CLERICAL MEDICAL INVESTMENT GROUP LIMITED

FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2008

Registered Number 3196171

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DIRECTORS' AND COMPANY INFORMATION

DIRECTORS	M Christophers* S J Colsell J Dawson R A Devey B J Duffin* P N C Gale* A G Kane T A Leonard A M Peck* J van der Wielen ** Non Executive Director*		
SECRETARY	P J Veale		
REGISTERED OFFICE	33 Old Broad Street London EC2N 1HZ		
PRINCIPAL PLACES OF BUSINESS	<u>Bristol Head Office</u> 10 Canons Way Bristol BS1 5LF	<u>Clevedon Office</u> Tickenham Road Clevedon BS21 6BD	<u>Aylesbury Office</u> Walton Street Aylesbury HP21 7QW
AUDITORS	KPMG Audit Plc 8 Salisbury Square London EC4Y 8BB		

DIRECTORS' REPORT

The Directors present their Report and the audited Financial Statements for the year ended 31 December 2008.

BUSINESS REVIEW

The Company, which is authorised by the Financial Services Authority and is a member of the Association of British Insurers, is a wholly owned subsidiary of HBOS Financial Services Limited.

The Company's principal activity is the transaction of long term insurance and investment business and associated investment activities including non profit, with profit and unit linked business in the United Kingdom and abroad. Throughout the year the Company made its life and pension products available principally through independent financial advisers. The Company also reassures business with and from fellow subsidiary undertakings of the ultimate parent undertaking and with and from insurance entities external to the Group. This includes the majority of the pension linked business that is reassured to the Company's subsidiary Clerical Medical Managed Funds Limited.

On 1 October 2008, the directors passed a special resolution, supported by a solvency statement under Section 641 of the Companies Act 2006, to reduce the Company's share capital from 1,709,000,000 ordinary shares of £1 each to 150,000,000 shares of £1 each. The solvency statement was registered by Companies House on 9 October 2008 and therefore the reduction in share capital became effective as of that date. As a result of this, the Company's distributable reserves increased by £1,559,000,000. This has enabled the Company to pay a larger dividend than in previous years.

RISK MANAGEMENT

The key risks of the Company are considered to be market risk (currency, interest rate and price), credit and liquidity risk, insurance risk and operational risk.

Detailed analysis of the risks and their management is included within the notes to the financial statements.

The risks associated with the activities of the Company are overseen by the Risk Control Committee of the Insurance & Investment Division of HBOS plc. The Committee, which is chaired by a Director of HBOS plc, reviews all risk and compliance issues affecting the Company, as well as the other wholly owned companies within the Insurance & Investment Division.

In addition to the Risk Control Committee, there are a number of other committees responsible for different aspects of corporate governance of HBOS plc and its major subsidiaries. Further details of these committees and compliance with the Combined Code on corporate governance are included in the HBOS plc annual report and accounts.

There is a Long Term Business Governance Committee, the role of which is to consider the balance of interests between policyholders and shareholders and to make recommendations to the board.

PERFORMANCE

The profit for the year after taxation was £261.9 million (2007: £492.3 million), and loss before taxation £34.2 million (2007: £379.3 million profit). During the year a dividend of £610 million was paid (2007: £204 million). This included £60m of dividends received from Halifax Life Limited (2007: £451m).

The new business sold during the year amounted to £372.8 million (2007: £424.9 million), on an Annual Premium Equivalent (APE) basis, which is calculated as annualised regular premium new business plus one tenth of single premium new business. Total insurance premiums recognised in the Income Statement were £784.9 million (2007: £642.5 million) and total investment premiums deposit accounted were £1,927.5 million (2007: £2,365.4 million).

The Funds Under Management are approximately £17 billion (2007: £19 billion).

The Directors believe that the Company currently has adequate capital resources, has had throughout the year and will continue to do so in the foreseeable future.

The Directors have chosen the above Key Performance Indicators they consider appropriate to the principal activity of the Company.

DIRECTORS' REPORT (continued)

FUTURE DEVELOPMENTS

A business plan is produced for the operations of the HBOS Financial Services group of companies, of which the Company is part. Progress against this is monitored regularly by the Board. The Company expects to continue to transact long term insurance and investment business and associated investment activities for the foreseeable future.

The Company has no employees. All staff providing services to the Company are employed by HBOS plc.

POST BALANCE SHEET EVENTS

Details of post balance sheet events including the acquisition of HBOS plc by Lloyds TSB Group plc are given in Note 35 to the financial statements.

ULTIMATE HOLDING COMPANY

As at 31 December 2008 the Company's immediate parent company was HBOS Financial Services Limited. The company regarded by the directors as the ultimate parent company at 31 December 2008 was HBOS plc, a limited liability company incorporated and domiciled in Scotland, which was also the parent undertaking of the largest group of undertakings for which group accounts are drawn up and of which the Company is a member.

From 16 January 2009, Clerical Medical Investment Group Limited's ultimate parent undertaking and controlling party is Lloyds Banking Group plc (formerly Lloyds TSB Group plc) which is incorporated in Scotland. Lloyds Banking Group plc will produce consolidated accounts for the year ended 31 December 2009. Copies of the annual report and accounts of Lloyds TSB Group plc for the year ended 31 December 2008 may be obtained from Lloyds Banking Group's head office at 25 Gresham Street, London EC2V 7HN.

Prior to 16 January 2009, HBOS plc was the ultimate parent undertaking of Clerical Medical Investment Group Limited. Copies of the annual report and accounts of HBOS plc for the year ended 31 December 2008 may be obtained from HBOS plc's registered office at The Mound, Edinburgh, EH1 1YZ.

SUPPLIER PAYMENT POLICY

The Company's suppliers are paid through HBOS plc's centralised Accounts Payable department.

For the forthcoming period HBOS plc's policy for the payment of suppliers will be as follows:

- Payment terms will be agreed at the start of the relationship with the supplier and will only be changed by agreement;
- Standard payment terms to suppliers of goods and services will be 30 days from receipt of a correct invoice for satisfactory goods or services which have been ordered and received unless other terms are agreed in a contract;
- Payment will be made in accordance with the agreed terms or in accordance with the law if no agreement has been made; and
- Suppliers will be advised without delay when an invoice is contested and disputes will be settled as quickly as possible.

HBOS plc complies with the Better Payment Practice Code. Information regarding this Code and its purpose can be obtained from the Better Payment Practice Group's website at www.payontime.co.uk.

The Company had trade creditors outstanding at 31 December 2008 representing 19 days of purchases.

DIRECTORS' REPORT (continued)

DIRECTORS

The Directors who served during the year were as follows:

M Christophers	
S J Colsell*	
J Dawson	
R A Devey*	
B J Duffin*	*Appointed 24 January 2008*
P N C Gale*	*Appointed 24 January 2008*
T A Leonard	
A M Peck*	*Appointed 24 January 2008*

The following Directors were appointed after 31 December 2008:

A G Kane	*Appointed 4 March 2009*
J van der Wielen*	*Appointed 4 March 2009*

* *Member of the Long Term Business Governance Committee*

Particulars of the Directors' emoluments are given in note 34 to the financial statements.

GOING CONCERN

As set out in the 'Principles underlying Going Concern Assumption' in the Basis of Preparation section of the Notes to the Accounts, the Directors are satisfied that the Company has adequate resources to continue in business for the foreseeable future and consequently the going concern basis continues to be appropriate in preparing the accounts.

AUDIT INFORMATION

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they each are aware, there is no relevant audit information of which the Company's auditors are unaware; and each Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

ANNUAL GENERAL MEETING

Pursuant to a Resolution passed by the members, the Company has elected to dispense with the holding of Annual General Meetings, of laying accounts before the Company in General Meeting and with the obligation to reappoint auditors annually.

By order of the Board

P J Veale
Secretary

33 Old Broad Street
London
EC2N 1HZ

23 March 2009

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS

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

Company law requires the Directors to prepare Financial Statements for each financial year. Under that law they have elected to prepare the Financial Statements in accordance with IFRSs as adopted by the EU and applicable law.

The Financial Statements are required by law to present fairly the financial position and the performance of the Company; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing these Financial Statements, the directors are required to:
- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its Financial Statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CLERICAL MEDICAL INVESTMENT GROUP LIMITED

We have audited the financial statements of Clerical Medical Investment Group Limited for the year ended 31 December 2008, which comprise the Income Statement, the Balance Sheet, the Statement of Charges in Equity, the Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 7.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

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

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

Opinion

In our opinion:

- the Financial Statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Company's affairs as at 31 December 2008 and of its profit for the year then ended; and
- the Financial Statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the Financial Statements.

KPMG Audit Plc

KPMG Audit Plc
Chartered Accountants
Registered Auditor

8 Salisbury Square
London
EC4Y 8BB

23 March 2009

INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008

	Note	2008 £m	2007 £m
TOTAL REVENUE		215.8	1,981.0
Net insurance revenue	3	629.7	480.3
Gross earned premiums on insurance contracts		784.9	642.5
Less reinsurers' share of gross earned premiums on insurance contracts		(155.2)	(162.2)
Other revenue		(413.9)	1,500.7
Fee and commission income		77.9	86.2
Investment income	4	1,932.0	1,158.1
Finance income	7	46.0	43.1
Net realised gains recorded in the income statement		662.1	769.1
Net fair value losses recorded in the income statement	5	(3,191.9)	(1,006.8)
Income from shares in group undertakings		60.0	451.0
TOTAL EXPENSES		(250.0)	(1,601.7)
Net insurance claims and benefits	6	(4,001.1)	(683.8)
Gross insurance contracts claims and benefits paid		(930.0)	(898.7)
Less reinsurers' share of gross insurance contracts claims and benefits paid		201.5	202.4
Gross change in insurance contracts liabilities		(3,248.8)	(119.8)
Less reinsurers' share of gross change in insurance contracts liabilities		(23.8)	132.3
Other expenses		3,751.1	(917.9)
Change in unallocated surplus		1,028.2	72.0
Net change in investment contracts liabilities		3,280.5	(387.5)
Finance costs	7	(103.1)	(89.2)
Fee and commission expenses		(93.8)	(79.2)
Other operating and administration expenses	8	(360.7)	(434.0)
(Loss) / profit before taxation		(34.2)	379.3
Total income tax credit	9	296.1	113.0
Taxation attributable to policyholder returns		172.8	74.6
Taxation attributable to shareholders		123.3	38.4
Profit after taxation		261.9	492.3

The accounting policies and notes set out on pages 13 to 64 are an integral part of the Financial Statements.

BALANCE SHEET
AS AT 31 DECEMBER 2008

	Note	2008 £m	2007 £m
ASSETS			
Intangible assets	10	**270.8**	294.0
Property and equipment	11	**77.4**	161.4
Deferred costs	12	**477.9**	413.1
Investment properties	13	**1,491.2**	2,274.1
Investment in Group undertakings and participating interests	14	**2,027.4**	6,159.2
Reinsurance assets	15	**9,734.4**	11,097.1
Prepayments and accrued income	16	**41.4**	36.7
Current tax receivable	25	**7.8**	105.7
Financial assets			
Financial assets at fair value through income statement			
Derivative assets	17	**665.5**	101.5
Equity investments	18	**5,174.9**	5,962.9
Debt investments	18	**8,580.6**	5,775.6
Insurance receivables	19	**4.9**	49.5
Other receivables	19	**642.2**	558.0
Cash and cash equivalents	20	**289.3**	267.8
Total assets		**29,485.7**	33,256.6
LIABILITIES AND EQUITY			
LIABILITIES			
Insurance contracts liabilities	21, 24	**10,742.0**	8,012.1
Unallocated surplus	22	**469.2**	1,497.4
Deferred tax liability	25	**183.5**	389.0
Financial liabilities			
Derivative liabilities	17	**131.1**	37.9
Investment contracts liabilities	23, 24	**13,934.5**	19,625.5
Borrowings	26	**169.0**	51.4
Other insurance financial liabilities	27	**65.4**	99.1
Accruals and deferred income	28	**26.5**	28.2
Other liabilities	29	**541.3**	196.1
Subordinated liabilities	30	**1,319.5**	1,059.1
Total liabilities		**27,582.0**	30,995.8
CAPITAL & RESERVES ATTRIBUTABLE TO COMPANY'S EQUITY HOLDERS			
Issued share capital	31	**70.0**	1,629.0
Share premium account	31	**1.0**	1.0
Other reserves		**-**	2.6
Retained earnings		**1,832.7**	628.2
Total equity		**1,903.7**	2,260.8
Total liabilities and equity		**29,485.7**	33,256.6

The accounting policies and notes set out on pages 13 to 64 are an integral part of the Financial Statements.

These accounts were approved and authorised for issue by the Board of Directors on 23 March 2009 and were signed on its behalf by:

T A LEONARD
DIRECTOR

R A DEVEY
DIRECTOR

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2008

	Issued Share Capital £m	Share Premium Account £m	Other Reserves £m	Retained Earnings £m	Total £m
Balance as at 1 January 2007	**1,629.0**	**1.0**	**611.7**	**(271.8)**	**1,969.9**
Net profit for the year	-	-	-	492.3	492.3
Dividend paid to parent undertaking	-	-	-	(204.0)	(204.0)
Transfer of reserves	-	-	(611.7)	611.7	-
Foreign exchange translation	-	-	2.6	-	2.6
Balance as at 31 December 2007	**1,629.0**	**1.0**	**2.6**	**628.2**	**2,260.8**
Balance as at 1 January 2008	**1,629.0**	**1.0**	**2.6**	**628.2**	**2,260.8**
Net profit for the year	-	-	-	261.9	261.9
Dividend paid to parent undertaking	-	-	-	(610.0)	(610.0)
Reduction of Issued Share Capital under Section 641 of the Companies Act 2006	(1,559.0)	-	-	1,559.0	-
Transfer of reserves	-	-	(2.6)	2.6	-
Foreign exchange translation	-	-	-	(9.0)	(9.0)
Balance as at 31 December 2008	**70.0**	**1.0**	**-**	**1,832.7**	**1,903.7**

The accounting policies and notes set out on pages 13 to 64 are an integral part of the Financial Statements.

CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2008

	Note	2008 £m	2007 £m
CASH FLOW FROM OPERATING ACTIVITIES			
Loss before taxation (Excluding dividends received from group undertaking of £60m (2007: £451m))		(94.2)	(71.7)
Movement in property and intangible assets		107.2	125.3
Increase in deferred costs		(64.8)	(98.0)
(Decrease)/increase in deferred income		(1.7)	8.9
Increase/(decrease) in insurance contracts liabilities		2,696.2	(480.5)
Decrease in unallocated surplus		(1,028.2)	(72.0)
Decrease in investment contracts liabilities		(5,691.0)	(496.0)
Decrease/(increase) in reinsurance assets		1,362.7	(744.2)
Decrease in investment property		782.9	490.1
Decrease/(increase) in equity investments		788.0	(196.0)
(Increase)/decrease in debt investments		(2,805.0)	957.3
(Increase)/decrease in derivative investments		(470.8)	40.1
Decrease in Investment in Group undertakings and participating interests		4,131.8	125.7
Net decrease in other operating assets and liabilities		552.3	148.3
Taxation reclaimed		188.5	68.6
Net cash inflow/(outflow) from operating activities		453.9	(194.1)
CASH FLOW FROM INVESTING ACTIVITIES			
Loans repaid from subsidiary undertakings		-	54.2
Dividends received from group undertakings		60.0	451.0
Net cash inflow from investing activities		60.0	505.2
CASH FLOW FROM FINANCING ACTIVITIES			
Increase in overdraft		117.6	10.3
Equity dividends paid		(610.0)	(204.0)
Net cash outflow from financing activities		(492.4)	(193.7)
Net increase in cash and cash equivalents		21.5	117.4
Cash and cash equivalents at the beginning of the year	20	267.8	150.4
Cash and cash equivalents at 31 December	20	289.3	267.8

The accounting policies and notes set out on pages 13 to 64 are an integral part of the Financial Statements.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

1. Accounting policies

Clerical Medical Investment Group Limited ("the Company") is a limited liability company incorporated in the United Kingdom. The principal activity of the Company is the undertaking of ordinary long term insurance and investment business in the UK and overseas. The Company offers a wide range of life insurance products such as annuities, pensions, whole life, term life and investment type products.

The Financial Statements for the year ended 31 December 2008 were authorised for issue in accordance with a resolution of the directors on 23 March 2009.

1.1 Financial Statements

The financial statements of Clerical Medical Investment Group Limited comprise the Income Statement, Balance Sheet, Statement of Changes in Equity, and Cash Flow Statement together with the related Notes to the Financial Statements.

1.2 Statement of compliance

The Financial Statements have been prepared in accordance with International Financial Reporting Standards ('IFRS') and interpretations issued by the International Financial Reporting Interpretations Committee ('IFRIC') as adopted by the European Union. The standards applied by the Company are those endorsed by the European Union and effective at the date the financial statements are approved by the Board. Consequently, the financial statements comply with International Financial Reporting Standards.

The financial statements also comply with the relevant provisions of Part VII of the Companies Act 1985, as amended by the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004. Additionally the Company has applied Financial Reporting Standard 27 'Life Assurance' issued by the UK Accounting Standards Board as appropriate.

1.3 Basis of preparation

(a) Principles underlying going concern assumption

During 2008, global financial markets experienced difficult conditions which have been characterised by a marked reduction in liquidity. As a consequence of this, governments and central banks carried out a series of actions to address the lack of liquidity within their respective banking systems. In the UK these actions have included the introduction by the Bank of England of liquidity support, through schemes (collectively 'Bank of England facilities') such as the extended Long–Term Repo open market operations and the Special Liquidity Scheme ('SLS') whereby banks and building societies can exchange eligible securities for UK Treasury bills; and the creation of a credit guarantee scheme by HM Treasury, providing a government guarantee for certain short and medium term senior debt securities issued by eligible banks. During 2008 HBOS plc has made use of these measures in order to maintain and improve a stable funding position.

In the context of this continued turbulence and uncertainty in the financial markets, combined with a deteriorating global economic outlook, HBOS plc has also taken steps to strengthen its capital position in order to provide a buffer against further shocks to the financial systems and to ensure that it remains competitive. On 15 January 2009, in conjunction with the takeover of HBOS plc by Lloyds TSB Group plc, HBOS plc raised £11,345m (net after costs) in preference and ordinary share capital.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008

1.3 Basis of preparation (continued)

On 16 January 2009, following completion of the acquisition of the HBOS Group by Lloyds Banking Group plc, the Group became a wholly owned subsidiary.

There is a risk despite the substantial measures taken so far by governments that further deterioration in the markets could occur. In addition the economic conditions in the UK are deteriorating more quickly than previously anticipated placing further strain on the Lloyds Banking Group's capital resources. The key dependencies on successfully funding the Lloyds Banking Group's balance sheet include the continued functioning of the money and capital markets at their current levels; the continued access of the Lloyds Banking Group to central bank and Government sponsored liquidity facilities including access to HM Treasury's credit guarantee scheme and access to the Bank of England's various facilities; limited further deterioration in the Lloyds Banking Group's credit ratings; and no significant or sudden withdrawal of deposits resulting in increased reliance on money markets or Government support schemes.

The directors are satisfied that the Company has adequate resources to continue in business for the foreseeable future. The Company has received confirmation that it is the current intention of Lloyds Banking Group plc to ensure that the Company, as a subsidiary of HBOS plc, should have at all times for the foreseeable future access to adequate resources to continue to trade and meet their liabilities as they fall due. Accordingly, the financial statements of the Company have been prepared on a going concern basis.

The Company is exempt by virtue of IAS 27 Consolidated and Separate Financial Statements from the requirement to prepare group Financial Statements. These Financial Statements present information about the Company as an individual undertaking and not about its group.

(b) Basis of Measurement

The financial statements have been prepared under the historical cost basis, except that the following assets and liabilities are stated at their fair values: derivatives, financial instruments held for trading, financial instruments designated at fair value through the income statement, and investment properties.

1.4 Critical Accounting Judgements

The preparation of the financial statements necessarily requires the exercise of judgement in the application of accounting policies which are set out on pages 13 to 24. These judgements are continually reviewed and evaluated based on historical experience and other factors. The principal critical accounting judgements made by the Company that have a material financial impact on the financial statements are as follows: insurance and investment liabilities, deferred acquisition costs and the ascertainment of fair values of reinsurance assets, financial assets, liabilities, derivative financial instruments and of investment properties and the determination of impairment losses

1.5 Critical Accounting Estimates

The preparation of the financial statements requires the Company to make estimations where uncertainty exists. The principal critical accounting estimates made by the Company are considered in Note 2. Disclosures about estimates and the related assumptions are also included in the appropriate Note.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

1.6 Summary of significant accounting policies

The accounting policies below have been consistently applied to all periods presented in these financial statements.

(a) Product classification

The Company has classified its long term assurance business in accordance with IFRS 4 Insurance Contracts as follows:

Insurance contracts are contracts containing significant insurance risk. Such contracts remain insurance contracts until all rights and obligations are extinguished or expired;

Investment contracts with a discretionary participation feature ('DPF') are contracts that do not contain significant insurance risk but that contain discretionary participation features, which for the Group are its with profit contracts; and

Investment contracts are contracts that have neither significant insurance risk nor a DPF.

Insurance Contracts and Investment Contracts with DPF

Insurance contracts and investment contracts with DPF liabilities written within the with-profit fund, including both traditional and unitised with-profit contracts, are calculated with reference to the expected payout using realistic and, where applicable, market consistent assumptions in accordance with FRS 27 'Life Assurance' Insurance contract liabilities within the non-profit funds are calculated in accordance with the Prudential Sourcebook for Insurers ('INSPRU') issued by the UK Financial Services Authority. For insurance contracts, premiums are recognised as revenue when due from the policyholder and claims payable are recorded when notified or due. For unitised with-profit contracts, where the policyholder has the choice to invest in a unit-linked investment fund, deposits and withdrawals are accounted for directly on the balance sheet. Similarly, for investment contracts with DPF, deposits and withdrawals are accounted for directly in the balance sheet.

At each reporting date an assessment is made of whether liabilities are adequate using current estimates of future cash flows and taking into account the value of any related Value in Force (VIF) asset. Any deficiency is immediately charged to the income statement by establishing a provision on the balance sheet.
Costs related to the acquisition of new long-term insurance and investment with DPF contracts are expensed as incurred.

Investment Contracts

The Company's investment contracts, which include collective investment schemes, are primarily unit-linked. These contracts are managed and evaluated on a fair value basis in accordance with the terms of the contracts as benefits are linked to the fair value of the assets supporting the contracts. Accordingly, the investment contract liabilities have been designated at fair value through the income statement with fair value changes recognised through change in investment contract liabilities. The fair value of the liabilities is estimated using a valuation technique. In accordance with this technique the liability is established as the bid value of the assets held to match the liability, less an allowance in relation to deductions made to the liability for tax on the capital gains relating to the matching assets. Deposits and withdrawals are accounted for directly in the balance sheet as adjustments to the liability with other changes recognised in the income statement.

Revenue in relation to investment management services is recognised as the services are provided. Incremental costs directly attributable to securing the Company's contractual right to benefit from providing investment management services in relation to investment contracts, other than through a business combination or portfolio transfer (refer to the accounting policy for intangible assets), are recognised as an asset if it is probable that they will be recovered. Incremental costs include commissions paid to intermediaries and other similar costs. This asset, referred to as deferred origination costs, is amortised as the related investment management revenue is recognised, and its recoverability assessed at each balance sheet date on a portfolio basis.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

1.6 Summary of significant accounting policies (continued)

(b) Revenue recognition

Premium income

Gross premiums written are accounted for on a cash basis in respect of single premium business and pensions business not subject to contractual regular premiums. For all other classes of business, gross premiums written are accounted for in the year in which they are due for payment. Outward reinsurance premiums are accounted for when the related gross premiums written are recognised. Gross premiums written exclude any taxes or duties based on premiums.

Interest income

All income from listed stocks and shares is included in the accounts when the security becomes ex-dividend. Other investment income, including interest income from fixed interest investments and rent, is accrued up to the balance sheet date. Realised gains and losses on investments are calculated as the difference between net sales proceeds and the original cost. Rental income from investment properties is also recognised in investment income and it is recognised in the period it is due.

Realised gains and losses

Realised gains and losses on the sale of property and equipment is the difference between net sales proceeds and the original cost. Realised gains and losses are recognised in the income statement when the sale transaction occurred.

Fees and commission

Fees and commission income, and commission expenses are recognised in the income statement as the related service is provided except those that are integral to the effective interest rate calculations or to investment contract deferred origination costs.

Fees and commission recognised in the income statement include service fees, agency and management fees, transaction fees, guarantee fees, letter of credit fees, asset management fees and non-utilisation fees.

Fees and commission included in the effective interest calculation are those that are incremental and directly attributable to the origination of the product and which are integral to the yield of the product. These include arrangement fees, incentives such as cash backs, intermediary fees and commissions, high loan to value fees and procurement fees.

(c) Expense recognition

Claims

Life insurance business claims reflect the cost of all claims incurred during the year, including claims handling costs. Death claims and surrenders are recorded on the basis of notifications received. Maturities and annuity payments are recorded when due.

Interest paid

Interest paid is recorded in the period in which it is incurred.

Commission

Commission payable is accounted for on the same basis as the corresponding premiums, except for commission payable under indemnity terms, which is charged when paid.

Finance Costs

Finance costs include interest on the late payment of claims. This is recognised when it is incurred.

1.6 Summary of significant accounting policies (continued)

(d) Intangible assets

Software

Costs associated with the development of software for internal use, subject to de minimis limits, are capitalised if the software is technically feasible and the Company has both the intent and sufficient resources to complete the development. Costs are only capitalised if the asset can be reliably measured and will generate future economic benefits to the Company either through sale or use.

Only costs that are directly attributable to bringing the asset into working condition for its intended use are capitalised. These costs include all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in a manner intended by management. Other development expenditure is recognised in the income statement as an expense as incurred.

Capitalised development expenditure and purchased software is stated at cost less accumulated amortisation and impairment losses. Once the software is ready for use, the capitalised costs are amortised over their expected lives, generally four years. Capitalised software is assessed for impairment where there is an indication of impairment. Where impairment exists, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss recognised in the income statement. The amortisation charge for the asset is then adjusted to reflect the asset's revised carrying amount.

Subsequent expenditure is only capitalised when it increases the future economic benefits embodied in the specific asset to which it relates.

Purchased Value of In-Force

The Company's contractual rights to benefits from providing investment management services in relation to investment contracts, as well as insurance and investment contracts with DPF, acquired in business combinations and portfolio transfers are measured at fair value at the time of acquisition. The resulting asset is referred to as purchased value of in-force ('PVIF') and is amortised over the estimated lives of the contracts on a systematic basis. At each reporting date an assessment is made to determine if there is any indication of impairment. Where impairment exists, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss recognised in the income statement. The amortisation charge is then adjusted to reflect the revised carrying amount.

(e) Property

Property, is stated at cost less accumulated depreciation and impairment losses.

Freehold land is not depreciated. Freehold and leasehold property, other than freehold investment properties, is stated at cost and depreciated over fifty years or the length of the lease term if shorter. Improvements to leasehold properties are stated at cost and are depreciated in equal instalments over the lesser of the remaining life of the lease or eight years. Premiums are amortised over the period of the lease.

Subsequent costs are included in the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably.

Property and equipment is assessed for impairment where there is an indication of impairment. Where impairment exists, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss recognised in the income statement. The depreciation charge for the asset is then adjusted to reflect the asset's revised carrying amount.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008

1.6 Summary of significant accounting policies (continued)

(f) Deferred costs

Commission and other acquisition costs incurred during the financial period that vary with and are related to securing new insurance contracts and/or renewing existing insurance contracts and investment contracts with DPF, but which relate to subsequent financial periods, are deferred to the extent that they are recoverable out of future revenue margins. Deferred acquisition costs ("DAC") are capitalised and amortised over the life of the contract.

Commission and other acquisition costs incurred in relation to securing investment contracts are likewise capitalised as deferred origination costs ("DOC") and amortised as the related revenue is recognised.

All other costs are recognised as expenses when incurred.

An impairment review is performed by category of business at each reporting date. Where there is any indication of impairment the carrying value is written down to the recoverable amount.

(g) Investment properties

Investment properties comprise freehold and leasehold property that are held, either to earn rental income, or for capital appreciation or both. They are initially recognised at cost and are fair valued annually. Rental income from investment properties is recognised on a straight-line basis over the term of the lease and any gains or losses arising from a change in the fair value are recognised in the income statement in the period that they occur.

(h) Reinsurance

Contracts entered into with reinsurers under which the Company is compensated for losses on insurance contracts issued by the Company, and that meet the classification requirements for insurance contracts, are classified as reinsurance contracts held. The benefits to which the Company is entitled under these contracts are recognised as reinsurance assets. These assets consist of short term balances due from reinsurers as well as longer term receivables that are dependent on the expected claims and benefits arising under the related insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts, in accordance with the terms of each reinsurance contract, and are regularly reviewed for impairment. All significant reinsurance is with Group undertakings

(i) Fair values of financial assets and liabilities

Fair value determinations for financial assets and financial liabilities are based on, if readily available, either bid market prices at the close of business on the balance sheet date for listed instruments, or broker or dealer price quotations, or by reference to current market values of another instrument which is substantially the same. If prices are not readily available, the fair value is based on either internal valuation models or management's estimate of amounts that could be realised under current market conditions, assuming an orderly liquidation over a reasonable period of time. Certain financial instruments, including financial derivative instruments, are valued using pricing models that consider, among other factors, contractual and market prices, correlation, time value of money, credit risk, yield curve volatility factors and / or prepayment rates of the underlying positions. The use of different pricing models and assumptions could produce materially different estimates of fair values.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

1.6 Summary of significant accounting policies (continued)

(j) Recognition and derecognition of financial assets and liabilities

The Company recognises financial assets and liabilities upon origination.

