HALIFAX INDEPENDENT FINANCIAL ADVISERS LIMITED

DIRECTORS' REPORT

AND

FINANCIAL STATEMENTS

31 DECEMBER 2011

Member of Lloyds Banking Group plc

CONTENTS

COMPANY INFORMATION

Board of Directors

R W Fletcher
N L N Machray

Company Secretary

K J Mckay

Auditors

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
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Bristol
BS1 5QD

Registered Office

Trinity Road
Halifax
West Yorkshire
HX1 2RG

Company Registration Number

2367078

DIRECTORS' REPORT

Principal activity and review of the business

The Directors present the audited financial statements of Halifax Independent Financial Advisers Limited (the "Company"), a limited liability company domiciled and incorporated in the United Kingdom The principal activity of the Company is to generate initial commission from the sale of annuity products under the trading name Bank of Scotland Annuity Service (BOSAS) and to act as an Independent Financial Adviser

BOSAS generates new business mainly through the Bank of Scotland Investment Service and St James' Place, fellow group entities which focus on high net worth individuals

In September 2000, the Company closed to new business as an Independent Financial Adviser The Company continues to generate renewal commission as a result of its existing book of business

The Company is a wholly owned subsidiary of Halifax Financial Services (Holdings) Limited The Company's ultimate parent company and ultimate controlling party is Lloyds Banking Group plc

Results and dividend

The result of the Company for the year ended 31 December 2011 is a profit after taxation of £4,575k (2010 £4,013k), and this has been transferred to reserves The Directors consider this result to be satisfactory in light of the activities of the Company The Directors do not recommend the payment of a final dividend (2010 £nil)

Key performance indicators

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 13

The Company's turnover for the year ended 31 December 2011 is £7,989k (2010 £7,852k) Existing business continues to generate gross renewal commission, this amounted to £1,735k for the year (2010 £2,065k) BOSAS generated initial commission of £6,254k from the sale of annuity products (2010 £5,787k)

The Directors are of the opinion that the information presented in the Retail Mediation Activities Return ("RMAR"), 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

The Company also forms part of the Insurance Division of Lloyds Banking Group plc The development, performance and position of this Division are discussed in Lloyds Banking Group plc's financial statements, which do not form part of this report

Future outlook

The Directors consider that the Company's activities will continue unchanged in the foreseeable future

Principal risks and uncertainties

The management of the business and the execution of the Company's strategy are subject to a number of risks The financial risk management objectives and policies of the Company and the exposure to credit, market and financial soundness risk are set out in note 13

Directors

The names of the current Directors are listed on page 3 There have been no changes in directorships since 31 December 2010

Particulars of the Directors' emoluments are set out in note 14

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

DIRECTORS' REPORT (CONTINUED)

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

Policy and practice on payment of creditors

The Company follows "The Better Payment Practice 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 Publication Orders Live (0845 015 0010), quoting reference URN 04/606

The Company'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 Company 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 Lloyds Banking Group plc The number of days shown in this report, to comply with the provisions of the Companies Act 2006, is 14 days (2010 14 days)

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 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 Company and of the profit or loss of the Company for that period In preparing these financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently;
- make 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,
- 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 enable them to ensure that the financial statements comply with the Companies Act 2006 They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

By order of the Board

K J Mckay
Company Secretary
16 April 2012

INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF HALIFAX INDEPENDENT FINANCIAL ADVISERS LIMITED

We have audited the financial statements of Halifax Independent Financial Advisers Limited for the year ended 31 December 2011 which comprise the Statement of Comprehensive Income, the Balance Sheet, the Statement of Cash Flows, the Statement 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

Respective responsibilities of Directors and auditors

As explained more fully in the statement of Directors' Responsibilities set out on page 5, 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 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 Company's affairs as at 31 December 2011 and of its profit and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matters 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

Joanne Leeson (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Bristol
16 April 2012

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2011

	Notes	2011 £000	2010 £000
Revenue			
Revenue	2	7,989	7,852
Finance income	3	45	35
Total revenue		8,034	7,887
Expenses			
Operating expenses	4	(1,809)	(2,314)
Total expenses		(1,809)	(2,314)
Profit before tax		6,225	5,573
Taxation charge	6	(1,650)	(1,560)
Profit after tax		4,575	4,013

There are no items of comprehensive income which have not already been presented in arriving at the profit for the year Accordingly, the profit for the year is the same as total comprehensive income for the year

All activities are continuing

The notes set out on pages 11 to 23 are an integral part of these financial statements

