2998217
Highway Insurance Group Ltd

Contents

LV= by numbers

£126.2m
Underlying operating profit

9.9%
With-profits investment performance

53%
General insurance increase in profits

15%
Life business increase in sales

£861m
Capital Resources

£20.9m
Mutual bonus

5m
Members and customers

70%
Brand awareness

17
Offices

5,600
Employees

Our Strategy

Our strategy is to grow the value of our business for the benefit of our members

To achieve this we aim to put the customer at the centre of everything we do and live by our three brand promises

Easy to do business with
Great value
A caring approach

Throughout our 170 year history, this focus on the customer has been key to the products and services we have offered and is the guiding principle behind the ongoing success of the group

Today with over 5,600 employees working in 17 offices across the UK, we are the UK's largest friendly society and a leading financial mutual, with more than five million members and customers

Our Heritage Business

Whilst growing our successful general and life insurance businesses, we are also very mindful of our heritage and our members who have contributed to it We define our "Heritage" business as

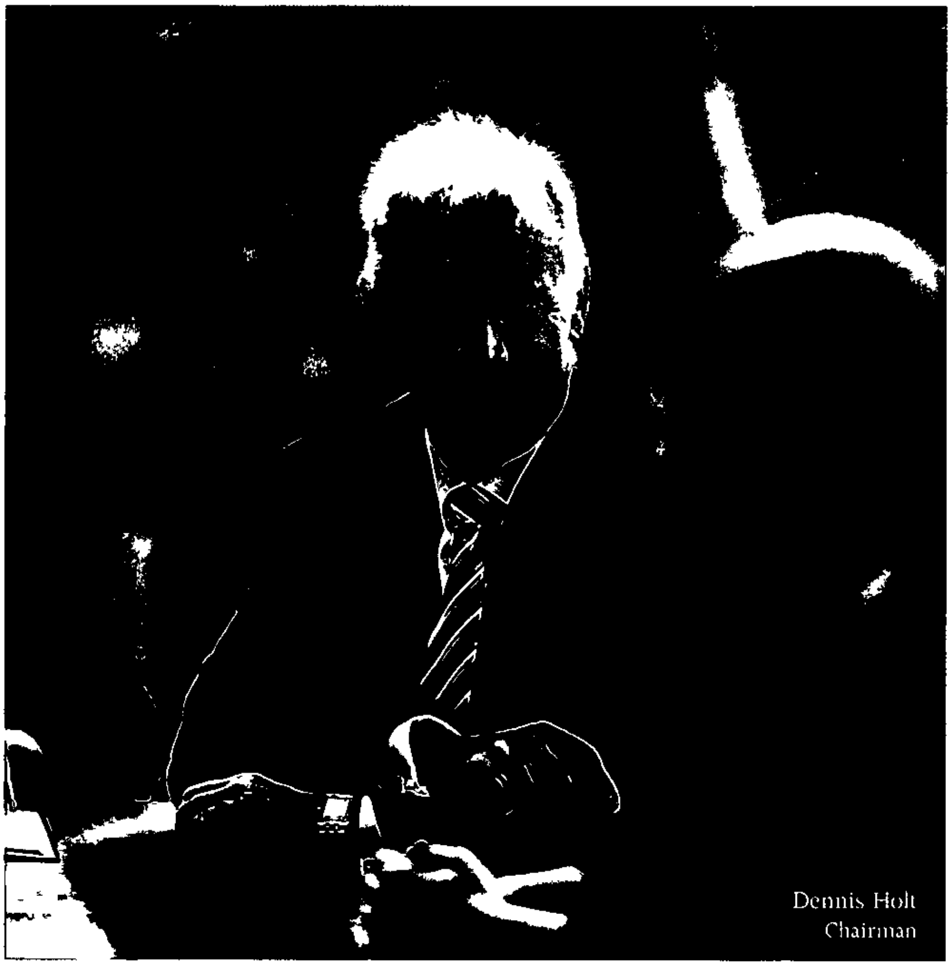
- With-profits policies originally written by Liverpool Victoria Friendly Society, including new with-profits sales
- With-profits and other policies originally written by the Royal National Pension Fund for Nurses (RNPFN) before its transfer to LV= in 2001
- Non-profit annuities purchased from the proceeds of with-profits pension policies together with a minor number of other policies which includes some transferred from other companies

We are committed to offering our with-profits members a fair return on their investments, honouring any guarantees we have made on our policies and providing all our members with great customer service

We also have a mutual bonus scheme, designed to reward eligible members for their ownership of LV= and the risks taken in supporting the establishment and growth of the group's trading businesses

Statements and Reviews

Chairman Statement



Dennis Holt
Chairman

Our purpose remains to help people look after what they love and to deliver on our vision to be Britain's best-loved insurer

Mutal bonus for with-profits members

The banking crisis of 2008 caused an enormous shock to economies throughout the world, and the consequences are still with us Businesses and consumers continue to be financially stressed as a hesitant recovery is attempted It will clearly be some years yet before stability is fully restored In this context, LV= is well placed to help customers with our focus on offering good value, relevant products, backed up by award-winning customer service Our purpose remains to help people look after what they love and to deliver on our vision to be Britain's best-loved insurer In so doing, we are confident that we will achieve our overriding goal of creating value for the benefit of our members

General insurance

The general insurance business has been completely transformed over the last six years to become a major player in retail markets, and one that is known for its award-winning customer service We are now number three in private motor insurance (cars and motorbikes) with an 11% market share and a significant player in our other key lines, particularly home insurance and small business insurance

We have a good mix of products across personal and commercial lines and we are now well established in both the direct and broker channels We have 2 7 million customers in our direct business and, having come from a standing start in 2007, the broker business now has 1 4 million customers, both considerable achievements in a market that is highly competitive

This business is now self-supporting in terms of cash and capital generation, and for the first time returned £38 million of funds to the group following a year of record profits in 2012

Life

Our life business has similarly refocused over the same period, concentrating on market segments with attractive margins and good growth potential As a result we have strengthened our market share positions whilst building profitability We are the market leader in advised income protection and a top three provider for pension drawdown, enhanced annuities and equity release

Our with-profits policies continue to be among the best-performing in the market The first full year with Threadneedle Asset Management Ltd (TAM) managing the assets has seen continued good performance and as a result we have maintained our record of exceeding relevant benchmarks in the short, medium and longer terms

Enterprise Value

+3%

With-profits asset shares outperformed benchmark by 1 5% producing a total overall return for the fund of 9 9%

Group

LV= now has a well established and strong brand This awareness along with our distinctive and award-winning customer service proposition and products means that we are well placed for future profitable growth Fundamental to this is that we put our people at the heart of our business We have been externally recognised by Towers Watson as a high performing organisation and we believe that the culture we have created for our people results in high performing teams, focused on driving the business forward for members

Member value

As LV= is a mutual and not a quoted company, we use Enterprise Value as a way of measuring our market value in a way that is broadly equivalent to a quoted company Our overall Enterprise Value has increased by 3% this year, after taking mutual bonus into account, and follows a 9% increase in 2011

In line with our core ambition of creating value for the benefit of our members, I am pleased to confirm that, for the second consecutive year, the board has approved a mutual bonus for with-profits members of £20 9 million (2011 £18 6 million) reflecting the impressive full year performance and the strength and sustainability of the Society's financial future Group total balance sheet assets are also up 11% to £11 4 billion from £10 3 billion in 2011

Maintaining standards

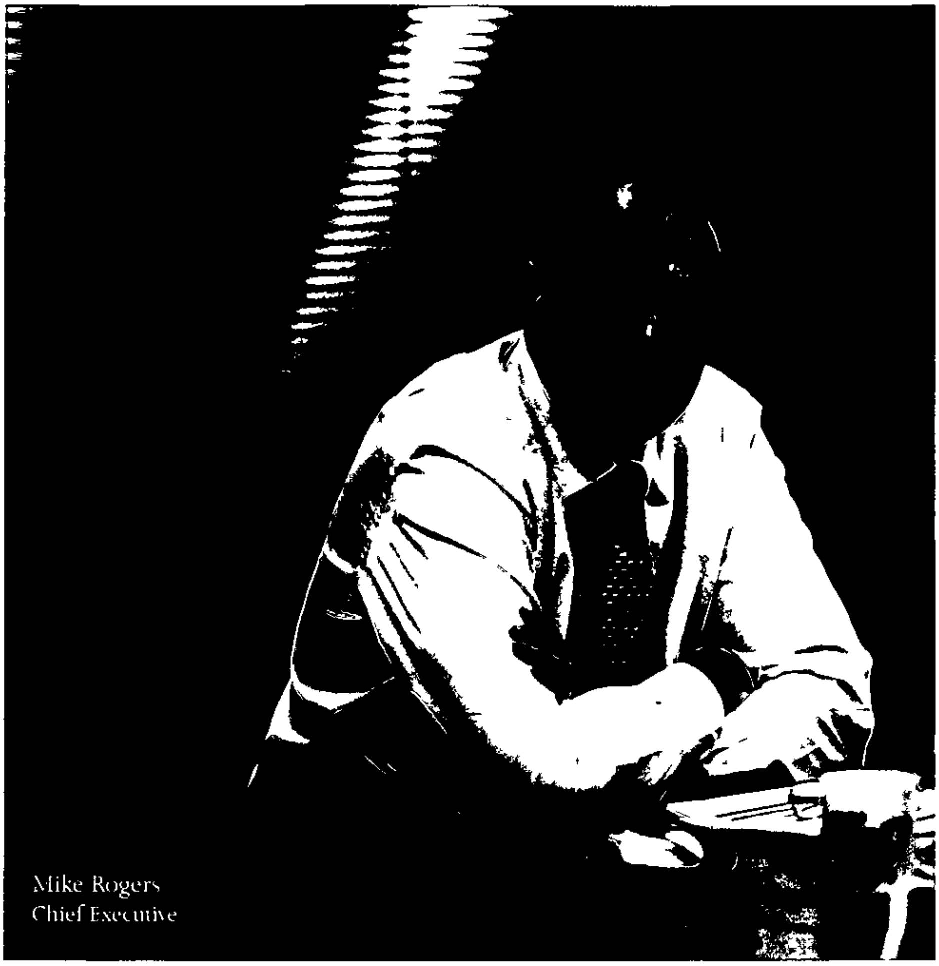
The board continues to guide the development and delivery of our strategy, and to oversee all material aspects of the management of risk and return We continue to apply the same standards of best practice corporate governance that an equivalent shareholder-owned business would be expected to meet

Board changes in the year included welcoming James Dean as a new non-executive director and chair of the Audit Committee, and saying farewell, with our thanks, to Ian Reynolds who stood down having served a term of four years

We have well established competitive positions in attractive markets across general and life insurance which provide the group with a diversity of earnings Our capital position remains strong enabling us to retain a high equity backing ratio for the benefit of our with-profits members as well as paying a mutual bonus

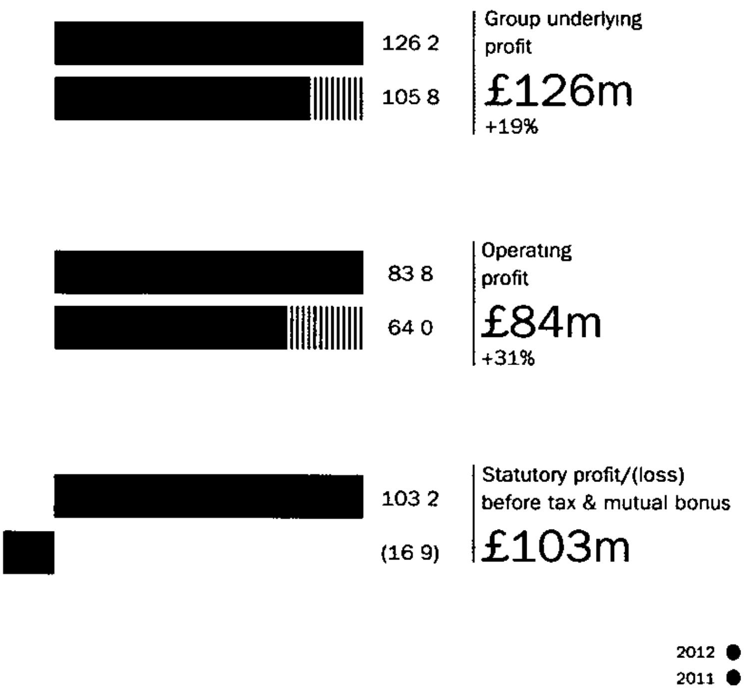
I would like to thank all our members and customers for their loyalty to LV= and our employees for their commitment and hard work We will strive to ensure that we continue to retain your confidence

Chief Executive Statement



Mike Rogers
Chief Executive

We are now established as one of the UK's top three private motor insurers with over 70% brand recognition



I'm pleased to report that 2012 saw a strong strategic and financial performance from all areas of the LV= group This is the fifth year of increased growth and underlying profitability As well as a strong trading performance, we made significant steps in embedding our vision to be Britain's best-loved insurer

Group underlying operating profit increased by 19% to £126 2 million contributing to an operating profit increase of 31% to £83 8 million and a profit before tax and mutual bonus of £103 2 million (2011 loss of £16 9 million) LV='s financial position remains strong and we have over £1 billion of capital resources as at 31 December 2012

We participate in markets where we have a competitive advantage and where there are good prospects for continued manageable and profitable growth Our composite model provides diversity of earnings, a good balance between capital generating and consuming businesses, a powerful shared brand and customer proposition as well as important operational leverage across business support functions These strengths mean we feel well placed to continue to be successful in the future

83%
employee engagement

85%
of our employees think we are an ethical organisation

88%
feel positive about our brand and values

We are now established in top five positions in the majority of our chosen markets in both life and general insurance and we have clear strategic visions for each business which are coming to fruition

General insurance

I'm pleased to report that general insurance had an extremely good financial year Stronger than expected return from investments delivered an underlying operating profit of £117 1 million (2011 £76 4 million) Profitability was achieved despite some £25 million of exceptional weather related costs and further strengthening of our reserves During the year we saw a return to price competition in the general insurance market with downward pressure on motor and home rates, which we do not believe is sustainable into 2013, given continuing personal injury costs and low projected investment returns Our pre-tax return on capital employed was also significantly ahead of our expectations Our focus on key product lines such as car and home in the last five years means we are now established and profitable in these markets and we can increasingly focus on broadening our offering

We were particularly pleased to see the continued strong growth of our SME business line with GWP up 40% to £74 6 million and a strong improvement in our combined operating ratio for this business Most of the growth in our motor book came from our direct business, which grew its customers by 260,000 over the year We are now established as one of the UK's top three private motor insurers, with over 70% prompted brand recognition, an excellent customer service reputation and strong renewal rates

During the course of 2012 the general insurance business received many industry accolades from both consumers and the industry alike The most prestigious of these was being voted General Insurer of the Year at the British Insurance Awards

Looking forward to 2013, we do not anticipate a repeat of the strong investment return seen in 2012, however we anticipate a continued underwriting profit together with increased revenue growth across home, motor and SME, leading to returns on capital and growing cash generation, allowing continued capital flow to the Society

Life business

Our protection and retirement businesses in life saw excellent growth in sales of 15% and an underlying operating profit of £26 3 million (2011 £24 5 million) Our strategy of focusing on market segments with attractive margins and good growth potential where we have relative scale and expertise, has resulted in a continued strengthening of our market share positions We maintained our top three position in enhanced annuities, a market which is continuing to show strong growth driven by a shift in demographics

In protection our position as a specialist, focused on market leading positions in income protection and critical illness, amongst others, has allowed us to grow in a market which is generally stagnant 2012 was a very challenging regulatory year for the life industry and we successfully managed the initial introduction of the Retail Distribution Review and gender pricing, neither of which we anticipate will have a significant impact on our business model or prospects

Looking forward we plan to continue to develop our direct to consumer proposition and hope to see renewed growth in the protection market as economic conditions ease We believe there is the opportunity for continued progression in our specialist retirement business across both annuities and pensions, where we are a leading player in the drawdown market and pension consolidation

Group-wide

During the year we continued to invest in preparation for Solvency II, including the development of our internal model application and enterprise risk management framework The delay to the implementation of Solvency II, announced during the latter part of 2012, is frustrating but much of the investment will continue to bear fruit for us as we manage our capital and risks ever more effectively

Within our legacy business lines, the team continue to work hard in relation to matured policies that have not been claimed As a result since 2007 we have reunited members and their beneficiaries with over £14 million in unclaimed assets

The morale of our people is crucial to the success of our business since it has a direct impact on the experience that our customers receive To measure how our employees feel about working at LV= we conduct an annual staff survey called 'Engage' across the group The survey, conducted in October 2012, showed that 88% of those working at LV= felt positive about the brand and its values, 85% said that LV= is an ethical organisation and 83% said they felt engaged as an employee

These results are despite the decision to close our employee final salary pension scheme to future accrual with effect from 1 July 2013, and offer to move all affected employees to a defined contribution scheme from that date We remain committed to providing our employees with a competitive retirement proposition

Our brand goes from strength to strength and we are attracting increasing recognition and awareness across consumers and the introducer community, including

- Moneywise Most trusted car insurer – voted for by consumers
- Moneyfacts Award for best car insurer and best customer services – voted for by consumers
- Winner of best customer services in financial services at the European Call Centre Awards – voted for by the industry
- Financial Adviser Five star life and pensions provider – voted for by the industry
- Moneyfacts Best income protection provider – voted for by consumers

In a challenging year LV= has been able to deliver excellent results Despite the uncertain outlook for the UK economy, we are confident that our successful business model and strong competitive position in our chosen markets leaves us well placed for 2013

Finance Director Review

Philip Moore
Finance Director

We focus on delivering strong returns for members, while managing and protecting our capital position

Overview

Throughout 2012 LV= operated against a backdrop of volatile financial markets, continued weakness in the UK economy and uncertainty in Europe, with the FTSE 100 falling as low as 5,270 in May and credit spreads widening to 2 87% at the start of the year

Despite this we can once again report a good financial performance this year with the life and general insurance businesses continuing to perform well and the investment returns of our with-profits members' assets outperforming market benchmarks

As a result of this success, LV= has delivered on its financial aims of delivering strong returns to members, while managing the capital position and continuing to foster ongoing growth

Underlying operating profit in 2012 of £126 2 million (2011 £105 8 million) reflects another year of profitable growth from both the life and general insurance businesses This is particularly notable given the increased competition in the markets in which we operate

The £120 million improvement in IFRS profit before tax to £103 2 million (2011 loss before tax £16 9 million) reflects the underlying operating profit performance and positive short-term investment fluctuations, particularly in life, which accounted for £89 million of the improvement year on year

Results for 2012

The table opposite summarises the underlying operating profit split between our businesses Underlying operating profit excludes the impact of model and valuation changes, and a margin for prudence in the life valuation assumptions compared to the value of new business assumptions for example in the credit default allowance

Results for 2012 – unaudited

£m	2012	2011 Restated*
General Insurance	**117.1**	76 4
Life	**26 3**	24 5
Group	**(17 2)**	4 9
Underlying operating profit	**126 2**	105 8
Additional margin for credit default and other risks**	**(29 4)**	(18 9)
Model and valuation changes***	**(13.0)**	(22 9)
Operating Profit	**83.8**	64 0
Accounting policy differences (IFRS)****	**(11.6)**	(7 7)
Short-term investment fluctuations	**65.7**	(46 4)
Centrally managed costs	**(22 7)**	(13 8)
Amortisation of intangibles	**(12.0)**	(13 0)
Profit/(loss) before tax	**103.2**	(16 9)
Mutual bonus	**(20 9)**	(18 6)
Income tax expense	**(34 3)**	(42 2)
Pension scheme actuarial (loss)/gain net of tax	**(145 5)**	69 7
Transfer from the unallocated divisible surplus	**(97 5)**	(8 0)

Restatements have been made to the prior year results to reflect the following changes
The heritage with-profit trading results are now reported within the group result rather than within the life business
Heritage underlying operating profit mainly comprises expense under or over runs
Life results have been restated to reflect the change in the tax gross up rate applied to life value add and additional margin for credit default risk Previously these items were grossed up at 20% Going forward the tax gross up will be based on the weighted average tax rate applicable In 2012 this was calculated at 5%
Life and group underlying profit have been restated to reflect loss of earnings in the life business on funds which have been paid across to the group as dividends in 2011 and 2012

Additional margin for credit default and other risks represents the difference for new business between management s best estimate of credit default which is used to calculate the value of new business reported within underlying operating profit and the market consistent basis used for valuing policies This is principally driven by the annuity business within life

Model and valuation changes represent the impact on the in-force business of changes in valuation assumptions and improvements in the actuarial models used to value existing policies

The life result includes changes in the present value of future profits expected to emerge from policies in-force during the year Where this differs from the treatment under IFRS an adjustment is made in the Accounting policy differences (IFRS) line

Underlying operating profit

£126m

+19%

Operating profit

£84m

+31%

Profit before tax

£103m

The general insurance business has continued to perform strongly delivering a record underlying operating profit in 2012 of £117 1 million which is £40 7 million better than 2011 This growth was driven by good investment returns and profitable expansion in chosen segments, particularly direct motor, partially offset by exceptional weather claims

The life business saw sales growth of 15% in 2012, most notably in key product lines of enhanced annuities, equity release, pensions and protection This growth drove an increase in underlying operating profit of 7% to £26 3 million

Group underlying operating profit includes unallocated group overheads and also the net trading profit or loss of the heritage with-profits business and the return on the group's free capital The loss in 2012 reflects recurring group overheads and also non-recurring cost overruns in the with-profits business as well as a lower return on the free capital

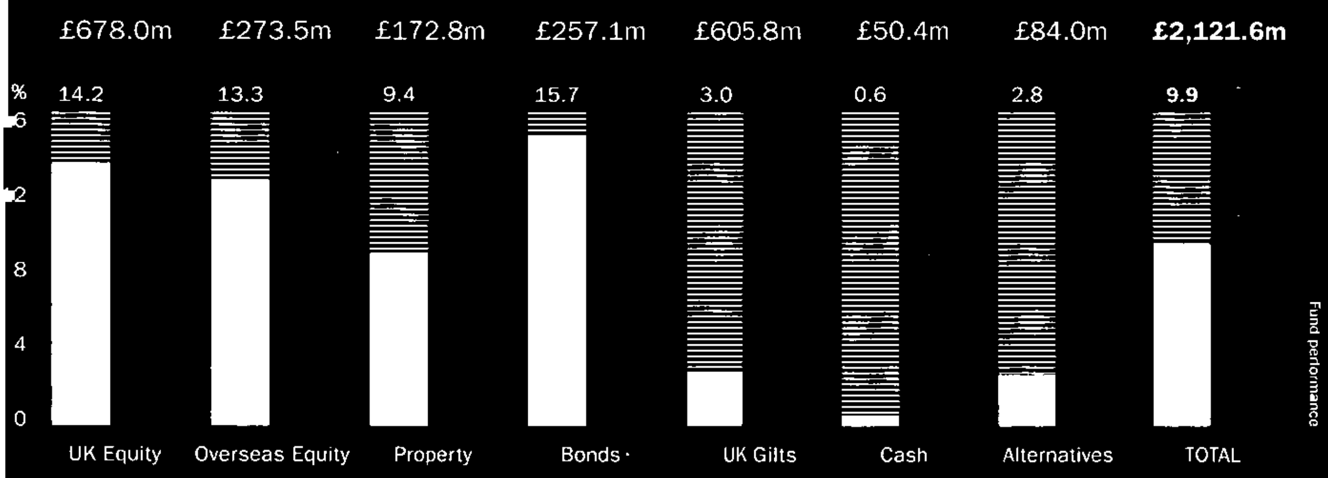
Our IFRS profit before tax of £103 2 million shows growth of £120 1 million reflecting

- Growth in underlying operating profit offset by increased prudence in valuation assumptions particularly credit risk,
- Strong short-term investment performance reflecting market value gains, in particular benefiting from narrower credit spreads in the annuity business bond portfolio and improved equity performance, and
- Centrally managed costs - the group incurred non-recurring costs of £22 7 million mainly in respect of regulatory projects and the decision to reserve an additional £15 million for payment protection insurance claims (PPI) relating to the former banking business which closed in 2010 The net costs included a pension curtailment gain of £13 million

The pension scheme actuarial loss of £145 5 million in 2012 (2011 gain £69 7 million) calculated under IAS19, is primarily due to a reduction in the rate used to discount the scheme's liabilities, and also reflects the impact of this year's triennial review As at 31 December 2012 the scheme reported a deficit of £10 2 million (2011 £106 9 million surplus)

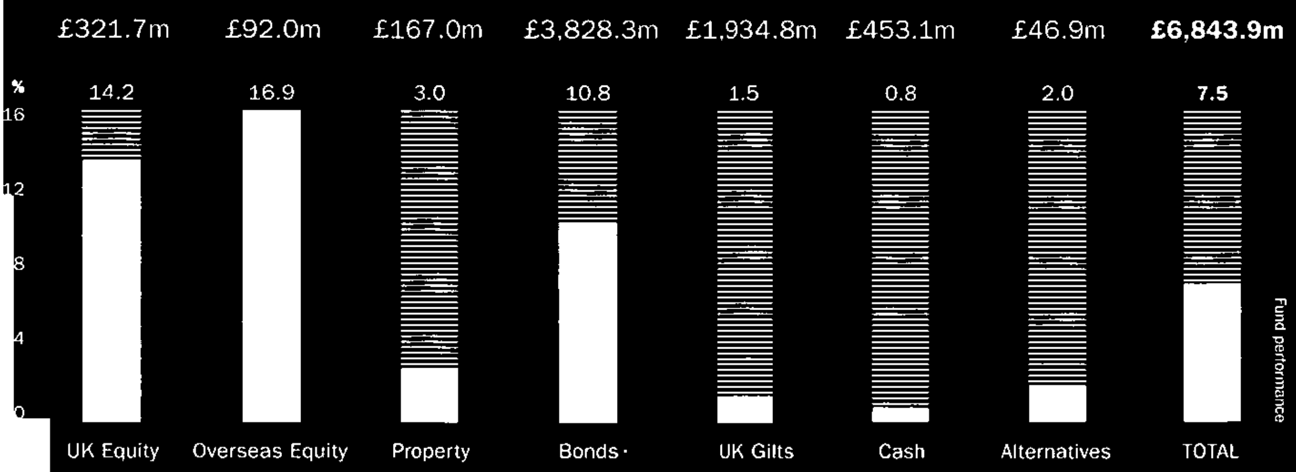
Heritage with-profits fund performance

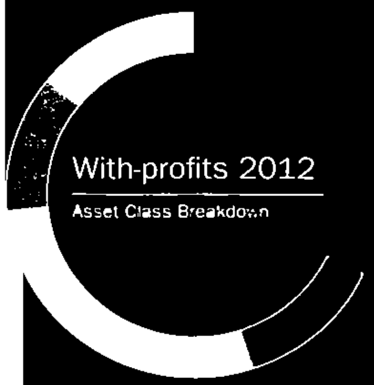
Assets Under Management
Heritage WP Fund
Benchmark



Other Group Assets fund performance

Assets Under Management
Weighted performance





UK Equity	32.0%
Overseas Equity	12.9%
UK Gilts	28.6%
Bonds	12.1%
Property	8.1%
Alternative	4.0%
Cash	2.4%

UK Equity	4.7%
Overseas Equity	1.3%
UK Gilts	28.3%
Bonds	55.9%
Property	2.4%
Alternative	0.7%
Cash	6.6%

9.9%

Total overall return on with-profits assets

* Bonds excluding Gilts

Investment performance

Threadneedle Asset Management – 2012 was the first full calendar year with Threadneedle managing LV='s investments and this partnership proved very successful with six of the seven major asset classes achieving or exceeding their market standard benchmark

With-profits – The strongest performing fund was the Liverpool Victoria Friendly Society (LVFS) with-profits fund with an absolute return of 9 9% Outperformance was mainly driven by stock selection within the equity markets Threadneedle delivered strong relative performance for our with-profits members (some 1 5% points above benchmark) ensuring that LV= remains near the top of the industry performance tables

Other Group Assets – Outside of the LVFS with-profits fund the majority of the assets are invested in bonds and gilts which performed in line with the market The absolute return on these assets was 7 5% which has proven very beneficial to both our annuity book and general insurance business

Capital management

Capital is managed on both economic and regulatory bases to ensure we have sufficient funds to meet our business objectives, promises we have made to our members and policyholders and regulatory requirements Capital is monitored and managed both at a group and entity level

We operate through three main companies

- LVFS is the parent company of the group and the company where we write the majority of our life insurance business LVFS is also the sponsor of our staff pension funds
- Liverpool Victoria Insurance Company (LVIC) and Highway Insurance Company (HICO) – these are the companies which write our general insurance business

We seek to deploy capital where we believe the risk is properly rewarded Asset and liability matching is extensively used and risks are hedged where we believe we would otherwise receive insufficient return for the risk taken or to reduce volatility

We report our capital position on a regulatory basis using current European legislation which defines the capital requirements an organisation must meet The two different bases reported below are

- Peak 1 (a traditional valuation basis), and
- Peak 2 (more realistic for with-profits business)

Capital resources

£m	**2012**	2011
Admissible Assets	**7,865**	7,186
Add back capital requirements of regulated related undertakings	**254**	242
Mathematical reserves (after distribution of surplus)	**(6,686)**	(6,123)
Regulatory current liabilities	**(353)**	(381)
Available capital resources	**1,080**	924
Capital requirements of regulated related undertakings	**(254)**	(242)
Capital resources of RNPFN fund	**(179)**	(164)
Peak 1 Capital requirement	**(240)**	(218)
Peak 1 excess regulatory capital (excluding RNPFN)	**407**	300
With-Profits Insurance Capital Component	**(221)**	(65)
Peak 2 excess capital resources (excluding RNPFN)	**186**	235

During 2012 the main movements in regulatory capital were

£m	**Peak 1**	**Peak 2**
Excess capital at 31 December 2011	**300**	**235**
Opening adjustments	(1)	(60)
Expected changes	12	4
Economic variances	147	59
Basis changes (non-economic)	166	46
Claims experience variances	(54)	(1)
Expense variances	(34)	(48)
New business	(129)	(17)
Staff pension scheme	(32)	(32)
Mutual bonus	-	(21)
Other	32	40
Increase in Risk Capital Margin	-	(19)
Excess capital at 31 December 2012	**407**	**186**

Risk appetite

We have embedded our approach to risk management through our risk appetite This defines a corridor of capital we wish to maintain by risk and entity and we regularly monitor and report our position against our risk appetite If capital moves outside of our defined risk appetite we have a pre-determined and documented series of management actions which we will take to restore the position

Capital management actions 2012

During 2012 we have taken a number of actions to improve our capital position and to reduce the sensitivity of our capital position to market movements Examples of actions taken

- Refining the investment strategy in our annuity book,
- Hedging fixed interest exposure for our deferred annuity book within the with-profits business,
- Hedging of the majority of our longevity risk in our staff pension scheme, and
- Hedging the majority of economic exposure to interest rates and inflation risk for the staff pension scheme

Stress and scenario testing

In addition to calculating capital on the required regulatory regime, we undertake a series of stress and scenario tests to ensure the robustness of our solvency position in regard to different levels of new business growth, movements in investment markets and changes in other assumptions such as the longevity of our enhanced annuity business

In looking at movements in investment markets we consider a number of single stresses (e g equities falling by 40%) and also a number of multivariate stresses (because markets are correlated we expect extreme movements, in say equity markets, to affect other markets, such as the level of credit spreads) These are considered by looking at our distribution of expected market events and we test a number of points on the distribution i e one in 10, one in 100, one in 200 In addition we run a number of 'real world' scenarios such as a repeat of the credit crunch of 2008 and 2009, where we know the exact economic conditions which affected the investment markets, and this enables us to test the robustness of our business model should these conditions be repeated

We use the outcomes of the stress and scenario testing to develop the management actions we would undertake if our capital or other performance measures move outside of our defined risk appetite The impact of some of these stresses is given in note 3 of these accounts As a result of this work and the potential impact that a return to volatile markets would have on our capital base we have developed a number of potential management actions, for example, increasing capital resources through reinsurance structures or other forms of external capital raising which would increase our financial flexibility

Liquidity management

Following continued growth in profits the general insurance business returned funds of £38 million to the group

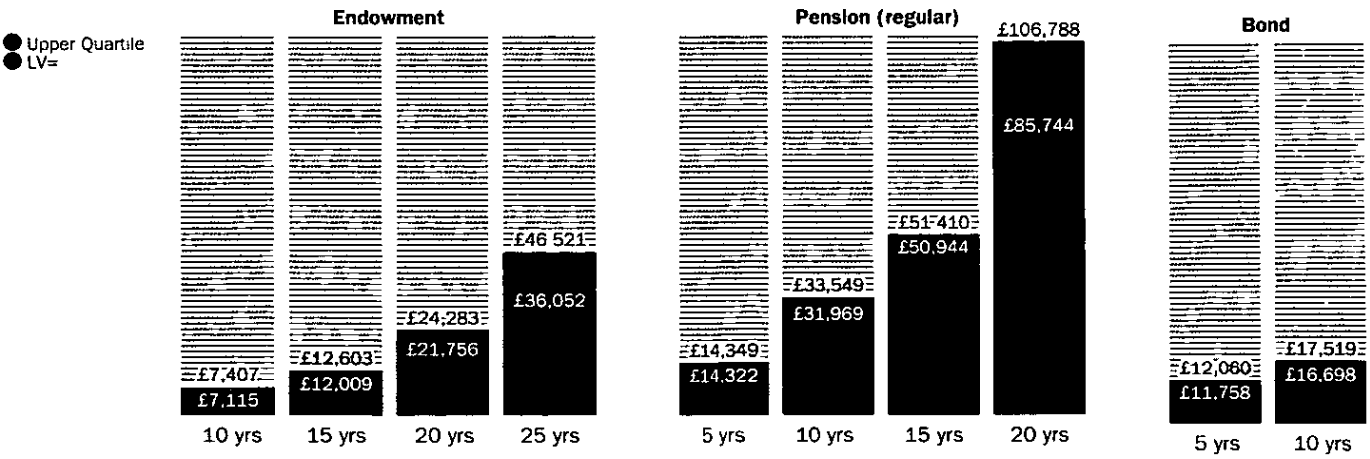
The group manages liquidity primarily through its asset and liability management process which ensures that, on a fund by fund basis and also at legal entity level, assets are held to match liabilities both by amount and by maturity

The group generates cash from profitable trading in the general insurance business and from realised margins on in-force long term insurance policies Surplus cash is used to fund new business growth and central costs

When reserves are strengthened or released at a fund level, assets are either transferred from or paid to the LVFS Estate Fund In addition, surplus capital is held at subsidiary level to ensure that individual entities are adequately capitalised and have sufficient liquidity to meet their obligations as they fall due

Heritage with-profits payouts and industry comparison

Recent maturity and surrender values for LVFS with-profit policies show that LV= continues to perform in the top quartile when compared against industry payouts



Notes

1 The payouts are based on the following policies
Endowment – Policyholder aged 30 at entry monthly premium of £50 maturing 1 February 2012
Bond – An investment of £10 000 as at 1 November 2012
Pension (regular) – Policyholder retiring at age 65 monthly premium of £200 maturing 1 January 2013

2 The industry payouts are taken from the most recent past performance surveys and relate to maturities during 2012 and 2013 The sources are
Endowment – Money Management survey published May 2012
Bond – Money Management survey published December 2012
Pension – Money Management survey published March 2013

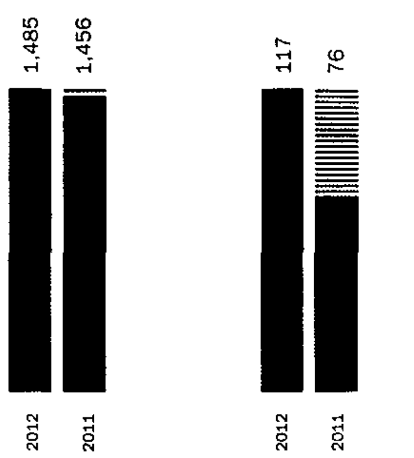
Conclusion

Overall 2012 was a strong year for the LV= group, despite the challenging economic climate While the signs of economic recovery remain fragile, we have a sufficient capital base, manage risk actively, maintain a robust business model and so feel confident that we are well placed to continue growing profitably in our respective markets

Our Businesses

General Insurance Business

John O'Roarke
Managing Director of General Insurance



Gross written premiums (£m)
£1,485m
+2%

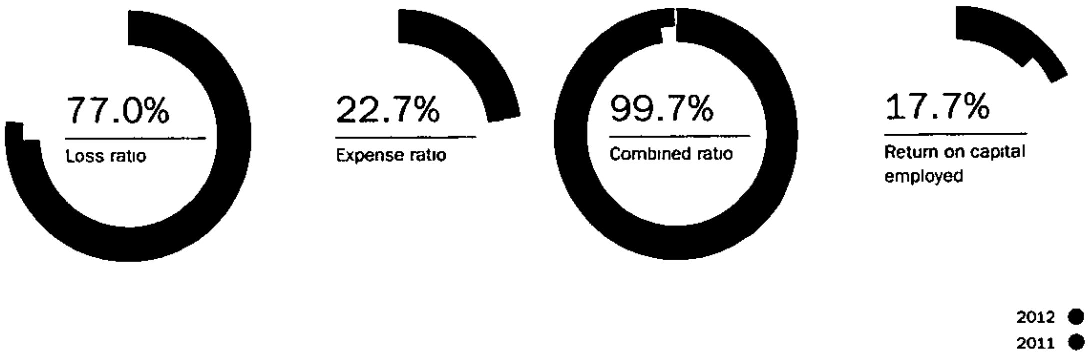
Operating profit (£m)
£117m
+53%

53% increase in profits to £117 million

Review of 2012

In 2012 the general insurance business delivered continued growth in both market share and profitability We now insure three million vehicles, representing a motor market share of approximately 11%, as well as a further 1 1 million policies across other business lines Underlying operating profits climbed to a record level of £117 million, more than £40 million up on 2011 Investment returns contributed £112 million (2011 £46 million) to operating profits Our direct and broker businesses both contributed strongly to operating profits at £64 million and £53 million respectively

These profits were delivered despite a very challenging year for the insurance industry as a whole The year began with severe storms in January, followed by three separate flood events spread throughout the year, which generated a total claims cost of £25 million Our results were also impacted by a further increase in personal injury claims frequency The increase came primarily from low-value whiplash claims, indicating that claims management companies and law firms were accelerating claims activity in anticipation of changes in the law (the Legal Aid, Sentencing and Punishment of Offenders Act – LASPO), which are due to take effect in April 2013 Despite these adverse influences we are pleased to report that we were still able to achieve a sub-100% combined operating ratio of 99 7%



	2012	2011
Gross written premiums	**£1,485m**	£1,456m
Underwriting profit	**£5m**	£30m
Investment return	**£112m**	£46m
Operating profit	**£117m**	£76m
Loss ratio	**77 0%**	74 5%
Expense ratio	**22 7%**	23 2%
Combined ratio	**99 7%**	97 7%
Pre tax return on capital employed	**17 7%**	12 9%
Motor in force policies	**3 0m**	2 9m
Total in force policies	**4.1m**	3 9m

