101	11	1	1	50%
Barbirolli Square Limited Partnership	53	3	4	4	50%

Group	2010				
	Assets £ m	Liabilities £ m	Revenues £ m	Profit £ m	Average interest held %
The Great Wigmore Partnership	70	4	1	1	50%
Barbirolli Square Limited Partnership	56	2	5	4	50%

Company	2011				
	Assets £ m	Liabilities £ m	Revenues £ m	Profit £ m	Average interest held %
The Great Wigmore Partnership	101	11	1	1	50%

Company	2010				
	Assets £ m	Liabilities £ m	Revenues £ m	Profit £ m	Average interest held %
The Great Wigmore Partnership	70	4	1	1	50%

Due to the nature of the above holdings, there is no fixed term associated with these investments.

The Great Wigmore Partnership is registered in the United Kingdom, in accordance with the Limited Partnerships Act 1907. The principal activity of the Partnership is investment in, and development of, freehold and leasehold property in the United Kingdom. The Partnership had no capital commitments, contractual obligations or contingent liabilities at 31 December 2011 (2010: none).

Barbirolli Square Limited Partnership is registered in Scotland as a limited partnership under the Limited Partnerships Act 1907. The principal activity of the Partnership is that of property investment which the General Partner considers offers potential to deliver attractive returns within an acceptable risk profile. The Partnership had no capital commitments, contractual obligations or contingent liabilities at 31 December 2011 (2010: none).

There are no restrictions on the ability of any of the joint ventures to distribute funds to investors.

22. Derivative financial instruments

In the normal course of business, the Group enters into swap contracts, option contracts, index futures contracts and forward foreign exchange contracts. All such contracts are undertaken either for efficient portfolio management purposes or for the purpose of matching contractual liabilities. In addition, the Company has entered into a swap for the specific purpose of hedging movements in the fair value of certain subordinated debt, as described in note 35.

Swap contracts include interest and inflation rate swaps. An interest or inflation rate swap is an agreement between two parties to exchange fixed and variable rate interest payments, based upon interest or inflation rates defined in the contract, without the exchange of the underlying principal amount.
Option contracts include index and single equity options. Such options represent a contract sold by one party to another party offering the right, but not the obligation, to buy or sell a financial asset at an agreed price on a specified future date or within a specified period of time.

Index futures contracts are used to hedge the investment portfolio against adverse movements in underlying markets or effecting policy switches between markets without the need to trade the underlying securities. Futures may also be used for the purposes of efficient portfolio management provided that their substance would otherwise be permitted as a series of direct transactions.

Forward foreign exchange contracts are an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate.

Details regarding derivative financial instruments are given in the following tables:

Group	2011			2010		
	Contract Amount £ m	**Fair value asset £ m**	**Fair value liabilities £ m**	**Contract Amount £ m**	**Fair value asset £ m**	**Fair value liabilities £ m**
Derivative financial instruments held for trading:						
Swap contracts	11,579	586	1,104	5,429	137	384
Option contracts	5,628	639	8	8,648	69	14
Index futures contracts	2,787	19	30	1,623	13	13
Forward foreign exchange contracts	4,702	50	19	3,060	44	42
Derivative financial instruments designated as fair value hedges	885	96	-	560	51	-
Derivative financial instruments designated as net investment hedges	49	-	1	-	-	-
Total	25,630	1,390	1,162	19,320	314	453

Company	2011			2010		
	Contract Amount £ m	**Fair value asset £ m**	**Fair value liabilities £ m**	**Contract Amount £ m**	**Fair value asset £ m**	**Fair value liabilities £ m**
Derivative financial instruments held for trading:						
Swap contracts	3,629	111	617	4,104	54	308
Option contracts	782	33	-	8,618	65	12
Index futures contracts	572	2	8	434	2	5
Forward foreign exchange contracts	1,238	14	3	1,004	5	9
Derivative financial instruments designated as fair value hedges	560	65	-	560	51	-
Total	6,781	225	628	14,720	177	334

Derivative financial instrument fair value assets include £1,180m for Group and £140m for Company (2010: £158m for Group and £77m for Company) that is expected to be recovered more than one year after the reporting date.

Derivative financial instrument fair value liabilities include £1,052m for Group and £567m for Company (2010: £369m for Group and £295m for Company) that is expected to be settled more than one year after the reporting date.

The fair value hedge included in the above tables represents interest rate swaps in respect of the interest payments relating to subordinated debt issued by the Group. This instrument forms part of a hedge relationship with the subordinated debt issued.

The net investment hedge included in the table above is held in respect of the European branch of the Group. The hedge has been put in place to offset the currency exposure relating to the branch with changes in the fair value of the derivative being taken directly to equity.

Assets amounting to £196m (2010: £70m) were accepted by the Group and £34.8m (2010: £17.3m) by the Company as collateral. It is permitted to sell or repledge these assets in the absence of default of the owner of the collateral. No collateral was sold or repledged during the year or in the prior year. The Group has an obligation to return these assets to the pledgor.

23. Loans and receivables

	2011		2010	
	£ m	**£ m**	**£ m**	**£ m**
	Group	*Company*	*Group*	*Company*
Insurance business:				
Amounts receivable in respect of direct insurance business	95	42	40	39
Amounts receivable under reinsurance contracts	28	24	7	7
Other loans and receivables:				
Investments held in a liquidity fund	17,171	-	-	-
Accrued interest and rent	600	299	375	288
Amounts due from related parties	263	304	1,147	1,242
Other	920	511	555	173
Total	19,077	1,180	2,124	1,749

Of the above total, £106m for Group and £106m for Company (2010: £103m for Group and £103m for Company) is expected to be recovered more than one year after the reporting date.

Amounts due from reinsurers represent reinsurance receivables where the Company has the right to cover losses on contracts provided to policyholders.

None of the above balances are interest-bearing (2010: £nil).

There is no significant concentration of credit risk with respect to loans and receivables. Further information in respect of credit risk is given in note 42.

24. Investments at fair value through income

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Shares and other variable yield securities	52,173	6,940	35,312	12,673
Debt and other fixed/variable income securities	37,580	8,942	20,644	10,128
Deposits with credit institutions	-	-	1,287	10
Other investments	96	747	162	707
Total investments at fair value	89,849	16,629	57,405	23,518

Of the total debt securities above, £8,044m (2010: £10,845m) for Group and £4,144m (2010: £5,713m) for Company are listed government bonds.

Of the debt securities, £18,033m for Group and £8,691m for Company (2010: £19,350m for Group and £9,570m for Company) is expected to be recovered more than one year after the reporting date. Due to the nature of equity securities and investments in pooled investment funds, there is no fixed term associated with these securities.

25. Cash and cash equivalents

Cash and cash equivalents for the purposes of the statement of cash flows include the following:

	2011		2010	
	£ m	£ m		£ m
	Group	*Company*	*Group*	*Company*
Cash at bank	679	48	505	42
Short term deposits	310	-	-	-
Cash at bank	989	48	505	42
Investments held by liquidity funds (note 23)	17,171	-	-	-
Less: amounts with a maturity of three months or more	(1,322)	-	-	-
	16,838	48	505	42
Less: borrowings (note 38)	(7)	(4)	(11)	(4)
Total	16,831	44	494	38

Cash and cash equivalents in the above table contains amounts of £8,565m (2010: £153m) which are held entirely within the long-term insurance funds of the Group. These balances are not therefore readily available for use by the Group.

26. Share capital

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Allotted, called up and fully paid share capital:				
1,470,092,670 (2010: 648,929,000) ordinary shares of £1 each	1,470	1,470	649	649
Total	1,470	1,470	649	649

During the year, the immediate parent of the Company increased its investment in the Company's share capital by £821m.

27. Other reserves

The balance of other reserves was established on 3 March 2000 at the point when the Company acquired certain long term business assets and liabilities following the demutualisation of Scottish Widows Fund and Life Assurance Society ("SWFLAS"). The balance at 3 March 2000 represented the amount of surplus assets over liabilities allocated to the Non-Participating Fund and Shareholders Fund of the Company under the Scheme of Transfer ("the Scheme"). Since that date, the balance of other reserves has reduced as net transfers have been made to retained earnings.

Movements in the balance of other reserves are disclosed in the statement of changes in equity. The Non-Participating Fund made a contingent loan to the With Profits Fund on the demutualisation of SWFLAS. Under the terms of the Scheme, the With Profits Fund is entitled to receive the profits arising on the business allocated to the Non-Participating Fund at demutualisation but is then required to repay the contingent loan by a corresponding amount. There were no movements in other reserves during the year ended 31 December 2011 or 31 December 2010.

28. Minority interest in equity

Minority interest comprises holdings in the following investments which are partly, but not wholly, owned by the Group:

Group	2011 £ m	2010 £ m
Dalkeith Corporation LLC	-	-
Total	-	-

29. Insurance and participating investment contract liabilities

An analysis of the change in insurance and participating investment contract liabilities and reinsurers' share of insurance and participating investment contract liabilities is as follows:

Group	2011 £ m	2011 £ m	2011 £ m	2010 £ m	2010 £ m	2010 £ m
	Gross	*Reinsurance*	*Net*	*Gross*	*Reinsurance*	*Net*
At 1 January	40,202	496	39,706	36,446	408	36,038
Adjustment on acquisition	30,053	265	29,788	-	-	-
New business	3,331	53	3,278	2,367	17	2,350
Changes in existing business	(4,922)	(392)	(4,530)	1,389	71	1,318
Assumption changes	1,054	360	694	-	-	-
At 31 December	69,718	782	68,936	40,202	496	39,706

Company	2011 £ m	2011 £ m	2011 £ m	2010 £ m	2010 £ m	2010 £ m
	Gross	*Reinsurance*	*Net*	*Gross*	*Reinsurance*	*Net*
At 1 January	38,066	18,413	19,653	34,333	15,999	18,334
Adjustment on acquisition						
New business	3,051	1,051	2,000	2,367	1,123	1,244
Changes in existing business	(2,518)	(1,156)	(1,363)	1,366	1,291	75
Assumption changes	297	325	(28)	-	-	-
At 31 December	38,896	18,633	20,262	38,066	18,413	19,653

As the Group is wholly owned by an entity which prepares group financial statements, the Group has taken advantage of the provisions contained in FRS 27 and has not presented a capital position statement and supporting disclosures. Information in which the Group is included is given in the financial statements of LBG.

The regulatory capital and required capital of the Company are disclosed in note 42 (c) iii).

An analysis of the expected maturities of insurance and participating investment contract liabilities is given in note 42.

30. Unallocated surplus

An analysis of the change in unallocated surplus is as follows:

	2011 £ m	2011 £ m	2010 £ m	2010 £ m
	Group	*Company*	*Group*	*Company*
At 1 January	325	325	328	328
Adjustment on acquisition	338	-	-	-
Change recognised through the statement of comprehensive income	(365)	(86)	(3)	(3)
At 31 December	298	239	325	325

Of the above total, £298m for Group and £239m for Company (2010: £325m for Group and £325m for Company) is expected to be settled more than one year after the reporting date.

31. Future profits on non-participating business in the With Profits Fund

An analysis of the change in future profits on non-participating business in the Scottish Widows With Profits Fund is as follows:

	2011 £ m	£ m	2010 £ m	£ m
	Group	*Company*	*Group*	*Company*
At 1 January	86	86	126	126
Change recognised through the statement of comprehensive income*	(41)	(41)	(40)	(40)
At 31 December	45	45	86	86

*The movement in this balance is recognised through the statement of comprehensive income, within change in insurance and participating investment contract liabilities.

Of the above total, £45m for Group and £45m for Company (2010: £40m for Group and £40m for Company) is expected to be recovered more than one year after the reporting date.

32. Provisions for other liabilities and charges

Group	German insurance business litigation £ m	Other £m	Total £ m
At 1 January 2011	-	5	5
Adjustment on acquisition	-	3	3
Charge for the year	175	(6)	169
Amount utilised in the period	(5)	-	(5)
At 31 December 2011	170	2	172

Provision in relation to German insurance business litigation

CMIG has received a number of claims in the German courts, relating to policies issued by CMIG but sold by independent intermediaries in Germany, principally during the late 1990s and early 2000s. CMIG has won the majority of decisions to date, although a small number of regional district and appeal courts have found against CMIG on specific grounds. CMIG's strategy includes defending claims robustly and appealing against adverse judgments. The ultimate financial effect, which could be material, will only be known once all relevant claims have been resolved. However, consistent with this strategy, and having regard to the costs involved in managing these claims, and the inherent risks of litigation, the Group recognised a provision of £175 million. Management believes this provision, less the amount utilised in the period, represents the most appropriate estimate of the financial impact, based upon a series of assumptions, including the number of claims received, the proportion upheld, and resulting legal and administration costs.

This provision requires significant judgement by management in determining appropriate assumptions, including the number of claims received, the proportion upheld, and resulting legal and administration costs. Assuming that all other assumptions remain unchanged, if in the longer term the level of claims was ten percentage points higher (lower) than estimated then the cost would increase (decrease) by approximately £3m; and if uphold rates were ten percentage points higher (lower) than estimated then the cost would increase (decrease) by approximately £13m.

The Group will re-evaluate the assumptions underlying its analysis at each reporting date as more information becomes available. As noted above, there is inherent uncertainty in making estimates; actual results in future periods may differ significantly from the amount provided.

Other

Other provisions include provisions held in respect onerous leases on investment properties.

33. Retirement benefit obligations

The majority of the Company's employees are members of the SRBS, although certain employees are members of the LBG Schemes. All schemes provide defined benefits and/or defined contribution benefits to the members of those schemes.

Scottish Widows Retirement Benefits Scheme

The latest full valuation of the SRBS was carried out as at 1 May 2009; this has been updated to 31 December 2011 by a qualified actuary employed by Scottish Widows. Employee contributions made during the year were £2m (2010: £2m).

The principal assumptions used in determining the pension benefit obligations for the Scottish Widows plc Group, as determined by the Trustees, are as follows:

	2011 %	2010 %
Rate of inflation – Retail Prices Index	3.00	3.40
Rate of Inflation – Consumer Price Index	2.00	2.90
Rate of salary increases	2.00	2.00
Rate of increase for pensions in payment	2.80	3.20
Discount rate	5.00	5.50
Expected rate of return on assets (average)	4.87	6.20
Deferred pensions revaluation	2.00	2.90

The sensitivity of the pension scheme deficit at the reporting date, before application of the "corridor", to changes in the key assumptions set out above is set out below. The table demonstrates the effect of a change in a key assumption whilst other assumptions remain unchanged. Numbers in brackets represent an increase in a deficit or a reduction in a surplus.

	2011 £000	2010 £000
0.2% (2010: 0.2%) increase in discount rate	16,400	34,500
0.2% (2010: 0.2%) decrease in discount rate	(15,400)	(36,800)
0.2% (2010: 0.2%) increase in inflation rate	(17,000)	(30,500)
0.2% (2010: 0.2%) decrease in inflation rate	15,500	28,800
1 year increase in mortality age rating	16,300	18,700
1 year decrease in mortality age rating	(17,200)	(18,500)

The above changes would be offset by an equal and opposite change in the amount of unrecognised actuarial gains and losses, with no net impact on the pension scheme surplus or deficit reported on the balance sheet.

