

The Standard Life Assurance Company

Annual Financial Statements for the year ended 31 December 2005

Registration no: Scotland Number SZ4



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Directors and Officers

Executive Directors

Sandy Crombie (Group Chief Executive)
John Hylands
Trevor Matthews
Alison Reed
Keith Skeoch

Non-executive Directors

Sir Brian Stewart (Chairman)
Lord Blackwell
Alison Mitchell
Jocelyn Proteau
Hugh Stevenson
Kent Atkinson
Gerry Grimstone (Deputy Chairman)

Company Secretary

Malcolm Wood

Registered Office

Standard Life House
30 Lothian Road
Edinburgh
EH1 2DH

Registered Number

SZ4

Auditors

PricewaterhouseCoopers LLP
Edinburgh

Report by the Directors

The directors present their report and the audited financial statements for the year ended 31 December 2005.

Principal activities and business review

The Standard Life Group commenced business in Edinburgh in 1825. Today we are one of the largest financial services groups in the United Kingdom with gross earned premiums of £3,609m and contributions received under investment contracts of £6,952m for the 12 months ended 31 December 2005, and funds under management for Standard Life Investments of £119bn at 31 December 2005. We are a diversified financial services group and our principal activities consist of the provision of life assurance and pensions, investment management, banking and healthcare insurance products. We use the "Standard Life" brand to promote, market and sell financial products in these sectors.

Life assurance and pensions

We have a significant position in the United Kingdom life assurance and pensions market with a market share of 8.4% in 2005 in terms of new business annual premium equivalent (APE) having written £908m of new business APE in 2005. The principal distribution channel for life assurance and pensions products in the United Kingdom is Independent Financial Advisers (IFAs). We have a strong position in this sector of the market with a market share of 10.9% of new business APE written through IFAs in 2005. In addition, we are the fourth largest life assurance and pensions provider (by gross premium income) in Canada, with a market share of approximately 9.8%.

We also have operations in life assurance and pensions in Germany, Ireland and Hong Kong and interests in life assurance and pensions joint ventures in India and China.

Investment management

Our investment management business is principally operated by Standard Life Investments, which managed £119bn of assets for both the Standard Life Group and third parties as at 31 December 2005.

Third party funds under management have grown from £5.3bn in 1998 to £28.1bn as at 31 December 2005. Through Standard Life Investments, we also have an interest in an asset management joint venture in India.

Banking

Our banking business is operated through Standard Life Bank, which offers a range of mortgages and savings products. Standard Life Bank had a mortgage portfolio of approximately £10.6bn as at 31 December 2005. Approximately £4bn of the funding for this portfolio was provided by Standard Life Bank's deposit book and the balance of the funding comes from external debt and capital.

Healthcare insurance

Our UK healthcare insurance business is operated by Standard Life Healthcare and is one of the largest private medical insurers in the United Kingdom (ranking third with a market share of 5.7% in terms of APE).

Strategic review

In the early part of 2004, the Group undertook a strategic review of its businesses. As a result, the Directors decided to proceed with a plan to demutualise the Group and subsequently list the shares on the London Stock Exchange, subject to the satisfactory completion of all legal, regulatory and other requirements. A Special General Meeting is proposed for 31 May 2006, to seek approval of the demutualisation and flotation plans.

As part of the demutualisation, the Company will transfer substantially all of its business, undertakings and assets to several wholly owned subsidiaries of the newly formed proprietary company, Standard Life PLC. The membership rights of all Standard Life's members will cease, subject to receipt of the demutualisation shares or other demutualisation benefits, in accordance with the provisions of the Scheme of Demutualisation.

Report by the Directors

Directors

The names of the current directors are listed on page 3. Kent Atkinson was appointed a director of the Company on 26 January 2005. Sir Nicholas Monck retired as a director on 22 March 2005. David Newlands resigned as a director on 6 March 2006. Alison Reed was appointed as Group Finance Director on 13 June 2005. Keith Skeoch was appointed a director of the Company on 6 March 2006.

The directors who will retire by rotation at the Annual General Meeting are Sir Brian Stewart, Lord Norman Blackwell, Gerry Grimstone and Alison Mitchell and their re-election will be proposed. Alison Reed and Keith Skeoch, who have been appointed to office since the last Annual General Meeting, will also retire at the Annual General Meeting and will be proposed for re-election.

Employees

The Group is committed to an equal opportunities policy. The sole criterion for selection or promotion is the suitability of any applicant for the job regardless of ethnic origin, religion, sex, marital status or disablement. The Group will continue to employ, arrange for retraining, or retire on disability pension any member of staff who becomes disabled, as may be appropriate.

Employee engagement

It is the Group's policy to have effective communication and consultation with staff. Staff involvement is achieved through meetings, briefings and newsletters which help to ensure that staff are fully aware of the organisation's goals and results. In addition, staff representatives are elected to a number of Area Consultative Committees and to National Consultative Committees which meet formally with management twice a year to discuss matters of general staff interest or concern. Minutes of these meetings are made available to staff. Since the Company is mutual, there is no employee share scheme but appropriate long-term incentive schemes are in place.

Use of voting rights

As an institutional investor the Group has a policy of always voting on resolutions at General Meetings of UK companies. If the Group intends to vote against or abstain from voting on such resolutions this will be made known to the company concerned beforehand.

Supplier payment policy

It is the Group's policy to negotiate payment terms with suppliers and to pay in accordance with the terms agreed. The average duration of amounts owing to Group trade creditors at 31 December 2005 was 7 days (2004 : 11 days), based on the ratio of Group trade creditors at the end of the year to the amounts invoiced during the year by trade creditors.

Charitable and other donations

The Group supports charitable and other appropriate bodies through its Community Investment Programme. Cash donations to charities in the UK amounted to £342,364 (2004: £445,709), of which £246,063 related to donations to the Standard Life Charity Fund.

At the Annual General Meeting on 6 April 2004, a resolution was passed authorising the Company to make political donations to EU political organisations and to incur EU political expenditure up to £50,000 in total. This resolution was updated and passed at the 2005 Annual General Meeting to authorise the Company to make donations and incur expenditure to which section 347C(1) of the Companies Act 1985 ("the Act") applies. The definitions of 'donations' and 'EU political expenditure' which are contained in Part XA of the Act are very broad, and might cover activities which form part of the normal non-political relationship between the Group and the political world. The Board does not believe that the Group has, in the year to 31 December 2005, made any such donations or incurred any such expenditure.

Report by the Directors

Risk Management

The Group manages its various risks as outlined in Note 31 of the financial statements.

Directors' responsibilities

Company law requires the directors to prepare financial statements for each financial period which comply with the Act and give a true and fair view of the state of affairs of the Group and the Company and of the results of the Group for that period. In addition, the directors should take all reasonable steps to ensure that adequate accounting records are maintained, that the assets of the Group are safeguarded and that fraud and other irregularities are prevented or detected.

The annual financial statements for the year ended 31 December 2005 are published in hard copy printed form and on the Group's website at www.standardlife.com. The directors are responsible for the maintenance and integrity of the annual financial statements on this website in accordance with UK legislation governing the preparation and dissemination of financial statements. Access to the website is available outside the UK, where comparable legislation may be different.

The directors confirm that suitable accounting policies, consistently applied with the exception of the change in accounting policy referred to in section (a) of the Accounting Policies, and supported by reasonable and appropriate judgements and estimates, have been used in the preparation of the financial statements of the Group and the Company for the year ended 31 December 2005. The directors also confirm that the financial statements have been appropriately prepared on a going concern basis and that applicable accounting standards have been followed as described in the Accounting Policies.

Corporate Social Responsibility policy

A Corporate Social Responsibility (CSR) committee reviews CSR policies, practices and performance, drives development, highlights risks and opportunities and serves as a reference point for all CSR work throughout the Group. The Group maintains a section of the corporate website devoted to CSR, www.standardlife.com/responsibility. It contains statements of the Group's policies relating to community investment, employees, the environment, human rights and socially responsible investment. Further details of the Group's social and environmental practices and achievements are set out in the Corporate and Social Responsibility Report.

Auditors

The reappointment of the auditors, PricewaterhouseCoopers LLP will be proposed at the Annual General Meeting.

On behalf of the Board of Directors

Malcolm Wood, Secretary
Edinburgh, 28 March 2006



Corporate Governance

Application of the Combined Code

The directors have reviewed the Group's corporate governance procedures and have chosen to comply with the relevant requirements of the revised Combined Code on Corporate Governance ("the Combined Code"), as issued by the Financial Reporting Council in July 2003. The directors consider that throughout the period, the Group complied with all relevant provisions of Section 1 of the Combined Code. The principles of the Combined Code have been applied as detailed below.

Organisational structure

The organisational structure of the Group is clearly defined by reference to business units, including subsidiary companies and branch operations. Authority for managing the Group is delegated to the executive directors and senior managers. For each subsidiary, the appropriate senior managers have been appointed as directors. The boards of key subsidiary companies also include an appropriate number of independent non-executive directors. The management of each business unit is the responsibility of the relevant directors and senior management.

The Board of Directors

The roles and responsibilities of the Board are set out in a formal Board Charter. The Charter also identifies certain matters which are specifically reserved for decision by the Board. These include approval of the objectives and strategies of the Group and its subsidiaries and branches, and approval of significant changes in the Group's capital or corporate structure or in its structures of management or internal control as well as the approval of specific transactions, communications and appointments. In addition, the Charter specifies the role of the Group Chief Executive to manage the Group's business on a day-to-day basis, subject to the matters reserved.

The Board, comprising the Chairman, four executive directors and eight independent non-executive directors (in 2005), meets on a monthly basis to consider key business issues. When necessary, the Board will meet more frequently, and during the year, met on a further two occasions. Directors receive relevant briefing papers in advance of Board and committee meetings, and receive regular reports on the Group's financial position, key areas of the Group's business operations and other material issues.

The Roles of the Chairman and the Group Chief Executive

The division of responsibilities between the Chairman and Group Chief Executive is clearly defined and the roles are separate. The responsibilities are documented in the approved Board Charter. The Chairman is responsible for the leadership of the Board and the Group Chief Executive for the management of the Group. In discharging his responsibilities, the Group Chief Executive is advised by the executive directors and senior managers of the business units.

Directors' Independence

The Board considers all of the non-executive directors to be independent in character and judgement. There are no relationships or circumstances which are likely to affect the independent judgement of any of these directors. The Chairman has been a director of the Company since 1993. Given the long-term nature of much of the Group's business, the Board considers that such length of service is important to the balance of the Board. He is also Chairman of Scottish & Newcastle PLC. The Board has considered the Chairman's commitments and is satisfied that he has sufficient time to devote to his position as Chairman of the Company.

Re-election

Directors retire by rotation every three years and are also subject to re-election at the first Annual General Meeting following their appointment.

Corporate Governance

Professional development

Directors receive appropriate induction training when joining the Board and, on appointment, commit to continuing their development, allowing them to maintain the standard expected of directors. In addition, an ongoing programme of development and training is provided. During the period, Board training sessions took place on relevant topics including regulatory and financial reporting developments. At any time, in furtherance of their duties, the directors may seek independent professional advice at the Company's expense.

The Company Secretary

All directors have access to the advice and services of the Company Secretary. He is responsible for advising the Board, through the Chairman, on all governance matters, for ensuring that Board procedures are followed, and relevant rules and regulations observed.

Performance evaluation

The Board has, through the Nominations Committee, developed a formal annual review process to assess how well the Board, its committees and directors are performing and how their respective performances might be improved. This assesses performance against the relevant terms of reference. The process involves the use of questionnaires and interviews with all Board members to gather information, followed by a review discussion. The review also assesses the performance of each director and the contribution he or she makes against agreed performance objectives. The result of this process is the preparation of individual and overall Board action plans including agreed recommendations, objectives and timescales.

The Chairman and the non-executive directors met in the absence of the executive directors during the period. The non-executive directors, led by Hugh Stevenson, the Senior Independent Director, also met once during the period without the Chairman being present to consider the Chairman's performance.

Board committees

The Board has established a number of committees, each of which operates within specific terms of reference. Details of these committees, including membership and duties, are set out on pages 11 to 22.