BALANCE SHEET AS AT 31 DECEMBER 2011

	Notes	2011 £000	2010 £000
ASSETS			
Current assets			
Financial assets			
Amounts due from Group undertakings	14	6,989	1,341
Cash and cash equivalents	7	9,996	10,306
Total assets		16,985	11,647
EQUITY AND LIABILITIES			
Capital and reserves attributable to Company's shareholder			
Share capital	8	200	200
Retained earnings		12,717	8,142
Total equity		12,917	8,342
LIABILITIES			
Non-current liabilities			
Provision for other liabilities and charges	9	150	197
Current liabilities			
Financial liabilities			
Other financial liabilities	10	93	184
Amounts due to Group undertakings	14	2,175	1,364
Current tax payable	11	1,650	1,560
Total liabilities		4,068	3,305
Total liabilities and shareholder's equity		16,985	11,647

Approved on behalf of the Board on 16 April 2012

Neil Machray

N L N Machray
Director

The notes set out on pages 11 to 23 are an integral part of these financial statements

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	2011 £000	2010 £000
Cash flows from operating activities			
Profit before tax		6,225	5,573
Adjustments for			
Finance income	3	(45)	(35)
Net (increase)/decrease in operating assets and liabilities	12	(4,975)	1,033
Taxation paid		(1,560)	(1,025)
Net cash flows from operating activities		(355)	5,546
Cash flows from investing activities			
Interest received	3	45	35
Net cash flows from investing activities		45	35
Net (decrease)/increase in cash and cash equivalents		(310)	5,581
Cash and cash equivalents at the beginning of the year		10,306	4,725
Net cash and cash equivalents at the end of the year	7	9,996	10,306

The notes set out on pages 11 to 23 are an integral part of these financial statements

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

	Share capital	Retained earnings	Total
	£000	£000	£000
Balance as at 1 January 2010	200	4,129	4,329
Profit for the year and total comprehensive income	-	4,013	4,013
Balance as at 31 December 2010	200	8,142	8,342
Profit for the year and total comprehensive income	-	4,575	4,575
Balance as at 31 December 2011	200	12,717	12,917

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 13

The notes set out on pages 11 to 23 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 Company 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 sheet, the statement of cash flows, the statement of changes in equity and the related notes

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, are set out below

a) Basis of preparation

The financial statements have been prepared

(1) in accordance with the International Accounting Standards ("IASs") and International Financial Reporting Standards ("IFRSs") issued by the International Accounting Standards Board and the Standards and Interpretations ("SICs") and International Financial Reporting Interpretations ("IFRICs") issued by its International Financial Reporting 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, and

(3) under the historical cost convention

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

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 Company's operations have been issued and are mandatory for accounting periods beginning on or after 1 January 2011 Their relevance to the Company's operations is assessed at note 15

Details of standards and interpretations in issue but which have not been adopted early are set out at note 16

b) Revenue

Revenue, which arose wholly in the United Kingdom consists of commission and fees earned in respect of insurance and investment business and is stated net of commissions and fees paid for introduction of business Revenue is recognised in the period in which it accrues

c) Finance income

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

d) Expense recognition

Operating expenses are recognised in the statement of comprehensive income in the period in which they accrue

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

1. Accounting policies (continued)

e) 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 Company 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 liabilities are stated at amortised cost (as described in policy j below)

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

f) 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 recoverable amount, are assessed using cost price and the factors above, either by a significant amount or for a prolonged period of time are individually reviewed.

Impairment process

Objective evidence that an asset or group of assets is impaired includes observable data that comes to the attention of the 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 flows 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 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 Company

The Company first assesses whether objective evidence of impairment exists individually for assets that are individually significant If the Company 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.

g) Taxes

Tax on the profit or loss for the year is recognised in the statement of comprehensive income within taxation charge and comprises 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

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

1. Accounting policies (continued)

h) Cash and cash equivalents

Cash and cash equivalents includes cash at bank and bank overdrafts

i) Provisions for other liabilities and charges

Provisions are recognised when the Company 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 assessments of the time value of money and, where appropriate, the risks specific to the liability

j) 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

k) 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

2. Revenue

	2011 £000	2010 £000
New business commission	6,254	5,787
Renewal commission	1,735	2,065
Total	7,989	7,852

3. Finance income

	2011 £000	2010 £000
Bank interest	45	35
Total	45	35

4. Operating expenses

	2011 £000	2010 £000
Group recharges	1,520	2,087
Movement in provision	36	15
Computer costs	79	68
Sales and marketing fees	3	2
Compensation	52	112
Other expenses	119	30
Total	1,809	2,314