Gross written premiums grew by just 2% for the year as a whole but this masked divergent experience between products and channels The direct business continued to grow very strongly, increasing the number of in-force car insurance policies by 17% to 1 78 million This resulted in gross premiums written for direct car insurance rising by 15% to £662 million Within home insurance, where competition is intense, the direct business grew by 6% to 529,000 in-force policies and total gross premiums also rose by 9% to £146 million

The broker business wrote £655 million of premiums in total, which was 9% down on 2011 In commercial lines, however, written premiums grew by 16% to £160 million, predominantly due to growth in the SME sector This growth reflects our increasingly strong relationships with regional brokers and a successful online proposition for broker-sourced commercial package policies In commercial motor, we found that market premium rates remained inadequate and we were content not to seek growth in market share and as a result commercial motor business grew by just 1% to £85 million Similarly, increased price competition in broker motor personal lines saw sales fall 16% to £481 million

Our customers

2012 was also a year in which we made further progress in making it easy for our customers to do business with us One example of this was our implementation of a new claims system which allowed us to redesign and significantly enhance our claims processes This has led to a more efficient and personalised claims service and resulted in an increase in customer satisfaction scores and a 12% reduction in the claims lifecycle

Our brand awareness also continues to gain momentum and we now have over 70% awareness amongst consumers

As in previous years, the quality and consistency of our customer service was re-affirmed by a number of important customer service awards Our customers voted us 'Best Car Insurance Provider' in the Consumer Moneyfacts awards and 'Most Trusted Provider in the Moneywise awards The Consumer Association's Which? magazine voted us a recommended provider for car and home insurance and we have topped their tables for travel insurance and breakdown cover

In all, we won more than 20 awards in 2012, covering all aspects of our business from underwriting and marketing, through to claims handling and customer service, as well as for counter fraud initiatives and analytics The two most prestigious awards resulted in LV= being named General Insurer of the Year at the British Insurance Awards and the Best Customer Services provider in financial services at the European Call Centre Awards

Motor in force policies

3.0m

Total in force policies

4.1m

Statements and Reviews
Our Businesses
Risk Management
Corporate Governance
Our Accounts

Regulatory uncertainty

As we enter 2013, the UK motor insurance market faces considerable uncertainty as a result of planned or potential legal and regulatory developments The most important of these is the enactment, through LASPO, of the so-called Jackson reforms to civil litigation costs and funding One of the objectives of these reforms is to cut the legal costs associated with personal injury claims and to ban 'referral fees' paid to organisations who introduce claimants to law firms We believe these reforms are essential in order to address the dramatic increase in spurious whiplash claims which has occurred over recent years and which has driven up the cost of insurance for honest motorists

On the regulatory front, the motor insurance industry is currently co-operating with the Competition Commission in a review which aims to identify possible anti-competitive practices in the provision of accident repairs and car hire We welcome the review as we believe it could be effective in eliminating unnecessary frictional costs in our industry which have been a contributory factor to premium inflation over recent years

Finally, we are concerned that the Government and the insurance industry have not yet been able to agree a policy for insuring people who live in flood risk areas The current 'Statement of Principles' whereby insurers continue to offer cover for flood risk properties already on their books, ends in June 2013 Our commitment to continue to offer insurance to all our existing customers remains unchanged but we are working closely with the ABI to find a solution to the problem faced by the wider market

Looking ahead

Despite the combination of increased competitive pressures and an uncertain legal and regulatory environment we are well positioned to continue generating strong returns on capital from the general insurance business We have built a large and loyal customer base on the back of our straightforward promises of great value and quality service This, combined with a team of exceptionally capable and committed employees, means we are well placed to make the most of opportunities which will emerge as market conditions improve

GI Performance

£1,485m
Gross written premiums

£64m
Direct business operating profit

£53m
Broker business operating profit

11%
Motor market share

Life Performance

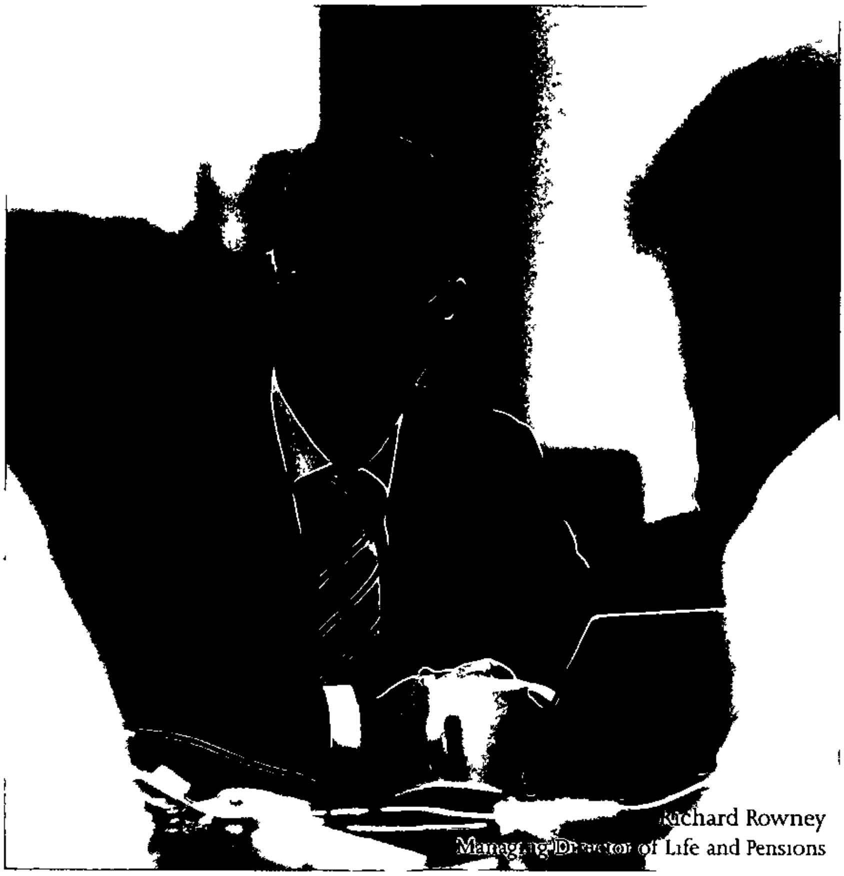
£157m
Annual premium equivalent

15%
Increase in sales

Market Leader
For advised income protection

Top 3
provider for pension drawdown, enhanced annuity and equity release

Life Business



Richard Rowney
Managing Director of Life and Pensions

We are the market leader in advised income protection and a top three provider for pension drawdown, enhanced annuities and equity release

Review of 2012

2012 was another strong year for the life business as we increased year-on-year sales to record levels across a number of key business lines Total sales for 2012 were £157 million, a 15% increase on the previous 12 months

Our strategy of remaining focused on market segments with attractive margins and good growth potential where we have relative scale and expertise, has resulted in a continued strengthening of our market share positions

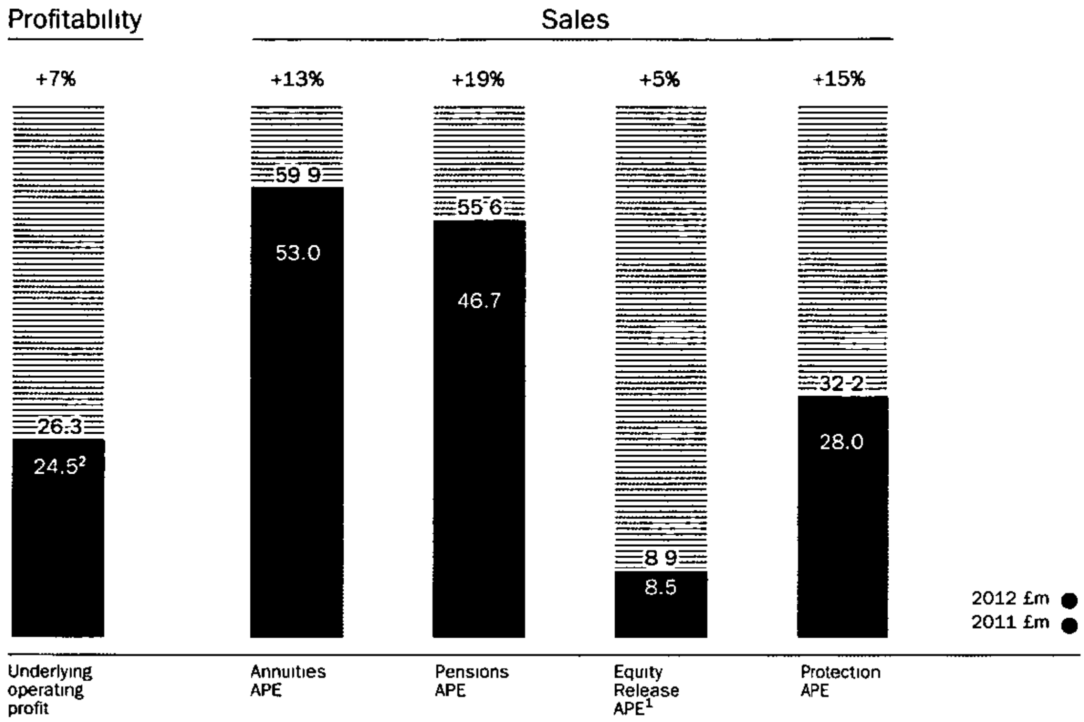
As a result of the strong performance we delivered a 7% increase in underlying operating profit to £26 3 million £11 2 million of this was generated in our retirement solutions business and £15 1 million was within our protection business

This was achieved against a challenging regulatory backdrop for the life and pensions industry as a whole, driven by the implementation of a number of regulatory and legislative changes including the retail distribution review (RDR)

We have maintained strong cost disciplines, with costs as a percentage of our liabilities improving from 4 2% to 3 6%

Within our results we have strengthened our assumptions for the credit default risk which is integral to the yield on bond investments that back our enhanced annuity business

This strengthening of assumptions has been offset by benefits from more favourable economic conditions, which remain challenging, but saw credit spreads narrow during the year



Notes
APE = Annual Premium Equivalent This is a measure comprising new regular premium sales plus 10% of single premiums

1 Equity release loans are reported internally on an APE basis Actual loans advanced during 2012 were £89 million (2011 £85 million)

2 Restated see page 13 for details

Combining great service with 'best in class' products

We remain committed to achieving excellent service standards and 2012 was another strong year for both customer and IFA satisfaction Our reputation as a customer-focused insurer was recognised across a number of industry service awards including the FT Adviser five star service provider awards and LifeSearch awards for best service and best overall product provider

In addition our products also won a number of awards during 2012 including the Gold Standard award for Individual Pensions and for Protection, Best Equity Release Provider in six separate industry awards and the Moneyfacts award for Income Protection Provider of the year

Underlying operating profit

£26.3m

Widening our distribution reach

Our strategy to develop multi-channel distribution capability has underpinned our growth and momentum during the year We were successful in launching a number of new partnerships and network arrangements and using our brand to grow our direct to consumer channel

Key highlights included welcoming the RAC as a key partner in the distribution of our protection products and the renewal of our successful relationship with ASDA which sells our 50 Plus protection product

We extended our already successful strategic partnership with Sesame (with circa 25% market share of the adviser network) to include our retirement solutions products

The adviser and corporate partner distribution channels remain important for us, however the introduction of RDR is likely to shift consumer behaviour in the future and as a result we have invested further in our direct to consumer channel Our strong consumer brand should help us to access customers who may no longer be served by the IFA market

We became RDR compliant well in advance of the regulatory deadline, ensuring that our products and charging structures were compliant with the new regulations

We helped advisers maximise the opportunity that the new gender directive regulation represented Our unique guarantee, which allowed customers to guarantee gender specific rates on protection business right up to the deadline of 21 December, set us apart in the market We were the only provider to offer this guarantee, which demonstrated our commitment to help advisers do the best for customers

Looking ahead

Despite a challenging economic and regulatory backdrop our life business has helped drive significant growth and value for our members over the past five years

Looking to the future, lack of clarity in the market remains, particularly with economic uncertainty continuing to affect consumer sentiment and regulatory changes continuing to impact However we remain confident our well established brand and commitment to outstanding service and quality products places us in an excellent position

Our business strategy to focus on specialist protection and retirement propositions across both IFA and direct to consumer channels means that we are well placed to respond to the changing marketplace We are less exposed to reduced demands from austerity measures as we don't focus on the wealth accumulation or regular savings market

We are also well positioned to take advantage of the favourable demographics over the coming years The 'baby-boomer' customer segment is now at retirement age and faces the challenge of how they'll maximise the value of their accumulated wealth in retirement These customers are becoming more sophisticated with their purchases and we are therefore expecting to see growth in the retirement area of our business with a particular interest in equity release, enhanced annuities and specialist pensions such as SIPPs

The demand for protection products is expected to remain relatively static as economic uncertainty continues and people continue to make every penny count However, we predict that there will be a shift in customer demand towards simple protection products that meet modern day consumer needs Alongside this there will be continued demand for well designed and well serviced more complex products supported by a thriving protection adviser sector We are well placed to support both areas in 2013 and expect to be able to gain market share as a result of our focus and protection expertise

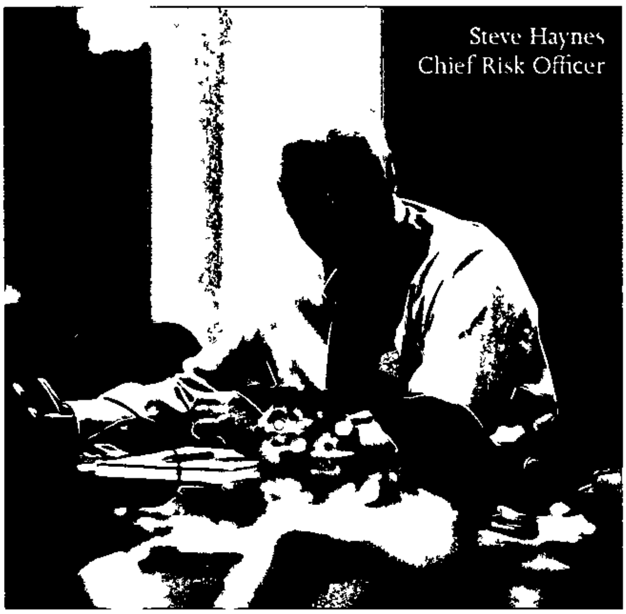
Our strategy remains unaltered We want to be the UK's leading retirement and protection specialist, focusing on profitable, fast growth markets, where we have relative scale

Our focus areas in 2013 will be to

- Maintain growth through the launch of new propositions within the protection and retirement markets,
- Improve our margins through sophisticated risk management expertise,
- Remain disciplined on costs, whilst investing in future capability to maintain our competitive advantage,
- Invest in the training and development of our people, equipping them to provide outstanding service in our chosen niche markets, and
- Continue to manage exposure to market risk in our investments

Risk Management

Risk Report



The role of risk management

The effective management of risk supports the delivery of our strategy, protects the value that we create for members, and helps us to identify opportunities where we can make better use of our capital

Our risk management approach is based on the group's enterprise risk management framework and has the following core objectives

- To set out the risks that the group is able and wishes to accept
- To maintain a risk management and governance framework that in particular assesses and manages the risk-return trade-off
- To measure and monitor the group's risk exposures against the board's approved risk appetite statements and risk limits

LV='s approach to risk

The board has established, through a set of statements, the risk principles and practices the business is expected to adhere to These statements are reviewed at least annually and reflect both the group's strategic plans and the risk strategy The statements approved by the board in 2012 are set out below

In conducting its business LV= adopts a group-wide perspective on risk, and aims to avoid undue concentration, operate within its risk appetite, ensure fair treatment of customers and be competitive in our chosen markets,

LV= will take on risks that it has the capability to understand and manage and which support the group's aim of optimising value for its members, delivering expected policyholder benefits and ensuring it manages the with-profits business in line with the Principles and Practices of Financial Management,

LV= has an appetite for insurance risk in the life and non-life sectors As LV= has long term liabilities, it also retains illiquidity premium through its investment strategy,

LV= takes on market risk in its non-life business, in its with-profits funds in line with policyholder reasonable expectations, and in its pension funds If risk free rates are low, LV= may seek market risk with its mutual capital to earn a higher return, and

As an insurer LV= is exposed to other risks (such as persistency, expense and operational risk) and it manages these to optimise the risk-adjusted return

LV='s risk management and governance framework

LV= has a strong risk culture which is based on the risk management and governance framework The key goals of the framework are

- To ensure a consistent measurement of risk and capital that enables the group to optimise the risk-return trade-off,
- To minimise ambiguity by defining the roles, responsibilities and reporting procedures of the risk and capital decision makers in the group, and
- To ensure that the group identifies, assesses, and manages the material risks to which it is exposed and operates a robust control framework to maintain these risks within risk appetite

Risk appetite

The amount of risk that the group is willing and able to accept is measured and monitored by the board establishing a risk appetite statement and an associated risk tolerance and limit for each major risk dimension The board approved the following risk appetite statements in 2012

Dimension	Risk appetite statement
Capital and Liquidity	LV= will hold sufficient solvency capital and liquidity to ensure that the group can continue to trade following an adverse movement in markets
Earnings	The volatility of LV='s earnings is consistent with the reasonable expectations of with-profits policyholders and other stakeholders
Brand	The group will always seek to uphold its brand image and its vision to be 'Britain's best-loved insurer'
Regulatory	LV= has no appetite for regulatory weaknesses or failings that lead to censure actions
Operational & Capability	The group seeks to minimise operational risk events across the business

Risk governance

The roles and responsibilities for risk management are based on the 'three lines of defence' model The businesses and support functions are responsible for risk taking, implementing the risk management framework and embedding the risk culture (first line of defence) The risk function is accountable for overseeing and challenging the identification, measurement, management, monitoring and reporting of key risks and for developing the risk management framework (second line of defence) The internal audit team provides an independent assessment of the risk framework and the internal control processes (third line of defence)

The businesses and support functions are responsible for ensuring that the controls are effective and will report to the board on any control weaknesses

The Board Risk Committee helps the board to oversee risk and risk management across LV= The businesses and support functions have established Asset and Liability Committees (ALCOs) and Risk Committees to assist them in the execution of their first line of defence responsibilities, and the chief risk officer chairs the Group Executive Risk Committee to support the execution of the second line of defence responsibilities These relationships are summarised in the diagram below

To support a consistent and rigorous approach to risk management across LV=, the risk function has established a set of formal risk policies and risk standards These policies and standards detail the management and control requirements for the group and are reviewed regularly to ensure they align with any changes in the external environment or in the business strategy

As part of this approach the businesses and support functions are required to regularly identify and review their risk exposures and risk controls Where any risks are outside of appetite, action plans are put in place which are reviewed and monitored by the Group Executive Risk Committee

The risk function then aggregates and reports the risks along with an assessment against the risk appetite and risk limits to the Board Risk Committee This reporting also assesses emerging risks and the results of the thematic reviews performed in respect of the group's products and processes

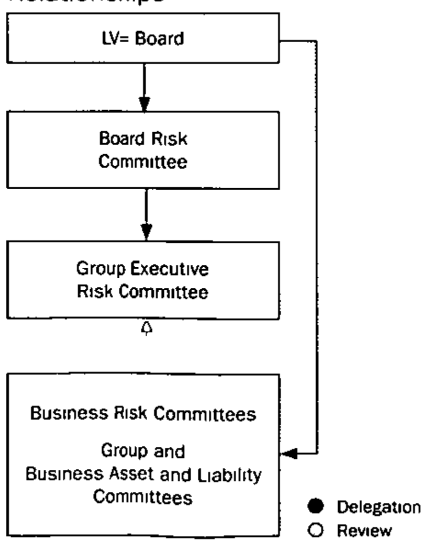
Roles and responsibilities

Board and Board Risk Committee
- Set strategic objectives
- Monitor performance
- Set risk appetite
- Set and uphold values
- Approve risk policies

Second line Chief Risk Officer
- Set business standards
- Monitor performance
- Oversee risk & capital management
- Provide challenge
- Recommend risk management activity

First line Chief Executive/Business & Support Functions
- Oversee risk management
- Monitor risk and capital profile
- Monitor business performance
- Operate in line with agreed policy
- Report to the second line and board

Relationships



Principal risks and uncertainties

A common risk categorisation basis is used across LV= to ensure a consistent record of the names, descriptions and structure of the group's risks. The principal risks to which LV= is exposed are shown below:

Risk type	Definition	Management and mitigation examples
Financial markets risk	The risk that arises from adverse fluctuations or increased volatility in asset values, asset income or interest rates. This includes credit spread widening.	• Active asset management and hedging, including the use of derivatives • Pension fund de-risking • Asset and liability duration matching
Credit counterparty risk	The risk of financial loss as a result of the default or failure of third parties to meet their payment obligations, or variations in market values as a result of changes in expectations related to these risks.	• Investment restrictions on aggregate and fund credit quality • Investment restrictions on sovereign and corporate exposure to some Eurozone countries • Credit counterparty limits and monitoring
Life insurance risk	The risk that arises from the inherent uncertainties as to the occurrence, amount and timing of life insurance liabilities (for example adverse movements in mortality, longevity, and persistency).	• Clearly controlled and defined pricing criteria • Product mix management to optimise capital strain versus return • Use of reinsurance to mitigate mortality/ morbidity/ longevity risks
General insurance risk	The risk that experience is adverse to current best-estimate assumptions underlying the underwriting result (for example adverse movements in claims, or catastrophe experience).	• Use of reinsurance to reduce the impact of catastrophe and large claims risks • Use of data, models and analysis to control pricing and risk selection • Review and analysis of claims and reserve development
Liquidity risk	The risk that LV= and/or its subsidiaries, though solvent, do not have sufficient financial resources available to meet their obligations when they fall due.	• Asset liability matching • Cash flow reporting and forecasting • Active asset mix management
Operational risk	The risk of financial loss resulting from inadequate or failed internal processes, people and systems, or from external events, including changes in the legal and regulatory environment.	• Attestation process that reports to the board on the effectiveness of controls • Risk reporting and root cause analysis processes
Strategic risk	Risk of not achieving the group's strategic plan as a result of internal (e.g. ineffective, inefficient or inadequate senior management processes) or external factors (e.g. economic, legal, political changes) that serve to undermine either the strategy itself or its execution.	• Annual planning process (5 year business plans produced) • Regular tracking and reporting of key strategic risks to the board • Annual strategy review with the board and external input and challenge

Risk environment and profile

The financial markets proved to be more stable in 2012 than in 2011 with gilt yields remaining low, credit spreads contracting, and the FTSE 100 Index rising by circa 6%. The notable exception to these improving trends was the second quarter which witnessed a return to Euro-driven uncertainty which was ultimately dampened by a strong policy response from central banks and Eurozone governments.

Nonetheless, the UK remains in a prolonged economic downturn, and the Euro crisis, the US fiscal cliff and high levels of government borrowing provide ongoing threats to UK growth, consumer confidence and the volatility and performance of investment markets.

The risk profile of LV= didn't change significantly during 2012 and the biggest risks we face continue to arise from adverse movements in financial markets and adverse trends in general insurance underwriting and claims.

During the year LV= completed a number of actions to improve the management of its risks; including:

- Hedges that reduced the risk exposures to rising inflation and interest rates and also reduced the exposure to increases in the volatility of interest rates and equities in the general insurance investment portfolios;
- Reinsurance to reduce exposure to longevity in the staff pension scheme; and
- Asset liability management in the annuity portfolio to further reduce interest rate risk in that portfolio

Corporate Governance

Our approach to Corporate Governance

We choose to observe the requirements of the annotated version of the UK Corporate Governance Code, even though we are not formally bound by it[1]

Compliance with the Annotated Code for the year ended 31 December 2012

The board considers that we fully comply with the applicable principles and provisions of the Annotated Code with the exception of a decision taken by the board that only the chairman will offer himself for annual re-election by members at the Annual General Meeting

Developments in corporate governance

In September 2012 the Financial Reporting Council published an updated version of the UK Corporate Governance Code, an annotated version adapted to the circumstances of mutual organisations was then produced by the Association of Financial Mutuals in November 2012 In early 2013 we completed a review of the amended Annotated Code and following this review we have taken appropriate action to ensure we are compliant including setting out our policy on boardroom diversity

Following the 'comply or explain' principle of the Annotated Code, the board decided that from the 2012 AGM the chairman would stand for annual re-election Dennis Holt, our current chairman is retiring immediately following the 2013 AGM and the chairman designate, Mark Austen, is standing for re-election as a non-executive director In this respect we will not be fully compliant with the Annotated Code, which recommends the annual re-election of all directors, but the board has, in any event, determined that the annual election of the chairman provides an adequate means for members to register concern with the performance of the board directors who continue to stand for re-election at least every three years

Appraising the board's performance

Every year the performance of board members is reviewed both individually and as a team The senior independent director reviews the performance of the chairman, and the chairman reviews the performance of all other directors

The UK Corporate Governance Code recommends that FTSE 350 companies, or equivalents, (which would include LV=) commit to an externally facilitated review of board effectiveness at least every three years A review of the board and its committees therefore commenced in late 2012 The outcome of this review will be considered by the board at its April 2013 meeting

The board

Our board currently comprises six non-executive and four executive directors All the non-executive directors (apart from the chairman, for whom the test of independence is not applicable) are regarded as independent We therefore satisfy the Annotated Code's recommendation that, excluding the chairman, at least half the board should consist of independent non-executive directors

1 The annotated version of the UK Corporate Governance Code and the best practice guidance was published by the Association of Financial Mutuals (the Annotated Code)

Balance of the board

The board contains an appropriate balance of expertise in management, investment, administrative and financial services to meet the requirements of our members and customers

Executive directors

Mike Rogers
Philip Moore
Richard Rowney
John O'Roarke

Non-executive directors

Dennis Holt
Mark Austen
Caroline Burton
James Dean
John Edwards
Cath Keers

Board members

Dennis Holt (64) Chairman

Dennis's experience in banking and insurance spans 36 years as an executive and a further seven as a non-executive director, involving a wide-range of economic and competitive environments He spent 31 years at Lloyds TSB including as retail banking director on the main board This was followed by five years at AXA as UK chief executive and a member of the global executive committee In his six years as LV='s chairman he has led the board as it repositioned the business and delivered on its growth and profit ambitions Dennis is also chairman of Beazley plc

Member of the Risk Committee and the Remuneration and Nomination Committees

Mike Rogers (48) Chief Executive

After graduating from Cambridge University in 1986 Mike spent 20 years working for Barclays Bank where he carried out a variety of roles in the UK and overseas Among his senior appointments at Barclays, Mike was managing director of Small Business, Premier Banking and UK Retail Banking achieving a post-graduate Diploma in Leadership from Exeter University in 1995 In May 2006 he joined LV= as chief executive leading the business into profitability and transforming it into the vibrant and successful mutual it is today

Member of the Investment Committee and Nominations Committee

Philip Moore (53) Finance Director

Having held executive positions at several leading financial institutions Philip s career in finance has spanned almost 30 years He has acquired extensive knowledge in areas such as risk management, actuarial functions and asset management and was chief executive at Friends Provident until 2007 when he joined the Pensions Corporation This was followed by his appointment as finance director at LV= in 2010 As well as being part of the board and executive team at LV=, Philip is also a non-executive of Towergate Partnership Ltd

Member of the Investment Committee

Richard Rowney (42) Managing Director of Life and Pensions

Richard has a first class honours degree and spent 14 years at Barclays Bank holding a number of senior positions across corporate and retail banking including overseeing integration of the Woolwich and Barclays' retail banks He joined LV= in 2007 as chief operating officer where he transformed the operational support areas to ensure they could support the fast growing trading businesses going forward Richard was appointed managing director of life and pensions in 2010 and is also vice-chairman of Bournemouth and Poole College, the eighth largest education college in the UK

Member of the Investment Committee

John O'Roarke (55) Managing Director of General Insurance

John qualified as a chartered accountant and has spent 25 years in the insurance industry He worked for Churchill Insurance for 13 years where he was finance director and then managing director, leading the company to become one of the UK s best known insurers John was appointed chief operating officer of RBS Insurance in 2003 but left RBS in 2005 to set up ABC Insurance, acquired by LV= in 2006 He became managing director of LV= general insurance the same year, leading the team that has quadrupled the size of the general insurance business and produced strong profit contributions

Mark Austen (63) Senior Independent Non-Executive Director

Mark qualified as a chartered management accountant in 1972 and spent the majority of his career at PricewaterhouseCoopers managing their global financial services consulting business His broad range of skills across several disciplines includes advising organisations on their strategies, acquisitions, operations, HR policies and technology As well as being nominated as LV='s next chairman, Mark is also a non-executive director of Standard Bank plc and Mott McDonald Group Ltd

Chairman of the Risk Committee and a member of the Audit, Investment and Remuneration and Nomination Committees

John Edwards (57) Non-Executive Director

John s career in the insurance and investment sector spans over 35 years His past roles include chief executive of Clerical Medical Investment Group, chief executive of the HBOS Insurance and Investment Division and chief executive of International Financial Services at Lloyds Banking Group He has also served as a non-executive director of St James s Place and Esure As well as his position on the LV= board he is also a non-executive director of Nottingham Building Society where he also chairs their Risk Committee

Chairman of the Investment Committee and member of the Risk Committee

Caroline Burton (63) Non-Executive Director

Caroline has a strong life insurance background and is a highly experienced figure in the asset management industry having spent 26 years with Guardian Royal Exchange plc, where she was in charge of investments from 1990 until 1999 She acts as a pensions and business adviser for a number of pension funds and charities and her expertise puts her in good stead to monitor the management of LV='s assets She is also a non-executive director of Rathbone Brothers plc, TR Property Investment Trust plc and Blackrock Small Companies Investment Trust plc

Member of the Audit Committee and the Investment Committee

Cath Keers (47) Non-Executive Director

Cath has over 20 years marketing and sales experience having worked at BskyB, Next and Avon In 2008 she won a lifetime achievement award for her outstanding impact during her career at O2, where she was customer director in charge of refocusing the organisation s customer strategy She brings a wealth of retail industry expertise to the LV= board and holds other non-executive positions at Telefonica O2 Europe, Royal Mail and the Home Retail Group (for Homebase and Argos)

Chairman of the Remuneration and Nomination Committees and a member of the With-Profits Committee

James Dean (55) Non-Executive Director

James is a chartered accountant and is recognised as an expert in insurance accounting having spent much of his 30 years' experience in audit and advisory roles As a senior partner at Ernst & Young he dealt with clients such as AXA, Prudential, Legal & General, RSA and Aviva, serving on boards outside the firm including as chairman of the ICAEW Insurance Committee He is also a former global IFRS leader for the insurance sector

Chairman of the Audit Committee and member of the Risk Committee

Board committees

The following board committees met during 2012

- the Group Audit Committee,
- the Group Risk Committee,
- the Investment Committee,
- the Remuneration and Nominations Committee,
- the With-Profits Committee

The terms of reference for the board committees are reviewed each year and published on our website They can be viewed at LVcom/board-committees

Board and committee membership and attendance in 2012

	Liverpool Victoria Friendly Society Board	Audit Committee	Risk Committee	Investment Committee	Remuneration & Nominations Committee	With-Profits Committee
Meetings in the year	**11**	**5**	**4**	**4**	**5**	**5**
Dennis Holt	10/10	n/a	4/4	n/a	5/5	n/a
Mark Austen	9/10	5/5	4/4	4/4	1/1*	n/a
Ian Reynolds	9/9	4/4	3/3	n/a	3/4	4/4
John Edwards	10/10	n/a	4/4	3/4	n/a	n/a
Cath Keers	7/10	n/a	n/a	n/a	5/5	4/5
Caroline Burton	10/10	5/5	n/a	4/4	n/a	n/a
Mike Rogers	10/10	n/a	n/a	4/4	1/1*	n/a
Philip Moore	11/11	n/a	n/a	4/4	n/a	n/a
John O'Roarke	10/10	n/a	n/a	n/a	n/a	n/a
Richard Rowney	11/11	n/a	n/a	4/4	n/a	n/a
James Dean	5/6	2/2	1/2	n/a	n/a	n/a

n/a Not applicable
*Meeting to discuss Nomination Committee business only

Audit Committee

The Audit Committee is made up of

- James Dean (chairman from October 2012)
- Mark Austen
- Caroline Burton

Ian Reynolds chaired the committee until he stood down in October 2012

The Audit Committee meets at least five times a year with other attendees including, but not limited to

- the chief executive,
- the group financial director,
- the internal audit director,
- the chief risk officer,
- the group financial controller,
- senior management in finance, and
- the external auditor (currently PricewaterhouseCoopers (PwC)

All the members of the committee are independent and bring significant and relevant skills and experience to the function of the committee All members undertake induction training and continuing professional development James Dean, in particular, as the chairman, has the requisite 'recent and relevant financial experience , as recommended by the Annotated Code

The key objectives of the Audit Committee are to

- Work alongside the Risk Committee, to keep the performance of LV='s internal control systems under review,
- Discharge its responsibilities in respect of external financial reporting,
- Ensure the independence of the group's external auditor,
- Monitor the appropriateness and adequacy of the plans and resourcing of the internal audit function, and
- Engage independent counsel and other advisers as it deems necessary to carry out its duties

During 2012 the Audit Committee discharged its responsibilities by

Internal controls

- Considering a number of reports on the group's internal controls and risk management functions and identified key issues, initiating actions for these to be resolved,
- Conducted a full annual review of the effectiveness of all material controls including financial, operational and compliance controls and risk management systems The review's aim was to assess the effectiveness of the control environment and identify any areas for improvement, and
- Reviewed the arrangements through which employees can raise concerns about possible irregularities relating to financial reporting or other matters including reviewing all whistle blowing reports

Financial reporting

- Reviewed the half year and year end processes and financial statements of the group, which encompassed the general insurance and life business results, including recommending the Annual Report to the board,
- Analysed and scrutinized the key accounting policies, judgments and actuarial assumptions with management, the external auditors and the actuarial function holder The committee specifically reviewed the assumptions for credit risk default, the risk free rate, cost inflation and allocation,
- Considered management's regular reviews of the going concern status of the group, and
- Monitored the financial results communicated to members, including the Report and Accounts

Internal audit

- Reviewed the effectiveness and activities of the internal audit function and ensured that it has appropriate standing within the group This review included the results of an internal survey, with the committee concluding that it was a high performing function, while also confirming support for focus on priority issues required by the regulator and in keeping pace with a fast growing business,
- Met privately with the internal audit director,
- Ensured that significant findings and recommendations made by the internal auditor and management's proposed response were received, discussed and appropriately acted upon, and
- Reviewed the proposed internal audit plan for the coming year to ensure that it addressed key areas of risk and that there was appropriate co-ordination with the external auditor

External audit

- Reviewed the performance of the external auditor, including the chairman meeting privately with the auditor to give feedback The committee concluded that the external auditor was effective and recommended the reappointment of the external auditor for a further one year term, agreeing the scope of the audit fee for the forthcoming period,
- Agreed guidelines and monitored the use of the external auditor for any non-audit related work to ensure its continued independence was not prejudiced,
- Reviewed and approved the external auditor's proposed audit scope and approach for the current year as set out in its 2012 audit plan, in the light of the group's present circumstances and changes in regulatory and other requirements,
- Discussed with the external auditor any audit problems encountered in the normal course of audit work, including any restrictions on audit scope or access to information as part of ensuring that significant findings and recommendations made by the external auditor and management's proposed response were received, discussed and appropriately acted upon,
- Met privately with the external auditor PwC, and
- Considered and monitored the independence of the external auditor including any potential conflicts of interest

The committee reviewed its terms of reference and effectiveness in 2012, as it does at least annually, and a change to take ownership of the financial internal model, previously held by the Risk Committee, was recommended to the board For 2013 a group wide project is underway to review and document the committee governance structure, including the terms of reference and delegated authorities In addition, the Audit Committee is also actively seeking to appoint an additional independent non-executive director to join the committee in 2013 to further enhance its effectiveness

The Risk Commitee

Risk Committee is made up of

- Mark Austen (chairman)
- Dennis Holt
- James Dean
- John Edwards

Ian Reynolds also served on the Risk Committee during 2012

The Risk Committee meets at least four times a year with other attendees including, but not limited to

- the chief executive,
- the group finance director,
- the chief risk officer,
- the internal audit director, and the head of compliance

It is the chairman's practice to meet separately with the chief risk officer ahead of most meetings The principal role of the committee is to consider the risks faced by LV= and advise the board More specifically its main activities during 2012 included

- Agreeing and monitoring risk strategy, risk appetite and individual limits for specific types of risk (e g financial markets risk and credit risk),
- Reviewing and assessing the risk oversight provided by management in connection with current and emerging risk exposures,
- Assessing the impact of management's strategic plans on the risk profile of the group,
- Monitoring the effectiveness of management in identifying and recording the principal risks,
- Gaining assurance that an appropriate culture in relation to the management of risk continued to be maintained, with particular focus on performance measurement,
- Scrutinising the Individual Capital Assessment (ICA) prepared by management and recommending its acceptance to the board, and
- Receiving reports from the chief risk officer and the head of compliance on a wide range of issues, including regulatory change

During 2013, the committee will focus on the continued implementation of an own risk and solvency assessment process, risk based performance measures and reporting, a refreshed oversight and apportionment process and enhanced monitoring of LV='s conduct risk framework

A further change is that the responsibility to scrutinise the ICA will be assumed by the Audit Committee This will support the Board Risk Committee focus on monitoring the risk profile and associated capital requirements of the group in light of its current and projected free assets

Remuneration and Nomination Committee

Sitting as the Remuneration Committee, the committee met five times during 2012 and is expected to meet four times in 2013 The committee is made up of three independent non-executive directors

- Cath Keers (chairman)
- Dennis Holt
- Mark Austen

Input is provided by the HR director and the chief risk officer, who attend by invitation On behalf of the board, the committee determines

- Our broad policy on executive remuneration, and
- The specific packages for each of the executive directors and certain senior managers

More details of the group s policy on executive and senior management remuneration, and the activities of the committee during the year are set out in the Directors Report on Remuneration

In its capacity as the Nomination Committee, which also includes the group chief executive as a member, the committee

- Evaluates the balance of skills, knowledge and experience on, and required by, the board for board appointments and certain senior management roles, and
- Prepares a description of the role and capabilities required for any particular appointment

Recruitment consultants will usually be instructed to help compile a shortlist of candidates for interview for board vacancies The committee will then recommend appointments to the board for approval During 2012 the Nomination Committee oversaw the recruitment of James Dean to the board The committee intends to recruit a further non-executive director during 2013 following the retirement of Dennis Holt on 23 May 2013

Investment Committee

The Investment Committee comprises three non-executive directors

- John Edwards (chairman)
- Caroline Burton
- Mark Austen, and

four executive directors comprising

- the chief executive,
- the group finance director,
- the managing director of the life and pensions business, and
- the finance director of the general insurance business

The committee meets four times a year and the group's chief investment officer, chief risk officer and representatives from the group's asset manager, TAM usually attend by invitation

It is responsible for

- Monitoring and reviewing the management of our investments by TAM, and
- Confirming to the board each year that the continued appointment of TAM remains appropriate, having regard to the operation of its mandates and relative performance and charges compared to alternative providers

With-Profits Committee

The With-Profits Committee meets at least five times a year, and comprises

- Graham Burville (independent chairman)
- Cath Keers
- John Perks, the managing director of our retirement solutions business