The following table sets out the frequency of, and attendance at, Board and Board Committee meetings during the period:

	Group Board	Audit Committee	Remuneration Committee	Nominations Committee	Investment Committee	Demutualisation Committee
Number of meetings	14	7	7	2	10	18
Sir Brian Stewart	14	-	-	2	-	16
Executive Directors						
Sandy Crombie	14	-	-	2	-	17
John Hylands	14	-	-	-	-	18
Alison Reed (i)	9	-	-	-	-	-
Trevor Matthews	14	-	-	-	-	-
Non-Executive Directors						
Kent Atkinson (ii)	12	6	-	-	-	-
Lord Norman Blackwell	14	7	6	-	-	18
Gerry Grimstone	14	-	7	-	9	16
Alison Mitchell	13	-	-	-	9	-
Sir Nicholas Monck (iii)	3	2	-	-	2	-
David Newlands (iv)	14	7	-	2	-	17
Jocelyn Proteau	14	5	-	1	-	-
Hugh Stevenson	13	-	7	2	10	-

(i) Alison Reed was appointed on 13 June 2005, and since appointment has attended nine out of nine Board meetings.

(ii) Kent Atkinson was appointed on 26 January 2005, and since appointment has attended twelve out of thirteen Board meetings.

(iii) Sir Nicholas Monck retired on 22 March 2005 and prior to his retirement attended three out of three Board meetings.

(iv) David Newlands resigned on 6 March 2006.

Corporate Governance

Relations with members

The Group communicates with members using a range of media. The Annual General Meeting (AGM), to which all eligible members are invited, allows members to discuss relevant business issues with the Board. Notice of the AGM, Summary Financial Statements and related AGM papers are issued before the meeting to allow members to consider the items of business. At the meeting, the level of proxies lodged and the numbers for and against each resolution are reported together with details of how the Chairman of the meeting has exercised his discretion in respect of proxies lodged in his favour.

The Group website at www.standardlife.com also contains up to date information on the Group and its Corporate Governance. The Annual Report and Accounts are available for view on the website or members can request a hard copy. A regular magazine, 'Update' is issued to all members, and this provides current information on the Group and answers frequently asked questions. Members' roadshow presentations provide additional information and the opportunity for members to discuss relevant business issues with directors and senior managers.

Risk Identification and assessment

Scope and nature of risk reporting and measurement systems

The Board has approved the Group Risk Management Policy which sets out the overall framework through which risks are managed across the Group. The framework is designed to support the identification, assessment, monitoring and control of risks that are significant to the Group's business objectives. Risks are categorised as market, credit, liquidity, insurance or operational risk, and Group policies have been established for each of these categories. The policies are reviewed and approved annually by the Board. The policies define the Group's interpretation of these risks, detail the reporting requirements to the Group Risk Committees and the Board, and contain limits and structures approved by the Board to ensure that appropriate controls are in place and maintained over the risk exposures. Regular reports are submitted to the Board summarising the Group's overall exposure. The reporting systems are replicated at each business unit in the Group to allow the key risks to be filtered to the Board. Further information on how the Group manages and mitigates these risks is included in Note 31 of the financial statements.

Structure and organisation of the risk management function

The Group has an established risk management function whose role is to support the Board in meeting its risk management responsibilities. Group Risk Management has overall responsibility for reporting to the Board in relation to setting and controlling risk exposures. It drafts the Group risk policies for the Board's approval. It also supports and monitors the effective implementation of the policies at Group and business unit levels and supports the Risk Committees. Risk functions have also been established in each business unit. The role of these functions is to implement the Group policies as appropriate to each business unit.

Risk oversight

During 2005 the Group had two senior management risk committees, the Group Technical Risk Committee (GTRC) and the Group Operational Risk Committee (GORC); these committees had formal terms of reference and met regularly. Their role was to support the implementation and monitoring of the Group risk policies and to report to the Group Chief Executive and the Board on the effectiveness of the implementation of the policies. In January 2006, a Group Asset & Liability Committee (ALCO) was created to replace the GTRC. The Group ALCO's mandate is to ensure that the financial risks (credit, market, liquidity and insurance) inherent in the Group's activities are identified and managed in accordance with the appetite and limits approved by the Board. The Group ALCO is chaired by the Group Finance Director, and its members include senior finance representatives of the Group Companies. The GORC is chaired by the Director, Group Risk & Compliance and its members include senior managers with operational responsibilities at each Group company.

Corporate Governance

Internal control framework

The directors have overall responsibility for the Group's system of internal control and for the ongoing review of its effectiveness. The system was in place throughout the period and up to the date of the approval of the Annual Financial Statements. It is designed to manage, rather than eliminate, the risk of failure to meet business objectives and can only provide reasonable, not absolute, assurance against material misstatement or loss.

The effectiveness of internal controls is reviewed regularly by Group Internal Audit and Group Compliance, which report their findings to the Audit Committee and the Board. As noted below, a specific annual review is also undertaken by the directors.

Review of internal controls

In accordance with the Combined Code, and the further guidance in the Turnbull Report, the Board has reviewed the effectiveness of the system of internal control. This incorporated a review of the Group's internal control framework and an assessment of the internal control issues raised during the period through the reports provided by Group Internal Audit, Group Compliance and Group Risk Management. It also included reviewing the results of the process of direct self-certification where directors and senior managers across the Group confirm their compliance with the relevant elements of the Group's internal control framework, including policies and minimum standards. The review covered material internal controls, including financial, operational and compliance risk controls. *Where material control weaknesses were identified, corrective action plans were put in place and monitored regularly.*

Report of the Audit Committee

Composition of the Audit Committee

The members of the Audit Committee, who are all independent non-executive directors, are:

Kent Atkinson (Chairman)
David Newlands (resigned 6 March 2006)
Lord Norman Blackwell
Sir Nicholas Monck (retired 22 March 2005)
Jocelyn Proteau
Gerry Grimstone

On 6 March 2006, David Newlands announced he would step down from the Board and his role as Chairman of the Audit Committee. Kent Atkinson, the former Finance Director of Lloyds TSB, was appointed a director on 26 January 2005 and assumed the Chair of the Audit Committee on 6 March 2006. The Board believes that the new Chairman of the Audit Committee has recent and relevant financial experience. Gerry Grimstone, was appointed a director on 22 July 2003 and was appointed to the Audit Committee on 14 March 2006.

Role of the Audit Committee

The Audit Committee's remit is to consider any matter relating to the financial affairs of the Group, its internal and external audit arrangements and its internal control and compliance arrangements, which it determines to be desirable. A copy of the Committee's terms of reference is available from the Group's website at www.standardlife.com. The Audit Committee meets at least four times a year, although will meet more frequently when required, and during the current period met seven times. At least once a year, it meets with the external and internal auditors without management being present. Audit Committee meetings are also attended by the Group Chief Executive, Group Finance Director and other members of senior management as appropriate. The Audit Committee reports its activities and makes recommendations to the Board.

The Audit Committee reviews the financial statements of the Group, the Company's regulatory returns and any formal statements relating to the financial performance of the Group and Group companies. This incorporates consideration of significant accounting policies, estimates and judgements applied, changes made to these during the period, and the view of the external auditors. It considers the effectiveness of the Group's internal audit function and monitors the external auditors' independence and objectivity and the effectiveness of the external audit process. It receives regular updates from the Group Operational Risk Committee and Group Technical Risk Committee. The Audit Committee also reviews the arrangements by which staff of the Group may, in confidence, raise concerns about possible impropriety in matters of financial reporting and other matters under the Committee's remit. Any concerns are independently investigated and the Committee ensures that appropriate follow up action is taken. In undertaking its duties the Committee is authorised by the Board to obtain any information it requires from any director or employee of the Group. The Committee is also authorised to seek, at the expense of the Group, appropriate professional advice inside and outside the Group whenever it considers this necessary.

External audit

The Audit Committee approves statutory and regulatory audit fees annually. A policy is in place which aims to support and safeguard the objectivity and independence of the auditors, taking into consideration relevant professional and regulatory requirements, so that the services provided are not impaired by the provision of certain allowed non-audit services. The policy prohibits the auditors from performing certain types of non-audit services and ensures that where non-audit fees are significant, they are subject to the approval of the Audit Committee. The involvement of the auditors in performing non-audit work has increased during the period, primarily as a result of the implementation of International Financial Reporting Standards (IFRS) and preparations for the proposed demutualisation.

The Committee reviews annually a report provided by the external auditors confirming their independence and objectivity within the context of regulatory requirements and professional standards. The Audit Committee, having reviewed the service provided by the external auditors, considers PricewaterhouseCoopers LLP to be independent.

Report of the Audit Committee

The Audit Committee assesses the qualifications, expertise and resources of the external auditors in order to assess their effectiveness. It considers the scope and planning of the external audit of the Group, reviewing the findings with the external auditors. It also approves the terms of engagement and remuneration to be paid to the external auditors for audit services and reviews and agrees the engagement letter issued by the external auditors at the start of each audit.

The Audit Committee has responsibility for making a recommendation to the Board on the appointment, reappointment and removal of the external auditors. The external audit was the subject of a tender process in 2003, following which the present auditors were re-appointed.

Internal audit

The Audit Committee is required to assist the Board to fulfil its responsibilities relating to the effectiveness of the internal audit function. To fulfil these duties the committee reviews the internal audit programme and ensures that the internal audit function is adequately resourced, considers the scope and planning of the internal audit of the Group and reviews any findings with the internal auditors.


Kent Atkinson, Chairman, Audit Committee
Edinburgh, 28 March 2006

Report of the Remuneration Committee

Foreword

Standard Life's remuneration approach is to reward outstanding performance that benefits policyholders and not reward poor performance. This report gives full details of all the remuneration paid to directors during the last year.

During 2005, the Remuneration Committee (the Committee) conducted a review of the Group's pension provisions in light of proposed changes to pension legislation taking effect from 6 April 2006 ('A' day). The results of this review are outlined below.

All the new arrangements are in line with best practice and recognise the Group's strong commitment to good corporate governance.

Remuneration Committee

The members of the Committee, who are all independent non-executive directors, are Gerry Grimstone (Chairman), Hugh Stevenson and Lord Blackwell.

The Committee considers and makes recommendations to the Board on the remuneration policy and rewards for the Chairman, the executive directors and senior executives. A copy of the Committee's terms of reference is available from the Group's website at www.standardlife.com.

New Bridge Street Consultants LLP continue to provide the Committee with independent remuneration advice. Other than assisting in the Committee's work, New Bridge Street Consultants LLP have also been assisting with the design of all-employee share plans. The Committee receives information on comparative pay data from Towers Perrin. It also receives advice from the Group Chief Executive, Group Operations Director and the Compensation and Benefits Manager concerning the implementation of remuneration policy.

Remuneration policy

The Group believes that its people are a key factor in contributing to the overall success of the organisation and is committed to providing total remuneration packages which enable it to attract, reward and retain high quality staff. Remuneration packages are based on market rates and on an individual's contribution to the Group's performance.

The Group seeks to provide remuneration packages which reward superior performance in a manner which is consistent with the long-term interests of policyholders. For executives, this is achieved by ensuring that potential rewards under long-term incentive arrangements are greater than those available under short-term incentive plans.

During 2004 the Committee reviewed the Group's incentive arrangements. This has led to amendments being made to the performance related annual bonus and to the implementation of a new Long-Term Incentive Plan (LTIP), both from January 2005, the details of which are described below.

Remuneration packages for the Group's executive directors comprise: base salary, a number of benefits (to be delivered through a flexible benefits programme from June 2006), pension provision, short-term (annual) bonus and participation in a long-term incentive plan. The salaries and other emoluments shown in the directors emoluments table below cover the 12 months to 31 December 2005. The figures relating to 2004 cover the 13.5 month accounting period to 31 December 2004 and are not directly comparable to the salaries and emoluments paid this year. Details of each element of the package are as follows:

Base salary

The Committee, assisted by its independent advisor, reviews annually data concerning the level of salaries paid to senior executives performing similar roles in the financial services industry and more broadly where appropriate. It also considers the prevailing circumstances of the Group and base salary levels throughout the organisation. The contribution and the level of experience of each executive director are taken into account to determine base salary. This is then reviewed by the Committee in the context of the total remuneration package.

Report of the Remuneration Committee

Benefits

Executive directors are eligible to receive benefits comprising car allowance, health care provision and beneficial loans on equivalent terms to other employees. There are no special arrangements for directors. Where appropriate, reasonable relocation costs for new directors are met by the Group.

Pension arrangements

In the UK, Standard Life's defined benefit pension scheme was closed to new entrants, including any new directors, from 16 November 2004. All new recruits from this date are offered participation in a defined contribution pension scheme. UK based executive directors who joined Standard Life before 16 November 2004 are members of a staff pension scheme which provides pensions on a final salary basis. The normal retirement age is 60 for the UK scheme and 65 for the Canadian scheme.