The mortality assumptions used are illustrated by the following years of life expectancy in retirement:

	2011 Years	2010 Years
Life expectancy for member aged 60, on the valuation date		
Men	27	27
Women	28	28
Life expectancy for member aged 60, 15 years after the valuation date		
Men	29	28
Women	30	30

The assets of the SRBS and the expected rates of return are summarised as follows:

	2011			2010		
	Fair value of assets	Proportion of total assets	Expected long-term rate of return	Fair value of assets	Proportion of total assets	Expected long-term rate of return
	£ m	%	%	£ m	%	%
Equities	285	35.3	8.3	355	46.3	8.3
Fixed Interest Gilts	5	0.6	3.0	-	-	-
Index linked gilts	254	31.5	2.8	213	27.8	3.9
Non-government bonds	106	13.0	4.9	96	12.5	4.9
Property	31	3.8	6.6	35	4.5	7.3
Swaps	(6)	(0.7)	-	-	-	-
Cash	133	16.5	2.6	68	8.9	3.9
Total fair value of scheme assets	808	100	4.9	767	100	6.2

The amounts recognised in the Group's balance sheet are as follows:

	2011 £ m	2010 £ m
Fair value of scheme assets	808	767
Present value of defined benefit obligations	(773)	(725)
Unrecognised losses	92	58
Unrecognised curtailment losses	(12)	(12)
Asset recognised in the balance sheet	115	88

The above amount is generally expected to be settled more than one year after the reporting date (2010: more than one year).

As referred to in the accounting policies, gains and losses are not recognised unless the cumulative gain or loss at the end of the previous reporting period exceeds the greater of 10 per cent of the scheme assets or liabilities.

The amounts recognised in the statement of comprehensive income are as follows:

	2011 £ m	2010 £ m
Current service cost	18	18
Interest cost on benefit obligation	41	39
Cost of curtailment	-	(76)
Unrecognised net actuarial loss for curtailment	-	12
Net actuarial losses recognised	-	1
Expected return on scheme assets	(49)	(43)
Past service cost	-	-
Net expense/(income) recognised	10	(49)

Of the total net income for the year, a credit of £46m for SRBS and £nil for the LBG schemes (2010: credit of £46m for SRBS and £nil for the LBG schemes) has been included within operating expenses and a credit of £4m for SRBS and £nil for the LBG schemes (2010: credit of £4m for SRBS and £nil for the LBG schemes) has been included within other income. Net actuarial losses of £nil (2010: £1m) for SRBS have been recognised as a charge within total comprehensive income.

The actual return on the assets of the scheme amounted to a gain of £27m (2010: gain of £83m).

Movements in the present value of defined benefit obligations for the SRBS are as follows:

	2011 £ m	2010 £ m
At 1 January	725	763
Current service cost	18	18
Interest cost on benefit obligations	41	39
Benefits paid	(20)	(20)
Scheme obligations transferred to Scottish Widows Investment Partnership Group Limited at 31 December	(2)	(10)
Actuarial losses	11	11
Settlements/curtailments	-	(76)
At 31 December	773	725

Movements in the fair value of the assets of the SRBS during the year are as follows:

	2011 £m	2010 £ m
At 1 January	767	661
Expected return on scheme assets	49	43
Contributions received	37	56
Scheme assets transferred to Scottish Widows Investment Partnership Group Limited at 31 December 2010	(2)	(9)
Benefits paid	(20)	(20)
Actuarial (losses)/gains	(23)	36
At 31 December	808	767

The estimated amount of contributions expected to be paid during the financial year ended 31 December 2011 is £45m (2010: £45m).

A summary of the financial position of the SRBS, excluding unrecognised gains and losses, and the five year history of experience adjustments is as follows:

	2011 £ m	2010 £ m	2009 £ m	2008 £ m	2007 £ m
Fair value of scheme assets	808	767	661	573	646
Present value of defined benefit obligations	(773)	(725)	(763)	(565)	(624)
(Deficit)/surplus in the scheme	35	42	(102)	8	22
Experience adjustments on scheme liabilities:					
Amount	£1m	£9m	£7m	(£5m)	£0m
Percentage of scheme liabilities	0.1%	(1.1%)	1.0%	1%	0%
Experience adjustments on scheme assets:					
Amount	£(24)m	£38m	£(51)m	(£124m)	£3m
Percentage of scheme assets	2.9%	4.7%	8%	21%	0%
Effect of curtailment benefit obligation:					
Amount	-	(£7m)	-	-	-
Percentage of scheme liabilities	-	(0.9%)	-	-	-

The SRBS also includes a defined contribution section: new employees are offered membership of this section of the scheme. During the year ended 31 December 2011, the charge to the Group's statement of comprehensive income in respect of this scheme was £2m (2010: £2m), representing the contributions payable by SWS in accordance with the scheme's rules. There were no outstanding or prepaid contributions at 31 December 2011.

In March 2011, the Company provided a guarantee to the trustees of SRBS to explicitly cover the minimum legal obligations imposed on the employers (SWS and SWIP) by Sections 75 of the Pension Act 1995. As a result, the Company will be liable to its proportionate share of the deficit in the SRBS at the relevant time (calculated as the cost of securing benefits with an insurer) in the event that: SRBS is wound up; the employers become insolvent; or an employer ceases to employ active members of SWRBS at a time when another employer continues to do so. The guarantee is considered to have an immaterial

value on the basis that the likelihood of the events detailed arising are considered remote. Consequently, there are currently no indications that any amounts payable under this guarantee will materially affect the financial position of the Company.

Other schemes

Defined contribution schemes

The Company's ultimate parent company operates a number of defined contribution schemes, principally the defined contribution sections of the LBG Schemes; new employees are offered membership of the defined contribution section of the Lloyds Banking Group Pension Scheme No. 1.

During the year ended 31 December 2010, the charge to the statement of comprehensive income in respect of these schemes was nil (2010: nil), representing the contributions payable by the Company in accordance with each scheme's rules. There were no outstanding or prepaid contributions at 31 December 2011.

Defined benefit schemes

The Company's ultimate parent company has established a number of defined benefit pension schemes in the UK and overseas. A small number of the Company's employees are members of the defined benefit sections of the LBG Schemes. These are funded schemes providing retirement benefits calculated as a percentage of final salary depending on length of service; the minimum retirement age under the rules of the schemes is 50.

The latest full valuations of the two main schemes were carried out as at 30 June 2008; these have been updated to 31 December 2011 by qualified independent actuaries.

The amounts shown below relate to the Company's share of obligations arising from membership by the Company's employees of the defined benefit schemes operated by the Company's ultimate parent company.

The amounts recognised in the Group's balance sheet are as follows:

	2011 £ m	2010 £ m
Fair value of scheme assets	150	150
Present value of defined benefit obligations	(180)	(201)
Unrecognised losses	3	25
Liability recognised in the balance sheet	(27)	(26)

The above amount is generally expected to be settled more than one year after the reporting date (2010: more than one year).

The movements in the liability recognised in the balance sheet are as follows:

	2011 £ m	2010 £ m
At 1 January	26	27
Exchange and other	-	(1)
At 31 December	26	26

The following information relates to the LBG Schemes as at 31 December 2011

In accordance with IAS 19 "Employee Benefits", the remaining information below relates to the LBG Schemes operated by the Company's ultimate parent company.

The Company's ultimate parent company expects to pay contributions of approximately £224m in respect of the LBG Schemes in 2012.

Movements in the present value of defined benefit obligations during the year are as follows:

	2011 £ m	2010 £ m
At 1 January	16,627	16,962
Merger of No1 and AMC schemes	-	31
Current service costs	166	175
Interest cost on benefit obligations	897	931
Benefits paid	236	(622)
Actuarial gains	(604)	(278)
Past service cost	10	19
Curtailment	-	(591)
At 31 December	17,332	16,627

Movements in the fair value of scheme assets during the year are as follows:

	2011 £ m	2010 £ m
At 1 January	16,290	14,662
Merger of No1 and AMC schemes	-	30
Expected return on scheme assets	1,009	952
Contributions received	413	216
Benefits paid	146	(622)
Actuarial gains	(604)	1,052
At 31 December	17,254	16,290

The principal actuarial and financial assumptions used in the valuations of all of the Lloyds Banking Group's defined benefit pension schemes, including the No's 1 and 2 schemes, were as follows:

	2011 %	2010 %
Rate of inflation – Retail Prices Index	3.00	3.40
Rate of inflation – Consumer Price Index	2.00	2.90
Rate of salary increases	2.00	2.00
Rate of increase for pensions in payment and deferred pensions	2.80	3.20
Discount rate	5.00	5.50

The sensitivity of the LBG Scheme's deficit at the reporting date to changes in the key assumptions set out above is set out below. The table demonstrates the effect of change in key assumptions whilst other assumptions remain unchanged. Numbers in brackets represent an increase in a deficit or a reduction in a surplus.

	2011 £ m	2010 £ m
0.2% (2009: 0.2%) increase in discount rate	909	930
0.2% (2009: 0.2%) decrease in discount rate	(957)	(976)
0.2% (2009: 0.2%) increase in inflation rate	(798)	(791)
0.2% (2009: 0.2%) decrease in inflation rate	783	754
1 year increase in life expectancy	(655)	(620)
1 year decrease in life expectancy	667	632

In addition, the mortality assumptions used for the LBG Schemes are illustrated by the following years of life expectancy in retirement:

	2011 Years	2010 Years
Life expectancy for member aged 60, on the valuation date		
Men	27	27
Women	28	28
Life expectancy for member aged 60, 15 years after the valuation date		
Men	29	29
Women	30	30

The mortality assumptions used in the scheme valuations are based on standard tables published by the Institute and Faculty of Actuaries which were adjusted in line with both current industry experience and the actual experience of the relevant schemes.

An analysis of the impact of a reasonable change in these assumptions is provided in the 2011 annual report and accounts of the LBG. Copies of the 2011 annual report and accounts of LBG may be obtained from the Group Secretary's Department, Lloyds Banking Group plc, 25 Gresham Street, London, EC2V 7HN.

The expected return on scheme assets for all of the Lloyds Banking Group's schemes, including the No's 1 and 2 schemes, is based on the following assumptions:

	2011 %	2010 %
Equities	8.3	8.3
Fixed interest gilts	4.0	4.5
Index linked gilts	3.9	4.1
Non-government bonds	4.9	6.0
Property	7.3	7.5
Money market instruments and cash	3.9	4.3

The expected return on scheme assets in 2012 for all of the Lloyds Banking Group's schemes, including the No's 1 and 2 schemes, uses the following assumptions:

	2012 %
Equities	7.3
Fixed interest gilts	3.0
Index linked gilts	2.8
Non-government bonds	4.9
Property	6.6
Money market instruments and cash	2.6

Composition of scheme assets:

	2011 £ m	2010 £ m
Equities	6,495	7,481
UK fixed interest gilts	391	540
UK index linked gilts	4,692	3,188
Sterling non-government bonds	2,882	2,248
Property	1,311	1,323
Derivative assets	642	837
Cash, and other assets and liabilities	841	673
At 31 December	17,254	16,290

The assets of all the funded pension plans are held independently of the Lloyds Banking Group's assets in separate trustee administered funds.

The expected return on plan assets is determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields at the reporting

date. Expected returns on equity and property investments reflect long-term real rates of return experienced in the respective markets.

Experience adjustments history relating to the Lloyds Banking Group's schemes (since the adoption of IAS 19):

	2011 £ m	2010 £ m	2009 £ m	2008 £ m	2007 £ m
Fair value of scheme assets	17,332	16,290	14,662	12,433	14,746
Present value of defined benefit obligation	(17,254)	(16,627)	(16,962)	(14,089)	(15,303)
	78	(337)	(2,300)	(1,656)	(557)
Unrecognised actuarial losses/(gains)	(769)	679	2,146	217	(1,234)
Asset/(liability) in the Lloyds Banking Group balance sheet	(691)	342	(154)	(1,439)	(1,791)
Experience losses on scheme liabilities	(132)	(466)	(3)	(29)	(180)
Experience gains/(losses) on scheme assets	146	1,052	440	(3,227)	147

The expense recognised in the statement of comprehensive income comprises:

	2011 £ m	2010 £ m
Current service cost	166	175
Interest cost on benefit obligation	897	931
Expected return on scheme assets	(1,009)	(952)
Past service cost	10	19
Amortisation outside corridor	-	48
Immediate recognition of curtailment	-	89
Curtailment	-	(591)
Total pension expense	64	(281)

34. Accruals and deferred income

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Accrued expenses	117	17	128	23
Deferred income	134	1,338	129	1,204
Total	251	1,355	257	1,227

Of the above total, £89m Group and £1,165m Company (2010: £100m Group and £1,066m Company) is expected to be settled more than one year after the reporting date.

35. Subordinated debt

The carrying value shown in the balance sheet is as follows:

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	Company	Group	Company
Subordinated debt	1,745	1,345	1,360	1,360
Issue costs	13	4	5	5
	1,758	1,349	1,365	1,365
Accrued interest on subordinated debt	26	7	8	8
Fair value hedge adjustment	91	68	37	37
Total	1,875	1,424	1,410	1,410

Company	2011		2010	
	£ m	£ m	£ m	£ m
	Carrying value	*Fair value*	*Carrying value*	*Fair value*
Undated subordinated liabilities	624	364	610	454
Dated subordinated liabilities	800	820	800	800
Total	1,424	1,184	1,410	1,254

Details of the subordinated liabilities issued and loaned to the Company are as follows: 1) £560m of step-up perpetual subordinated notes issued by the Company, in September 2005. Redemption of the notes is at the option of the Company, and is generally not allowable prior to the first call date on 24 September 2015. Interest is payable on an annual basis at a rate of 5.125% until the first call date, after which point interest is payable on a variable rate basis at three monthly intervals. Repayment of the notes is subordinate to the claims of the Company's senior creditors, including all policyholders.

The interest rate risk of the notes is managed using a derivative which is accounted for using hedge accounting, as set out in note 22.

2) £800m of floating rate subordinated notes, issued by the Company in June 2010. Redemption of the notes is due in 2040. However, the notes may be redeemed at an earlier date provided that certain conditions, including the provision of six months' written notice of the intention to redeem, are met. Interest is payable on a quarterly basis at a rate of 3 month LIBOR plus 5.1%. Repayment of the notes is subordinate to the claims of the Company's senior creditors, including all policyholders.

Group	2011		2010	
	£ m	£ m	£ m	£ m
	Carrying value	*Fair value*	*Carrying value*	*Fair value*
Undated subordinated liabilities	899	603	610	454
Dated subordinated liabilities	976	969	800	800
Total	1,875	1,572	1,410	1,254

Details of the subordinated liabilities issued and loaned to the Group's subsidiary CMIG by Clerical Medical Finance plc are as follows:

£51m of 7.375% undated Subordinated Guaranteed Bonds, the redemption of which is at the option of Clerical Medical Finance plc and is generally not allowable prior to 5 November 2019. The interest rate charged to CMIG by Clerical Medical Finance plc is 7.61%.

€219m of 6.45% dated Subordinated Guaranteed Bonds maturing on 5 July 2023. Redemption of the bonds is at the option of Clerical Medical Finance plc and is generally not allowable prior to July 2013, after which time if the bond has not been redeemed floating rate interest is payable. The interest rate charges to CMIG by Clerical Medical Finance plc is 6.555%

€388m of 4.25% undated Subordinated Guaranteed Bonds. Redemption of the bonds is at the option of Clerical Medical Finance plc and is generally not allowable prior to 27 June 2015, after which time if the bond has not been redeemed floating rate interest is payable. The interest rate charged to the CMIG by Clerical Medical Finance plc is 4.27%. An interest rate swap has been put in place in respect of the €388m tranche of the subordinated debt, which is accounted for using hedge accounting, as set out in note 1 (z).

The fair value of undated subordinated liabilities has been calculated using published bid prices at the reporting date. The fair value of dated subordinated liabilities has been assessed by management with reference to published prices.