Graham Burville has extensive and relevant industry experience and was formerly CEO of Police Mutual

Ian Reynolds also served on the With-Profits Committee during 2012

The role of the Committee is to

- Bring independent judgement to the assessment of compliance with the statement of Principles and Practice of Financial Management, and
- Monitor how any competing or conflicting interests between different groups of policyholder are resolved

The committee can engage external professional advisors to assist in delivering its objectives effectively and draws on the expertise of an independent with-profits actuary, Nick Dumbreck, who was appointed in February 2012

Group Executive Committee

The chief executive chairs this weekly committee meeting to monitor our business performance It also meets monthly in order to help him meet the responsibilities which the board has delegated to him

Matters reserved for the board

There is a clear list of matters which only the board can decide on, other matters are delegated to the group chief executive Matters reserved to the Society's board include

A) Strategy and planning
- determining and overseeing delivery of the group's strategy
- approval and monitoring of long-term strategic plans/objectives
- approval and monitoring of the group annual business plan

B) Risk
- allocating capital based on risk and return criteria
- determining the risk appetite of the business and overseeing its usage

C) Financial matters Approval of
- capital and revenue expenditure exceeding £5 million within agreed budget and £2 5 million outside agreed budget and any other expenditure outside the normal course of business
- the Annual Bonus Declaration
- the Individual Capital Assessment and its submission to the FSA
- the Valuation Report and the Annual Report and Accounts
- Member Bonus

D) Mergers, acquisitions and disposals
- approval of mergers, acquisitions and disposals and overseeing effective integration

E) Governance and compliance Approval of
- the Notice of AGM (including reappointment of auditors), any proposed amendments to the Memorandum & Rules and related documentation in connection with the AGM
- any charitable or political donations
- the membership of board committees
- the terms of reference of board committees and subsidiary company boards
- the appointment of company nominees to the Staff Pension Scheme trustee company board
- policy changes in pension entitlement and SPS funding

F) Appointment and removal of officers
- appointment and removal of the Society's chairman, deputy chairman (if appointed), senior independent director, company secretary, group chief executive, chief investment officer, chief risk officer, with-profits actuary and actuarial function holder and directors of the Society and its subsidiaries

In 2012 the board met eight times for formal board meetings, twice on an ad hoc basis to discuss specific issues and once for an ad hoc strategy session In 2013 the board expects to meet at least eight times and to have two strategy sessions

There was one new appointment to the board in 2012 James Dean joined the board as a non- executive director in July

Under the Society's Rules all directors are required to stand for re-election at least once every three years, and therefore Mark Austen and Mike Rogers will be offering themselves for re-election at the 2013 Annual General Meeting along with our new appointee James Dean We are actively recruiting an additional non-executive director who it is anticipated will join the board during 2013 and will offer themselves for re-election at the 2014 AGM

Member relations

The board believes that communicating with members is of prime importance An important mechanism for this is the LV= Member Panel, currently comprised of 30 members This group meets with our chairman, his executive team and other senior managers to learn about our recent performance, strategy, and future plans and to provide input and challenge The board will continue to monitor the effectiveness of this interaction and make further changes as appropriate

We also operate the LV= Community which allows us to send regular emails to over 11,000 users with the latest LV= news, offers and the opportunity to take part in research Participants give us valuable input and comments on new developments, such as product design or customer service processes

The Member Care Line is a free and exclusive benefit that handled over 1,100 phone calls in 2012 where members were seeking medical or legal advice We also run a Member Support Fund which provides one-off financial grants to members who find themselves, through no fault of their own, in severe financial difficulties Requests for help are assessed by a small independent committee of members Grants that were awarded during the year amounted to almost £33,000 Our members are also entitled to discounts on a range of products

Directors' Report

Rachel Small
Company Secretary

The directors of Liverpool Victoria Friendly Society Limited present their annual report together with the accounts for the year ended 31 December 2012

Our members

+6,000

2012	1,133,000
2011	1,127,000

Business activities and future prospects

LV= is an incorporated friendly society that, together with various subsidiaries, carries out insurance and financial services business in the United Kingdom, through LVFS and its subsidiaries These activities cover with-profits assurance, life protection (both term and whole of life), annuities, equity release, motor, home, pet and travel insurance The directors consider that all the activities undertaken by the group during the year were within its rules and any relevant regulatory permissions

A review of the business for the year ending 31 December 2012, recent events and likely future developments is included below

The board sets objectives and priorities supported by key performance indicators (KPIs) and targets, which it monitors on a regular basis throughout the year

During 2012, the key objectives and priorities were

- Achieving the profit and enterprise value target results for each business unit,
- Completing the transformation of the general insurance business into a mature cash generative business,
- Sharing the financial returns from our trading businesses with members via a mutual bonus scheme,
- Completing the implementation of a major new system for the management of general insurance claims,
- Further enhancing our enterprise risk management framework, operating at all times to required regulatory standards,
- Completing our programme to achieve compliance with the requirements of Solvency II and the new regime established by the Retail Distribution Review, and
- Achieving progress towards our goal to be Britain's best-loved insurer

Board directors and interests
The current members of the board and details of its various committees are shown on pages 32 to 35 together with their dates of appointment

John O'Roarke is a minority shareholder in LV Insurance Management Limited with a 1 11% shareholding and is a party to the contract for LVFS to acquire the remaining interest in that company Further details are given in note 40 to the Financial Statements

We continued to maintain liability insurance cover for our directors and officers during the year

With-profits bonus declaration
We have declared an annual bonus for the year ending 31 December 2012 at 1% of the sum assured for Industrial Branch business and at 2 0% of the sum assured for conventional Ordinary Branch life business Interim bonus rates will also be at these levels Terminal bonus rates in 2012 maintain our highly competitive position

Basis of accounting
These accounts are presented using International Financial Reporting Standards (IFRS), as adopted by the European Union, drawn up on a going concern basis The directors are satisfied that the group has adequate resources to continue in business for the foreseeable future and that accordingly the going concern basis is appropriate Further details about the directors' responsibilities for the accounts are described below

Fixed assets
Changes in our fixed assets are shown in note 27 of these accounts

Margin of solvency
Throughout the year and at 31 December 2012 we held the required capital resources for each business class as prescribed by the Financial Services Authority

Independent auditor
A resolution for the re-appointment of PricewaterhouseCoopers LLP as auditor will be proposed at the 2013 AGM

Managing risk and return
We look to create value for members by maintaining an appropriate balance between the returns that we seek and the level and type of risk we take on in order to achieve these returns

To better manage risk levels on a day to day basis a system of capital budgets is in place for each business Each business is expected to manage its position in line with its capital budget and risk appetite position

A full overview of our risk management can be found on page 26 Note 3 of these accounts also provides further detail about our risk management and control

Internal control
The board has overall responsibility for the group's internal control systems and for monitoring effectiveness Implementation and maintenance of the internal control systems are the responsibility of the executive directors and senior management The performance of the internal control systems is reviewed by the relevant board committees, principally the Audit Committee, which take reports from the internal audit, compliance and risk functions

The group's internal control systems are designed to manage, rather than eliminate, the risk of failure to meet business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss In assessing what constitutes reasonable assurance, the board has regard to materiality and to the relationship between the cost of, and benefit from, internal control systems

In 2012, the board undertook a full annual review of the effectiveness of the material controls, as recommended by the UK Corporate Governance Code The review incorporated an evaluation of the group's framework and an assessment of any significant internal control issues that were raised during the year in relation to financial, operational and compliance risk controls Whenever any significant control weaknesses are identified actions are taken, or agreed plans are put in place and tracked by the board to implementation The system was in place throughout the year and as at the date this Report was approved

Charitable donations
A full view of our charitable donations and corporate social responsibility activities can be found on page 43 In 2012 no political donations were made

People employed by the group and its subsidiaries
The average number of people we employ and our total employee costs are shown in note 38 of the accounts

Membership
As at 31 December 2012, we had 1,133,000 (2011 1,127,000) members

We make all reasonable and cost effective attempts to trace and contact members if we believe their address details are incorrect When all reminder or tracing techniques have been exhausted we maintain a record of the relevant member and, if they have an unpaid claim, the policy remains open for payment until we can re-establish contact

Statement of disclosure of information to the auditor

As at the date of this report each director confirms that

1) so far as (s)he is aware, there is no information relevant to the audit of the Society's financial statements for the year ending 31 December 2012 of which the auditor is unaware,
2) (s)he has taken all steps that (s)he ought to have taken in his/her duty as a director to make him/herself aware of any relevant audit information and to establish that the Society s auditor is aware of that information

Responsibilities of the board of directors for the accounts

The Friendly Societies Act 1992 (1992 Act) requires a friendly society's Committee of Management to prepare accounts for each accounting period As we are incorporated under the 1992 Act our board of directors has assumed the responsibilities and duties of the Committee of Management in relation to these accounts

These accounts must comply with the relevant provisions of the 1992 Act, and present fairly the financial position, financial performance and cash flows of the society and the group at the end of the accounting period In carrying out this duty, the directors have chosen to use IFRS as adopted by the European Union

Legislation in the UK that governs the preparation and publication of accounts may differ from legislation in other jurisdictions A fair presentation of our accounts in accordance with IFRS requires our directors to

- Select suitable accounting policies and ensure they are applied consistently,
- Prepare the accounts on a going concern basis, unless it is inappropriate to presume that the Society and the group will continue in business,
- Make judgements and accounting estimates that are reasonable and prudent,
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- Provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Society and the group's financial position and financial performance, and
- State that the Society and the group have complied with applicable IFRSs, subject to any material departures disclosed and explained in the accounts

The directors are also responsible for maintaining

- Proper accounting records which are intended to disclose with reasonable accuracy, at any time, the financial position of the Society and the group,
- Appropriate internal control systems to safeguard our assets and to prevent and detect fraud and other irregularities, and
- The integrity of the corporate and financial information included on our website LVcom

The directors are responsible for the maintenance and integrity of the group's website Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

Each of the directors, whose names and functions are shown on page 32, confirm that to the best of their knowledge and belief

- The group financial statements, which have been prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the group,
- The Business Review on pages 12 to 16 includes a fair review of the development and performance of the business and the position of the group, and
- A description of the group's principal risks and details of the group's risk governance structure are provided on pages 26 to 28

By order of the Board of Directors

Rachel Small

Rachel S Small, Company Secretary
27 March 2013

Corporate Social Responsibility

Business ethics

As a leading financial mutual we take our responsibilities as an ethical company seriously Our approach to corporate social responsibility is embedded in our culture and positive attitude towards everyone we deal with

Supplier ethics

We recognise it is important to build successful and collaborative relationships with our suppliers and we expect them to support our ethical approach to business We base our working practices with them on our core values, and in return ask them to support our ethics Consequently we ask all our suppliers to act in accordance with our ethical supplier policy This requires them, among other things, to comply with all laws and regulations, not to exploit child labour and not to discriminate against their workforce In order to ensure this, a number of steps are taken These include (but are not limited to) rigorous due diligence of potential suppliers during the tender process and regular business assurance audits with suppliers to monitor compliance

Governance and responsible investment

We are committed to being a responsible investor and active owner This commitment is shared by TAM who are responsible for managing our investments They follow governance and responsible investment principles and procedures based on the United Nations backed Principles for Responsible Investment (PRI), the UK Stewardship Code as well as best practice corporate governance guidelines

It is our joint belief that well-governed companies are likely to outperform in the long run and therefore TAM consider a holistic understanding of risks and opportunities associated with certain companies, sectors or themes, as part of generating sustainable returns for their clients Their Governance and Responsible Investment (GRI) team has worked alongside the firm's investment professionals since 1998, facilitating integration of material environmental, social and governance (ESG) analysis into the investment process The GRI research and engagement primarily focuses on equities and is being expanded to cover ESG research to fixed income, where ESG risks and opportunities can impact credit scores

Complaints policy

We aim to provide an excellent standard of service to our members and customers, but recognise that there may be occasions where service falls below expectations Our policy is to deal with any complaints promptly, fairly and honestly

Processes are also in place to ensure we swiftly take any necessary preventative action We call this root cause analysis It means we closely monitor all complaints enabling us to quickly identify if there is a problem with our processes so we can put it right going forward

Where regulation or guidance govern complaint procedures, we have taken steps to ensure we remain compliant If we are unable to resolve the matter satisfactorily, the complainant will be advised to refer the matter to the Financial Ombudsman Service

Financial crime

LV= takes a highly proactive approach to fighting financial crime and in 2012 we achieved savings of £39 million as a result of our robust attitude We also handled a number of fraud cases that have set market precedent in the high court and in private and public prosecutions

Our goal is to create and deliver market-leading financial crime management This will ultimately enable us to offer lower premiums to customers as a result of the successful cancellation of fraudulent policies and the tackling of fraudulent claims

HR matters

The success of LV= continues to be driven by committed people right across the business We believe that happy people make happy customers and therefore we have created a culture of empowerment and support for our people

LV= continues to grow and during 2012 the HR team handled 30,000 job applications with a thousand new employees joining us during the year

As we grow, it is important to ensure that we maintain a sense of shared purpose and values so, every year, we conduct an independent survey to find out how engaged our employees feel This allows all of our people to give us detailed feedback about life at LV= across a broad range of topics

In 2012 we were recognised as a UK High Performing Organisation (HPO) by Towers Watson Towers Watson reviews businesses across the globe and publishes a list of those that it believes have high-performance cultures, focused on improving the return on talent investment and delivering measurable business results

We provide employees with information on issues relevant to their employment and our performance through meetings, regular magazines and an employee intranet We also drive an upbeat people culture through an effective internal communications programme which celebrates our values, image and competitiveness

The management team actively engages with an Employee Consultative Forum on issues important to employees, including their working environment, facilities, terms of employment and safety

Equal opportunities

We are committed to equal opportunities and the fair treatment of all our employees In line with our corporate values we undertake to treat all our employees with dignity, respect, and consideration We recognise our commitments under the law and are resolute to providing equal opportunities by ensuring that our practices and procedures follow legal requirements and good practice, as recommended by the Commission for Racial Equality, the Equal Opportunities Commission, and the Disability Rights Commission

Our policy is to treat all employees and applicants fairly and equitably regardless of gender, racial or cultural grounds, disability, age, marital status, religious beliefs, sexual orientation, trade union activity or any other category where discrimination cannot be reasonably justified We will ensure that no requirement or condition will be imposed without justification that could disadvantage individuals on any of these grounds

Diversity

Diversity and inclusion are fundamental to our culture and core values, and in creating an innovative, collaborative and high-energy work environment By embracing an inclusive culture that supports diverse talent, our people enable LV= to be successful

Our workforce gives customers access to a rich range of talent, representing different styles, perspectives and experiences This range of diversity, including gender balance, at all levels in the organisation is a critical strength that we are committed to fostering through a clear diversity and inclusion programme

LV= recognises the need to address gender imbalance at senior levels and therefore is working to identify and assist senior women through an appropriate mentoring and diversity programme Our new chairman for 2013, Mark Austen, has been invited to join the 30% club (a group of chairmen voluntarily committed to bringing more women onto UK corporate boards) and reflects the board's commitment to encouraging diversity within the workplace The board also sets periodic targets for female representation at senior levels and reviews progress

Talent management

We're committed to training and developing our people so they fulfil their potential Everyone has access to training programmes and follows a personal development plan to ensure they are equipped with the right skills and behaviours for their job

All our people have access to an e-learning platform which helps our people develop their skills through training that is accessible from both work and home It offers an extensive programme that can be tailored to the individual's personal development needs – covering induction and core knowledge to operational and leadership skills

We offer a range of training academies, open primarily to internal candidates, with the aim of providing a structured career path and the opportunity to gain external qualifications whilst in their role We also encourage our people to seek career progression within the group During 2012 over 750 people moved into a different position internally

Our pay and reward structure is designed to support the retention of our talented people and more information can be found in the Remuneration Report on pages 44 to 49

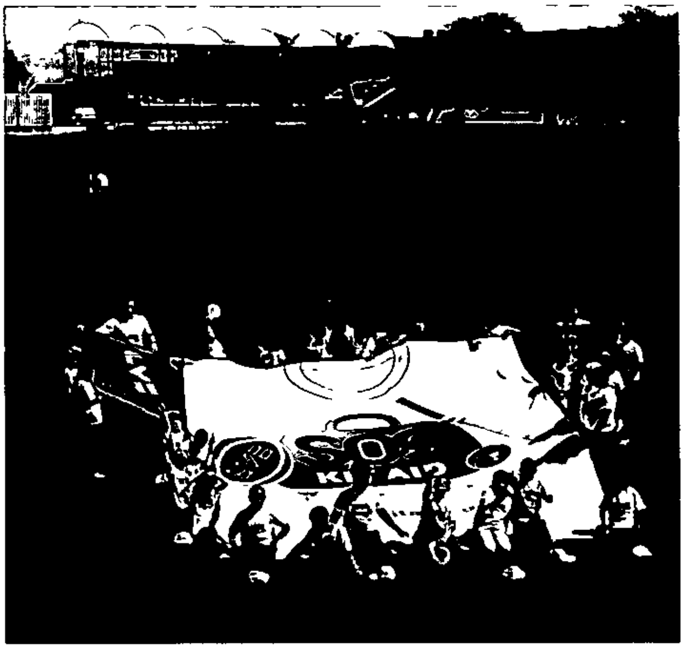
Our environment

Looking after the environment is part of being a responsible business As such we have an environmental strategy and policy to provide a structured approach across all areas of our business to manage, monitor and minimise our environmental impact We're committed to the continuous improvement of our impact on the environment and wherever practical we seek to reduce our footprint

Some of the ways we do this are

- Actively promoting and investing in efficiency measures in our offices,
- Ensuring all offices are 'binless' with recycling facilities in break areas,
- Effectively reducing the use of water by using water savers,
- Minimising waste and promoting recycling wherever possible,
- Placing energy efficiency as a significant factor in the purchase, lease or refurbishment of any LV= office, and
- Monitoring our environmental performance, code of conduct and ethical standards

Our Corporate Social Responsibility Programme



Support for local communities	31%
Employee contributions	28%
Members	9%
Matched giving	11%
Community sponsorship	21%

Giving something back to our local communities and supporting our people's charitable activities is hugely important to us

We take our responsibilities to our members, customers, employees and the wider community seriously and we're passionate about making a positive impact – particularly for those most in need Last year as a business and through our employee efforts we contributed £1 04 million, around 1% of our profits towards this aim

Supporting our local communities

We believe our employees know where our support is needed most – so we put them in the driving seat to look at where we can best offer help

We established a network of 13 Community Committees representing our larger offices Each committee is made up of a small group of LV= employees who meet on a monthly basis to assess requests for help from their local communities and to decide which good causes could benefit from our support

In 2012 the committees distributed £265,000 Their activities ranged from donating a minibus to Huddersfield's Forget Me Not children's hospice, to funding a pantomime for 2,400 needy Bournemouth families They supported a total of 250 local charities, good causes and projects during the year

Last year we invested £55,000 in the LV= schools programme This programme focuses on five schools near our biggest offices, teaching pupils about business, finance and how to prepare themselves for employment Last year 58 volunteers from across LV= helped deliver workshops and mock assessment centres to around 780 students

Our unique approach has not gone unnoticed During 2012 three of our committees were officially recognised with our Huddersfield, Hitchin and Bristol offices winning awards for their outstanding contribution to the community

As well as the work our committees do, we also have a number of long term local sponsorships in place These include LV= KidZone, LV= Streetwise, The Mary Rose Museum in Portsmouth and the LV= Brentwood half marathon and fun run

Sponsorships

Working with national partners means we can broaden our reach and benefit more people with our caring approach, and we invested £222,000 in our pursuit of this

A large number of disadvantaged children can't take part in sport because they don't have the necessary kit or equipment LV= SOS Kit Aid is an innovative scheme which collects and recycles unwanted cricket and rugby kit and distributes it to kids who need it most

Not only does LV= SOS Kit Aid complement our commercial sponsorships in cricket and rugby, but last year it gave 28,000 young people a chance to play these types of sports that they otherwise wouldn't have had

Our support of the Queen Elizabeth II Fields Challenge is helping to safeguard access to outdoor recreational spaces across the UK and by working with them we ve managed to save 13 playing fields near our main offices for future generations

Supporting our people to do good

We believe that by providing our employees with the tools and support to do good things creates a caring culture at the work place We offer a variety of support to recognise their contributions and help them make a difference

Our charity and time matching schemes give our people the tools to go out and help others We offer our people matched funding on money they personally raise, up to £500 and up to two and half days each year to volunteer in the community

We encourage our people to get behind national fundraising events, such as BBC Children in Need and Comic Relief, to which we make corporate donations in appreciation of their efforts

We also provide payroll giving, a mechanism whereby our employees can donate money from their monthly salary to a charity close to their heart We also run a scheme where the pennies from their net pay are collected and donated to a charity near their office

Through these activities our employees raised £296,000 for good causes, which we supported with matched giving and corporate donations of £115,000

Supporting our members

We award grants to members in financial hardship from the Member Support Fund In 2012 these grants helped 43 members and amounted to almost £33,000 We also operate a Member Care Line which offers members medical and legal advice and handles enquiries about the Member Support Fund This helpline was provided at a cost of £42,000

For the first time in 2012 we gave our members the opportunity to select a charity to benefit from our AGM donation £15,000 was donated to Scope which was chosen at random after being nominated by one of our members

28,000
youngsters helped by LV= SOS Kit Aid

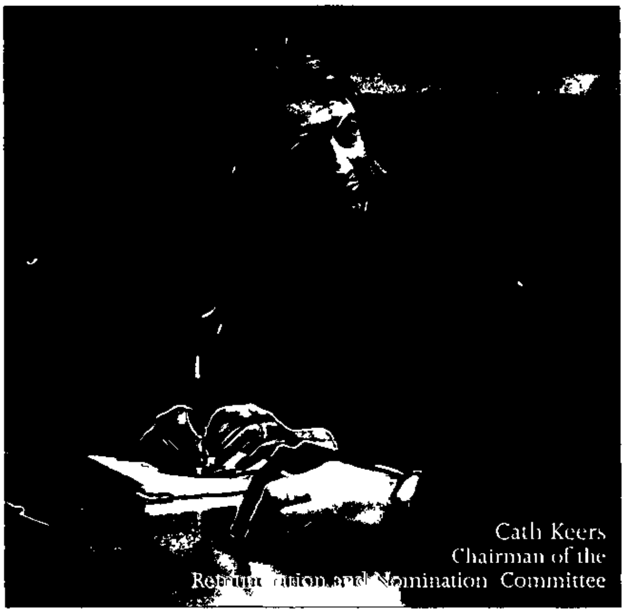
250
charities good causes and projects supported in 2012

91%*
employees who think we do good things in the community

* This score was achieved in an independent employee survey conducted in October 2012

Statements and Reviews | Our Businesses | Risk Management | Corporate Governance | Our Accounts

Directors' Report on Remuneration



Cath Keers
Chairman of the
Remuneration and Nomination Committee

Recent years have seen a marked change in remuneration practices across the financial services sector External regulation has sought to strengthen the link between remuneration and the long-term financial health and stability of firms in our industry Whilst detailed regulation on executive pay in the insurance sector has yet to emerge, the committee has sought to ensure that the way in which we reward the Society's leadership is consistent with members' interests and the long-term health of the Society

To that end, the Remuneration Committee carried out a review during 2012 of our remuneration framework to ensure that it remains consistent with both members' interests and our aspiration to be a "destination employer" This included a review of the structure of our variable pay schemes in the context of evolving best practice among FTSE 250 financial sector companies and others in the mutual sector As a result, we have made changes to the Long Term Incentive Plan (LTIP) and introduced a deferral mechanism into the annual bonus for our most senior employees to ensure that a sufficient portion of their pay is linked to longer-term performance Details of these changes are set out in this report We also set priorities around reviewing the levels of remuneration from the most junior to the most senior employees, and we continue to monitor this

Activities in 2012

In 2012 the committee met four times The matters addressed included

- Reviewing, and recommending to the board, the LTIP for the period 2012-14,
- Recommending the salary, bonus and LTIP awards for the group chief executive, the executive directors and certain key executives,
- Reviewing all incentive schemes in operation across LV=, with particular reference to sales incentives and ensuring the right behaviour towards customers at all times, including the payments which may be earned under the 2010-12 LTIP,
- Continuing to ensure that risk is properly assessed as part of the award of bonuses and that adjustments are made to reflect any breach of agreed risk appetites,
- Determining the impact of and associated actions required from relevant remuneration regulation,
- Reviewing LV='s overall remuneration model to ensure that it continues to meet all of the group's employment objectives while taking account of changing external trends,
- Assessing the impact of the upcoming changes to the governance and reporting of executive pay in listed companies, and determining how the Society will reflect these changes as a matter of good practice in its own governance and reporting, and
- Reviewing the effectiveness of the committee and the continuing appropriateness of its terms of reference

The Remuneration Committee

The responsibilities of the remuneration committee include determining the broad policy for remunerating the executive directors and agreeing the remuneration of each executive director and other senior managers The committee reviews remuneration policy and strategy at least once a year All incentive and bonus schemes are established and monitored by the committee

Members of the committee are provided with regular training and topical briefing sessions on developments and trends in executive remuneration, particularly as this relates to the financial sector

Committee membership

During 2012 the committee members were,

- Cath Keers (who chaired the committee)
- Dennis Holt
- Ian Reynolds (who served until 26 July 2012)
- Mark Austen (who joined the committee from the same date)

Attendance at committee meetings and advisors

The group chief executive is invited to meetings except when his own remuneration is being discussed Other senior employees, such as the group chief risk officer, the human resources director and the group head of reward, regularly provide advice to the committee and normally attend meetings by invitation

New Bridge Street (which is a part of Aon plc) is the committee's independent external advisor During the course of the year, New Bridge Street provided advice to the committee on remuneration levels and structures, and attended meetings at the invitation of the committee During the course of the year, Aon provided other services to the Society, however, the committee considers that adequate structures are in place to ensure the independence of the advice received from New Bridge Street

Seeking the views of members

The committee is keen to hear members' perspective on the Society's remuneration policy and the remuneration decisions which the committee takes on members' behalf To this end, the chairman of the committee conducted a presentation and feedback session to the members' panel immediately before the Society's 2012 AGM, at which a detailed explanation of remuneration policy and its implementation was given and there was an opportunity for members to ask questions We intend to hold a similar session in the future

In addition, the Directors' Remuneration Report is subject to an advisory vote of members at the AGM In 2012, the report was approved with 90% of votes cast being in favour From 2014, two separate votes will be taken one on the Society's remuneration policy for directors, and a second on the implementation of the policy during the prior year This is in line with upcoming changes in legislation on executive pay governance that will apply to listed companies and which the Society, whilst not formally required to do so, proposes to adopt as a matter of good practice

Remuneration policy

Our approach to remuneration policy is designed to support recruitment, motivation and retention, and hence align to our members' best interests Remuneration is considered in the context of the financial services sector and our individual businesses Our objective continues to be to provide total remuneration packages at the relevant mid-market level for good performance (with a significant proportion of total remuneration dependent upon performance) and top quartile remuneration for exceptional performance Our remuneration policy is strongly influenced by good risk management practice to ensure that management is not incentivised to act in a manner that is prejudicial to the long-term interests of members This policy for executive directors is described in more detail below

While we currently remain outside the scope of the FSA's remuneration code, we keep it under regular review and aspire to follow its spirit

In determining the remuneration of the Society's directors, the committee takes into account the pay arrangements across the Society as a whole The committee seeks to ensure that the underlying principles which form the basis for decisions on directors' pay are consistent with those on which reward decisions for all our colleagues are taken

Remuneration policy for non-executive directors

Fees for the non-executive directors are determined by the board, based on the responsibility and time committed to the group's affairs and appropriate market comparisons Individual non-executive directors do not take part in discussions regarding their own fees

No other remuneration is paid apart from these non-pensionable fees, except where we reimburse authorised expenses Non-executive directors' contracts state that either party can give three months' notice of termination

Element of pay	Objective	Award level	Performance criteria	Performance period
Base salary	To attract and retain high performing individuals to lead the society	Our policy is to pay salaries at the mid-market level for satisfactory individual performance, in line with the relevant market for the job.	No performance criteria per se, but the performance of the individual is taken into account when salary levels are reviewed	N/A
Benefits	To operate a competitive benefits and pension structure that provides adequate protection to our employees and aids recruitment and retention	• Car allowance • Medical insurance • Income protection cover (executive level only) • Group product discounts, which are available to all staff and directors on equal terms.	N/A	N/A
Pension*	To provide the facility for competitive and viable retirement income	We operate two pension schemes: a defined benefit pension scheme (DB) and a defined contribution pension scheme (DC): executive directors are eligible to participate in one, depending on their date of joining LV=. Employer contributions paid are: DB scheme – 17.8% of salary DC scheme – up to 14% of salary Alternatively an executive director may choose to receive a cash sum of up to 22% of salary in lieu of pension contributions.	N/A	N/A
Annual bonus	To drive and reward delivery of near-term business objectives	Chief executive max: 110% Board executive directors and other directors max: 80% Around half the maximum is paid for target performance	Evaluation against annual group and divisional financial objectives, risk metrics and a balanced scorecard of personal objectives	1 year performance period Awards may be partly deferred (see below) for up to three further years, during which time they remain linked to ongoing performance
Long-term incentive plan (LTIP)	To drive and reward longer term business objectives, including the value of the society to its members	Chief executive award value: 100% of base salary Board executive directors award value: 75% of base salary Other participants below Board Executive Director: maximum 60%	Growth in Enterprise Value and relative investment performance of the Society	3 year performance period Two thirds of any resulting payment will be deferred for up to two further years, during which time it remains linked to ongoing performance

Executive director's salaries

	w.e.f 1 April 2012	**w.e.f 1 April 2013**
Mike Rogers	£508,000	**£520,700**
Philip Moore	£348,500	**£355,000**
Richard Rowney	£307,500	**£315,000**
John O'Roarke	£282,500	**£290,000**

* With effect from 1 July 2013 we will be closing our final salary scheme to the build up of future benefits. All existing final salary scheme members will have the option to move into our defined contribution pension scheme

Remuneration policy for executive directors

The remuneration of our executive directors comprises salary, an annual performance bonus, participation in LTIP with returns based on group performance, together with a contributory pension and other benefits Bonus and incentive schemes are designed to provide a strong alignment of interest between the individual and the members of the Society Our executive directors are subject to a notice period of 12 months

Salary

Salaries are set taking account of several factors including individual experience, responsibilities, function and sector, along with individual and company performance, they are reviewed (but not necessarily increased) each year In order to provide an external context, the committee reviews a range of benchmarking information on pay levels in organisations of comparable size and complexity to LV=

Group annual performance bonus

Executive directors are eligible to receive an annual non-pensionable performance bonus if they achieve a number of challenging financial, business and personal objectives These are all linked to the achievement of our strategic objectives

For the executive directors, the scheme for 2012 could pay a maximum of 80% of salary (110% in the case of the chief executive) The maximum payment could only be achieved in the case of exceptional individual performance and significant divisional out-performance

Our annual performance bonus scheme rewards other employees in the same way on the basis of group results, divisional results and personal contribution A performance plan is agreed with each executive for the performance year using a balanced scorecard approach, comprising the following goals

- strategic and financial
- customer and member
- risk and compliance
- people

Risk is taken into account when appraising all performance measures and the committee may reduce or cancel any bonus payment if it considers that risk exceeded acceptable levels Progress and achievements are monitored at the half year point and at the end of the year via a formal performance development review In the case of the CEO this is conducted by the chairman of the board with input from the non-executive directors

Bonus deferral

From 2013 onwards (i e the annual bonus paid in respect of 2012 performance), part of an executive's annual bonus may be required to be deferred How much deferral is required is determined by the overall balance of the total remuneration package and is designed so that we are in line with FSAs guidelines on deferred remuneration Whilst the Society does not fall within the scope of these regulations, it seeks to adopt these principles as a matter of best practice

In general, the committee will ensure that at least 40% of the variable remuneration paid to any senior employee (including executive directors) is delivered in long-term pay If this ratio is not met, then a portion of the annual bonus payment for that year will be deferred For employees whose variable remuneration is £500,000 or more, the requirement will be that 60% be in long-term pay

Any amount deferred will be paid in equal parts over the following three years During the deferral period, the value of deferred amounts will be tied to the value of the with-profits fund, thereby creating a link to ongoing performance

Long term incentive plan (LTIP)

The Society operates a long-term incentive plan (LTIP) for senior employees, which is designed to ensure alignment between reward and the long-term interests of our members Each LTIP scheme runs for a three year period, with a new scheme commencing on 1 January each year

It is the role of the committee to approve the structure of each year's LTIP, ensuring that it is appropriately designed so as to provide appropriate incentives to individuals to contribute towards the achievement of the Society's objectives and, at the maturity of each scheme, to ensure that outcomes have not been inappropriately influenced by taking risks outside the corporate risk appetite

The LTIP is designed to ensure it rewards performance in a manner closely aligned to members' interests This means payment reflects our medium and long-term targets to grow Enterprise Value, which is our estimate of the market value of the group and is the benchmark by which we measure our long-term performance For the purposes of the LTIP, the Enterprise Value of the group is assessed with reference to clearly defined valuation bases These valuation bases are reviewed every three years by independent advisers For any LTIP payments to be made, Enterprise Value must grow at a minimum stipulated annual growth rate over each year of the scheme, taking into account the nature of the risks which the group undertakes Payments are made after review and approved by the Remuneration Committee

Membership of the LTIP is by invitation of the board and restricted to those few individuals who, by their roles and position within the group, are best placed to influence or directly contribute to our longer-term growth Individuals are granted an amount ('the award') at the date of joining the scheme, which is calculated as a percentage of their salary (up to a maximum of 100% in the case of the group chief executive)

Board remuneration – audited

	Annual remuneration (£,000)					Total remuneration (£,000)			
	Salary	Bonus	Deferred bonus	Other benefits	Total 2012	Total 2011	LTIP 2010-12	Total 2012	Total 2011
Mike Rogers[1]	**505**	**427**	**132**	**127**	**1,191**	1,131	1,431	**2,622**	2,177
Philip Moore[1]	**346**	**208**	**52**	**55**	**661**	609	732	**1,393**	609
Richard Rowney[1]	**306**	**240**	–	**51**	**597**	568	585	**1,182**	943
John O Roarke[1&2]	**281**	**220**	–	**45**	**546**	54	–	**546**	314
Dennis Holt	**153**	–	–	–	**153**	150	n/a	**153**	150
Mark Austen	**72**	–	–	–	**72**	68	n/a	**72**	68
John Edwards	**62**	–	–	–	**62**	58	n/a	**62**	58
Cath Keers	**61**	–	–	–	**61**	57	n/a	**61**	57
Ian Reynolds[3]	**60**	–	–	–	**60**	64	n/a	**60**	64
Caroline Burton[4]	**56**	–	–	–	**56**	15	n/a	**56**	15
James Dean[5]	**22**	–	–	–	**22**	–	n/a	**22**	–
Gill Nott[6]	–	–	–	–	–	28	n/a	–	28
	1,924	**1,095**	**184**	**278**	**3,481**	2,802	2,748	**6,229**	4,483

1 Other benefits includes payments in lieu of pension contributions (Mike Rogers £111 000 Philip Moore £41 000 Richard Rowney £37 000 John O Roarke £31 000)
2 Appointed 23 November 2011
3 Resigned 31 October 2012
4 Appointed 9 November 2011
5 Appointed 26 July 2012
6 Resigned 26 May 2011

Long Term Incentive Plan summary of awards and amounts vested – audited

	Award	Unvested awards at 1 January 2012 (1)	Awards made in the year (1)	Additional value on vesting of 2010-2012 scheme (2)	To be paid in respect of 2010-2012 scheme (2)	Unvested awards at 31 December 2012 (3)
Mike Rogers	2010-12	**477,000**	–	**954,000**	**(1,431,000)**	–
	2011-13	**477,000**	–	–	–	**477,000**
	2012-14	–	**495,000**	–	–	**495,000**
Philip Moore	2010-12	**244,000**	–	**488,000**	**(732,000)**	–
	2011-13	**244,000**	–	–	–	**244,000**
	2012-14	–	**255,000**	–	–	**255,000**
Richard Rowney	2010-12	**195,000**	–	**390,000**	**(585,000)**	–
	2011-13	**212,000**	–	–	–	**212,000**
	2012-14	–	**225,000**	–	–	**225,000**

1 Unvested awards are shown at the base award level Unvested awards at 1 January 2012 are in respect of awards granted in 2010 and 2011
2 For the 2010-2012 LTIP scheme growth in Enterprise Value and investment performance both exceeded the "above benchmark targets and accordingly the amounts paid to participating employees were at the maximum level (i e in aggregate three times the base award)
3 Unvested awards at 31 December 2012 are in respect of awards granted in 2011 and 2012
4 John O Roarke did not participate in the LTIP schemes summarised above

The amount paid depends on the group's performance against our Enterprise Value targets and also on investment performance, with a maximum achievable payout of three times the award In determining whether Enterprise Value targets have been achieved, the Remuneration Committee may, where appropriate, make positive or negative adjustments for the financial impacts of any management actions which affect the calculation of the Enterprise Value, to ensure that the calculation is fully aligned to the interest of members For some LTIP scheme participants, a proportion of any payment is linked to the group's investment performance For this portion to produce a maximum payment, an average outperformance of the relevant benchmark of at least 0 6% per annum must be achieved

During the course of 2012, the committee made a number of changes to the structure of the LTIP which are intended to strengthen the alignment with members' interests and reinforce the link to the Society's underlying financial strength For the 2013 cycle, the following changes will apply

- No payment will be made unless a mutual bonus is also paid in that year (any amounts earned in a year in which no mutual bonus is paid would be deferred until such time as a bonus was paid),
- No payment will be made unless the Society is operating at least at a threshold level of capital adequacy in that year, and
- For senior participants in the LTIP (including the executive directors) payment of any resulting award will be made one third after the three year period, one third after a further year of deferral and the final third after two years further deferral, the value of any deferral will be directly linked during the deferral period to the value of the Society's with-profits funds

Additionally from 2013 onwards, the maximum payout under the LTIP scheme will reduce from three times the award value to two times

Neither the annual bonus nor the LTIP are contractual entitlements of those potentially eligible to participate in them

Both annual performance bonuses paid and/or deferred and LTIP payments are subject to claw-back in the event of any material misstatement (including where significant losses subsequently emerge which were not recorded at the time) or gross misconduct

Pensions and other benefits

Since 1 January 2010 we have provided a defined contribution pension scheme for new employees where we contribute twice the amount contributed by each employee within a range of employee contributions from a minimum of 3% to a maximum of 7% of salary Previously we offered a final salary scheme, although now closed to new members, existing members continued to accrue benefits in this scheme

With effect from 1 July 2013 we will be closing our final salary scheme to the build up of future benefits All existing final salary scheme members will have the option to move into our defined contribution pension scheme from that date

Remuneration during 2012

The remuneration of individual directors, including that of the chairman and highest paid director, is detailed on page 48

Annual bonus 2012

During 2012, the group significantly exceeded many of its financial performance targets, whilst continuing to grow the business and delivering on our major promises and commitments to our members The committee determined that the bonuses for the executive directors should therefore be at 110% for the chief executive, 75% for the finance director, 78% for the MD, Life Insurance, 78% for the MD, General Insurance