In the UK, the accrual rate prior to 16 November 2004 was $1/60^{\text{th}}$ of final salary for each year of service. From this date, all staff, including executive directors, decided whether to agree to sacrifice a percentage of pensionable pay in order to retain this level of accrual or accept a lower future accrual rate of $1/80^{\text{th}}$ of pensionable pay. The level of sacrifice from 16 November 2004 was 2% of pensionable pay and rose to 3.5% from 16 November 2005. It rises to 5% of pensionable pay from 16 November 2006. Post retirement increases in pensions are discretionary and in the past have been based on retail price index inflation.

In Canada, there is a final salary pension scheme which encompasses defined benefit and defined contribution elements. Prior to 1 January 2005, the accrual rate was $1/60^{\text{th}}$. From this date, the accrual rate is $1/80^{\text{th}}$ and employees are required to contribute 25% of the cost of the benefits and Standard Life contributes 75% of the cost of the benefits. All employee contributions are directed to the defined contribution option of the pension plan. The plan applies to all employees.

For death during pensionable service in the UK, a lump sum of up to four times salary is payable, together with a spouse's pension of up to one-third of the member's pensionable salary. In Canada, a lump sum equal to the commuted value of the pension to which the member is entitled is payable to the surviving spouse, together with a spouse's pension equal to 30% of pensionable earnings. For death in retirement, a spouse's pension of up to two-thirds of the member's pension is payable. Children's allowances are payable, usually up to the age of 18 (25 in Canada if in full time education), and protection is afforded in the event of disablement.

The Committee has reviewed executive pension provisions in the light of the proposed changes in pension legislation which become effective from 6 April 2006. Those who joined the Group before 16 November 2004 (Sandy Crombie, John Hylands and Trevor Matthews) will have the option to:

- retain membership of the defined benefit pension scheme on existing terms;
- sacrifice 5% of base salary which the employer will inject into a defined contribution scheme along with a further employer contribution of 27.5% of base salary; or
- receive a non-consolidated cash supplement of 25% of base salary.

For UK executive directors with service prior to 1982 (only Sandy Crombie and John Hylands), a past commitment has been made that up to the age of 65 annual pension increases should be made in line with salary inflation and (for John Hylands) that he would be able to accrue by age 60 the level of pensionable service that would have applied at age 65.

As part of the Committee's review of executive pension provisions, it requested Sandy Crombie and John Hylands to forego the special increase provision for service after 5 April 2006. As compensation for this, the Group has injected a payment of £35,600 for Sandy Crombie and £38,100 for John Hylands in March 2006 into their respective Retirement Account Plans which are individual money purchase arrangements attached to the main staff defined benefit pension scheme. The payments were calculated by the Scheme Actuary and were based on the present value of the difference between the special pension increase rate and the normal increase rate for service after 5 April 2006.

John Hylands will continue to accrue pensionable service as described above whilst he remains in the defined benefit pension scheme. In the event that he elects to opt out of the scheme after 5 April 2006, the Committee has indicated that he will receive compensation on a cost neutral basis at his retirement date for any loss of accrued service.

Report of the Remuneration Committee

Alison Reed joined Standard Life on 13 June 2005 and does not participate in the defined benefit pension arrangement. Her contract provides for a notional pension allowance of 20% of annual base salary which was subject to review by the Committee. She sacrifices 25% of the earnings cap from this allowance and the Group pays an equivalent amount into the defined contribution pension scheme on her behalf. The balance of the pension allowance (£20,150 in 2005) was paid in equal monthly instalments subject to tax and national insurance deductions. For death during service, a lump sum of up to four times salary is payable. As mentioned above, the Committee has determined that the level of the non-consolidated cash supplement has been increased to 25% of base salary and under the terms of the contract agreed when hiring Alison Reed, this will be backdated to her start date. She received a payment of £12,477 in February 2006 to reflect this change for the period between her start date and 31 December 2005. The total payment of £32,627 is included in the Taxable Benefits column in Table 1 (below).

Annual bonus

Each executive director participates in a performance related non-pensionable annual bonus scheme. Group performance and individual contribution determine the amount paid to each executive director.

New bonus plan

As part of its review the Remuneration Committee introduced a new annual bonus scheme from 1 January 2005. The amount of annual bonus that can be earned is capped and is based on salary level as at the end of the relevant period. For the Group Chief Executive the scheme is designed to deliver a bonus of 50% of salary for achieving target performance and he has a maximum potential bonus of 100% of salary. For the other executive directors, achieving target performance would deliver a payment of 45% of base salary, and the maximum potential is 90% of salary. These figures have been set by the Committee to ensure that there will be a significant degree of stretch between the performance required for achieving target and maximum bonus payments.

For executive directors, the Committee has determined that 20% of bonus potential may be payable for an executive director achieving pre-determined personal targets during the year as assessed by the Committee. The balance of any potential bonus (80%) relates to the financial performance of the Group and the business for which the director is responsible. For the Group Chief Executive, the Group Finance Director and the Group Demutualisation Director, the entire 80% of annual bonus potential will depend on the Group's results. For the Chief Executive of UK & Europe Life and Pensions, 50% of total potential bonus will depend on the UK & Europe Life and Pensions performance and 30% will depend on the Group's performance.

Financial performance is measured by comparing the year's actual profitability compared to budgeted profitability. For example, European Embedded Value (EEV) profits before tax are used for life and pension businesses, and for Standard Life Investments, Standard Life Bank and Standard Life Healthcare, operating profits before interest and tax are used. The Group's profitability is the sum of these businesses' EEV and operating profits. Since each business unit is also expected to operate within clear capital plans, the Committee has discretion to reduce payments on an exceptional basis if capital usage is significantly greater than planned. All payments under the annual bonus scheme are taken into account when calculating the profits earned by the Group and/or the relevant business.

Long-term incentive plans

During 2004 the Committee reviewed the previous long-term incentive plans (LTIP) and concluded that a new non-pensionable LTIP (the 2005 Plan) should be implemented. As a result of the change to the financial year-end date awards are granted in January of each year from 2005 onwards. As awards were previously granted in November of each year, there is no 2004 plan.

2005/2006 Awards

In 2005, approximately 80 of the Group's most senior executives, including the executive directors, were granted an award under the LTIP. This is a significantly smaller population of participants than in previous years and reflects the Committee's desire to ensure that long-term rewards are focused on the individuals who can deliver longer term results.

The awards take the form of a right to receive a cash payment in three years' time provided that a performance condition is achieved (described below) and the executive remains employed by Standard Life. However, should the Group's shares become listed during the three-year vesting period, the awards will be converted into awards over Standard Life shares using the average share price during the period of 20 days commencing with date of flotation. The flotation will not trigger a payment of bonus or early vesting of awards.

Report of the Remuneration Committee

The performance target is based on the Group's return on capital. Return on capital is defined as the sum of the operating profits of Standard Life Bank, Standard Life Healthcare and Standard Life Investments and the EEV profits of the UK, Canadian and International life and pension businesses divided by a Group capital figure as defined in the rules of the Plan.

The target is set on a sliding scale basis and performance will be measured over a three-year period. For example, for the 2005 awards, the return on capital for the year ending 31 December 2007 will be compared with the target. If the performance condition is not met at this first and only review then the awards lapse.

This performance target has been chosen by the Committee because it is an appropriate measure of the financial performance of the Group as a whole, it is aligned to the corporate goals of the Group and has universal application across all participants.

For 2006, approximately 80 of the Group's most senior executives, including the executive directors, were granted an award under the LTIP. The performance target is the return on capital and, as part of the Company's transition in reporting EEV profits, the return on capital over the two years ending 31 December 2008 will be compared with target.

For both awards, the maximum bonus levels available to the Group Chief Executive will be 175% of salary. The maximum bonus levels for the other executive directors will be 100% of salary.

2002/2003 Awards

The 2002 and 2003 awards were granted under an earlier LTIP (which has been replaced with the plan described above). These two awards have three-year performance periods commencing on 16 November of the relevant year and the rules of the former plan state that the Board will assess the Group's success in creating value for its participating with profits policyholders over the relevant three years. In making this assessment, the Board will take into account the profitability of the Group's operations, investment returns on the Group's with profits funds and such other matters as it may consider relevant. Comparative information will be used where available. As the basis of its review, the Board assesses each business unit's performance and considers the relative weighting each business unit has on overall Group performance.

The maximum bonus percentage for each of the current executive directors, reflecting their responsibilities during the respective three-year performance periods, is as follows:

	2002 Award	2003 Award
Sandy Crombie	100%	100%
John Hylands	85%	85%

For Claude Garcia, the maximum bonus percentage was 200%.

For the 2002 award, the three-year performance period ended on 15 November 2005 and the Board, in making its assessment, has determined that zero vesting is applicable. Awards have therefore lapsed and there is no opportunity to retest performance at a future date.

Personal Bonus - Trevor Matthews

Special recruitment arrangements were required when hiring Trevor Matthews and these were fully explained in the Remuneration Report in the 2004 Annual Report and Accounts. To compensate him for the future potential gain in lost share options and other long-term equity benefits, a non-pensionable personal bonus arrangement was agreed for 2004, 2005 and 2006. The maximum bonus available is 85% of base salary. Specific objectives are agreed at the start of each business year with the Board. For the business year ended 31 December 2005, the Board have approved a personal bonus payment of £363,375.

Recruitment of Alison Reed

No special recruitment arrangements, other than that relating to pension provision (described above) were made on recruitment of Alison Reed.

Report of the Remuneration Committee

Retirement of Claude Garcia

Claude Garcia stepped down from his position as President, Canadian Operations and as an executive director from 31 December 2004. He remained in employment in a consultancy capacity until his retirement, on 12 November 2005, on his previous terms and conditions of employment and continued to participate in the annual bonus arrangement and long-term incentive plans until his date of retirement. For the period 1 January 2005 to 12 November 2005 he received a salary of £283,802, benefits to the value of £14,992 and a bonus payment of £110,962. He also received a payment of £32,298 in respect of an award under the 2005 long-term incentive plan up to his date of retirement. He will receive no further payment in respect of the 2002, 2003 or 2005 LTIP.

Policy on service contracts

All executive directors have service contracts that provide for a twelve month notice period from the Group.

Dates of service contracts are:

Sandy Crombie	21 October 2005
John Hylands	20 November 2002
Trevor Matthews	1 July 2004
Alison Reed	13 June 2005
Keith Skeoch	6 March 2006

With the exception of John Hylands, no directors have contracts which contain any provisions for compensation payments beyond the terms of their service agreement on termination. In light of the Group's request for John Hylands to lead the demutualisation programme, he has agreed with the Group that should his employment be terminated following completion of the demutualisation programme, he will be entitled to receive a termination payment equal to 12 months salary with benefits and that such package will be no worse than that which would be available to other senior executives in a similar position at the date of termination.

Keith Skeoch was appointed to the Board on 6 March 2006, therefore no information on his remuneration is provided in this report.

The Chairman and the non-executive directors have letters of appointment with one month's notice provision on either side. The date of first appointment for the Chairman and each non-executive director is:

Sir Brian Stewart	27 April 1993
Lord Blackwell	24 June 2003
Gerry Grimstone	22 July 2003
Alison Mitchell	16 December 2000
Sir Nicholas Monck	16 August 1997 (retired 22 March 2005)
David Newlands	16 June 1999 (resigned 6 March 2006)
Jocelyn Proteau	26 August 2003
Hugh Stevenson	16 June 1999
Kent Atkinson	26 January 2005

The letters of appointment do not contain any provisions for compensation payments to be made to the Chairman and non-executive directors on termination.

Policy on external appointments

Subject to the Board's approval, executive directors are able to accept a limited number of external appointments to the boards of other organisations. Any fees may be retained by the individual. Alison Reed receives fees of £42,500 as a non-executive director of British Airways PLC. Sandy Crombie is an active member of the Board of the Association of British Insurers, but received no fee for this work.

Chairman and non-executive directors' remuneration

The Chairman and non-executive directors are not eligible to participate in annual bonus plans, long-term incentive plans or pension schemes (except as disclosed in Table 3: Directors' pension information, footnote 4). Their fees are set by the Board after taking advice from the Group Chief Executive and take into account the time commitment and responsibility of the roles and the fees paid by other comparable organisations within the financial services sector.