36. Non-participating investment contract liabilities

An analysis of the change in net investment contract liabilities is as follows:

Group	2011 Gross £ m	2011 Reinsurance £ m	2011 Net £ m	2010 Gross £ m	2010 Reinsurance £ m	2010 Net £ m
At 1 January	16,226	-	16,226	15,774	-	15,774
Adjustment on acquisition	12,084	76	12,008			
New business	392	3	389	236	-	236
Changes in existing business	(2,328)	(14)	(2,316)	216	-	216
At 31 December	26,374	65	26,309	16,226	-	16,226

Company	2011 Gross £ m	2011 Reinsurance £ m	2011 Net £ m	2010 Gross £ m	2010 Reinsurance £ m	2010 Net £ m
At 1 January	13,852	10,375	3,477	13,498	9,807	3,691
New business	246	221	25	83	40	43
Changes in existing business	(412)	(85)	(327)	271	528	(257)
At 31 December	13,686	10,511	3,175	13,852	10,375	3,477

An analysis of the contractual and expected maturities of non-participating investment contract liabilities is given in note 42.

37. Other financial liabilities

	2011 £ m *Group*	2011 £ m *Company*	2010 £ m *Group*	2010 £ m *Company*
Insurance business:				
Amounts payable in respect of direct insurance business	425	216	251	227
Amounts payable on reinsurance contracts	17	-	-	-
Other liabilities:				
Due to related parties	707	566	2,303	2,245
Due to brokers	289	179	147	27
Repurchase creditor	287	-	-	-
Other	510	128	430	153
Total	2,235	1,089	3,131	2,652

Of the above total, £274m Group (2010: £nil Group) is expected to be settled more than one year after the reporting date. All of the Company balance is expected to be settled within one year of the reporting date (2010: all of the balance). Included within other liabilities, as required by IAS 32 "Financial Instruments: Presentation", is £100 of 6% cumulative preference shares issued by the Company during 2005.

38. Borrowings

	2011 £m *Group*	2011 £ m *Company*	2010 £m *Group*	2010 £ m *Company*
Bank overdrafts	7	4	11	4
Total	7	4	11	4

The fair value of the balances set out above is not materially different to the carrying value due to the short-term nature of these balances.

39. (Increase)/decrease in operating assets and liabilities

	2011		2010	
	£ m	£ m	£m	£ m
	Group	*Company*	*Group*	*Company*
Increase in operating assets:				
Retirement benefit surplus	-	-	(88)	-
Deferred costs	(70)	25	(67)	1
Investment properties	208	62	(294)	(132)
Assets arising from reinsurance contracts held	(3,894)	(1,901)	(87)	(2,982)
Investment in joint ventures	-	(17)	(13)	(9)
Prepayments	10	1	(18)	(2)
Financial assets:				
Derivative financial instruments	(415)	(48)	(91)	(34)
Loans and receivables	2,100	569	(2,101)	(2,106)
Investments at fair value through income	14,319	2,580	(4,919)	(1,994)
Net increase/(decrease) in operating assets	12,258	1,271	(7,678)	(7,258)
Increase in operating liabilities:				
Insurance contract and participating investment contract liabilities	(497)	871	3,796	3,773
Unallocated surplus	(366)	(85)	(3)	(3)
Pension and other post retirement benefit obligation	(26)	-	(18)	-
Provision for other liabilities and charges	164	-	4	-
Accruals and deferred income	(293)	128	44	78
Financial liabilities:				
Subordinated debt	12	14	825	825
Non-participating investment contract liabilities	(1,937)	(166)	453	354
Derivative financial instruments	534	295	268	232
Other financial liabilities	(2,130)	(1,563)	2,358	2,177
External interest in mutual investment funds	8,101	-	266	-
Net increase/(decrease) in operating liabilities	3,562	(506)	7,993	7,436
Net decrease in operating assets and liabilities	15,820	765	315	178

40. Dividends paid

	2011 £ m	2010 £ m
Total dividends paid on equity shares	-	210

The dividend paid in the year amounted to nil pence per share (2010: 32.4 pence per share).

41. Insurance and investment contract liabilities – assumptions, change in assumptions and sensitivities

Policyholder liabilities can be analysed into With Profit Fund liabilities and non-participating fund liabilities. In accordance with FRS 27, the liabilities of the With Profit Funds are accounted for using the "realistic" capital regime of the FSA ("realistic" liabilities). All non-participating liabilities are accounted for using a traditional prospective actuarial discounted cash flow methodology.

(1) Processes used to determine key assumptions in respect of insurance and investment contracts

(a) Liabilities of the With Profits Funds calculated on a "realistic" basis

The Group has With Profits Funds within the Company and its subsidiary CMIG containing both insurance and participating investment contracts. The main components of the realistic liabilities are:

- with profits benefit reserves, i.e. the total asset shares for with-profits policies;
- the costs of options and guarantees;
- deductions levied against asset shares; and
- the impact of smoothing policy.

The realistic assessment is carried out using a stochastic simulation model which values liabilities on a market consistent basis. The calculation of realistic liabilities uses best estimate assumptions of e.g. mortality, persistency and expenses.

The processes for determining the key assumptions are set out below, and remain unchanged from the prior year:

- Investment returns and discount rates

  A stochastic economic scenario generator, which uses recognised asset models, provides future asset value and yield scenarios; these determine investment returns for each scenario. The economic scenario generator is calibrated to observable yield curves and option prices where possible. Nominal interest rates are modelled using a standard interest rate model, calibrated to risk-free yields. The risk-free yield is defined as the spot yield derived from the UK gilt yield curve. The liabilities are valued by discounting projected future cashflows using the risk free yield.

- Investment volatility

  The volatility of future equity returns in excess of nominal interest rates has been calibrated to ten-year at-the-money-forward options on appropriate indices. The indices used are the FTSE-100, the EuroStoxx-50, and the S&P 500. For property, no observable prices exist and so volatility has been derived from analysis of historic data.

- Mortality

  The mortality assumptions, including allowances for improvements in longevity for annuitants, are based on recent actual experience, industry tables and projection models, and mortality rates implied by indicative reinsurance terms.

- Persistency

  Persistency is a function of both the rate of policy termination and the rate at which policyholders stop paying regular premiums. The assumed levels of these rates are based on a combination of historical experience and management's views on future experience taking into consideration potential changes that may result from guarantees and options becoming more valuable under adverse market conditions.

- Maintenance expenses

  Allowance is made for the charges applied to the With Profits Funds and these are, for conventional with-profits business, governed by the relevant Schemes of Transfer.

- Guaranteed annuity option take-up rates

  The guaranteed annuity option take-up rates are set with regard to the Company's recent actual experience, increased to reflect future uncertainties where the exercise of options by policyholders might increase liabilities.

(b) Liabilities outwith the With-Profit Funds

(i) Insurance contracts and investment contracts with discretionary participation feature

The liabilities of the Group and Company are determined on the basis of recognised actuarial methods and consistently with the approach to be used for the FSA returns. 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 probabilities of occurrence.

The liabilities will vary with movements in interest rates (this applies in particular to the cost of guaranteed benefits payable in the future) and with movements in the cost of life assurance and annuity benefits for which future mortality is uncertain.
Assumptions are made in respect of all material factors affecting future cashflows, including future interest rates, mortality and costs. Generally, assumptions used to value the liabilities contain a margin for adverse deviation and are determined as required by FSA rules. This margin for adverse deviation is based on management's judgment and reflects management's views on the inherent level of uncertainty. The assumptions to which the liabilities are most sensitive are the interest rates used to discount the cashflows and the mortality assumptions, particularly those for annuitants.

The key assumptions used in the measurement of the non-participating fund liabilities are:

- **Interest rates**

  The rates used are derived consistently with the approach to be used for the FSA returns. 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. Margins for risk are allowed for in the assumed interest rates. These are derived from the limits contained in the FSA Rules, including reductions made to the available yields to allow for default risk based upon the credit rating of each stock, and an over-riding restriction which limits the yield from investments in property by reference to the yield from appropriate long-term gilts.

- **Mortality and morbidity**

  The mortality and morbidity assumptions, including allowances for improvements in longevity for annuitants, are set with regard to the Group's actual experience where this provides a reliable basis, and relevant industry data otherwise, and includes a margin for adverse deviation. The assumptions have additional margins over the With Profit Fund assumptions, as required by FSA regulations. Improvements in female annuitant mortality are assumed to follow the CMI 2011

projection for females from the Actuarial profession's mortality committee with a long term rate of improvement of 1.5% per annum. Similarly improvements in male annuitant mortality are assumed to follow the CMI 2011 projection for males from the Actuarial Profession's mortality committee with a long term rate of improvement of 1.5% per annum.

- **Maintenance expenses**

  Allowance is explicitly made for future policy costs. Expense loadings are determined by reference to an internal analysis of current and expected future expense levels, plus a margin for adverse deviations. Explicit allowance is made for future expense inflation from the valuation date. No allowance is made for any expected reductions in expense levels that have not occurred at the valuation date.

- **Persistency rates**

  Prudent lapse rate assumptions have been used for term assurance business. Whether a lapse rate is prudent broadly depends on whether the policy liability is negative or positive at any point in its life, thus for each policy a high lapse rate is assumed at points where the projected liability is negative and a low lapse rate is assumed at points where the projected liability is positive.

(ii) Investment contracts without discretionary participation feature

These contracts are unit-linked, and the liability is determined as the value of the units allocated to the contracts plus an allowance for other amounts not reflected in the unit value.

(2) Key assumptions

(a) With Profits Fund - Scottish Widows plc

Assumptions are set for the "realistic" valuation of the Company's With Profits Fund. In addition, liabilities in respect of non-participating policies in the With Profits Fund were also accounted for on the regulatory assessment.

(i) Investment returns and discount rates

In the "realistic" valuation of liabilities in calibrating the economic scenario generator, the risk-free yield curve is defined as the yield curve for UK gilts.

The following interest rates are assumed in the regulatory valuation of non-participating policies in the With Profits Funds:

Class of business	2011 Interest Rate (Net)	2010 Interest Rate (Net)
Annuities in Payment	3.50%	4.50%
Deferred Annuities	3.40%	3.90%

(ii) Investment volatility (realistic liabilities only)

The calibration of the stochastic simulation model uses implied volatilities of derivatives where possible, or historical observed volatility where it is not possible to observe meaningful prices. For example, as at 31 December 2011, the 10 year-equity-implied-at-the-money assumption was set at 27.2 per cent (26.1 per cent as at 31 December 2010). The assumption for property volatility was 15 per cent (31 December 2010: 15 per cent). The volatility of interest rates has been calibrated to the implied volatility of swaptions which was broadly 19 per cent as at 31 December 2011 (31 December 2010: 15 per cent).

(iii) Mortality assumptions

The mortality assumptions for the main classes of business are as follows:

		2011	2010
Assurances (excluding term assurances)			
Conventional With-Profits	Males		
	Smoker	81% AMS00 ult	81% AMS00 ult
	Non-smoker	73% AMN00 ult	73% AMN00 ult
	Unknown	68% AMC00 ult	68% AMC00 ult
	Females		
	Smoker	61% AFS00 ult	61% AFS00 ult
	Non-smoker	80% AFN00 ult	80% AFN00 ult
	Unknown	65% AFC00 ult	65% AFC00 ult
Unitised Assurances	Males	52% AMC00 ult	57% AMC00 ult
	Females	62% AFC00 ult	64% AFC00 ult

		2011	2010
Annuities			
Self-employed / Personal Pensions	Males	84% RMV 2000 ult CMI_2011_M_1.25%	81% RMV 2000 ult mc(1.25%)
	Females	103% RFV 2000 ult CMI_2011_F_1.25%	88% RFV 2000 ult 75%mc(1.25%)
Other Annuities in payment	Males	90-113% PCMA 2000 ult CMI_2011_M_1.25%	95 - 106% PCMA 2000 ult mc(1.25%)
	Females	93-106% PCFA 2000 ult CMI_2011_F_1.25%	85 - 98% PCFA 2000 ult 75%mc(1.25%)
Deferred Annuities	Males	85% AMC00 ult *	85% AMC00 ult *
	Females	77% AFC00 ult *	77% AFC00 ult *

With regard to the above tables:

'mc' denotes that explicit provision for future mortality improvement is made by applying the 'Medium Cohort' projection factors from the Actuarial profession's Continuous Mortality Investigation for the period starting on 31 December 2002 to the 2000 base tables (adjusted as above). 75% means 75% of the 'Medium Cohort' projection factors are used. If a percentage is shown in brackets this is a minimum annual improvement rate for all future years and ages.

For end 2011, 'CMI_2011_M_1.25%' denotes that future improvement factors, which are applied from 31 December 2002, are taken from CMI 2011 tables for males, with a long term improvement rate of 1.25% per annum. Similarly 'CMI_2011_F_1.25%' tables are used for females. CMI_2011 denotes that explicit provision for future mortality improvement is made by applying the 2011 version of Continuous Mortality Investigation mortality projection model released in November 2011.

* For deferred annuities an explicit provision for future improvement has been made by assuming mortality in deferment reduces at a rate of 3% pa from the valuation date through deferment.

(iv) Other assumptions

Deferred annuity contracts with a guaranteed-rate annuity option have been valued based upon an assumed rate of take-up of the guaranteed annuity option of 85.0% for the realistic assessment (85.0% assumed at 31 December 2010).

(b) With Profits Fund - Clerical Medical Investment Group Limited

Assumptions are given for the "realistic" valuation of CMIG's With Profits Fund. In addition, liabilities in respect of non-participating policies in the With Profits Fund were also accounted for on the traditional regulatory assessment.

(i) Investment returns and discount rates

In the "realistic" valuation of liabilities in calibrating the economic scenario generator, the risk-free yield curve is defined as the yield curve for UK gilts.

(ii) Investment volatility (realistic liabilities only)

The calibration of the stochastic simulation model uses implied volatilities of derivatives where possible, or historical observed volatility where it is not possible to observe meaningful prices. For example, as at 31 December 2011, the 10 year-equity-implied-at-the-money assumption was set at 27.2% (26.1% as at 31 December 2010). The assumption for property volatility was 15% (31 December 2010: 15%). The volatility of interest rates has been calibrated to the implied volatility of swaptions which was broadly 19% as at 31 December 2011 (31 December 2010: 15%).

(iii) Mortality assumptions

The mortality assumptions for the main classes of business are as follows:

		2011
Assurances (excluding term assurances)		
Conventional With-Profits	Males	50% AMC00 Ultimate
	Females	60% AFC00 Ultimate
Unitised Assurances	Males	90% AMC00 Ultimate
	Females	95% AFC00 Ultimate
Annuities		
Self-employed / Personal Pensions	Males	96% PCMA00 CMI_2011_M_1.25%
	Females	94% PCFA00 CMI_2011_F_1.25%
Other Annuities in payment	Males	96% PCMA00 CMI_2011_M_1.25%
	Females	94% PCFA00 CMI_2011_F_1.25%
Deferred Annuities	Males	96% PCMA00
	Females	CMI_2011_M_1.25%) 94% PCFA00 CMI_2011_F_1.25%

With regard to the above tables:

'CMI_2011_M_1.25%' denotes that future improvement factors, which are applied from 31 December 2002, are taken from CMI 2011 tables for males, with a long term improvement rate of 1.25% per annum. Similarly 'CMI_2011_F_1.25%' tables are used for females. CMI_2011 denotes that explicit provision for future mortality improvement is made by applying the 2011 version of Continuous Mortality Investigation mortality projection model released in November 2011.

