

# **CLERICAL MEDICAL FINANCE PLC**

## **ANNUAL REPORT AND FINANCIAL STATEMENTS**

**31 DECEMBER 2015**



Member of Lloyds Banking Group plc

**CONTENTS**

Company Information	3
Strategic Report	4-5
Directors' Report	6-7
Independent Auditors' Report to the Members of Clerical Medical Finance Plc	8-9
Statement of Comprehensive Income for the year ended 31 December 2015	10
Balance Sheet as at 31 December 2015	11
Statement of Cash Flows for the year ended 31 December 2015	12
Statement of Changes in Equity for the year ended 31 December 2015	13
Notes to the Financial Statements for the year ended 31 December 2015	14 - 28

**COMPANY INFORMATION**

**Board of Directors**

A M Parsons  
J M Black  
M E Williams

**Secretary**

A Yuille

**Independent Auditors**

PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
2 Glass Wharf  
Bristol  
BS2 0FR

**Registered Office**

33 Old Broad Street  
London  
EC2N 1HZ

**Company Number**

3850542

**STRATEGIC REPORT**

The directors present their strategic report on Clerical Medical Finance Plc ("the Company") for the year ended 31 December 2015.

As part of the LBG Insurance Division strategy the Company provides finance to Scottish Widows Limited (formerly Clerical Medical Insurance Group Ltd), a life insurance company within the LBG group. Subordinated debt raised by the Company is used to fund Scottish Widows Limited ("SWL") insurance and savings business. The funds loaned to SWL are on similar interest and repayment terms as those applied to the subordinated debt raised by the Company such that the Company returns a non significant pre tax profit.

**Result for the year**

The result of the Company for the year ended 31 December 2015 is a profit after tax of £0.2m (2014: loss of £0.5m), and this has been transferred to reserves.

On 24 June 2015 SWL settled a €388m (£276m) loan at an interest rate of 4.27% to the Company, with which the Company exercised its option to redeem €388m loan at an interest rate of 4.25% dated subordinated guaranteed bonds.

The carrying value of the subordinated assets at the year end was £48.4m (2014: £350.6m). The decrease is due to redemption of Euro-denominated loans to SWL. Interest income receivable on the subordinated assets as a percentage of the average subordinated asset in the period was 4.96% (2014: 4.56%).

The carrying value of the subordinated liabilities at the year end was £50.5m (2014: £352.8 m). The decrease is due to the redemption of Euro-denominated loans to bondholders. The interest expense payable on the subordinated liabilities as a percentage of the average subordinated liabilities in the year was 4.97% (2014: 4.68%).

**Key performance indicators**

The Directors are of the opinion that the information presented in the financial statements provides the management information, necessary for the Directors to understand the development, performance and position of the business of the Company. The Company also forms part of the Insurance Division of LBG. The development, performance and position of this Division are discussed in LBG's annual report, which does not form part of this report.

**Liquidity**

The Company is dependent on the liquidity of SWL. SWL regularly monitors its liquidity position to ensure that, even under stressed conditions, the Group has sufficient liquidity to meet its obligations and remain within the approved risk appetite.

**STRATEGIC REPORT (Continued)****Review of the business***Litigation in Germany in relation to Scottish Widows Limited branch business*

The Group has received a number of claims from customers relating to policies issued by Clerical Medical Investment Group Limited (recently renamed Scottish Widows Limited) but sold by independent intermediaries in Germany, principally during the late 1990s and early 2000s. Following decisions in July 2012 from the Federal Court of Justice (FCJ) in Germany the Group recognised provisions totalling £520 million during the period to 31 December 2014. Recent experience has been slightly adverse to expectations and the Group has noted decisions of the FCJ in 2014 and 2015 involving German insurers in relation to a German industry-wide issue regarding notification of contractual 'cooling off' periods. Accordingly, a provision increase of £25 million has been recognised giving a total provision of £545 million. The remaining unutilised provision as at 31 December 2015 is £124 million (31 December 2014: £197 million).

The validity of the claims facing the Group depends upon the facts and circumstances in respect of each claim. As a result the ultimate financial effect, which could be significantly different from the current provision, will only be known once all relevant claims have been resolved.

This ongoing matter has not resulted in any impact in these financial statements.

**Future outlook**

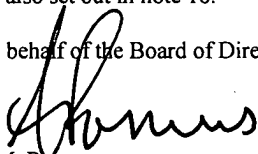
The Directors consider that the Company's principal activities will continue unchanged in the foreseeable future.

**Principal risks and uncertainties**

The management of the business and the execution of the Company's strategy are subject to a number of risks. The financial risk management objectives and policies of the company and the exposure to market, credit, financial soundness and operational risks are set out in note 16.

In addition, the Company is also exposed to financial reporting risk, in particular the risk of reputational damage, loss of investor confidence and/or financial loss arising from the adoption of inappropriate accounting policies, ineffective controls over financial reporting and financial reporting fraud. The financial and risk management objectives and policies of the company in respect of financial reporting risk are also set out in note 16.