LTIP payments in 2012

The LTIP scheme which started on 1 January 2010 required annual growth in total of the business units Enterprise Value of between 9% and 20% per annum over the three year period ending 31 December 2012 For some LTIP scheme participants an above benchmark return on investment performance of 60 basis points per annum was also required It has been determined that these hurdles were exceeded and accordingly a maximum payout of £7 5 million (excluding employer's national insurance contributions) has been distributed among 47 participants

LTIP cycles currently in progress

- The schemes which started on 1 January 2011 and 2012 require a minimum of 9% per annum growth in the Enterprise Value of the business units to be achieved by 31 December 2013 and 2014 respectively For some participants, these schemes also require an above benchmark return on investment performance of 60 basis points per annum These schemes are still open and have 56 and 79 remaining participants respectively
- For the schemes which started on 1 January 2011 and 1 January 2012, if the performance conditions are met these would pay out between £2 2 million and £8 8 million and £2 8 million and £11 3 million respectively, depending on performance
- The amount charged to comprehensive income in 2012 in respect off all open LTIP schemes was £9 6 million (2011 £7 3 million)
- The estimated costs of any expected awards under the schemes are charged as expenses in equal instalments over the three year performance period concerned

Long Term Incentive Plans – performance of current schemes

The tables below summarise the performance targets of the LTIP Scheme awards granted in 2010, 2011 and 2012 together with performance from the start of each Scheme to 31 December 2012

Performance targets

Level of award	Enterprise Value Growth (1)	Relative Investment Performance (2)
Minimum (75% of base award)	**9%**	**0 basis points**
Maximum (300% of base award)	**20%**	**≥60 basis points**

Cumulative performance versus target

LTIP Scheme	Enterprise Value Growth (3)	Investment Performance (4)
2010-2012 LTIP Scheme (started 1 January 2010)	**29 5%**	**+117 basis points**
2011-2013 LTIP Scheme (started 1 January 2011)	**16 2%**	**+50 basis points**
2012-2014 LTIP Scheme (started 1 January 2012)	**22 1%**	**+142 basis points**

For Scheme participants measured on investment performance, 75% of their initial award is based on Enterprise Value performance and 25% on Relative Investment Performance

1 Annualised growth in SBU Enterprise Value
2 Annualised investment performance return relative to benchmark return
3 Annualised growth in Enterprise Value from start of Scheme to 31 December 2012
4 Annualised performance return relative to benchmark from start of Scheme to 31 December 2012

Directors' loans

As at 31 December 2012 and 31 December 2011 there were no loans outstanding from directors

The directors approved the Directors Report on Remuneration on 27 March 2013

Cath Keers
Chairman of the Remuneration Committee

Glossary

ABI Association of British Insurers

AFS Association of Friendly Societies

Annual Premium Equivalent (APE) A measure commonly used to calculate and compare the size of a life company It is calculated by adding the total annual premiums received and 10% of all single premiums received in the year

Asset shares Asset shares reflect the amount of money paid into with-profits policies by way of premiums and investment returns, less the costs of administering those policies

Association of Financial Mutuals (AFM) The trade body that represents mutual insurers, Friendly Societies and other financial mutuals in the UK It was formed in January 2010 after a merger of the Association of Friendly Societies and the Association of Mutual Insurers

Capital resources The amount of capital that we have to run our business

Enterprise Value As LV= is not quoted on the stockmarket, Enterprise Value is our measure of the market value of the business Any rise or fall in Enterprise Value will also tell us if we are growing member value A complex formula is used to calculate our Enterprise Value, and the figure is independently verified every three years

Friendly Society: Friendly Societies were set up in the 19th century to help and encourage underprivileged people to improve their financial wellbeing As they are mutuals, Friendly Societies are owned by members rather than shareholders

FSA: The Financial Services Authority regulates the financial services industry in the UK

FTSE. FTSE is an independent company that provides indices to measure how stockmarkets and other financial markets perform In the UK, the FTSE 100 index is widely used by the media to report on the valuation of the largest 100 quoted companies on the UK Stock Exchange

Heritage business. Principally, the Society's with-profit policies, together with the policies acquired from RNPFN

GWP Gross written premiums

ICA Individual capital assessment is the process by which the Financial Services Authority (FSA) requires insurance companies to make an assessment of the regulated company's own capital requirements, which is then reviewed and agreed by the FSA

IFRS International Financial Reporting Standards are used to ensure a company's reported accounts are prepared to common standards across the world

ILAG Investment and Life Assurance Group

Industrial branch Part of our heritage business and typically contains small premium whole of life and endowment policies

Mutual A business that is owned by its members rather than by shareholders

Mutual bonus. A discretionary enhancement to asset shares to share the results of the group s performance

OEICs Open-Ended Investment Companies are investment funds similar to investment trusts They are open-ended because they can take money from new investors at any time Equally they can pay back investors whenever the investor chooses OEICs often adopt an umbrella structure where the investor can get access through the umbrella fund to a number of sub-funds which invest with different objectives

Ordinary branch Part of our heritage business and typically consists of traditional with-profits endowments, whole of life policies, annuities and pensions

Pension annuity An annuity uses the proceeds of a pension fund to provide an income for a fixed term or the rest of your life

Periodic payment orders (PPOs) An annuity style award paid to claimants instead of a lump sum, where indexed payments can be varied to meet likely future changes in circumstance This transfers mortality and investment risk from the claimant to the insurer

PHI· Permanent Health Insurance is an insurance policy paying benefits to policyholders who are incapacitated and hence unable to work due to illness or accident

Protection A policy providing a cash sum on the death or critical illness of the life assured

PVIF Present value of acquired in-force business occurs when a life insurance company makes an acquisition Part of the purchase price represents the value of the insurance contracts in the target company This is in effect, the present value of the policies acquired

RCM: Risk capital margin is the additional capital a firm would need to hold to cover the effects of a number of 'What if ?' scenarios that have been prescribed by the FSA These scenarios assess the capital implications from combined movements in financial markets (equity, property, credit spreads, interest rates) and persistency of the business The RCM is the capital required to cover the worst case scenario

Retail Distribution Review (RDR) A fundamental review by the FSA designed to help address insufficient trust and confidence in financial services products and services In particular, it is intended to drive increased professionalism in the tied and independent financial advice areas and will change the way that financial advice is organised and paid for

RNPFN. Royal National Pension Fund For Nurses

Risk appetite. The amount of risk that a business is prepared to accept or keep when carrying out its everyday activities

Self Invested Personal Pension (SIPP)· Unlike normal personal pension plans, where the pension company limits your choice of investments to those that it manages, SIPPs allow investors the opportunity to make their own investment decisions

SME. Small, Medium Enterprises – within the commercial line of the general insurance business

Solvency II. An EU-wide project that sets out to provide a comprehensive new framework for insurance supervision and regulation This aims to strengthen protection for policyholders by ensuring that companies allocate enough capital to cover all the risks in their business

Strategic business unit (SBU) LV= is made up of two business units (Life and General Insurance), each of which focuses on profitably delivering a specific part of our overall group business plan

Threadneedle Asset Management (TAM) A leading international investment manager with a strong track record of outperformance across asset classes

TCF Treating Customers Fairly is an industry-wide initiative designed to ensure financial providers meet basic principles of product information, suitability and performance

UK Corporate Governance Code· The Code sets out standards of good practice for listed companies It covers, amongst other things, the board composition and its accountability and relations with business owners Mutual organisations such as LV= do not have to adhere to the Code, but we choose to comply with the Annotated Code as published by the AFM as we believe it is good business practice to do so

Unallocated divisible surplus (UDS) The amounts that have yet to be formally declared as bonuses for participating policyholders together with the free assets of the group

Underlying operating profit The operating profit before one-off items such as basis and methodology changes, short-term investment fluctuations and amortisation of intangibles

With-profits fund An investment fund where we combine all of our with-profits investors' money and manage it on their behalf The fund normally invests in UK and overseas shares, fixed interest securities including Government stocks and bonds, property, cash, and our own business activities We regularly monitor where we invest the fund to take account of future liabilities

Our Accounts

Independent auditors' report to the members of Liverpool Victoria Friendly Society Limited

We have audited the financial statements of Liverpool Victoria Friendly Society Limited for the year ended 31 December 2012 which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Cash Flows and the related notes for the Society and the Group 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 the Board of Directors and auditors

As explained more fully in the Responsibilities of the Board of Directors for the financial statements set out on page 39, the Board of Directors is responsible for preparing financial statements which give a true and fair view The Society has also chosen to comply with the Annotated UK Corporate Governance Code specified by the Association of Financial Mutuals 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 Society's members as a body in accordance with the Friendly Societies Act 1992 and the Regulations made under it 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 Society's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the Board of Directors, and the overall presentation of the financial statements In addition, we read all the financial and non-financial information in the Report and Financial Statements 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, in accordance with IFRSs as adopted by the European Union, of the state of the Society's and the Group's affairs as at 31 December 2012 and of the income and expenditure and cash flows of the Society and the Group for the year then ended, and
- have been properly prepared in accordance with the Friendly Societies Act 1992

Opinion on other matters prescribed by the Friendly Societies Act 1992

In our opinion the Directors' Report has been prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it, and the information given therein is consistent with the financial statements for the financial year

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Friendly Societies Act 1992 requires us to report to you if, in our opinion

- proper accounting records have not been kept, or
- the financial statements are not in agreement with the accounting records, or
- we have not received all the information and explanations and access to documents that we require for our audit

In accordance with our instructions from the Society we review whether the Corporate Governance Statement reflects the Society's compliance with the eight provisions of the Annotated UK Corporate Governance Code specified by the Association of Financial Mutuals We have nothing to report in respect of this review

David Roper
Senior Statutory Auditor
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Bristol
27 March 2013

Statement of Comprehensive Income

Year ended 31 December 2012

		Group		Society	
		2012	2011 Restated see Note 1	**2012**	2011
	Notes	**£m**	£m	**£m**	£m
Gross earned premiums	4	**2,446 2**	2,196 5	**959 1**	862 8
Premiums ceded to reinsurers	4	**(108 8)**	(93 0)	**(75 6)**	(99 7)
Net earned premiums	4	**2,337 4**	2,103 5	**883 5**	763 1
Fee and commission income	6	**16 5**	18 5	**6 6**	5 2
Investment income	7	**320 2**	261 4	**337 0**	284 9
Net gains on investments	8	**374 7**	425 4	**214 1**	372 9
Other income	9	**41 7**	51 0	**5 9**	19 1
Total income		**3,090 5**	2,859 8	**1,447 1**	1,445 2
Gross benefits and claims	10	**(1,819 3)**	(1,669 3)	**(646 6)**	(657 3)
Claims ceded to reinsurers	10	**110 8**	86 4	**61 8**	102 4
Net benefits and claims	10	**(1,708 5)**	(1,582 9)	**(584 8)**	(554 9)
Gross change in long-term contract liabilities	22	**(711 3)**	(771 6)	**(714 8)**	(773 4)
Change in long-term contract liabilities ceded to reinsurers	22	**74 4**	96 0	**74 4**	7 1
Net change in contract liabilities	22	**(636 9)**	(675 6)	**(640 4)**	(766 3)
Finance costs	11	**(0 5)**	(0 5)	**-**	-
Investment return allocated to external unit holders		**(32 9)**	2 1	**-**	-
Other operating and administrative expenses	12	**(608 5)**	(619 8)	**(218 6)**	(171 7)
Other expenses		**(641 9)**	(618 2)	**(218 6)**	(171 7)
Total benefits, claims and expenses		**(2,987 3)**	(2,876 7)	**(1,443 8)**	(1,492 9)
Profit/(loss) before tax and mutual bonus		**103 2**	(16 9)	**3 3**	(47 7)
Mutual bonus	14	**(20 9)**	(18 6)	**(20 9)**	(18 6)
Income tax expense	34	**(34 3)**	(42 2)	**(13 4)**	(26 9)
Pension scheme actuarial (losses)/gains net of tax	39	**(145 5)**	69 7	**(145 5)**	69 7
Transfer from the Unallocated divisible surplus	46	**97 5**	8 0	**176 5**	23 5
Total comprehensive income for the year		**-**	-	**-**	-

As a Friendly Society, all net earnings are for the benefit of participating policyholders and are carried forward within the Unallocated divisible surplus Accordingly, there is no profit for the year shown in the Statement of Comprehensive Income

The Group and the Society have not presented a Statement of Changes in Equity as there are no equity holders in either the Group or Society as the Society is a mutual organisation

Statement of Financial Position
as at 31 December 2012

		Group		Society	
		2012	2011 Restated see Note 1	2012	2011 Restated see Note 1
	Notes	£m	£m	£m	£m
Assets					
Intangible assets	26	**251 9**	261 5	–	4 6
Deferred acquisition costs	23	**100 1**	94 7	–	–
Pension benefit asset	39	–	108 1	–	108 1
Property and equipment	27	**23 9**	20 6	**6 9**	5 0
Investment properties	28	**164 7**	219 9	**131 7**	151 4
Investments in group undertakings	29	–	–	**902 3**	957 6
Corporation tax asset	35	–	–	**2 0**	–
Deferred tax asset	36	**14 2**	31 0	**13 0**	17 7
Prepayments and accrued income	31	**106 6**	61 3	**64 3**	48 1
Financial assets					
– Fair value through income	15	**9,484 1**	8,020 3	**7,058 9**	6,016 1
– Derivative financial instruments	16	**70 8**	143 8	**68 5**	143 8
Loans and other receivables	19	**103 0**	116 0	**128 6**	154 9
Reinsurance assets	24	**447 2**	336 9	**297 4**	223 0
Insurance receivables	30	**227 3**	216 5	**12 6**	10 2
Cash and cash equivalents		**436 6**	719 1	**123 3**	283 4
Total assets		**11,430 4**	10,349 7	**8,809 5**	8,123 9
Liabilities					
Unallocated divisible surplus	46	**860 9**	958 4	**878 6**	1,055 1
Insurance contract liabilities	21	**8,657 4**	7,748 0	**6,603 3**	5,946 2
Investment contract liabilities	17	**959 3**	800 9	**959 3**	800 9
Net asset value attributable to external unit holders		**503 9**	429 1	–	–
Pension benefit obligation	39	**10 2**	1 2	**10 2**	1 2
Provisions	40	**66 0**	55 5	**63 1**	52 0
Corporation tax liability	37	**7 6**	28 4	–	13 0
Financial liabilities					
– Derivative financial instruments	16	**51 2**	3 8	**51.2**	3 8
– Other financial liabilities	20	**75 5**	77 2	**81 4**	72 7
Insurance payables	32	**44 7**	41 6	**26 2**	31 6
Trade and other payables	33	**193 7**	205 6	**136 2**	147 4
Total liabilities		**11,430 4**	10,349 7	**8,809 5**	8,123 9

The financial statements on page 55 to 125 were approved by the Board of Directors on 27 March 2013 and signed on its behalf by

R S Small
Secretary

Statement of Cash Flows
Year ended 31 December 2012

		Group		Society	
		2012	2011 Restated see Note 1	2012	2011 Restated see Note 1
	Notes	£m	£m	£m	£m
Cash and cash equivalents at 1 January		**719 1**	547 4	**283 4**	289 0
Cash flows arising from					
Operating activities					
Cash generated from operating activities	50	**411 8**	414 4	**272 5**	140 5
Net increase in investments held at fair value through income		**(985 0)**	(582 9)	**(720 6)**	(497 2)
Purchase of investment properties		**(0 2)**	(12 5)	**(0 2)**	(2 9)
Proceeds from sale of investment properties		**54 2**	106 1	**18 7**	96 2
Dividend income received		**96 1**	119 5	**165 2**	152 0
Interest and other income received		**180 4**	137 0	**150 9**	123 4
Rental income on investment properties		**6 1**	7 3	**6 5**	7 1
Finance cost paid	11	**(0 5)**	(0 5)	**–**	–
Income tax paid		**(38 3)**	(13 6)	**(23 7)**	(13 6)
Net cash flows (used in)/generated from operating activities		**(275 4)**	174 8	**(130 7)**	5 5
Investing activities					
Proceeds from sale of property and equipment		**(0 1)**	–	**–**	–
Increase in investment in group undertakings		**–**	–	**(45 1)**	(15 2)
Redemption of loans to subsidiaries		**–**	–	**13 0**	–
Repayment in long-term loan from subsidiary		**–**	–	**5 8**	4 5
Purchase of property and equipment	27	**(7 0)**	(3 1)	**(3 1)**	(0 4)
Net cash flows (used in)/generated from investing activities		**(7 1)**	(3 1)	**(29 4)**	(11 1)
Net (decrease)/increase in cash and cash equivalents		**(282 5)**	171 7	**(160 1)**	(5 6)
Cash and cash equivalents at 31 December		**436 6**	719 1	**123 3**	283 4
Cash and cash equivalents comprise					
Bank balances		**98 0**	156 9	**22 4**	107 5
Short-term bank deposits		**338 6**	562 2	**100 9**	175 9
		436 6	719 1	**123 3**	283 4

The Group classifies the cash flows for the acquisition and disposal of financial assets as operating cash flows, as the purchases are funded from the cash flows associated with the origination of insurance and investment contracts

Notes to the Financial Statements
31 December 2012

Significant accounting policies
This section describes the LV= Group's significant accounting policies and accounting estimates that relate to the financial statements and notes as a whole. If an accounting policy or an accounting estimate relates to a specific note, the applicable accounting policy and/or accounting estimate is contained within the relevant note.

1. Significant accounting policies

1 1 Basis of presentation
The Group financial statements consolidate the results of the Society and its subsidiary companies The Group's and Society's financial statements conform to International Financial Reporting Standards (IFRS) and interpretations issued by the IFRS Interpretations Committee (IFRIC) as published by the International Accounting Standards Board and adopted by the European Union In addition the Society's financial statements comply with the Friendly Societies (Accounts & Related Provisions) Regulations 1994 (the Regulations)

In accordance with IFRS 4 on Insurance Contracts, the Group has applied existing accounting practices for insurance contracts and participating investment contracts modified as appropriate to comply with the IFRS framework and applicable standards Further details are given in accounting policy 1 3b below

Insurance contracts are accounted for in accordance with the Statement of Recommended Practice issued by the Association of British Insurers in December 2005, and amended in December 2006 In certain businesses, the accounting policies or accounting estimates have been changed, to measure designated insurance liabilities using current market interest rates and allowing for other changes to regulatory reporting practices The Group measures the liability on insurance and with-profit contracts in line with the 'realistic' reporting regime of the Financial Services Authority (FSA) More detail on the valuation of insurance and investment contracts is given in the accounting policies disclosed within Notes 17 and 21

The financial statements have been prepared under the historical cost convention as modified by the revaluation of investment properties and financial assets and liabilities (including derivatives) at fair value through income

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below These policies have been consistently applied to all years presented, unless otherwise stated

After making enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future The Group therefore continues to adopt the going concern basis in preparing its consolidated financial statements

Restatements
The Statement of Comprehensive Income has been restated to reclassify interest on loans secured on residential property from Fee and commission income to Investment income

The Statement of Financial Position and Statement of Cash Flows have been restated to gross up Bank balances and Other financial liabilities to reflect cash collateral received

1.2 Significant accounting estimates and judgements
The preparation of financial statements in accordance with IFRS requires the use of estimates It also requires management to exercise judgement in applying the accounting policies The key areas involving a high degree of judgement or complexity, or areas where assumptions are significant to the financial statements are highlighted under the relevant note

Significant accounting estimates and judgements are disclosed in

- Fair value of financial assets (Note 15)
- Insurance contract liabilities (Note 21)
- Goodwill and intangible assets (Note 26)
- Pension benefit asset/(obligation) (Note 39)

1 3 Accounting policies
a Consolidation
Subsidiaries
Subsidiaries are all entities, including Open Ended Investment Companies (OEICs), over which the Group (directly or indirectly) has the power to govern the financial and operating policies generally accompanying 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 Subsidiaries are fully consolidated from the date on which control is transferred to the Group using uniform accounting policies consistently applied across the Group They are excluded from consolidation from the date on which control ceases

The Group uses the purchase method of accounting to account for the acquisition of subsidiaries Accordingly, the cost of an acquisition is measured as the fair value of the cash or other assets given, equity instruments issued and liabilities incurred or assumed at the date control passes Identifiable assets acquired, liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the Statement of Comprehensive Income for the period

Intra-group transactions, balances and unrealised gains on intra-group transactions are eliminated on consolidation Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred

Where the Group invests in specialised investment vehicles (such as OEICs) and owns greater than 50% of the unit shareholding, they are consolidated The interests of other parties in these vehicles will be classified as liabilities and appear as 'Net asset value attributable to external unit holders because they are puttable instruments The external unit holders' share of the net investment return on the OEICs is charged or credited to the Statement of Comprehensive Income as investment return allocated to external unit holders

Details of the Society's principal subsidiaries are given in Note 43

Notes to the Financial Statements continued

31 December 2012

1. Significant accounting policies (continued)

Associates and joint ventures in property holding companies
The Group invests in associate companies and jointly controlled entities that hold investment properties, with holdings ranging between 25% and 99%

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights

The investments in associates and the Group's interests in jointly controlled entities have not been consolidated under the equity method but are designated as investments at fair value through income under UK unlisted investments in accordance with the exemptions permitted under IAS 28 and IAS 31 applicable to investment-linked insurance funds

b Contract classification
The Group issues contracts that transfer insurance risk, financial risk or both

Insurance contracts are those contracts that 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 that are at least 10% more than the benefits payable if the insured event did not occur

Investment contracts are those contracts that transfer financial risk with no significant insurance risk

All participating contracts have been classified as participating insurance contracts as these contracts entitle the holder to receive, as a supplement to guaranteed benefits, additional benefits or bonuses

- that are likely to be a significant portion of the total contractual benefits,
- whose amount or timing is contractually at the discretion of the Group, and
- that are contractually based on
  i) the performance of a specified pool of contracts or a specified type of contract,
  ii) realised and/or unrealised investment returns on a specified pool of assets held by the fund, or
  iii) the unallocated surplus of the fund that issues the contract

c Foreign currencies
Monetary assets and liabilities denominated in foreign currencies are translated to sterling at rates of exchange ruling at the end of the year Purchases and sales of investments denominated in foreign currencies are translated at the rates prevailing at the dates of the transactions Exchange gains and losses are dealt with in that part of the Statement of Comprehensive Income in which the underlying transaction is reported

d. Financial assets and liabilities
Recognition
The Group classifies its financial assets and liabilities upon initial recognition into the following categories
- Financial assets and liabilities at fair value through income
- Derivative financial instruments
- Loans and receivables
- Other financial liabilities

The accounting policy for each type of financial asset or liability is included within the relevant note for the category

Derecognition
A financial asset is derecognised when
- the rights to receive cash flows from the asset have expired, or
- the Group has transferred its rights to receive cash flows from the asset and has
  - transferred the risks and rewards of the asset, or
  - has transferred control of the asset

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires

e Liability adequacy testing
Insurance and participating investment contract liabilities
At each reporting date, an assessment is made of whether the recognised long-term contract liabilities are adequate, using current estimates of future cash flows If that assessment shows that the carrying amount of the liabilities (less related assets) is insufficient in light of the estimated future cash flows, the deficiency is recognised in the Statement of Comprehensive Income by setting up an additional liability

General Insurance
At each Statement of Financial Position date liability adequacy tests are performed to ensure the adequacy of insurance contract liabilities, net of related deferred acquisition costs In performing these tests current best estimates of future contractual cash flows and claims handling and administration expenses as well as investment income from the assets backing such liabilities are used Any deficiency is immediately charged to the Statement of Comprehensive Income initially by writing off deferred acquisition costs and by subsequently establishing an unexpired risk provision Any deferred acquisition cost written off as a result of this test cannot subsequently be reinstated

f Impairment of non-financial assets
Assets that have an indefinite useful life, for example goodwill, are not subject to amortisation and are tested annually for impairment Assets that are subject to amortisation or depreciation 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 recoverable amount The recoverable amount is the higher of an asset's fair value less costs to sell and value in use For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units)

Non-financial assets, other than goodwill, that suffered impairment are reviewed for possible reversal of the impairment at each reporting date

g Cash and cash equivalents
Cash and cash equivalents comprise cash at bank and in hand, and short-term deposits with an original maturity of three months or less

For the purpose of the consolidated cash flow statement, cash and cash equivalents are as defined above but are shown net of outstanding bank overdrafts

Notes to the Financial Statements continued

31 December 2012

1. Significant accounting policies (continued)

1 4 Changes and future developments in accounting policies
(i) New and amended standards adopted by the Group
There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on or after 1 January 2012, that would be expected to have a material impact on the Group

(ii) New standards and interpretations not yet adopted
A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2013, and have not been applied in preparing these consolidated financial statements None of these is expected to have a significant effect on the consolidated financial statements of the Group, except the following set out below

Amendment to IAS 1, 'Financial statement presentation' regarding other comprehensive income The main change resulting from these amendments is a requirement for entities to group items presented in 'other comprehensive income' (OCI) on the basis of whether they are potentially reclassifiable to profit or loss subsequently (reclassification adjustments) The amendments do not address which items are presented in OCI

IFRS 13, 'Fair value measurement', aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs The requirements, which are largely aligned between IFRSs and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs or US GAAP

IAS 19, 'Employee benefits', was amended in June 2011 The impact on the Society will be as follows to immediately recognise all past service costs, and to replace interest cost and expected return on plan assets with a net interest amount that is calculated by applying the discount rate to the net defined benefit liability (asset) The Group is yet to assess the full impact of the amendments

IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities IFRS 9 was issued in November 2009 and October 2010 It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments IFRS 9 requires financial assets to be classified into two measurement categories those measured as at fair value and those measured at amortised cost The determination is made at initial recognition The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument For financial liabilities, the standard retains most of the IAS 39 requirements The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch The Group is yet to assess IFRS 9 s full impact and intends to adopt IFRS 9 no later than the accounting period beginning on or after 1 January 2015, subject to endorsement by the EU The Group will also consider the impact of the remaining phases of IFRS 9 when completed by the Board

IFRS 10, 'Consolidated financial statements', builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company The standard provides additional guidance to assist in the determination of control where this is difficult to assess The Group is yet to assess IFRS 10's full impact and intends to adopt IFRS 10 no later than the accounting period beginning on or after 1 January 2013, subject to endorsement by the EU

IFRS 12, 'Disclosures of interests in other entities', includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles The Group is yet to assess IFRS 12's full impact and intends to adopt IFRS 12 no later than the accounting period beginning on or after 1 January 2013, subject to endorsement by the EU

IAS 27 (revised) 'Separate financial statements', issued in May 2011 This standard includes the provisions on separate financial statements that are left after the control provisions of IAS 27 have been included in the new IFRS 10 The Group is yet to assess the full impact of the amendments and intends to adopt the amended IAS 27 no later than the accounting period beginning on or after 1 January 2013

IAS 28 (revised) 'Investments in associates and joint ventures', issued in May 2011 This standard includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11 The Group is yet to assess the full impact of the amendments and intends to adopt the amended IAS 28 no later than the accounting period beginning on or after 1 January 2013

IFRS 11 'Joint arrangements', issued in May 2011 This standard provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form There are two types of joint arrangements joint operations and joint ventures Joint operations arise where a joint operator has rights to the assets and obligations relating to the arrangement and hence accounts for its interest in assets, liabilities, revenue and expenses Joint ventures arise where the joint operator has rights to the net assets of the arrangement and hence equity accounts for its interest Proportional consolidation of joint ventures is no longer allowed The Group is yet to assess IFRS 11 s full impact and intends to adopt IFRS 11 no later than the accounting period beginning on or after 1 January 2013

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Group

Notes to the Financial Statements continued

31 December 2012

Capital and risk management

This section details the capital and risk management approach of the Society and Group The Group seeks to create value for its members by maintaining an appropriate balance between the capital available to support risk and the level and type of risk it takes on in order to achieve returns. The risk appetite for each type of principal risk is set based on the amount necessary to meet the FSA's capital requirements

2. Capital management

The Society retains capital within its Unallocated divisible surplus to meet the key objectives

(i) To ensure financial stability and to support the risks it takes on as part of its business,
(ii) To enable the Group's strategy to be implemented,
(iii) To give confidence to policyholders and other stakeholders who have relationships with the Group, and
(iv) To comply with capital requirements imposed by its UK regulator, the FSA

At least annually, these objectives are reviewed and benchmarks are set by which to judge the adequacy of the Group's capital The capital position is monitored against those benchmarks to ensure that sufficient capital is available to the Group In the event that sufficient capital is not available, actions would be taken either to raise additional capital or to reduce the amount of risk accepted thereby reducing the capital requirement through, for example, reinsurance, reducing business volumes or a change in investment strategy

The Group complied with all externally imposed capital requirements to which it was subject throughout the reporting period

Capital statement

The tables below set out the capital resources available to the individual life funds and other activities of the Group

Reconciliation of Available Capital Resources

The following table reconciles the Unallocated divisible surplus presented in the Statement of Financial Position and total available capital resources calculated on a regulatory basis

	2012 £m	2011 £m
Unallocated divisible surplus	**878 6**	1,055 1
Regulatory adjustments		
- Adjustment to reserves to realistic basis	**355 1**	196 6
- Adjustment to cost of investment in subsidiaries (note 1)	**(319 8)**	(362 1)
- Inadmissible assets (note 2)	**(13 2)**	(130 4)
	900 7	759 2
RNPFN Fund not available to the Group (note 3)	**179 5**	164 5
Total Available Capital Resources	**1,080 2**	923 7

Notes

1 Represents the difference between the cost of investment in subsidiaries and the value for regulatory purposes net of the capital requirement

2 Inadmissible assets include pension scheme, deferred tax and goodwill

3 RNPFN denotes Royal National Pension Fund for Nurses, which is a ring-fenced fund The free assets attributable to this fund are reported as insurance contract liabilities of the Society

Movements in capital are analysed below

	2012 £m	2011 £m
Capital at 1 January	**923 7**	1,050 9
Effect of investment variations	**199 2**	23 9
Effect of changes in market conditions	**(52 6)**	(9 5)
Effect of changes in assumptions	**166 3**	(13 9)
New business	**(128 6)**	(94 3)
Other	**(27 8)**	(33 4)
Capital as at 31 December	**1,080 2**	923 7

Notes to the Financial Statements continued

31 December 2012

2. Capital management (continued)

Regulatory Capital	2012 £m	2011 £m
Admissible assets	**7,865 7**	7,185 9
Add back capital requirements of regulated related undertakings	**253 9**	241 5
Mathematical reserves (after distribution of surplus)	**(6,686 0)**	(6,123 1)
Regulatory current liabilities	**(353 4)**	(380 6)
Available capital resources	**1,080 2**	923 7
Capital requirements of regulated related undertakings	**(253 9)**	(241 5)
Capital resources of RNPFN fund	**(179 5)**	(164 4)
Peak 1 capital requirement	**(239 6)**	(218 0)
Peak 1 excess regulatory capital (excluding RNPFN surplus)	**407 2**	299 8
With-profits insurance capital component	**(220 8)**	(64 6)
Peak 2 excess capital resources (excluding RNPFN surplus)	**186 4**	235 2

The RNPFN fund s capital is available to support the RNPFN participating contract fund only It is comfortably in excess of the required capital margin and, therefore, the Society is not required to provide further capital support to this business

Available capital - Long-term insurance contracts

For the long-term insurance contract funds the Group is required to hold sufficient capital to meet the FSA capital requirements based on the risk capital margin (RCM) determined in accordance with the FSA's regulatory rules under its realistic capital regime together with the Individual Capital Assessment (ICA) which takes into account certain business risks not reflected in the RCM The determination of the RCM depends on various actuarial and other assumptions about potential changes in market prices, future operating experience and the actions management would take in the event of particular adverse changes in market conditions

Management intends to maintain surplus capital in excess of the RCM and ICA to meet the FSA's total requirements and to maintain an appropriate additional margin over this to absorb changes in both capital and capital requirements

i) Participating insurance contracts

For the Group's participating contract (with-profits) funds the available capital is determined in accordance with the 'realistic balance sheet' regime prescribed by the FSAs regulations under which liabilities to policyholders include both declared bonuses and the constructive obligation for future bonuses not yet declared The available capital resources include an estimate of the value of their respective estates, which is the surplus in the fund in excess of any constructive obligations to policyholders The unallocated capital represents the capital resources of the individual participating contract fund to which it relates and is available to meet regulatory and other solvency requirements of the fund For these participating contract funds the liabilities included in the Statement of Financial Position comprise only amounts relating to policyholders

ii) Non participating insurance contracts

For non participating business the relevant capital requirement is the minimum solvency requirement determined in accordance with FSA regulations For this business a lower capital surplus is targeted by management since the capital requirement is less subject to fluctuation and the capital amount is after deducting liabilities that include additional prudential margins

The other activities of the Group have total available capital which is significantly higher than the minimum requirements established by the FSA for each of the regulated entities and, in principle, the excess is available to the Society In practice, higher levels of capital are held within each business operation to provide appropriate cover for risk and new business growth

All available capital within LVFS is ultimately available to support the Society's participating contract fund However the available capital resources of each regulated entity are generally subject to restrictions as to their availability to meet requirements that may arise elsewhere in the Group For other non participating funds, the available surplus held in the fund is attributable to Society policyholders and, subject to meeting the regulatory requirements of these businesses, this capital is available to meet requirements elsewhere in the Group

Sensitivity of long-term insurance contract liabilities

Long-term insurance contract liabilities are sensitive to changes in market conditions and other assumptions which have been factored into their calculation, such as mortality or persistency rates In some cases allowance is also made when calculating liabilities for the effect of management and/or policyholder actions in different economic conditions on future assumptions such as asset mix, bonus rates and surrender values

Market conditions – assumptions are made about investment returns and interest rates when valuing liabilities Any adverse change in either variable may have the effect of reducing available capital as they may also impact corresponding asset valuations

Assumptions – long-term trend differences in mortality, morbidity, expense or persistency rates will result in the need to change assumptions This may require a strengthening or release of reserves Depending on policy type this sensitivity will differ, for example a change in mortality rates will have a different impact for annuity contract liabilities when compared to term assurance liabilities In addition to persistency, assumptions are made about policyholders' behaviour in relation to guarantees and options In turn these assumptions are sensitive to both investment return and interest rates

Further disclosure of the impact on the Unallocated divisible surplus from sensitivity analysis is provided in Note 3 Risk management and control

Notes to the Financial Statements continued

31 December 2012

2. Capital management (continued)

Financial guarantees and options

a) Participating insurance contracts

As a normal part of operating activities, the Society has given guarantees and options, including interest rate guarantees, in respect of certain long-term insurance contracts

Provision is made for such guarantees and options within the FSA realistic liabilities of the Group's participating insurance contract funds Under the FSAs rules these must be measured at fair value using market consistent stochastic models A stochastic approach includes measuring the time value of guarantees and options, which represents the additional cost arising from uncertainty surrounding future economic conditions The time value is evaluated by projecting a large number of possible future outcomes under a wide range of economic scenarios, for example possible outcomes for interest rates and equity returns These realistic liabilities have been included within the Statement of Financial Position

The material guarantees and options in the participating insurance contract funds are

i) Guaranteed annuity options - the RNPFN participating insurance contract fund has written individual pensions which contain guaranteed annuity rate options (GAOs), where the policyholder has the option to take the benefits from a policy in the form of an annuity based on guaranteed conversion rates

ii) Maturity value guarantees - many of the Group's participating insurance contracts have minimum maturity values reflecting the sums assured plus declared annual bonus

iii) Money-back guarantees - some of the policies written within the Group provide a guarantee or option to pay out all the premiums paid in (at a certain point in time)

b) Non participating insurance contracts

The Group has also written contracts which include guarantees and options within its non participating insurance contract funds These funds are not subject to the requirements of the FSA's realistic reporting regime and liabilities are evaluated by reference to statutory reserving rules Provision for guarantees and options in the non participating funds has been included within liabilities

The material guarantees and options in the non participating insurance contract funds are guaranteed annuity options Similar options to those written in the participating insurance contract fund have been written in relation to non participating contracts Provision for these guarantees does not materially differ from a provision based on a market consistent stochastic model

c) No Negative Equity Guarantees

The Group has made promises to certain policyholders in relation to equity release mortgages that payments on these policies will meet the mortgage value covered Further details on these are disclosed within Note 15

3. Risk management and control

The Group seeks to create value for its members by maintaining an appropriate balance between the capital available to support risk and the level and type of risk it takes on in order to achieve returns for policyholders The principal types of risk, which are detailed below, have been identified and risk appetite for each of these has been set based on the amount necessary to meet the FSA's capital requirements The Group recognises the critical importance of having efficient and effective risk management systems in place and these take the form of

- Board and Executive committees with clear terms of reference
- Financial and non-financial committees
- A clear organisation structure with documented allocation of responsibilities
- A uniform methodology of risk assessment, which is embedded within all companies in the Group so that they operate within agreed tolerances and with appropriate controls in place
- Regular reviews of risks by senior managers, where frequency of review is determined by the potential impact of the risk and its likelihood

a) Insurance risk

Insurance risk is the risk that arises from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities Long-term insurance risk arises from mortality, morbidity, persistency and expense variances General insurance risk arises from risks in general insurance contracts which lead to significant claims in terms of quantity or value These would include significant weather events, subsidence, substantial medical claims and major accidents on a single policy Systems are in place to measure, monitor and control exposure to all these risks These are documented in policies for underwriting, pricing, claims and reinsurance To mitigate risk in the life and general insurance businesses the Group places reinsurance

Long-term insurance contracts

Protection and annuity business is at risk from adverse changes in mortality experience from the time when the policies were underwritten In the case of policies that pay out on death, the risk is that mortality experience worsens, whereas for annuities, the risk is that mortality experience improves These two types of business therefore to some extent offset each other in a risk sense On protection business, the Group uses underwriting procedures, backed up with medical screening if appropriate, designed to price accurately for such risks and reinsurance is in place to limit the quantum of risk retained on each policy The Group s annuity business is partially reassured

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

Income protection and critical illness business is at risk from changes in morbidity rates Where there is an increased incidence of ill health or an increase in the duration of such ill health, the Group is exposed to higher claims than expected The Group has underwriting procedures, including medical and financial screening if appropriate, to price accurately for such risks and reinsurance is in place to limit the risk retained on each policy

Persistency risk influences the ability to recover acquisition costs from margins within the products The risk is greater in early years but reduces significantly as time passes For long-term insurance contract liabilities there is an allowance built in to allow for future withdrawals

Higher than expected expense costs will increase the reserves required The Group is exposed to the risk that the charges it deducts from policyholder benefits are not sufficient to cover future expenses

The table below sets out the concentration of long term insurance and investment contract liabilities on a realistic basis by type of contract All business is written in the UK