(iv) Other assumptions

Deferred annuity contracts with a guaranteed-rate annuity option have been valued based upon an assumed rate of take-up of the guaranteed annuity option of 85.0% for the realistic assessment (85.0% assumed at 31 December 2010).

(c) Non-participating funds

The principal assumptions underlying the calculation of the each of the Group's subsidiaries non-participating fund liabilities are given below.

(i) Investment returns and discount rates

Scottish Widows plc

Class of business	2011 Interest rate (net) %	2010 Interest rate (net) %
Conventional Life business and non-unit reserves on linked life business	1.92	2.48
Annuities in payment reinsured to Scottish Widows Annuities Limited	3.37	4.28

Clerical Medical Investment Group Limited

Class of business	2011 Interest rate (net) %
Conventional Life business and non-unit reserves on linked business	0.57
Annuities in payment	2.54

Halifax Life Limited

Class of business	2011 Interest rate (net) %
Non-unit reserves on linked business	0.71
Annuities in payment	1.64

St Andrew's Life Assurance plc

Class of business	2011 Interest rate (net) %
Conventional Life business	0.57
Non-unit reserves on linked business	0.57

(ii) Mortality assumptions

Scottish Widows plc

The mortality assumptions for the main classes of business are as follows:

		2011	2010
Term Assurances			
	Males		
	Smoker	95-160% TMS00(5) select	100-165% TMS00(5) select
	Non smoker	90-180% TMN00(5) select	90-170% TMN00(5) select
	Unknown	90% TMN00(5) select to 150% TMC00(5) select	90% TMN00(5) select to 165% TMC00(5) select
	Females		
	Smoker	90-130% TFS00(5) select	90-130% TFS00(5) select
	Non smoker	95-190% TFN00(5) select	95-190% TFN00(5) select
	Unknown	95% TFN00(5) select to 150% TFC00(5) select	95% TFN00(5) select to 155% TFC00(5) select

		2011	2010
Annuities			
Purchased (whole life)	Males	94% IML 2000 ult CMI_2011_M_1.5%	74% IML 2000 ult mod lc (1.5%)
	Females	84% IFL 2000 ult CMI_2011_F_1.5%	100% IFL 2000 ult 75%mc (1.5%)
Self-employed / personal Pensions	Males	76% RMV 2000 ult CMI_2011_M_1.5%	73% RMV 2000 ult mod lc (1.5%)
	Females	93% RFV 2000 ult CMI_2011_F_1.5%	80% RFV 2000 ult 75%mc (1.5%)
Other Annuities in payment	Males	82 - 113% PCMA 2000 ult CMI_2011_M_1.5%	86 - 108% PCMA 2000 ult mod lc (1.5%)
	Females	84 - 96% PCFA 2000 ult CMI_2011_F_1.5%	78 - 89% PCFA 2000 ult 75%mc (1.5%)
Deferred annuities	Males	75% AMC00 ult *	75% AMC00 ult *
	Females	70% AFC00 ult *	70% AFC00 ult *

With regard to the above tables:

For end 2010: 'mod lc' denotes that explicit provision for future mortality improvement is made by applying, for the period starting on 31 December 2002, 100% of the 'Medium Cohort' projection factors until 31 December 2006, and thereafter 100% of the 'Long Cohort' projection factors from the Actuarial profession's Continuous Mortality Investigation Committee to the 2000 base tables (adjusted as above). 'mc' denotes that explicit provision for future mortality improvement is made by applying the 'Medium Cohort' projection factors from the Actuarial profession's Continuous Mortality Investigation for the period starting on 31 December 2002 to the 2000 base tables (adjusted as above). 75%mc means 75% of the 'Medium Cohort' projection factors are used. If a percentage is shown in brackets this is a minimum annual improvement rate for all future years and ages.

For end 2011, 'CMI_2011_M_1.5%' denotes that future improvement factors, which are applied from 31 December 2002, are taken from CMI 2011 tables for males, with a long term improvement rate of 1.5% per annum. Similarly 'CMI_2011_F_1.5%' tables are used for females.

* For deferred annuities, 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.

Clerical Medical Investment Group Limited

The mortality assumptions for the main classes of business are as follows:

		2011
Term Assurances		
	Males	57.5% TMC00 Select
	Females	63.25% TFC00 Select
Annuities		
Purchased (whole life)	Males	86.4% PCMA00 CMI_2011_M_1.5%
	Females	84.6% PCFA00 CMI_2011_F_1.5%
Self-employed / personal Pensions	Males	86.4% PCMA00 CMI_2011_M_1.5%
	Females	84.6% PCFA00 CMI_2011_F_1.5%
Other Annuities in payment	Males	86.4% PCMA00 CMI_2011_M_1.5%
	Females	84.6% PCFA00 CMI_2011_F_1.5%
Deferred annuities	Males	86.4% PCMA00 CMI_2011_M_1.5%
	Females	84.6% PCFA00 CMI_2011_F_1.5%

With regard to the above tables:

'CMI_2011_M_1.5%' denotes that future improvement factors, which are applied from 31 December 2002, are taken from CMI 2011 tables for males, with a long term improvement rate of 1.5% per annum. Similarly 'CMI_2011_F_1.5%' tables are used for females.

Halifax Life Limited

The mortality assumptions for the main classes of business are as follows:

Product	2011	
	Male	**Female**
UL Individual Pensions Regular Premium	83% AMC00 U	77% AFC00 U
UL Individual Pensions Single Premium	83% AMC00 U	77% AFC00 U
UL Group Pension	94% AMC00 U	88% AFC00 U
Pension Annuities	86% PCMA00 CMI_2011_M_1.5%	85% PCFA00 CMI_2011_F_1.5%
Deferred Annuities	86% PCMA00 CMI_2011_M_1.5%	85% PCFA00 CMI_2011_F_1.5%

With regard to the above tables:

'CMI_2011_M_1.5%' denotes that future improvement factors, which are applied from 31 December 2002, are taken from CMI 2011 tables for males, with a long term improvement rate of 1.5% per annum. Similarly 'CMI_2011_F_1.5%' tables are used for females.

St Andrew's Life Assurance plc

The mortality assumptions for the main classes of business are as follows:

Term Assurances	2011
Males	
Smoker	97.75% TMS00U
Non-Smoker	97.75% TMN00U
Females	
Smoker	97.75% TFS00U
Non-Smoker	115% TFN00U

Investment Bonds	2011	2010
Males	77% AMC00U	66% AMC00U
Females	93.5% AFC00U	83% AFC00U

(3) The effect of changes in key assumptions

(a) With Profits Funds

There is no net impact on profit before tax of the changes in key assumptions within the With Profits Funds as any change in policyholder liabilities is offset by an equal and opposite movement in the unallocated surplus of the long-term business.

(b) Non-participating funds

Changes in certain key assumptions were made during 2011 with the following impacts on profit after tax:

	Impact on profit after tax £m	Impact on profit after tax £m
	Group	*Company*
Variable		
Mortality	190	13
Expenses	161	49
Default deductions	(146)	(2)
Inflation	92	17

(4) Sensitivity analysis (in respect of insurance and participating investment contracts only)

(a) With Profits Funds

There is no net impact on profit before tax of the changes in key assumptions within the With Profits Funds as any change in policyholder liabilities is offset by an equal and opposite movement in the unallocated surplus of the long-term business.

(b) Non-participating funds

The following table demonstrates the effect of changes in key assumptions on profit after tax assuming that the other assumptions remain unchanged. In practice this is unlikely to occur, and changes in some assumptions may be correlated.

Variable	Change in variable	Impact on profit after tax £ m	Impact on profit after tax £ m
		Group	*Company*
Annuitant Mortality	5% reduction	(135)	(5)
Other Mortality	5% reduction	26	15
Lapses	10% reduction	(32)	(5)
Maintenance expenses	10% reduction	110	30
Interest rate – change in redemption yield [1]	0.25% reduction	(44)	(3)
Interest rates – change in valuation margin [2]	0.25% reduction	(221)	n/a

(1) This interest rate sensitivity shows the impact of a 0.25 per cent movement in gilt yields and all of the consequential impacts on key economic assumptions including the investment returns, the valuation rates of interest and values of assets backing the business in question. This excludes any impact on assets not backing the liabilities.

(2) This interest rate sensitivity shows, for pensions annuity business, the impact of a change to the valuation rate of interest without a corresponding change to asset yields; this would increase the margin available to cover default and other risks.

42. Risk management

The principal activity of the Group is the undertaking of ordinary long-term insurance and savings business and associated investment activities in the United Kingdom. The Group offers a wide range of life insurance products such as annuities, pensions, whole life, term life and investment type products through independent financial advisers, the Lloyds Banking Group network and direct sales. The Company also reinsures business with subsidiary undertakings and with insurance entities external to the Group. This includes the majority of the pensions linked business, which is reinsured to the Company's subsidiary, SWUF, the annuity business which is reinsured to the Company's subsidiary SWA, and new protection business, which is reinsured to the Company's subsidiary, CMIG.

The Group assesses the relative costs and concentrations of each type of risk through the Individual Capital Assessment ("ICA") and material issues are escalated to the Insurance Risk Committee and the Insurance Executive Committee.

This note summarises these risks and the way in which the Group manages them.

(a) Governance framework

The Group is part of Lloyds Banking Group ("LBG"), which has established a risk management function with responsibility for implementing the Lloyds Banking Group risk management framework within the Group.

Responsibility for the setting and management of risk appetite and risk policy resides with the Board of each Group company. The Board manages risks in line with LBG and Insurance Division risk policies. The Board has delegated operational implementation to the Insurance Executive Committee.

The approach to risk management ensures that there is effective independent checking or "oversight" of key decisions through the operation of a "three lines of defence" model. The first line of defence is line management, who have direct accountability for risk decisions. The Risk function provide oversight and challenge and form the second line of defence. Internal Audit constitutes the third line of defence, which provides the required independent assurance to the Audit Committee and the Board that risks within the Group are recognised, monitored and managed within acceptable parameters.

An enterprise-wide risk management framework for the identification, assessment, measurement and management of risk is in place. The framework is in line with Lloyds Banking Group's risk management principles and covers the full spectrum of risks that the Group and Company are exposed to. Under this framework, risks are categorised according to an approved Lloyds Banking Group risk language which has been adopted across the Group. This covers the principal financial risks faced by the Group, including the exposures to market, insurance, credit, financial soundness and operational risk. The performance of the Group, its continuing ability to write business and the strategic management of the business depend on its ability to manage these risks.

Policy owners, identified from appropriate areas across the business, are responsible for drafting the Lloyds Banking Group and Insurance risk policies, for ensuring that they remain up-to-date and for facilitating any changes. These policies are subject to at least an annual review, or earlier if deemed necessary. Limits are prescribed within which those responsible for the day to day management of each Group company can take decisions. Line management are required to follow prescribed reporting procedures to the bodies responsible for monitoring compliance with policy and controlling the risks.

(b) Risk appetite

The Board has defined the methodology for the management of risk appetite and approved appropriate limits. Limits are defined for the Scottish Widows Group as a whole and for the individual risk components. The limits are defined in terms of the amount of capital required to be held to cover certain specified stressed scenarios.

Exposure to each type of risk is monitored against prescribed limits and the results of these tests are reported to the Boards of the relevant companies. Where the exposure to any risk exceeds a trigger amount, the Insurance Executive Committee must approve an action plan to reduce the exposure or the Scottish Widows Group Board must approve a revised limit.

(c) Financial risks

The Group writes a variety of insurance and investment contracts which are subject to a variety of financial risks, as set out below. Contracts can be either single or regular premium and conventional (non-profit), with-profits or unit-linked in nature.

The Group is exposed to a range of financial risks through its financial assets, financial liabilities, reinsurance assets and insurance and investment contract liabilities. In particular, the key financial risk is that long-term investment proceeds are not sufficient to fund the obligations arising from its insurance and investment contracts. The most important components of financial risk are market, insurance, credit and financial soundness risk.

The market risks that the Group primarily faces due to the nature of its investments and liabilities are interest rate, equity, property and foreign exchange risk.

The Group manages these risks in a numbers of ways, including risk appetite assessment and monitoring of capital resource requirements. In addition, the Principles and Practices of Financial Management ("PPFM") set out the way in which the with-profits business is managed. The Group also uses financial instruments (including derivatives) as part of its business activities and to reduce its own exposure to market risk and credit risk.

For with-profits business, subject to minimum guarantees, policyholders' benefits are influenced by the smoothed investment returns on assets held in the With Profits Funds. The smoothing cushions policyholders from daily fluctuations in investment markets. This process is managed in accordance with the published PPFM's.

The Group bears financial risk in relation to the guaranteed benefits payable under these contracts. The amount of the guaranteed benefits increases as additional benefits are declared and allocated to policies.

For unit-linked business, policyholders' benefits are closely linked to the investment returns on the underlying internal funds. In the short term, profit and equity are therefore largely unaffected by investment returns on assets in internal unit-linked funds as any gains or losses will be largely offset by changes in the corresponding insurance and investment contract liabilities, provided that there is appropriate matching of assets and liabilities within these funds. However, any change in the market value of these funds will have an indirect impact on the Group and Company through the collection of annual management and other fund related charges. As markets rise or fall, these charges rise or fall correspondingly.

For non-participating business, the principal market risk is interest rate risk, which arises because assets and liabilities may exhibit differing changes in market value as a result of changes in interest rates. Asset and liability matching is used to mitigate the impact of changes in interest rates. Where there is no matching the difference is not material.
Financial assets and financial liabilities are measured on an ongoing basis either at fair value or at amortised cost. The summary of significant accounting policies (note 1) describes how the classes of financial instruments are measured and how income and expenses, including fair value gains and losses, are recognised.

The timing of the unwind of the deferred tax assets and liabilities is dependent on the timing of the unwind of the temporary timing differences, arising between the tax bases of the assets and liabilities and their carrying amounts for financial reporting purposes, to which these balances relate.

The sensitivity analyses given throughout this note are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur as changes in some of the assumptions may be correlated, for example changes in interest rates and changes in market values. The sensitivity analysis presented also represents, in accordance with the requirements of IFRS 7, management's assessment of a reasonably possible alternative in respect of each sensitivity, rather than worst case scenario positions.

(1) Market risk

Market risk is the risk of reductions in earnings and/or value, through financial or reputational loss, from unfavourable market movements. This risk typically arises from fluctuations in market prices (equity and property risk), market interest rates (interest rate risk) and foreign exchange rates (foreign exchange risk), whether such changes are caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

Investment holdings within the Group are diversified across markets and, within markets, across sectors. Holdings of individual assets are diversified to minimise specific risk and large individual exposures are monitored closely. For assets held outwith unit-linked funds, investments are only permitted in countries and markets which are sufficiently regulated and liquid.

Market risk policy is dependent on the nature of the funds in question, and can be broadly summarised as follows:

- Assets held in shareholder funds are invested in money market funds, gilts and investment grade bonds to match regulatory capital requirements. The balance of the shareholder fund assets is managed in line with the policies of the Lloyds Banking Group to optimise shareholder risk and return. This includes suitable use of derivatives to minimise shareholder risk.
- Unit-linked assets are invested in accordance with the nature of the fund mandates.
- Conventional non-profit liabilities are "close matched" as far as possible in relation to currency, nature and duration.
- With Profits liabilities are managed in line with the published PPFMs. Benchmarks and minimum and maximum holdings in asset classes are specified to allow limited investment management discretion whilst ensuring adequate diversification. Variable rate bonds and associated additional swap transactions provide significant protection to the With Profits Funds from the effects of interest rate falls in respect of the cost of guaranteed annuity rates.