On behalf of the Board of Directors



A M Parsons  
Director  
24 March 2016

**DIRECTORS' REPORT****Principal activities and review of the business**

The Directors present the audited financial statements of the Company. The Company is a limited liability Company domiciled and incorporated in the United Kingdom.

The Company is a subsidiary of HBOS Financial Services Limited. The company's ultimate parent company and ultimate controlling party is Lloyds Banking Group plc ("LBG").

The Company's principal activity is to act as a finance company for Scottish Widows Limited a fellow subsidiary of LBG. Subordinated debt raised by the Company is loaned to Scottish Widows Limited on similar interest and repayment terms as those applied to the subordinated debt raised by the Company.

**Results and dividend**

The result of the Company for the year ended 31 December 2015 is a profit after tax of £0.2m (2014: loss of £0.5m). No interim dividend was paid during the year (2014: £nil). The Directors do not recommend the payment of a final dividend (2014: £nil). Further information on the results of the Company is provided in the Strategic Report.

**Post balance sheet events**

No significant post balance sheet events have been identified affecting the Company's financial statements.

**Directors**

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

JE Clatworthy (resigned 29 February 2016)  
M E Williams (appointed 10 March 2016)

Particulars of the Directors' emoluments are set out in note 17.

LBG has granted to the Directors of the Company a deed of indemnity through deed poll which constituted 'qualifying third party indemnity provisions' for the purposes of the Companies Act 2006. The deed was in force during the whole of the financial year and at the date of approval of the financial statements. Directors no longer in office but who served on the Board of the Company at any time in the financial year had the benefit of this contract of indemnity during that period of service. The indemnity remains in force for the duration of a Director's period of office. The deed indemnifies the Directors to the maximum extent permitted by law. The Deed for existing Directors is available for inspection at the registered office of LBG. In addition, LBG has in place appropriate Directors and Officers Liability Insurance cover which was in place throughout the financial year.

**Corporate governance statement**

In accordance with the Financial Conduct Authority's Disclosure and Transparency Rule ("DTR") 7.2.1, the disclosures required by DTR 7.2.5R are within note 16 to the financial statements and are therefore incorporated into this report by reference.

**Disclosure of information to auditors**

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

**Political contributions**

During the year, the Group made no political contributions (2014: £nil).

**Financial risk management**

Disclosures relating to financial risk management are included in note 16 to the accounts and are therefore incorporated into this report by reference.

**DIRECTORS' REPORT (Continued)****Statement of Directors' responsibilities**

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

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

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of these financial statements as presented on the Company's website [www.clericalmedical.co.uk](http://www.clericalmedical.co.uk). Legislation in England and Wales governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

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

- the Company financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Company; and
- the Strategic Report on pages 4 to 5 and the Directors' Report on pages 6 to 7 includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces.

On behalf of the Board of Directors



A M Parsons  
Director  
24 March 2016

**Independent auditors' report to the member of Clerical Medical Finance Plc****Report on the financial statements****Our opinion**

In our opinion, Clerical Medical Finance Plc's financial statements (the "financial statements"):

- give a true and fair view of the state of the Company's affairs as at 31 December 2015 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

**What we have audited**

The financial statements, included within the Annual Report, comprise:

- the balance sheet as at 31 December 2015;
- the statement of comprehensive income for the year then ended;
- the statement of cashflows for the year then ended;
- the statement of changes in equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and IFRSs as adopted by the European Union.

In applying the financial reporting framework, the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

**Opinions on other matters prescribed by the Companies Act 2006**

In our opinion:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the information given in the Corporate Governance Statement set out in the report with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

**Other matters on which we are required to report by exception*****Adequacy of accounting records and information and explanations received***

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

***Directors' remuneration***

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

**Corporate governance statement**

Under the Companies Act 2006 we are required to report to you if, in our opinion, a corporate governance statement has not been prepared by the company. We have no exceptions to report arising from this responsibility.



**Independent auditors' report to the member of Clerical Medical Finance Plc (continued)****Responsibilities for the financial statements and the audit****Our responsibilities and those of the directors**

As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose.

We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

**What an audit of financial statements involves**

We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

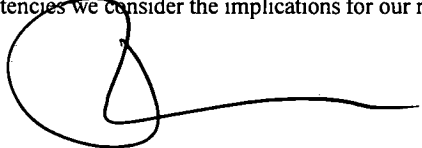
This includes an assessment of:

- whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.