The Company derecognises a financial asset when the contractual rights to the cash flows from the asset expire or it transfers the right to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in the transferred financial asset that is created or retained by the Group is recognised as a separate asset.

The Company derecognises a financial liability when its contractual obligations are discharged or cancelled or expired.

(k) Derivatives

Derivatives are measured at fair value and initially recognised on the date the contract is entered into. Where the fair value of a derivative is positive, it is carried as a derivative asset and where negative as a derivative liability. The gain or loss from changes in fair value is taken directly to the income statement.

Hedge accounting allows one financial instrument, generally a derivative such as a swap, to be designated as a hedge of another financial instrument such as a loan. At inception of the hedge relationship formal documentation is drawn up specifying the hedging strategy, the component transactions and the methodology that will be used to measure effectiveness.

Monitoring of hedge effectiveness is undertaken continually. A hedge is regarded as effective if the change in fair value or cash flows of the hedge instrument and the hedged item are negatively correlated within a range of 80% to 125%, either for the period since effectiveness was last tested or cumulatively since inception.

The Company uses two hedge accounting methods.

Firstly, the Company uses fair value hedge accounting which offsets the change in the fair value of the hedging instrument against the change in the fair value of the hedged item in respect of the risk being hedged. The hedged item is adjusted for the fair value of the risk being hedged irrespective of its financial instrument classification. These changes in fair value are recognised in the income statement. Adjustments made to the carrying amount of the hedged item for fair value hedges will be amortised on an effective interest rate basis over the remaining expected life in line with the presentation of the underlying hedged item. If the hedge is highly effective the net impact on the income statement is minimised.

Secondly, hedging of net investments in foreign operations is discussed within the foreign currencies accounting policy.

A derivative may be embedded in another financial instrument, known as the host contract. Where the economic characteristics and risks of an embedded derivative are not closely related to those of the host contract, the embedded derivative is separated from the host and held separately on the balance sheet at fair value, except for those instruments that have been designated at fair value through the income statement, where the derivative is not separated from the host instrument. Changes in fair value are taken to the income statement through net trading income, and the host contract is accounted for in accordance with the policy for that class of financial instrument.

If quoted or market values are not available then derivative fair values are determined using valuation techniques that are consistent with techniques commonly used by market participants to price these instruments. These techniques include discounted cash flow analysis and other pricing models. The fair values calculated from these models are regularly compared with prices obtained in actual market transactions to ensure reliability. In all material instances these techniques use only observable market data.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008

1.6 Summary of significant accounting policies (continued)

(l) Designation of financial instruments

The Company has classified its financial instruments in accordance with IAS 39 Financial Instruments: Recognition and Measurement. In some instances the classification is prescribed whilst in others the Company is able to exercise judgement in determining the classification as follows:

Derivative instruments are classified as 'at fair value through the income statement' unless they form part of an effective hedging relationship. The Company's accounting policy for hedge accounting is described under the policy for derivatives;

Portfolios of assets and liabilities that are managed and the performance evaluated on a fair value basis in accordance with a documented risk or investment management strategy are designated on initial recognition 'at fair value through the income statement'. This includes assets in support of the long term assurance business.

Other non-derivative financial assets where there is no active market and which have fixed or determinable payments are classified as 'loans and receivables'.

Investment contract liabilities within the long term assurance business are designated by the Company as 'at fair value through the income statement';

All other financial liabilities are classified as 'at amortised cost'.

The accounting treatment of these financial instruments is set out in the relevant accounting policy.

(m) Investment securities

Investment securities comprises of equity investments and debt investments.

Investment securities designated at fair value through the income statement are carried at fair value. Gains, losses and related income are taken to other operating income as they arise, except for those related to insurance and investment business which are taken to net investment income related to insurance and investment business.

The fair values of investment securities trading in active markets are based on market prices or broker/dealer valuations. Where quoted prices on instruments are not readily and regularly available from a recognised broker, dealer or pricing service, or available prices do not represent regular transactions in the market, the fair values are estimated using quoted market prices for securities with similar credit, maturity and yield characteristics or similar valuation models. Asset backed securities ('ABS') not traded in an active market are valued using valuation models that include non-market observable inputs. These models use observed issuance prices in related asset classes, market correlations, prepayment assumptions and external credit ratings. Additional assessments are then made on possible deterioration in credit risk for each individual security and on additional liquidity considerations for particular asset classes.

(n) Insurance receivables

Insurance receivables are recognised when due and measured at fair value.

(o) Cash and cash equivalents

Cash and cash equivalents consist of cash and balances at central banks that are freely available, and loans and advances to banks with an original maturity of three months or less excluding financial assets that are held for trading purposes.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

1.6 Summary of significant accounting policies (continued)

(p) Long term assurance business liabilities

The estimation of the Company's insurance and investment contracts with discretionary participating features ('DPF') liabilities relies on a number of assumptions in forecasting future experience. The selection of appropriate assumptions requires the application of material judgement and is made with reference to historic trends, taking into account the analysis of actual versus expected experience as well as industry data.

The accounting policy for insurance contracts and investment contracts with DPF and the description of long term assurance business in Note 24(a) describe the assumptions that are made when calculating the value of these contracts, which also impact on the unallocated surplus. The Company applies significant judgement when selecting the rates of persistency to be used in these calculations. The considerations given to lapse and surrender rate assumptions are detailed in Note 24(c). The sensitivity of the Company's results to changes in certain key variables on long term insurance and investment contracts with DPF are disclosed in Note 24(d).

(q) Unallocated surplus

The unallocated surplus is accounted for as a liability as permitted by IFRS 4. The carrying value of the unallocated surplus is determined as the residual assets of the with-profit fund after providing for the with-profit liabilities in accordance with the policies described above.

(r) Taxation

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

The tax charge is analysed between tax that is payable in respect of policyholder returns and tax that is payable on shareholders' equity returns. This allocation is based on an assessment of the effective rate of tax that is applicable to shareholders' equity for the year.

Deferred tax is provided in full using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following differences are not provided: the initial recognition of assets and liabilities that affects neither accounting nor taxable profit, and overseas earnings where remittance is controlled by the Company. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, based on tax rates that are enacted or substantially enacted at the balance sheet date.

Deferred and current tax assets and liabilities are offset when they arise in the same tax reporting group and where there is both a legal right of offset and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

(s) Borrowings

All borrowings and loans taken up are initially recognised at cost, being the fair value of the consideration received, net of issue costs associated with such borrowings or loans.

After initial recognition, interest bearing borrowings and loans are subsequently measured at amortised cost, using the effective interest rate method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Subordinated liabilities consist of dated and undated loan capital. The interest payable is recognised in the income statement through interest expense.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

1.6 Summary of significant accounting policies (continued)

(t) Provisions

The Company recognises a provision if there is a present obligation as a consequence of either a legal or a constructive obligation resulting from a past event. To recognise this it should be probable that an outflow of economic resources, that can be reliably measured, will be required to settle the obligation. Provisions are measured as the discounted expected future cash flows taking account of the risks and uncertainties associated with the specific liability where appropriate.

A constructive obligation is only deemed to exist in respect of restructuring provisions once a detailed restructuring plan has been formally approved and the plan has been announced publicly or work on the restructure has commenced.

(u) Investments in subsidiaries

Investments in subsidiaries are included in the Company's financial statements. These include equity investments in, and capital contributions to subsidiary entities. These are carried at cost less impairment provisions. At each reporting date an assessment is undertaken to determine if there is any indication of impairment. This assessment can include reviewing factors such as the solvency, profitability and cash flows generated by the subsidiary. If there is an indication of impairment, an estimate of the recoverable amount is made. If the carrying value exceeds the recoverable amount then a provision for impairment is made to reduce the carrying value to the recoverable amount.

Where the Company owns a majority holding in a Collective Investment Scheme, held in support of the long term assurance liabilities, the holding has been classified as a group undertaking and fair valued at the balance sheet date with all gains and losses being accounted for through the income statement.

(v) Repurchase agreements

Securities sold subject to repurchase agreements are retained within the balance sheet where the Company retains substantially all of the risks and rewards of ownership. Funds received under these arrangements are included within deposits by banks, customer accounts or financial liabilities held for trading. Conversely, securities acquired under commitments to resell are not recognised in the balance sheet as debt securities where substantially all the risks and rewards do not pass to the Company. In this case, the purchase price is included within loans and advances to banks, loans and advances to customers, or financial assets held for trading. The difference between sale and repurchase prices for such transactions is reflected in the income statement over the lives of the transactions, within interest payable or interest receivable as appropriate

(w) Current, non current disclosure

For each asset and liability line item that combines amounts expected to be recovered or settled within twelve months after the balance sheet date, those items will be classified as current at the balance sheet date and the remaining balance will be classified as non-current.

(x) Netting

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right of offset and there is an intention and ability to settle on a net or simultaneous basis. Where master netting agreements allow for offset only on default by one of the parties, the Company presents the disclosures on a gross basis.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

1.6 Summary of significant accounting policies (continued)

(y) Foreign currency

The financial statements are presented in Sterling which is the Company's functional and presentation currency.

Foreign currency transactions are translated into Sterling at the exchange rate prevailing at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated at balance sheet date exchange rates. Exchange differences arising, including those from changes in the amortised cost of foreign currency monetary available for sale assets, are recognised in the income statement except for differences arising from hedges of net investments in foreign operations and derivatives related to cash flow hedges which are recognised directly in equity.

Non-monetary assets and liabilities carried at historical cost are translated using the historical exchange rate.

The results and financial position of all group entities that have a functional currency different from sterling are translated into sterling as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of the balance sheet; and

- income and expenses are translated at the average exchange rates for the period (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions).

All resulting exchange differences are recognised in retained earnings within equity.

(z) IFRS and IFRIC not yet applied

The following standards and interpretations have not yet been adopted by the European Union, are not effective for the year ended 31 December 2008 and have not been applied in preparing the financial statements. Where appropriate disclosures will be revised in the financial statements in the year in which the standard or interpretation becomes applicable.

IFRS 8 'Operating Segments' which is effective for periods commencing on or after 1 January 2009. This standard replaces IAS 14 'Segmental Reporting' and its application will not have any impact upon the financial results of the Company as it does not change the recognition or measurement of transactions in the consolidated financial statements. The standard aligns the disclosure of operating segments in the financial statements with the internal reporting of segments to senior management. Adoption by the Company will modify the measurement basis for segments and extend the disclosures for segment reporting in the consolidated financial statements.

Amendments to IAS 1 'Presentation of Financial Statements: A Revised Presentation' which is effective for periods commencing on or after 1 January 2009. The revised standard will affect the presentation of owner changes in equity and of comprehensive income. Adoption will not change the recognition, measurement or disclosure of specific transactions or events as required by other standards.

IFRS 1 'First-time adoption of IFRS' which is effective for periods commencing on or after 1 January 2009. As the Group and Company reports under IFRS, the application of this amendment in 2008 would not have any effect upon the financial statements.

Amendments to IAS 27 'Consolidated and Separate Financial Statements' which is effective for periods commencing on or after 1 January 2009. This amendment removes the definition of the cost method of accounting for an investment in a subsidiary. Application in 2008 would not have had an effect upon the financial statements.

'Improvements to IFRS 2008' The majority of these improvements are effective for periods commencing on or after 1 January 2009 and their application would not have had a material effect upon the financial statements.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

1.6 Summary of significant accounting policies (continued)

Amendments to IAS 39 'Financial Instruments: Recognition and Measurement: Eligible Hedged Items' which is effective for periods commencing on or after 1 July 2009. This amendment clarifies what can be designated as a hedged item in a hedge accounting relationship and application in 2008 would not have had a material impact upon the financial statements.

Amendments to IAS 39 'Reclassification of Financial Assets': Effective Date and Transition which is effective on or after 1 July 2008. This amendment clarifies the effective date and transition requirements for the change to the standard issued in October 2008 permitting entities to reclassify non derivative financial assets out of the fair value through profit and loss category in particular circumstances. The application of this amendment would not have affected the financial statements as the Group accounting policy accords with the requirements.

Revised IFRS 3 'Business Combinations' and amended IAS 27 'Consolidated and Separate Financial Statements'. These changes are effective for periods beginning on or after 1 July 2009 with the main effects being that the cost of investment will comprise the consideration paid to the vendors for equity with acquisition costs being expensed immediately; goodwill will be accounted for only upon the acquisition of a subsidiary as subsequent changes in interest will be recognised in equity and only upon the loss of control will any profit or loss be recognised in income. Further, any pre-existing stake held will, where control is subsequently gained, be revalued with any profit or loss arising being booked to income. These changes will affect the manner in which acquisitions and disposals made by the Company are accounted for after the implementation of the revised Business Combinations standard and related revisions to IAS 27.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

2. Use of estimates, assumptions and judgments

The principal use of estimates, assumptions and judgements are as follows:

(a) Claims liability arising from insurance contracts

The estimation of the ultimate liability arising from claims made under insurance contracts is the Company's most critical accounting estimate. There are several sources of uncertainty that need to be considered in the estimation of the liability that the Company will ultimately pay for those claims.

For life insurance contracts, estimates are made as to the expected number of deaths for each of the years in which the Company is exposed to risk. The Company bases these estimates on standard industry and national mortality tables that reflect historical mortality experience, adjusted where appropriate to reflect the Company's unique risk exposure. The estimated number of deaths determines the value of possible future benefits to be paid out, which will be factored into ensuring sufficient cover by reserves, which in return is monitored against current and future premiums. For those contracts that insure risk to longevity, prudent allowance is made for expected future mortality improvements, but epidemic, as well as wide ranging changes to lifestyle, could result in significant changes to the expected future mortality exposure. All of these result in even more uncertainty in estimating the ultimate liability.

Estimates are also made as to future investment income arising from the assets backing life insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments.

Estimates for future deaths, voluntary terminations, investment returns and administration expenses are used to calculate the liability over the term of the contract. At each reporting date, these estimates are reassessed for adequacy and changes will be reflected in adjustments to the liability.

Stochastic valuation techniques are used to assess the value of options and guarantees in the with-profit fund.

(b) Investment contracts fair value

The Company issues investment contracts that are designated at fair value through the income statement. For the financial instruments that are not quoted in active markets, their fair values are determined by using valuation techniques. Such techniques (which are internally generated valuation models), are validated and periodically reviewed by an independently qualified person. A variety of factors are considered in these valuation techniques, including time value of money, credit risk and volatility factors. Changes in assumptions about these factors could have a material impact on the reported fair values of these financial instruments.