Report of the Remuneration Committee

Audited information

Directors' remuneration for 2005

1. Directors' emoluments, excluding LTIP and pension information

Emoluments in respect of the 12-month period ended 31 December 2005 are shown below.

Group performance and individual contribution determined the amount of annual bonus paid to each executive director. The Committee reviewed both actual performance against previously set demanding profit targets to determine the group element of the award and also the personal element, which reflects the executive's success in meeting individually tailored targets.

	Base Salary / Fees £000	Taxable Benefits £000	Annual Bonus £000	Total 2005 £000	Total for 13.5 months to 31/12/2004 £000	Total 2004 ¹ £000
Executive Directors						
Sandy Crombie ²	656	20	686	1,362	682	606
John Hylands ³	332	17	300	649	458	407
Trevor Matthews ⁴	475	36	774	1,285	1,615	-
Alison Reed ⁵	249	58	220	527	-	-
Non-Executive Directors						
Sir Brian Stewart	150	-	-	150	137	122
Kent Atkinson ⁶	48	-	-	48	-	-
Lord Blackwell ⁷	54	-	-	54	41	37
Gerry Grimstone ⁸	60	-	-	60	45	40
Alison Mitchell	50	-	-	50	41	37
David Newlands ⁹	80	-	-	80	67	60
Jocelyn Proteau ¹⁰	70	-	-	70	41	37
Hugh Stevenson ¹¹	80	-	-	80	66	58
Former Executive Directors						
Claude Garcia ¹²	-	-	-	-	367	326
Iain Lumsden ¹³	-	-	-	-	151	-
Former Non-Executive Directors						
The Hon Roy MacLaren ¹⁴	-	-	-	-	39	-
David Lewis ¹⁵	-	-	-	-	20	-
Sir Nicholas Monck ¹⁶	15	-	-	15	43	38
Total	2,319	131	1,980	4,430	3,813	-

- The 12-month equivalent figure is provided for those individuals who were directors for the full 13.5 month period. It is a proportion (366/412 or 88.8%) of the total 2004 (13½ month) figure.
- Sandy Crombie elected to sacrifice £14,165 from his salary in return for an equivalent employer contribution into the defined benefit pension scheme. The total emoluments for the 13½ month business year ended 31/12/04 (£682k) do not include any bonus payment. Notwithstanding his contractual right to a payment of £200,000, Sandy Crombie did not accept any bonus for 2003/04, nor did he accept a LTIP payment of £324,355.
- John Hylands elected to sacrifice £7,115 from his salary in return for an equivalent employer contribution into the defined benefit pension scheme. He decided not to accept a LTIP payment of £68,147 in 2004.
- Trevor Matthews elected to sacrifice £10,198 from his salary in return for an equivalent employer contribution into the final salary pension scheme. In order to provide compensation for loss of share options and other long-term equity benefits, the Board agreed a non-pensionable personal bonus arrangement for 2004, 2005 and 2006. For 2005, the Board have approved a personal bonus payment of £363,375 related to his recruitment arrangements and this is included under annual bonus. Appointed to the Board on 1 July 2004, his remuneration in 2004 related to the period from appointment to the business year-end. Full details of the special recruitment arrangements required when hiring Trevor Matthews in 2004, including the payment of compensation on joining of £1,043,471, were fully disclosed in the 2004 Annual Report and Accounts.
- Alison Reed was appointed on 13 June 2005. Base salary, taxable benefits and annual bonus in the above table relate to the period since appointment to the year-end. Taxable benefits include a pension allowance of 25% of base salary from which she has elected to sacrifice £14,300 and in return the Group makes an equivalent employer contribution into a money purchase pension scheme. She has also incurred relocation expenses of £2,322 to date.
- Appointed 26 January 2005.
- Lord Blackwell's total fee includes a fee as Chairman of Life & Pensions (£4,000).
- Gerry Grimstone's total fee includes a fee as Chairman of the Remuneration Committee (£10,000).
- David Newlands' total fee includes a fee as Deputy Chairman (£20,000) and Chairman of the Audit Committee (£10,000). He resigned as a Director on 6 March 2006.
- Jocelyn Proteau's fee reflects the extra responsibilities in relation to Canadian domestication. His 'normal' fee would be £60,000, which includes a fee as Chairman of the Canadian Board (£10,000).
- Hugh Stevenson's total fee includes a fee as Senior Independent Director (£20,000) and Chairman of Standard Life Investments (£10,000).
- Claude Garcia stepped down from his position as President, Canadian Operations and as an executive director from 31 December 2004. He remained in employment in a consultancy capacity until his retirement on 12 November 2005 and under the terms of his contract received payment of base salary (£283,802), taxable benefits (£14,992) and annual bonus (£110,962) for the period from 1 January 2005 to his date of retirement.
- Resigned as a director 12 January 2004, retired on 31 January 2004. Base salary and taxable benefits in the above table relate to the period from 16 November 2003 to his date of retirement.
- Retired on 23 November 2004.
- Resigned on 25 June 2004.
- Retired 22 March 2005.

Report of the Remuneration Committee

2. Directors' interests in cash based long-term incentive plans (LTIPs)

	Maximum unvested LTIPs outstanding at 31/12/2004 ¹ £000	Amounts paid in period ² £000	LTIPs that have lapsed ³ £000	Maximum value of LTIPs that could vest in 2006 ⁴ £000	Maximum value of LTIPs that could vest in 2007 ⁵ £000
Sandy Crombie	1,136	-	542	584	1,138
John Hylands	502	-	230	272	331
Trevor Matthews ⁶	-	-	-	-	475
Alison Reed ⁷	-	-	-	-	383
Former Executive Director					
Claude Garcia ⁸	865	32	897	-	-

1. This column shows the aggregate maximum value of cash awards outstanding at 31 December 2004. This comprises the 2002 and 2003 cash awards.
2. This column represents the cash amount paid to participants in the period to 31 December 2005. For Claude Garcia this payment relates to the 2005 award up to his retirement date.
3. This column shows the cash awards which have lapsed during the period due to the performance conditions not being met. This column represents the full 2002 awards. For Claude Garcia it also represents the full 2003 award and part of the 2005 award.
4. This column shows the maximum cash value of the 2003 awards which covers the performance period from 16 November 2003 to 15 November 2006, with vesting thereafter subject to performance.
5. This column shows the maximum cash value of the 2005 awards which covers the performance period from 1 January 2005 to 31 December 2007, with vesting thereafter subject to performance.
6. Trevor Matthews did not receive awards in 2002 or 2003.
7. Alison Reed did not receive awards in 2002 or 2003. She was granted a 2005 award on 13 June 2005 and the maximum value expressed in the above table is prorated to reflect this date.
8. Claude Garcia's awards are denominated in Canadian dollars and the exchange rate of £1 = \$2.005 as at 31 December 2005 (2004: £1 = \$2.303) has been used in this table. He retired as a director on 31 December 2004 but remained in employment in a consultancy capacity until his retirement on 12 November 2005. He participated in LTIPs until his date of retirement. He will receive no further payment in respect of the 2002, 2003 or 2005 awards.

3. Directors' pension information

	Age at 31/12/2005	Years of pensionable service at 31/12/2005	Accrued entitlement at 31/12/2004 or date of retirement £000	Additional pension earned during the year £000	Additional pension earned in excess of inflation £000	Transfer value of additional pension in excess of inflation £000	Accrued entitlement at 31/12/2005 or date of retirement £000	Transfer value of pension at 31/12/2004 £000	Increase in transfer value £000	Transfer value of pension at 31/12/2005 or date of retirement £000
Sandy Crombie ¹	56	36	388	41	29	570	429	6,669	1,633	8,302
John Hylands ²	54	29	159	7	2	33	166	2,142	363	2,505
Trevor Matthews ³	53	1	2	3	3	55	5	22	61	83
Sir Brian Stewart ⁴	60	10	5	-	-	-	5	77	12	89
Former Executive Director										
Claude Garcia ⁵	65	31	157	33	19	263	190	1,786	800	2,586

1. The increase in transfer value (£1,633,000) includes an employer contribution of £14,165 resulting from Sandy Crombie's decision to sacrifice this element of his salary.
2. The increase in transfer value (£363,000) includes an employer contribution of £7,115 resulting from John Hylands' decision to sacrifice this element of his salary.
3. Trevor Matthews' total contractual pension entitlement is 1/60th of uncapped base salary for each year of company service. In addition to the above, he has additional benefits provided via unfunded unapproved arrangements. The accrued pension and transfer value at 31 December 2005 were £6,575 and £147,000 respectively. The increase in transfer value (£61,000) includes an employer contribution of £10,198 resulting from his decision to sacrifice this element of his salary.
4. Sir Brian Stewart was a member of a scheme which provided pensions based on final fees payable in respect of services as a director of the Group. The Group wound up this scheme on 16 November 2001 and he is no longer entitled to earn additional pension benefits from the Group.
5. Retired on 12 November 2005 – data for 2005 is at date of retirement.

Report of the Remuneration Committee

Unaudited information

Except for Canada, members of the schemes have the option to pay additional voluntary contributions to secure additional pension. These are not included in the above table.

The pension entitlement shown is that which would be paid annually on retirement, based on service to 31 December 2005. Transfer values have been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN 11. These represent actuarial liabilities of the schemes, not sums due to the directors.

Related party transactions

Unfunded pensions paid to former non-executive directors were £nil (2004 : £4,210).

All transactions between directors and the Group are on commercial terms which are equivalent to those available to all employees. During the year to 31 December 2005 the directors contributed £6m (2004 : £0.6m) to products sold by the Group.

On behalf of the Board of Directors

Gerry Grimstone, Chairman, Remuneration Committee

Edinburgh, 28 March 2006

Gerry Grimstone

Other Board Committees

Nominations Committee

Sir Brian Stewart (Chairman)
David Newlands (resigned 6 March 2006)
Jocelyn Proteau
Hugh Stevenson
Sandy Crombie

The Committee met two times during the year. Mr Proteau attended one meeting of the Committee. All other members attended both meetings of the Committee.

The Committee, consisting of a majority of independent non-executive directors, keeps under review the leadership needs of the Group, both executive and non-executive, with a view to ensuring the continued ability of the Group to compete effectively in the marketplace. It meets when required to make recommendations to the Board on new Board appointments and carry out other activities related to the composition and effectiveness of the Board.

When considering new appointments, the Committee evaluates the balance of skills, knowledge and experience of the Board, and following this, prepares a description of the role, including the capabilities required. Once a role description has been agreed, the Committee will interview suitable candidates, and make appropriate recommendations to the Board. The process used to determine Board appointments includes the use of external search consultants.

The Committee approves processes for succession planning, which take into account the skills and expertise required by the Board and senior management within the Group, to allow the Group to operate effectively. A copy of the Committee's Terms of Reference is available from the Group's website at www.standardlife.com.

The Committee also reviews annually the time commitment required from non-executive directors and is satisfied that they have sufficient time to meet their commitment to the Group. The formal letter of appointment received by non-executive directors is available from the Company Secretary.

The Committee changed its name to the Nominations and Governance Committee on 3 January 2006.

Investment Committee

Hugh Stevenson (Chairman)
Gerry Grimstone
Alison Mitchell
Sir Nicholas Monck (retired 22 March 2005)
Kent Atkinson (appointed 31 January 2006)

The Investment Committee meets regularly to review and report to the Board on matters relevant to the management of the Group's investments. The Chief Executive Officer of Standard Life Investments attends meetings of the Committee, together with other appropriate members of staff of Standard Life Investments. A copy of the Committee's Terms of Reference is available from the Group's website at www.standardlife.com.

Other Board Committees

Demutualisation Committee

Sir Brian Stewart (Chairman)

Lord Norman Blackwell

Sandy Crombie

Gerry Grimstone

John Hylands

David Newlands (resigned 6 March 2006)

Alison Reed (appointed to the Demutualisation and IPO Committee on 31 January 2006)

The Demutualisation Committee met broadly on a fortnightly basis during the year to monitor the progress of the Group's demutualisation programme. The Committee considers major and strategic issues arising from the programme on which Board decisions are required.

The Committee reviews the effectiveness of the programme structure and organisation, including approving the appointment of external advisors. The Committee provides regular reports and recommendations to the Board in respect of these matters.

The Committee changed its name to the Demutualisation and Initial Public Offering (IPO) Committee on 3 January 2006.