Joanne Leeson (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Bristol  
24 March 2016

## STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2015

	Note	2015 £ 000	2014 £ 000
<b>Revenue</b>			
Interest income	2	9,622	16,943
Other income	3	224	528
<b>Total revenue</b>		<b>9,846</b>	<b>17,471</b>
<b>Expenses</b>			
Finance costs	4	9,435	16,988
Other expenses	5	245	1,123
<b>Total expense</b>		<b>9,680</b>	<b>18,111</b>
<b>Profit / (Loss) before tax</b>		<b>166</b>	<b>(640)</b>
Taxation credit	7	27	138
<b>Profit / (Loss) for the year</b>		<b>193</b>	<b>(502)</b>

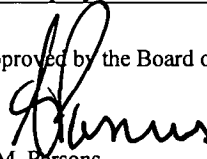
There are no items of comprehensive income which have not already been presented in arriving at the profit / (loss) for the year. Accordingly, the profit for the year is the same as total comprehensive income / (expense) for the year.

The notes set out on pages 14 to 28 are an integral part of these financial statements.

## BALANCE SHEET AS AT 31 DECEMBER 2015

	Note	2015 £ 000	2014 £ 000
<b>ASSETS</b>			
Financial assets:			
Loans and receivables	8	48,350	350,579
Other receivables	9	3,066	9,573
Cash and cash equivalents	10	4,899	4,718
Current tax asset	11	-	77
<b>Total assets</b>		<b>56,315</b>	<b>364,947</b>
<b>EQUITY AND LIABILITIES</b>			
Capital and reserves attributable to Company's equity shareholder			
Share capital	12	225	225
Retained earnings		4,945	4,752
<b>Total equity</b>		<b>5,170</b>	<b>4,977</b>
<b>Liabilities</b>			
Financial liabilities:			
Subordinated liabilities	13	50,548	352,757
Other financial liabilities	14	563	7,213
Current tax liabilities	15	34	-
<b>Total liabilities</b>		<b>51,145</b>	<b>359,970</b>
<b>Total equity and liabilities</b>		<b>56,315</b>	<b>364,947</b>

Approved by the Board on 24 March 2016.

  
A M Parsons  
Director

The notes set out on pages 14 to 28 are an integral part of these financial statements.

## STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2015

		2015	2014
	Note	£ 000	£ 000
<b>Cashflow from operating activities</b>			
Profit / (Loss) before tax		166	(640)
Adjusted for:			
Amortisation of finance costs on subordinated debt	5	21	1,123
Other subordinated debt movements		-	(505)
Amounts received on redemption of sub debt from Scottish Widows Limited	13	287,766	-
Movement in other receivables		6,507	476
Movement in other liabilities		(6,650)	(454)
Taxation received / (paid)		137	(137)
<b>Net cash inflow / (outflow ) from operating activities</b>		<b>287,947</b>	<b>(137)</b>
<b>Cashflow from financing activities</b>			
Redemption of subordinated debt	13	(287,766)	-
<b>Net cash outflow from financing activities</b>		<b>(287,766)</b>	<b>-</b>
<b>Net increase /(decrease) in cash and cash equivalents</b>		<b>181</b>	<b>(137)</b>
Cash and cash equivalents at the beginning of the year		4,718	4,855
<b>Net cash and cash equivalents at the end of the year</b>	10	<b>4,899</b>	<b>4,718</b>

The notes set out on pages 14 to 28 form an integral part of these financial statements.

## STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2015

	Share capital (£ 000)	Retained earnings (£ 000)	Total equity (£ 000)
<b>Balance as at 1 January 2014</b>	<b>225</b>	<b>5,254</b>	<b>5,479</b>
Loss and total comprehensive loss for the year	-	(502)	(502)
<b>Balance as at 31 December 2014</b>	<b>225</b>	<b>4,752</b>	<b>4,977</b>
Profit and total comprehensive income for the year	-	193	193
<b>Balance as at 31 December 2015</b>	<b>225</b>	<b>4,945</b>	<b>5,170</b>

The notes set out on pages 14 to 28 form an integral part of these financial statements.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

**1. Accounting policies**

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

**(a) Basis of preparation**

The financial statements of the Company have been prepared:

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

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

(3) under the historical cost convention, as modified by the revaluation of certain financial assets and financial liabilities at fair value through profit or loss as set out in the relevant accounting policies.

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

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

**(b) Foreign currency translation**

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.

Financial assets and liabilities denominated in foreign currencies are translated at balance sheet date exchange rates. Exchange gains and losses are recognised in the statement of comprehensive income as incurred, within other income or other expenses.

**(c) Interest income**

Interest income consists of interest receivable on subordinated assets. Interest income is recognised in the statement of comprehensive income as it accrues, using the effective interest method.

**(d) Finance costs**

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

**(e) Dividends payable**

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

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

**1. Accounting policies (continued)****(f) Financial assets and financial liabilities**

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

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

All financial assets and financial liabilities are designated at fair value through profit or loss, with the exception of certain loans and receivables and other financial liabilities which are stated at amortised cost (as described in note 1(g) and 1(m) below). The classification depends on the purpose for which the financial assets and financial liabilities were acquired.