An analysis of financial assets and financial liabilities at fair value through income according to their fair value hierarchy (as defined in note 1 (d)) is given below:

2011

Group

	Fair value hierarchy			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**
Equity securities	51,397	1	776	52,174
Debt securities	18,993	18,587	-	37,580
Deposits with credit institutions	-	-	-	-
Other investments	-	96	-	96
Derivative financial assets	14	1,376	-	1,390
Total assets	70,404	20,060	776	91,240
Derivative financial liabilities	32	1,130	-	1,162
Non-participating investment contract liabilities	-	26,374	-	26,374
Total liabilities	32	27,504	-	27,536

Company

	Fair value hierarchy			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**
Equity securities	6,702	-	238	6,940
Debt securities	4,077	4,865	-	8,942
Other investments	-	747	-	747
Derivative financial assets	2	223	-	225
Investment in subsidiaries at fair value	4,398	77	481	4,956
Total assets	15,179	5,912	719	21,810
Derivative financial liabilities	8	621	-	629
Non-participating investment contract liabilities	-	13,686	-	13,686
Total liabilities	8	14,307	-	14,315

2010

Group

	Fair value hierarchy			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**
Equity securities	34,832	-	480	35,312
Debt securities	9,480	11,164	-	20,644
Deposits with credit institutions	1,287	-	-	1,287
Other investments	-	162	-	162
Derivative financial assets	13	301	-	314
Total assets	45,612	11,627	480	57,719
Derivative financial liabilities	14	439	-	453
Non-participating investment contract liabilities	-	16,226	-	16,226
Total liabilities	14	16,665	-	16,679

Company

	Fair value hierarchy			
	Level 1	**Level 2**	**Level 3**	**Total**
	£m	**£m**	**£m**	**£m**
Equity securities	12,471	-	202	12,673
Debt securities	5,618	4,510	-	10,128
Deposits with credit institutions	10	-	-	10
Other investments	-	707	-	707
Derivative financial assets	2	175	-	177
Investment in subsidiaries at fair value	145	89	417	651
Total assets	18,246	5,481	619	24,346
Derivative financial liabilities	5	329	-	334
Non-participating investment contract liabilities	-	13,852	-	13,852
Total liabilities	5	14,181	-	14,186

Of the debt securities classified as Level 2 above, £1,263m of the Company assets and £2,026m of the Group assets (2010: £1,083m Company and £1,145m Group) have been valued using a modelled price or based on a price from a single broker. The models used to derive these prices use only observable data and are therefore level 2 rather than level 3. The remaining assets are priced using prices obtained via a price vendor. This vendor obtains prices from a number of different market makers in corporate bonds and calculates a consensus price to give the best reflection of the market price on that day. On the basis that this price may not be based on actual trades and as information regarding the volume of individual trades is not readily available, these assets have been classified as level 2 rather than level 1.

The derivative securities classified as Level 2 above have been valued using a tri-party pricing model as determined by the Pricing Source Agreement between SWIP and State Street. Prices are sourced from external sources, counterparties, and the Investment Manager. Where the primary value is within tolerance of the secondary value, the primary value will be utilised. If the primary and secondary values are out of tolerance, then the primary value will be validated against the tertiary value. If it is within tolerance the primary value will be applied. If primary and tertiary values are outwith tolerance, then the secondary value is validated against the tertiary value. If secondary and tertiary values are within tolerance, then the secondary value is applied. If they are out of tolerance then the investment manager is notified to allow them to make the final pricing decision.

Assets classified as level 3 comprise private equity investments and property investment vehicles. Private equity investments are valued using the financial statements of the underlying companies prepared by the general partners, adjusted for known cash flows since valuation and subject to a fair value review to take account of other relevant information. Property investment vehicles are valued based on the net asset value of the relevant company which incorporates surveyors' valuations of property. Whilst such valuations are sensitive to estimates, it is believed that changing one or more of the assumptions to reasonably possible alternative assumptions would not change the fair value significantly.

The table below shows movements in the assets and liabilities measured at fair value based on valuation techniques for which any significant input is not based on observable market data (level 3 only).

Group

	2011		**2010**	
	£m	**£m**	**£m**	**£m**
	Assets	*Liabilities*	*Assets*	*Liabilities*
Balance at 1 January	541	-	398	-
Adjustment on acquisition	387	-	-	
Net gains or losses recognised within net gains and losses on assets and liabilities at fair value though income in the statement of comprehensive income	(201)	-	62	-
Purchases	50	-	81	-
Balance at 31 December	777	-	541	-
Total gains and losses for the period included in the statement of comprehensive income for assets and liabilities held at 31 December	(201)	-	62	-

Company

	2011		2010	
	£m	£m	£m	£m
	Assets	*Liabilities*	*Assets*	*Liabilities*
Balance at 1 January	653		558	-
Total net gains or losses recognised within net gains and losses on assets and liabilities at fair value though income in the statement of comprehensive income	45	-	33	-
Purchases	21			
		-	62	-
Balance at 31 December	719	-	653	-
Total gains and losses for the period included in the statement of comprehensive income for assets and liabilities held at 31 December	45	-	33	-

Total gains or losses for the period included in the statement of comprehensive income, as well as total gains or losses relating to assets and liabilities held at the reporting date, are presented in the statement of comprehensive income, through net gains and losses on assets and liabilities at fair value through income and net fair value gains and losses on assets and liabilities at fair value through income respectively.

(i) Equity risk

The exposure of the Group's insurance and investment contract business to equity risk relates to financial assets and financial liabilities whose values will fluctuate as a result of changes in market prices other than from interest and foreign exchange fluctuations. This is due to factors specific to individual instruments, their issuers or factors affecting all instruments traded in the market. Accordingly, the Group monitors exposure limits both to any one counterparty and any one market.

The sensitivity analysis below illustrates how the fair value of future cash flows in respect of equities and properties, net of offsetting movements in insurance and investment contract liabilities, will fluctuate because of changes in market prices at the reporting date.

	Impact on profit after tax and equity for the year	
	2011	2010
	£ m	£ m
9.8% (2010: 3.9%) increase in equity prices	1	(3)
9.8% (2010: 3.9%) decrease in equity prices	(1)	3
2.9% (2010: 1.7%) increase in property prices	-	-
2.9% (2010: 1.7%) decrease in property prices	-	-

(ii) Interest rate risk

Interest rate risk is the risk that the value of future cash flows of a financial instrument will fluctuate because of changes in interest rates and the shape of the yield curve. Interest rate risk in respect of the Group's insurance and investment contracts arises when there is a mismatch in duration or yield between liabilities and the assets backing those liabilities.

The Group's interest rate risk policy requires that the maturity profile of interest-bearing financial assets is appropriately matched to the guaranteed elements of the financial liabilities.

A fall in market interest rates will result in a lower yield on the assets supporting guaranteed investment returns payable to policyholders. This investment return guarantee risk is managed by matching assets to liabilities as closely as possible.
An increase in market interest rates will result in a reduction in the value of assets subject to fixed rates of interest which may result in losses if, as a result of an increase in the level of surrenders, the corresponding fixed income securities have to be sold.

The effect of changes in interest rates in respect of financial assets which back insurance contract liabilities is given in note 41. The effect on the Group of changes in the value of investments held in respect of investment contract liabilities due to fluctuations in market interest rates is negligible as any changes will be offset by movements in the corresponding liability.

The sensitivity analysis below illustrates how the fair value of future cash flows in respect of interest-bearing financial assets, net of offsetting movements in insurance and investment contract liabilities, will fluctuate because of changes in market interest rates at the reporting date.

	Impact on profit after tax and equity for the year	
	2011	2010
	£ m	£ m
25 basis points (2010: 25 basis points) increase in yield curves	31	(8)
25 basis points (2010: 25 basis points) decrease in yield curves	(33)	5

(iii) Foreign exchange risk

Foreign exchange risk relates to the effects of movements in exchange markets including changes in exchange rates. The overall risk to the Group is minimal due to the following:

- The Group's principal transactions are carried out in pounds sterling;
- The Group's financial assets are primarily denominated in the same currencies as its insurance and investment contract liabilities; and
- Other than shareholder funds, all non-linked investments of the non-profit funds are in sterling or are currency matched. The effect on the Group of changes in the value of investments held in respect of investment contract liabilities due to fluctuations in foreign exchange rates is negligible as any changes will be offset by movements in the corresponding liability.

(2) Insurance risk

Insurance risk is the risk of reductions in earnings and/or value through financial or reputational loss due to fluctuations in the timing, frequency and severity of insured events and to fluctuations in the timing and amount of claim settlements. The principal risk the Group faces under insurance contracts is that the actual claims and benefit payments exceed the amounts expected at the time of determining the insurance liabilities.

The nature of the Group's business involves the accepting of insurance risks which primarily relate to mortality, morbidity, persistency and expenses. Each company within the Group which transacts new business underwrites policies to ensure an appropriate premium is charged for the risk or that the risk is declined.

The Group principally writes the following types of life insurance contracts:

- Life assurance – where the life of the policyholder is insured against death or permanent disability, usually for pre-determined amounts
- Annuity products – where typically the policyholder is entitled to payments which cease upon death
- Morbidity products – where the policyholder is insured against the risk of contracting a defined illness

For contracts where death is the insured risk, the most significant factors that could increase the overall level of claims are epidemics or widespread changes in lifestyle, such as eating, smoking and exercise habits, resulting in earlier or more claims than expected. The possibility of a pandemic, for example one arising from Swine Flu, is regarded as a potentially significant mortality risk.

For contracts where survival is the insured risk, the most significant factor is continued improvement in medical science and social conditions that would increase longevity.

For contracts with fixed and guaranteed benefits and fixed future premiums, there are no mitigating terms and conditions that significantly reduce the insurance risk accepted. For participating investment contracts, the participating nature of these contracts results in a significant portion of the insurance risk being shared with the policyholder.

Insurance risk is also affected by the policyholders' right to pay reduced or no future premiums, to terminate the contract completely or to exercise a guaranteed annuity option. As a result, the amount of insurance risk is also subject to policyholder behaviour. On the assumption that policyholders will make decisions that are in their best interests, overall insurance risk will generally be aggravated by policyholder behaviour. For example, it is likely that policyholders whose health has deteriorated significantly will be less inclined to terminate contracts insuring death benefits than those policyholders who remain in good health.

The Group has taken account of the expected impact of policyholder behaviour in setting the assumptions used to measure insurance and investment contract liabilities.

The principal methods available to the Group to control or mitigate longevity, mortality and morbidity risk are through the following processes:

- Underwriting (the process to ensure that new insurance proposals are properly assessed);
- Pricing-to-risk (new insurance proposals would usually be priced in accordance with the underwriting assessment);
- Claims management;
- Product design;
- Policy wording; and
- The use of reinsurance and other risk mitigation techniques.

Rates of mortality and morbidity are investigated annually based on the Group's recent experience and future mortality assumptions are set using the latest population data available. Each Company's reinsurance arrangements are reviewed at least annually.

Persistency risk is the risk associated with the ability to retain long-term business and the ability to renew short-term business. The Group aims to reduce its exposure to persistency risk through revising the commission structure on future product developments and undertaking various initiatives to promote customer loyalty. These initiatives are aimed both at the point of sale and through direct contact with existing policyholders, for example through annual statement information packs.

Further information on assumptions, changes in assumptions and sensitivities in respect of insurance and participating investment contracts is given in note 41.

(3) Credit risk

Credit risk is the risk of reductions in earnings and/or value, through financial or reputational loss, as a result of the failure of the party with whom the Group or Company has contracted to meet its obligations.

Investment counterparty default risk arises primarily from holding invested assets to meet liabilities, and reinsurer default credit risk primarily arises from exposure to reinsurers.

Credit risk in respect of unit-linked funds is borne by the policyholders and credit risk in respect of With Profits funds is largely borne by the policyholders. Consequently, the Group has no significant exposure to credit risk for those funds.

For non-linked funds investments, limits on the exposure to a single entity are specified and monitored. Bond exposures are managed through credit rating bands and maximum exposures to individual assets and sectors are set. Assets are restricted to securities in a specified list of countries, and limits applicable to property portfolios are set to prevent concentration of exposure to single tenants and single buildings.

Shareholder funds are managed in line with the Insurance Credit Risk Policy and the wider Lloyds Banking Group Credit Risk Policy and the principles are the same as those outlined above in respect of non-linked funds.

Reinsurance is primarily used to reduce insurance risk. However, it is also sought for other reasons such as improving profitability, reducing capital requirements and obtaining technical support. In addition, reinsurance is also used to offer Investment Fund Links which we are unable to provide through other means. The Group's reinsurance strategy is to reduce the volatility of profits through the use of reinsurance whilst managing the insurance and credit risk within the constraints of the risk appetite limits.

The Group has reinsurance on all significant lines of business where mortality or morbidity risk exceeds set retention limits. This does not, however, discharge the Group's liability as primary insurer. If a reinsurer fails to pay a claim for any reason, the Group remains liable for the payment to the policyholder. All new material reinsurance treaties are subject to Board approval and all reinsurance arrangements are reviewed annually to ensure that the reinsurance strategy is being achieved. This includes an assessment of the exposure to each reinsurer to ensure that it is within the defined limit.

Policies are treated as lapsed when payments from the policyholder have not been received for three consecutive months and the policyholder has not provided further information in respect of the non-payment of premiums.

Exposure to other trade debtors is assessed on a case by case basis, using a credit rating agency where appropriate.

The tables below analyse financial assets subject to credit risk using Standard & Poor's rating or equivalent.

Group – As at 31 December 2011

	Total £ m	AAA £ m	AA £ m	A £ m	BBB or lower £ m	Not rated £ m
Assets arising from reinsurance contracts held	4,720	-	529	4,105	9	77
Debt securities	37,580	22,214	2,330	7,215	5,126*	695
Deposits with credit institutions	-	-	-	-	-	-
Derivative financial instruments	1,390	-	-	1,390	-	-
Loans and receivables	19,077	1,920	8,437	7,642	124	954
Cash at bank	989	12	94	883	-	-
Total	63,756	24,146	11,390	21,235	5,259	1,726

*Of which £4,109m is BBB rated.

Amounts classified as "not rated" in the above tables are not rated by Standard and Poor's or an equivalent rating agency.

Included in the loans and receivables balance above is £4m (2010: £451m) in respect of assets that were past due but not impaired at the reporting date. There were no impaired assets at 31 December 2011 or 31 December 2010. No terms in respect of financial assets had been renegotiated at 31 December 2011 or 31 December 2010.

As at 31 December 2010

	Total £ m	AAA £ m	AA £ m	A £ m	BBB or lower £ m	Not rated £ m
Debt securities	20,644	13,278	1,426	3,405	2,411*	124
Deposits with credit institutions	1,287	1,287	-	-	-	-
Derivative financial instruments	314	-	1	313	-	-
Loans and receivables	2,124	102	20	901	68	1,033
Assets arising from reinsurance contracts held	2,328	-	-	-	-	2,328
Cash and cash equivalents	505	-	-	505	-	-
Total	27,202	14,667	1,447	5,124	2,479	3,485

*Of which £2,340m is BBB rated.