Independent Auditors' Report to the members of The Standard Life Assurance Company

We have audited the group and parent company financial statements (the "financial statements") of The Standard Life Assurance Company for the year ended 31 December 2005 which comprise the Group Income Statement, the Group and Parent Company Balance Sheets, the Group and Parent Company Cash Flow Statements, the Group and Parent Company Statement of Recognised Income and Expenses and the related notes. These financial statements have been prepared under the accounting policies set out therein. We have also audited, at the request of the directors, the information in the Report of the Remuneration Committee that is described as having been audited.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities. The directors are also responsible for preparing the Report of the Remuneration Committee (because the Company applies the requirements of Schedule 7A to the Companies Act 1985 as if it were a listed company).

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 also, at the request of the directors, audit the part of the Report of the Remuneration Committee to be audited (because the Company applies the requirements of Schedule 7A to the Companies Act 1985 as if it were a listed company). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, 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.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Report of the Remuneration Committee to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if 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 other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' Report, the unaudited part of the Report of the Remuneration Committee, the Corporate Governance Statement and the Report of the Audit Committee and the other Board Committees. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

We also, at the request of the directors (because the company applies the Financial Services Authority listing rules as if it were a listed company), review whether the corporate governance statement reflects the company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

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 and the part of the Report of the Remuneration Committee to be audited. 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 group's and 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 and the part of the Report of the Remuneration Committee to be audited 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 and the part of the Report of the Remuneration Committee to be audited.

Independent Auditors' Report to the members of The Standard Life Assurance Company

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 December 2005 and of its result and cash flows for the year then ended;
- the parent company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 December 2005 and cash flows for the year then ended;
- the financial statements and the part of the Report of the Remuneration Committee to be audited have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors

Edinburgh, 28 March 2006

Consolidated Income Statement for the year ended 31 December 2005

	Notes	Group	
		12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Revenue			
Gross earned premium		3,609	4,351
Premium ceded to reinsurers		(93)	(96)
Net earned premium		3,516	4,255
Net investment return	2	14,377	9,892
Income arising from associates and joint ventures	11	99	86
Fee and commission income	3	360	296
Other income		54	48
Total net revenue		18,406	14,577
Expenses			
Claims and benefits paid		4,195	5,112
Claim recoveries from reinsurers		(59)	(61)
Change in reinsurance assets	21	(112)	(41)
Change in insurance and participating liabilities	21	5,167	2,840
Change in investment contract liabilities		5,886	3,912
Change in deduction from liabilities due to present value of future results	21	(488)	-
Administration expenses			
Restructuring and demutualisation expenses	36	84	75
Other administration expenses	4	2,066	2,273
		2,150	2,348
Change in liability for third party interest in consolidated funds		43	16
Operating expenses		16,782	14,126
Finance costs		109	80
Result before tax		1,515	371
Tax expense	7	531	353
Transfer to/(from) unallocated divisible surplus		901	(15)
Increase in net assets attributable to minority interest		83	33
Balance on Income Statement		-	-

The result after tax and transfer to/(from) unallocated divisible surplus for the year of £83m (2004 : £33m) represents the increase in net assets attributable to minority interest.

Consolidated Balance Sheet as at 31 December 2005

	Notes	Group	
		2005 £m	2004 £m
Assets			
Intangible assets	8	44	27
Deferred acquisition costs	9	290	269
Investments in associates and joint ventures	11	2,608	1,891
Investment property	12	9,907	8,779
Property and equipment	13	590	699
Deferred tax assets	14	75	43
Reinsurance assets	21	779	617
Loans and receivables	15	12,496	12,171
Derivative financial assets	16	247	230
Investment securities	17		
Equity securities and interests in pooled investment funds		43,601	35,494
Debt securities		43,830	37,562
		87,431	73,056
Other debtors	18	1,342	1,392
Cash and cash equivalents	19	4,451	2,840
Total assets		120,260	102,014
Minority interest		340	250
Liabilities			
Non-participating contract liabilities			
Non-participating insurance contracts	20,21	21,158	18,854
Non-participating investment contracts	20,21	40,929	30,597
		62,087	49,451
Participating contract liabilities			
Participating insurance contracts	20,21	19,633	18,264
Participating investment contracts	20,21	18,076	15,929
Present value of future results on non-participating contracts	20,21	(1,528)	(1,041)
Unallocated divisible surplus	23	4,827	3,678
		41,008	36,830
Third party interest in consolidated funds		358	77
Borrowings	24	6,233	5,701
Subordinated liabilities	25	1,878	1,600
Pension and other post retirement benefit provisions	26	386	472
Deferred income	27	238	234
Deferred tax liabilities	14	559	428
Current tax liabilities	14	240	100
Customer accounts related to banking activities and deposits by banks	28	5,134	5,147
Derivative financial liabilities	16	241	358
Other liabilities	29	1,558	1,366
Total liabilities and minority interest		120,260	102,014

Approved on behalf of the Board of Directors on 28 March 2006 by the following Directors:

Sir Brian Stewart, Chairman
Sandy Crombie, Group Chief Executive
Alison Reed, Group Finance Director

Am Crombie

Alison Reed

Consolidated Statement of Recognised Income and Expenses for the year ended 31 December 2005

	Notes	Group	
		12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Fair value losses on cash flow hedges		(4)	-
Fair value losses on cash flow hedges transferred to Income Statement		-	(5)
Actuarial gains/(losses) on defined benefit pension schemes	26	22	(42)
Revaluation of land and buildings	13	11	16
Exchange differences on translating foreign operations	23	218	(93)
Aggregate tax effect of items not recognised in Income Statement		-	4
Other		1	-
Net income/(expense) not recognised in the Income Statement transferred to/(from) unallocated divisible surplus		248	(120)
Net income/(expense) recognised in the Income Statement transferred to/(from) the unallocated divisible surplus		901	(15)
Total transfer to/(from) unallocated divisible surplus		1,149	(135)

Further information is included in Note 23.

Consolidated Cash Flow Statement for the year ended 31 December 2005

	Notes	Group	
		12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Cash flows from operating activities			
Transfer to/(from) unallocated divisible surplus		901	(15)
Tax expense		531	353
Increase in net assets attributable to minority interest		83	33
Operating result before tax		1,515	371
Gain on disposal of property and equipment		(10)	-
Depreciation of property and equipment	4	17	35
Amortisation of intangible assets	4	7	6
Amortisation of deferred acquisition costs	4	72	333
Impairment losses on deferred acquisition costs	4	-	44
Impairment losses on property and equipment	4	9	18
Reversal of impairment on property and equipment	4	(8)	-
Change in present value of future results on non-participating contracts		(488)	-
Interest cost on other borrowings		(4)	-
Adjustment for finance costs on bank activities		136	92
Finance costs		109	80
Foreign exchange loss on investment activity		6	26
Income arising from associates and joint ventures	11	(99)	(86)
Net (increase)/decrease in operating assets and liabilities	30	395	(1,119)
Adjustment for investment income		(39)	3
Taxation paid		(285)	(319)
Net cash flows from operating activities		1,333	(516)
Cash flows from investing activities			
Purchase of property and equipment	13	(84)	(173)
Proceeds from sale of property and equipment	13	21	1
Net proceeds from disposal of subsidiaries	10	179	-
Acquisition of investment in joint ventures	11	(8)	-
Acquisition of investment in associates	11	(18)	-
Purchase of intangible assets	8	(24)	(17)
Net cash flows from investing activities		66	(189)
Cash flows from financing activities			
Proceeds from other borrowings		11	73
Repayment of other borrowings		(2)	(122)
Proceeds from subordinated liabilities		263	560
Interest paid on subordinated liabilities		(107)	(65)
Capital contributions from minority interest		18	38
Dividends paid to minority interest		(7)	(4)
Net cash flows from financing activities		176	480
Net increase/(decrease) in cash and cash equivalents		1,575	(225)
Cash and cash equivalents at the beginning of the year	19	2,696	2,940
Effects of exchange rate changes on cash and cash equivalents		75	(19)
Cash and cash equivalents at the end of the year	19	4,346	2,696
Supplemental disclosures			
Included in operating activities are:			
Interest received		2,910	2,875
Dividend received		1,110	978
Rental income received on investment properties		618	548

Company Balance Sheet as at 31 December 2005

		Company	
	Notes	2005 £m	2004 £m
Assets			
Intangible assets	8	36	20
Deferred acquisition costs	9	212	210
Investments in subsidiaries	10	25,314	6,770
Investments in associates and joint ventures	11	1,937	1,606
Investment property	12	4,385	6,005
Property and equipment	13	415	573
Deferred tax assets	14	59	15
Reinsurance assets	21	1,104	978
Loans and receivables	15	711	938
Derivative financial assets	16	158	196
Investment securities	17		
Equity securities and interests in pooled investment funds		35,067	30,238
Debt securities		21,989	30,836
		57,056	61,074
Other debtors	18	707	1,039
Cash and cash equivalents	19	2,429	1,215
Total assets		94,523	80,639
Undated intercompany financial instrument			
	43	245	-
Liabilities			
Non-participating contract liabilities			
Non-participating insurance contracts	20,21	15,934	14,761
Non-participating investment contracts	20,21	33,735	25,055
		49,669	39,816
Participating contract liabilities			
Participating insurance contracts	20,21	19,633	18,264
Participating investment contracts	20,21	18,076	15,929
Present value of future results on non-participating contracts	20,21	(1,528)	(1,041)
Unallocated divisible surplus	23	4,597	3,730
		40,778	36,882
Borrowings	24	68	124
Intragroup subordinated liabilities	25	1,611	1,600
Pension and other post retirement benefit provisions	26	216	348
Deferred income	27	223	221
Deferred tax liabilities	14	399	381
Current tax liabilities	14	147	62
Derivative financial liabilities	16	120	136
Other liabilities	29	1,047	1,069
Total liabilities and undated intercompany financial instrument		94,523	80,639

Approved on behalf of the Board of Directors on 28 March 2006 by the following Directors:

Sir Brian Stewart, Chairman
Sandy Crombie, Group Chief Executive
Alison Reed, Group Finance Director

Am Crombie

B Stewart

Alison Reed

Company Cash Flow Statement for the year ended 31 December 2005

		Company	
	Notes	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Cash flows from operating activities			
Transfer to/(from) unallocated divisible surplus		786	(6)
Tax expense		310	256
Coupon payments on undated intercompany financial instrument		6	-
Operating result before tax		1,102	250
Gain on disposal of property and equipment		(10)	-
Depreciation of property and equipment		2	33
Amortisation of intangible assets		4	1
Amortisation of deferred acquisition costs		29	286
Impairment losses on deferred acquisition costs		-	44
Impairment losses on property and equipment		9	11
Reversal of impairment on property and equipment		(4)	-
Change in present value of future results on non-participating contracts		(488)	-
Finance costs		100	80
Foreign exchange (gain)/loss on investment activity		(7)	23
Income arising from associates and joint ventures	11	(67)	(71)
Net (increase)/decrease in operating assets and liabilities	30	1,451	(279)
Adjustment for investment income		(212)	(45)
Taxation paid		(248)	(275)
Net cash flows from operating activities		1,661	58
Cash flows from investing activities			
Purchase of property and equipment	13	(43)	(157)
Proceeds from sale of property and equipment	13	40	-
Acquisition of subsidiaries net of cash*	10	-	(298)
Acquisition of investment in joint ventures	11	(4)	-
Acquisition of investment in associates	11	(14)	-
Purchase of intangible assets	8	(20)	(13)
Net cash flows from investing activities		(41)	(468)
Cash flows from financing activities			
Repayment of other borrowings		-	(2)
Proceeds from subordinated liabilities		-	555
Interest paid on subordinated liabilities		(100)	(65)
Coupon payment on undated intercompany financial instrument	43	(6)	-
Increase in undated intercompany financial instrument	43	(245)	-
Net cash flows from financing activities		(351)	488
Net increase/(decrease) in cash and cash equivalents		1,269	78
Cash and cash equivalents at the beginning of the year	19	1,091	1,030
Effects of exchange rate changes on cash and cash equivalents		1	(17)
Cash and cash equivalents at the end of the year	19	2,361	1,091
Supplemental disclosures			
Included in operating activities are:			
Interest received		1,568	2,288
Dividend received		1,251	789
Rental income received on investment properties		338	432

* The acquisition of subsidiaries reflects the impact of domestication of the Canadian subsidiary. Refer to Note 42 Domestication of Canadian non-participating business.