The administration of the Company is undertaken by other members of Lloyds Banking Group plc A recharge is levied from these undertakings to the other Group companies in respect of those costs incurred by the Company

No staff are employed directly by the Company (2010 nil) All staff providing services to the Company are employed by other subsidiaries of Lloyds Banking Group plc The employee costs, including pension costs and share-based payment costs, are included in the Group recharges

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

5. Auditors' remuneration

Audit fees are borne by another Lloyds Banking Group plc subsidiary and are as follows

	2011 £000	2010 £000
Fees payable for the audit of the Company's current year annual report	14	27
Fees payable for other services		
Reporting returns for the Company	5	5
Total audit fees	19	32

6. Taxation

(a) Current year tax charge

	2011 £000	2010 £000
Current tax:		
UK corporation tax	1,650	1,560
Total current tax	1,650	1,560

(b) Reconciliation of tax charge

	2011 £000	2010 £000
Profit before tax	6,225	5,573
Tax at 26.5% (2010: 28%)	1,650	1,560
Total	1,650	1,560

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% On 21 March 2012, the Chancellor announced that the main rate of corporation tax will be reduced from 26% to 24% with effect from 1 April 2012

7. Cash and cash equivalents

Cash and cash equivalents for the purpose of the statement of cash flows include the following

	2011 £000	2010 £000
Cash at bank	9,996	10,306
Total	9,996	10,306

8. Share capital

	2011 £000	2010 £000
Authorised share capital		
1,000,000 shares of £1 each	1,000	1,000
Alloted, called up and fully paid share capital		
200,000 shares of £1 each	200	200

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

9. Provisions for other liabilities and charges

Mortgage Endowment Provision

The mortgage endowment provision relates to expected costs arising from endowment review cases The amount of the provision has been calculated using past trends, experience to date of the percentage of cases upheld and average compensation payments made

The changes in provisions and any additions made during the year have been charged to operating expenses in the statement of comprehensive income

	2011 £000	2010 £000
At 1 January	197	312
Provisions made during the year	36	15
Provisions utilised during the year	(83)	(130)
Total	150	197

10. Other financial liabilities

	2011 £000	2010 £000
Other financial liabilities	93	184
Total	93	184

11. Tax liability

	2011 £000	2010 £000
Current tax payable	1,650	1,560
Total	1,650	1,560

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

	2011 £000	2010 £000
Increase in operating assets:		
Amounts due from Group undertakings	(5,648)	(83)
Net increase in operating assets	(5,648)	(83)
Increase in operating liabilities:		
Provisions for other liabilities and charges	(47)	(115)
Financial liabilities		
Other financial liabilities	(91)	(72)
Amounts due to Group undertakings	811	1,303
Net increase in operating liabilities	673	1,116
Net (increase)/decrease in operating assets and liabilities	(4,975)	1,033

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

13. Risk management

The Company is an independent financial adviser in the sale of Life, Pensions, Unit Trust and ISA business This note summarises the risks associated with the Company's business and the ways in which the Company manages them.

(a) Governance framework

The Company is part of the Insurance Division of Lloyds Banking Group plc This Division has established a risk management function with responsibility for implementing Lloyds Banking Group plc risk management framework within the Company

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 Risk provides 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 Board that risks within the Company 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 plc's risk management principles and covers the full spectrum of risks that the Company is exposed to Under this framework, risks are categorised according to an approved Lloyds Banking Group plc risk language which has been adopted across the Group This covers the principal financial risks faced by the Company, including the exposures to market, credit and financial soundness risk. The performance of the Company and the strategic management of the business depend on its ability to manage these risks

Responsibility for the management of all risk resides with the Board of each Company, who have delegated their authority to the Insurance Executive Committee

Policy owners, identified from appropriate areas across the business, are responsible for drafting Lloyds Banking Group plc 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 the 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 Company has defined the methodology for the management of risk appetite and has approved appropriate limits Where appropriate for each risk component, limits are defined in terms of the amount of capital required to be held to cover certain specific 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 Company 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 Board must approve a revised limit.

(c) Financial risks

The Company is exposed to a range of financial risks through its financial assets and financial liabilities The most important components of financial risk are credit, market and financial soundness risk.

The market risk that the Company primarily faces due to the nature of its financial assets and financial liabilities is interest rate risk.

The Company manages these risks in a number of ways, including risk appetite assessment and monitoring of cash flow requirements The Company also uses financial instruments as part of its business activities

Financial assets and financial liabilities are measured on an ongoing basis 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 are recognised.