Amounts which were past due but not impaired are analysed as follows:

Group – As at 31 December 2011

	Total £ m	Less than 1 month £ m	1 – 3 months £ m	3 – 12 months £ m	More than 12 months £ m
Loans and receivables	4	2	-	1	1
Total	4	2	-	1	1

As at 31 December 2010

	Total £ m	Less than 1 month £ m	1 – 3 months £ m	3 – 12 months £ m	More than 12 months £ m
Loans and receivables	451	104	87	184	76
Total	451	104	87	184	76

Company – As at 31 December 2011

	Total £ m	AAA £ m	AA £ m	A £ m	BBB or lower £ m	Not rated £ m
Assets arising from reinsurance contracts held	33,017	-	404	4,002	-	28,611
Debt securities	8,942	5,932	342	1,566	1,069*	33
Derivative financial instruments	225	-	-	225	-	-
Loans and receivables	1,980	39	7	336	31	1,567
Cash and cash equivalents	48	-	-	48	-	-
Total	44,212	5,971	753	6,177	1,100	30,211

*Of which £1,046m is BBB rated.

Amounts classified as "not rated" within loans and receivables and amounts due from reinsurers in respect of non-participating investment contracts include £1,135m (2010: £1,242m) due from other Group companies which are not rated by Standard & Poor's or an equivalent rating agency.

Company - As at 31 December 2010

	Total £ m	AAA £ m	AA £ m	A £ m	BBB or lower £ m	Not rated £ m
Debt securities	10,128	7,222	602	1,287	992*	25
Deposits with credit institutions	10	10	-	-	-	-
Derivative financial instruments	177	-	1	176	-	-
Assets arising from reinsurance contracts held	25,937	-	-	-	-	25,937
Loans and receivables	4,077	50	4	838	29	3,156
Cash and cash equivalents	42	-	-	42	-	-
Total	40,371	7,282	607	2,343	1,021	29,118

*Of which £938m is BBB rated.

Amounts classified as "not rated" in the above tables are not rated by Standard and Poor's or an equivalent rating agency.

Included in the loans and receivables balance above is £1m (2010: £158m) is respect of assets that were past due but not impaired at the reporting date. There were no impaired assets at 31 December 2011 or 31 December 2010. No terms in respect of financial assets had been renegotiated at 31 December 2011 or 31 December 2010.

Amounts which were past due but not impaired are analysed as follows:

As at 31 December 2011

	Total £ m	Less than 1 month £ m	1 – 3 months £ m	3 – 12 months £ m	More than 12 months £ m
Loans and receivables	1	1	-	-	-
Total	1	1	-	-	-

As at 31 December 2010

	Total £ m	Less than 1 month £ m	1 – 3 months £ m	3 – 12 months £ m	More than 12 months £ m
Loans and receivables	158	46	52	55	5
Total	158	46	52	55	5

(i) Concentration risk

Credit concentration risk

Credit concentration risk relates to the inadequate diversification of credit risk. At 31 December 2011 and 31 December 2010, the Group did not have any significant concentration of credit risk with a single counterparty or group of counterparties where limits applied.

The Group maintains strict control on the use of derivatives by each fund as set out in the Insurance Derivatives Risk Policy ("DRP").

Credit risk is managed through the setting and regular review of counterparty credit and concentration limits on asset types which are considered more likely to lead to a concentration of credit risk. For other asset types, such as UK government securities or investments in funds falling under the UCITS Directive, no limits are prescribed as the risk of credit concentration is deemed to be immaterial. This policy supports the approach mandated by the FSA for regulatory reporting.

At 31 December 2011 and 31 December 2010, the Group did not have any significant concentration of credit risk with a single counterparty or group of counterparties where limits applied. With the exception of Government bonds and UCITS funds, the largest aggregated counterparty exposure is less than 0.1% (2010: less than 0.1% of the Group's total assets).

The Group maintains strict control limits on the derivative positions held by each fund as set out in the DRP.

Liquidity concentration risk

Liquidity concentration risk arises where the Group is unable to meet its obligations as they fall due or do so only at an excessive cost, due to over-concentration of investments in particular financial assets or classes of financial asset.

As most of the Group's invested assets are diversified across a range of marketable equity and debt securities in line with the investment options offered to policyholders it is highly unlikely that a material concentration of liquidity concentration could arise.

This is supplemented by active liquidity management in the Group, to ensure that even under stress conditions the Group has sufficient liquidity as required to meet its obligations. This is delegated by the Board to and monitored through the Shareholder and With-Profits Investment Management Committee ("SAWPIM"), Operational Banking Committee and Capital Working Group ("CWG").

(ii) Collateral management

The Group maintains strict control limits on net open derivative positions, namely the difference between purchase and sale contracts, by both amount and term. The amount subject to credit risk at any one time is limited to the current fair value of instruments that are favourable to the Group (that is, assets), which in relation to derivatives is only a fraction of the contract or notional values used to express the volume of instruments outstanding. For all derivative asset positions, the value of all collateral held is at least equal to the value of the asset held on the balance sheet.

Collateral in respect of OTC derivatives

The requirement for collateralisation, including the levels at which collateral is required and the types of asset that are deemed to be acceptable collateral, are set out in a Credit Support Annex ("CSA"). A CSA is a bilateral legal agreement which, once signed, forms part of the International Swaps and Derivatives Association ("ISDA") agreement between the Company and the counterparty.

A CSA must be completed for OTC derivatives as part of the contracts for such transactions. The CSA will require collateralisation where any net exposure to a counterparty exceeds the OTC counterparty limit, which must be established in accordance with the DRP. The aggregate uncollateralised exposure to any one counterparty must not exceed limits specified in the DRP. Where derivative counterparties are related, the aggregate net exposure is considered for the purposes of applying these limits.

The aggregate exposure, net of any collateralisation, to any one counterparty, across all life companies, funds and transactions, should not exceed £10m.

Acceptable collateral is defined in each instance and must take into account the quality and appropriateness of the proposed collateral as well as being acceptable to the entity receiving the collateral. Collateral may include the following:

- Sovereign government debt of developed economies
- Supranational debt denominated in eligible currencies
- Corporate bonds denominated in eligible currencies
- Equities denominated in eligible currencies

- Cash (this is received and invested in the SWIP Global Liquidity Fund)

Assets with the following carrying amounts have been pledged in accordance with the terms of the relevant CSAs entered into in respect of various OTC derivative contracts:

	2011		2010	
	£ m	£ m	£ m	£ m
	Group	*Company*	*Group*	*Company*
Financial assets:				
Investments at fair value through income	577	497	227	186
Total	577	497	227	186

The Company has the right to recall any collateral pledged provided that this is replaced with alternative acceptable assets. Collateral pledged continues to be recognised on the Company's balance sheet. No account is taken of collateral held. The policy of the Company is not to repledge assets. No collateral (2010: £nil) was sold during the year. At 31 December 2010, assets with a fair value of £151m (2010: £274m) were available to the Company to sell in the absence of default by the counterparty. None of these assets were past due or impaired at 31 December 2011 or 31 December 2010. In the event of default, assets received as collateral are sold.

Collateral held in respect of OTC derivatives at 31 December 2011 had a fair value of £775m (2010: £70m).

All collateral held relates to fully performing assets.

Collateral in respect of stocklending

The Group enters into stocklending transactions. The SAWPIM is responsible for setting the parameters of stocklending and therefore changes to these parameters. The accepted collateral can include cash, equities, certain bonds and money market instruments. On a daily basis, the fair value of collateral is compared to the fair value of stock on loan. The value of collateral must always exceed the value of stock on loan. Further information in respect of collateral relating to stocklending is given in note 46.

Stocklending is permitted in accordance with the Insurance Credit Risk Policy on stocklending. All stocklending takes place on an open/call basis, enabling the loan to be recalled at any time within the standard settlement terms of the market concerned.

The policy requires all lending to be undertaken via a partial indemnified programme (where the operator of the programme provides an indemnification against borrower and collateral default). The partial programme does not cover the re-investment of outright cash and therefore the policy specifies that the SAWPIM will set counterparty limits for the re-investment of such balances.

Additionally, the SAWPIM will set limits on the maximum amount of any security that may be lent and the markets in which lending can take place.

The policy requires acceptable collateral to be pledged to at least the value of securities lent and sets specific parameters over what qualifies as acceptable collateral.

There were no collateral defaults in respect of stocklending during the year ended 31 December 2011 (2010: none) which required a call to be made on collateral.

(4) Financial soundness risk

Financial soundness risk covers the risk of financial failure, reputational loss or loss of earnings and/or value arising from a lack of liquidity, funding or capital and/or the inappropriate recording, reporting or disclosure of financial, taxation and regulatory information.

(i) Financial and prudential regulatory reporting, tax and disclosure risks

The Group and Company are exposed to the risk that policies and procedures are not sufficient to maintain adequate books and records to support statutory (including the requirement to prepare consolidated financial statements), regulatory and tax reporting and to prevent and detect financial reporting fraud.

The Group has developed procedures to ensure that compliance with both current and potential future requirements are understood and that policies are aligned to its risk appetite. The Group maintains a system of internal controls, consistently applied, providing reasonable assurance that transactions are recorded and undertaken in accordance with delegated

authorities that permit the preparation and disclosure of financial statements (including consolidated financial statements), regulatory reporting and tax returns in accordance with IFRSs, statutory and regulatory requirements.

The Group undertakes a programme of work designed to support an annual assessment of the effectiveness of internal controls over financial reporting, to identify tax liabilities and to assess emerging legislation and regulation.

(ii) Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in raising funds to meet its financial commitments as they fall due, or can secure them only at an excessive cost. Liquidity risk may result from either the inability to sell financial assets quickly at their fair values; or from an insurance liability falling due for payment earlier than expected; or from the inability to generate cash inflows as anticipated.

Liquidity risk has been analysed as arising from payments to policyholders (including those where payment is at the discretion of the policyholder) and non policyholder related activity (such as investment purchases and the payment of shareholder expenses).

In order to quantify the liquidity risk exposure on all types of business other than annuity contracts, various stress tests are considered. Liquidity risk is measured by comparing the projected outflow in the stress scenario for twelve months of surrenders and three months of maturities against the sum of liquid resources available. In conducting this assessment, no account is taken of future policyholder inflows. The Company had coverage of at least 100% at 31 December 2011 (2010: at least 100%) in all stress scenarios considered. On a consolidated basis, coverage was at least 100% at 31 December 2011 (2010: at least 100%).

Liquidity risk in respect of each of the major product areas is primarily mitigated as follows:

Annuity contracts:

Assets are held which are specifically chosen to correspond to the expectation of timing of annuity payments. Gilts and corporate bonds are selected to reflect, as closely as possible, the expected annuity payments and are regularly rebalanced to ensure that this remains the case in future.

With-profits contracts

For with-profits business, a portfolio of assets is held in line with investment mandates which will reflect policyholder expectations as set out in the published PPFMs.

Liquidity is maintained within the portfolio via the holding of cash balances and a substantial number of highly liquid assets, principally gilts and bonds. Management also have the ability to sell less liquid assets at a reduced price if necessary, with any loss passed on to policyholder in line with policyholders' reasonable expectations. Losses are managed and mitigated by anticipating policyholder behaviour and sales of underlying assets within funds.

Non-participating contracts

For unit-linked products, portfolios are invested in accordance with unit fund mandates. Deferral clauses are included in policyholder contracts to give time, when necessary, to realise linked assets without being a forced seller. As at 31 December 2011, there are no funds under management subject to deferral.

For non-linked products other than annuity contracts, backing investments are mostly held in gilts with minimal liquidity risk. Investments are arranged to minimise the possibility of being a distressed seller whilst at the same time investing to meet policyholder obligations. This is achieved by anticipating policyholder behaviour and sales of underlying assets within funds.

Shareholder funds

For shareholder funds, liquidity risk is managed in line with the Insurance Liquidity Risk Policy and the wider Lloyds Banking Group Funding and Liquidity Risk Policy.

The following tables indicate the timing of the contractual cash flows arising from the Group and Company's financial liabilities, as required by IFRS 7. The table is based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Company is obliged to pay. The table includes both interest and principal cash flows.

Liquidity risk in respect of insurance and participating investment contract liabilities has been analysed based on the expected pattern of maturities as permitted by IFRS 4 rather than by contractual maturity. A maturity analysis of non-participating investment contracts based on expected contract maturities is also given as it is considered that this analysis provides additional useful information in respect of the liquidity risk relating to contracts written by the Group and Company.

Group – As at 31 December 2011

Liabilities	Carrying amount (discounted) £ m	Contractual cash flows (undiscounted) No stated maturity £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Non-participating investment contract liabilities	26,374	-	26,374	-	-	-	-
External interests in mutual investment funds	15,928	5,411	10,516	-	-	-	-
Derivative financial instruments	1,162	-	23	490	42	213	1,400
Subordinated debt	1,875	396	-	19	70	930	2,178
Borrowings	7	-	7	-	-	-	-
Other financial liabilities	2,235	83	2,102	-	-	50	-
Total	47,581	5,890	39,022	509	112	1,193	3,578

As at 31 December 2010

Liabilities	Carrying amount (discounted) £ m	Contractual cash flows (undiscounted) No stated maturity £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Non-participating investment contract liabilities	16,226	-	16,226	-	-	-	-
External interests in mutual investment funds	1,839	-	1,839	-	-	-	-
Derivative financial instruments	453	-	22	40	(3)	50	70
Subordinated debt	1,410	-	-		852	675	-
Borrowings	11	-	9	-	-	-	-
Other financial liabilities	3,131	-	3,097	-	-	-	-
Total	23,070	-	21,193	40	849	725	70

The contractual cash flow analysis set out above has been based on the earliest possible contractual date, regardless of the surrender penalties that might apply and has not been adjusted to take account of such penalties.

An analysis of the contractual cash flows in respect of insurance and investment contract liabilities by expected contract maturity, on a discounted basis, is shown below:

As at 31 December 2011

Maturity Analysis for insurance and investment contracts	Total £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Insurance and participating investment contracts	69,894	600	1,397	4,509	17,337	46,051
Non-participating investment contracts	26,374	167	269	1,035	4,788	20,115

As at 31 December 2010

Maturity Analysis for insurance and investment contract liabilities	Total £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Insurance and participating investment contracts	40,202	226	608	1,978	8,655	28,735
Non-participating investment contracts	16,226	45	79	197	1,481	14,424

Company – As at 31 December 2011

Liabilities	Carrying amount (discounted) £ m	Contractual cash flows (undiscounted) No stated maturity £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Borrowings	3	-	3	-	-	-	-
Non-participating investment contract liabilities	13,686	-	13,686	-	-	-	-
Derivative financial instruments	628	-	12	-	35	165	1,119
Subordinated debt	1,424	-	-	19	58	880	1,910
Other financial liabilities	1,089	-	1,089	-	-	-	-
Total	16,827	-	14,790	19	93	1,045	3,029

As at 31 December 2010

Liabilities	Carrying amount (discounted) £ m	Contractual cash flows (undiscounted) No stated maturity £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Non-participating investment contract liabilities	13,852	-	13,852	-	-	-	-
Derivative financial instruments	334	-	-	17	(11)	14	(78)
Subordinated debt	1,410	-	-	-	852	675	
Borrowings	4	-	4	-	-	-	-
Other financial liabilities	2,652	-	2,652	-	-	-	-
Total	18,252	-	16,508	17	841	689	(78)

The contractual cash flow analysis set out above has been based on the earliest possible contractual date, regardless of the surrender penalties that might apply and has not been adjusted to take account of such penalties.