	2012			2011		
	Gross	Reinsurance	Net	Gross	Reinsurance	Net
Group	£m	£m	£m	£m	£m	£m
Whole life	**1,462 6**	**(44 7)**	**1,417 9**	1,426 7	(18 6)	1,408 1
Endowment	**678 7**	**-**	**678 7**	758 9	-	758 9
Term Assurance	**83 4**	**(116 3)**	**(32 9)**	45 0	(77 2)	(32 2)
Guaranteed annuity pensions	**1,281 9**	**(22 5)**	**1,259 4**	1,269 7	(21 2)	1,248 5
Pure endowment pensions	**2,797 7**	**(19 9)**	**2,777 8**	2,108 4	(24 1)	2,084 3
Critical illness	**48.6**	**(33 3)**	**15 3**	59 1	(38 1)	21 0
Income protection	**67.0**	**(55 9)**	**11 1**	96 3	(40 8)	55 5
ISA	**69.8**	**-**	**69 8**	68 7	-	68 7
Other	**86 9**	**(4 8)**	**82 1**	91 9	(3 0)	88 9
	6,576 6	**(297 4)**	**6,279 2**	5,924 7	(223 0)	5,701 7
Long-term claims liabilities	**42 4**	**-**	**42 4**	40 0	-	40 0
Unit linked	**964 6**	**-**	**964 6**	806 9	-	806 9
	7,583 6	**(297 4)**	**7,286 2**	6,771 6	(223 0)	6,548 6

The table below sets out the impact on long-term insurance contract liabilities, the Unallocated divisible surplus and Profit before tax for movements in key assumptions

Sensitivity analysis for the change in assumptions used in long-term insurance contract liabilities	Impact on Profit before tax £m	Impact on the Unallocated divisible surplus £m	Impact on gross long-term insurance contract liabilities £m
Increase in mortality rates by 5%	**42 8**	**42 8**	**(14 7)**
Increase in morbidity rates by 5%	**(8 0)**	**(8 0)**	**24 4**
Reduction in persistency by 5%	**0 1**	**0 1**	**6 3**
Increase in expenses by 10%	**(15 6)**	**(15 6)**	**21 6**

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

General Insurance

The Group s general insurance ('GI') activities are primarily concerned with the pricing, accepting and management of risks from its policyholders In accepting risks the Group is committing to paying claims and therefore these risks must be understood The Group manages these risks through its underwriting strategy, reinsurance arrangements and proactive claims handling

For a portfolio of insurance contracts where the theory of probability is applied to pricing and provisioning, the principal risk that the Group faces under its insurance contracts is the risk that actual claims exceed the carrying value of the Group s insurance liabilities The risk arises from the inherent uncertainties as to the occurrence, amount and timing of insurance claims For general insurance contracts this is primarily represented by exposure to risks which may lead to significant claims in terms of frequency or value These would include significant weather events, subsidence and large single claims arising from either the motor business (injury claims) or SME business (liability and/or property claims) Procedures are in place to measure, monitor and control exposure to all these risks

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be In addition, a more diversified portfolio is less likely to be affected by a change in any subset of the portfolio The Group has developed its insurance underwriting strategy to diversify the type of insurance risks accepted and within each of these categories to achieve a sufficiently large population of risks to reduce the variability of the expected outcome

Property business (domestic and commercial) is exposed to catastrophic risks such as result from storms or floods as well as risks such as subsidence The Group has entered into reinsurance contracts which provide protection against catastrophic weather events

Motor business is exposed to the risk of large personal injury claims, where the claim amounts can be significant due to the cost of care required for the claimant The Group has entered into excess of loss reinsurance contracts which reduce its exposure to large claims The reinsurance retention is £5 0m per claim (2011 £5 0m per claim)

Commercial business is exposed to large individual property losses and also to liabilities arising from employment and commercial activities The Group has entered into reinsurance contracts which provide protection against these liabilities

The Group has historic Quota share and Excess of loss reinsurance contracts which reduce the Group's exposure to large claims

The table below sets out the concentration of General Insurance contract liabilities by type of contract

	2012			2011		
	Gross	**Reinsurance**	**Net**	Gross	Reinsurance	Net
Group	**£m**	**£m**	**£m**	£m	£m	£m
Motor	**1,071 5**	**(117 8)**	**953.7**	857 3	(94 3)	763 0
Household	**57 8**	**(0 2)**	**57 6**	53 9	–	53 9
Travel	**1 0**	**–**	**1 0**	1 0	–	1 0
Commercial	**153 4**	**(17 0)**	**136 4**	114 8	(6 6)	108 2
Other	**3 4**	**–**	**3 4**	2 9	–	2 9
	1,287 1	**(135 0)**	**1,152 1**	1,029 9	(100 9)	929 0

The claims provision is the estimated cost of outstanding claims from expired risks The provision is calculated largely from using our own historic claims development data How much the past claim development will reflect future claims development will be impacted by the following factors

- Changes in actuarial processes and methodology
- Changes in risk profile
- Changes in underwriting, rating and policy conditions
- Changes in legislation and regulation (e g Periodic Payment Orders ('PPOs) Ministry of Justice reforms, changes to the Ogden discount rate, etc)
- Changes in other external factors (e g claims farming/accident management firms)

It is therefore very important that the impact of these items on claims development is understood Whilst every effort has been made to ensure the claims provision appropriately allows for such changes, there remains uncertainty in the eventual reserve outcome as a result This uncertainty can change from year to year depending on the timing and magnitude of these items

The Group has identified two specific areas of uncertainty that it has explicitly allowed for within the claims provision but where the outcome could be worse than the amount allowed for These are

- Uncertainty in the proportion of claims identified by the Group as being likely to settle on a PPO basis that actually settle on a PPO basis
- Uncertainty in relation to the Ogden discount rate

The claims provision includes a specific allowance for claims identified as having the potential to settle on a PPO basis This allowance is based on the mean cost of claims derived from a range of scenarios based on the PPO settlement rate for the claims If all of these claims settled as PPOs, the reserves would deteriorate by an estimated £8 6m from the position shown above

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

The Ogden discount rate is set by the Lord Chancellor It is currently 2 5% but a revision is under consideration with a decision possible by late 2013 Whilst there are many views across the industry in terms of what the change should be, the general consensus is that a reduction in the rate is likely The claims provision has included an allowance for a change in the Ogden discount rate, using a scenario based approach as for PPOs The allowance is broadly equivalent to a reduction in the discount rate to 1 75% If the discount rate was to reduce to 1 5%, the claims provision would deteriorate by £4 4m A reduction to 1% would lead to a deterioration of £14 3m

The claims provision is also sensitive to the number and cost of large motor claims (defined as greater than £1m), which have been incurred but not reported and reserved We would typically expect a number of large claims from expired risks to be identified in the future, either from being newly reported or from existing claims increasing in magnitude above the £1m threshold The claims provision allows for £23 7m of late reported/reserved large claims Therefore, if six new claims at £5m each were reported, for example, this would lead to a £6 3m deterioration in the reserves, whereas four new £5m claims would lead to a £3 7m improvement

The tables below reflect the cumulative incurred claims including both claims notified and incurred but not reported ('IBNR') for each successive accident year at each Statement of Financial Position date, together with the cumulative payments to date The Group aims to maintain appropriate reserves in order to protect against adverse future claims experience and developments

Analysis of claims development – gross of reinsurance	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m	2011 £m	2012 £m	Total £m
Initial estimate of gross provision	396 9	500 9	521 5	551 0	560 2	539 6	606 9	771 2	906 4	1,086 2	
One year later	402 8	487 2	523 6	527 5	512 6	540 2	589 2	823 0	912 5		
Two years later	385 4	466 3	494 5	505 1	489 4	500 2	589 2	838 5			
Three years later	356 3	450 0	472 1	490 2	485 9	490 0	587 9				
Four years later	346 4	437 8	462 6	477 2	487 6	491 0					
Five years later	343 6	434 7	457 3	477 5	492 5						
Six years later	342 8	436 0	457 6	476 6							
Seven years later	342 9	435 9	454 7								
Eight years later	342 4	436 1									
Nine years later	344 6										
Current estimate of cumulative claims	344 6	436 1	454 7	476 6	492 5	491 0	587 9	838 5	912 5	1,086 2	6,120 6
Cumulative payments to date	(336 6)	(428 2)	(451 2)	(469 5)	(461 3)	(461 5)	(515 3)	(654 6)	(650 7)	(455 2)	(4,884 1)
Liability recognised in the Statement of Financial Position for 2003 to 2012 accident years	8 0	7 9	3 5	7 1	31 2	29 5	72 6	183 9	261 8	631 0	1,236 5
Liability recognised in the Statement of Financial Position in respect of prior accident years											33 8
Claims handling provision											16 8
Gross General Insurance claims liabilities as at 31 December 2012											**1,287 1**

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

Analysis of claims development – net of reinsurance	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m	2011 £m	2012 £m	Total £m
Initial estimate of net provision	357 4	445 6	484 2	513 4	505 8	506 8	584 0	762 1	897 2	1,060 6	
One year later	364 3	437 1	473 8	474 7	462 9	482 9	578 0	802 9	897 1		
Two years later	352 8	415 8	439 2	467 0	440 2	464 0	564 7	818 9			
Three years later	328 1	407 0	429 5	451 4	441 1	456 7	562 1				
Four years later	327 5	393 2	423 4	443 7	430 1	457 6					
Five years later	316 6	391 5	421 9	441 9	431 3						
Six years later	314 7	392 7	421 1	441 2							
Seven years later	315 2	389 4	419 8								
Eight years later	316 6	391 0									
Nine years later	319 9										
Current estimate of cumulative claims	319 9	391 0	419 8	441 2	431 3	457 6	562 1	818 9	897 1	1,060 6	5,799 5
Cumulative payments to date	(315 3)	(388 6)	(417 2)	(434 3)	(420 3)	(434 4)	(506 8)	(653 5)	(645 8)	(455 2)	(4,671 4)
Liability recognised in the Statement of Financial Position for 2003 to 2012 accident years	4 6	2 4	2 6	6 9	11 0	23 2	55 3	165 4	251 3	605 4	1,128 1
Liability recognised in the Statement of Financial Position in respect of prior accident years											7 2
Claims handling provision											16 8
Net General Insurance claims liabilities as at 31 December 2012											**1,152 1**

b) Financial risk

i) Market risk

Market risk is the risk of adverse or favourable impacts due to fluctuations in equity prices, interest rates (including credit spreads and bond yields), exchange rates or property prices It arises due to fluctuations in liabilities arising from products sold and the value of investments held The Group has defined policies and procedures in place to control the major components of market risk Threadneedle Asset Management Ltd is our investment manager who operates under contractual Investment Management Agreements Assets are invested under agreed investment guidelines that reflect the Group's investment risk appetite Investment performance is monitored closely by the Group Chief Investment Officer and the Investment Committee in order to ensure compliance with the relevant regulatory limits for solvency purposes and with guidelines set for each fund Investments held are primarily listed on recognised stock exchanges

Limits on the Group's exposure to equities are defined both in aggregate terms and by geography, industry and counterparty Tactical asset allocation meetings are held weekly, and strategic asset allocation meetings quarterly, to discuss investment return and concentration and to agree any changes required

Equity price risk

The Group is exposed to equity price risk from daily fluctuations in the market values of the equity portfolio These assets are used to support contractual liabilities arising from investment and long-term insurance contracts For investment and long-term linked insurance contracts the price movements are matched with corresponding movements in contractual obligations For participating insurance contracts the aim is to achieve growth in excess of the obligations The associated risk is hedged using derivatives For general insurance contracts, equities are held to achieve an investment return The associated risk is mitigated by investing in a diverse portfolio of high quality securities Holdings are diversified across industries and concentrations in any one company or industry are limited by parameters established by the Investment Committee

Interest rate risk

The Group monitors interest rate risk by calculating the mean duration of the investment portfolio and the liabilities issued The mean duration is an indicator of the sensitivity of the assets and liabilities to changes in current interest rates The mean duration of the liabilities is determined by means of projecting expected cash flows from the contracts using best estimates of mortality and voluntary terminations The mean duration of the assets is calculated in a consistent manner During 2012 the Group managed this risk through an active use of gilt yield hedges, in the form of contracts for differences

Credit spread risk

In addition to Interest rate risk, described above, a widening of corporate bonds spreads over and above risk-free yields will lead to a fall in the fair value of the Group's portfolio of corporate bonds and vice-versa For the investment and long-term linked insurance contracts this movement is matched with corresponding movements in contractual liabilities, for the general insurance business liabilities are undiscounted and so unaffected in current value by changes in credit spreads The Group monitors Credit spread risk by regularly reviewing its exposure to corporate bonds by both credit rating and duration

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

Currency risk

The Group is exposed to foreign currency exchange risk within the investment portfolio supporting the Group's operations from purchased investments that are denominated or payable in currencies other than sterling There is no other exposure to currency risk

The table below summarises the Group's exposure, after hedging, to foreign currency exchange risk in sterling

	2012					2011				
	Euro £m	US Dollar £m	Yen £m	Other £m	Total £m	Euro £m	US Dollar £m	Yen £m	Other £m	Total £m
Derivatives	**(34 6)**	**(46 6)**	**–**	**(6 1)**	**(87 3)**	(13 1)	(32 4)	–	(4 1)	(49 6)
Equity securities	**87 9**	**136 8**	**60 9**	**103 5**	**389 1**	105 1	205 3	59 0	90 6	460 0
Debt securities	**24 0**	**43 0**	**–**	**–**	**67 0**	8 9	32 3	3 3	0 5	45 0
Other investments	**14 6**	**–**	**–**	**–**	**14 6**	2 7	–	–	–	2 7
Cash and cash equivalents	**11 3**	**5 6**	**–**	**0 2**	**17 1**	21 7	3 7	0 1	0 4	25 9
	103 2	**138 8**	**60 9**	**97 6**	**400 5**	125 3	208 9	62 4	87 4	484 0

The sensitivity of investment assets to a 10% increase/decrease in Euro and US Dollar exchange rates, net of derivatives, is £10 3m and £13 9m respectively In determining the percentage rates to use in this sensitivity analysis the movements in actual market rates of Euro and US Dollars during 2012 was taken into account The above table incorporates all material currency risk to profit before tax Therefore, a 10% increase/decrease across all currencies could impact profit before tax by up to £40 1m

Some foreign debt securities are denominated in sterling so bear no currency risk and have not been included within the above table

Eurozone exposure

The Group has some exposure to the main countries involved in the ongoing difficulties being experienced within the Eurozone as disclosed below, the table shows the Group's exposure by country of incorporation of the counterparty at 31 December 2012

	Sovereign £m	Non-Sovereign £m	Total £m
Ireland	**–**	**332 8**	**332 8**
Italy	**0.4**	**35 9**	**36 3**
Portugal	**–**	**2 7**	**2 7**
Spain	**–**	**90 3**	**90 3**
France	**–**	**322 6**	**322.6**
Other Eurozone	**–**	**872 6**	**872.6**
Total	**0 4**	**1,656 9**	**1,657 3**

The Group has no exposure to either Greece or Cyprus Non-sovereign exposure includes £74m of subordinated debt

Property price risk

The Group is exposed to property price risk on the commercial properties it holds as investments Values of properties are determined from the future value of cash flows and the Group enters into leases following an assessment of the tenant's ability to pay the rent and service charges For investment and long-term linked insurance contracts the price movements are matched with corresponding movements in contractual obligations For participating insurance contracts the aim is to achieve growth in excess of the obligations The associated risk is mitigated by investing in a diverse portfolio of high quality properties

Derivative risk

Derivatives are used to reduce exposure to fluctuations in interest rates, exchange rates and for efficient portfolio management purposes The principal derivatives used for this function are interest rate contracts (including interest rate swaps and options), forward foreign exchange contracts and equity derivatives (index futures and options) respectively This risk is managed through the Group Asset and Liability Committee

Asset and liability matching

The Group manages its financial positions with an asset liability management (ALM) framework that has been developed to achieve long-term investment returns in excess of its obligations under insurance and investment contracts The principal technique of the Group s ALM is to match assets to the liabilities arising from insurance contracts by reference to the type of benefits payable to contract holders

The Group's ALM is integrated with the management of the financial risks associated with the Group s other financial assets and liabilities not directly associated with insurance and investment liabilities

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

Summary of market risk sensitivities

The table below sets out the impact on long-term insurance contract liabilities, the Unallocated divisible surplus and Profit before tax for movements in sectors of the market that the Group is invested in, net of derivatives

Sensitivity analysis to movements in key market sectors	Impact on Profit before tax £m	Impact on the Unallocated divisible surplus £m	Impact on gross long-term insurance contract liabilities £m
Equity values fall by 20%	(36 5)	(35 8)	(190 5)
Equity values increase by 20%	50 9	50 1	180 8
Property values fall by 12 5%	(10 3)	(10.3)	(15 7)
Property values increase by 12 5%	10 1	10 1	17 3
Credit spreads fall by 100bps	70 9	60 4	169 1
Credit spreads increase by 100bps	(66 4)	(56 4)	(157 1)
15 year Gilt yields fall by 17 5%	24 6	23 2	264 3
15 year Gilt yields increase by 17 5%	(21 2)	(20 0)	(240 8)

In determining the percentage rates to use in the sensitivity analysis the Group has made reference to those set by the regulators for calculating the risk capital margin

Asset values and, where appropriate, asset shares are adjusted to reflect the change in each sensitivity Future policy related liabilities are recalculated using these revised values and, where appropriate, economic scenarios generated by an asset model calibrated to the revised risk free rate

ii) Credit risk

Credit risk is the risk of loss due to counterparties failing to meet all or part of their obligations in a timely fashion

The principal credit risks arise from exposure to counterparties through exposure to corporate bonds, reinsurers' share of insurance liabilities, amounts due from reinsurers in respect of claims already paid, amounts due from insurance contract holders, amounts due from insurance intermediaries and counterparty risk with respect to derivative transactions

Policies are in place to control the major components of credit risk, including counterparty default and concentration risk The Group places limits on its exposure to a single counterparty, or groups of counterparties, and to geographical and industry segments

Reinsurance is used to manage insurance risk This does not, however, discharge the Group's liability as primary insurer If a reinsurer fails to pay a claim, the Group remains liable for the payment to the policyholder The creditworthiness of reinsurers is considered by reviewing their financial strength prior to finalisation of any contract and on an annual basis

The tables below show the credit profile of the Group's assets The credit risk profile of the Society is materially consistent with that of the Group

Credit risk exposure 2012	AAA £m	AA £m	A £m	BBB £m	Below BBB £m	Not rated £m	Total £m
Debt and other fixed income securities	3,006 2	402 0	1,712 3	1,126 5	33 6	32 5	6,313 1
Loans secured on residential property	–	–	–	–	–	415 3	415 3
Other	–	–	–	–	–	5 4	5 4
Deposits with credit institutions	–	–	–	–	–	14 6	14 6
Loans secured by policies	–	–	–	–	–	0 4	0 4
Other loans	–	–	–	–	–	0 3	0 3
Short-term deposits	–	37 5	250 2	–	–	50 9	338 6
	3,006 2	439 5	1,962 5	1,126.5	33 6	519 4	7,087 7
Reinsurance assets							
- non linked	–	285.0	89 7	1 0	–	36 0	411 7
- linked	–	35.5	–	–	–	–	35 5
	3,006 2	760 0	2,052 2	1,127 5	33 6	555 4	7,534 9

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

Credit risk exposure 2011	AAA £m	AA £m	A £m	BBB £m	Below BBB £m	Not rated £m	Total £m
Debt and other fixed income securities	2,947 1	392 1	1,236 0	698 4	33 7	33 7	5,341 0
Loans secured on residential property	–	–	–	–	–	334 2	334 2
Other	–	–	–	–	–	1 7	1 7
Loans secured by policies	–	–	–	–	–	0 6	0 6
Other loans	–	–	–	–	–	0 4	0 4
Short-term deposits	–	55 0	501 9	1 0	–	4 3	562 2
	2,947 1	447 1	1,737 9	699 4	33 7	374 9	6,240 1
Reinsurance assets							
- non linked	3 5	185 5	88 9	–	–	36 0	313 9
- linked	–	23 0	–	–	–	–	23 0
	2,950 6	655 6	1,826 8	699 4	33 7	410 9	6,577 0

The tables below show the age analysis of the Group's past due and/or impaired assets

Age analysis of assets past due but not impaired 2012	**<30 days £m**	**31 to 60 days £m**	**61 to 90 days £m**	**>90 days £m**	**Total past due but not impaired £m**	**Past due and impaired £m**	**Total £m**
Loans and other receivables	–	–	–	–	–	–	–
Insurance receivables	**5 5**	**3 9**	**1 8**	**5 6**	**16 8**	**0 6**	**17 4**
	5 5	**3 9**	**1 8**	**5 6**	**16 8**	**0 6**	**17 4**

Age analysis of assets past due but not impaired 2011	<30 days £m	31 to 60 days £m	61 to 90 days £m	>90 days £m	Total past due but not impaired £m	Past due and impaired £m	Total £m
Loans and other receivables	0 1	–	–	–	0 1	0 1	0 2
Insurance receivables	6 4	2 7	0 1	0 7	9 9	0 6	10 5
	6 5	2 7	0 1	0 7	10 0	0 7	10 7

Collateral

For over-the-counter derivative transactions undertaken by the Group, collateral is received from the counterparty The collateral can be sold or repledged by the Group and is repayable if the contract terminates or the contract's fair value decreases At 31 December 2012, the fair value of such collateral held was £65 5m (2011 £131 4m) No collateral received from the counterparty has been sold or repledged (2011 £nil)

In addition the Group has pledged £67 0m (2011 £nil) of corporate bonds as collateral in relation to cash flow swaps entered into during the year

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

iii) Liquidity risk

Liquidity risk is the risk that the Group does not have sufficient available liquid assets to meet its obligations as they fall due

Sources of liquidity risk have been identified and systems are in place to measure, monitor and control liquidity exposures These are documented in liquidity policies

Liquidity is maintained at a prudent level, with a buffer to cover contingencies including the provision of temporary liquidity to subsidiary companies

The maturity of the financial assets of the Group has been disclosed within the individual notes to the financial statements

The table below summarises the maturity profile of the financial liabilities of the Group based on remaining undiscounted contractual obligations, except for long-term insurance participating (commonly referred to as "with-profits") contracts where maturity profiles are determined on the discounted estimated timing of net cash outflows

Group **Maturity profile of financial liabilities 2012**	**Within 1 year £m**	**1-3 years £m**	**3-5 years £m**	**Over 5 years £m**	**Linked £m**	**Total £m**
Insurance contract liabilities	**497 1**	**646.0**	**340 7**	**6,350 6**	**77 0**	**7,911 4**
Investment contract liabilities	–	–	–	–	**959 3**	**959 3**
Net asset value attributable to unit holders	**503 9**	–	–	–	–	**503 9**
Provisions	**59 0**	**7 3**	**0 3**	–	–	**66 6**
Financial liabilities						
- Derivative financial instruments	–	–	–	**51 2**	–	**51 2**
- Other financial liabilities	**65 5**	**0 3**	–	**9 7**	–	**75 5**
Insurance payables	**44 7**	–	–	–	–	**44 7**
Trade and other payables	**190 0**	**2 4**	**2 4**	**88 2**	–	**283 0**
	1,360.2	**656 0**	**343 4**	**6,499 7**	**1,036.3**	**9,895 6**

Group Maturity profile of financial liabilities 2011	Within 1 year £m	1 3 years £m	3-5 years £m	Over 5 years £m	Linked £m	Total £m
Insurance contract liabilities	443 9	619 6	364 1	5,515 4	57 6	7,000 6
Investment contract liabilities	–	–	–	–	800 9	800 9
Net asset value attributable to unit holders	429 1	–	–	–	–	429 1
Provisions	6 5	48 1	0 8	0 7	–	56 1
Financial liabilities						
- Derivative financial instruments	–	3 8	–	–	–	3 8
- Other financial liabilities	67 1	–	–	10 1	–	77 2
Insurance payables	41 6	–	–	–	–	41 6
Trade and other payables	201 7	2 3	2 4	89 4	–	295 8
	1,189 9	673 8	367 3	5,615 6	858 5	8,705 1

For investment and long-term linked insurance contracts (unit linked) the Group matches all the assets on which the unit prices are based with assets in the portfolio Therefore the Group is not exposed to price, currency, credit or interest risk in respect of these contracts The Group is responsible for ensuring there is sufficient liquidity within the asset portfolio to enable liabilities to unit linked policyholders to be met as they fall due

Notes to the Financial Statements continued

31 December 2012

3. Risk management and control (continued)

Society Maturity profile of financial liabilities 2012	Within 1 year £m	1-3 years £m	3-5 years £m	Over 5 years £m	Linked £m	Total £m
Insurance contract liabilities	77 3	104 0	164 4	6,180 6	77 0	6,603 3
Investment contract liabilities	-	-	-	-	959 3	959 3
Provisions	57 8	5 0	0 3	-	-	63 1
Financial liabilities						
- Derivative financial instruments	-	-	-	51 2	-	51 2
- Other financial liabilities	65 6	0 6	0 5	14 7	-	81 4
Insurance payables	26 2	-	-	-	-	26 2
Trade and other payables	136 2	-	-	-	-	136 2
	363 1	109 6	165 2	6,246 5	1,036 3	7,920 7

Society Maturity profile of financial liabilities 2011	Within 1 year £m	1 3 years £m	3-5 years £m	Over 5 years £m	Linked £m	Total £m
Insurance contract liabilities	107 8	190 3	184 7	5,405 8	57 6	5,946 2
Investment contract liabilities	–	–	–	–	800 9	800 9
Provisions	5 1	46 8	0 4	–	–	52 3
Financial liabilities						
- Derivative financial instruments	–	3 8	–	–	–	3 8
- Other financial liabilities	66 8	5 9	–	–	–	72 7
Insurance payables	31 6	–	–	–	–	31 6
Trade and other payables	147 4	–	–	–	–	147 4
	358 7	246 8	185 1	5,405 8	858 5	7,054 9

iv) Other risk types

Operational risk

Operational risk is the risk of loss, resulting from inadequate or failed internal processes, systems, human error or from external events, including legal and regulatory risk

Senior managers are responsible for the identification, assessment, control and monitoring of operational risks and for reporting these to the Risk Committee in accordance with the Group's escalation criteria Operational risks are assessed in terms of their probability and impact in accordance with Group policy

Group risk

Group risk is the risk of contagion that the Society incurs from its membership of a group of firms The Group Risk Committee oversees the management of such risks

Strategic risk

Strategic risk is the risk arising from the implementation of agreed strategy It includes risks arising from political, economic, sociological and technological changes, competitor actions and capital adequacy

Executive management identifies strategic risks when drawing up business plans for approval by the Board and monitors these, ensuring that excess risk is reported to the Group Risk Committee and Board

Notes to the Financial Statements continued

31 December 2012

Performance

The notes included within this section focus on the performance and results of the Society and Group Information on the income generated, benefits and claims paid, expenditure incurred and mutual bonus declared are presented here

4. Net earned premiums

Accounting for net earned premiums

Long-term insurance contracts

Regular premiums on long-term insurance contracts are recognised as income when due for payment For single premium business, recognition occurs on the date from which the policy is effective Reinsurance premiums payable are accounted for when due for payment

Annual premium equivalent (APE), a measure of new business activity that is calculated as the sum of annualised regular premiums from new business plus ten per cent of single premiums on new business written during the period

General insurance contracts

General insurance premiums written reflect business coming into force during the year Earned premium is written premium adjusted for unearned premium Unearned premium is that proportion of a premium written in a year that relates to periods of risk after the Statement of Financial Position date Unearned premiums are calculated on a time apportionment basis The proportion attributable to subsequent periods is deferred as a provision for unearned premiums

Investment contracts

Premiums and claims relating to investment contracts are not recognised in the Statement of Comprehensive Income but are recorded as contributions to and deductions from the investment contract liabilities recorded in the Statement of Financial Position

		Group		Society	
Gross written premiums		**2012 £m**	2011 £m	**2012 £m**	2011 £m
Long-term insurance contracts - participating business					
Investments and savings	- single premium	**61 5**	45 7	**61 5**	45 7
Pensions and annuities	- single premium	**10 8**	8 7	**10 8**	8 7
Investments and savings	- regular premium	**44 3**	52 9	**44 3**	52 9
Pensions and annuities	- regular premium	**15 2**	16 9	**15.2**	16 9
Long-term insurance contracts - non participating business					
Pensions and annuities	- single premium	**677 3**	601 1	**677 3**	601 1
Investments and savings	- regular premium	**0 3**	0 5	**0 1**	0 2
Pensions and annuities	- regular premium	**6 8**	7 7	**6 8**	7 7
Life and health protection	- regular premium	**131 7**	116 9	**131 2**	116 4
Long-term linked insurance contracts					
Investments and savings	regular premium	**0 3**	0 9	**0 3**	0 9
Pensions and annuities	- regular premium	**0.4**	1 8	**0.4**	1 8
Life and health protection	- regular premium	**11 2**	10 5	**11 2**	10 5
General insurance contracts					
Motor		**1,109.1**	1,124 9	**-**	-
Household		**140.3**	128 8	**-**	-
Other		**235 5**	201 9	**-**	-
Change in unearned premiums provision		**1 5**	(122 7)	**-**	-
Gross earned premiums		**2,446 2**	2,196 5	**959 1**	862 8
Premiums ceded to reinsurers					
Long term insurance premiums		**(75 6)**	(68 1)	**(75.6)**	(99 7)
General insurance business		**(35 0)**	(27 7)	**-**	-
Change in unearned premiums provision		**1 8**	2 8	**-**	-
		(108 8)	(93 0)	**(75 6)**	(99 7)
Net earned premiums		**2,337 4**	2,103 5	**883 5**	763 1
Gross written premiums for investment contracts which are deposit accounted for and not included above		**270 0**	214 0	**270 0**	214 0

All contracts are written in the UK apart from Highway Insurance Company Limited which writes a proportion of its general insurance business in Ireland These Irish net earned premiums totalled £3 9m in 2012 (2011 £10 1m)

Notes to the Financial Statements continued

31 December 2012

5. New business premiums

Gross new business – long-term contracts		Group 2012 £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Long-term insurance contracts - participating business					
Investments and savings	- single premium	**61 5**	45 7	**61 5**	45 7
Pensions and annuities	- single premium	**10 8**	8 7	**10 8**	8 7
Investments and savings	- regular premium	**0 9**	1 1	**0 9**	1 1
Long-term insurance contracts - non participating business					
Pensions and annuities	- single premium	**677 3**	601 1	**677 3**	601 1
Life and health protection	- regular premium	**26 5**	23 8	**26 5**	23 8
Long-term linked insurance contracts					
Pensions and annuities	- regular premium	**–**	0 4	**–**	0 4
Life and health protection	- regular premium	**4 3**	3 2	**4 3**	3 2
		781 3	684 0	**781 3**	684 0
Investment contracts					
Pensions and annuities	- regular premium	**270 0**	214 0	**270 0**	214 0
		1,051.3	898 0	**1,051 3**	898 0

Gross written premiums for investment contracts are deposit accounted for and not included within net earned premiums
All gross new business premiums relate to individual business and are disclosed on an APE basis

Recurrent single premium rebates from the Department for Works and Pensions are included as new business single premiums
Pensions vested into annuity contracts during the year are included as new annuity single premium business at the annuity purchase price
Where periodic premiums are received other than annually, the periodic new business premiums are stated on an annualised basis

Group gross premiums earned – general business	2012 £m	2011 £m
Motor	**1,133 3**	1,030 5
Household	**135 2**	120 6
Commercial	**151 9**	128 0
Other	**66 0**	53 8
	1,486 4	1,332 9

6. Fee and commission income

Accounting for fee and commission income

Fees from investment contracts for investment management, other policy administration charges and fund management fees are recognised as income when earned Commission earned from financial intermediary services is taken to income when earned This primarily comprises initial commission income receivable on services provided to clients during the year when policies have gone on risk and renewal commission received during the year on an accruals basis

	Group 2012 Restated £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Policy administration fees	**13 3**	11 6	**6 3**	4 9
Fund management fees	**–**	2 7	**–**	–
Commission income	**3 2**	4 2	**0.3**	0 3
	16 5	18 5	**6.6**	5 2

Notes to the Financial Statements continued

31 December 2012

7. Investment income

Accounting for investment income

Investment income includes dividends, interest from investments at fair value, interest on loans and receivables, interest on loans secured on residential property and rents Dividends are included on an ex-dividend basis Interest receivable on loans and receivables is calculated on an effective interest rate basis The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability

	Group		Society	
	2012	2011	2012	2011
		Restated		
	£m	£m	£m	£m
Rental income from investment properties	**6 1**	7 4	**6.1**	7 4
Income from investments at fair value through income				
- Interest income	**204 6**	123 2	**165 0**	126 8
Dividend income	**96 6**	117 4	**71 6**	71 2
Interest on loans and receivables	**0 8**	1 7	**0 3**	0 9
Interest on loans secured on residential property	**12 1**	11 7	–	–
Dividend income from group undertakings	–	–	**94 0**	78 6
	320 2	261 4	**337 0**	284 9

8. Net gains/(losses) on investments

Accounting for net gains / (losses) on investments

- Realised gains or losses

Realised gains and losses on investments are calculated as the difference between net sales proceeds and purchase price

- Unrealised gains and losses

Unrealised gains and losses on investments represent the difference between the valuation of fair value assets at the Statement of Financial Position date and their valuation at the last Statement of Financial Position date, or where purchased during the year, the purchase price An adjustment is made to unrealised gains and losses for the prior year s unrealised element included in the current year's realised gains and losses

	Group		Society	
	2012	2011	2012	2011
	£m	£m	£m	£m
Investment properties	**(1 2)**	(1 9)	**(1 2)**	(1 9)
Investments at fair value through income				
- Debt securities	**109 0**	350 3	**86 4**	335 1
- Equity securities	**295 0**	(33 1)	**241 5**	(34 5)
- Derivatives at fair value through income	**(28 1)**	110 1	**(22 6)**	108 6
Investments in group undertakings	–	–	**(90 0)**	(34 4)
	374.7	425 4	**214 1**	372 9

Included within net gains on investments are realised gains of £148 8m (2011 £174 4m) for the Group and realised gains of £126 0m (2011 £114 9m) for the Society

9. Other income

Accounting for other income

Other income primarily relates to interest receivable and unit linked income

	Group		Society	
	2012	2011	2012	2011
	£m	£m	£m	£m
Interest receivable	**22 1**	17 6	**0 1**	0 2
Unit linked income	**5 5**	3 8	**5 5**	3 8
Other income	**14 1**	29 6	**0 3**	15 1
	41 7	51 0	**5 9**	19 1

Notes to the Financial Statements continued

31 December 2012

10. Net benefits and claims

Accounting for net benefits and claims

Long-term insurance contracts

Maturity claims and regular annuity payments are accounted for when due for payment Surrenders are accounted for on the earlier of the date when paid or when the policy ceases to be included within the long-term insurance contract liability Death claims and other claims are accounted for when the Group is notified The value of claims on participating insurance contracts includes bonuses paid or payable Claims values include related internal and external claims handling costs Reinsurance recoveries are accounted for in the same period as the related claim

General insurance contracts

Claims incurred comprise claims and related internal and external claims handling costs paid in the year and changes in the provisions for outstanding claims, including provisions for claims incurred but not reported and related claims handling costs, together with any other adjustments to claims from previous years

The estimated cost of claims includes expenses to be incurred in settling claims and a deduction for the expected value of recoveries However, it is likely that the final outcome will prove to be different from the original liability established Provisions are adjusted at the Statement of Financial Position date to represent an estimate of the expected outcome

	Group		Society	
	2012	2011	**2012**	2011
	£m	£m	**£m**	£m
Gross benefits and claims				
Long-term insurance contracts				
Benefits and claims paid	**649 3**	667 7	**644 2**	661 8
Change in the provision for claims	**2 4**	(4 6)	**2 4**	(4 5)
General insurance contracts				
Claims paid	**910 3**	816 5	**–**	–
Change in the provision for claims	**257 3**	189 7	**–**	–
	1,819 3	1,669 3	**646 6**	657 3
Claims ceded to reinsurers				
Long-term insurance contracts				
Benefits and claims paid	**(61 8)**	(54 5)	**(61.8)**	(102 4)
General insurance contracts				
Claims paid	**(14 9)**	(7 4)	**–**	–
Change in the provision for claims	**(34 1)**	(24 5)	**–**	–
	(110 8)	(86 4)	**(61 8)**	(102 4)
	1,708 5	1,582 9	**584 8**	554 9
Net benefits and claims for investment contracts which are deposit accounted for and not included above (refer to Note 17)	**192 6**	120 5	**192 6**	120 5

11. Finance costs

	Group		Society	
	2012	2011	**2012**	2011
	£m	£m	**£m**	£m
Interest expense on loans and borrowings	**0.5**	0 5	**–**	–
	0 5	0 5	**–**	–

Notes to the Financial Statements continued

31 December 2012

12. Other operating and administrative expenses

Accounting for other operating and administrative expenses

Other operating and administrative expenses are accounted for as incurred Acquisition costs relate to the costs of acquiring new business during the financial year These include all commission and incentive payments to sales staff and third parties incurred in writing new contracts Where the benefit of these costs will be recognised in future accounting periods the costs are deferred

	Group		Society	
	2012	2011	**2012**	2011
	£m	£m	**£m**	£m
Commission paid on acquisition of business	**195 6**	184 2	**57 7**	50 1
Movement in deferred acquisition costs	**(5 4)**	(14 0)	**-**	-
Write-off following termination of reinsurance contract (see Note 23)	**-**	58 1	**-**	-
Amortisation of intangible assets	**12 0**	13 0	**4.6**	4 7
Depreciation on property and equipment - owned	**2 5**	1 7	**0 8**	0 8
Depreciation on property and equipment - finance leases	**0 9**	0 9	**-**	-
Loss on disposal of property and equipment	**0 4**	-	**0 4**	0 1
Investment management expenses and charges	**12 8**	3 8	**16 5**	23 6
Auditors remuneration	**2 2**	1 4	**1 6**	0 7
Employee benefits expense	**216 4**	209 7	**216 4**	209 7
Impairment of financial assets	**0 4**	(0 4)	**-**	0 1
Management charge allocated to group undertakings	**-**	-	**(191.1)**	(186 8)
Rent, rate and other facilities expense	**28 6**	18 2	**21 1**	13 2
Marketing and advertising	**45 9**	40 4	**19.2**	15 8
Other staff costs	**30 7**	29 0	**13 1**	14 3
IT costs	**39 4**	45 8	**21 6**	23 7
Fees	**58 3**	61 1	**25 0**	27 9
Other expenses	**27 8**	14 0	**17 7**	5 0
Claims handling cost recognised in Gross benefits and claims	**(60 0)**	(47 1)	**(6 0)**	(31 2)
	608 5	619 8	**218 6**	171 7

13. Auditors' remuneration

	2012	2011
	£m	£m
Audit of Society	**0 4**	0 5
Fees payable to the Society's auditors and its associates for other services		
- Audit of subsidiaries	**0 5**	0 3
- Audit-related assurance services	**0 2**	0 2
- Tax advisory services	**0 1**	0 1
- Other non-audit services not covered above	**1.0**	0 3
	2.2	1 4

14. Mutual Bonus

The Board declared a mutual bonus of £20 9m (2011 £18 6m) in respect of the year ended 31 December 2012

Notes to the Financial Statements continued

31 December 2012

Financial assets and liabilities

This section presents information relating to the financial assets and liabilities (excluding insurance contract-related assets and liabilities which are disclosed in Note 20) held by the Society and Group. These financial asset and liabilities are held at either fair value or amortised cost as defined by the Group's accounting policies

15. Financial assets – Fair value through income

Accounting for financial assets and liabilities at fair value through income

Financial assets at fair value through income has two sub categories

- Financial assets held for trading, and
- Those designated at fair value through income at inception