(c) Financial assets at fair value through the income statement

Fair values are based on quoted market prices for the specific instrument, comparisons with other highly similar financial instruments, or the use of valuation models. As a result of the potential uncertainty in computed fair values, valuation adjustments are an integral part of the valuation process and are applied consistently from period to period. Establishing valuations inherently involves the use of judgement and management also applies its judgement in establishing reserves against indicated valuations for aged positions, deteriorating economic conditions (including country specific risks), concentrations in specific industries, types of instruments or currencies, market liquidity, model risk itself and other factors.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

3. Net insurance revenue

	2008 £m	2007 £m
With DPF	118.5	151.3
Without DPF	666.4	491.2
Gross insurance contract premium revenue	**784.9**	642.5
With DPF	-	-
Without DPF	(155.2)	(162.2)
Reinsurers' share of insurance contract premium revenue	**(155.2)**	(162.2)
With DPF	118.5	151.3
Without DPF	511.2	329.0
Total net insurance premium revenue	**629.7**	480.3

4. Investment income

	2008 £m	2007 £m
Financial assets at fair value through Income Statement		
Interest income	**193.0**	227.2
Dividend income	**397.1**	349.2
Cash and cash equivalents interest income	**5.6**	5.8
Rental income from investment properties	**123.5**	129.3
Foreign currency translation differences	**1,134.9**	320.7
Other	77.9	125.9
Total investment income	1,932.0	1,158.1

5. Net fair value (losses) / gains recorded in the income statement

	2008 £m	2007 £m
Net loss on financial assets at fair value through income statement	**(2,709.0)**	(715.9)
Net loss on investment properties	**(731.8)**	(257.9)
Net gain / (loss) on derivative hedging instrument	**41.0**	(16.1)
Net (loss) / gain on hedged loan	**(41.1)**	15.8
Net gain / (loss) on derivative financial instruments	**249.0**	(32.7)
Total net fair value losses recorded in the income statement	**(3,191.9)**	(1,006.8)

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

6. Net insurance claims and benefits

	2008 £m	2007 £m
With DPF	651.1	594.3
Without DPF	278.9	304.4
Gross insurance contract claims and benefits paid	**930.0**	898.7
With DPF	-	-
Without DPF	(201.5)	(202.4)
Reinsurers' share of gross insurance contract claims and benefits paid	**(201.5)**	(202.4)
With DPF	651.1	594.3
Without DPF	77.4	102.0
Total insurance contract claims and benefits paid	**728.5**	696.3
With DPF	202.1	53.9
Without DPF	3,046.7	65.9
Gross change in insurance contract liabilities	**3,248.8**	119.8
With DPF	-	-
Without DPF	23.8	(132.3)
Reinsurers' share of change in insurance contract liabilities	**23.8**	(132.3)
With DPF	202.1	53.9
Without DPF	3,070.5	(66.4)
Total change in insurance contract liabilities	**3,272.6**	(12.5)
Total insurance claims and benefits paid and net change in insurance contract liabilities	**4,001.1**	683.8

7. Finance income and finance costs

	2008 £m	2007 £m
Finance income		
Interest receivable on SWAP	**28.5**	22.6
Interest income from group undertakings	**17.5**	20.5
Total finance income	**46.0**	43.1
Finance costs		
Interest expense on bank overdraft	**3.3**	6.3
Interest payable on subordinated debt	**62.5**	55.5
Interest payable on swap	**36.9**	27.1
Other interest	**0.4**	0.3
Total finance costs	**103.1**	89.2

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

8. Other operating and administration expenses

	2008 £m	2007 £m
Acquisition costs	**60.7**	51.7
Amortisation and impairment of intangible assets	**28.3**	85.0
Auditors' remuneration		
Fee for statutory audit	**0.8**	0.7
Fee for audit of reports to regulators	**0.1**	0.1
Expenses relating to investment properties generating rental income	**13.0**	7.8
Investment management expenses	**92.2**	97.4
Management fee paid to HBOS plc	**132.6**	191.3
Impairment of subsidiaries	**33.0**	-
Total other operating and administration expenses	**360.7**	434.0

The profit of the company is stated after charging an amount of £3.1m (2007: £2.9m) in respect of services received by the company which have been settled by way of share-based payment arrangements. All staff providing services to the company are employed by the ultimate parent undertaking, HBOS plc, in whose shares settlement is made. The amount charged is recharged on a proportionate basis from HBOS plc. Details of the share-based payment schemes within the HBOS Group are included on an aggregated basis in the HBOS plc consolidated financial statements.

Costs recharged for staff providing services to the Company include contributions to defined benefit and defined contribution pension schemes. Details of these schemes are included in the financial statements of HBOS plc. Contributions to defined benefit schemes amounted to £1.3m (2007: £2.6m). Contributions to defined contribution schemes amounted to £2.0m (2007: £0.9m).

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

9. Tax on (loss) / profit

(a) Current year tax credit

	2008 £m	2007 £m
Current tax	90.6	(69.2)
UK corporation tax charge for the period	(50.0)	(87.2)
UK corporation tax credit in respect of earlier periods	140.6	18.0
Deferred tax	205.5	182.2
Deferred tax credit for the period	206.3	153.2
Impact of change in UK tax rate	-	12.2
Deferred tax (charge) / credit in respect of earlier periods	(0.8)	16.8
Total tax credit	296.1	113.0

	2008 £m	2007 £m
Income tax credit relating to policyholders	172.8	74.6
Income tax credit relating to shareholders	123.3	38.4
Total income tax credit on profit / (loss)	296.1	113.0

(b) Reconciliation of tax on profit / (loss)

	2008 £m	2007 £m
Loss / (profit) before taxation	(34.2)	379.3
Tax on loss / (profit) at domestic corporation tax rate of 28.5%	9.7	(113.8)
Income not subject to tax	17.2	140.1
Differences due to UK basis of life taxation	(48.6)	(19.0)
Losses not previously recognised	-	-
Prior year movements relating to shareholder tax	142.6	19.7
Impact of change in UK tax rate	-	12.2
Effect of tax rates in foreign jurisdictions	2.4	(0.8)
Total tax attributable to shareholders	123.3	38.4
Policyholder tax	172.8	74.6
Total income tax credit	296.1	113.0

(c) Tax charged to equity

	2008 £m	2007 £m
Deferred tax	-	6.2
Total tax charge to equity	-	6.2

	2008 £m	2007 £m
Tax charge to equity relating to shareholders	-	6.2
Total tax charged to equity	-	6.2

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

10. Intangible assets

	2008 Software development cost	2008 PVIF	2008 Total	2007 Software development cost	2007 PVIF	2007 Total
	£m	£m	£m	£m	£m	£m
Cost						
At 1 January	**0.9**	**651.4**	**652.3**	-	651.4	651.4
Additions	5.1	-	5.1	0.9	-	0.9
At 31 December	**6.0**	**651.4**	**657.4**	0.9	651.4	652.3
Accumulated amortisation and impairment						
At 1 January	-	**(358.3)**	**(358.3)**	-	(273.2)	(273.2)
Amortisation	(0.9)	(27.4)	(28.3)	-	(36.8)	(36.8)
Impairment	-	-	-	-	(48.3)	(48.3)
Disposals	-	-	-	-	-	-
At 31 December	**(0.9)**	**(385.7)**	**(386.6)**	-	(358.3)	(358.3)
Net book value at 31 December	**5.1**	**265.7**	**270.8**	0.9	293.1	294.0

11. Property

	2008	2007
	£m	£m
Cost		
At 1 January	**161.4**	202.5
Additions	**20.4**	25.9
Disposals	**(53.2)**	(58.4)
Transferred to investment properties (note 13)	**(51.2)**	(8.6)
At 31 December	**77.4**	161.4
Accumulated depreciation		
At 1 January	-	-
Depreciation charge for the year	-	-
Disposals	-	-
At 31 December	-	-
Net book value at 31 December	**77.4**	161.4

Included within property are assets that are in the course of construction, including properties that will be classified as investment properties upon completion, amounting to £68.6m (2007: £161.0m). Included in the assets in the course of construction is land amounting to £19.2m (2007: £29.7m).

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

12. Deferred costs

	2008 Deferred acquisition costs £m	2008 Deferred origination costs £m	2008 Total £m	2007 Total £m
At 1 January	100.3	312.8	413.1	315.1
Acquisition costs deferred during the year	52.3	116.8	169.1	177.6
Acquisition costs, transferred during the year	124.3	(123.5)	0.8	-
Amortisation / origination	(50.4)	(54.7)	(105.1)	(79.6)
At 31 December	226.5	251.4	477.9	413.1

During the year to 31 December 2008, changes have been made to certain investment bonds with additional life cover being added. In accordance with IFRS 4 'Insurance Contracts', this results in these products transferring from being accounted for as investment contracts to insurance contracts, which has resulted in a £124.3m increase in deferred acquisition costs.

13. Investment properties

	2008 £m	2007 £m
Balance at 1 January	2,274.1	2,764.2
Net disposals	(102.3)	(240.8)
Transferred from property (note 11)	51.2	8.6
Net fair value losses	(731.8)	(257.9)
Balance at 31 December	1,491.2	2,274.1

Investment properties are stated at fair value and are considered to be realisable within 12 months. Fair value adjustments are recorded in the income statement.

During the year ended 31 December 2008, £123.5m (2007: £129.3m) was recognised as rental income in the income statement and £13.0m (2007: £7.8m) in respect of direct operating expenses was recognised as an expense in the income statement relating to investment property.

Within additions is included an amount of £69.2m (2007: £70.0m) representing capitalised expenditure.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

14. Investment in Group undertakings and participating interests

Particulars of the Company's principal group undertakings and participating interests are shown below. Other holdings in group undertakings and participating interests are not considered to be material.

Group Undertakings	Country of Incorporation or Registration	Type of business		% Held
Clerical Medical Managed Funds Limited	England and Wales	Life Insurance	*	100.0
Halifax Life Limited	England and Wales	Life Insurance	*	100.0
Clerical Medical Forestry Limited	England and Wales	Property Investments	*	100.0
CM Venture Investments Limited	Isle of Man	Investment Company	*	100.0
Lands Improvement Holdings plc	England and Wales	Investment Company	*	100.0
CM Non Sterling Property Company S.A.R.L.	Luxembourg	Property Investments	*	100.0
CMI Universe – Austrian	Luxembourg	Open-Ended Investment Company		100.0
CMI Universe – CMIG Access 80%	Luxembourg	Open-Ended Investment Company		100.0
CMI Universe – Euro Top 50 Equity	Luxembourg	Open-Ended Investment Company		100.0
Insight Discretionary – Investment Fund of Funds II – ICVC	England and Wales	Open-Ended Investment Company		99.9
Insight Discretionary – Euro S Cap	England and Wales	Open-Ended Investment Company		97.1
Global Investment ICVC - HBOS Far East Focus Fund	England and Wales	Open-Ended Investment Company		82.8
UK & Fixed Interest ICVC - HBOS UK Strategic (130/30) Fund	England and Wales	Open-Ended Investment Company		66.6
Global Investment ICVC - HBOS European Strategic (130/30) Fund	England and Wales	Open-Ended Investment Company		66.5
Global Investment ICVC - HBOS US Strategic (130/30) Fund	England and Wales	Open-Ended Investment Company		66.5
Global Investment ICVC - HBOS Japan Focus Fund	England and Wales	Open-Ended Investment Company		66.4
UK & Fixed Interest ICVC - HBOS UK Focus Fund	England and Wales	Open-Ended Investment Company		66.4
UK & Fixed Interest ICVC - HBOS UK High Income Fund	England and Wales	Open-Ended Investment Company		66.4
Global Investment ICVC - HBOS Emerging Markets Focus Fund	England and Wales	Open-Ended Investment Company		66.1
Global Investment ICVC - HBOS US Focus Fund	England and Wales	Open-Ended Investment Company		66.1
Global Investment ICVC - HBOS European Focus Fund	England and Wales	Open-Ended Investment Company		66.0
UK & Fixed Interest ICVC - HBOS UK Smaller Companies Fund	England and Wales	Open-Ended Investment Company		66.0
Insight Discretionary – Euro Disc	England and Wales	Open-Ended Investment Company		64.4
Global Investment ICVC - HBOS European Special Situations Fund	England and Wales	Open-Ended Investment Company		62.2
Actively Managed ICVC - HBOS Absolute Return Fund	England and Wales	Open-Ended Investment Company		62.1
Insight Professional – UK Small Cap	England and Wales	Open-Ended Investment Company		58.4
Actively Managed ICVC - HBOS Diversified Income Fund	England and Wales	Open-Ended Investment Company		51.3
Actively Managed ICVC - HBOS Diversified Return Fund	England and Wales	Open-Ended Investment Company		51.2

* These subsidiary undertakings are direct subsidiaries of the Company. All subsidiary shares held are ordinary shares.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

14. Investment in Group undertakings and participating interests (continued)

	Group undertakings	Collective Investment Schemes	Total
	Ordinary Shares £m	Ordinary Shares £m	£m
Valuation			
31 December 2007	935.9	5,223.3	6,159.2
31 December 2008	**1,114.7**	**912.7**	**2,027.4**
Cost			
31 December 2007	935.9	4,626.0	5,561.9
31 December 2008	**1,114.7**	**1,232.0**	**2,346.7**

15. Reinsurance assets

	2008 £m	2007 £m
Reinsurers' share of insurance contracts (note 21)	**2,270.4**	2,294.2
Reinsurers' share of investment contracts (note 23)	**7,464.0**	8,802.9
Total reinsurance assets	**9,734.4**	11,097.1

	2008 £m	2007 £m
Current reinsurance assets	**901.4**	1,000.2
Non current reinsurance assets	**8,833.0**	10,096.9
Total reinsurance assets	**9,734.4**	11,097.1

16. Prepayments and accrued income

	2008 £m	2007 £m
Total prepayments	**25.8**	17.3
Other prepayments	**25.8**	17.3
Total accrued income	**15.6**	19.4
Rent	**15.6**	19.4
Total prepayments and accrued income	**41.4**	36.7

The carrying amounts disclosed above reflect the fair values at year end. It is expected that all prepayments and accrued income will be realised within a year from the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

17. Derivative financial instruments

The Company's collateralised derivative financial instruments are classified as held for trading. A variety of equity futures are part of the portfolio matching the unit linked investment and insurance liabilities.

In 2007, the Company purchased interest rate swap contracts to exchange the fixed rate on the subordinated debt (shown in note 30) for a floating rate, in line with group accounting policy. The risk of a fixed interest rate is borne by Bank of Scotland Treasury.