No assets are classified as held-to-maturity, available-for-sale or for trading; no liabilities are classified as held for trading.

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

**(g) Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that are not designated as fair value through profit or loss at initial recognition.

Loans and receivables are initially recognised at fair value less directly attributable transaction costs and subsequently measured at amortised cost, subject to impairment, with the exception of accrued interest, which is accounted for at fair value, reflecting the amounts receivable at the year end.

A charge for impairment in respect of loans and receivables would be made in the statement of comprehensive income when there is objective evidence that the Company will not be able to collect all amounts due according to their original terms. The impairment charge would be recognised through operating expense in that part of the statement of comprehensive income in which the original transaction was reported. Further information on the Company's impairment policy is set out at policy (i).

**(h) Cash and cash equivalents**

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

**(i) Impairment****Financial assets**

The carrying value of all financial assets held at amortised cost is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable. The identification of impairment and the determination of recoverable amounts is an inherently uncertain process involving various assumptions and factors, including the financial condition of the counterparty, expected future cash flows, observable fair prices and expected net selling prices. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its estimated recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

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

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its estimated recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows. If there is objective evidence that an impairment loss has occurred, the amount of the loss is charged to the relevant line in the statement of comprehensive income in the period in which it occurs.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

**1. Accounting policies (continued)****(i) Impairment (continued)****Impairment process**

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

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

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

**(j) Taxes**

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

**Current tax**

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

**(k) Share capital**

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

**(l) Subordinated liabilities**

Subordinated liabilities comprise undated loan capital. They are recognised initially at fair value, being the issue proceeds net of transaction costs incurred. Subordinated liabilities are subsequently stated at amortised cost: any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the statement of comprehensive income through amortisation of finance costs on subordinated debt over the period of the liabilities using the effective interest rate applicable to the instrument. Interest payable is recognised in the statement of comprehensive income, through finance costs (see 1(d)).

The subordinated guaranteed bonds were classified as a liability at the time that the instrument was issued on the basis of the existence of a capital disqualification event considered to be a genuine settlement provision.

**(m) Other financial liabilities**

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



## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 1. Accounting policies (continued)

## (n) Effective interest rate

Revenue on financial instruments classified as loans and receivables and finance costs on financial liabilities at amortised cost, are recognised on an effective interest rate basis. This calculation takes into account interest received or paid and fees and commissions paid or received that are integral to the yield as well as incremental transaction costs and all other premiums and discounts. The effective interest rate is the rate that discounts the expected future cash flows over the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial instrument at initial recognition.

## 2. Interest income

	2015 £ 000	2014 £000
Interest income on loans	9,622	16,943
<b>Total</b>	<b>9,622</b>	<b>16,943</b>

On 24 June 2015 the Company exercised its option to redeem €388m of 4.25% dated subordinated guaranteed bonds. The proceeds on original issue had been loaned to Scottish Widows Limited on similar interest and repayment terms. Scottish Widows Limited repaid this Euro loan on 24 June 2015.

## 3. Other income

	2015 £ 000	2014 £ 000
Other income	224	528
<b>Total</b>	<b>224</b>	<b>528</b>

Other income includes amortisation of finance costs on the £sterling and €Euro loans receivables

## 4. Finance costs

	2015 £ 000	2014 £ 000
Interest payable on bond issues	9,435	16,988
<b>Total</b>	<b>9,435</b>	<b>16,988</b>

Finance costs relate to the interest payable on subordinated guaranteed bonds in the year.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 5. Other expenses

	2015 £ 000	2014 £ 000
Loss on foreign currency exchange	-	2
Amortisation of finance costs on subordinated debt	245	537
Adjustment of prior year amortisation of finance cost	-	584
<b>Total</b>	<b>245</b>	<b>1,123</b>

Other expenses includes amortisation of finance costs on the pound and euro subordinated liabilities and the foreign exchange loss on the euro subordinated liabilities, arising as a result of movement in exchange rates.

The prior year balance includes an adjustment of £584,000 to account for an understatement in amortisation of finance costs in 2013.

No staff are employed directly by the Company (2014: none). All staff providing services to the Company are employed by other subsidiaries of LBG.

## 6. Auditors remuneration

Audit fees are borne by another subsidiary within LBG and are as follows:

	2015 £	2014 £
Fees payable for the audit of the Company's current year annual report	2,605	2,500
Fees payable for other services:		
Other services - audit related	5,675	5,500
<b>Total</b>	<b>8,280</b>	<b>8,000</b>

## 7. Taxation credit

## a) Current year tax credit

	2015 £ 000	2014 £ 000
<b>Current Tax:</b>		
UK Corporation tax	27	138
<b>Total</b>	<b>27</b>	<b>138</b>

## b) Reconciliation of tax (charge) / credit

	2015 £ 000	2014 £ 000
<b>Profit / (Loss) before tax</b>	<b>166</b>	<b>(640)</b>
<b>Tax at 20.25% (2014: 21.5%)</b>	<b>(34)</b>	<b>138</b>
<b>Prior year tax credit</b>	<b>61</b>	<b>-</b>
<b>Total</b>	<b>27</b>	<b>138</b>

The Finance Act 2013 was substantively enacted on 2 July 2013. The Act further reduced the main rate of corporation tax to 21% with effect from 1 April 2014 and 20% with effect from 1 April 2015.