The Company's operating portfolio of investment assets includes unit trusts and other investment funds that are classified for financial reporting purposes as subsidiaries. Cash flows in relation to these assets are classified as operating cash flows in the Company Cash Flow Statement.

Accounting policies

(a) Basis of preparation

The Group's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the International Accounting Standards Board (IASB) as endorsed by the European Commission (EC) for use in the European Union (EU). All relevant standards and interpretations have been endorsed by the EU. The IASB has published an amendment to IAS 19 *Employee Benefits* (2004) and amendments to IAS 39 *The Fair Value Option* (2005). These amendments are not mandatory until 2006 but the Group has chosen to adopt them early and they are reflected in the consolidated financial statements.

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and liabilities (including derivative instruments) at fair value through profit or loss (FVTPL), property and investment property. These are the Group's first consolidated financial statements under IFRS and IFRS 1 *First time Adoption of International Financial Reporting Standards* has been applied. The principal accounting policies set out below have been consistently applied to all financial reporting periods presented in these consolidated financial statements and by all Group entities, unless otherwise stated. Unless otherwise stated in the notes to these financial statements all amounts are expected to be settled/recovered after more than 12 months.

The Standard Life Assurance Company (the 'Company') has taken advantage of the exemption under Section 230 of the Companies Act 1985 from presenting its own Income Statement.

Comparatives

The Group has taken advantage of the exemption in IFRS 1, paragraph 36A, which allows certain comparative information presented in the first year of adoption of IFRS not to comply with IFRS 4 *Insurance Contracts*. The Accounting Standards Board (ASB) in the United Kingdom has issued Financial Reporting Standard 27 *Life Assurance* (FRS 27), which the Group has adopted from 1 January 2005.

Estimates

The preparation of financial statements, in conformity with generally accepted accounting principles (GAAP), requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Consistent with IFRS 1, any estimates included in the Group's opening IFRS Balance Sheet have been made by considering the information that existed at the time the estimate was made under previous GAAP, rather than information that became available after that date, after taking into account any applicable adjustments resulting from differences in accounting policies.

Change of the year-end reporting date

The Group changed its year-end reporting date during 2004 to 31 December 2004. The comparative period in these financial statements is therefore the period from 16 November 2003 to 31 December 2004.

Change in accounting policies during the period

In accordance with IFRS 4, the Group continues to apply the same accounting policies for the recognition and measurement of obligations arising from insurance contracts and investment contracts with discretionary participation features (DPF) that it used for the preparation of its published financial statements for the period ended 31 December 2004. The only exception is that the recognition and measurement requirements of FRS 27 have been adopted, as an improvement to the Group's accounting policies. The ASB issued FRS 27 on 13 December 2004 for mandatory application for accounting periods ending on or after 23 December 2005. As acknowledged within FRS 27 its retrospective application is difficult. The Group has assessed that it is impractical to restate the Balance Sheet at 16 November 2003 and the Income Statement for the period to 31 December 2004 for the impact of FRS 27. The Balance Sheet at 31 December 2004 has been restated. In accordance with FRS 27 participating contract liabilities are determined on a realistic basis and are reduced by the PVFP on non-participating contracts written in the with profits fund. DAC is only held on non-participating investment contracts to the extent of the DIR recognised. This has resulted in an increase in participating contract liabilities of £409m and a reduction in deferred acquisition costs of £1,788m at 31 December 2004. The participating contract liabilities are offset by the present value of future profits on non-participating contracts of £1,041m. The effect of these adjustments is to decrease deferred tax liabilities by £124m and deferred tax assets by £53m, offset by an increase to reinsurance assets of £6m. Corresponding amounts have been adjusted to the unallocated divisible surplus in accordance with FRS 27 resulting in a decrease of £1,079m at 31 December 2004 for Group. The impact for Company is a decrease to unallocated divisible surplus of £1,012m at 31 December 2004. FRS 27 requires insurance contracts to be classified into their participating and non-participating components and reflected as such on the Balance Sheet. A presentational adjustment has been made to reflect this classification for insurance and investment contracts.

Accounting policies (continued)

FRS 27 requires cost of guarantees to be valued on a fair value approach. FRS 27 permits the PVFP on the non-participating business written within the with profits fund to be deducted from the realistic liability as this value is included within the realistic liability calculation.

Standards, interpretations and amendments to published standards that are not yet effective

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2006 or later periods. The Group has not early adopted these standards, amendments, and interpretations as described below:

IAS 21 (Amendment), *The effects of changes in foreign exchange rates: Net investment in a foreign operation* (effective from 1 January 2006): The amendment alters the requirement for a monetary item that forms part of a reporting entity's net investment in a foreign operation to be denominated in the functional currency of either the reporting entity or the foreign operation. This will be applied by the Group from annual periods beginning 1 January 2006 and is not considered to have a material impact on the Group's results.

IAS 39 (Amendment), *Cash Flow Hedge Accounting of Forecast Intragroup Transactions* (effective from 1 January 2006): The amendment allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in the consolidated financial statements, provided certain conditions are met. The Group is not currently planning to take advantage of this amendment.

Amendment to IAS 39 and IFRS 4 – *Financial guarantee contracts*: The amendment clarifies whether financial guarantees fall within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* or IFRS 4 and stipulates the measurement method to be applied to such guarantees. The Group has not early adopted this amendment and therefore it will be applied from annual periods beginning 1 January 2006. The amendment is not considered to have an impact at Group level and Management is currently assessing the impact at company level.

IFRS 7 *Financial Instruments: Disclosures* and a complementary amendment to IAS 1 *Presentation of Financial Statement*: Revised guidance on implementing IFRS 4, *Presentation of Financial Statements – Capital Disclosures* (effective from 1 January 2007). IFRS 7 introduces new disclosures to the information on financial instruments and the revision to IFRS 4 reflects the changes made by IFRS 7 and affects the disclosure section of the guidance. The amendment to IAS 1 introduces disclosures on the level of management of capital resources. This will be applied by the Group from annual periods beginning 1 January 2007. The Standard has no financial impact but will change the disclosures surrounding the Group's Financial Instruments and Insurance Contracts.

Interpretations that are not relevant to the Group's operations: IFRIC 5 *Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*, IFRIC 4, *Determining whether an Arrangement contains a Lease* (all effective from 1 January 2006), IFRIC 7, *Applying Hyperinflationary economies for the first time* (effective 1 March 2006) and IFRIC 6, *Waste Electrical and Electronic Equipment* (effective 1 December 2005) are not relevant to the Group's operations.

Key judgements made in selecting accounting policies

In selecting accounting policies where IFRS permits a choice of policy, management have applied judgement in determining the most appropriate policy to be applied, as detailed below:

- **Designation of financial assets:**
Policy choice made on the basis of achieving the best matching with the associated liabilities.
- **Recognition of actuarial gains and losses on defined benefit plans:**
Policy choice made in order to minimise Income Statement volatility.
- **Unallocated divisible surplus:**
Policy choice made not to recognise any guaranteed element separately and thus record the full unallocated divisible surplus as a liability.
- **Cash Flow Statement:**
Indirect method chosen on the basis that it is simpler than the direct method and consistent with the approach adopted by our peers.
- **Deferred acquisition costs (DAC):**
Policy choice made to include DAC on non-profit contracts in the with profit fund implicitly in the present value of future results (PVFP) up to the extent of the deferred income reserve (DIR) on investment contracts (written in the with profit fund) on the basis of simplicity.

Accounting policies (continued)

- Exclude PVFP on insurance subsidiaries owned by the with profits fund:
Policy choice made on the basis of simplicity and relevance post demutualisation.
- Accounting for property:
Policy choice made on the basis of consistency with previous policy and in order to achieve the best matching with the associated liabilities.

In addition management has applied judgement in estimating balances in particular around the valuation of actuarial liabilities (refer Notes 20 and 22), the valuation of the defined benefit pension obligation (Note 26) and the valuation of unlisted securities.

(b) Basis of consolidation

The Group financial statements consolidate the Income Statements and Balance Sheets of the Company and its subsidiary undertakings. Associate and joint venture undertakings are accounted for using the equity method from the date that significant influence or joint control (respectively) commences until the date this ceases.

Investments in subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies. Such power, generally but not exclusively, accompanies a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group, through until the date that control ceases.

The Group uses the purchase method of accounting for the acquisition of subsidiaries. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

The Group has three categories of investment in subsidiaries: those that are deemed operating subsidiaries as they undertake the activities of the Group; those that raise finance for the Group's operating subsidiaries; and those that are investment companies as their primary function is to generate capital or income growth through holding investments. In the financial statements of the Company subsidiaries held for investment purposes are classified as FVTPL (as they are managed on a fair value basis). All other subsidiaries are accounted for at cost.

Any impairment on individual investments in subsidiaries held at cost is determined, at each reporting date, by an evaluation of the exposure on a case-by-case basis.

Impairment losses are calculated and recorded on an individual basis in a manner consistent with the impairment policy described in section (g) below.

The same approach is used for investments in associates and joint ventures.

Investments in associates and joint ventures

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

Where the Group has a significant holding in an investment vehicle that meets the definition of an associate or joint venture and that investment in associates backs policyholder liabilities including the unallocated divisible surplus, that investment is accounted for at fair value through profit and loss in accordance with IAS 39.

All other associates and joint ventures are equity accounted for and in this case, the Group's investment in associates and joint ventures includes goodwill (net of any impairment loss) identified on acquisition.

Investments in associates and joint ventures that are equity accounted for are initially recognised at cost and adjusted thereafter for the post-acquisition change in the Group's share of net assets of the associate. The Group's share of post-acquisition results of its associates is recognised in the Income Statement. The Group's share of any post-acquisition movements in reserves, where the associate recognised a gain or loss directly in equity, is recognised in unallocated divisible surplus. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment.

Where the Group's share of losses in an associate equals or exceeds its interest in an associate, including any other unsecured receivables, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations in connection with or made payments on behalf of an associate.

Accounting policies (continued)

(c) Classification of insurance and investment contracts

The measurement basis of assets and liabilities of long-term business contracts is dependent upon the classification of those contracts into either insurance or investment contracts depending upon whether significant insurance risk exists. For those investment contracts containing discretionary participating features (e.g. with profits business) IFRS 4 permits the continued application of previously applied GAAP, except where a change is deemed to make the financial statements more relevant to the economic decision-making needs of users and no less reliable, or more reliable, and no less relevant to those needs. The Group has chosen to apply this approach, which therefore includes the requirements of FRS 27 to its UK with profits fund.

Generally, product classes are sufficiently homogeneous to permit a single classification at the level of the product class. However, in some cases, a product class may contain individual contracts that fall across multiple classifications ('hybrid contracts'). For certain significant hybrid contracts the product class is separated into the insurance element, a non-participating investment element and a participating investment element so that each element is accounted for separately.

(d) Revenue Recognition

Deposit accounting for non-participating investment contracts

Contributions received in respect of investment contracts are treated as policyholder deposits and not reported in the Income Statement. Claims paid to policyholders are treated as a reduction to these deposits. The change in policyholder liabilities is reflected each period in the Income Statement.

Investment contracts not classified as unit linked are measured at amortised cost. Amortised cost is calculated as the fair value of policyholder contributions at the date of initial recognition, less the net effect of payments such as transaction costs and front-end fees, plus or minus the cumulative amortisation (using the effective interest rate (EIR) method) of any difference between that initial amount and the maturity value, and less any write-down for surrender payments. The EIR is the rate that equates the discounted cash payments to the initial amount.

All contractual initial fees and incremental transaction costs directly attributable to the issue of the contract are deemed to be attached to issuing the financial liability and are included within the EIR calculation.

Deposit accounting is also applied to reinsurance contracts that do not qualify as insurance contracts under section (c) above.

The fees and transaction costs associated with investment contracts are treated in accordance with the policy described below for investment income.

Premiums

Premium income on insurance contracts and participating investment contracts are recognised when due for payment.

General insurance premiums are accounted for when written. Premiums are recognised as earned income over the period of the policy having regard to the incidence of risk.

Investment income

Investment gains and losses resulting from changes in both market value and foreign exchange on investments classified as FVTPL are recognised in the Income Statement in the period in which they occur.

Changes in the fair value of derivative financial instruments that are not hedging instruments are recognised immediately in the Income Statement.

Realised gains and losses are calculated as the difference between net sales proceeds and the amount paid to acquire the investment, including the initial transaction costs. Unrealised gains/losses reflected in the Income Statement are calculated as the difference between the current valuation of investments and their valuation at the last Balance Sheet date or the amount paid to acquire them at subsequent acquisition during the period. Unrealised gains and losses are adjusted each period for gains and losses realised through sale.