All investments of the Group classified as fair value are designated as fair value through income at inception Such assets are measured at market prices, or prices consistent with market ratings should no price be available Any unrealised or realised gains or losses are taken to the Statement of Comprehensive Income, as fair value gains or losses, or realised gains or losses respectively, as they occur

Financial assets at fair value through income include listed and unlisted investments, units in authorised unit trusts, open ended investment companies (OEICs), loans secured on residential property and other investments

Financial liabilities at fair value through income include derivative financial instruments and investment contract liabilities, see Notes 16 and 17 respectively

The IFRS "fair value hierarchy" levels for financial assets and liabilities required under IFRS7 are disclosed within Note 18

Loans secured on residential property

The fair value of the loans secured on residential property is determined using discounted cash flows which take into account the interest rolled up on the loans, maturity profiles and expected future funding costs The swap rate used as an input to the discount rate is matched to the expected term of the underlying loans A 'No Negative Equity Guarantee' liability is fair valued using discounted cash flows and is netted off against the fair value of the assets

A Group undertaking provides 'No Negative Equity Guarantee' contracts to customers on equity release mortgages The contractual terms of these guarantees require the company to make payments equivalent to any shortfall between the market value of customers' property and the value of the loan plus accrued interest at the date of redemption

The guarantee is initially recognised at the fair value of the liability on the date the guarantee is given and is subsequently measured at fair value The fair value is calculated by applying stochastic scenario models, applying assumptions for interest rates, future house price inflation and its volatility, mortality rates and early loan repayment rates, to give management's best estimate of the discounted value of cash flows required to settle any future financial obligation arising at the Statement of Financial Position date

The guarantee is included within Financial assets – Fair value through income in the Statement of Financial Position The movement in the fair value of the guarantee is taken to the Statement of Comprehensive Income

Significant accounting estimates and judgements

Fair value of financial assets

Market observable inputs are used wherever possible In the absence of an active market, estimation of fair value is achieved by using valuation techniques such as recent arm's length transactions, discounted cash flow analysis and option pricing models For discounted cash flow analysis, estimated future cash flows and discount rates are based on current market information and rates applicable to financial instruments with similar yields, credit quality and maturity characteristics This valuation will also take into account the marketability of the assets being valued

Details of the key assumptions used in the absence of an active market are contained in the fair value estimation tables, as required by IFRS7, disclosed in Note 18

Notes to the Financial Statements continued

31 December 2012

15. Financial assets – Fair value through income (continued)

	Group 2012 £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Financial assets - Fair value through income				
Shares, other variable yield securities and units in unit trusts				
– UK listed	**2,107 8**	1,725 3	**3,051.7**	2,756 3
– UK unlisted	**112 3**	113 9	**112 3**	113 9
– Overseas listed	**437 3**	409 5	**70.5**	48 5
– Overseas unlisted	**92 9**	94 7	**92 0**	91 5
Debt and other fixed income securities				
– UK listed	**4,189 9**	3,841 2	**2,595 7**	2,198 9
– Overseas listed	**2,123 2**	1,499 8	**765 2**	532 0
Loans secured on residential property	**415 3**	334 2	**366 2**	111 1
Other	**5 4**	1 7	**5.3**	1 7
Loan to group undertaking	**–**	–	**–**	162 2
	9,484 1	8,020 3	**7,058 9**	6,016 1
Within one year	**3,186 2**	1,852 3	**3,510 4**	2,114 1
Over one year	**6,297 9**	6,168 0	**3,548 5**	3,902 0
	9,484 1	8,020 3	**7,058 9**	6,016 1
Assets held to cover linked liabilities included above	**1,000 8**	855 8	**1,000 8**	855 8

The loan to group undertaking was designated at fair value through income within the Society to avoid an accounting mismatch across the Group, the loan was repaid in 2012

16. Derivative financial instruments

Accounting for derivative financial instruments

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 There are no designated hedging relationships within the Group that qualify for hedge accounting, all are classified as held for trading

Changes in the fair value of derivative instruments are recognised immediately in gains or losses on investments in the Statement of Comprehensive Income for the period Realised gains or losses are taken to the Statement of Comprehensive Income on occurrence

Group	2012 Contract/ notional amount £m	2012 Fair value – asset £m	2012 Fair value – liability £m	2011 Contract/ notional amount £m	2011 Fair value – asset £m	2011 Fair value – liability £m
Interest rate swaps	**635 0**	**20 0**	**–**	486 9	64 2	–
Gilt hedges	**1,417 1**	**1.0**	**–**	–	–	–
Cash flow swaps	**79 4**	**–**	**(51.2)**	–	–	–
Swaptions	**151 9**	**17 9**	**–**	196 7	29 6	–
Forward exchange contracts	**3 3**	**–**	**–**	3 5	–	–
Equity/index derivatives	**233 6**	**31 9**	**–**	1,111 4	50 0	(3 6)
Property index swap	**–**	**–**	**–**	20 0	–	(0 2)
	2,520 3	**70.8**	**(51 2)**	1,818 5	143 8	(3 8)

Notes to the Financial Statements continued

31 December 2012

16. Derivative financial instruments (continued)

The Group uses derivatives to hedge the effect of changes in variable rate borrowings on its fixed rate loan portfolio, to reduce exposure to payouts under guaranteed annuity contracts and to protect against falls in the FTSE 100 In 2012, the general insurance business entered into gilt hedge contracts for differences, as a result a significant proportion of the general insurance asset portfolio is hedged against stock market and gilt yield movements

	2012			2011		
Society	**Contract/ notional amount £m**	**Fair value – asset £m**	**Fair value – liability £m**	Contract/ notional amount £m	Fair value – asset £m	Fair value – liability £m
Interest rate swaps	**635 0**	**20 0**	**–**	486 9	64 2	–
Cash flow swaps	**79 4**	**–**	**(51 2)**	–	–	–
Swaptions	**151 9**	**17 9**	**–**	196 7	29 6	–
Equity/index derivatives	**153 6**	**30 6**	**–**	1,110 0	50 0	(3 6)
Property index swap	**–**	**–**	**–**	20 0	–	(0 2)
	1,019 9	**68 5**	**(51 2)**	1,813 6	143 8	(3 8)

17. Investment contract liabilities

Accounting for investment contract liabilities

Investment contract liabilities are recognised when contracts are entered into and premiums are charged These liabilities are initially recognised at transaction price excluding any transaction costs directly attributable to the issue of the contract

Deposits and withdrawals are recorded directly as an adjustment to the contract liability in the Statement of Financial Position, a method known as deposit accounting Fees charged and investment income received are recognised in the Statement of Comprehensive Income when earned

Fair value adjustments are measured at each reporting date and are recorded in the Statement of Comprehensive Income Fair value is calculated as the number of units allocated to the policyholder in each unit linked fund multiplied by the unit price of those funds at the Statement of Financial Position date The fund assets and liabilities are valued on a basis consistent with that used to measure the equivalent assets and liabilities in the Statement of Financial Position, adjusted for the discounted effect of future tax arising from any unrealised gains or losses For a contract that can be cancelled by the policyholder, the fair value cannot be less than the surrender value

The liability is derecognised when the contract expires, is discharged or is cancelled

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Balance at 1 January	**800 9**	741 2	**800 9**	741 2
Deposits received from policyholders	**270 0**	214 0	**270 0**	214 0
Payments made to policyholders and fees deducted	**(192 6)**	(120 5)	**(192 6)**	(120 5)
Change in contract liabilities as shown in the Statement of Comprehensive Income	**81 0**	(33 8)	**81 0**	(33 8)
Balance at 31 December	**959 3**	800 9	**959 3**	800 9

The change in contract liabilities as shown in the Statement of Comprehensive Income comprises principally the allocation of the net investment return to policyholders of investment contracts less allowances for taxes Investment contracts are not reinsured

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation

The following fair value estimation tables, as required by IFRS7, present the Group's and Society's assets and liabilities measured at fair value by level of the fair value measurement hierarchy at 31 December 2012

The fair value of financial instruments included in the Level 1 category is based on published quoted bid market prices in an active market at the year-end date A market is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis

Level 2 financial instruments are not traded in an active market or their fair value is determined using valuation techniques These valuation techniques maximise the use of data from observable current market transactions (where it is available) using pricing obtained via pricing services, even where the market is not active It also includes financial assets with prices based on broker quotes

Specific valuation techniques used to value financial instruments classified as Level 3 include

- Quoted market prices or dealer quotes for similar instruments (unlisted shares)
- The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows based on observable yield curves
- The fair value of forward exchange contracts is determined using forward exchange rates at the Statement of Financial Position date, with the resulting value discounted back to present value
- The fair value of the loans secured on residential property is determined using discounted cash flows which take into account the interest rolled up on the loans, maturity profiles and expected future funding costs The swap rate used as an input to the discount rate is matched to the expected term of the underlying loans The No Negative Equity Guarantee liability is fair valued using discounted cash flows and is netted off against the fair value of the assets
- The fair value of Investment contract liabilities are calculated on a consistent basis to the underlying investments as described in Note 17
- Other techniques, such as discounted cash flow analysis, are used to determine fair value for the other financial instruments

If one or more of the significant inputs is not based on observable market data, the instrument is included in Level 3

Any changes to fair value are recognised within net gains/losses on investments within the Statement of Comprehensive Income with the exception of Investment contract liabilities where the movement is recognised within the gross change in contract liabilities Details of these gains/losses are disclosed within Notes 8 and 22 respectively

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation (continued)

Group	2012 Level 1 £m	2012 Level 2 £m	2012 Level 3 £m	2012 Total fair value £m	2011 Level 1 £m	2011 Level 2 £m	2011 Level 3 £m	2011 Total fair value £m
Financial assets								
Derivative financial instruments								
Interest rate swaps	–	–	20 0	20 0	–	–	64 2	64 2
Gilt hedges	–	–	1 0	1 0	–	–	–	–
Swaptions	–	–	17.9	17 9	–	–	29 6	29 6
Equity/index derivatives	1 2	–	30 7	31 9	10 3	–	39 7	50 0
	1 2	–	69 6	70 8	10 3	–	133 5	143 8
Financial assets held at fair value through income								
Shares, other variable yield securities and units in unit trusts								
– UK listed	1,284 6	823 2	–	2,107 8	1,095 6	629 7	–	1,725 3
– UK unlisted	–	–	112 3	112 3	–	–	113 9	113 9
– Overseas listed	395 7	41 6	–	437 3	378 7	30 8	–	409 5
– Overseas unlisted	–	–	92 9	92 9	–	–	94 7	94 7
Debt and other fixed income securities								
– UK listed	2,155 1	2,034 8	–	4,189 9	2,302 9	1,537 6	0 7	3,841 2
– Overseas listed	2 9	2,120 3	–	2,123 2	7 9	1,490 8	1 1	1,499 8
Loans secured on residential property	–	–	415 3	415 3	–	–	334 2	334 2
Other	5.4	–	–	5 4	1 7	–	–	1 7
	3,843.7	5,019 9	620 5	9,484 1	3,786 8	3,688 9	544 6	8,020 3
	3,844 9	5,019 9	690 1	9,554 9	3,797 1	3,688 9	678 1	8,164 1
Financial liabilities								
Investment contract liabilities	–	844 6	114 7	959 3	–	687 5	113 4	800 9
Derivative financial instruments								
Cash flow swaps	–	–	51 2	51 2	–	–	–	–
Equity/index derivatives	–	–	–	–	3 6	–	–	3 6
Property index swap	–	–	–	–	–	–	0 2	0 2
	–	–	51 2	51 2	3 6	–	0 2	3 8
	–	844 6	165 9	1,010 5	3 6	687 5	113 6	804 7

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation (continued)

	2012				2011			
	Level 1	Level 2	Level 3	Total fair value	Level 1	Level 2	Level 3	Total fair value
Society	£m	£m	£m	£m	£m	£m	£m	£m
Financial assets								
Derivative financial instruments								
Interest rate swaps	**–**	**–**	**20 0**	**20 0**	–	–	64 2	64 2
Swaptions	**–**	**–**	**17 9**	**17 9**	–	–	29 6	29 6
Equity/index derivatives	**–**	**–**	**30 6**	**30 6**	10 3	–	39 7	50 0
	–	**–**	**68 5**	**68 5**	10 3	–	133 5	143 8
Financial assets held at fair value through income								
Shares, other variable yield securities and units in unit trusts								
– UK listed	**668 3**	**2,383 4**	**–**	**3,051 7**	727 2	2 029 1	–	2,756 3
– UK unlisted	**–**	**–**	**112 3**	**112 3**	–	–	113 9	113 9
– Overseas listed	**68 7**	**1 8**	**–**	**70 5**	48 5	–	–	48 5
– Overseas unlisted	**–**	**–**	**92 0**	**92 0**	–	–	91 5	91 5
Debt and other fixed income securities								
– UK listed	**1,716 5**	**879 2**	**–**	**2,595 7**	1,670 5	527 7	0 7	2,198 9
– Overseas listed	**2 8**	**762 4**	**–**	**765 2**	7 5	523 4	1 1	532 0
Loan to group undertaking	**–**	**–**	**–**	**–**	–	–	162 2	162 2
Loans secured on residential property	**–**	**–**	**366 2**	**366 2**	–	–	111 1	111 1
Other	**5 3**	**–**	**–**	**5 3**	1 7	–	–	1 7
	2,461 6	**4,026 8**	**570 5**	**7,058 9**	2,455 4	3,080 2	480 5	6,016 1
	2,461 6	**4,026 8**	**639 0**	**7,127 4**	2,465 7	3,080 2	614 0	6,159 9
Financial liabilities								
Investment contract liabilities	**–**	**844 6**	**114 7**	**959 3**	–	687 5	113 4	800 9
Derivative financial instruments								
Cash flow swaps	**–**	**–**	**51.2**	**51 2**	–	–	–	–
Equity/index derivatives	**–**	**–**	**–**	**–**	3 6	–	–	3 6
Property index swap	**–**	**–**	**–**	**–**	–	–	0 2	0 2
	–	**–**	**51.2**	**51 2**	3 6	–	0 2	3 8
	–	**844 6**	**165 9**	**1,010 5**	3 6	687 5	113 6	804 7

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation (continued)

The table below presents the movements in Level 3 financial instruments for the year ended 31 December 2012

Group	At 1 January 2012 £m	Total gains/ (losses) recognised through income £m	Purchases £m	Sales* £m	Transfers to level 1 and level 2 £m	At 31 December 2012 £m
Financial assets						
Derivative financial instruments						
Interest rate swaps	64 2	(0 1)	–	(44 1)	–	20 0
Gilt hedges	–	1 0	–	–	–	1 0
Swaptions	29 6	(2 3)	–	(9 4)	–	17 9
Equity/index derivatives	39 7	(9 0)	–	–	–	30 7
	133 5	(10 4)	–	(53 5)	–	69 6
Financial assets held at fair value through income						
Shares, other variable yield securities and units in unit trusts						
– UK unlisted	113 9	11 6	0 8	(14 0)	–	112 3
– Overseas unlisted	94 7	1 0	0 6	(3 4)	–	92 9
Debt and other fixed income securities						
– UK listed	0 7	–	–	–	(0 7)	–
– Overseas listed	1 1	–	–	–	(1 1)	–
Loans secured on residential property	334 2	10 8	89 0	(18 7)	–	415 3
	544 6	23 4	90 4	(36 1)	(1 8)	620 5
	678 1	13 0	90 4	(89 6)	(1 8)	690 1
Financial liabilities						
Investment contract liabilities	113 4	1 3	–	–	–	114 7
Derivative financial instruments						
Cash flow swaps	–	(4 3)	55 5	–	–	51 2
Property index swap	0 2	–	–	(0 2)	–	–
	0 2	(4 3)	55 5	(0 2)	–	51 2
	113 6	(3 0)	55 5	(0 2)	–	165 9

* In relation to Loans secured on residential property, sales represents loans repaid

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation (continued)

Group	At 1 January 2011 £m	Total gains/(losses) recognised through income £m	Purchases £m	Sales £m	At 31 December 2011 £m
Financial assets					
Derivative financial instruments					
Interest rate swaps	10 7	53 5	–	–	64 2
Swaptions	33 0	8 9	–	(12 3)	29 6
Equity/index derivatives	-	9 7	30 0	–	39 7
	43 7	72 1	30 0	(12 3)	133 5
Financial assets held at fair value through income					
Shares, other variable yield securities and units in unit trusts					
– UK unlisted	146 1	(25 8)	4 1	(10 5)	113 9
– Overseas unlisted	95 0	14 1	1 8	(16 2)	94 7
Debt and other fixed income securities					
– UK listed	2 2	0 4	–	(1 9)	0 7
– Overseas listed	–	(3 1)	4 2	–	1 1
Loans secured on residential property	187 0	70 3	87 3	(10 4)	334 2
	430 3	55 9	97 4	(39 0)	544 6
	474 0	128 0	127 4	(51 3)	678 1
Financial liabilities					
Investment contract liabilities	137 4	-	–	(24 0)	113 4
Derivative financial instruments					
Swaptions	27 6	–	–	(27 6)	–
Property index swap	–	–	0 2	–	0 2
	27 6	–	0 2	(27 6)	0 2
	165 0	–	0 2	(51 6)	113 6

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation (continued)

Society	At 1 January 2012 £m	Total gains/ (losses) recognised through income £m	Purchases £m	Sales* £m	Transfers to level 1 and level 2 £m	At 31 December 2012 £m
Financial assets						
Derivative financial instruments						
Interest rate swaps	64 2	(0 1)	–	(44 1)	–	20 0
Swaptions	29 6	(2 3)	–	(9 4)	–	17 9
Equity/index derivatives	39 7	(9 1)	–	–	–	30 6
	133 5	(11 5)	–	(53 5)	–	68 5
Financial assets held at fair value through income						
Shares, other variable yield securities and units in unit trusts						
– UK unlisted	113 9	11 6	0 8	(14 0)	–	112 3
– Overseas unlisted	91 5	0 4	0 6	(0 5)	–	92.0
Debt and other fixed income securities						
– UK listed	0 7	–	–	–	(0 7)	–
– Overseas listed	1.1	–	–	–	(1.1)	–
Loan to group undertaking	162 2	(22 1)	–	(140 1)	–	–
Loans secured on residential property (note 1)	111 1	43 0	219 4	(7.3)	–	366 2
	480 5	32 9	220 8	(161.9)	(1 8)	570 5
	614 0	21 4	220 8	(215 4)	(1 8)	639 0
Financial liabilities						
Investment contract liabilities	113 4	1 3	–	–	–	114 7
Derivative financial instruments						
Cash flow swaps	–	(4 3)	55 5	–	–	51 2
Property index swap	0 2	–	–	(0 2)	–	–
	0 2	(4 3)	55 5	(0 2)	–	51 2
	113 6	(3 0)	55 5	(0 2)	–	165 9

Note 1 The £219 4m included as purchases of Loans secured on residential properties includes amounts transferred from a subsidiary, Liverpool Victoria Equity Release Limited as part of a December 2012 loan restructure with the Society

* In relation to Loans secured on residential property, sales represents loans repaid

Notes to the Financial Statements continued

31 December 2012

18. Fair value estimation (continued)

Society	At 1 January 2011 £m	Total gains/(losses) recognised through income £m	Purchases £m	Sales £m	At 31 December 2011 £m
Financial assets					
Derivative financial instruments					
Interest rate swaps	10 7	53 5	–	–	64 2
Swaptions	33 0	8 9	–	(12 3)	29 6
Equity/index derivatives	–	9 7	30 0	–	39 7
	43 7	72 1	30 0	(12 3)	133 5
Financial assets held at fair value through income					
Shares, other variable yield securities and units in unit trusts					
– UK unlisted	140 3	(25 8)	4 1	(4 7)	113 9
– Overseas unlisted	88 1	14 3	1 8	(12 7)	91 5
Debt and other fixed income securities					
– UK listed	2 2	0 4	–	(1 9)	0 7
– Overseas listed	–	(3 1)	4 2	–	1 1
Loan to group undertaking	131 7	29 1	6 4	(5 0)	162 2
Loans secured on residential property	–	25 6	87 3	(1 8)	111 1
	362 3	40 5	103 8	(26 1)	480 5
	406 0	112 6	133 8	(38 4)	614 0
Financial liabilities					
Investment contract liabilities	137 4	–	–	(24 0)	113 4
Derivative financial instruments					
Swaptions	27 6	–	–	(27 6)	–
Property index swap	–	–	0 2	–	0 2
	27 6	–	0 2	(27 6)	0 2
	165 0	–	0 2	(51 6)	113 6

Notes to the Financial Statements continued

31 December 2012

19. Loans and other receivables

Accounting for loans and other receivables

Loans are initially measured at fair value and then subsequently measured at amortised cost using the effective interest rate method

Receivables are recognised when due and comprise amounts due to the Society from group undertakings and other receivables They are initially recognised at fair value and then subsequently held at amortised cost

The Group assesses at each Statement of Financial Position date whether a loan or receivable, or a group of loans or receivables, is impaired For loans, the amount of any impairment loss is measured as the difference between the carrying amount and the present value of future cash flows For receivables, where there is objective evidence that the carrying value is impaired then the impairment loss will be recognised in the Statement of Comprehensive Income

Provision for impairment of loans

Provisions for impairment of loans and receivables are based on appraisals of loans and receivables both collectively and individually Provisions are made to reflect the estimated net realisable amount, taking into account potential future recoveries and the original effective interest rate Balances are written off in full when the debt is considered irrecoverable

Specific provisions have been made in respect of all identified impaired advances In calculating the required provision an appropriate factor is applied based on the present value of expected future cash flows, which is subject to periodic review to ensure its continuing applicability based on current experience, to reflect the probability that not all such loans will result in eventual loss Collective provisions have been made in respect of losses which, although not yet specifically identified, are expected from experience to arise

	Group		Society	
	2012	2011	2012	2011
	£m	£m	£m	£m
Deposits with credit institutions	**14 6**	–	–	–
Loans secured by policies	**0 4**	0 6	**0 4**	0 6
Other loans	**0 3**	0 4	**0 3**	0 4
Amounts due from group undertakings	–	–	**87 4**	109 6
Managing agents rental receivable	**12 5**	17 0	**12 5**	17 0
Investments receivable	**16 5**	13 2	**16 5**	13 2
Other receivables	**58 7**	84 8	**11 5**	14 1
	103 0	116 0	**128 6**	154 9
Within one year	**98 8**	112 4	**126 0**	154 0
Over one year	**4 2**	3 6	**2 6**	0 9
	103 0	116 0	**128 6**	154 9

The carrying amounts disclosed above reasonably approximate fair value at the Statement of Financial Position date

20. Other financial liabilities

	Group		Society	
	2012	2011 Restated	2012	2011 Restated
	£m	£m	£m	£m
Collateral received	**65 5**	66 8	**65 5**	66 8
Subordinated note (EUR12m - interest payable at the 3 month Euro Deposit Rate plus a margin of 3 65%)	**9 7**	10 0	–	–
Amounts due to group undertakings	–	–	**15 7**	5 6
Other	**0 3**	0 4	**0 2**	0 3
	75 5	77 2	**81 4**	72 7

The carrying amounts disclosed above reasonably approximate fair value at the Statement of Financial Position date

Notes to the Financial Statements continued

31 December 2012

Insurance contract-related assets and liabilities

This section presents information relating to insurance contract-related assets and liabilities held by the Society and Group The assumptions used in the valuation of the insurance contract liabilities are disclosed within Note 25 with sensitivities to these assumptions disclosed separately within Note 3

21. Insurance contract liabilities

Accounting for insurance contract liabilities

Participating business

The liability is calculated in accordance with the FSA's realistic' liability regime In particular, provision is made for all bonus payments (declared and future, reversionary and terminal) estimated, where necessary, in a manner consistent with the relevant fund s Principles and Practices of Financial Management (PPFM) The liability includes an allowance for the time and intrinsic value of options and guarantees granted to policyholders and for possible future management actions

The realistic liabilities are based on the aggregate value of policy asset shares reflecting past premiums, investment return, expenses and charges applied to each policy Allowance is also made for policy-related liabilities such as guarantees, options and future bonuses calculated using a stochastic model simulating investment returns, asset mix, expense charges and bonuses

Since the realistic liabilities include an allowance for future bonuses to participating contract policyholders that will be payable out of returns on non participating business, an amount within the participating contract fund is recognised representing the value of non-participating business Such an amount is not recognised for business written outside participating contract funds

In determining the realistic value of liabilities for participating contracts, indirect account is taken of the value of future profits on non-participating business written out of participating contract funds This is separately identifiable and is all in respect of policyholder liabilities The excess of the value of those future profits has been deducted from the realistic liabilities rather than recognising it as an asset

Non-participating business

The liability is calculated to comply with the reporting requirements under the FSA's Integrated Prudential Sourcebook using a gross premium valuation method or a method at least as prudent as the gross premium method The principal assumptions are given in the notes to the financial statements The Society and relevant subsidiaries have adopted the modified statutory solvency basis in the valuation of provisions for non-participating business

Liabilities for non-participating business are either included within the long-term insurance contract liabilities or the investment contract liabilities, depending upon the product classification

General insurance claims and insurance contract liabilities

Claims incurred comprise claims and related internal and external claims handling costs paid in the year and changes in the provisions for outstanding claims, including provisions for claims incurred but not reported and related claims handling costs, together with any other adjustments to claims from previous years Where applicable, deductions are made for recoveries from other parties

Provision is made for the estimated cost of claims incurred but not settled, including the cost of claims incurred but not reported The estimated cost of claims includes expenses to be incurred in settling claims and a deduction for the expected value of recoveries However, given the inevitable uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established Provisions are adjusted at the Statement of Financial Position date to represent a best estimate of the expected outcome Provisions are calculated allowing for reinsurance recoveries and a separate asset is recorded for the reinsurers' share of the provision

Unexpired risks

For general insurance contracts, provision is made, if required, for any anticipated claims and claims handling costs that are anticipated to exceed the unearned premiums, net of deferred acquisition costs An estimate is made for future investment income arising from the unearned premiums, and used to reduce the unexpired risk provision Unexpired risk surpluses and deficits are offset where business classes are managed together and a provision is made if an aggregate deficit arises

Significant accounting estimates and judgements

Valuation of investment and long-term insurance contract liabilities

The liability is based on assumptions reflecting the best estimate at the time allowing for a margin of risk and adverse deviation All contracts are subject to a liability adequacy test, which reflects management's best current estimate of future cash flows

The assumptions used for mortality, morbidity and longevity are based on standard industry or reinsurers' tables, adjusted where appropriate to reflect the Group's own experience In particular, for impaired annuities the mortality assumptions are based on reinsurers' tables with an individual loading applied depending on the nature of the impairment The assumptions used for investment returns, expenses, lapse and surrender rates are based on current market yields, product characteristics, and relevant claims experience The assumptions used for discount rates are based on current market risk rates, adjusted for the Group's own risk exposure Due to the long-term nature of these obligations, the estimates are subject to significant uncertainty

Notes to the Financial Statements continued

31 December 2012

21. Insurance contract liabilities (continued)

Valuation of general insurance contract liabilities

For general insurance contracts, estimates are made for the expected ultimate cost of claims reported as at the Statement of Financial Position date and the cost of claims incurred but not yet reported (IBNR) to the Group It can take a significant period of time before the ultimate cost of claims can be established with certainty, and the final outcome may be better or worse than that provided Standard actuarial claims projection techniques are used to estimate outstanding claims Such methods extrapolate the development of paid and incurred claims, recoveries from third parties, average cost per claim and ultimate claim numbers for each accident year, based upon the observed development of earlier years and expected loss ratios The main assumption underlying these techniques is that past claims development experience is used to project ultimate claims costs Allowance for one-off occurrences or changes in legislation, policy conditions or portfolio mix are also made in arriving at the estimated ultimate cost of claims in order that it represents the most likely outcome, taking account of all the uncertainties involved To the extent that the ultimate cost is different from the estimate, where experience is better or worse than that assumed, the surplus or deficit will be credited or charged to gross benefits and claims within the Statement of Comprehensive Income in future years

a) Analysis of insurance contract liabilities and reinsurance assets

		2012			2011		
Group	**Notes**	**Gross £m**	**Reinsurance £m**	**Net £m**	Gross £m	Reinsurance £m	Net £m
Long-term insurance contract liabilities	21 b	**6,504 9**	**(261 9)**	**6,243 0**	5,852 8	(200 0)	5,652 8
Long term linked insurance contract liabilities	21 c	**77 0**	**(35 5)**	**41 5**	77 9	(23 0)	54 9
Long-term claims liabilities	21 d	**42.4**	**–**	**42 4**	40 0	–	40 0
		6,624 3	**(297 4)**	**6,326 9**	5,970 7	(223 0)	5,747 7
General insurance unearned premiums	21 e	**746 0**	**(14 8)**	**731 2**	747 4	(13 0)	734 4
General insurance claims liabilities	21 f	**1,287 1**	**(135 0)**	**1,152 1**	1,029 9	(100 9)	929 0
		2,033 1	**(149 8)**	**1,883 3**	1,777 3	(113 9)	1,663 4
		8,657 4	**(447 2)**	**8,210 2**	7,748 0	(336 9)	7,411 1

		2012			2011		
Society	**Notes**	**Gross £m**	**Reinsurance £m**	**Net £m**	Gross £m	Reinsurance £m	Net £m
Long-term insurance contract liabilities	21 b	**6,484 0**	**(261 9)**	**6,222 1**	5,828 4	(200 0)	5,628 4
Long term linked insurance contract liabilities	21 c	**77 0**	**(35 5)**	**41 5**	77 9	(23 0)	54 9
Long-term claims liabilities	21 d	**42 3**	**–**	**42 3**	39 9	–	39 9
		6,603 3	**(297 4)**	**6,305 9**	5,946 2	(223 0)	5,723 2

Included within the "Other" category disclosed in tables 21b and 21c are amounts totalling £48 4m, as at 31 December 2011, in relation to the termination of the reinsurance agreement between the Society and Liverpool Victoria Life Company Limited Further details on this transaction are disclosed in Note 47

b) Movement in long-term insurance contract liabilities

	2012			2011		
Group	**Gross £m**	**Reinsurance £m**	**Net £m**	Gross £m	Reinsurance £m	Net £m
Balance at 1 January	**5,852 8**	**(200 0)**	**5,652 8**	5,038 0	(120 5)	4,917 5
Premiums received	**105 7**	**(26 1)**	**79 6**	207 7	(27 6)	180 1
Liabilities paid for death maturities, surrenders, benefits & claims	**(624 6)**	**23 7**	**(600 9)**	(543 6)	24 5	(519 1)
New business	**652.4**	**(33 2)**	**619 2**	572 8	(42 1)	530 7
Benefits and claims variation	**98.8**	**(0 1)**	**98 7**	2 5	(3 4)	(0 9)
Fees deducted	**(36 4)**	**–**	**(36 4)**	(17 4)	–	(17 4)
Accretion of investment income or change in unit prices	**404 1**	**(1.9)**	**402 2**	613 9	(0 1)	613 8
Adjustment due to changes in assumptions						
- Mortality/morbidity	**30 1**	**(13.3)**	**16 8**	(2 9)	9 5	6 6
- Investment return	**35 6**	**(1.3)**	**34 3**	(18 0)	–	(18 0)
- Expense	**(16 7)**	**1 9**	**(14 8)**	0 7	3 0	3 7
- Lapse and surrender rates	**(30 2)**	**–**	**(30 2)**	11 2	(0 3)	10 9
- Discount rate	**(28 3)**	**(4 1)**	**(32 4)**	76 8	(18 9)	57 9
- Model changes	**63 2**	**–**	**63 2**	(49 5)	10 6	(38 9)
- Other	**(22 5)**	**(7 5)**	**(30 0)**	(58 0)	(34 7)	(92 7)
Mutual bonus	**20 9**	**–**	**20 9**	18 6	–	18 6
Balance at 31 December	**6,504 9**	**(261.9)**	**6,243 0**	5,852 8	(200 0)	5,652 8

Notes to the Financial Statements continued

31 December 2012

21. Insurance contract liabilities (continued)

b) Movement in long-term insurance contract liabilities (continued)

Society	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**5,828 4**	**(200.0)**	**5,628 4**	5,011 8	(165 6)	4,846 2
Premiums received	**104 9**	**(26 1)**	**78 8**	215 7	(53 8)	161 9
Liabilities paid for death maturities, surrenders, benefits & claims	**(619 9)**	**23 7**	**(596 2)**	(547 5)	37 3	(510 2)
New business	**652 4**	**(33 2)**	**619 2**	569 8	(32 2)	537 6
Benefits and claims variation	**99 1**	**(0 1)**	**99 0**	0 9	1 8	2 7
Fees deducted	**(36 4)**	**-**	**(36 4)**	(18 4)	3 1	(15 3)
Accretion of investment income or change in unit prices	**404 0**	**(1 9)**	**402 1**	614 4	(1 9)	612 5
Adjustment due to changes in assumptions						
- Mortality/morbidity	**30 1**	**(13 3)**	**16 8**	0 2	(0 6)	(0 4)
- Investment return	**35 6**	**(1 3)**	**34 3**	(18 0)	-	(18 0)
- Expense	**(16 7)**	**1 9**	**(14 8)**	(0 2)	6 2	6 0
- Lapse and surrender rates	**(30 2)**	**-**	**(30 2)**	11 2	(0 3)	10 9
- Discount rate	**(28 5)**	**(4 1)**	**(32 6)**	81 0	(32 8)	48 2
- Model changes	**62 7**	**-**	**62 7**	(51 4)	16 7	(34 7)
- Other	**(22 4)**	**(7 5)**	**(29 9)**	(59 7)	22 1	(37 6)
Mutual bonus	**20 9**	**-**	**20 9**	18 6	-	18 6
Balance at 31 December	**6,484 0**	**(261 9)**	**6,222 1**	5,828 4	(200 0)	5,628 4

c) Movement in long-term linked insurance contract liabilities

Group	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**77 9**	**(23 0)**	**54 9**	68 7	(6 5)	62 2
Premiums received	**81 2**	**(15 7)**	**65 5**	31 9	(10 0)	21 9
Liabilities paid for death maturities, surrenders, benefits & claims	**(40 8)**	**14 2**	**(26.6)**	(35 8)	8 8	(27 0)
New business	**(12 9)**	**(22 5)**	**(35 4)**	(0 1)	(8 7)	(8 8)
Benefits and claims variation	**(9 5)**	**(0.1)**	**(9 6)**	(3 8)	(1 2)	(5 0)
Fees deducted	**(6 4)**	**-**	**(6 4)**	(2 4)	-	(2 4)
Accretion of investment income or change in unit prices	**3 5**	**(1.2)**	**2 3**	0 5	-	0 5
Adjustment due to changes in assumptions						
- Mortality/morbidity	**(9 1)**	**(8 0)**	**(17 1)**	3 2	3 4	6 6
- Expense	**(15 4)**	**1 1**	**(14 3)**	(4 8)	1 1	(3 7)
- Lapse and surrender rates	**-**	**-**	**-**	0 2	(0 1)	0 1
- Discount rate	**8 6**	**(2 5)**	**6 1**	16 2	(4 1)	12 1
- Model changes	**-**	**-**	**-**	(8 7)	3 8	(4 9)
- Other	**(0 1)**	**22 2**	**22 1**	12 8	(9 5)	3 3
Balance at 31 December	**77 0**	**(35 5)**	**41 5**	77 9	(23 0)	54 9

Notes to the Financial Statements continued

31 December 2012

21. Insurance contract liabilities (continued)

c) Movement in long-term linked insurance contract liabilities (continued)

Society	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**77 9**	**(23 0)**	**54 9**	68 7	(50 4)	18 3
Premiums received	**81 2**	**(15 7)**	**65 5**	23 9	(19 4)	4 5
Liabilities paid for death maturities, surrenders, benefits & claims	**(40 8)**	**14 2**	**(26 6)**	(31 7)	13 6	(18 1)
New business	**(12 9)**	**(22 5)**	**(35 4)**	2 9	(5 1)	(2 2)
Benefits and claims variation	**(9 5)**	**(0 1)**	**(9 6)**	(2 2)	0 6	(1 6)
Fees deducted	**(6 4)**	**–**	**(6 4)**	(1 5)	1 1	(0 4)
Accretion of investment income or change in unit prices	**3 5**	**(1 2)**	**2 3**	–	(0 7)	(0 7)
- Mortality/morbidity	**(9 1)**	**(8 0)**	**(17 1)**	0 1	(0 2)	(0 1)
- Expense	**(15 4)**	**1 1**	**(14 3)**	(3 9)	2 2	(1 7)
- Lapse and surrender rates	**–**	**–**	**–**	0 2	(0 1)	0 1
- Discount rate	**8 6**	**(2 5)**	**6 1**	11 9	(9 1)	2 8
- Model changes	**–**	**–**	**–**	(6 8)	6 0	(0 8)
- Other	**(0 1)**	**22 2**	**22 1**	16 3	38 5	54 8
Balance at 31 December	**77 0**	**(35 5)**	**41 5**	77 9	(23 0)	54 9

d) Movement in long-term claims liabilities

Group	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**40 0**	**–**	**40 0**	44 6	–	44 6
Claims notified	**651 7**	**(61 8)**	**589 9**	663 1	(54 5)	608 6
Claims paid during the year	**(649 3)**	**61 8**	**(587 5)**	(667 7)	54 5	(613 2)
Balance at 31 December	**42 4**	**–**	**42 4**	40 0	–	40 0

Society	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**39 9**	**–**	**39 9**	44 4	–	44 4
Claims notified	**646 6**	**(61 8)**	**584 8**	657 3	(102 4)	554 9
Claims paid during the year	**(644 2)**	**61 8**	**(582 4)**	(661 8)	102 4	(559 4)
Balance at 31 December	**42 3**	**–**	**42 3**	39 9	–	39 9

e) Movement in general insurance unearned premiums

Group	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**747 4**	**(13 0)**	**734 4**	624 7	(10 2)	614 5
Premiums written in the year	**1,484 9**	**(35 0)**	**1,449 9**	1,455 6	(27 7)	1,427 9
Premiums earned during the year	**(1,486 3)**	**33 2**	**(1,453 1)**	(1,332 9)	24 9	(1,308 0)
Balance at 31 December	**746 0**	**(14 8)**	**731 2**	747 4	(13 0)	734 4

f) Movement in general insurance claims liabilities

Group	2012 Gross £m	2012 Reinsurance £m	2012 Net £m	2011 Gross £m	2011 Reinsurance £m	2011 Net £m
Balance at 1 January	**1,029 9**	**(100 9)**	**929.0**	840 1	(76 4)	763 7
Movement in claims incurred in prior accident years	**32 7**	**(23 5)**	**9 2**	35 0	(22 7)	12 3
Claims incurred in the current accident year	**1,080 1**	**(25 5)**	**1,054 6**	927 5	(9 2)	918 3
Claims paid during the year	**(855 6)**	**14 9**	**(840 7)**	(772 7)	7 4	(765 3)
Balance at 31 December	**1,287 1**	**(135 0)**	**1,152 1**	1,029 9	(100 9)	929 0