The Finance Act 2015 which was substantively enacted on 26 October 2015 included legislation to reduce the corporation tax rate applicable from 1 April 2017 to 19% and from 1 April 2020 to 18%.

The proposed reduction in the rate of corporation tax to 17% on 1 April 2020 is expected to be enacted during 2016.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 8. Loans and receivables

	2015 £ 000	2014 £ 000
Amounts owed by group undertakings	48,350	350,579
<b>Total</b>	<b>48,350</b>	<b>350,579</b>

The receivables relate to funds deposited with Scottish Widows Limited (formerly Clerical Medical Investment Group Limited). The deposits bear nominal interest at 7.61% (2014: between 4.27% and 7.61%) depending on the terms of the specific deposit, this income being received through the statement of comprehensive income. Further information in respect of amounts owed by group undertakings is given in note 17.

The balances above include £0.2m (2014: £9.2m) due from Scottish Widows Limited in respect of amortised transaction costs.

## 9. Other receivables

	2015 £ 000	2014 £ 000
Accrued interest receivable	3,066	9,573
<b>Total</b>	<b>3,066</b>	<b>9,573</b>

The above receivables are owed by group undertakings. Further information in respect of amounts owed by group undertakings is given in note 17.

## 10. Cash and cash equivalents

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

	2015 £ 000	2014 £ 000
Investments in a liquidity fund	4,899	4,718
<b>Total</b>	<b>4,899</b>	<b>4,718</b>

Investments in the liquidity funds are held for the purpose of meeting short-term cash commitments and are included in cash equivalents.

## 11. Current tax asset

	2015 £ 000	2014 £ 000
Current tax receivable	-	77
<b>Total</b>	<b>-</b>	<b>77</b>

## 12. Share capital

	2015 £ 000	2014 £ 000
Allotted, called up and fully paid share capital: 225,000 (2014: 225,000) ordinary shares of £1 each	225	225
<b>Total</b>	<b>225</b>	<b>225</b>

There were no changes in ordinary share capital during the year.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 13. Subordinated liabilities

This note provides information about the contractual terms of the Company's interest-bearing loans and borrowings. For more information about the Company's exposure to interest rate and foreign currency risk, see note 16.

	2015 £ 000	2014 £ 000
<b>Non-current liabilities</b>		
Subordinated guaranteed bonds	50,548	352,757
<b>Total</b>	<b>50,548</b>	<b>352,757</b>

On 24 June 2015 the Company exercised its option to redeem €388m of 4.25% dated subordinated guaranteed bonds. The proceeds of which had been loaned to SWL on similar interest and repayment terms. The subordinated guaranteed bonds had a maturity date of 5 July 2023, but offered the Company the option to redeem the bonds from 5 July 2013, after which time if the bonds had not been redeemed a floating rate interest would have been payable. The sterling value of this redemption was £288m. Prior to repayment SWL repaid in full a corresponding amount to the Company. Further information on the Company's credit risk is available in note 16.

The subordinated guaranteed bonds are carried at amortised cost. The amortisation schedule is set out below:

	2015 £ 000	2014 £ 000
Nominal value	50,680	353,151
Amortisation in one year	(34)	(262)
Amortisation two to five years	(98)	(132)
Amortisation over five years	-	-
<b>As at 31 December</b>	<b>50,548</b>	<b>352,757</b>

The debt repayment schedule for the subordinated guaranteed bonds (by nominal value) is set out below:

## As at 31 December 2015

	Total £ 000	Less than 1 year £ 000	1-2 years £ 000	2-5 years £ 000	More than 5 years £ 000
<b>Subordinated Guaranteed Bonds</b>					
(nominal value):					
£51m – at 7.375%	50,680	-	-	-	50,680
<b>Total</b>	<b>50,680</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>50,680</b>

## As at 31 December 2014

	Total £ 000	Less than 1 year £ 000	1-2 years £ 000	2-5 years £ 000	More than 5 years £ 000
<b>Subordinated Guaranteed Bonds</b>					
(nominal value):					
£51m – at 7.375%	50,680	-	-	-	50,680
€388m – at 4.25%	302,471	-	-	-	302,471
<b>Total</b>	<b>353,151</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>353,151</b>

The €388m subordinated guaranteed bonds were redeemed on 24 June 2015

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 13. Subordinated liabilities (continued)

Details of the terms for the subordinated guaranteed bonds are as follows:

£51m of 7.375% undated Subordinated Guaranteed Bonds, the redemption of which is at the option of the Company and is generally not allowable prior to 5 November 2019.