The fair values of derivative financial instruments at the year end are as follows:

	2008		2007	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Foreign exchange derivatives				
Forward foreign exchange	53.0	29.6	-	-
Interest rate derivatives				
Interest rate swaps	60.2	33.0	-	-
Options	147.2	2.5	56.4	1.1
Futures	52.0	40.5	0.5	0.5
Equity and commodity related contracts				
Options and swaps	341.8	25.5	0.3	-
Held for hedging				
Interest rate swaps	11.3	-	44.3	36.3
Total derivative financial assets / liabilities	665.5	131.1	101.5	37.9

	2008 £m	2007 £m
Current net derivative financial instruments	534.4	63.6
Non current net derivative financial instruments	-	-
	534.4	63.6

In order to improve the presentation of derivative financial instruments, more detail on the types of instruments has been provided in the table above. The 2007 derivatives have been amended accordingly.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

18. **Financial assets at fair value through income statement**

	Fair value through income statement 2008 £m	Fair value through income statement 2007 £m
Equity investments		
Listed	**5,027.2**	5,962.9
Unlisted	**147.7**	-
Total	**5,174.9**	5,962.9
Debt investments		
Listed	**8,364.6**	5,772.6
Unlisted	**216.0**	3.0
Total	**8,580.6**	5,775.6
Total financial assets at fair value through income statement	**13,755.5**	11,738.5

The Company enters into securities lending transactions and repurchase agreements, whereby cash and securities are temporarily received or transferred as collateral. Where the securities sold subject to repurchase are retained on the balance sheet the funds received under these arrangements are recognised as liabilities. Assets and liabilities relating to such arrangements at 31 December are as follows:

	Asset		**Related Liability**	
	2008 £m	2007 £m	**2008 £m**	2007 £m
Equity Investments	**255.8**	1,407.6	**265.4**	1,465.3
Debt Investments	**1,601.1**	2,855.8	**1,770.2**	3,139.9
Assets subject to repurchase	**1,856.9**	4,263.4	**2,035.6**	4,605.2

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

19. Insurance and other receivables

Insurance receivables

	2008 £m	2007 £m
Due from policyholders	4.2	39.5
Due from agents, brokers and intermediaries	0.7	10.0
Total insurance receivables	4.9	49.5

	2008 £m	2007 £m
Current insurance receivables	4.9	49.5
Non current insurance receivables	-	-
	4.9	49.5

Other receivables

	2008 £m	2007 £m
Due from related parties	512.6	433.7
Outstanding interest, dividends and rent	79.6	89.2
Outstanding proceeds from sale of investments	4.9	5.8
Other receivables	45.1	29.3
Total other receivables	642.2	558.0

	2008 £m	2007 £m
Current other receivables	453.4	395.0
Non current other receivables	188.8	163.0
	642.2	558.0

The carrying amounts disclosed above reflect fair values at year end.

20. Cash and cash equivalents

	2008 £m	2007 £m
Cash at bank and in hand	265.9	82.8
Short term deposits	23.4	185.0
Total cash and cash equivalents	289.3	267.8

The effective interest rate on short term bank deposits was 3.4% (2007: 4.1%) and these deposits have an average maturity of 1 day.

Policyholder funds include £48.0m (2007: £84.8m) cash and cash equivalents. This is not available to settle liabilities outside of the policyholder funds.

Included in cash at bank and in hand is cash held with a related party, Bank of Scotland Plc, of £80.7m (£2007: £22.8m).

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

21. Insurance contract liabilities

		2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
With DPF	(a)	5,256.3	-	5,256.3
Without DPF	(b)	5,485.7	(2,270.4)	3,215.3
Total insurance contract liabilities		10,742.0	(2,270.4)	8,471.6

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Current insurance contract liabilities	1,227.0	(174.0)	1,053.0
Non current insurance contract liabilities	9,515.0	(2,096.4)	7,418.6
	10,742.0	(2,270.4)	8,471.6

(a) Insurance contracts with DPF

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Opening balance	5,306.3	-	5,306.3
Movement	(62.5)	-	(62.5)
Changes in assumptions	12.5	-	12.5
Closing balance	5,256.3	-	5,256.3

(b) Insurance contracts without DPF

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Opening balance	2,705.8	(2,294.2)	411.6
Movement	142.7	20.2	162.9
Changes in assumptions	34.4	3.6	38.0
Transfer In (note 12)	2,602.8	-	2,602.8
Closing balance	5,485.7	(2,270.4)	3,215.3

(c) Summary of (a) and (b)

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Opening balance	8,012.1	(2,294.2)	5,717.9
Movement	80.2	20.2	100.4
Changes in assumptions	46.9	3.6	50.5
Transfer In (note 12)	2,602.8	-	2,602.8
Closing balance	10,742.0	(2,270.4)	8,471.6

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

21. **Insurance contract liabilities (continued)**

		2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
With DPF	(a)	5,306.3	-	5,306.3
Without DPF	(b)	2,705.8	(2,294.2)	411.6
Total insurance contract liabilities		8,012.1	(2,294.2)	5,717.9

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Current insurance contract liabilities	846.7	(217.5)	629.2
Non current insurance contract liabilities	7,165.4	(2,076.7)	5,088.7
	8,012.1	(2,294.2)	5,717.9

(a) **Insurance contracts with DPF**

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Opening balance	5,869.6	-	5,869.6
Movement	(628.4)	-	(628.4)
Changes in assumptions	65.1	-	65.1
Closing balance	5,306.3	-	5,306.3

(b) **Insurance contracts without DPF**

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Opening balance	2,632.6	(2,161.9)	470.7
Movement	158.3	(127.9)	30.4
Changes in assumptions	(55.0)	(4.4)	(59.4)
Impact of PS06/14	(30.1)	-	(30.1)
Closing balance	2,705.8	(2,294.2)	411.6

(c) **Summary of (a) and (b)**

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Opening balance	8,502.2	(2,161.9)	6,340.3
Movement	(470.1)	(127.9)	(598.0)
Changes in assumptions	10.1	(4.4)	5.7
Impact of PS06/14	(30.1)	-	(30.1)
Closing balance	8,012.1	(2,294.2)	5,717.9

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

22. Unallocated surplus

	2008 £m	2007 £m
Opening balance	**1,497.4**	1,569.4
Movement	**(1,014.5)**	22.7
Changes in liability assumptions	**(13.7)**	(94.7)
Closing balance	**469.2**	1,497.4

23. Investment contract liabilities

		2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Investment contracts with DPF	(a)	6,166.0	-	6,166.0
Investment contracts without DPF	(b)	7,768.5	(7,464.0)	304.5
Total investment contract liabilities		13,934.5	(7,464.0)	6,470.5

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Current investment contract liabilities	1,445.4	(727.4)	718.0
Non current investment contract liabilities	12,489.1	(6,736.6)	5,752.5
	13,934.5	(7,464.0)	6,470.5

(a) Investment contracts with DPF

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Opening balance	7,203.4	-	7,203.4
Movement	(1,038.6)	-	(1,038.6)
Changes in assumptions	1.2	-	1.2
Closing balance	6,166.0	-	6,166.0

(b) Investment contracts without DPF

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Opening balance	12,422.1	(8,802.9)	3,619.2
Movement	(2,017.2)	1,338.9	(678.3)
Changes in assumptions	6.6	-	6.6
Transfer Out (note 12)	(2,643.0)	-	(2,643.0)
Closing balance	7,768.5	(7,464.0)	304.5

(c) Summary of (a) and (b)

	2008 Gross liabilities £m	2008 Reinsurance £m	2008 Net of reinsurance £m
Opening balance	19,625.5	(8,802.9)	10,822.6
Movement	(3,055.8)	1,338.9	(1,716.9)
Changes in assumptions	7.8	-	7.8
Transfer Out (note 12)	(2,643.0)	-	(2,643.0)
Closing balance	13,934.5	(7,464.0)	6,470.5

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

23. Investment contract liabilities (continued)

		2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Investment contracts with DPF	(a)	7,203.4	-	7,203.4
Investment contracts without DPF	(b)	12,422.1	(8,802.9)	3,619.2
Total investment contract liabilities		19,625.5	(8,802.9)	10,822.6

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Current investment contract liabilities	2,462.6	(782.7)	1,679.9
Non current investment contract liabilities	17,162.9	(8,020.2)	9,142.7
	19,625.5	(8,802.9)	10,822.6

(a) Investment contracts with DPF

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Opening balance	8,549.7	-	8,549.7
Movement	(1,335.9)	-	(1,335.9)
Changes in assumptions	(10.4)	-	(10.4)
Closing balance	7,203.4	-	7,203.4

(b) Investment contracts without DPF

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Opening balance	11,571.8	(8,191.0)	3,380.8
Movement	850.3	(611.9)	238.4
Changes in assumptions	-	-	-
Closing balance	12,422.1	(8,802.9)	3,619.2

(c) Summary of (a) and (b)

	2007 Gross liabilities £m	2007 Reinsurance £m	2007 Net of reinsurance £m
Opening balance	20,121.5	(8,191.0)	11,930.5
Movement	(485.6)	(611.9)	(1,097.5)
Changes in assumptions	(10.4)	-	(10.4)
Closing balance	19,625.5	(8,802.9)	10,822.6

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

24. Insurance and investment contract liabilities – Terms, assumptions and sensitivities

(a) Long term assurance

The Company principally writes the following contracts which contain insurance risk:

- Life assurance – the policyholder is insured against death or permanent disability usually for pre-determined amounts (principally mortality and disability risk).
- Annuity products – the policy holder is entitled to payments for life and is therefore insured against living longer than expected (principally longevity and market risk).
- Traditional with-profits business – the primary purpose of these products is to provide a long term smoothed investment vehicle to the policyholder, protecting them against short term market fluctuations. The policyholder is also usually insured against death and the policy may carry an annuity option at maturity (principally market risk).
- Unitised business - the primary purpose of these products is to provide an investment vehicle but where the policyholder is also insured against death (principally market risk).

(b) Options and guarantees

The products with the most significant guarantees and options include with-profit bonds, which allow withdrawals to be taken without penalty and bonds encashed at a specific date on guaranteed terms. In addition certain pension contracts contain an option that allows the policyholder to take an annuity benefit at any time between their 60th and 75th birthday at annuity rates that were guaranteed at the outset of the contract.

For contracts where there are guarantees and options the most significant factor determining the cost of the guarantees and options (other than economic conditions in which the option or guarantee has value) is the actual take up rate of options. The most significant factor in determining take up rates is customer behaviour which is influenced by a number of factors, including the value of the contracts, general awareness of financial matters and the quality of advice they obtain. The financial impact is dependent on the value of corresponding investments, interest rates and longevity at the time of the claim.

In order to quantify the risks of these guarantees the Company makes use of stochastic modelling techniques to determine the possible and most likely ranges of outcomes. Additionally, the Company makes use of matching techniques in order to match part of the expected cash flows arising under contracts with financial instruments.

(c) Assumptions

The key assumptions used in the measurement of liabilities for insurance contracts and investment contracts with DPF are determined by the Board on advice from the Actuarial Function Holder. Material judgment is required in the choice of assumptions relating to insurance contracts and investment contracts with DPF. The assumptions that have the greatest effect on the income statement of the Company are:

<u>Mortality and longevity rates</u>

The process used to determine the Company's mortality and longevity assumptions starts with an internal investigation of the Company's actual mortality experience over the last five years. This investigation is updated regularly. The results of this investigation are considered in the context of a number of factors including the credibility of results (which will be affected by the volume of data available), any exceptional events that have occurred during the period being considered, any known or expected trends in underlying data and relevant published market data.

The rates derived from the Company's experience are adjusted in the light of the factors mentioned above to derive a set of "best estimate" rates. No deliberate margins for prudence are introduced as part of this process. These "best estimate" assumptions will be used in the projections of "best estimate" cash flows. For insurance and investment with DPF contracts within the non profit funds, the liabilities are assessed on a prudent basis and hence the rates used need to include a margin for adverse deviation that will increase liabilities and provide some protection from the risk that actual experience is worse that the "best estimate" assumptions. The intention is that the margin added should be sufficiently prudent that there is no significant foreseeable risk that liabilities to policyholders will not be met as they fall due. Additionally trends in mortality improvement are only anticipated where they will increase the liability.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

24. Insurance and investment contract liabilities – Terms, assumptions and sensitivities (continued)

(c) Assumptions (continued)

Mortality and longevity rates (continued)

The following assumptions are used:

Portfolio assumptions by type of business impacting net liabilities	Mortality		Valuation rate of interest	
	2008	2007	2008	2007
Non profit Policies				
Pension Annuities Males	85% PCMA00(mc) with minimum 1.5% improvement	97.5% PMA92 (mc) with minimum 1.5% improvements	4.81%	4.99%
Females	90% PCFA00 (75%mc) with minimum 1% improvement	80% PFA92 (75% mc) with minimum 1% improvements	4.81%	4.99%
Term Assurances Males	22-49.5% AM92 Ult	60.5-71.5% AM92 Ult	1.94%-2.43%	4.06% - 5.08%
Females	22-44% AF92 Ult	58.3-71.5% AF92 Ult	1.94%-2.43%	4.06% - 5.08%
With Profit Policies				
Guaranteed Annuity Options Males	90% PMA00 (mc) with minimum 1.5% improvements	103% PMA92 (mc) with minimum 1.5% improvements	Market consistent stochastic deflators calibrated to gilt yield curve	Market consistent stochastic deflators calibrated to gilt yield curve
Females	95% PFA00 (75% mc) with minimum 1% improvements	90% PFA92 (75% mc) with minimum 1% improvements		
Unitised With-profit Sterling Reserves		55%-77% AM92 Ult/77%-132% AF92 Ult	2.99% unit growth rate (net)	4.55% Unit Growth Rate
Life assurance	60.5%-77% AM92 Ult / 77% - 121% AF92 Ult	49.5% AM80 Ult/132% AF80 Ult		
Pensions	22%-66% AM92 Ult/ 22%-82.5% AF92 Ult	55%-88% AM/F92 Ult	3.74% unit growth rate	4.55% Unit Growth Rate

For life assurance policies, increased mortality rates would lead to a larger number of claims and claims occurring sooner than anticipated, increasing the expenditure and reducing profits for shareholders.

24. Insurance and investment contract liabilities – Terms, assumptions and sensitivities (continued)

For annuity contracts, lower longevity (or equivalently, increased mortality) would decrease payments thereby reducing expenditure and increasing profits for the shareholders.

Investment return

Investment Return assumptions are used to calculate the future projected cash flows in order to calculate the non-unit reserves on unitised insurance contracts and on unitised investment contracts with DPF. The return assumed is the 15 year gilt yield. In isolation an increase in the investment return assumption for these policies would lead to lower non-unit reserves and so higher shareholder profits.

For annuity contracts the assets and liabilities are broadly matched meaning that a change in the long term investment return would have a limited impact on shareholder profits.

Valuation rate of interest

The valuation rate of interest is the rate used to discount the projected cash flows on the contracts in order to determine the value of liabilities as at the date of reporting.

For insurance and investment with DPF contracts in the non profit funds, the liabilities are calculated using a prudent valuation rate of interest determined according to specific rules set out by the Financial Services Authority. These rules specify that the valuation rate of interest should be set by reference to a prudent estimate of the future yield on the assets of the fund with an additional prudent margin being taken to allow for future investment risk. For insurance and investment contracts with DPF in the with-profit funds the liabilities are calculated using a market consistent stochastic model calibrated to the prevailing gilt yield curve at the time of the liability assessment. The volatility of future investment returns is a key assumption within the model.

An increase in the valuation rate of interest in isolation would lead to an increase in shareholder profits.