For loans and receivables measured at amortised cost, interest income is calculated using the EIR method and is recognised in the Income Statement.

Dividend income is recognised when the right to receive payment is established.

Accounting policies (continued)

Rental income is recognised in the Income Statement on a straight-line basis over the term of the lease.

Fee and commission income

Commissions received or receivable, are recognised as revenue on the commencement or renewal date of the related policies. However, when it is probable the Group will be required to render further services during the life of the policy, the commission is deferred as a liability and is recognised as the services are provided.

Non-participating investment contracts and fund management business

All fees and costs are deemed to be associated with the provision of investment management services and are recognised, subject to recoverability, as the services are provided. Front-end fees, which are charged on the inception of investment management contracts, are deferred as a liability and recognised over the life of the contract. Ongoing fees that are charged periodically, either directly or by making a deduction from invested funds, are recognised as received, which corresponds to when the services are provided.

(e) Expense recognition

Claims and benefits paid

Life assurance

Maturity claims and annuities are accounted for when due for payment. Surrenders are accounted for when paid or, if earlier, on the date when the policy ceases to be included within the calculation of the insurance liability. Death claims and all other claims are accounted for when notified.

Claims payable include the direct costs of settlement. Reinsurance recoveries are accounted for in the same period as the related claim.

General insurance

Claims are accounted for when there is sufficient evidence of their existence and a reasonable assessment can be made of the monetary amount involved. Provision is made at the Balance Sheet date for the total expected cost of settlement of all claims incurred in respect of events up to that date, whether reported or not, together with related claims handling expenses, less amounts already paid.

(f) Foreign currency

Foreign currency transactions and fair values are translated using the exchange rates applying to the functional currency, prevailing at the dates of the transactions or at the date the fair value was determined with related foreign currency exchange gains or losses reflected in the Income Statement. Translation differences on non-monetary items such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as owner-occupied properties, are included in the fair value reserve in the unallocated divisible surplus. Refer to the paragraph on owner-occupied properties in section (h) below.

Group companies

The Income Statements of foreign subsidiaries and branches are translated into the presentation currency of the Group at average exchange rates for the year. Assets and liabilities of foreign subsidiaries and foreign branches are translated at the closing rate at the Balance Sheet date. On consolidation, exchange differences arising from the translation of the net investment in foreign subsidiaries, foreign branches, and of borrowings and other currency instruments designated as hedges of such investments, are taken to the unallocated divisible surplus.

(g) Impairment of non-financial assets

The carrying amounts of non-financial assets are reviewed at each Balance Sheet date to determine whether there is any indication of impairment. An impairment loss is recognised in the Income Statement for the amount by which the asset's carrying amount exceeds its recoverable amount.

The recoverable amount of an asset is the greater of its net selling price (fair value less costs to sell) and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit, or group of units, to which the asset belongs.

Accounting policies (continued)

(h) Property and equipment

Owner-occupied properties and properties under development are recognised initially at cost and subsequently at depreciated fair value. Properties are valued, at least annually, by external independent qualified valuers.

Movements in the fair value of owner-occupied properties and properties under development are taken to the revaluation reserve in the unallocated divisible surplus. Reductions below cost are reflected in the Income Statement.

Owner-occupied properties are depreciated on a straight-line basis over their estimated useful lives, generally between thirty and fifty years. The depreciable amount of an asset is determined by the difference between the fair value and the residual value. The residual value is the amount that would be received on disposal if the asset was already at the age and condition expected at the end of its useful life. Properties under development are not depreciated.

Computer equipment, motor vehicles and other property is capitalised at cost and depreciation is charged to the Income Statement, within administration expenses, on a straight-line basis, over their estimated useful lives of between two and four years.

(i) Investment property

Property held for long-term rental yields or investment gain that is not occupied by companies in the Group is classified as investment property.

Investment property is initially recognised at cost including any directly attributable transaction costs. Subsequently investment property is measured at fair value. Fair value is determined without any deduction for transaction costs that may be incurred on sale or other disposal, unless the property is under development with a view to resale. Gains or losses arising from changes in fair value are accounted for in the Income Statement.

Investment properties are valued, on the same basis as owner-occupied properties.

Property located on land that is held under an operating lease is classified as investment property as long as it is held for long-term rental yields and is not occupied by the companies in the Group. The initial cost of the property is the lower of the fair value of the property and the present value of the minimum lease payments.

Rental income from investment property is recognised in the Income Statement on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, and are also spread over the term of the lease.

(j) Income tax

Current tax

The current tax expense is based on the taxable results for the year, using tax rates enacted or substantially enacted at the Balance Sheet date, including any adjustments in respect of prior years.

Deferred tax

Deferred tax is provided in full, using the Balance Sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax assets are recognised to the extent that it is probable that future taxable results will be available against which the temporary differences can be utilised.

Temporary differences arising from investments in subsidiaries and associates give rise to deferred tax in the Company Balance Sheet only to the extent that it is probable that the temporary difference will reverse in the foreseeable future or the Company does not control the timing of the reversal of that difference.

Deferred tax is recognised in the Income Statement except when it relates to items recognised directly in the Statement of Recognised Income and Expense in which case it is credited or charged directly to the unallocated divisible surplus through the Statement of Recognised Income and Expenses.

Accounting policies (continued)

(k) Reinsurance assets

Reinsurance assets primarily include balances due from both insurance and reinsurance companies for ceded insurance liabilities. Amounts recoverable from reinsurers are estimated in a manner consistent with the assumptions used for ascertaining the underlying policy benefits, subject to the terms of the contract. Reinsurance assets that do not qualify as insurance contracts, under the classification requirements described in section (c) above, are classified as financial assets and measured in accordance with IAS 39 at FVTPL.

Amounts due from reinsurers in respect of claims incurred are separately recognised in 'Other debtors' and are accounted for on a basis consistent with loans and receivables. Refer to the accounting policy in section (m) below.

If a reinsurance asset is considered to be impaired, the carrying amount is reduced to the recoverable amount and the impairment loss is recognised in the Income Statement. The recoverable amount is determined as the carrying amount less any impairment losses. Impairment losses are determined using the process adopted for assessing the impairment of financial assets held at amortised cost on an individual basis. Refer to the accounting policy in section (m) below.

(l) Deferred acquisition costs (DAC)

Investment contracts

Incremental costs directly related to the cost of acquiring new business (i.e. commission) are deferred, to the extent that they are deemed recoverable from future charges. The recoverability test takes account of any front-end fees that have been deferred and the Present Value of Future Profits (PVFP) asset recognised on these contracts.

For those investment contracts written within the with profit fund of the Company and its branches, the Group has chosen not to recognise deferred acquisition costs separately from the associated PVFP asset except to the extent of any Deferred Income Reserve (DIR) on those contracts.

The DAC asset is amortised on a consistent basis with the DIR liability in line with the expected emergence of profits from the underlying product grouping. Refer to section (u) for the accounting policy on DIR.

Participating insurance and investment contracts (i.e. with profit contracts)

Acquisition costs are not capitalised in respect of participating contracts in line with realistic valuation requirements.

Non-participating insurance contracts

For those insurance contracts falling within the scope of the FSA realistic capital regime (i.e. written within the with profit fund of SLAC and all branches) the Group has chosen not to recognise deferred acquisition costs separately from the associated PVFP asset.

Implicit allowance is made for DAC with the Canadian Asset Liability Valuation Model (CALM) thus no explicit DAC asset has been included in the Balance Sheet for insurance written by the Canadian subsidiary in the Group financial statements.

(m) Loans and receivables

Deposits with credit institutions, mortgage assets and other financial asset balances, such as other debtors are classified as Loans and receivables.

Loans and receivables are measured on origination at fair value less directly attributable transaction costs. Subsequently, the asset is measured at amortised cost, using the EIR method, less any impairment losses.

Impairment on individual loans is determined, at each reporting date, by an evaluation of the exposure on a case-by-case basis. The impairment loss is calculated as the difference between the present value of future cash flows, discounted at the loan's original effective rate, and the loan's current carrying value. The amount of any impairment loss is recorded in the Income Statement.

If there is no evidence of impairment on an individual basis, a collective impairment review is undertaken whereby the assets are grouped together, on the basis of similar credit risk characteristics, in order to calculate a collective impairment loss. This process accounts for impairments existing at the Balance Sheet date that are not evident until a future date.

Accounting policies (continued)

(n) Intangible assets

Intangible assets, including internally developed software and software purchased from third parties, are recognised in the Balance Sheet if it is probable that the relevant future economic benefits attributable to the asset will flow to the Group and its cost can be measured reliably.

Internally developed software and software purchased from third parties are capitalised as intangible assets and amortised over their estimated useful life when they are either identified as separable (i.e. capable of being separated from the entity and sold, transferred, rented, or exchanged) or they arise from contractual or other legal rights, regardless of whether those rights are transferable or separable.

Intangible assets are carried at cost less accumulated amortisation and any accumulated impairment losses. Amortisation is charged to the Income Statement on a straight-line basis over the estimated useful lives of the relevant software. Impairment losses are calculated and recorded on an individual basis in a manner consistent with the impairment policy described in section (g) above.

(o) Investment securities and derivatives

Designation as fair value through profit or loss (FVTPL)

Financial assets and liabilities are designated at FVTPL where the asset or liability is part of a group of assets that are evaluated and managed on a fair value basis. The Group holds a portfolio of equities and debt securities that are managed and monitored, through quarterly investment reports, on a fair value basis so as to maximise returns for with profits policyholders. The Group uses derivative financial instruments including forwards, swaps, futures, and options for the purposes of matching contractual liabilities, reducing investment risks and for efficient portfolio management activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for speculative trading purposes.

All investment securities and derivatives are designated as FVTPL.

Fair value measurement

The Group recognises these assets at fair value on the trade date of the transaction. In the case of derivatives where no initial premium is paid or received the initial measurement value is nil. Directly attributable transaction costs are not included in the initial measurement value but are recognised in the Income Statement.

Fair values are based upon the current quoted bid price where an active market exists. Where a quoted price in an active market cannot be obtained an appropriate market consistent valuation technique (for example discounted cash flows and recent market transactions) is used to determine fair value. If a price/technique is not available to provide a reliable fair value the investment is carried at cost less a provision for impairment.

Designated as held to maturity (HTM)

The Group classifies certain government bonds, held for regulatory purposes, as held to maturity (HTM) financial assets. HTM financial assets are recognised as assets on the trade date and initially measured at fair value plus any directly attributable transaction costs incurred on recognition. At each subsequent reporting date, the Group measures the HTM investments at amortised cost, using the EIR method, less any impairment losses identified. Interest revenue on HTM financial assets is calculated on an EIR basis and is recognised in the Income Statement.

Hedge accounting

The Group has designated certain derivative positions as fair value hedging instruments where the derivative financial instrument hedges the changes in fair value of a recognised asset or liability, or an identified portion of such an asset or liability, that is attributable to particular risk and could affect the Income Statement. The change in fair values of both the hedging instruments and the underlying asset or liability are recognised in the Income Statement.

Where a derivative financial instrument is designated and qualifies as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probably forecasted transaction, the effective part of any gain or loss resulting from the change in fair value of the derivative financial instrument is recognised directly in the unallocated divisible surplus.

Accounting policies (continued)

Hedge accounting is discontinued in the event that the hedge relationship is ineffective, expires, matures or is terminated. The gain or loss relating to the ineffective portion is recognised immediately in the Income Statement. A hedge is ineffective if the change in the fair value/cash flows of the hedging instrument does not significantly offset the changes in the fair value/cash flows of the hedged item.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, the effectiveness of the hedging relationship.

Embedded derivatives

Options, guarantees and other derivatives embedded in a host contract are separated and recognised as a derivative unless they are considered closely related to the host contract, meet the definition of an insurance contract or if the host contract itself is measured at fair value with changes in fair value recognised in income.

(p) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, any highly liquid investments which have a maturity date within three months of the date of acquisition and bank overdrafts that are repayable on demand and form an integral part of the Group's cash management.

(q) Interest bearing loans and borrowings

Interest bearing loans and borrowings are recognised initially at fair value, less attributable transaction costs. Subsequent to initial recognition, interest bearing loans and borrowings are carried at amortised cost with any difference between the carrying value and redemption value being recognised in the Income Statement over the period of the borrowings on an EIR basis.