The bonds are guaranteed on a subordinated basis by Scottish Widows Limited, a fellow subsidiary of LBG, after the claims of Scottish Widows Limited senior creditors including all policyholders. The proceeds of each bond issue were loaned to Scottish Widows Limited on similar interest, repayment and subordination terms as those applicable to the bonds as detailed in note 8.

Tranche	Original issue	Amount redeemed	Outstanding at 31 December 2015	Outstanding at 31 December 2014
7.375% originally issued: Nov 1999 / Dec 2000	£200m	£149m	£51m	£51m
4.25% originally issued: June 2005	€750m	€750m	-	€388m

## 14. Other financial liabilities

	2015 £ 000	2014 £ 000
Accrued interest on subordinated guaranteed bonds	563	7,213
<b>Total</b>	<b>563</b>	<b>7,213</b>

## 15. Current tax liabilities

	2015 £000	2014 £000
Current tax payable	34	-
<b>Total</b>	<b>34</b>	<b>-</b>

## 16. Risk management

The Company's principal activity is to act as a finance company for Scottish Widows Limited, a fellow subsidiary undertaking. Subordinated debt raised by the Company is loaned to Scottish Widows Limited on similar interest and repayment terms as those applied to the subordinated debt raised by the Company.

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

## (a) Governance framework

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

Responsibility for the setting and management of risk appetite and risk policy resides with the Board, who manage risks in line with LBG and Insurance risk policies. The Board has delegated operational implementation to the Insurance Risk Committee.

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

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

**16. Risk management (continued)****(a) Governance framework (continued)**

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

During the year, policy owners, identified from appropriate areas across the business, are responsible for drafting the Insurance risk policies where Lloyds Banking Group policies do not capture Insurance-specific regulations or requirements for ensuring that they remain up-to-date, and for facilitating any changes. These policies are subject to at least an annual review, or earlier if deemed necessary. Limits are prescribed within which those responsible for the day to day management of each Group company can take decisions. Line management are required to follow prescribed reporting procedures to the bodies responsible for monitoring compliance with policy and controlling the risks.

**(b) Risk Appetite**

Risk appetite is the amount and type of risk that the Board is prepared to seek, accept or tolerate and is fully aligned to Insurance and LBG strategy. The Board has defined the methodology for the management of risk appetite and approved a set of risk appetite statements that cover financial risks (earnings, insurance, capital, credit, market and liquidity), operational risks, people risks, conduct risks, regulatory & legal risks, financial reporting risks and governance risks. The risk appetite statements set limits for exposures to the key risks faced by the business. Risk appetite is set at an Insurance level.

Experience against risk appetite is reported monthly (by exception) and quarterly (in full) to the Insurance Risk Committee, quarterly (by exception) to the Insurance Risk Oversight Committee (IROC), and twice yearly to the Board. Copies are also supplied regularly to Insurance's regulators as part of the close and continuous relationship. Reporting focuses on ensuring, and demonstrating to the Board, and their delegate the IROC, that Insurance is run in line with approved risk appetite. Any breaches of risk appetite require clear plans and timescales for resolution.

**(c) Financial risks**

The Company is exposed to a range of financial risks through its financial assets and financial liabilities.

The Company manages these risks in a number of ways, including monitoring of cash flow requirements. The Company also uses financial instruments as part of its business activities and to reduce its own exposure to market risk and credit risk.

Financial assets and financial liabilities are measured on an ongoing basis at amortised cost. The summary of significant accounting policies (note 1) describes how the class of financial instruments are measured and how income and expenses, including fair value gains and losses, are recognised.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 16. Risk management (continued)

## (c) Financial risks (continued)

The following tables analyse the carrying amount of assets and liabilities, with financial assets and financial liabilities being presented according to their IAS 39 classification:

	2015	2014
	£000	£000
<b>Financial assets</b>		
Cash and cash equivalents	4,899	4,718
Accrued interest receivable	3,066	9,573
Amortised cost:		
Loans receivable	48,350	350,579
	<b>56,315</b>	<b>364,870</b>

**Other Assets**

Current tax receivable	-	77
<b>Total assets</b>	<b>56,315</b>	<b>364,947</b>

	2015	2014
	£000	£000
<b>Financial liabilities</b>		
Amortised cost:		
Subordinated liabilities	50,548	352,757
Other financial liabilities	563	7,213
	<b>51,111</b>	<b>359,970</b>

**Other liabilities**

Current tax payable	34	-
<b>Total liabilities</b>	<b>51,145</b>	<b>359,970</b>

## (1) Market risk

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

The fair values together with the carrying amounts of those assets and liabilities affected by market risk shown in the balance sheet are as follows:

	2015		2014	
	Carrying amount	Fair value	Carrying amount	Fair value
	£000	£000	£000	£000
Cash and cash equivalents	4,899	4,899	4,718	4,718
Loans to group undertaking	48,350	53,658	350,579	357,656
Subordinated guaranteed bonds	(50,548)	(53,658)	(352,757)	(357,656)

The carrying amount of Loans to group undertakings above includes £0.2m (2014: £9.2m) due from Scottish Widows Limited in respect of amortised transaction cost.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 16. Risk management (continued)

## c) Financial risks (continued)

## 1) Market risk (continued)

The carrying amount of Loans to group undertakings and subordinated guaranteed bonds above is recognised initially at fair value, being the issue proceeds net of transaction costs incurred, and subsequently stated at amortised cost using the effective interest method.

The fair value of Loans to group undertakings and subordinated guaranteed bonds above are based on the open market value of the Subordinated guaranteed bonds, excluding amortised transaction costs.

## (i) Equity and property risk

The Company is not exposed to equity or property risk through its financial assets and financial liabilities.

## (ii) Interest rate risk

Interest rate risk is the risk that the value of future cash flows of a financial instrument will fluctuate because of changes in interest rates and the shape of the yield curve.

*Effective interest rates and re-pricing analysis*

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and the periods in which they re-price:

	Note	Effective Interest rate	2015			Effective Interest rate	2014		
			Total £000	6 months or less £000	More than 5 years £000		Total £000	6 months or less £000	More than 5 years £000
Cash and cash equivalents	10	0.5%	4,899	4,899	-	0.5%	4,718	4,718	-
<b>Loans to group undertaking:</b>	<b>8</b>								
GBP		7.8%	48,350	48,350	-	7.8%	48,346	48,346	-
Euro		4.4%	-	-	-	4.4%	302,233	302,233	-
<b>Subordinated guaranteed bonds:</b>	<b>13</b>								
GBP		7.6%	(50,548)	(50,548)	-	7.6%	(50,378)	(50,378)	-
GBP		7.3%	-	-	-	7.3%	(136)	(136)	-
Euro		4.4%	-	-	-	4.4%	(302,243)	(302,243)	-

Interest rates on interest-bearing financial assets and financial liabilities are closely matched. Any increase or decrease in interest rates would, therefore, not have a material impact on profit and loss.

## (iii) Foreign exchange risk

Foreign exchange risk relates to the effects of movements in exchange markets including changes in exchange rates.

The interest receivable and payable, and the value of the Company's assets and liabilities, may be affected by currency translation movements. The Directors believe that the impacts of such moves are not significant since the assets of the Company held in currency are substantially matched by liabilities in the same currency.

The Company receives income and pays expenses in currencies other than sterling and the sterling values of these transactions can be affected by movements in exchange rates, likewise however the value of the income and expenses are substantially matched. The value of the net asset exposure to currencies other than sterling is £nil (31 December 2014: £774,000 net asset exposure).



## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

**16. Risk management (continued)****c) Financial risks (continued)****2) Credit risk**

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

Credit risk is managed in line with the Insurance Credit Risk Policy and the wider Lloyds Banking Group Credit Risk Policy.

Company is primarily exposed to credit risk through the subordinated guaranteed bonds loaned on to Scottish Widows Limited. Accordingly the Company is dependent upon Scottish Widows Limited to meet its commitments in respect of the subordinated guaranteed bonds issued. Management monitor closely the solvency position and the credit risk exposure of Scottish Widows Limited and the Company. They are satisfied that, as a consequence of the risk management procedures in place, as set out in the financial statements of Scottish Widows Limited, this risk is suitably managed.

There were no past due or impaired financial assets at 31 December 2015 (2014: none). No terms in respect of financial assets had been renegotiated at 31 December 2015 or 31 December 2014.

**3) Financial soundness risk**

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

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

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

The Company has developed procedures to ensure that compliance with both current and potential future requirements are understood and that policies are aligned to its risk appetite. The Company maintains a system of internal controls, consistently applied, providing reasonable assurance that transactions are recorded and undertaken in accordance with delegated authorities that permit the preparation and disclosure of financial statements (including consolidated financial statements), regulatory reporting and tax returns in accordance with IFRSs, statutory and regulatory requirements.

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

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

**16. Risk management (continued)****c) Financial risks (continued)****3) Financial soundness risk (continued)****(ii) Liquidity risk**

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

Liquidity risk is managed in line with the LBG Funding and Liquidity Risk Policy.

Liquidity risk has been analysed as arising from the settlement of balances from other group undertakings of £51,416,000 (2014: £360,152,000) which in turn is used to settle balances owed on subordinated guaranteed bonds.

**(iii) Capital risk**

Capital risk is defined as the risk that:

- the Company has insufficient capital to provide a stable resource to absorb all loss up to a confidence level defined in the risk appetite;
- the Company loses reputational status by having capital that is regarded as inappropriate, either in quantity, type or distribution; and/or
- the capital structure is inefficient.