Expense and expense inflation

Operating expense assumptions reflect the projected costs of maintaining and servicing in force policies and associated overhead expenses. The current expenses are analysed having regard to the volume and type of business in-force to derive per policy expense assumptions. These per policy assumptions are assumed to increase over the course of the projections in line with assumed inflation rates. An increase in the level of expenses would reduce profits for the shareholders.

Lapse, paid up and surrender rates (persistency)

A lapse occurs when the termination of a policy results from the non-payment of premiums due under that policy. A surrender occurs when a policyholder decides voluntarily to terminate their policy. A policy becomes paid up when premiums cease but the policy still has a value.

The process used to determine policy lapse and surrender rates is similar to that used to determine mortality and longevity rates. The previous experience of the Company is analysed using statistical techniques. As the experience can vary considerably between different product types and for policies which have been in-force for different periods, the internal analysis breaks the data down into homogeneous groups for the purpose of this analysis. This analysis is updated regularly.

For investment with DPF contracts within the with-profit fund, the liabilities are required to be determined using realistic or "best estimate" assumptions.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

24. Insurance and investment contract liabilities – Terms, assumptions and sensitivities (continued)

(c) Assumptions (continued)

For all other business no lapse or surrender assumptions are used in the determination of the policy liabilities.

Lapses and surrenders vary according to both contract type and length of time a contract has been in force. No lapses and surrenders have been presented because it is impracticable to summarise information in a meaningful way.

The impact of an increase / decrease in lapse and surrender rates on contracts without guarantees and options would most likely result in a decrease / increase in profits as the contract would no longer be / continue to be in force to generate cash flows in the future. However, for certain policies with valuable guarantees and options (principally within the with-profit fund), increased / decreased lapse and surrender rates may be beneficial / detrimental to the Company as the policyholder loses / retains the ability to exercise the potentially valuable guarantee or option when / until their policy terminates.

Discretionary participating bonus rates

The determination of distributions to insurance and investment with DPF contract policyholders is made by the Board based on local regulations and in line with arrangements in individual policy contracts. For contracts with DPF in the With-profits fund distributions to policyholders are governed by the principles and practices set out in the fund's Principles and Practices for Financial Management ("PPFM"). No changes were made to the distribution policies for contracts with discretionary participation features during the year under review.

(d) Sensitivities

In general the liabilities are broadly matched by the backing assets and hence the value of shareholder equity at the valuation date is relatively insensitive to changes in financial conditions and investment markets:

- An increase in interest rates at the valuation date would result in a reduction in shareholder equity due to a fall in the value of fixed interest investments in the shareholder.
- A fall in equity and property market values would result in an increase in non-unit reserves on unit-linked insurance business and hence the value of shareholder equity would reduce. Realistic reserves on contracts with DPF would fall.

The value of shareholder equity at the valuation date would also be impacted by changes in future expenses and demographic experience:

- A reduction in future maintenance expenses would increase shareholder equity due to a reduction in non-unit reserves in respect of unit-linked insurance contracts.
- An increase in morbidity and mortality rates would reduce shareholder equity, as there would be an increase in reserves for protection business and an increase in non-unit reserves for insurance contracts
- A reduction in future surrender rates would increase shareholder equity at 31 December 2008, as there is likely to be an increase in the value of DAC. Realistic reserves on contracts with DPF would be likely to increase (assuming that option take-up rate remains unaltered).

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

25. Tax assets and liabilities

	2008 £m	2007 £m
Tax payable	-	-
Tax receivable	7.8	105.7
Total current tax asset	**7.8**	105.7
Deferred tax asset	**67.0**	20.5
Deferred tax liability	**(250.5)**	(409.5)
Total deferred tax liability	**(183.5)**	(389.0)

(a) Current tax asset

	2008 £m	2007 £m
At 1 January	**105.7**	243.5
Amounts credited / (charged) to the income statement	**90.6**	(69.2)
Tax recoveries during the year	**(188.5)**	(68.6)
At 31 December	**7.8**	105.7

(b) Deferred tax assets and liabilities

	At 1 January 2008 £m	Charged as deferred tax to income for the year £m	Change in tax rate charged to the income statement £m	Charge to equity for the year £m	At 31 December 2008 £m
Assets					
Expenses deferred for tax purposes	(19.5)	0.5	-	-	**(19.0)**
Unrealised losses on investments	-	(47.3)	-	-	**(47.3)**
Accelerated capital allowances	(1.0)	0.3	-	-	**(0.7)**
Liabilities					
Unrealised gains on investments	187.9	(187.9)	-	-	-
Deferred costs	111.0	18.2	-	-	**129.2**
PVIF	116.3	(5.5)	-	-	**110.8**
Other insurance related items	(5.7)	16.2	-	-	**10.5**
	389.0	**(205.5)**	-	-	**183.5**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

25. Tax assets and liabilities (continued)

(b) Deferred tax assets and liabilities (continued)

	At 1 January 2007	Charged as deferred tax to income for the year	Other charges to income for the year	Charge to equity for the year	At 31 December 2007
	£m	£m	£m	£m	£m
Assets					
Expenses deferred for tax purposes	(17.7)	(1.8)	-	-	**(19.5)**
Tax losses	(19.8)	19.8	-	-	-
Accelerated capital allowances	-	(1.0)	-	-	**(1.0)**
Liabilities					
Unrealised gains on investments	311.3	(123.4)	-	-	**187.9**
Accelerated capital allowances	14.2	(14.2)	-	-	-
Deferred costs	92.3	26.6	(7.9)	-	**111.0**
PVIF	145.8	(24.6)	(4.9)	-	**116.3**
Other insurance related items	39.0	(51.5)	0.6	6.2	**(5.7)**
	565.1	**(170.1)**	**(12.2)**	**6.2**	**389.0**

	2008 £m	2007 £m
At 1 January	**389.0**	565.1
Charged as deferred tax to income for the year	**(205.5)**	(170.1)
Impact of change in UK tax rate	-	(12.2)
Other charges to income for the year	-	-
Charge to equity for the year	-	6.2
At 31 December	**183.5**	389.0

Deferred tax assets are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable. Deferred tax assets have not been recognised in respect of unrelieved capital losses of £3.9m (2007: £3.9m), as there is insufficient certainty as to the availability of future profits. These amounts have no expiry date.

As a result of the Finance Act 2007, the main UK Corporation Tax Rate reduced from 30% to 28% in April 2008.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

26. Borrowings

	2008 £m	2007 £m
Bank overdraft	169.0	51.4
Total borrowings	169.0	51.4

The borrowings as at 31 December 2008 were subject to an average variable interest rate of 5.41% (2007: 6.50%).

27. Other insurance financial liabilities

	2008 £m	2007 £m
Insurance business		
Amounts payable on direct insurance business	65.4	98.0
Investment securities and debts		
Outstanding purchases of investment securities	-	1.1
Total other insurance financial liabilities	65.4	99.1

The estimated fair values of amounts due are the amounts repayable within the next 12 months and are the amounts as recorded at year end.

28. Accruals and deferred income

	2008 £m	2007 £m
Accruals	8.2	10.6
Deferred income	18.3	17.6
Total accruals and deferred income	26.5	28.2

	2008 £m	2007 £m
Current accruals and deferred income	8.2	10.6
Non current accruals and deferred income	18.3	17.6
Total accruals and deferred income	26.5	28.2

The carrying amounts disclosed above reflect the fair values at year end.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

29. Other liabilities

	2008 £m	2007 £m
Amounts due to related parties	**79.0**	103.5
Trade payables	**0.1**	-
Social security and other taxes	**29.7**	4.0
Balances due to brokers	**23.7**	19.5
Repurchase creditor	**349.2**	-
Other	**59.6**	69.1
Other liabilities	**541.3**	196.1

The estimated fair values of trade and other liabilities are the amounts repayable on demand and are the amounts as recorded at year end.

For reclassification of amounts due to related parties for 2007, see note 30.

30. Subordinated liabilities

In June 2005 Clerical Medical Finance plc, a fellow subsidiary undertaking, issued €750m of 4.25% undated Subordinated Guaranteed Bonds (current sterling value £705.3m). Redemption of the bonds is at the option of HBOS Financial Services Ltd, the Company's parent undertaking, and is generally not allowable prior to 27 June 2015, after which time if the bond has not been redeemed floating rate interest is payable. The effective interest rate of the bond is 4.4%.

In July 2001 Clerical Medical Finance plc, issued €400m of 6.45% dated Subordinated Guaranteed Bonds maturing on 5 July 2023 (current sterling value £379.3m). Redemption of the bonds is at the option of HBOS Financial Services Ltd and is generally not allowable prior to July 2013, after which time if the bond has not been redeemed floating rate interest is payable. The effective interest rate of the bond is 6.6%.

Previously Clerical Medical Finance plc issued £200.0m of 7.38% undated Subordinated Guaranteed Bonds (current sterling value £197.3m), the redemption of which is at the option of HBOS Financial Services Ltd and is generally not allowable prior to 5 November 2019. The first tranche of £150.0m was issued in November 1999 and the remainder in December 2000. The effective interest rate of the first tranche is 7.8% and the second is 7.2%.

The bonds are guaranteed on a subordinated basis by the Company, after the claims of the Company's senior creditors including all policyholders. The proceeds were loaned to the Company on similar interest, repayment and subordination terms as those applicable to the Bonds.

The fair value together with the carrying amount shown in the balance sheet is as follows:

	2008		2007	
	Carrying amount £m	Fair value £m	Carrying amount £m	Fair value £m
Subordinated liabilities	**1,282.0**	**799.1**	1,030.8	1,003.8
Accrued interest on subordinated liabilities	**37.5**	-	28.3	-
Subordinated liabilities	**1,319.5**	**799.1**	1,059.1	1,003.8

The fair value of the subordinated guaranteed bonds is their open market value. The carrying value is calculated on an effective interest rate basis, adjusted for foreign exchange movements and amortised issue costs. The 2008 carrying value is stated gross of foreign exchange movement of £260.4m (2007: (£76.4m)).

In order to improve the information presented in the current year, accrued interest on subordinated liabilities has been included in subordinated liabilities rather than in amounts due to related parties. Accordingly, 2007 subordinated liabilities have been adjusted to reflect this improvement. This has reduced amounts due to related parties (note 29) by £28.3m in 2007.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

31. Issued share capital and reserves

Ordinary shares	2008 £m	2007 £m
Authorised share capital		
150,000,000 ordinary shares of £1 each	**150.0**	1,709.0
Issued share capital		
70,000,000 ordinary shares of £1 each	**70.0**	1,629.0

In December 2001 the Company issued 159,000,000 ordinary shares of £1 each at a premium of 0.63 pence, giving rise to a share premium account of £1.0m. All shares issued are fully paid, there are no rights, preferences or restrictions attached to the shares.

On 1 October 2008, the directors passed a special resolution, supported by a solvency statement under Section 641 of the Companies Act 2006, to reduce the Company's authorised share capital from 1,709,000,000 ordinary shares of £1 each to 150,000,000 shares of £1 each. The resolution, together with the solvency statement, was registered by Companies House on 9 October 2008 and therefore the reduction in share capital became effective as of that date.

32. Loan facility

In December 2005 the Company provided an upper tier two loan, with a nominal amount of £100m, which was issued to Clerical Medical Managed Funds Limited, a subsidiary undertaking. The loan has no repayment date and interest is charged at 0.25% above base rate. The loan is included in 'Other receivables' within 'Due from related parties'.

In December 2006 a loan facility was provided to Clerical Medical Venture Investments Limited, a subsidiary undertaking. The ultimate termination date of the facility is 31 December 2014 and interest is charged at 5% per annum. At 31 December 2008 the facility balance was £55.9m (2007: £63m), which includes compound interest. The borrowings are included in 'Other receivables' within 'Due from related parties'.

The company holds six loan portfolios with Clerical Medical Europe Financial Services B.V., a subsidiary undertaking. The borrowings are included in 'Other receivables' within 'Due from related parties'. A summary detail of each portfolio is listed below:

Portfolio Name	Initiation Date	Repayment Date	Interest Rate	Nominal Amount	Currency
Agents Alliance	July 2003	January 2010	Euribor + 100 basis points	5m	Euros
EMF	December 2002	January 2010	Euribor + 200 basis points	9m	Euros
VSP - 1	July 2003	January 2010	Euribor + 100 basis points	4m	Euros
VSP - 2	July 2005	January 2010	Euribor + 100 basis points	4.588m	Euros
Protrust	February 2004	January 2010	Euribor + 100 basis points	4.1m	Euros
Master Finance	January 2005	January 2010	Euribor + 100 basis points	1.3m	Euros

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies

The Company issues contracts that transfer insurance and financial risk or both. This section summarises these risks and the way the Company manages them.

31 December 2008	Attributable to the shareholder	Attributable directly to the with profits fund	Attributable to unit linked funds	Total Policyholder Funds *	Total insurance and investment business
	£m	£m	£m	£m	£m
ASSETS					
Intangible assets	270.8	-	-	-	**270.8**
Property and equipment	-	77.4	-	77.4	**77.4**
Investment properties	1.1	1,173.5	316.6	1,490.1	**1,491.2**
Deferred costs	477.9	-	-	-	**477.9**
Investment in Group undertakings and participating interests	921.2	582.6	523.6	1,106.2	**2,027.4**
Reinsurance assets	1,801.7	-	7,932.7	7,932.7	**9,734.4**
Prepayments and accrued income	1.1	32.9	7.4	40.3	**41.4**
Current tax receivable	(5.2)	10.6	2.4	13.0	**7.8**
Financial assets					
Financial assets at fair value through income statement					
Derivative assets	53.4	611.9	0.2	612.1	**665.5**
Equity investments	78.0	3,580.5	1,516.4	5,096.9	**5,174.9**
Debt investments	1,171.0	6,414.0	995.6	7,409.6	**8,580.6**
Insurance receivables	6.2	-	(1.3)	(1.3)	**4.9**
Other receivables	671.7	25.0	(54.5)	(29.5)	**642.2**
Cash and cash equivalents	241.3	20.4	27.6	48.0	**289.3**
Total Assets	**5,690.2**	**12,528.8**	**11,266.7**	**23,795.5**	**29,485.7**
LIABILITIES					
Insurance contract liabilities	1,973.6	5,256.3	3,512.1	8,768.4	**10,742.0**
Unallocated surplus	-	469.2	-	469.2	**469.2**
Deferred tax liability	161.5	22.0	-	22.0	**183.5**
Current tax payable	-	-	-	-	-
Financial liabilities					
Derivative liabilities	4.4	121.6	5.1	126.7	**131.1**
Investment contract liabilities	33.8	6,166.0	7,734.7	13,900.7	**13,934.5**
Borrowings	27.0	142.0	-	142.0	**169.0**
Other insurance financial liabilities	60.5	4.9	-	4.9	**65.4**
Accruals and deferred income	25.5	0.9	0.1	1.0	**26.5**
Other liabilities	180.7	345.9	14.7	360.6	**541.3**
Subordinated liabilities	1,319.5	-	-	-	**1,319.5**
Total Liabilities	**3,786.5**	**12,528.8**	**11,266.7**	**23,795.5**	**27,582.0**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

31 December 2008	Attributable to the shareholder	Attributable directly to the with profits fund	Attributable to unit linked funds	Total Policyholder Funds *	Total insurance and investment business
	£m	£m	£m	£m	£m
EQUITY					
Issued share capital	70.0	-	-	-	**70.0**
Share premium account	1.0	-	-	-	**1.0**
Other reserves	-	-	-	-	-
Retained earnings	1,832.7	-	-	-	**1,832.7**
Total equity	**1,903.7**	-	-	-	**1,903.7**
Total liabilities and equity	**5,690.2**	**12,528.8**	**11,266.7**	**23,795.5**	**29,485.7**

* Policyholder funds include the unit linked and with-profit funds where investment risk is for the account of the policyholder and has no direct impact on the shareholder's balance sheet and accordingly have been excluded from the above shareholder analysis.