An analysis of insurance and investment contract liabilities by expected contract maturity, on a discounted basis, is shown below:

As at 31 December 2011

Maturity Analysis for insurance and investment contract liabilities	Total £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Insurance and participating investment contracts	38,895	285	651	2,301	8,416	27,242
Non-participating investment contracts	13,686	51	86	208	1,553	11,788

As at 31 December 2010

Maturity Analysis for insurance and investment contract liabilities	Total £ m	Less than 1 month £ m	1-3 months £ m	3-12 months £ m	1-5 years £ m	More than 5 years £ m
Insurance and participating investment contracts	38,066	229	461	2,135	8,663	26,578
Non-participating investment contracts	13,852	45	79	197	1,482	12,049

(iii) Capital risk

Capital risk is defined as the risk that:

- the Group, or one of its separately regulated subsidiaries, has insufficient capital to meet its regulatory capital requirements;
- the Group has insufficient capital to provide a stable resource to absorb all losses up to a confidence level defined in the risk appetite;
- the Group loses reputational status by having capital that is regarded as inappropriate, either in quantity, type or distribution; and/or
- the capital structure is inefficient.

The business of several of the companies within the Group is regulated by the FSA. The FSA specifies the minimum amount of capital that must be held by each of the regulated companies within the Group in addition to their insurance liabilities.

Within the Insurance Division, capital risk is actively monitored by the CWG.

Under the FSA rules, each insurance company within the Group must hold assets in excess of the higher of:

(i) the Pillar 1 amount, which is calculated by applying fixed percentages of mathematical reserves and capital at risk; and

(ii) the Pillar 2 amount, which is derived from an economic capital assessment undertaken by each regulated company, which is reviewed by the FSA.

The minimum required capital must be maintained at all times throughout the year. These capital requirements and the capital available to meet them are regularly estimated in order to ensure that capital maintenance requirements are being met.

The Group's objectives when managing capital are:

- to comply with the insurance capital requirements set out by the FSA in the UK;
- to have sufficient further capital to safeguard the Group's ability to continue as a going concern so that it can continue to provide returns for the shareholder and benefits for other stakeholders;
- when capital is needed, to require an adequate return to the shareholder by pricing insurance and investment contracts according to the level of risk associated with the business written; and
- to meet the requirements of the Schemes of Transfer.

The Company manages the capital structure and makes adjustments to reflect changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to the shareholder, return capital to the shareholder, issue new shares or sell assets.

The Company's capital comprises all components of equity, movements in which are set out in the statement of changes in equity and includes subordinated debt (note 35).

The table below sets out the regulatory capital and the required capital held at 31 December in each year on a Pillar 1 basis. The current year information is, in general, an estimate that will be updated once the FSA returns for the year are finalised.

	2011 £ m	2010 £ m
Regulatory capital held	7,958	5,689
Regulatory capital required	4,277	3,022

All minimum regulatory requirements were met during the year.

(d) Operational risk

Operational risk covers the risk of reductions in earnings and/or value, through financial or reputational loss, from inadequate or failed internal processes and systems, operational inefficiencies, or from people related or external events. By its very nature, operational risks can arise from a wide range of the Groups activities that involve people, processes and systems

Customer treatment and processes risk

The risk of reductions in earnings and/or value, through financial or reputational loss, from inappropriate or poor customer treatment. Associated risks include poor product design and development, customer advice, customer service and customer complaint handling. Customer process risk includes customer transactions and processing errors due to incorrect capturing of customer information and/or systems failure.

Customer treatment and how LBG as a whole manages its customer relationships affects all aspects of the Group's operations and is closely aligned with achievement of LBG's strategic aim – to create deep long lasting relationships with its customers. Currently there is a high level of scrutiny regarding the treatment of customers by financial institutions from the press, politicians and regulatory bodies.

People risk

The risk of reductions in earnings and/or value through financial or reputational loss, from inappropriate resource management, employee relations, legal action in relation to people, or health and safety issues.

The Group continues to face risks relating to its ability to attract, retain and develop high calibre talent as a result of challenges arising from ongoing regulatory and public interest in remuneration practices and delivery of LBG's integration requirements.

Financial crime and security risk

Financial crime risk covers the risk of reduction in earnings and/or value, through financial or reputational loss, associated with financial crime and failure to comply with related legal and regulatory obligations, these losses may include censure, fines or the cost of litigation. Security risk relates to potential losses as a result of the theft of, or damage to the Group's assets, the loss, corruption, misuse or theft of the Group's information assets or threats or actual harm to the Group's people. This also includes risks relating to terrorist acts, other acts of war, geographical, pandemic or other such events.

Organisational infrastructure and change risk

Organisational infrastructure risk covers the risk of reductions in earnings and/or value, through financial or reputational loss, resulting from poor internally facing business processes at a Group, divisional or company level. Organisational infrastructure in this context embraces the structures, systems and processes that provide direction, control and accountability for the enterprise. Change risk comprises the risk of potential loses from change initiatives failing to deliver to requirements, budget or timescale, failing to implement change effectively or failing to realise desired benefits.

Although now over two years into the successful implementation of the programme, there continue to be delivery of benefits as the programme moves into its final phase of execution.

Supplier management risk

The risk of reductions in earnings and/or value through financial or reputational loss from services with outsourced partners or third party suppliers.

IT Systems risk

The risk of reductions in earnings and/or value through financial or reputational loss resulting from the development, delivery and maintenance of effective IT solutions.

(e) Legal and regulatory risks

Legal and regulatory risk is the risk of reductions in earnings and/or value, through financial or reputational loss, from failing to comply with the laws, regulations or codes applicable.

A provision is held in respect of German litigation. This is discussed further in note 32.

The Group also faces a number of legal and regulatory risks, reflecting the volume and pace of change within the UK. This impacts the Group both operationally, in terms of costs of compliance and uncertainty about regulatory expectations, and strategically, through pressure on key earnings streams. The latter could potentially result in major changes to business and pricing models, particularly in the UK retail market. Business planning processes continue to reflect change to the regulatory environment.

Regulators are interested in protecting the rights of the policyholders and ensuring that the Group is satisfactorily managing affairs for the benefit of the policyholders. Regulators are also keen to ensure that the Group maintains appropriate solvency levels to meet unforeseen liabilities arising from reasonably foreseeable economic shocks or natural disasters. As such, the Group is subject to regulatory requirements which prescribe and impose certain restrictive provisions.

43. Related party transactions

(a) Ultimate parent and shareholding

The Group's immediate parent undertaking is Scottish Widows Financial Services Holdings, a company registered in the United Kingdom. Scottish Widows Financial Services Holdings has taken advantage of the provisions of the Companies Act 2006 and has not produced consolidated financial statements. .

The Company's ultimate parent company and ultimate controlling party is Lloyds Banking Group plc, which is also the parent undertaking of the largest group of undertakings for which group accounts are drawn up and of which the Company is a member. Lloyds TSB Bank plc is the parent undertaking of the smallest such group of undertakings. Copies of the Lloyds Banking Group plc financial statements in which the Company is consolidated can be obtained from the Group Secretary's Department, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN.

(b) **Transactions and balances with related parties**

Transactions between the Group and other companies in the Lloyds Banking Group

In accordance with IAS 24 "Related Party Disclosures", transactions and balances between Group companies have been eliminated on consolidation and have not been reported as part of the consolidated financial statements.

The Group has entered into the following transactions with other related parties during the year and holds the following balances with other related parties at the end of the year:

	Transactions in the Year		Outstanding Balance at 31 December	
	2011 £ m	2010 £ m	2011 £ m	2010 £ m
Relationship				
Ultimate parent undertaking:				
Shares in ultimate parent undertaking – book cost	-	-	113	113
Shares in ultimate parent undertaking – market value	-	-	16	16
Customer remediation income and amounts receivable	18	21	2	1
Expense recharges and amounts payable	(328)	(251)	(50)	(56)
Investments and amounts receivable	(8)	-	178	-
Other related parties:				
Bank account balances	-	-	341	519
Bank charges	(15)	-	-	-
Intercompany debtor balances	-	-	200	890
Investment assets	-	-	2,038	8,038
Intercompany creditor balances	-	-	(18)	(24)
Dividend income and amounts receivable	14	14	-	2
Annual management charges and amounts receivable	32	35	2	2
Interest income	30	57	3	24
Interest expense	95	-	-	-
Expense recharges and amounts payable	82	147	(81)	25
Reinsurance commission	-	92	-	92
Reinsurance expenses	-	35	-	35
Reinsurance claims	-	22	-	22
Reinsurance premiums	20	(132)	26	(132)
Rebates on annual management charges	(29)	(29)	(1)	(1)
Investment management fees	(90)	(58)	(16)	(6)
Commission	(22)	(11)	(2)	(4)
Subordinated debt	-	-	(1,371)	(800)
Subordinated debt interest paid	(1)	(24)	(12)	-

Transactions between the Company and other companies in the Lloyds Banking Group

The Company has entered into the following transactions with other related parties during the year and holds the following balances with other related parties at the end of the year:

	Transactions in the Year		Outstanding Balance at 31 December	
	2011 £ m	2010 £ m	2011 £ m	2010 £ m
Relationship				
Subsidiary undertaking:				
Investment assets	-	-	3,197	802
Intercompany debtor balances	-	-	50	45
Dividend income and amounts receivable	36	4	-	1
Contingent loan and interest receivable	8	7	744	630
Reinsurance claims and amounts payable	2,776	2,989	(11)	(13)
Investment management fee rebates	7	7	-	-
Loan notes and interest receivable	4	4	38	38
Customer remediation income and amounts receivable	-	-	69	66
Annual management charges received	28	42	-	-
Reinsurance commission	373	195	80	-
Reinsurance premiums	(3,383)	(3,151)	(45)	-
Reinsurance claims	30	22	6	
Reinsurance expenses	-	-	-	31
Expense recharges and amounts payable	(202)	(228)	(53)	(11)
Annual management charges paid	(2)	(2)	-	-
Renewal commission and amounts receivable	16	12	2	1
Interest income	19	-	-	-
Other related parties:				
Bank account balances	-	-	132	140
Investment assets	-	-	1,208	4,605
Intercompany debtor balances	-	-	158	890
Intercompany creditor balances	-	-	(21)	(13)
Interest income	28	41	3	24
Dividend income and amounts receivable	3	-	-	-
Reinsurance commission	-	92	-	92
Reinsurance expenses	-	-	-	45
Reinsurance premiums	-	(132)	-	(132)
Reinsurance claims	-	22	-	22
Investment management fees	(16)	(16)	(1)	(1)
Commission	(5)	(4)	(25)	(11)
Subordinated debt	-	-	(800)	(800)
Subordinated debt interest paid	(23)	(24)	-	-
Other interest paid	(24)	-	(12)	-

The above balances are unsecured in nature and are expected to be settled in cash.

Transactions between the Group and key management

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company which, for the Company, are the Executive Directors.

Transactions between the key management personnel of the Group and parties related to them as defined by IAS 24 are as follows:

Key management compensation:

	Group		*Company*	
	2011 £ m	2010 £ m	2011 £ m	2010 £ m
Salaries and other short-term benefits	2.7	1.9	1.0	1.5
Post-employment benefits	0.1	0.1	-	0.1
Share-based payments	1.2	0.4	0.7	0.3
Total	4.0	2.4	1.7	1.9

Certain members of key management in the Group, including the highest paid director, provide services to other companies within the Lloyds Banking Group. In such cases, for the purposes of this note, figures have been included based on an apportionment to the Group of the total compensation earned.

Of the amount disclosed above, £1.2m Group and £0.4m Company is in respect of Directors of SW (2010: Group £1.1m and Company £0.6m). No retirement benefits are accruing for Directors (2010: two) under defined benefit pension schemes. Two Directors (2010: one) are paying into a defined contribution scheme.

During the year £nil (2010: £nil) was paid to Directors of the Group as compensation for loss of office.

Detail regarding the highest paid Director is as follows:

	Group		Company	
	2011 £m	2010 £m	2011 £m	2010 £m
Apportioned aggregate emoluments	0.3	0.2	0.1	0.1
Defined benefits pension scheme accrued benefit at 31 December (all amounts less than £1m)	-	-	-	-

The highest paid Director exercised share options during the year and was granted shares in respect of qualifying service during the year. This was also the case in the prior year.

Other transactions between key management and the companies in the Lloyds Banking Group:

Deposits

	2011 £000	2010 £000
Outstanding at 1 January	-	5
Placed during the year	-	-
Interest earned during the year	-	-
Withdrawn during the year	-	(5)
Outstanding at 31 December	-	-

Other

	2011 £000	2010 £000
Value of investments managed by entities within the Lloyds Banking Group	2,991	137
Insurance premiums paid	-	-
Insurance claims received	274	-

Other transactions

HM Treasury

In January 2009, HM Treasury became a related party of the Company following its subscription for ordinary shares in LBG, the Company's ultimate parent company, issued under a placing and open offer. As at 31 December 2011, HM Treasury held a 40.2 percent (2010: 40.6 percent) interest in LBG's ordinary share capital and, consequently, HM Treasury remained a related party of the Company throughout 2011.

There were no material transactions between the Group or Company and HM Treasury during the year (2010: none) that were not made in the ordinary course of business or that are unusual in their nature or conditions. In addition, the Group and Company have entered into transactions with HM Treasury on an arm's length basis including, but not exclusively in relation to, the payment of corporation tax and value added tax.

44. Share-based payments

During the year ended 31 December 2011 the Lloyds Banking Group operated the following share based payment schemes, all of which are equity settled.

Deferred bonus plans

Bonuses in respect of the performance in 2011 of employees within certain of the Group's bonus plans have been recognised in these financial statements in full. The amounts to be settled in shares are included within the total charge to the income statement detailed above.

Lloyds Banking Group executive share option schemes

The executive share option schemes were long term incentive schemes available to certain senior executives of the Group, with grants usually made annually. Options were granted within limits set by the rules of the schemes relating to the number of shares under option and the price payable on the exercise of options. The last grant of executive options was made in August 2005. These options were granted without a performance multiplier and the maximum limit for the grant of options in normal circumstances was three times annual salary. Between April 2001 and August 2004, the aggregate value of the award based upon the market price at the date of grant could not exceed four times the executive's annual remuneration and, normally, the limit for the grant of options to an executive in any one year would be equal to 1.5 times annual salary with a maximum performance multiplier of 3.5. Prior to 18 April 2001, the normal limit was equal to one year's remuneration and no performance multiplier was applied.

Performance conditions for executive options

For options granted up to March 2001
The performance condition was that growth in earnings per share must be equal to the aggregate percentage change in the Retail Prices Index plus three percentage points for each complete year of the relevant period together with a further condition that Lloyds Banking Group plc's ranking based on total shareholder return (calculated by reference to both dividends and growth in share price) over the relevant period should be in the top fifty companies of the FTSE 100.
The relevant period for the performance conditions began at the end of the financial year preceding the date of grant and continued until the end of the third subsequent year following commencement or, if not met, the end of such later year in which the conditions were met. Once the conditions were satisfied the options remained exercisable without further conditions. If they were not satisfied by the tenth anniversary of the grant the options would lapse.

For options granted from August 2001 to August 2004
The performance condition was linked to the performance of Lloyds Banking Group plc's total shareholder return (calculated by reference to both dividends and growth in share price) against a comparator group of 17 companies including Lloyds Banking Group plc. The performance condition was measured over a three year period which commenced at the end of the financial year preceding the grant of the option and continued until the end of the third subsequent year. If the performance condition was not then met, it was measured at the end of the fourth financial year. If the condition was not then met, the options would lapse. To meet the performance conditions, the Group's ranking against the comparator group was required to be at least ninth. The full grant of options only became exercisable if the Group was ranked first. A performance multiplier (of between nil and 100 per cent) was applied below this level to calculate the number of shares in respect of which options granted to Executive Directors would become exercisable, and were calculated on a sliding scale. If Lloyds Banking Group plc was ranked below median the options would not be exercisable. Options granted to senior executives other than Executive Directors were not so highly leveraged and, as a result, different performance multipliers were applied to their options. For the majority of executives, options were granted with the performance condition but with no performance multiplier. Options granted in 2004 became exercisable as the performance condition was met on the re-test. The performance condition vested at 14 per cent for Executive Directors, 24 per cent for Managing Directors, and 100 per cent for all other executives.