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

The Company's objectives when managing capital is to have sufficient capital to safeguard the Company's ability to continue as a going concern so that it can continue to provide returns for the shareholder and benefits for other stakeholders;

**4) Operational risks**

Operational risk covers the risk of reductions in earnings and/or value, through financial or reputational loss, from inadequate or failed internal processes and systems, or from people related or external events.

**17. Related party transactions****(a) Ultimate parent and shareholding**

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

The Company's ultimate parent company and ultimate controlling party is Lloyds Banking Group plc, which is also the parent undertaking of the largest group of undertakings for which group Financial Statements are drawn up and of which the Company is a member.

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

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 3) Related party transactions (continued)

## (b) Transactions and balances with related parties

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

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

Relationship	Transactions in the Year		Outstanding Balance at 31 December	
	2015	2014	2015	2014
	£000	£000	£000	£000
<b>Other related parties:</b>				
Loans receivable and accrued interest	(308,735)	(21,189)	51,416	360,152

All the transactions summarised above were entered into on an arm's length basis. The amounts outstanding at the end of the year are included in other receivables / payables as appropriate and are repayable on demand unless otherwise specified in the relevant note. The Company paid no dividends to its parent company in the year ended 31 December 2015 (2014: nil).

## Transactions between the Company and key management personnel

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

The Directors consider that they receive no remuneration for their services to the Company.

## HM Treasury

In January 2009, HM Treasury became a related party of the Company following its subscription for ordinary shares in LBG, the Company's ultimate parent company, issued under a placing and open offer. As at 31 December 2015, HM Treasury held a 9.12% (2014: 24.9%) interest in Lloyds Banking Group's ordinary share capital and, consequently, HM Treasury remained a related party of the Company throughout 2015.

There were no material transactions between the Company and HM Treasury during the year (2014: none) that were not made in the ordinary course of business or that are unusual in their nature or conditions. In addition, the Company has entered into transactions with HM Treasury on an arm's length basis including, but not exclusively in relation to, the payment of corporation tax, employment tax, and value added tax.

## 18. Contingent Liability

The Company provides for potential tax liabilities that may arise on the basis of the amounts expected to be paid to tax authorities. This includes open matters where Her Majesty's Revenue and Customs ('HMRC') adopt a different interpretation and application of tax law which might lead to additional tax. A number of Group companies, including the Company, have an open matter in relation to a claim for group relief of losses incurred in a former Irish banking subsidiary of the Lloyds Banking Group, which ceased trading on 31 December 2010. In the second half of 2013 HMRC informed the Lloyds Banking Group that their interpretation of the UK rules, permitting the offset of such losses, denies these claims; if HMRC's position is found to be correct, management estimate that this would result in an increase in the Company's current tax liability of approximately £61,000. The Lloyds Banking Group does not agree with HMRC's position and, having taken appropriate advice, does not consider that this is a case where additional tax will ultimately fall due on the Company.'

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015

## 19. Future accounting developments

The following pronouncement may have an impact on the Company's financial statements but are not applicable for the year ended 31 December 2015 and have not been applied in preparing these financial statements. Except as disclosed below, the full impact of these accounting changes is being assessed by the Company.

Pronouncement	Nature of change	IASB effective date
IFRS 9 "Financial Instruments" <sup>1,2</sup>	Replaces IAS 39 "Financial Instruments: Recognition and Measurement."	Annual periods beginning on or after 1 January 2018

IFRS 9 requires financial assets to be classified into three measurement categories, fair value through profit and loss, fair value through other comprehensive income and amortised cost, on the basis of the objectives of the entity's business model for managing its financial assets and the contractual cash flow characteristics of the instruments. The requirements for derecognition are broadly unchanged from IAS 39. The standard also retains most of the IAS 39 requirements for financial liabilities except for those designated at fair value through profit or loss whereby that part of the fair value change attributable to the entity's own credit risk is recorded in other comprehensive income.

IFRS 9 also replaces the existing IAS 39 'incurred loss' impairment approach with an expected credit loss approach. Loan commitments and financial guarantees not measured at fair value through profit or loss are also in scope.

The hedge accounting requirements of IFRS 9 are more closely aligned with risk management practices and follow a more principle-based approach than IAS 39.

IFRS 9 is not expected to have a significant financial impact on the financial results or position of the Company.

<sup>1</sup> At the date of this report, the pronouncement is awaiting EU endorsement.

<sup>2</sup> IFRS 9 is the initial stage of the project to replace IAS 39. Future stages are expected to result in amendments to IFRS 9 to deal with changes to the impairment of financial assets measured at amortised cost and hedge accounting, as well as a reconsideration of classification and measurement. Until all stages of the replacement project are complete, it is not possible to determine the overall impact on the financial statements of the replacement of IAS 39.