The sensitivity analysis given throughout this note is 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 the most likely other outcomes in respect of each sensitivity, rather than worst case scenario positions

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

13. Risk management (continued)

(c) Financial risks (continued)

(1) Market risk

Market risk is the risk of reductions in earnings and/or value, through financial or reputational loss, from unfavorable market movements This risk typically arises from fluctuations in market interest rates (interest rate 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.

(i) 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 arises in respect of cash balances which are either held on deposit or invested in a cash fund and also in respect of any overdrawn bank balances None of the other financial assets or financial liabilities of the Company are interest-bearing

If interest rates were to increase or decrease by 25 basis points, the impact on profit and loss after tax is considered to be immaterial in respect of cash balances

(2) 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 Company has contracted to meet its obligations

Credit risk is managed in line with Lloyds Banking Group plc Credit Risk Policy

(3) 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 regulatory reporting, tax and disclosure risk

The Company is exposed to the risk that policies and procedures are not sufficient to maintain adequate books and records to support statutory, regulatory and tax reporting and to prevent and detect financial reporting fraud.

Lloyds Banking Group plc 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 Lloyds Banking Group plc 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 and tax returns in accordance with IFRSs, statutory and regulatory requirements

Lloyds Banking Group plc 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

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

13. Risk management (continued)

(c) Financial risks (continued)

(ii) Liquidity risk

Liquidity risk is the risk that the Company 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 the inability to generate cash inflows as anticipated.

Liquidity risk is managed in line with Lloyds Banking Group plc's Funding and Liquidity Risk Policy

All of the financial assets of the Company are held for managing liquidity risk Cash and cash equivalents of £9,996k (2010 £10,306k) have no stated maturity but can be accessed on demand Amounts due from Group undertakings of £6,989k (2010 £1,341k) are generally recoverable within one month from the reporting date

Liquidity risk has been analysed as arising from the settlement of balances owed to other group undertakings of £2,175k (2010 £1,364k) and other financial liabilities of £93k (2010 £184k) These amounts are all contractually due within one month from the reporting date

(iii) Capital risk

Capital risk is defined as the risk that.

- the Company has insufficient capital to meet its regulatory capital requirements,
- the Company has insufficient capital to provide a stable resource to absorb all losses up to a confidence level defined in the risk appetite,
- the Company 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 the Company is regulated by the FSA. The FSA specifies the minimum amount of capital that must be held by the Company in addition to its liabilities

Within the Insurance business unit, capital risk is actively monitored by the Insurance Capital Working Group

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 Company's objectives when managing capital are

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

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 The Company receives most of its funding from its parent and does not raise funding externally

The table below sets out the regulatory capital and the required capital held at 31 December in each year

	2011 £000	2010 £000
Regulatory capital held	8,342	4,329
Regulatory capital requirement	10	10

All minimum regulatory requirements were met during the year

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

13. Risk management (continued)

(c) Financial risks (continued)

(iii) Capital risk (continued)

Compliance with FSA regulatory requirements

The Capital Requirements Directive created a revised regulatory capital framework across Europe governing how much capital financial services firms must retain In the United Kingdom, this is being implemented by our regulator, the FSA which has created new rules and guidance specifically through the creation of the General Prudential Sourcebook (GENPRU) and the Prudential Sourcebook for UCITS (UPRU)

The FSA framework consists of three 'Pillars':

- Pillar 1 sets out the minimum capital requirements that companies need to retain to meet their credit, market and operational risk,
- Pillar 2 requires each company, and the FSA, to take a view on whether the company needs to hold additional capital against firm-specific risks not covered by Pillar 1, and
- Pillar 3 requires each company to develop a set of disclosures which will allow market participants to assess key information about its underlying risks, risk management controls and capital position.

Rule II of BIPRU sets out the provision for Pillar 3 disclosure This must be done in accordance with a formal disclosure document The disclosure of this document meets the Group's obligation with respect to Pillar 3, and is found at www lloydsbankinggroup com

iv) Operational risks

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 Lloyds Banking Group plc as a whole manages its customer relationships affects all aspects of the Group's operations and is closely aligned with achievement of Lloyds Banking Group plc'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 Lloyds Banking Group plc's integration requirements

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

(c) Financial risks (continued)

(iv) Operational risks (continued)

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 implantation 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