For options granted in 2005
The same conditions applied as for grants made up to August 2004, except that:

- the performance condition was linked to the performance of Lloyds Banking Group plc's total shareholder return (calculated by reference to both dividends and growth in share price) against a comparator group of 15 companies including Lloyds Banking Group plc;
- if the performance condition was not met at the end of the third subsequent year, the options would lapse; and
- the full grant of options became exercisable only if the Group was ranked in the top four places of the comparator group. A sliding scale applied between fourth and eighth positions. If Lloyds Banking Group was ranked below the median (ninth or below) the options would lapse.

Options granted in 2005 became exercisable as the performance condition was met when tested. The performance condition vested at 82.5 per cent for all options granted.

Save-As-You-Earn-Schemes

Eligible employees may enter into contracts through the Save As You Earn schemes to save up to £250 per month and, at the expiry of a fixed term of three, five or seven years, have the option to use these savings within six months of the expiry of the fixed term to acquire shares in the Group at a discounted price of no less than 80 per cent of the market price at the start of the invitation.

Other Share Option Plans - Lloyds Banking Group Executive Share Plan 2003

The plan was adopted in December 2003 and under the plan share options may be granted to senior employees. Options under this plan have been granted specifically to facilitate recruitment and as such were not subject to any performance conditions. The plan's usage has now been extended to not only compensate new recruits for any lost share awards but also to make grants to key individuals for retention purposes with, in some instances, the grant being made subject to individual performance conditions.

Other Share Plans

i) Lloyds Banking Group Long-Term Incentive Plan

The Long Term Incentive Plan (LTIP) introduced in 2006 is aimed at delivering shareholder value by linking the receipt of shares to an improvement in the performance of the Group over a three year period. Awards are made within limits set by the rules of the plan, with the limits determining the maximum number of shares that can be awarded equating to three times annual salary. In exceptional circumstances this may increase to four times annual salary.

The performance conditions for awards made in March, April and August 2008 are as follows:
(i) For 50 per cent of the award (the EPS Award) – the percentage increase in earnings per share of the Group (on a compound annualised basis) over the relevant period needed to be at least an average of 6 percentage points per annum greater than the percentage increase (if any) in the Retail Prices Index over the same period. If it was less than 3 per cent per annum the EPS Award would lapse. If the increase was more than 3 per cent but less than 6 per cent per annum then the proportion of shares released would be on a straight line basis between 17.5 per cent and 100 per cent. The relevant period commenced on 1 January 2008 and ended on 31 December 2010.
(ii) For the other 50 per cent of the award (the TSR Award) – it was necessary for the Group's total shareholder return (calculated by reference to both dividends and growth in share price) to exceed the median of a comparator group (13 companies) over the relevant period by an average of 7.5 per cent per annum for the TSR Award to vest in full. 17.5 per cent of the TSR Award would vest where the Group's total shareholder return was equal to median and vesting would occur on a straight line basis in between these points. Where the Group's total shareholder return was below the median of the comparator group, the TSR Award would lapse. The relevant period commenced on 6 March 2008 and ended on 5 March 2011.

In 2008, awards were made of 375 per cent of base salary to the Group Chief Executive and two of the Executive Directors for retention purposes, and in light of data reviewed by the Remuneration Committee which showed total remuneration to be behind median both for the FTSE 20, and the other major UK banks.

As a consequence of the acquisition of HBOS and the general market turmoil, in March 2009 the Remuneration Committee decided that the performance test for the 2008 awards should be based on the performance of the Group up to 17 September 2008, the date prior to the announcement of the HBOS acquisition. The performance test was on a fair value basis, on the estimated probability, as at that date, of achieving the performance conditions. As a consequence, for all participants, other than those who were Executive Directors at the time the award was granted and a small number of other senior executives, the share awards vested at 29 per cent in March 2011.

The performance conditions for awards made in April, May and September 2009 are as follows:
(i) Earnings per share (EPS): relevant to 50 per cent of the award. Performance will be measured based on EPS growth over a three year period from the baseline EPS of 2008.
If the growth in EPS reaches 26 per cent, 25 per cent of this element of the award, being the threshold, will vest. If growth in EPS reaches 36 per cent, 100 per cent of this element will vest.
(ii) Economic Profit (EP): relevant to 50 per cent of the award. Performance will be measured based on the extent to which cumulative EP targets are achieved over the three year period.

If the absolute improvement in adjusted EP reaches 100 per cent, 25 per cent of this element of the award, being the threshold, will vest. If the absolute improvement in adjusted EP reaches 202 per cent, 100 per cent of this element will vest.
The EPS and EP performance measures applying to this 2009 LTIP award were set on the basis that the Group would enter into the Government Asset Protection Scheme. As the Group is not participating in the Government Asset Protection Scheme, in June 2010 the Remuneration Committee approved restated performance measures on a basis consistent with the EPS and EP measures used for the 2010 LTIP awards.

An additional discretionary award was made in April, May and September 2009. The performance conditions for those awards are as follows:
(i) Synergy Savings: The release of 50 per cent of the shares will be dependent on the achievement of target run□rate synergy savings in 2009 and 2010 as well as the achievement of sustainable synergy savings of at least £1.5 billion by the end of 2011. The award will be broken down into three equally weighted annual tranches. Performance will be assessed at the end of each year against annual performance targets based on a trajectory to meet the 2011 target. The extent to which targets have been achieved will determine the proportion of shares to be banked each year. Any release of shares will be subject to the Remuneration Committee judging the overall success of the delivery of the integration programme.

(ii) Integration Balanced Scorecard: The release of the remaining 50 per cent of the shares will be dependent on the outcome of a Balanced Scorecard of non financial measures of the success of the integration in each of 2009, 2010 and 2011. The Balanced Scorecard element will be broken down into three equally weighted tranches. The tranches will be crystallised and banked for each year of the performance cycle subject to separate annual performance targets across the four measurement categories of Building the Business, Customer, Risk and People and Organisation Development.

The performance conditions for awards made in March and August 2010 are as follows:
(i) EPS: relevant to 50 per cent of the award. Performance will be measured based on EPS growth over a three year period from the baseline EPS of 2009.
If the absolute improvement in adjusted EPS reaches 158 per cent, 25 per cent of this element of the award, being the threshold, will vest. If absolute improvement in adjusted EPS reaches 180 per cent, 100 per cent of this element will vest. Vesting between threshold and maximum will be on a straight line basis.
(ii) EP: relevant to 50 per cent of the award. Performance will be measured based on the compound annual growth rate of adjusted EP over the three financial years starting on 1 January 2010 relative to an adjusted 2009 EP base. If the compounded annual growth rate of adjusted EP reaches 57 per cent per annum, 25 per cent of this element of the award, being the threshold, will vest. If the compounded annual growth rate of adjusted EP reaches 77 per cent per annum, 100 per cent of this element will vest. Vesting between threshold and maximum will be on a straight line basis.

For awards made to Executive Directors, a third performance condition was set, relating to Absolute Share Price, relevant to 28 per cent of the award. Performance will be measured based on the Absolute Share Price on 26 March 2013, being the third anniversary of the award date. If the share price at the end of the performance period is 75 pence or less, none of this element of the award will vest. If the share price is 114 pence or higher, 100 per cent of this element will vest. Vesting between threshold and maximum will be on a straight line basis, provided that shares comprised in the Absolute Share Price element may only be released if both the EPS and EP performance measures have been satisfied at the threshold level or above. The EPS and EP performance conditions will each relate to 36 per cent of the total award.
The performance conditions for awards made in March and September 2011 are as follows:
(i) EPS: relevant to 50 per cent of the award. The performance target is based on 2013 adjusted EPS outcome. If the adjusted EPS reaches 6.4p, 25 per cent of this element of the award, being the threshold, will vest. If adjusted EPS reaches 7.4p, 100 per cent of this element will vest. Vesting between threshold and maximum will be on a straight line basis.
(ii) EP: relevant to 50 per cent of the award. The performance target is based on 2013 adjusted EP outcome.
If the adjusted EP reaches £567 million, 25 per cent of this element of the award, being the threshold, will vest. If the adjusted EP reaches £1,234 million, 100 per cent of this element will vest. Vesting between threshold and maximum will be on a straight line basis.

For awards made to Executive Directors, a third performance condition was set, relating to Absolute Total Shareholder Return, relevant to one third of the award. Performance will be measured based on the annualised Absolute Total Shareholder Return over the three year performance period. If the annualised Absolute Total Shareholder Return at the end of the performance period is less than 8 per cent, none of this element of the award will vest. If the Absolute Total Shareholder Return is 8 per cent, 25 per cent of this element of the award, being the threshold, will vest. If the Absolute Total Shareholder Return is 14 per cent or higher, 100 per cent of this element will vest. Vesting between threshold and maximum will be on a straight line basis. The EPS and EP performance conditions will each relate to 33.3 per cent of the total award.

Share Incentive Plan

Free shares

An award of shares may be made annually to employees based on a percentage of each employee's salary in the preceding year up to a maximum of £3,000. The percentage is normally announced concurrently with the Group's annual results and the price of the shares awarded is announced at the time of award. The shares awarded are held in trust for a mandatory period of three years on the employee's behalf, during which period the employee is entitled to any dividends paid on such shares. The award is subject to a non market based condition: if an employee leaves the Group within this three year period for other than a 'good' reason, all of the shares awarded will be forfeited. The last award of free shares was made in 2008.

Matching shares

The Group undertakes to match shares purchased by employees up to the value of £30 per month; these matching shares are held in trust for a mandatory period of three years on the employee's behalf, during which period the employee is entitled to any dividends paid on such shares. The award is subject to a non market based condition: if an employee leaves within this three year period for other than a 'good' reason, 100 per cent of the matching shares are forfeited. Similarly if the employees sell their purchased shares within three years, their matching shares are forfeited.

Full details of the ranges of exercise prices, weighted average exercise prices, weighted average remaining contractual life information and number of options outstanding for the above schemes overall can be found in the 2011 annual report and accounts of the Company's ultimate parent company. Copies of the ultimate parent company's 2011 annual report and accounts may be obtained from the Group Secretary's Department, Lloyds Banking Group plc, 25 Gresham Street, London, EC2V 7HN.

45. Operating leases

The total future minimum rental payments receivable under non-cancellable leases are as follows:

	2011 £ m	2010 £ m
Within 1 year	241	161
Between two and five years	874	574
Beyond five years	1,575	992
Total	2,690	1,727

The total of contingent rents recognised as income during the year was £nil (2010: £nil). The total of contingent rents recognised as operating expenses during the year was £nil (2010: £nil). Generally the Group's operating leases are for terms of 15 years or more.

46. Stocklending

The aggregate value of securities on loan by the Group is £7,364m (2010: £3,509m) and by the Company is £3,083m (2010: £1,967m). Securities on loan are included in investments at fair value through income and no account is taken of collateral held. The aggregate value of collateral held is £7,686m (2010: £4,502m) for Group and £3,231m (2010: £2,067m) for Company. Further detail in respect of collateral is provided in note 41.

47. Capital commitments

The Group has given an undertaking to provide up to EUR 170m (£148m) (2010: EUR 170m (£146m)) of capital to the European Balanced Property Fund. At 31 December 2011, EUR 141m (£123m) had been drawn down (2010: EUR 157m (£135m)). The remainder of the funds committed can be drawn down as required by the Fund.

The Group has contracted for, but not paid for, £nil (2010: nil) development expenses for investment property. Of this amount, the Company has contracted for, but not paid for, £nil (2010: £nil).

The Company invests in a number of private equity entities to which capital of EUR 370m (£309m) and £155m were committed at 31 December 2011 (2010: EUR 370m (£317m) and £129m). The total amount drawn down at 31 December 2011 was EUR 257m (£214m) and £105m (2010: EUR 247m (£211m) and £98m). The remainder of the funds committed can be drawn down as required by the Funds.

At a consolidated level, the Group invests in private equity entities to which capital of EUR 527m (£441m) and £155m were committed at 31 December 2011 (2010: EUR 527m (£452m) and £129m). The total amount drawn down at 31 December 2011 was EUR 366m (£306m) and £105m (2010: EUR 351m (£301m) and £98m). The remainder of the funds committed can be drawn down as required by the Funds.

48. Standards and interpretations effective in 2011

The Group has adopted the following new standards and amendments to standards which became effective for financial years beginning on or after 1 January 2011. None of these standards or amendments has had a material impact on these financial statements.

(i) "Improvements to IFRSs" (issued May 2010). Sets out minor amendments to IFRSs as part of the annual improvements process.
(ii) IAS 24 Related Party Disclosures (Revised). Simplifies the definition of a related party and provides a partial exemption from the requirement to disclose transactions and outstanding balances with the government and government-related entities. The Group has taken advantage of this exemption, which requires disclosure of significant transactions only with the government and government-related entities. Details of related party transactions are set out in note 43.

Details of those IFRSs pronouncements which will be relevant to the Group but which were not effective at 31 December 2011 and which have not been applied in preparing these financial statements are given in note 49.

49. Future accounting developments

The following pronouncements will be relevant to the Group but were not effective at 31 December 2011 and have not been applied in preparing these financial statements. The full impact of these accounting changes is being assessed by the Group.

Pronouncement	Nature of change	IASB effective date
IFRS 9 "Financial Instruments"	Replace those parts of IAS 39: 'Financial Instruments: Recognition and Measurement' relating to the classification, measurement and derecognition of financial assets and liabilities. It requires financial assets to be classified into two measurement categories, fair value and amortised cost, on the basis of the objectives of the entity's business model for managing its financial assets and the contractual cash flow characteristics of the instrument. The available-for-sale financial asset and held-to-maturity investment categories in the existing IAS 39 will be eliminated. The requirements for financial liabilities and derecognition are broadly unchanged from IAS 39.	Annual periods beginning on or after 1 January 2015.
IFRS 10 "Consolidated Financial Statements"	Supersedes IAS 27 "Consolidated and Separate Financial Statements" and SIC-12 Consolidation "Special Purpose Entities" and establishes principles for the preparation of consolidated financial statements when an entity controls one or more entities.	Annual periods beginning on or after 1 January 2013
IFRS 13 "Fair Value Measurement"	The standard defines fair value, sets out a framework for measuring fair value and requires disclosures about fair value measurements and applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements.	Annual periods beginning on or after 1 January 2013
IAS 19 "Employee Benefits"	Prescribes the accounting and disclosure by employers for employee benefits. Actuarial gains and losses (remeasurements) in respect of defined benefit pension schemes are no longer deferred using the corridor approach and are recognised immediately in other comprehensive income.	Annual periods beginning on or after 1 January 2013

[1] At the date of this report, these pronouncements are awaiting EU endorsement.

50. Post balance sheet events

The proposed further reductions in the rate of corporation tax to 22 per cent by 1 April 2014 are expected to be enacted separately each year. The effect of these further changes upon the Company's deferred tax balances cannot be reliably quantified at this stage.

The Finance Act 2012 is expected to contain changes which will impact the taxation of life insurance companies. The effect of these changes to the Group's deferred tax balances cannot be reliably quantified at this stage. However, we consider it likely that a large proportion of the unrecognised deferred tax asset in Clerical Medical Investment Group Limited in respect of unutilised expenses of £63m will be reinstated as a result of the changes in legislation.