31 December 2007	Attributable to the shareholder	Attributable directly to the with profits fund	Attributable to unit linked funds	Total Policyholder Funds *	Total insurance and investment business
	£m	£m	£m	£m	£m
ASSETS					
Intangible assets	294.0	-	-	-	**294.0**
Property and equipment	0.1	161.3	-	161.3	**161.4**
Investment properties	-	1,750.4	523.7	2,274.1	**2,274.1**
Deferred costs	413.1	-	-	-	**413.1**
Investment in Group undertakings and participating interests	953.3	4,092.7	1,113.2	5,205.9	**6,159.2**
Reassurance assets	1,701.4	-	9,395.7	9,395.7	**11,097.1**
Prepayments and accrued income	1.5	29.5	5.7	35.2	**36.7**
Current tax receivable	97.6	4.5	3.6	8.1	**105.7**
Financial assets					
Financial assets at fair value through income statement					
Derivative assets	44.3	56.9	0.3	57.2	**101.5**
Equity investments	-	5,123.1	839.8	5,962.9	**5,962.9**
Debt investments	1,726.6	2,678.2	1,370.8	4,049.0	**5,775.6**
Insurance receivables	19.6	15.4	14.5	29.9	**49.5**
Other receivables	345.9	221.0	(8.9)	212.1	**558.0**
Cash and cash equivalents	183.0	58.2	26.6	84.8	**267.8**
Total Assets	**5,780.4**	**14,191.2**	**13,285.0**	**27,476.2**	**33,256.6**

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

31 December 2007	Attributable to the shareholder £m	Attributable directly to the with profits fund £m	Attributable to unit linked funds £m	Total Policyholder Funds * £m	Total insurance and investment business £m
LIABILITIES					
Insurance contract liabilities	1,840.5	5,306.3	865.3	6,171.6	**8,012.1**
Unallocated surplus	-	1,497.4	-	1,497.4	**1,497.4**
Deferred tax liability	203.3	157.0	28.7	185.7	**389.0**
Current tax payable	-	-	-	-	-
Financial liabilities					
Derivative liabilities	36.3	1.6	-	1.6	**37.9**
Investment contract liabilities	61.0	7,203.4	12,361.1	19,564.5	**19,625.5**
Borrowings	51.4	-	-	-	**51.4**
Other insurance financial liabilities	95.6	2.1	1.4	3.5	**99.1**
Accruals and deferred income	28.2	-	-	-	**28.2**
Other liabilities	144.2	23.4	28.5	51.9	**196.1**
Subordinated liabilities	1,059.1		-	-	**1,059.1**
Total Liabilities	**3,519.6**	**14,191.2**	**13,285.0**	**27,476.2**	**30,995.8**
EQUITY					
Issued share capital	1,629.0	-	-	-	**1,629.0**
Share premium account	1.0	-	-	-	**1.0**
Other reserves	2.6	-	-	-	**2.6**
Retained earnings	628.2	-	-	-	**628.2**
Total equity	**2,260.8**	-	-	-	**2,260.8**
Total liabilities and equity	**5,780.4**	**14,191.2**	**13,285.0**	**27,476.2**	**33,256.6**

Subordinated liabilities and other liabilities have been re-presented as described in note 30.

(a) **Unit Linked Funds**

For unit linked funds the policyholders carry the investment risk with any changes in the underlying investments being reflected by an equal change in the underlying investment contract liabilities. Accordingly, credit, liquidity, interest and market risks related to the unit linked investments, investment contract liabilities and other related balances are excluded from our assessment of risks and sensitivities impacting on the Company. However, we note that an overall change in the market value of these funds will have an indirect impact on the Company through the collection of annual management and fund related charges. If the market increases these charges increase. If the market falls these charges will fall. These charges typically range between 0.5% and 1.5% per annum.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

(b) With-Profit Fund

The with-profit fund takes some investment risks with the aim of enhancing policyholder returns. The costs of guarantees are spread across contracts in the fund, but there remains a risk that the shareholder may have to fund guarantees on contracts.

For 'unitised' with-profit contracts the shareholder receives an annual management charge, typically ranging between 0.5% and 1.5% per annum, so that the risks to the shareholder are similar to unit linked contracts.

For 'traditional' with-profit contracts, which form the minority of the with-profit fund business, the shareholder receives one ninth of bonuses declared to policyholders as long as there is a distributable surplus within the fund.

In other respects, credit, liquidity, interest and market risks have little impact on the shareholders. The impact on profit and equity is via the shareholders' share of bonuses or in extreme scenarios where the fund is unable to meet its capital requirements. Accordingly, the related balances are not considered further in our assessment of financial risks impacting the Company.

The most important measures in controlling the risk within the with-profit fund include the pooling of with-profit risk; having agreed management actions to adjust the level of equity exposure in response to certain investment conditions; by recognising and holding appropriate levels of risk capital; by restricting holdings to assets which meet admissibility criteria; and by using derivative strategies to reduce downside risk. Through these actions, the shareholder is largely protected from an erosion of capital resources within the UK with-profit fund.

The Company has considered the financial risks of the with-profit fund along with the non profit fund and shareholders' assets and liabilities in the tables that follow. All linked and with-profit assets are considered to be current.

(c) Non Profit Business

The principal investment risk in the respect of the non profit business is interest rate risk which arises because assets and liabilities may exhibit differing changes in market value as a result of changes in interest rates. These risks are controlled by processes carried out to ensure an appropriate level of matching is maintained in the funds so that changes in fixed interest assets are substantially mitigated by offsetting changes in liabilities as well as through the use of and monitoring against fund mandates.

33.1 Risk Management Framework

33.1 (a) Governance

The risks associated with the activities of the Company are overseen by the Risk Control Committee of the Insurance & Investment Division of HBOS plc. The Committee, which is chaired by a Director of HBOS plc, reviews all risk and compliance issues affecting the Company, as well as the other wholly owned companies within the Insurance & Investment Division.

In addition to the Risk Control Committee, there are a number of other committees responsible for different aspects of corporate governance of HBOS plc and its major subsidiaries. Further details of these committees and compliance with the Combined Code on corporate governance are included in the HBOS plc annual report and accounts.

Further, there is a Long Term Business Governance Committee, the role of which is to balance the interests of policyholders and shareholders.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. **Risk management policies (continued)**

33.1 **(b) Capital Risk Management**

The Company has developed and implemented certain minimum stress and scenario tests for identifying the risks to which the business is exposed and quantifying their impact on capital. The results of these tests are reported to the Risk and Compliance Committee.

33.1 **(c) Regulatory**

Regulators are interested in protecting the rights of the policyholders and maintaining close attention to ensure that the Company is satisfactorily managing affairs for their benefit. At the same time, the regulators are also interested in ensuring that the Company maintains appropriate solvency. Accordingly, the UK regulator and other local regulatory bodies where the entity operates not only prescribe approval and monitoring of activities but also impose certain minimum capital requirements. These include, but are not limited to, the requirement to hold sufficient capital adequacy to minimise the risk of default and insolvency on the part of the insurance companies taking into account reasonably foreseeable adverse events.

33.2 **Financial risk**

33.2 **(a) Credit risk**

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company manages the level of credit risk it accepts through a comprehensive credit risk policy. This includes the use of credit ratings from independent rating agencies and where not available, by internal analysis. Additionally, the policy sets out exposure limits for each type of counterparty, product types and business sectors, which at no time during the year were exceeded.

The following table provides information regarding the credit risk exposure of the equity and debt securities within the Company at 31 December 2008 by classifying them according to credit ratings of the counterparties. Policyholder funds have been excluded from the analysis as the underlying risks are for the account of the policyholders and have no direct impact on the Company's results. The credit risk associated with all other assets is not considered significant.

31 December 2008	AAA £m	AA £m	A £m	Other Rated £m	Not rated £m	Policyholder £m	Total £m
Financial assets at fair value through income statement							
Derivatives	-	-	42.2	-	11.2	612.1	**665.5**
Equity investments	-	78.0	-	-	-	5,096.9	**5,174.9**
Debt investments	321.0	758.7	90.5	0.4	0.4	7,409.6	**8,580.6**
Total	**321.0**	**836.7**	**132.7**	**0.4**	**11.6**	**13,118.6**	**14,421.0**

31 December 2007	AAA £m	AA £m	A £m	Other Rated £m	Not rated £m	Policyholder £m	Total £m
Financial assets at fair value through income statement							
Derivatives	-	-	-	-	44.3	57.2	**101.5**
Equity investments	-	-	-	-	-	5,962.9	**5,962.9**
Debt investments	662.1	970.8	88.2	5.5	-	4,049.0	**5,775.6**
Total	**662.1**	**970.8**	**88.2**	**5.5**	**44.3**	**10,069.1**	**11,840.0**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

Collateral and other credit enhancements held

Collateral is the pledging of assets which in the event of default can be sold in order to realise some, or all, of the outstanding monies. HBOS has documented policies in respect of the criteria for recognition of collateral taken as credit risk mitigation and stock lending is only transacted with a select list of HBOS approved counterparties.

HBOS policy is to calculate the market value of collateral taken and periodically reassess it. In most cases the market value is assessed on a daily basis. Notwithstanding, revaluation is undertaken whenever HBOS has reason to believe that a significant decrease in market value has occurred. More frequent assessment is required where the market is subject to significant changes in conditions.

Where the collateral is held by a third party, HBOS takes reasonable steps to ensure that the third party segregates the collateral from its own assets.

HBOS policy is to ensure it has the ability to liquidate the collateral readily, the ability to establish objectively, a price or market value, the frequency with which the value can readily be obtained (including a professional appraisal or valuation), and the volatility or a proxy of the volatility of the value of the collateral. Both initial valuation and revaluation take into account any deterioration or obsolescence of the collateral. Particular attention is paid in valuation and revaluation to the effects of the passage of time on fashion- / date-sensitive collateral.

HBOS policy in recognising collateral is that there is the right to physically inspect the collateral ensuring also that the collateral taken as protection is adequately insured against damage.

Financial assets that are past due or individually assessed as impaired may be partially or fully collateralised or subject to other forms of credit enhancement.

The majority of the collateral held by the Company is either debt or equity securities. This is because the Company usually receives collateral on a like for like basis with regards to the securities which have been lent.

This same policy is adhered to when the Company has pledged collateral or holds collateral and is permitted to sell or repledge the collateral in the absence of default by the owner of the collateral.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

33.2 (b) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in raising funds to meet cash commitments associated with financial instruments. Liquidity risk may result from either the inability to sell financial assets quickly at their fair values; a counterparty failing on repayment of a contractual obligation; an insurance liability falling due for payment earlier than expected; or the inability to generate cash inflows as anticipated.

The Company has determined that liquidity risk does not represent a significant exposure to its long term assurance business. This assessment is based on the fact that the majority of investment and insurance contracts are long term in nature whilst the majority of investments are held in listed, readily realisable debt and equity instruments.

The table below sets out the contractual maturity of the Company's financial liabilities (excluding those related to policyholder funds recognised at the balance sheet date). The analysis of insurance contract liabilities is based on the expected timing of amounts recognised at the balance sheet date. Policyholder funds have been excluded from the analysis as the underlying risks are for the account of policyholders and have no direct impact on the Company's results.

31 December 2008	Attributable to the shareholder Up to a year £m	Attributable to the shareholder 1- 5 years £m	Attributable to the shareholder Over 5 years £m	Total attributable to the With Profits fund and Unit Linked fund £m	Total shareholder and Policyholder funds £m
Insurance contract liabilities	131.8	466.8	1,375.0	8,768.4	**10,742.0**
Unallocated surplus	-	-	-	469.2	**469.2**
Deferred tax liability		-	161.5	22.0	**183.5**
Current tax payable	-	-	-	-	-
Financial liabilities					
Derivative liabilities	4.4	-	-	126.7	**131.1**
Investment contract liabilities	-	-	33.8	13,900.7	**13,934.5**
Borrowings	27.0	-	-	142.0	**169.0**
Other insurance financial liabilities	60.5	-	-	4.9	**65.4**
Subordinated liabilities	37.5	379.3	902.7	-	**1,319.5**
Amounts due to related parties	46.6	-	-	32.4	**79.0**
Trade payables	0.1	-	-	-	**0.1**
Balances due to brokers and intermediaries	20.4	-	-	3.3	**23.7**
Repurchase creditor	-	-	-	349.2	**349.2**
Total	**328.3**	**846.1**	**2,473.0**	**23,818.8**	**27,466.2**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

31 December 2007	Attributable to the shareholder Up to a year £m	Attributable to the shareholder 1-5 years £m	Attributable to the shareholder Over 5 years £m	Total attributable to the With Profits fund and Unit Linked fund £m	Total shareholder and Policyholder funds £m
Insurance contract liabilities	129.3	511.7	1,199.5	6,171.6	**8,012.1**
Unallocated surplus	-	-	-	1,497.4	**1,497.4**
Financial liabilities					
Derivative liabilities	36.3	-	-	1.6	**37.9**
Investment contract liabilities	57.5	3.5	-	19,564.5	**19,625.5**
Borrowings	51.4	-	-	-	**51.4**
Other insurance financial liabilities	95.6	-	-	3.5	**99.1**
Subordinated liabilities	28.3	-	1,030.8	-	**1,059.1**
Trade payables	99.4	-	-	4.1	**103.5**
Balances due to brokers and intermediaries	1.0	-	-	18.5	**19.5**
Repurchase creditor	-	-	-	-	-
Total	**498.8**	**515.2**	**2,230.3**	**27,261.2**	**30,505.5**

Subordinated liabilities have been re-presented as described in note 30.

33.3 Market risk

Market risk is the risk of change in the fair value of financial instruments from fluctuation in foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (price risk), whether such change in price is caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

33.3 (a) Currency risk

The Company's principal transactions are carried out in Pound Sterling and its exposure to foreign exchange risk arises primarily with respect to the Euro.

The Company's financial assets are primarily denominated in the same currencies as its insurance and investment liabilities, which mitigate the foreign currency exchange rate risk for the overseas operations. In addition currency futures are used to further mitigate risk. Thus the main foreign exchange risk arises from recognised assets and liabilities denominated in currencies other than those in which insurance and investment liabilities are expected to be settled.