Notes to the Financial Statements continued

31 December 2012

22. Net (increase) / decrease in long-term contract liabilities

	Group 2012 £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Gross (increase) / decrease in long-term contract liabilities				
(Increase) / decrease in long-term insurance contract liabilities	**(652 1)**	(814 8)	**(655 6)**	(816 6)
Decrease / (increase) in long term linked insurance contract liabilities	**0 9**	(9 2)	**0 9**	(9 2)
(Increase) / decrease in investment contract liabilities	**(81 0)**	33 8	**(81.0)**	33 8
	(732 2)	(790 2)	**(735 7)**	(792 0)
Mutual bonus (disclosed separately in Note 14)	**20 9**	18 6	**20 9**	18 6
	(711 3)	(771 6)	**(714 8)**	(773 4)
Increase / (decrease) in long-term contract liabilities ceded to reinsurers				
Increase / (decrease) in long-term insurance contract liabilities	**61 9**	79 5	**61 9**	34 4
Increase / (decrease) in long term linked insurance contract liabilities	**12 5**	16 5	**12 5**	(27 3)
	74 4	96 0	**74 4**	7 1
	(636 9)	(675 6)	**(640 4)**	(766 3)

23. Deferred acquisition costs

Accounting for deferred acquisition costs

The costs of acquiring new business, other than for participating business, which are incurred during the financial year, but where the benefit of such costs will be obtained in subsequent accounting periods are deferred and recognised as an asset to the extent that they are recoverable out of margins in future matching revenues

In respect of insurance contracts, acquisition costs comprise all direct and indirect costs incurred in writing new contracts Deferred acquisition costs for insurance contracts are amortised over a period which is consistent with the assessment of the expected pattern of receipt of future revenue margins for each product type

For investment contracts, the costs of acquiring investment contracts are limited to the direct transaction costs associated with the acquisition of the business Deferred acquisition costs for investment contracts are amortised over the expected contract period

All deferred acquisition costs are tested for recoverability at each reporting date The carrying values are adjusted to recoverable amounts and any resulting impairment losses are charged to the Statement of Comprehensive Income

Group	Long term insurance contracts £m	General insurance contracts £m	Total £m
At 1 January 2012	–	94 7	94 7
Acquisition costs deferred	–	199 0	199 0
Amortisation and impairment	–	(193 6)	(193 6)
At 31 December 2012	**–**	**100 1**	**100 1**
At 1 January 2011	54 6	84 2	138 8
Acquisition costs deferred	17 7	185 6	203 3
Amortisation and impairment	(14 2)	(175 1)	(189 3)
Write-off following termination of reinsurance contract	(58 1)	–	(58 1)
At 31 December 2011	–	94 7	94 7

Deferred acquisition costs are all due within one year for both 2011 and 2012

Acquisition costs are costs of acquiring new business and include commissions, underwriting expenses and policy issue expenses There were no deferred acquisition costs held by the Society in 2012 (2011 £nil)

In 2011 the £58 1m write off in relation to the termination of the reinsurance contract was offset by a £57 4m movement in long-term insurance contract liabilities disclosed within Note 21 The overall impact on the Statement of Comprehensive Income was a loss of £0 7m

Notes to the Financial Statements continued

31 December 2012

24. Reinsurance assets

Accounting for reinsurance assets

The Group cedes insurance risk in the normal course of business for its long-term and general insurance businesses Reinsurance assets represent balances recoverable from reinsurance companies Recoverable amounts are estimated in a manner consistent with the outstanding claims provision Reinsurance premiums are recognised in the same period as the underlying contract that they relate to

		Group		Society	
		2012	2011	2012	2011
	Notes	£m	£m	£m	£m
Reinsurers' share of provision for unearned premiums	21 a	**14 8**	13 0	**–**	–
Reinsurers' share of long term insurance contract liabilities	21 a	**261 9**	200 0	**261 9**	200 0
Reinsurers' share of long-term linked insurance contract liabilities	21 a	**35 5**	23 0	**35 5**	23 0
Reinsurers share of claims liabilities	21 a	**135 0**	100 9	**–**	–
		447 2	336 9	**297 4**	223 0
Within one year		**(107 7)**	(33 1)	**(141 5)**	(63 7)
Over one year		**554 9**	370 0	**438 9**	286 7
		447 2	336 9	**297 4**	223 0

The carrying amounts disclosed above reasonably approximate fair value at the Statement of Financial Position date

25. Long-term insurance and investment contract liabilities valuation assumptions

The basis of the calculation of the long-term insurance contract liabilities is described in the accounting policies The liability is calculated separately for each life operation Material judgement is required in calculating the liability In particular there is discretion over the assumptions used For participating business, the liability is calculated in accordance with the FSA's realistic capital regime adjusted to exclude the associated tax liability Non participating liabilities are valued using a gross premium method

In calculating the realistic liabilities, account has also been taken of future management actions consistent with those set out in the Principles and Practices of Financial Management The most significant of these are changes to bonus assumptions and level of payouts

The assumptions used to calculate the liability depend on the circumstances prevailing in each of the life operations The assumptions used in determining the liability are estimated to give a result within the normal range of outcomes To the extent that the ultimate cost differs to the amounts provided, for example where experience is worse than that assumed, the surplus or deficit will be credited or charged to the Statement of Comprehensive Income in future years

When valuing options and guarantees the asset model used was the Barrie and Hibbert Market-Consistent Asset Model This is a deflator model based on published financial economic theory that is capable of market-consistent valuations for multiple asset classes in multiple currencies For this valuation it was calibrated to market data as at 31 December 2012 representative of the nature and term of the guarantees inherent in participating insurance contracts within the participating insurance contract funds

The accounting policies for long-term insurance and investment contract liabilities are included within Notes 21 and 17 respectively, sensitivities to changes in assumptions are included within Note 3

a) Society

i) Participating insurance contracts

For participating insurance contracts, a market consistent valuation is used to calculate the liability This involves placing a value on liabilities similar to the market value of assets with similar cash flow patterns The key assumptions used in this valuation are set out in the tables below

Interest Rates

The risk-free interest rates assumed are

Year	2012	2011
5	**0 91%**	1 14%
15	**2 60%**	2 81%
25	**3 39%**	3 37%
35	**3 62%**	3 48%

Other assumptions

Best estimate assumptions are set for inflation, mortality, expenses and persistency The future expense inflation assumption is modelled as RPI plus 0 5% (2011 RPI plus 0 7%), where RPI in both 2012 and 2011 is modelled stochastically

Asset mix for assets backing asset shares at the valuation date	2012	2011
Cash	**2 38%**	2 73%
Fixed interest	**40 68%**	39 75%
Equities	**48 79%**	49 45%
Property	**8 15%**	8 07%

Notes to the Financial Statements continued

31 December 2012

25. Long-term insurance and investment contract liabilities valuation assumptions (continued)

Mortality rate tables	2012	2011
Conventional Life Business	**75% AM80 Females -3**	75% AM80 Females -3
Conventional Pensions Business	**60% AM80 Females -3**	65% AM80 Females -3
Conventional Industrial Branch Business	**80% up to age 80, rising linearly to 100% at age 100 ELT16**	80% up to age 80, rising linearly to 100% at age 100 ELT16
Non Unitised Accumulating Pensions Business	**65% AM80**	65% AM80
Unitised Accumulating Life Business	**80% AM80/AF80**	80% AM80/AF80
Unitised Accumulating Pensions Business	**80% AM80**	80% AM80
Unitised Accumulating Bond Business	**80% AM80**	80% AM80
Unitised Accumulating Life ISA Business	**80% AM80 select/AF80 select**	80% AM80 select/AF80 select
Annuities in Payment	**Males RMV00 CMI_2009 2% LT** **Females RFV00 CMI_2009 1 5% LT**	Males RMV00 CMI_2009 2% LT Females RFV00 CMI_2009 1 5% LT

Per policy expenses – regular premiums	2012	2011
Conventional Life Business	**£34 90**	£32 60
Conventional Pensions Business	**£45 30**	£42 00
Conventional Industrial Branch Business	**£6 80**	£6 90
Non Unitised Accumulating Pensions Business	**£28 30**	£26 30
Unitised Accumulating Life Business	**£40 50**	£36 50
Unitised Accumulating Pensions Business	**£45 30**	£42 00
Unitised Accumulating Bond Business	**£42 80**	£37 50
Unitised Accumulating Life ISA Business	**£49 20**	£43 40
Annuities in Payment	**£48 20**	£43 40

A percentage of these amounts is used for single premium and paid up policies

Persistency - lapses, surrenders and paid up rates
A review of persistency is carried out annually Assumptions for each product class are adjusted where necessary to reflect more recent experience as evidenced in the persistency trend analysis or to reflect expected future trends as a result of anticipated future events

Options and guarantees
There are no guaranteed annuity or financial options within the Society participating contract funds There is an additional reserve calculated on a market consistent basis to cover market value restricter (MVR) free guarantees on with-profits bonds

Bonuses
The cost of bonuses incurred during the year ended 31 December 2012 was £96 3m (2011 £84 6m) of which £19 6m (2011 £22 5m) was included in the long-term insurance contract liabilities and £76 7m (2011 £62 1m) was included in Gross benefits and claims paid in the Statement of Comprehensive Income

ii) Non participating insurance contracts

Interest rate	2012	2011
Non-profit temporary assurances (original LVFS)	**2 40%**	1 90%
Non-profit temporary assurances	**Yield Curve***	2 50%*
Whole of life assurances	**Yield Curve***	2 50%*
Permanent health insurance		
a) active lives	**Yield Curve***	2 50%*
b) claims reserves	**Yield Curve***	2 50%*
Critical illness	**Yield Curve***	2 50%*
Other assurances	**Yield Curve***	2 50%*
Annuities in payment	**Yield Curve* + 1.2%**	4 00%

* Adjusted by a margin for risk and uncertainty which varies by product line

Notes to the Financial Statements continued
31 December 2012

25. Long-term insurance and investment contract liabilities valuation assumptions (continued)

Mortality rate tables	2012	2011
Non-profit temporary assurances (original LVFS)	**AM80/AF80**	AM80/AF80
Non-profit temporary assurances	**TMN00/TMS00 TFN00/TFS00**	TMN00/TMS00 TFN00/TFS00
Whole of life assurances	**AMC00/AFC00**	AMC00/AFC00
Other assurances	**AM92/AF92**	AM92/AF92
Annuities in payment	**Males 100% RGA 2011 tables with CMI_2009 1 25% LT Females 100% RGA 2011 tables with CMI_2009 1% LT**	Males 100% RGA 2011 tables with CMI_2009 1 25% LT Females 100% RGA 2011 tables with CMI_2009 1% LT

Appropriate adjustments were made to the standard mortality tables to take account of actual experience and publicly available market data

Morbidity rate tables	2012	2011
Permanent health insurance		
a) active lives	**CMIR12**	CMIR12
b) claims reserves	**CMIR12**	CMIR12
Critical illness	**Reinsurer rates**	Reinsurer rates

Appropriate adjustments were made to the standard morbidity tables to take account of actual experience and publicly available market data

Per policy expenses – regular premiums	2012	2011
Non-profit temporary assurances	**£18 15**	£18 11
Whole of life assurances	**£14 71**	£16 06
Permanent health insurance		
a) active lives	**£27 54**	£25 16
b) claims reserves (per policy in claim)	**£650 49**	£552 29
Critical illness	**£27 61**	£29 86
Other assurances	**£34 93**	£32 54
Annuities in payment	**£48 00**	£38 00

Other assumptions
Best estimate assumptions are set for inflation, mortality, expenses and persistency The future expense inflation assumption is modelled as RPI (2011 RPI + 0 7%)

Options and guarantees
There are no significant options and guarantees in the non-participating business

iii) Investment and long-term linked insurance contracts
The provision for unit linked pensions is equal to the value of the assets to which the contracts are linked There is one product included within the linked fund which is classified as an investment product and the liability is included within the long-term linked insurance contract liabilities

The provision for property-linked liabilities is equal to the value of the assets to which the contracts are linked and is included within investment contract liabilities

The provisions for index-linked permanent health insurance claims and index-linked temporary assurances have been calculated using the same mortality and morbidity assumptions as used for the corresponding non-linked liabilities for both 2012 and 2011

Interest rate	2012	2011
Unit linked pensions (original LVFS)	**Gilt yield + risk premium + margin for risk and uncertainty**	1 90%

Mortality rate tables	2012	2011
Unit linked pensions (original LVFS)	**92% AX92C20**	80% AX92C20

b) Liverpool Victoria Life Company Limited - Ordinary Long Term Fund

i) Participating insurance contracts
Liverpool Victoria Life Company Limited has no participating business

Notes to the Financial Statements continued

31 December 2012

25. Long-term insurance and investment contract liabilities valuation assumptions (continued)

ii) Non participating insurance contracts

Interest rate	2012	2011
Non-profit temporary assurances	**1 76%**	1 88%
Other assurances	**1 76%**	1 88%

Mortality rate tables	2012	2011
Non-profit temporary assurances	**TMN00/TMS00 TFN00/TFS00**	TMN00/TMS00 TFN00/TFS00
Other assurances	**AM92/AF92**	AM92/AF92

Appropriate adjustments were made to the standard mortality tables to take account of actual experience

Per policy expenses – regular premiums	2012	2011
Non-profit temporary assurances	**£27 17**	£19 92
Other assurances	**£27 17**	£35 79

Options and guarantees

There are no significant options and guarantees in the non-participating business

c) RNPFN fund

RNPFN denotes Royal National Pension Fund for Nurses, which is a ring-fenced fund The free assets attributable to this fund are reported as insurance contract liabilities of the Society

i) Participating business

For participating business, a market-consistent valuation is used to calculate the liability This involves placing a value on liabilities similar to the market value of assets with similar cash flow patterns The key assumptions used in this valuation are set out in the tables below

Interest Rates

The risk-free interest rates assumed are

Year	2012	2011
5	**0 91%**	1 14%
15	**2 60%**	2 81%
25	**3.39%**	3 37%
35	**3 62%**	3 48%

Other assumptions

Best estimate assumptions are set for inflation, mortality, expenses and persistency The future expense inflation assumption is modelled as RPI plus 0 5% (2011 RPI plus 0 7%), where RPI in both 2012 and 2011 is modelled stochastically

Asset mix for assets backing asset shares at the valuation date	2012	2011
Cash	**16.32%**	14 03%
Fixed interest	**57.59%**	57 86%
Equities	**23 47%**	25 40%
Property	**2 62%**	2 71%

Mortality rate tables	2012	2011
Conventional Life Business	**60% AM/F00 ult**	100% AM/F92 ult
Life Deferred Annuities	**50% AM/F00 ult**	100% AM/F92 ult
Pension Deferred Annuities	**50% AM/F00 ult**	100% AM/F92 ult
Unitised with-profits Business	**60% AM/F00 ult**	100% A67/70 ult

Per policy expenses – regular premiums	2012	2011
Conventional Life Business	**£34.84**	£32 53
Pensions Deferred Annuities	**£45 34**	£42 06
Life Deferred Annuities	**£34.84**	£32 51
Unitised with-profits ISA	**£49.30**	£43 06
Unitised with-profits Bond	**£41 18**	£38 14

Notes to the Financial Statements continued

31 December 2012

25. Long-term insurance and investment contract liabilities valuation assumptions (continued)

Persistency - lapses, surrenders and paid up rates

A review of persistency is carried out annually Assumptions are adjusted where necessary to reflect more recent experience as evidenced in the persistency trend analysis or to reflect expected future trends as a result of anticipated future events

Options and guarantees

The provisions held in respect of guaranteed annuity options are determined on a market consistent basis The total amount provided in respect of the future costs of the guaranteed annuity options was £92 3m (2011 £86 6m)

Bonuses

The cost of bonuses incurred during the year ended 31 December 2012 was £15 9m (2011 £21 0m) of which £0 7m (2011 £0 8m) was included in the long-term insurance contract liabilities and £15 2m (2011 £20 2m) was included in gross benefits and claims paid in the Statement of Comprehensive Income

ii) Non participating business

Interest rate	2012	2011
Non-profits assurances	**1.68%**	1 44%
Non-profits general deferred annuities	**1.68%**	1 44%
Annuities in Payment (post 31/12/91)	**1 68%**	1 44%
Annuities in Payment (other)	**2 10%**	1 80%
Pension Deferred Annuities	**2 10%**	1 80%

Mortality rate tables	2012	2011
Non-profits assurances	**72 0% AM/F00 ult**	115% AM/F92 ult
Non-profits general deferred annuities	**42 5% AM/F00 ult**	85% AM/F92 ult
Annuities in Payment (Male)	**61.2% as 2011 basis up to 2007, then CMI_2009, with a long-term improvement rate of 2 0%**	61 2% IML00 with improvements of 120% medium cohort over 2000 to 2004 and future improvements 120% medium cohort subject to a floor of 1 5%
Annuities in Payment (Female)	**72 3% as 2011 basis up to 2007, then CMI_2009, with a long-term improvement rate of 1 5%**	72 3% IFL00 with improvements of greater of 90% of medium cohort and CMIR17 over 2000 to 2004 and future improvements of greater of 90% medium cohort and CMIR17 subject to a floor of 1 5%
Pension Deferred Annuities	**42 5% AM/F00 ult**	85% AM/F92 ult

Appropriate adjustments were made to the standard mortality tables to take account of actual experience and publicly available market data

The provision for linked and unitised with-profits contracts is equal to the value of the units A non-unit liability consisting mainly of a sterling reserve calculated by carrying out cash flow projections on appropriate bases is included within the liability

Options and guarantees

There are no significant options or guarantees in the non participating business

iii) Linked fund

The provision for unit linked assurances is equal to the value of the assets to which the contracts are linked There are two products included within the linked fund, one is classified as an insurance product and the liability is included within the life and pension unit linked insurance contract liabilities, the other is classified as an investment product and the liability is included within the investment contract liabilities

Interest rate	2012	2011
Unit linked assurances	**1 68%**	1 44%

Mortality rate tables	2012	2011
Unit linked assurances	**72% AM/F00 ult**	115% AM/F92 ult

Notes to the Financial Statements continued

31 December 2012

Fixed assets and investments

This section gives detail on the tangible, intangible and investment assets of the Society and Group that are used to generate profit for the business

26. Intangible assets

Accounting for goodwill and other intangible assets

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate at the acquisition date and is included in intangible assets Goodwill is reviewed for impairment at the end of the first full year of acquisition Thereafter, it is tested at each Statement of Financial Position date for impairment against the recoverable amount (being the higher of value in use or fair value less cost) of the relevant cash generating unit and carried in the Statement of Financial Position at cost less accumulated impairment losses Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold

Goodwill arising on acquisitions prior to 1998 has been eliminated against the Unallocated divisible surplus This goodwill would be recognised in the Statement of Comprehensive Income should there be a subsequent disposal of the business to which it relates

Other intangibles

Where an acquisition takes place that gives access to existing customers, distribution channels or the right to charge for investment or policy administration services, the present value of these is recognised as an intangible asset

The carrying value of the asset is amortised, on a straight line basis over its expected economic life, and is assessed annually for impairment

The expected economic life of other intangibles carried by the Group is determined by reference to acquired business, considering factors such as the remaining terms of agreements, the normal lives of related products and the competitive position, and lies within the range of 10 to 20 years

Present value of acquired in-force business (PVIF)

On acquisition of a portfolio of long-term insurance contracts, the net present value of the Group s interest in the expected cash flows of the in-force business is capitalised in the Statement of Financial Position as an asset and is amortised, in line with the original expected run-off of 20 years, based on the anticipated lives of the related contracts

The carrying value of the asset is assessed annually using current assumptions in order to determine whether any impairment has arisen, compared to the amortised acquired value

Any amortisation or impairment charge is recorded in the Statement of Comprehensive Income within other operating and administrative expenses

Significant accounting estimates and judgements

The Group determines whether goodwill and other intangible assets are impaired at least on an annual basis This requires an estimation of the recoverable amount of the cash generating unit to which the goodwill is allocated The Group has allocated the goodwill to two single cash generating units based on the key operating segments of the Group

Impairment testing of goodwill

Goodwill is reviewed annually for impairment, or more frequently when there are indicators that impairment may have occurred, by comparing the carrying value to its recoverable amount The recoverable amount of the cash generating unit is based on value-in-use calculations The calculations are based upon discounting expected pre-tax cash flows at a risk-adjusted interest rate appropriate to the cash generating unit, the determination of both of which requires the exercise of judgement The estimation of pre-tax cash flows is sensitive to the periods for which forecasts are available and to assumptions regarding the long-term sustainable cash flows While forecasts are compared with actual performance and external economic data, expected cash flows reflect management's view of future performance

Details of the key assumptions used in the estimation of the recoverable amounts and the carrying value at the reporting date are contained at the end of this note

Notes to the financial statements continued

31 December 2012

26. Intangible assets (continued)

Group	Goodwill £m	Other intangible assets £m	PVIF £m	Total £m
Cost·				
At 1 January 2012	236 0	95 1	63 4	394 5
Additions	-	-	-	-
Disposals	-	-	-	-
Increase in buy out value (see Note 40)	2 4	-	-	2 4
At 31 December 2012	**238 4**	**95 1**	**63 4**	**396 9**
Accumulated amortisation				
At 1 January 2012	20 6	68 3	44 1	133 0
Charge for the year	-	8 1	3 9	12 0
Disposals	-	-		-
Impairment in year	-	-	-	-
At 31 December 2012	**20 6**	**76 4**	**48 0**	**145 0**
Net book value at 31 December 2012	**217 8**	**18 7**	**15 4**	**251 9**
Cost				
At 1 January 2011	230 7	95 1	63 4	389 2
Increase in buy out value	5 3	-	-	5 3
At 31 December 2011	236 0	95 1	63 4	394 5
Accumulated amortisation				
At 1 January 2011	20 6	59 8	39 6	120 0
Charge for the year	-	8 5	4 5	13 0
At 31 December 2011	20 6	68 3	44 1	133 0
Net book value at 31 December 2011	215 4	26 8	19 3	261 5

Present Value of acquired In-Force business (PVIF) is amortised in line with the original expected run off of 20 years, ending in 2018, based on the market value of the life policies

Other intangible assets comprise the value of the future benefit derived from the customer bases of RNPFN (in the Society), Britannia Road Rescue and Highway, and the value of the Tomorrow/Retirement Solutions distribution channel

Amortisation of £12 0m (2011 £13 0m) is presented within Other operating and administrative expenses in the Statement of Comprehensive Income There is no impairment in 2012 (2011 £nil)

Goodwill has been allocated to the individual cash generating units which are based on the key segments of the Group as follows

	Group 2012 £m	Group 2011 £m
Long-term insurance business	**66 7**	66 7
General insurance business	**171 7**	169 3
	238 4	236 0

Notes to the financial statements continued

31 December 2012

26. Intangible assets (continued)

Society	Other intangible assets £m
Cost	
At 1 January 2012	50 9
At 31 December 2012	**50 9**
Accumulated amortisation	
At 1 January 2012	46 3
Charge for the year	4 6
At 31 December 2012	**50 9**
Net book value at 31 December 2012	**-**
Cost	
At 1 January 2011	50 9
At 31 December 2011	50 9
Accumulated amortisation	
At 1 January 2011	41 6
Charge for the year	4 7
At 31 December 2011	46 3
Net book value at 31 December 2011	4 6

Key assumptions used in the annual impairment testing of intangible assets

The key assumptions used for impairment testing are set out below for both the long-term insurance business and the general insurance business The long-term insurance business incorporates both the Heritage and Life businesses

Long-term insurance business

The recoverable amount of the long-term insurance business has been determined using cash flow predictions based on financial plans approved by management covering a five-year period, with a terminal growth rate of 2% applied thereafter The forecast cash flows have been discounted at a pre-tax rate of 10% Based on the above assumptions, the recoverable amount exceeded the carrying amount including goodwill by £156 8m

A two percentage point increase in the discount rate would reduce the recoverable amount by £52 3m, the discount rate would need to be increased to 23% to reduce the recoverable amount to zero

A reduction in the forecast cash flows of 10% per annum would reduce the recoverable amount by £55 7m, the forecast cash flows would need to be reduced by 25% per annum to reduce the recoverable amount to zero

General insurance business

The recoverable amount of the general insurance business has been determined using cash flow predictions based on financial plans approved by management covering a five-year period, with a terminal growth rate of 2% applied thereafter The forecast cash flows have been discounted at a pre-tax rate of 10% Based on the above assumptions, the recoverable amount exceeded the carrying amount including goodwill by £755 1m

A two percentage point increase in the discount rate would reduce the recoverable amount by £285 9m, the discount rate would need to be increased to 20% to reduce the recoverable amount to zero

A reduction in the forecast cash flows of 10% per annum would reduce the recoverable amount by £151 4m, the forecast cash flows would need to be reduced by 50% per annum to reduce the recoverable amount to zero

Notes to the financial statements continued

31 December 2012

27. Property and equipment

Accounting for property and equipment

Operational property and equipment are held at cost less accumulated depreciation 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 Both property and equipment are depreciated on a straight line basis over their estimated useful lives The periods used are as follows

Freehold buildings and finance lease property*	50 years
Leasehold property enhancements*	10 years or lease term if shorter
Fixtures, fittings and motor vehicles	3 to 10 years
IT systems (spend over £1m)	3 years

Provision is made for any impairment in property and equipment

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each Statement of Financial Position date

Assets under construction represent the cost of assets under development These assets are not depreciated, the total cost is transferred to the appropriate asset class on completion and then depreciated over their estimated useful lives

*These are properties used by the Group for operational purposes and are not investment properties which are dealt with in Note 28

Group	Freehold and leasehold property £m	Leasehold property enhancements £m	Fixtures, fittings and motor vehicles £m	IT systems £m	Assets under construction £m	Total £m
Cost						
At 1 January 2012	41 1	9 1	7 9	2 1	-	60 2
Additions	0 2	3 5	2 3	1 0	-	7 0
Disposals	-	(0 5)	(0 1)	-	-	(0 6)
At 31 December 2012	**41 3**	**12 1**	**10 1**	**3 1**	**-**	**66 6**
Accumulated depreciation						
At 1 January 2012	32 1	3 6	3 7	0 2	-	39 6
Provided in the year	1 0	1 0	0 7	0 7	-	3 4
Disposals	-	(0 2)	(0 1)	-	-	(0 3)
At 31 December 2012	**33 1**	**4 4**	**4 3**	**0 9**	**-**	**42 7**
Net book value at 31 December 2012	**8 2**	**7 7**	**5 8**	**2 2**	**-**	**23 9**
Cost						
At 1 January 2011	41 1	7 9	7 4	-	0 9	57 3
Additions	-	1 2	0 7	1 2		3 1
Disposals	-	-	(0 2)	-	-	(0 2)
Transfers	-	-	-	0 9	(0 9)	-
At 31 December 2011	41 1	9 1	7 9	2 1	-	60 2
Accumulated depreciation						
At 1 January 2011	31 1	2 8	3 3	-	-	37 2
Provided in the year	1 0	0 8	0 6	0 2	-	2 6
Disposals	-	-	(0 2)	-	-	(0 2)
At 31 December 2011	32 1	3 6	3 7	0 2	-	39 6
Net book value at 31 December 2011	9 0	5 5	4 2	1 9	-	20 6

Included within the Freehold and leasehold property category are assets held under finance leases with a net book value of £5 2m (2011 £5 7m)

During 2011 £0 9m of assets were transferred from Assets under construction to IT systems representing the development cost of the claims centre computer system that became operational in 2011

Notes to the financial statements continued

31 December 2012

27. Property and equipment (continued)

Society	Leasehold property enhancements £m	Fixtures, fittings and motor vehicles £m	Total £m
Cost			
At 1 January 2012	4 7	6 0	10 7
Additions	1 6	1 5	3 1
Disposals	(0 5)	(0 1)	(0 6)
At 31 December 2012	**5 8**	**7 4**	**13 2**
Accumulated depreciation			
At 1 January 2012	2 3	3 4	5 7
Provided in the year	0 4	0 4	0 8
Disposals	(0 2)	-	(0 2)
At 31 December 2012	**2 5**	**3 8**	**6 3**
Net book value at 31 December 2012	**3 3**	**3 6**	**6 9**
Cost			
At 1 January 2011	4 5	6 0	10 5
Additions	0 2	0 2	0 4
Disposals	-	(0 2)	(0 2)
At 31 December 2011	4 7	6 0	10 7
Accumulated depreciation			
At 1 January 2011	1 9	3 1	5 0
Provided in the year	0 4	0 4	0 8
Disposals	-	(0 1)	(0 1)
At 31 December 2011	2 3	3 4	5 7
Net book value at 31 December 2011	2 4	2 6	5 0

Notes to the financial statements continued

31 December 2012

28. Investment properties

Accounting for investment properties
Investment properties are freehold and leasehold land and buildings held for long-term rental yields and capital growth They are held at fair value and changes in fair value are recorded as fair value gains or losses in the Statement of Comprehensive Income Fair value is determined annually by independent professional valuers based on market conditions

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Freeholds	**129 1**	183 8	**96 1**	115 3
Long leaseholds	**35 6**	36 1	**35 6**	36 1
	164 7	219 9	**131 7**	151 4

All investment properties held by the Group and the Society are occupied by third party tenants All properties occupied by Group undertakings are shown separately within Note 27

The market value movements in the year on land and buildings were

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Balance at 1 January	**219 9**	315 4	**151 4**	246 6
Additions	**0 2**	12 5	**0 2**	2 9
Disposals	**(49 1)**	(89 2)	**(16 4)**	(89 2)
Net fair value adjustment	**(6 3)**	(18 8)	**(3 5)**	(8 9)
Balance at 31 December	**164 7**	219 9	**131 7**	151 4
Due within one year	**47 5**	-	**14 5**	-
Over one year	**117 2**	219 9	**117 2**	151 4
	164 7	219 9	**131 7**	151 4

Investment properties due within one year represent £33m of properties held within the Threadneedle UK Property Fund II ICVC that is in the process of being wound up (refer Note 45) and an additional property held directly by the Society that is in the process of being sold

All investment properties are valued annually at fair value They were valued as at 31 December 2012 by qualified professional valuers working for Colliers International (UK) Plc who are professional, third party, independent Chartered Surveyors All valuations were carried out in accordance with the RICS Appraisal and Valuation Standards

The Group and Society enter into operating leases for all investment properties All rents are payable in advance and the rental income arising during the year amounted to £8 1m (2011 £8 9m) for the Group and the Society, which is included in investment income

Non recoverable expenses are deducted from rental income for investment properties and amounted to £2 0m (2011 £1 8m) for the Group and the Society

Notes to the financial statements continued

31 December 2012

29. Investments in group undertakings

Accounting for investments in group undertakings

The subsidiaries are held in the Society's Statement of Financial Position at cost less any provision for impairment An assessment of the realisable value is made at the year end and, if the Directors assess that there has been a permanent fall in that value below the carrying value, a provision is made to bring the carrying value down to the assessed realisable value

Society	2012 £m	2011 £m
Shares in subsidiaries		
Cost less provisions at 1 January	**723 2**	748 3
Additions	**399 6**	4 0
Sale of LVGIG Group to subsidiary undertaking	**(484 6)**	-
Increase / (reduction) in buy out provision (refer to Note 40)	**2 4**	5 3
Impairment write-off	**(90 0)**	(34 4)
	550 6	723 2
Loan stock in subsidiaries		
Cost at 1 January	**234 4**	223 2
Additions	**300 3**	11 2
Redemption	**(183 0)**	-
	351 7	234 4
Shares and loan stock in subsidiaries at 31 December	**902 3**	957 6

During the year the Society sold its investment in Liverpool Victoria General Insurance Group Limited (LVGIG) to LV Capital PLC, a subsidiary undertaking at cost In addition the Society invested in £300m of loan notes issued by LV Capital PLC

The Society made capital contributions during 2012 of £nil to Liverpool Victoria General Insurance Group Limited (2011 £4m), these are disclosed within additions in the table above

The Society has examined the carrying value of its subsidiaries and concluded that a provision for impairment of £90m was necessary in regard to its investment in Liverpool Victoria Life Company Limited (2011 £28 1m), this impairment arose due to the payment of dividends to the Society thereby reducing the value of the company

Further details of the Group's loan stock are given in Note 47 and the Group's investments in Notes 43 and 44

Statements and Reviews
Our Businesses
Risk Management
Corporate Governance
Our Accounts

Notes to the financial statements continued

31 December 2012

Other assets and liabilities

This section describes the other assets and liabilities arising from the life insurance business within the Society and the life insurance and general insurance businesses within the Group

30. Insurance receivables

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Due from policyholders	**148 1**	135 1	**1 0**	3 8
Due from agents, brokers and intermediaries	**67 5**	74 8	**-**	-
Due from reinsurers	**11 7**	6 6	**11 6**	6 4
	227 3	216 5	**12 6**	10 2

Insurance receivables are all due within one year for both the Group and the Society

The carrying amounts disclosed above reasonably approximate fair value at the Statement of Financial Position date

31. Prepayments and accrued income

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Accrued dividends	**4 0**	3 5	**1 5**	1 1
Accrued interest	**82 3**	45 2	**52 7**	38 6
Other prepayments and accrued income	**20 3**	12 6	**10 1**	8 4
	106 6	61 3	**64 3**	48 1

Prepayment and accrued income balances are all due within one year for both the Group and the Society

32. Insurance payables

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Due to policyholders	**33 2**	30 1	**25 5**	30 1
Due to brokers and intermediaries	**0 4**	0 8	**0 4**	0 8
Due to reinsurers	**11 1**	10 7	**0 3**	0 7
	44 7	41 6	**26 2**	31 6

The carrying amounts disclosed above reasonably approximate fair value at the Statement of Financial Position date

33. Trade and other payables

Accounting for trade and other payables

Trade and other payables are recognised as they fall due They are measured initially at fair value and subsequently at amortised cost

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Trade payables	**15 8**	11 2	**15 4**	10 5
Amounts owed to group undertakings	**-**	-	**37 1**	37 7
Other taxes and social security costs	**31 3**	32 2	**9 4**	10 1
Other creditors	**49 8**	59 5	**15 8**	21 7
Deferred rental income	**3 3**	3 3	**2 6**	2 2
Finance lease liabilities	**5 0**	5 1	**-**	-
Accruals and deferred income	**88 5**	94 3	**55 9**	65 2
	193 7	205 6	**136 2**	147 4

The carrying amounts disclosed above reasonably approximate fair value at the Statement of Financial Position date

Notes to the financial statements continued

31 December 2012

Taxation

This section presents information relating to tax charge and movements in the corporation and deferred tax assets and liabilities held by the Society and Group.