(v) Legal and regulatory risks

The Company also faces a number of legal and prudential regulatory risks, reflecting the volume and pace of change within the UK. This impacts the Company 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 investors and ensuring that the Company is satisfactorily managing affairs on behalf of the policyholders Regulators are also keen to ensure that the Company maintains appropriate solvency levels to meet unforeseen liabilities arising from reasonably foreseeable economic shocks or natural disasters As such, the Company is subject to regulatory requirements which prescribe and impose certain restrictive provisions

14. Related party transactions

(a) Ultimate parent and shareholding

The Company's immediate parent undertaking is Halifax Financial Services (Holdings) Limited, a Company registered in the United Kingdom Halifax Financial Services (Holdings) Limited 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 Lloyds Banking Group plc's 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

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

14. Related party transactions (continued)

(b) Transactions and balances with related parties

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

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	
Relationship	**2011 £000**	**2010 £000**	**2011 £000**	**2010 £000**
Parent undertakings:				
Expense recharges and amounts payable	(3,188)	(3,219)	(1,560)	(1,025)
Commission and amounts receivable	8,213	7,965	6,989	404
Other related parties:				
Expense recharges and amounts (payable)/receivable	(623)	658	(615)	599
Cash and amounts receivable	(132)	560	9,996	10,306

All the transactions summarised above were entered into on an arm's length basis The amounts outstanding at the end of the year are included in loans and receivables / payables as appropriate and are repayable on demand unless otherwise specified in the relevant note. All outstanding balances at the balance sheet date are unsecured. There are no amounts past due (2010 none) The Company paid no dividends to its parent company in the year ended 31 December 2011 (2010 £nil)

In addition to the transactions detailed above, the Company's staff costs in respect of the period October 2011 to December 2011 which amounted to £391,000 were paid by group companies on behalf of the Company These costs will not be recharged to the Company

Transactions between the Company 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 Directors and the Insurance Executive Committee.

Directors provide services to a number of companies, in some cases including companies for which they do not act as Directors Their benefits are allocated to the companies to which they provide services depending on the proportion of their time that they spend on each company Some of the Directors of the Company do not spend a significant proportion of their time providing services directly to the Company Their emoluments have been allocated and disclosed in the financial statements of the companies on which they do spend a significant proportion of their time

Transactions between the key management personnel of the Company and parties related to them as defined by IAS 24 "*Related Party Disclosures*" are as follows

Key management compensation:

	2011 £000	**2010 £000**
Salaries and other short-term benefits	3	13
Pension contributions and entitlements	-	1
Share-based payments	2	1
Total	5	15

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

14. Related party transactions (continued)

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

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

Retirement benefits are accruing for one Director (2010 two) under defined benefit pension schemes One Director (2010 one) is paying into a defined contribution scheme

HM Treasury

In January 2009, HM Treasury became a related party of the Company following its subscription for ordinary shares in Lloyds Banking Group plc, the Company's ultimate parent company, issued under a placing and open offer As at 31 December 2011, HM Treasury held a 40 per cent (2010 41 per cent) interest in Lloyds Banking Group plc's ordinary share capital and, consequently, HM Treasury remained a related party of the Company throughout 2011

There were no material transactions between the 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 Company has entered into transactions with HM Treasury on an arm's length basis including, but not exclusively in relation to, the payment of corporation tax Owing to the volume and diversity, such transactions are not disclosed

Share-based payments

During the year ended 31 December 2011, the Company's ultimate parent company operated share-based payment schemes, all of which are equity settled Further details in respect of these schemes can be found in the financial statements of that company

15. Standards and interpretations effective in 2011

The Company 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 Company 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 14

Details of those IFRSs pronouncements which will be relevant to the Company but which were not effective at 31 December 2011 and which have not been applied in preparing these financial statements are given in note 16

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (CONTINUED)

16. Future accounting developments

The following pronouncements may have a significant effect on the Company's financial statements but are not applicable for the year ending 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 Company

Pronouncement	Nature of change	IASB effective date
IFRS 9 *"Financial Instruments"*[1]	Replaces those parts of IAS 39 *"Financial Instruments Recognition and Measurement"* relating to the classification, measurement and derecognition of financial assets and liabilities 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 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 12 *"Disclosure of Interests in Other Entities"*	Requires an entity to disclose information that enables users of financial statements to evaluate the nature of, and risks associated with, its interests in other entities and the effects of those interests on its financial position, financial performance and cash flows	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 It 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

[1] IFRS 9 is the initial stage of the project to replace IAS 39 Future stages are expected to result in amendments to IFRS 9 to deal with changes to the impairment of financial assets measured at amortised cost and hedge accounting Until all stages of the replacement project are complete, it is not possible to determine the overall impact on the financial statements of the replacement of IAS 39

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

17. 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