33.3 (b) Interest rate risk

Interest rate risk is the risk that the value / future cash flows of a financial instrument will fluctuate because of changes in interest rates. The Company's interest rate risk policy requires it to manage interest rate risk by maintaining an appropriate mix of fixed and variable rate instruments and the use of interest rate swaps. The policy also requires it to manage the maturity profile of interest bearing financial assets and interest bearing financial liabilities.

As a consequence, the performance of the entity is not significantly affected by the level of its exposure to interest rate risk or changes to that exposure.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

The impact on profit after tax of a 25bps fall in interest rates as at the 31 December 2008 is a £1.4m profit (2007: £6.7m profit). In calculating this sensitivity it is assumed that other assumptions change only if they are directly affected by the revised economic conditions. For example, consequential effects on valuation basis are allowed for.

33.3 (c) Price risk

The Company's price risk exposure relates to holding financial assets and liabilities whose values will fluctuate in different ways as a result of changes in market prices other than as a result of interest and foreign exchange fluctuations. This can be due to factors specific to individual instruments, their issuers or factors affecting all instruments traded in the market. Accordingly, the Company limits its exposure to any one counterparty as well as the relevant foreign markets (refer to credit and currency exposure disclosures for concentration risks impacting price risks).

For certain long term business classes, the Company aims to hold assets whose values will move in line with the corresponding liabilities so as to limit the overall impact of price risk.

The impact on profit after tax of the market value of policyholder investments being 10% on average lower during the year is £20.7m loss (2007: £14.5m loss). This sensitivity reflects the impact of market movements on charges made to the funds and investment expenses incurred. In calculating this sensitivity, it is assumed that this change occurs in isolation, with no consequential effects assumed to other assumptions.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

33.3 (d) Insurance risk

Insurance risk is the risk that an insured event will occur including the uncertainty of the amount and timing of any resulting claim. The principal risk the Company faces under such contracts is that the actual claims and benefit payments exceed the carrying amount of insurance liabilities. This is influenced by the frequency of claims, severity of claims and subsequent development of long term claims.

The variability of risks is improved by diversification of risk of loss to a large portfolio of insurance contracts. A more diversified portfolio is less sensitive to losses arising due to particular risks in any subset of the portfolio. The variability of risks is also improved by careful selection and implementation of underwriting strategy and guidelines as well as the use of reinsurance arrangements. The Company reinsurance policy includes credit risk exposure limits to individual reinsurance groups which are dependent on credit rating and there are defined maximum retention limits for individual lives. In this way concentration of exposure to individual lives and reinsurance groups is controlled.

33.4 Capital management

33.4 (a) Capital Management

The Company's capital is managed by the Board with reference to the HBOS Group Capital Committee capital management objectives and the minimum capital requirements imposed by the regulators. In order to ensure sufficient capital is maintained by the Company at all times, the Board has approved a capital buffer policy. This policy requires that the company maintain capital in excess of the minimum regulatory requirements plus the approved minimum buffer over the planning period. To the extent that the Board assesses that the Company has capital in excess of its requirements, capital may be repatriated to its parent and ultimate parent company HBOS plc.

The Company's capital includes, to the extent that they exist, the following balances on the balance sheet: called up share capital, share premium account, other reserves, retained earnings, and subordinated liabilities and other items permitted to be recognised as regulatory capital under FSA Handbook Rules and Guidance.

There have been no material changes in the Group's approach to capital management during the year.

33.4 (b) Capital Requirements

The company is directly regulated by the Financial Services Authority (FSA), who set and monitor capital requirements.

The company complied with the FSA's capital requirements throughout 2008 and 2007.

33.4 (c) Capital Structure

The Company's capital is divided into tiers as directed by the Rules in the FSA Handbook. The Company holds Tier 1 capital items and qualifying Tier 2 capital. Tier 1 capital comprises shareholders' funds, after adjusting for items reflected in shareholders' funds which are treated differently for the purposes of capital adequacy. Tier 2 capital comprises qualifying subordinated loan capital.

The relative holdings of tiered capital comply with the FSA's capital gearing rules.

The table shows the consolidated balances, valuing regulated related undertakings using the adjusted solo solvency calculation required by the FSA Handbook.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

33. Risk management policies (continued)

33.4 (c) Capital Structure (continued)

	Note	2008 £m	2007 £m
Ordinary and preference share capital		**70.0**	1,629.0
Share premium		**1.0**	1.0
Profit and loss reserve		**1,832.7**	628.2
Other reserves		**-**	2.6
Other regulatory capital	(i)	**1,383.9**	2,732.4
Less: Regulatory deductions to Tier 1 capital	(ii)	**(294.7)**	(388.7)
Total Tier 1 capital		**2,992.9**	4,604.5
Subordinated debt		**1,282.0**	1,030.8
Other qualifying Tier 2 capital		**100.0**	100.0
Total Tier 2 capital		**1,382.0**	1,130.8
Total regulatory capital before deductions		**4,374.9**	5,735.3
Regulatory deductions to total capital	(iii)	**(816.7)**	(476.5)
Total regulatory capital after deductions		**3,558.2**	5,258.8

Notes

Note (i) – Other regulatory capital includes unallocated surplus, capital of regulated related undertakings and other items permitted to be treated as Tier 1 capital, such as positive valuation differences on translation of amounts to a regulatory reporting basis.

Note (ii) – Regulatory deductions to Tier 1 capital include reductions in respect of goodwill and intangible assets, deductions to Tier 1 capital of regulated related undertakings and negative valuation differences on translation of amounts to a regulatory reporting basis.

Note (iii) – Regulatory deductions to total capital include reductions in respect of exposures to assets in excess of regulatory limits, deductions to total capital of regulated related undertakings and inadmissible assets.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

34. Related party transactions

The Company is controlled by HBOS plc, a public listed company incorporated in the United Kingdom, whose shares are widely held by the general public.

	Transactions in the Year		Outstanding Balance at 31 December	
	2008	2007	**2008**	2007
	£m	£m	**£m**	£m
Relationship				
Parent undertaking:				
Receivables				
- HBOS Financial Services Limited				
Loans granted	-	25.2	-	-
- HBOS Insurance & Investment Group				
Other receivables (recharges)	-	0.6	**0.5**	(0.8)
Payables				
- HBOS Financial Services Limited				
Loans payable	-	(1.7)	-	-
Other payables (recharges)	**(137.8)**	174.8	**13.2**	(12.4)
- Halifax Plc				
Other payables (recharges)	**(1.0)**	210.6	**(4.1)**	(1.6)
Other Group companies:				
Receivables				
- Clerical Medical International Holdings BV				
Other receivables (recharges)	**0.6**	-	**20.2**	-
- CMI Insurance Company Ltd				
Other receivables	-	-	**5.6**	-
- CMI Insurance Luxembourg SA				
Loans granted	**152.9**	15.6	**202.1**	199.4
Other receivables (recharges)	**1.8**	-	-	-
- Halifax Investment Fund Managers				
Loans granted	**3.5**	-	**3.5**	-
- HECM Customer Services Limited				
Other receivables (factoring collections)	**31.4**	0.8	**0.5**	(5.9)
- Bank of Scotland Limited				
Other receivables (Bank accounts)	-	(1.4)	-	1.4
Cash at bank	**57.9**	-	**80.7**	22.8
- CMI Financial Services Ltd				
Other receivables (marketing recharge)	**4.8**	-	**0.3**	-
- Insight Investment Services Ltd				
Other receivable (investment charges)	**11.2**	-	**1.8**	-
- Clerical Medical International Group				
Loans granted	-	(2.1)	-	24.1
- Clerical Medical Finance Plc				
Interest receivable	**60.5**	(38.9)	**392.4**	199.3

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

34. Related party transactions (continued)

	Transactions in the Year		Outstanding Balance at 31 December	
	2008 £m	2007 £m	2008 £m	2007 £m
Payables				
- Halifax Investment Fund Managers				
Other payables (recharges)	(0.1)	-	(0.1)	-
- HECM Customer Services Limited				
Other receivables (factoring)	(29.9)	-	(1.9)	-
Other payables (recharges)	(2.7)	-	3.8	-
- Bank of Scotland Limited				
Other payables (recharges)	(175.7)	191.7	(13.9)	10.0
- CME Financial Services BV				
Other payables (recharges)	(64.5)	-	(18.3)	-
- CMI Financial Management Services Ltd				
Other payables (recharges)	(0.3)	-	(0.1)	-
- Heidelberger Leben Co				
Other payables (recharges)	(1.1)	-	(0.2)	-
- Insight Investment Management Ltd				
Other payable (investment charges)	(82.3)	15.9	(7.2)	(3.7)
- Invista				
Other payables (investment charges)	(13.6)	13.7	(5.0)	-
- Clerical Medical Finance Plc				
Loans and interest payable	(62.7)	55.7	(1,712.4)	(1,259.0)
- Clerical Medical International Group				
Other payables (reassurance)	-	755.9	-	(24.8)
Subsidiaries:				
Receivables				
- Clerical Medical Managed Funds Ltd				
Loans granted	-	-	100.0	100.0
Other receivables (reassurance)	110.6	245.0	64.1	13.9
Other receivables (stocklending)	30.6	-	31.2	-
- Clerical Medical Venture Investments				
Loans granted	(7.1)	(3.0)	55.9	63.0
- Halifax Life Limited				
Other receivables (commission)	2.0	-	15.6	-
Loans receivable	51.2	-	(0.3)	-
Payables				
- Clerical Medical Managed Funds Ltd				
Other payables (reassurance)	(0.7)	-	(4.0)	-
- Clerical Medical Forestry				
Loans payable	(34.1)	(0.5)	(28.2)	5.9
- Clerical Medical Properties				
Loans payable	-	-	(0.9)	(0.9)
- Halifax Life Limited				
Other payables	-	0.5	-	(64.6)
- St Andrews Life				
Other payables	-	1.1	-	-
Total	(94.6)	1,659.5	(805.2)	(733.9)

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

34. Related party transactions (continued)

All the transactions summarised were entered into on an arm's length basis and settled in cash. The amounts outstanding at the end of the year are included in other receivables / payables and subordinated liabilities as appropriate. The associated repayment terms are set out in note 32 for the loans. All other balances are repayable on demand. £60m dividends were received from Halifax Life Limited during 2008 (2007: £451m).

Key management personnel and members of their close families have undertaken transactions with the Clerical Medical Investment Group Limited and its subsidiary undertakings, joint ventures and associates in the normal course of business, details of which are given further below.

Life assurance and investment contracts (*)

	Number of key management personnel	**£000**
Valuation as at 1 January 2008 or date of appointment, if later	1	152
Premiums paid/amounts invested during the year	1	1
Other movements including investment returns	2	(40)
Total sum insured/value of investment at 31 December 2008	2	115

(*Life assurance contracts would be those with an encashment value; investment contracts would include pensions, ISA's, PEP's – whether self-selected or not - OEICs, investments and monies held in portfolio management services, etc)

The emoluments of directors providing services to the Company are:

	2008	2007
	£	£
Total emoluments	**288,658**	271,467
Pension contributions and entitlements	**40,521**	28,034
Termination benefits	**2,982**	48,500
Share based payments	**-**	38,352
Other long-term benefits	**39,121**	48,929

Retirement benefits are accruing to 3 (2007: 3) directors under a defined benefit scheme.

Directors sit on several boards and their benefits are allocated to a company depending on the proportion of their time that they spend as a director of that company.

Highest paid director (included above):	**2008**	2007
	£	£
Emoluments	**148,250**	-
Pension contributions and entitlements	**21,210**	-

The highest paid director's emoluments were not required to be disclosed for the year ended 31 December 2007 as they fell below the appropriate threshold.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (continued)

35. Events after balance sheet date

On 18 September 2008, with the support of the UK Government, the boards of HBOS plc ('HBOS') and Lloyds TSB Group plc ('Lloyds TSB') announced that they had reached agreement on the terms of the recommended acquisition of HBOS by Lloyds TSB. The terms of the acquisition were subsequently amended, as announced on 13 October 2008, at the same time as the announcement of the participation by HBOS and Lloyds TSB in the Government's action plan to recapitalise some of the major UK banks. The acquisition was to be implemented by means of a scheme of arrangement with a separate scheme of arrangements in relation to preference shares, under sections 895 to 899 of the Companies Act 2006.

On 12 January 2009 the Court of Session in Edinburgh, Scotland made an order sanctioning the scheme of arrangement for the acquisition and the preference share scheme of arrangement. The last day of trading in HBOS ordinary and preference shares was 14 January 2009.

On 15 January 2009 HBOS raised £11.5bn of capital (before costs and expenses) through an issue of £8.5bn of new ordinary shares under a placing with HM Treasury subject to clawback by existing shareholders, and an issue to HM Treasury of £3bn of new preference shares. Lloyds TSB raised £4.5bn (before costs and expenses) through an issue of £3.5bn of new ordinary shares under a placing with HM Treasury subject to clawback by existing shareholders, and an issue to HM Treasury of £1bn of new preference shares.

On 16 January 2009 the Lloyds TSB acquisition of HBOS completed following final court approval and Lloyds TSB was renamed Lloyds Banking Group plc. The exchange of HBOS shares for Lloyds Banking Group shares took place at an exchange ratio of 0.605 of a new Lloyds Banking Group share for every one HBOS share held. As a result, the UK Government through HM Treasury owned approximately 43.4% of the enlarged ordinary share capital of Lloyds Banking Group. In addition, each class of preference share issued by HBOS, including the preference shares issued to HM Treasury in the capital raising was replaced with an equal number of new Lloyds Banking Group preference shares.

HBOS ordinary and preference shares were de-listed from the Official List of the UK Listing Authority and admission to trading on the London Stock Exchange was cancelled on 19 January 2009 when trading in the new Lloyds Banking Group shares commenced.

Government Asset Protection Scheme

On 7 March 2009, the Company's ultimate parent undertaking, Lloyds Banking Group plc ("LBG"), announced its intention to participate in the Government's Asset Protection Scheme. LBG intends to participate in the Scheme in respect of assets and exposures on its consolidated balance sheet with an aggregate book value of approximately £250bn and will pay a fee to HM Treasury of £15.6bn which will be amortised over an estimated 7 year period. The proceeds of this fee will be applied by HM Treasury in subscribing for an issue of "B" shares of LBG, carrying a dividend of the greater of 7 per cent per annum and 125 per cent of the dividend on ordinary shares.

LBG has also agreed to replace the £4bn of preference shares held by HM Treasury with new ordinary shares which will be offered to eligible LBG shareholders pro rata to their existing shareholdings at a fixed price of 38.43 pence per ordinary share. These new ordinary shares will be offered to shareholders and new investors on the same basis as the Placing and Open Offer in November 2008. The ordinary share offer is fully underwritten by HM Treasury on substantially the same fee basis as the Placing and Open Offer conducted in November 2008.

Participation in the Scheme and the replacement of the preference shares is subject to approval by eligible LBG shareholders.