34. Income tax expense

- Current income tax

Current income tax liabilities and assets are measured at the amount expected to be paid to or recovered from the taxation authorities The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the Statement of Financial Position date

- Deferred income tax

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the Statement of Financial Position date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised

a) Current year tax charge

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Current tax charge				
Current year	**20 0**	39 3	**8 5**	23 9
Adjustment in respect of prior years	**(2 5)**	5 4	**0 2**	6 6
Total current tax	**17 5**	44 7	**8 7**	30 5
Deferred tax				
Excess of depreciation	**0 2**	1 0	**(0.3)**	-
Adjustment in respect of prior years	**-**	(10 5)	**-**	(6 9)
Temporary differences	**12 8**	(7 5)	**5 0**	3 3
Tax losses	**3 8**	14 5	**-**	-
Total deferred tax	**16 8**	(2 5)	**4 7**	(3 6)
Total income tax expense	**34 3**	42 2	**13 4**	26 9

b) Reconciliation of tax charge

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Profit/(loss) before tax	**103 2**	(16 9)	**3 3**	(47 7)
Tax calculated at the average standard rate of corporation tax in the UK at 24 5% (2011 26 5%)	**25 3**	(4 5)	**0 8**	(12 7)
Income and expenses not subject to tax	**(1.8)**	13 2	**(2 7)**	1 7
Impact of change in UK corporation tax rate on deferred tax	**0 5**	0 7	**-**	-
Unprovided deferred tax asset	**(11 1)**	22 1	**(11 1)**	22 1
Transfer pricing	**-**	-	**2 5**	-
Policyholder tax	**23 9**	15 8	**23 7**	16 1
Adjustment to current tax charge in respect of prior years	**(2 5)**	5 4	**0 2**	6 6
Adjustment to deferred tax charge in respect of prior years	**-**	(10 5)	**-**	(6 9)
Total charge	**34 3**	42 2	**13 4**	26 9

The standard rate of Corporation Tax in the UK changed from 26% to 24% with effect from 1 April 2012 Accordingly, the profits for this accounting period are taxed, where applicable, at an effective rate of 24 5%

35. Corporation tax asset

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Corporation tax receivable	**-**	-	**2 0**	-
	-	-	**2 0**	-

Notes to the financial statements continued

31 December 2012

36. Deferred tax asset

	Group £m	Society £m
Balance at 1 January 2012	31 0	17 7
Amounts recorded in the Statement of Comprehensive Income	(16 8)	(4 7)
Balance at 31 December 2012	**14 2**	**13 0**

i) Analysis of deferred taxation temporary differences	Group 2012 £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Excess of depreciation	**3 0**	3 0	**0 8**	0 5
Temporary differences on expenses	**11 4**	18 5	**12.2**	19 2
Temporary differences arising on consolidation	**(1 6)**	(2 3)	-	-
Temporary differences on unrealised gains	**1 4**	8 0	-	(2 0)
Tax losses	-	3 8	-	-
Deferred tax asset	**14 2**	31 0	**13 0**	17 7

ii) Deferred taxation asset not recognised	Group 2012 £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Temporary differences on expenses	**22 3**	9 6	**22 3**	9 6
Temporary differences on unrealised gains	**(14 9)**	(4 8)	**(14 9)**	(4 8)
Temporary difference for changes in actuarial base	**0 8**	(5 9)	**0 8**	(5 9)
Tax losses unrecognised	**19 2**	33 6	**13 9**	27 6
	27 4	32 5	**22 1**	26 5

The value of deferred tax assets expected to be recovered after more than 12 months is £7 6m in the Group (2011 £9 8m) and £7 7m in the Society (2011 £12 4m)

Deferred tax balances have been measured taking into account the change in the rate of UK Corporation Tax from 24% to 23% This change was substantively enacted on 3 July 2012 and will be effective from 1 April 2013

In addition to the changes in rates of Corporation Tax disclosed above, a number of further changes to the UK Corporation Tax system were announced in the 2013 draft Finance Bill and the March 2013 Budget Statement Further reductions to the main rate are proposed to reduce the rate to 21% by 1 April 2014 and then to 20% by 1 April 2015 These further changes had not been substantively enacted at the balance sheet date and, therefore, are not included in these financial statements Furthermore, the Finance Act 2012 introduced changes to the taxation of UK life companies, which will take effect from 1 January 2013 These changes have been taken into account in calculating the deferred tax position of the Society as at 31 December 2012 The impact of these changes has been to reduce the value of deferred tax assets by £5 1m when compared to the value of these assets had the changes not taken place

The valuation and recoverability of deferred tax assets relating to capital allowances in excess of depreciation, differences on expenses and gains and tax losses, is dependent on the availability of future taxable profits within the Society and Group Management forecasts currently support the future recoverability of the deferred tax asset recognised in the balance sheet as at 31 December 2012

37. Corporation tax liability

	Group 2012 £m	Group 2011 £m	Society 2012 £m	Society 2011 £m
Corporation tax	**7 6**	28 4	-	13 0
	7 6	28 4	-	13 0

Notes to the financial statements continued

31 December 2012

Employee benefits

This section details the costs and commitments associated with employing our staff

38. Employee benefits expense

Accounting for staff costs under IAS19

The Society and Group applies IAS 19 Employee benefits in its accounting for staff costs

Short-term employee benefits

Salaries, accrued bonuses and social security costs are recognised over the period in which the employees provide the services to which the payments relate

Post retirement benefits

The accounting policies and significant accounting judgements relating to pension benefits are disclosed within Note 39

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Wages and salaries	**181 9**	172 7	**181 9**	172 7
Social security costs	**17 2**	16 1	**17 2**	16 1
Defined benefit and defined contribution pension costs	**17 3**	20 9	**17 3**	20 9
	216 4	209 7	**216 4**	209 7

The number of employees during the year, including executive directors, calculated on a monthly average basis, was as follows

	Group		Society	
	2012 Number	2011 Number	**2012 Number**	2011 Number
Member and customer contact	**3,782**	3,269	**3,782**	3,269
Administration	**1,670**	1,513	**1,670**	1,513
	5,452	4,782	**5,452**	4,782

Notes to the financial statements continued
31 December 2012

39. Pension benefit asset / (obligation)

Accounting for pension benefits under IAS19

For defined benefit schemes, the net surplus or deficit is calculated annually with the assets measured at the fair value at the Statement of Financial Position date and the liabilities discounted at the rate of return available on high quality corporate bonds The net surplus, to the extent recoverable, or deficit is recognised as a pension benefit asset or liability in the Statement of Financial Position

The pension cost for the schemes is analysed between current service cost, past service cost and net return on pension scheme assets Current service cost is the actuarially calculated present value of the benefits earned by the active employees in each period Past service costs, relating to employee service in prior periods arising in the current period as a result of the introduction of, or improvement to, retirement benefits, are recognised in Other operating and administrative expenses on a straight-line basis over the period in which the increases in benefits vest or are earned

All movements other than actuarial gains and losses in respect of the pension benefit obligation are recognised in other operating and administrative expenses in the Statement of Comprehensive Income Actuarial gains and losses are recognised in the Statement of Comprehensive Income after profit/(loss) before tax and are disclosed net of tax

Contributions to defined contribution schemes are recognised as employee benefit expenses when they are due

Significant accounting estimates and judgements

The valuations of the pension benefit obligations for the two defined benefit schemes are determined using actuarial valuations These involve making assumptions about discount rates, expected future returns on assets, future salary increases, longevity and future pension increases Due to the long-term nature of these obligations, the estimates are subject to significant uncertainty

Details of the principal assumptions used for each of the defined benefit schemes are disclosed within the valuations of the individual schemes disclosed in sections (ii) and (iii) below

i) Summary

Pension benefit asset/(obligation)

	2012			2011		
	LV Scheme £m	Ockham £m	Total £m	LV Scheme £m	Ockham £m	Total £m
Asset	-	-	-	108 1	-	108 1
Obligation	**(7 7)**	**(2 5)**	**(10 2)**	-	(1 2)	(1 2)
	(7 7)	**(2 5)**	**(10 2)**	108 1	(1 2)	106 9

Actuarial net (loss)/gain

	2012			2011		
	LV Scheme £m	Ockham £m	Total £m	LV Scheme £m	Ockham £m	Total £m
Actuarial net (loss) / gain	**(138 0)**	**(7 5)**	**(145 5)**	66 5	3 9	70 4
Income tax credit/(expense)	-	-	-	-	(0 7)	(0 7)
Amount charged to total comprehensive income	**(138 0)**	**(7 5)**	**(145 5)**	66 5	3 2	69 7
Cumulative actuarial gain/(loss) recognised in the Statement of Comprehensive Income	**44 0**	**(0 7)**	**43 3**	182 0	6 8	188 8

Notes to the financial statements continued

31 December 2012

39. Pension benefit asset/(obligation) (continued)

ii) LV Scheme

a) Information about the scheme

The Society is responsible for the LV= Employee Pension Scheme (LV Scheme), a defined benefit pension scheme The scheme closed to new entrants on 31 December 2009 and on 1 November 2012 it was announced that the scheme would close to future accrual for existing members from July 2013 Accordingly allowance has been made for the closure to future accrual within the 31 December 2012 figures with a curtailment gain being recognised as a remeasurement event at the year end reporting date

On 6 December 2012 the Trustees of the LV Scheme entered into a Longevity Swap to mitigate the future mortality risk Further details on this are included within the Business Review section

From 1 January 2011 the rate of increase in deferred pensions changed from being related to RPI to CPI The impact of this was a reduction in the calculation of the liabilities

b) Net Statement of Financial Position

	2012 £m	2011 £m
Present value of defined benefit obligation	**(1,059 0)**	(942 0)
Fair value of plan assets	**1,051 3**	1,050 1
Pension benefit (obligation)/asset at the end of the year	**(7 7)**	108 1

The movement in the defined benefit obligation over the year is as follows	2012 £m	2011 £m
Beginning of year	**942 0**	854 4
Current service cost	**22 0**	19 1
Interest cost	**44 4**	46 2
Gain on curtailment	**(13 0)**	-
Actuarial losses	**104 3**	64 4
Benefits paid	**(37 1)**	(39 2)
Past service cost	**0 1**	0 5
Administrative expenses paid	**(3 7)**	(3 4)
End of year	**1,059.0**	942 0

The movement in the fair value of plan assets over the year is as follows	2012 £m	2011 £m
Beginning of year	**1,050.1**	870 3
Expected return on plan assets	**42.9**	47 9
Actuarial (losses)/gains	**(33 7)**	130 9
Employer contributions	**32 8**	43 6
Benefits paid	**(37 1)**	(39 2)
Administrative expenses paid	**(3 7)**	(3 4)
End of year	**1,051.3**	1,050 1

Notes to the financial statements continued

31 December 2012

39. Pension benefit asset/(obligation) (continued)

ii) LV Scheme (continued)

c) Amounts recognised in the Statement of Comprehensive Income	2012 £m	2011 £m
Current service cost	**22 0**	19 1
Interest cost	**44 4**	46 2
Expected return on assets	**(42 9)**	(47 9)
Curtailment gain	**(13 0)**	
Past service cost	**0 1**	0 5
Amount charged to income	**10 6**	17 9
Actuarial net loss/(gain)	**138 0**	(66 5)
Total amount charged/(credited) to comprehensive income	**148 6**	(48 6)

The actual return on plan assets was £9 2m (2011 £178 8m)

d) Principal assumptions used	2012	2011
Discount rate	**4 1%**	4 7%
Rate of salary increase	**3 0%**	3 65%
Expected return on plan assets	**n/a**	4 1%
RPI Inflation	**3 0%**	2 9%
CPI Inflation	**2 0%**	2 0%
Pension increases for in-payment benefits		
- RPI price inflation capped at 5% pa, floor of 3% pa	**3 5%**	3 5%
- RPI price inflation capped at 5% pa	**3 0%**	2 9%
- RPI price inflation capped at 2 5% pa	**2.2%**	2 1%
- CPI price inflation capped at 3 0% pa	**1.9%**	1 9%
Pension increases for deferred benefits		
- pre 6 April 2009 accrual	**2.0%**	2 0%
- post 6 April 2009 accrual	**2 0%**	2 0%
Scheme member valuation date	**31 March 2012**	31 March 2009

Mortality for members is assumed to follow the tables below as at 31 December 2012

Pre-retirement mortality Deferred pensioners		
- Males	1NMA x 0 95 table	1NMA x 0 95 table
- Females	1NFA x 0 98 table	1NFA x 0 98 table
Post-retirement mortality Non-pensioners		
- Males	LV specific tables from Club Vita	1NMA x 0 95 table
- Females (former employees)	LV specific tables from Club Vita	1NFA x 0 98 table
- Females (dependants)	LV specific tables from Club Vita	1NFA x 1 12 table
Post-retirement mortality current pensioners and dependants		
- Males	LV specific tables from Club Vita	1NMA x 0 85 table
- Females (former employees)	LV specific tables from Club Vita	1NFA x 0 88 table
- Females (dependants)	LV specific tables from Club Vita	1 NFA x 1 02 table

In all cases as at 31 December 2012 CMI Core 2011 projections with a long term trend of 1 25% have been applied (31 December 2011 medium cohort improvements have been applied from 2002 onwards and from 2009 a minimum annual rate of improvement of 1 25%pa has been applied)

Notes to the financial statements continued

31 December 2012

39. Pension benefit asset/(obligation) (continued)

ii) LV Scheme (continued)

e) Sensitivity analysis: Impact on defined benefit obligation of making changes to key assumptions

	Change in assumption	Impact on defined benefit obligation
Discount rate	Increase by 0 25%	Decrease by £48 0m (4 6%)
Inflation rate	Increase by 0 25%	Increase by £30 5m (2 9%)
Cash commutation	Nil	Increase by £16 1m (1 5%)
Mortality improvements long term rate	Increase by 0 25%	Increase by £14 0m (1 3%)

f) Plan asset information

Plan assets are comprised as follows

	Allocation percentage 2012	Allocation percentage 2011
Equities	**14 5%**	11 3%
Debt securities	**73 4%**	69 0%
Real estate/property	**8 6%**	8 9%
Other	**3 5%**	10 8%
Total	**100 0%**	100 0%

Expected contributions to the scheme for the year ending 31 December 2013 are £20m

g) Historical disclosure information	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Asset experience					
Asset (gains)/losses during year	**33.7**	(130 9)	(63 9)	(30 4)	107 6
Liability experience					
Obligation (gains)/losses during year	**17.2**	3 2	(14 6)	(15 5)	-
Funded status					
Defined benefit obligation	**(1,059 0)**	(942 0)	(854 4)	(813 9)	(667 1)
Fair value of assets	**1,051.3**	1,050 1	870 3	729 7	671 7
Net asset/(obligation)	**(7 7)**	108 1	15 9	(84 2)	4 6

h) Defined contribution pension schemes

New employees are eligible to join the defined contribution scheme The assets of this scheme are held separately from those of the Group in an independently administered fund The Group's contribution under this scheme amounted to £5 8m (2011 £4 2m)

Notes to the financial statements continued

31 December 2012

39. Pension benefit asset/(obligation) (continued)

iii) Ockham Pension Scheme

a) Information about the scheme

The Society is responsible for the Ockham Pension Scheme, a defined benefit scheme that is closed to new entrants

b) Net Statement of Financial Position	2012 £m	2011 £m
Present value of defined benefit obligation	**(117 5)**	(107 0)
Fair value of plan assets	**115 0**	105 8
Pension benefit obligation at the end of the year	**(2 5)**	(1 2)

The movement in the defined benefit obligation over the year is as follows	2012 £m	2011 £m
Beginning of year	**107.0**	97 6
Interest cost	**4 9**	5 2
Actuarial losses	**9.6**	4 8
Benefits paid	**(4 0)**	(3 7)
Past service cost	**-**	3 1
End of year	**117 5**	107 0

The movement in the fair value of plan assets over the year is as follows	2012 £m	2011 £m
Beginning of year	**105 8**	88 8
Expected return on plan assets	**4 0**	5 0
Actuarial gains	**2 1**	8 7
Employer contributions	**7 1**	7 0
Benefits paid	**(4 0)**	(3 7)
End of year	**115 0**	105 8

c) Amounts recognised in the Statement of Comprehensive Income	2012 £m	2011 £m
Interest cost	**4 9**	5 2
Expected return on assets	**(4 0)**	(5 0)
Past service cost	**-**	3 1
Amount charged to income	**0 9**	3 3
Actuarial net loss/(gain)	**7 5**	(3 9)
Total amount charged/(credited) to comprehensive income	**8 4**	(0 6)

The actual return on plan assets was £6 1m (2011 £13 7m)

Notes to the financial statements continued

31 December 2012

39. Pension benefit asset/(obligation) (continued)

iii) Ockham Pension Scheme (continued)

d) Principal assumptions used	**2012**	2011
Discount rate	**4 1%**	4 7%
Rate of salary increase	**3 00%**	3 65%
Expected return on plan assets	**n/a**	3 7%
Pension increases		
– linked to inflation	**3 0%**	2 9%
– fixed rate	**5 0%**	5 0%
Price inflation		
– RPI	**3 0%**	2 9%
– CPI	**2 0%**	2 0%

Mortality rate assumptions are based on the same mortality tables as disclosed within the LV Scheme

e) Sensitivity analysis Impact on defined benefit obligation of making changes to key assumptions

	Change in assumption	**Impact on defined benefit obligation**
Discount rate	Increase by 0 25%	Decrease by £4 8m (4 1%)
Inflation rate	Increase by 0 25%	Increase by £3 3m (2 8%)
Cash commutation	Nil	Increase by £3 7m (3 2%)
Mortality improvements long term rate	Increase by 0 25%	Increase by £1 6m (1 4%)

f) Plan asset information

Plan assets are comprised as follows

	Allocation percentage 2012	Allocation percentage 2011
Equities	**41 2%**	8 3%
Debt securities	**29 0%**	63 9%
Derivative swaps	**14 9%**	16 8%
Cash	**3 6%**	4 1%
Property	**0 8%**	0 7%
Other	**10 5%**	6 2%
Total	**100 0%**	100 0%

Expected contributions to the scheme for the year ending 31 December 2013 are £7m

g) Historical disclosure information	**2012 £m**	2011 £m	2010 £m	2009 £m
Asset experience				
Asset gains during year	**(2 1)**	(8 7)	(6 5)	(6 2)
Liability experience				
Obligation loss during year	**2 0**	-	1 1	3 7
Funded status				
Defined benefit obligation	**(117 5)**	(107 0)	(97 6)	(88 6)
Fair value of assets	**115 0**	105 8	88 8	75 2
Net obligation	**(2 5)**	(1 2)	(8 8)	(13 4)

Notes to the financial statements continued

31 December 2012

Provisions, contingent liabilities and commitments

This section describes the provisions, contingent liabilities and commitments of the Society and Group arising from the ongoing life and general insurance businesses and the exit from the banking and asset management businesses in prior years

40. Provisions

Accounting for provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated Where the Group expects some or all of a provision to be reimbursed it is recognised as a separate asset when the reimbursement is certain Provisions are measured at the present value of the expenditure required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation

The expense relating to provisions is presented in the Statement of Comprehensive Income

Onerous contracts

A provision is made for onerous contracts in which the unavoidable costs of meeting the obligation exceed the expected future economic benefits

Movement during the year on provisions

	Group				Society			
	Buy out payments £m	PPI provision £m	Other provisions £m	Total £m	Buy out payments £m	PPI provision £m	Other provisions £m	Total £m
Balance at 1 January 2012	38 6	6.6	10 3	55 5	38 6	6 6	6 8	52.0
Charge to the Statement of Comprehensive Income	-	15.0	3 3	18 3	-	15 0	3 0	18.0
Capitalised within goodwill	2 4	-	-	2 4	2 4	-	-	2.4
Utilised during the year	-	(8.2)	(2 0)	(10 2)	-	(8 2)	(1 1)	(9 3)
Balance at 31 December 2012	**41.0**	**13 4**	**11 6**	**66 0**	**41 0**	**13 4**	**8.7**	**63 1**

Other provisions relate to

	Group		Society	
	2012 £m	2011 £m	2012 £m	2011 £m
Employer taxes	**5 7**	5 3	**5 7**	5 3
Onerous contracts on property leases	**3 0**	1 8	**2 1**	0 4
Compensation payable on customer complaints	**2 0**	1 9	-	-
Other	**0 9**	1 3	**0 9**	1 1
	11 6	10 3	**8 7**	6 8

The buy out payments provision relates to the acquisition in 2006 by the Society of 95% of LV Insurance Management Limited (then known as ABC Insurance Solutions Limited) The 2006 contract provides for the Society to purchase the remaining 5% of LV Insurance Management Limited from its vendors, who include John O'Roarke, for a price based on the market value of the general insurance business at 31 December 2012 The consideration under this contract is being determined but was provisioned on 31 December 2012 at £41m Mr O'Roarke has a 22% interest in this liability

The payment protection insurance (PPI) provision is held to cover future payments in respect of claims relating to PPI policies potentially mis-sold to customers Following a review of outstanding PPI claims carried out during the year LV= increased the provision by £15m to cover the costs of expected future redress and administration At 31 December 2012, following payments made during the year of £8 2m, the provision was £13 4m Given the assumptions made it is expected that up to £10m of payments will be set against this provision during 2013, with the remainder of the provision utilised within five years

There are a large number of inter-dependent assumptions underpinning the PPI provision When considering the key assumptions separately, the most significant driver of the provision is complaint flow If the level of complaints were 10% higher (lower) than the estimated level for all policies, assuming no change in other assumptions, then the provision would have increased (decreased) by approximately £1 2m

The Group will re-evaluate the assumptions underlying its analysis at each reporting date as more information becomes available

Notes to the financial statements continued

31 December 2012

41. Contingent liabilities

Accounting for contingent liabilities

Contingent liabilities are disclosed if there is a possible future obligation as a result of a past event, or if there is a present obligation as a result of a past event but either a payment is not probable or the amount cannot be reasonably estimated.

The Society has granted a contingent loan facility to the RNPFN fund, a closed fund within the Group, up to a maximum of £100m, to be used in the event of a shortfall in the capital resources of that fund No drawdown of this facility is anticipated The Society has also granted a capital facility of £20m to the board of Liverpool Victoria General Insurance Group Limited to be used in the event of a shortfall in the capital solvency

As part of the arrangements whereby the Society transferred responsibility for the management of its investment portfolio to Threadneedle Asset Management Ltd and Threadneedle Investment Services Ltd ("Threadneedle"), Liverpool Victoria Portfolio Managers Ltd ("LVPM") resigned, and Threadneedle was appointed, as the Authorised Corporate Director ("ACD") of the LV= Property OEIC Simultaneous with the change in ACD, the Society provided an indemnity to Threadneedle for any losses incurred by Threadneedle as a result of any actual or suspected mis-pricing of the LV= Property OEIC by LVPM, including any costs of rectification or investor compensation No claims have been made under this indemnity

42. Commitments

Accounting for assets held under leases

Where assets are financed by leasing arrangements and the risks and rewards are substantially transferred to the Group, such finance leases are treated as if the assets had been purchased outright and the corresponding liability to the lessor is included as an obligation in trade and other payables Depreciation on leased assets is charged to the Statement of Comprehensive Income on a straight line basis over the lower of the term of the lease or its estimated useful life The capital element on finance leases is shown in the property and equipment note

Lease payments are treated as consisting of capital and interest elements and the interest is charged to the Statement of Comprehensive Income

All other leases are operating leases and the costs in respect of operating leases are charged on a straight line basis over the lease term The value of any lease incentive received to take on an operating lease (for example, rent free periods) is recognised as deferred income and is released over the life of the lease

a) Capital commitments

	Group		Society	
	2012 £m	**2011 £m**	**2012 £m**	**2011 £m**
Authorised and contracted commitments payable after 31 December not provided for in respect of				
– property investments	**0 7**	1 4	**0 7**	1 4
– other financial investments	**35 2**	49 5	**35 2**	49 5
– property and equipment	**-**	0 9	**-**	0 9
	35 9	51 8	**35 9**	51 8

Notes to the financial statements continued

31 December 2012

42. Commitments (continued)

b) Operating lease commitments

The Group leases various properties under non-cancellable operating lease agreements The leases have varying terms, escalation clauses and renewal rights The future aggregate minimum lease payments net of income under non-cancellable operating leases are as follows

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Within one year	**6 7**	6 7	**4 8**	5 0
Between one and five years	**19 4**	19 6	**14 3**	13 8
Over five years	**3 3**	5 7	**2 1**	3 3
	29 4	32 0	**21 2**	22 1

The Group has entered into commercial subleases for some of its properties that are unoccupied These leases have varying terms and escalation clauses Where these subleases are insufficient to cover the Group's operating lease agreements an onerous contract provision for unused premises is set up The future aggregate minimum sublease payments expected to be received under operating subleases is as follows

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Within one year	**1 0**	0 4	**0 7**	0 1
Between one and five years	**2 6**	0 7	**2 3**	-
	3 6	1 1	**3 0**	0 1

c) Finance lease commitments

It is the Group's policy to lease certain of its properties under finance leases The average lease term is 99 years Interest rates are fixed at the contract rate All leases are on a fixed repayment basis and no arrangements have been entered into for contingent payments The Group's obligations under finance leases are secured by the lessors' charges over the leased assets

	Group	
	2012 £m	**2011 £m**
Gross finance lease liabilities - minimum lease payments		
Within one year	**1 1**	1 1
Between one and five years	**4 8**	4 7
Over five years	**88 2**	89 4
	94 1	95 2
Future finance charges on finance leases	**(89 1)**	(90 1)
Present value of financial lease liabilities	**5 0**	5 1

	Group	
	2012 £m	**2011 £m**
The present value of finance lease liabilities is as follows		
Within one year	**0 2**	0 2
Between one and five years	**0 7**	0 7
Over five years	**4 1**	4 2
	5 0	5 1

d) Other financial commitments

The Group has entered into several long-term contracts following service outsourcing These contracts will end no later than 2018 An option to withdraw from some of these commitments in 2013 is available The present value of the remaining commitment is estimated at £89 5m (2011 £89 1m) for the Group and the Society These amounts have not been provided for in the financial statements

Notes to the financial statements continued

31 December 2012

Scope of consolidation

This section presents information on the Group's investments in subsidiaries, joint ventures, associates and open ended investment companies (OEICs)

Detail is also given of the unallocated divisible surplus of the Society and Group

43. Subsidiary undertakings

The principal subsidiary undertakings of the Society at 31 December 2012 are shown below
The Group and all principal undertakings are incorporated and domiciled in England and Wales All holdings are in relation to ordinary shares
The registered office is County Gates, Bournemouth BH1 2NF

Name	Principal Activity	Percentage Held
Subsidiaries		
Frizzell Financial Services Limited	Property management	100 0%
Highway Insurance Company Limited *	General insurance	100 0%
Highway Insurance Group Ltd * (Note 1)	General insurance holding company	100 0%
Liverpool Victoria Financial Advice Services Limited (Note 1)	Financial advice services	100 0%
Liverpool Victoria General Insurance Group Limited *	General insurance holding company	100 0%
Liverpool Victoria Insurance Company Limited *	General insurance	100 0%
Liverpool Victoria Life Company Limited	Life insurance	100 0%
Liverpool Victoria Portfolio Managers Limited	Investment management	100 0%
LV Capital PLC	Holding company	100 0%
LV Equity Release Limited	Equity release lifetime mortgages	100 0%
LV Insurance Management Limited * (Note 1)	Management services	95 0%
LV Life Services Limited (Note 1)	Management services	100 0%
NM Pensions Trustees Limited (Note 1)	Self invested personal pension (SIPP) administrator	100 0%

* Owned by a subsidiary undertaking of the Society

Note 1 - The financial statements of these subsidiary undertakings have not been audited for the year ended 31 December 2012 These subsidiary undertakings are exempt from the requirements of the Companies Act 2006 relating to the audit of individual accounts by virtue of Section 479 of the Companies Act 2006 The following other subsidiaries are also taking advantage of this exemption from the audit requirement LV Protection Limited, Liverpool Victoria Asset Management Limited, Ayresbrook Limited, NLC Name No 2 Limited, NLC Name No 7 Limited and Liverpool Victoria Banking Services Limited

All the principal subsidiaries have the same year end as the Society and all have been included in the consolidation

44. Associates and joint ventures

The associates and joint ventures of the Society at 31 December 2012 are shown below
They are incorporated and domiciled in England and Wales

Name	Class of shares	Year end	Principal activity	Percentage held
Joint ventures				
Great Victoria Partnership	*	31/03/2012	Investment property	50 0%

* The percentage held represents the share of the partnership capital and partner loans held by Liverpool Victoria Friendly Society as at 31 December 2012

Notes to the financial statements continued

31 December 2012

45. Open ended investment companies

The Open ended investment companies (OEICs) of the Society and Group at 31 December 2012 are shown below

All OEICs are incorporated and domiciled in England and Wales

Name	Principal Activity	Year end	Percentage of Units Held*
Threadneedle Investment Funds II ICVC	Open Ended Investment Company	31/12/2012	96 21%
which consists of			
Threadneedle European ex-UK Growth Fund			97 16%
Threadneedle Japan Growth Fund			100 00%
Threadneedle Pacific ex-Japan Growth Fund			100 00%
Threadneedle UK Equity Income Fund			92 31%
Threadneedle US Equity Income Fund			99 99%
Threadneedle UK Growth Fund			93 11%
Threadneedle Investment Funds III ICVC	Open Ended Investment Company	31/12/2012	72 03%
which consists of			
Threadneedle UK Corporate Bond Fund			95 61%
Threadneedle UK Fixed Interest Fund			99 70%
Threadneedle UK Index Linked Fund			96 01%
Threadneedle UK Money Market Fund			99 52%
Threadneedle Balanced Managed Fund			96 11%
Threadneedle Medium Long Corporate Bond Fund			40 47%
Threadneedle Short-Dated Corporate Bond			88 74%
Threadneedle Worldwide Select Fund			69 58%
Threadneedle Investment Funds IV ICVC	Open Ended Investment Company	31/03/2012	83 34%
which consists of			
Threadneedle Diversified Income Fund			40 10%
Threadneedle Managed Portfolio 3			79 28%
Threadneedle Managed Portfolio 4			84 51%
Threadneedle Managed Portfolio 5			85 43%
Threadneedle Managed Portfolio 6			89 50%
Threadneedle Managed Portfolio 7			86 21%
Threadneedle UK Property Fund II ICVC	Open Ended Investment Company	31/12/2012	31 41%
which consists of			
Threadneedle UK Property Fund			31 41%

In December 2012 it was announced that the Threadneedle UK Property Fund II ICVC was to close Threadneedle have consequently obtained permission from the Financial Services Authority to close the Company and have commenced the winding up process, which is expected to be completed in 2013

* excludes units held by the LV= Employee Pension Scheme

Notes to the financial statements continued

31 December 2012

46. Unallocated divisible surplus

Accounting for the Unallocated divisible surplus

The Unallocated divisible surplus represents the excess of assets over and above the long-term insurance contract liabilities and other liabilities It represents amounts that have yet to be formally declared as bonuses for the participating contract policyholders together with the free assets of the Society and Group Any profit or loss for the year arising through the Statement of Comprehensive Income (for the Society and for the Group) is transferred to or from the Unallocated divisible surplus

UK regulations, the Group's Principles and Practices of Financial Management, and the terms and conditions of participating contracts set out the bases for the determination of the amounts on which the participating additional discretionary contract benefits are based and within which the Group may exercise its discretion as to the quantum and timing of their payment to contract holders

	Group		Society	
	2012 £m	2011 £m	**2012 £m**	2011 £m
Balance at 1 January	**958 4**	966 4	**1,055.1**	1,078 6
Transfer to the Statement of Comprehensive Income	**(97 5)**	(8 0)	**(176.5)**	(23 5)
Balance at 31 December	**860 9**	958 4	**878 6**	1,055 1

Cumulative goodwill of £199 8m in the Group (£62 2m in the Society) arising on acquisitions prior to 1998 has been eliminated against the Unallocated divisible surplus This goodwill would be recognised in the Statement of Comprehensive Income should there be a subsequent disposal of the business to which it relates

Notes to the financial statements continued

31 December 2012

Other disclosures

This section details other disclosure matters, comprising related party transactions, directors' emoluments, with-profit actuary details and other relevant Society information

47. Related party transactions

The Group and Society enter into transactions with key management personnel in the normal course of business All transactions between group companies took place in accordance with relevant agreements Details of significant transactions carried out during the year with related parties are as follows

a) Sales of insurance contracts and other services

The Group has related party transactions with the LV= Employee Pension Scheme Until 31 October 2011 the Society provided fund management and administration services to the Scheme

In 2012 and 2011 the following amounts were charged to the Pension Scheme for the following services

	Fund Management Services		Administration Services		Total	
	2012 £m	2011 £m	**2012 £m**	2011 £m	**2012 £m**	2011 £m
Liverpool Victoria Friendly Society Limited	–	–	–	2 4	–	2 4
Liverpool Victoria Asset Management Limited	–	1 1	–	–	–	1 1

As at 31 December 2012 the LV= Employee Pension Scheme owed the Society £nil in respect of administration services (2011 £1 8m)

b) Other related parties disclosure

As disclosed in Note 41, the Society has granted a contingent loan facility to the RNPFN fund, a closed fund within the Group, which is disclosed in contingent liabilities

c) Key management compensation

Key management personnel of the Group comprise all executive and non-executive directors and senior management The summary of the compensation of key management personnel for the year is as follows

	Group	
	2012 £'000	2011 £ 000
Short-term employment benefits	**6,139**	6,740
Other long-term benefits	**2,865**	2 746
Post-employment benefits	**216**	440
Termination benefits	-	240
Total compensation of key management personnel	**9,220**	10,166

The Society makes contributions to the LV= Employee Pension Scheme of an average of 17 8% of pensionable salaries (2011 17 1% of pensionable salaries), subject to annual allowance limits, in respect of all permanent staff, including executive directors

Included within key management personnel are all the vendors of ABC Insurance Solutions Limited who, as part of the acquisition in 2006, entered into a contract with the Society Further details are disclosed within Note 40

The aggregate premiums payable for the year by the Group Executive and Non-Executive Directors in respect of the Group s products was £57,827 (2011 £58,756)

Notes to the financial statements continued

31 December 2012

47. Related party transactions (continued)

d) The following transactions have taken place between the Society and other group companies·

	2012 £m	2011 £m
Management charge by the Society	**191 1**	186 8
Investment management charge to the Society	-	(7 9)
Reinsurance ceded by the Society - claims recoveries	-	47 9
Reinsurance ceded by the Society - premiums paid	-	(31 5)
Deferred margin (included in other financial liabilities)	**10 1**	5 6
Beneficial interest of subsidiary in loans sold to the Society	**225 6**	90 4
Intra-group loans - net interest received by the Society	**5 8**	3 8

Balances outstanding between the Society and other Group companies

	2012 £m	2011 £m
Payable by the Society	**(52 8)**	(43 3)
Receivable by the Society	**87 4**	109 6
Loans owed to the Society	**351 7**	396 6

e) Loans to related parties

Loans owed to the Society represent a subordinated loan of £nil (2011 £183m) to Liverpool Victoria General Insurance Group Limited, secured loans of £51 7m (2011 £51 4m) to Liverpool Victoria Equity Release Limited and two new loans of £130m (unsecured subordinated loan) and £170m (unsecured senior loan note) to LV Capital PLC issued on 21 December 2012 All these loans are disclosed within loan stock in Note 29

In addition the Society has a loan of £nil (2011 £162 2m) to Liverpool Victoria Equity Release Limited designated at fair value through income disclosed in Note 15 This loan was repaid in December 2012 as part of the loan restructure with the Society

In March 2013 the remaining loan balance of £51 7m to Liverpool Victoria Equity Release Limited was repaid

The subordinated loan to Liverpool Victoria General Insurance Group Limited bore interest at 1% above UK six month LIBOR and was of a medium to long-term nature, this loan was repaid in full in December 2012
The terms of the loans to LV Capital PLC are
(i) A £130m unsecured subordinated loan note repayable in 2015 with an interest rate of LIBOR plus 8 5%
(ii) A £170m unsecured senior loan note repayable in 2047 with an interest rate of 9%
LV Capital may, subject to one month's notice and obtaining written agreement of the Society repay all or part of these loans
In addition to the loan notes disclosed above a £300m loan note was issued to LV Capital PLC by the Society on 10 December 2012 and subsequently cancelled on 21 December 2012

The loans to Liverpool Victoria Equity Release Limited have fixed interest and repayment terms established at the outset of each advance

On 30 November 2011 the Critical Illness and Income Protection reinsurance agreement between the Society and Liverpool Victoria Life Company Limited was terminated Assets totalling £34 4m were transferred to the Society in settlement of £91 8m of insurance contract liabilities less the value of the estimated future profits for the business stream A loss of £0 7m was recorded in the Statement of Comprehensive Income as a result of this transfer

48. With-Profits Actuary

The following information has been provided in accordance with section 77 of the Friendly Societies Act 1992

a) The With-Profits Actuary of the Society until 16 February 2012 was Mr P M Downey, who is employed by Liverpool Victoria Friendly Society The total emoluments of Mr Downey during this period on a pro rata basis were £23,604 (2011 £175,312) including car allowance and medical benefits Mr Downey is a participant in the Society's long term incentive plan and holds one insurance policy issued on normal staff terms by a subsidiary of the Society

b) On 16 February 2012, Mr N J Dumbreck took over as the Society's With-Profits Actuary from Mr P M Downey Mr Dumbreck is a Principal with the London office of Milliman LLP, an external consultancy firm The Society paid fees of £388,491, inclusive of VAT and expenses, to Milliman LLP during 2012 in respect of Mr Dumbreck's professional services It also paid fees of £54,000, inclusive of VAT and expenses, to Milliman LLP during 2012 in respect of services unrelated to Mr Dumbreck's role as With-Profits Actuary

c) Mr Dumbreck held four insurance policies issued on standard terms by one of the Society's subsidiaries He had no other pecuniary interest in any transactions with the Society at any time during the year

Notes to the financial statements continued

31 December 2012

49. Directors' emoluments

The aggregate amount of directors' emoluments was as follows

a) Aggregate emoluments including pension contributions and LTIPs	2012 £m	2011 £m
Aggregate emoluments	**6.3**	4 6

b) Emoluments of individual directors, including emoluments of the Chairman and highest paid director were as follows for the Society

	Annual remuneration £ 000						Total remuneration £ 000		
	Salary	Bonus	Deferred bonus	Other benefits	Total 2012	Total 2011	LTIP 2010-12	Total 2012	Total 2011
M J Rogers	**505**	**427**	**132**	**127**	**1,191**	1,131	**1,431**	**2,622**	2,177
PW Moore	**346**	**208**	**52**	**55**	**661**	609	**732**	**1,393**	609
R A Rowney	**306**	**240**	**–**	**51**	**597**	568	**585**	**1,182**	943
J B O Roarke (appointed 23 November 2011)	**281**	**220**	**–**	**45**	**546**	54	**–**	**546**	314
D Holt	**153**	**–**	**–**	**–**	**153**	150	**n/a**	**153**	150
M E Austen	**72**	**–**	**–**	**–**	**72**	68	**n/a**	**72**	68
J Edwards	**62**	**–**	**–**	**–**	**62**	58	**n/a**	**62**	58
C Keers	**61**	**–**	**–**	**–**	**61**	57	**n/a**	**61**	57
D I W Reynolds (resigned 31 October 2012)	**60**	**–**	**–**	**–**	**60**	64	**n/a**	**60**	64
C Burton (appointed 9 November 2011)	**56**	**–**	**–**	**–**	**56**	15	**n/a**	**56**	15
J Dean (appointed 26 July 2012)	**22**	**–**	**–**	**–**	**22**	–	**n/a**	**22**	–
G Nott (resigned 26 May 2011)	**–**	**–**	**–**	**–**	**–**	28	**n/a**	**–**	28
Total	**1,924**	**1,095**	**184**	**278**	**3,481**	2,802	**2,748**	**6,229**	4,483

Deferred bonus represents the amount of the 2012 performance bonus payable over the next three years Further details are disclosed within the Directors' Remuneration Report

Other benefits include cash allowance in lieu of pension, car allowances, medical, relocation, life assurance and other benefits in kind or their equivalent monetary value

c) Pension arrangements

R A Rowney and J B O'Roarke are members of the LV= Employee Pension Scheme, which is a defined benefit scheme PW Moore left the defined contribution scheme during the year

The directors' emoluments table above excludes the Society contributions to defined benefit and defined contribution pension schemes

The Society makes contributions to the LV= Employee Pension Scheme of an average of 17 8% of pensionable salaries (2011 17 1% of pensionable salaries), subject to annual allowance limits, in respect of all permanent staff This included amounts on behalf of executive directors of £0 1m (2011 £0 1m)

The Society has made no contributions to personal pension arrangements during 2012 (2011 £nil)

There were £8,500 of contributions to defined contribution pension schemes in 2012 (2011 £42,542)

Accrued pension at end of period	2012 £'000	2011 £ 000
R A Rowney	**27**	23
J B O'Roarke	**30**	26

Notes to the financial statements continued
31 December 2012

50. Cash generated from operating activities

	Group 2012 £m	Group 2011 Restated £m	Society 2012 £m	Society 2011 Restated £m
Profit/(loss) before tax and mutual bonus	**103 2**	(16 9)	**3 3**	(47 7)
Investment income	**(320 2)**	(261 4)	**(337 0)**	(284 9)
Net gains on investments	**(374 7)**	(425 4)	**(304 1)**	(407 3)
Finance costs	**0 5**	0 5	**-**	-
Net decrease/(increase) in derivatives	**92 3**	(12 7)	**100 1**	(14 1)
Non-cash items				
Expenses deferred during the year	**(5 4)**	44 1	**-**	-
Amortisation of intangible assets	**12 0**	13 0	**4 6**	4 6
Depreciation on property and equipment	**3 4**	2 6	**0 8**	0 8
Loss on disposal of property and equipment	**0 4**	-	**0 4**	0 1
Increase in capitalised goodwill	**(2 4)**	(5 3)	**(2 4)**	(5 3)
Decrease in provisions and pension obligation	**(17 9)**	(25 5)	**(17 3)**	(16 6)
Impairment write-offs in subsidiaries	**-**	-	**90 0**	34 4
Mutual bonus	**(20 9)**	(18 6)	**(20 9)**	(18 6)
Changes in working capital				
Decrease/(increase) in loans and receivables	**13 0**	(36 8)	**26 3**	(77 6)
Increase in reinsurance assets	**(110 3)**	(123 3)	**(74 4)**	(7 0)
(Increase)/decrease in insurance receivables	**(10 8)**	(23 3)	**(2 4)**	4 7
Increase in other prepayments and accrued income	**(7 7)**	(1 2)	**(1 7)**	(1 8)
Increase in insurance contract liabilities	**909 4**	1,131 9	**657 1**	821 3
Increase in investment contract liabilities	**158 4**	59 7	**158 4**	59 7
Increase in borrowings	**-**	-	**-**	5 6
(Decrease)/increase in other financial liabilities	**(1.7)**	55 3	**8 7**	55 9
Increase/(decrease) in insurance payables	**3 1**	9 0	**(5 4)**	7 9
(Decrease)/increase in trade and other payables	**(11 9)**	48 7	**(11 6)**	26 4
Cash generated from operating activities	**411 8**	414 4	**272 5**	140 5

51. Valuation

The latest published report on the valuation of Assets and Liabilities of the Society (the Annual FSA Insurance Return) was made at 31 December 2012 and is available on request from the Group Company Secretary, County Gates, Bournemouth, BH1 2NF and LV com

52. Society information

Liverpool Victoria Friendly Society is a UK incorporated and domiciled Friendly Society registered under the Friendly Societies Act 1992

LV= and Liverpool Victoria are trademarks of Liverpool Victoria Friendly Society Limited LV= and LV= Liverpool Victoria are trading styles of the Liverpool Victoria group of companies Liverpool Victoria is authorised and regulated by the Financial Services Authority and is a member of the ABI, AFS and ILAG

Registered office
County Gates
Bournemouth
BH1 2NF
Telephone 01202 292333