The interest arising from interest bearing loans and borrowings is classified on a basis consistent with the classification of the underlying debt, being that which supports the Group's operating activities.

(r) Subordinated liabilities and subordinated members' accounts

Subordinated liabilities and subordinated members' accounts are initially included in the Balance Sheet at the value of proceeds received net of issue expenses. The total finance costs are charged to the Income Statement over the relevant term of the instrument using the effective interest rate. The carrying amount of the debt is increased by the finance cost in respect of the reporting period and reduced by payments made in respect of the debt in the period.

(s) Leases

Leases, where a significant portion of the risks and rewards of ownership are retained by the lessor, are classified as operating leases. Payments made as lessees under operating leases (net of any incentives received from the lessor) are charged to the Income Statement on a straight-line basis over the period of the lease.

Lease income from operating leases is recognised in the Income Statement on a straight-line basis over the lease term. Initial direct costs incurred in arranging an operating lease are added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease income.

There are no material finance leases affecting the group as either lessor or lessee.

(t) Pension costs and other post retirement benefits

The Group operates a number of defined benefit and defined contribution plans, the assets of which are held in separate trustee-administered funds. The pension plans are funded by payments from employees and by the relevant Group companies, determined by periodic actuarial calculations.

For defined benefit plans the liability recognised in the Balance Sheet is the present value of the defined benefit obligation less the fair value of plan assets, together with adjustments for past service costs. Plan assets exclude any insurance contracts or non-transferable financial instruments issued by the Group. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method whereby estimated future cash outflows are discounted using interest rates of high quality corporate bonds denominated in the currency in which the benefits will be paid of similar term as the pension liability.

Accounting policies (continued)

Actuarial gains and losses are recognised in the Statement of Recognised Income and Expense in the period in which they occur.

For defined contribution plans, the Group pays contributions to publicly or privately administered pension insurance plans. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised in staff expenses when they are due.

(u) Deferred income reserve (DIR)

Front-end fees on financial instrument transactions (including bid-offer spread) are deferred as a liability and recognised over the period services are provided. The DIR liability is amortised on a basis consistent with the associated DAC asset. Refer to section (l) for the accounting policy on DAC.

(v) Insurance and investment contract liabilities

Participating insurance and investment contracts (with profit contracts)

Liabilities arising from with profits contracts are measured on an FSA realistic basis. Under this approach the value of liabilities is calculated as

- A with profits benefits reserve (WPBR); plus
- Future policy related liabilities (FPRL); plus
- The realistic current liabilities of the fund; less
- Projected non-participating policyholder benefits included in the FSA calculation.

The WPBR is primarily based on the retrospective calculation of accumulated asset shares, adjusted for future expected policyholder benefits and other outgoings. A market consistent stochastic valuation of the cost of options and guarantees is included in the calculation of the FPRL.

Non-participating insurance contracts

In accordance with Group policy for overseas subsidiaries, the method used to determine the insurance contract liabilities for the Canadian business (in the Group financial statements) is based on Canadian accounting and regulatory valuation principles (CALM). The Canadian regulations set the value of policy liabilities equal to the value of a set of supporting assets just sufficient with reinvestment and disinvestments to meet all policy liabilities when due. Generally, Canadian GAAP measures assets at cost or amortised cost, however, as the Group's policy is to measure investment securities at FVTPL an adjustment is made to the CALM liabilities to reflect the impact of the measurement change in the backing assets.

The insurance contract liabilities for conventional business are calculated using the gross premium method. In general terms, a gross premium valuation basis is one in which the premiums brought into account are the full amounts receivable under the contract. The method includes explicit estimates of premiums, expected claims, costs of maintaining contracts and future renewal expenses. Cash flows are discounted at the valuation rate of interest prescribed by the FSA.

The PVFP recognised on non-participating contracts is treated as part of the liability under participating contracts and presented separately on the face of the Balance Sheet. The PVFP is the estimated value of in force associated with non-participating business written in the with profits fund. It is calculated by considering discounted future expected cash flows arising from net business.

Non-participating investment contracts

Unit linked non-participating investment contracts are designated as FVTPL as they are implicitly managed on a fair value basis as their value is directly linked to the market value of the underlying portfolio of assets. The fair value of a unit linked liability is equal to the value of the (funded) units allocated to the contracts. The unit value is based on the bid value of the fund assets at the reporting date before expenses of selling or buying the underlying assets.

Liabilities for non-linked investment contracts are measured at amortised cost. Amortised cost is calculated as the fair value of premiums received at the date of initial recognition, less the net effect of principal payments such as transaction costs and front-end fees, plus or minus the cumulative amortisation (using the EIR method) of any difference between that initial amount and the maturity value, and less any write-down for surrender payments. At each reporting date, the amortised cost liability is determined as the value of future best estimate cash flows discounted at the EIR.

Accounting policies (continued)

Healthcare and general insurance

All healthcare and general insurance contracts are short-term contracts, generally of duration no longer than a year. Claims outstanding comprise provisions representing the estimated ultimate cost of settling, including claims notified but not settled by the Balance Sheet date ('outstanding claims'), and claims incurred as a result of events up to the Balance Sheet date not notified as at that date ('IBNR' claims).

A provision is made at the Balance Sheet date for the total expected cost of settlement of all claims incurred in respect of events up to that date, together with related claims handling expenses, less any amounts already paid. Unearned premiums represent that proportion of premiums received on in force contracts that relate to unexpired risks at the reporting date and are recognised as a liability.

Liability Adequacy Test

The Group applies a Liability Adequacy Test at each reporting date to ensure that the insurance liabilities are sufficient. This test is performed by comparing the carrying value of the liability and the discounted projections of future cash flows (including premiums, claims, expenses, investment return and other items), using best estimate assumptions.

If a deficiency is found in the liability (i.e. the carrying value amount of its insurance liabilities is less than the future expected cash flows) that deficiency is provided in full. The deficiency is recognised in the Income Statement by setting up a provision in the consolidated Balance Sheet.

(w) Unallocated divisible surplus (UDS)

The unallocated divisible surplus, which represents the excess of the assets held by the with profits fund over the liabilities under in force contracts calculated in accordance with the requirements of FRS 27, and other liabilities of the with profit fund is treated as part of the liability under participating contracts and presented separately on the face of the Balance Sheet.

(x) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. Segments have been separately identified after consideration of the various regulatory reporting regimes, the nature of the products sold, distribution channels, customer segments and management's view of the relative risks and rewards associated with each segment.

A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

All inter-segment transactions are priced on an arm's length basis under normal terms and conditions.

1. Segmental analysis

(a) Primary reporting format - Business segments

The Group is managed and organised into four reportable business segments:

Life & Pensions: offers a broad range of pensions, protection, savings and investment products to individual and corporate customers. Within these product classes are executive and group pension products, pooled pension funds and income protection products.

Healthcare & General Insurance: primarily provides insurance cover to customers for medical expenses, accident and sickness.

Investment Management: provides a range of investment products for individuals and institutional customers through a number of different investment vehicles such as mutual funds, limited partnerships and investment trusts. Asset classes offered via these vehicles include equities, bonds, cash and property. Segregated investment mandates are also provided to large investors. Investment management services are provided to other business segments.

Banking: offers a range of retail mortgage and deposit products via on-line and telephone operations.

On 1 January 2005 the Group established a shared service centre ('SSC') which is responsible for managing certain payroll functions and providing amenity services, human resource and IT support to the Group. These costs are allocated to the various business segments, the majority of which is included in the Life and Pension segment. Items for which there is no reasonable basis to allocate are included within the unallocated line in the segment note.

All inter-segment transactions are priced on an arm's length basis under normal commercial terms and conditions.

1. Segmental analysis (continued)

(i) Segmental Income Statement

12 months to 31 December 2005	Group					Total
	Life & Pensions	Healthcare & General Insurance	Investment Management	Banking	Elimination	
	2005 £m	2005 £m	2005 £m	2005 £m	2005 £m	2005 £m
Revenue from external customers						
Net earned premium	3,308	208	-	-	-	3,516
Net investment return	13,761	1	5	610	-	14,377
Income arising from associates and joint ventures	92	5	2	-	-	99
Other segment income	318	1	87	8	-	414
Total revenue from external customers	17,479	215	94	618	-	18,406
Inter-segment revenue	33	-	102	2	(137)	-
Total segment revenue	17,512	215	196	620	(137)	18,406
Expenses						
Segmental expenses	15,958	213	151	589	(129)	16,782
Finance costs	100	-	1	16	(8)	109
Total segment expenses	16,058	213	152	605	(137)	16,891
Segment result	1,454	2	44	15	-	1,515
Tax expense						531
Transfer to unallocated divisible surplus						901
Increase in net assets attributable to minority interest						83
						-
Other items included in the Income Statement are:						
Impairment losses recognised	9	-	-	1	-	10
Amortisation of intangible assets	3	-	-	4	-	7
Depreciation of property and equipment	17	-	-	-	-	17

(ii) Segmental Balance Sheet

At 31 December 2005	Group					Total
	Life & Pensions	Healthcare & General Insurance	Investment Management	Banking	Elimination	
	2005 £m	2005 £m	2005 £m	2005 £m	2005 £m	2005 £m
Assets						
Segment assets	105,490	111	188	11,812	(116)	117,485
Investments in associates and joint ventures	2,470	117	21	-	-	2,608
Total segment assets	107,960	228	209	11,812	(116)	120,093
Unallocated assets						167
Group assets						120,260
Minority interest	340	-	-	-	-	340
Liabilities						
Segment liabilities	106,894	234	216	11,820	(122)	119,042
Total segment liabilities and minority interest	107,234	234	216	11,820	(122)	119,382
Unallocated liabilities						878
Group liabilities and minority interest						120,260
Capital expenditure incurred during the year on:						
Intangible assets	20	-	-	4	-	24
Property and equipment	84	-	-	-	-	84
Deferred acquisition costs	42	27	1	-	-	70

1. Segmental analysis (continued)

(iii) Segmental Income Statement

13.5 months to 31 December 2004	Group					Total
	Life & Pensions	Healthcare & General Insurance	Investment Management	Banking	Elimination	
	2004 £m	2004 £m	2004 £m	2004 £m	2004 £m	2004 £m
Revenue from external customers						
Net earned premium	3,999	256	-	-	-	4,255
Net investment return	9,313	10	3	566	-	9,892
Income arising from associates and joint ventures	81	3	2	-	-	86
Other segment income	268	1	67	8	-	344
Total revenue from external customers	13,661	270	72	574	-	14,577
Inter-segment revenue	91	-	97	2	(190)	-
Total segment revenue	13,752	270	169	576	(190)	14,577
Expenses						
Segmental expenses	13,298	281	147	574	(174)	14,126
Finance costs	80	-	1	15	(16)	80
Total segment expenses	13,378	281	148	589	(190)	14,206
Segment result	374	(11)	21	(13)	-	371
Tax expense						353
Transfer from unallocated divisible surplus						(15)
Increase in net assets attributable to minority interest						33
						-
Other items included in the Income Statement are:						
Impairment losses recognised	62	-	-	-	-	62
Amortisation of intangible assets	1	-	-	5	-	6
Depreciation of property and equipment	33	1	1	-	-	35

(iv) Segmental Balance Sheet

At 31 December 2004	Group					Total
	Life & Pensions	Healthcare & General Insurance	Investment Management	Banking	Elimination	
	2004 £m	2004 £m	2004 £m	2004 £m	2004 £m	2004 £m
Assets						
Segment assets	88,765	192	142	11,303	(330)	100,072
Investments in associates and joint ventures	1,813	58	20	-	-	1,891
Total segment assets	90,578	250	162	11,303	(330)	101,963
Unallocated assets						51
Group assets						102,014
Minority interest	250	-	-	-	-	250
Liabilities						
Segment liabilities	89,838	255	169	11,310	(336)	101,236
Total segment liabilities and minority interest	90,088	255	169	11,310	(336)	101,486
Unallocated liabilities						528
Group liabilities and minority interest						102,014
Capital expenditure incurred during the year on:						
Intangible assets	14	-	-	3	-	17
Property and equipment	172	1	-	-	-	173
Deferred acquisition costs	641	44	1	-	-	686

1. Segmental analysis (continued)

(b) Secondary reporting format – Geographical segments

The geographical segments are the United Kingdom, Canada and International operations, which includes all other geographic regions.

Revenues are allocated based on the country in which the contracts are issued, or products are sold. Total assets and capital expenditure are allocated based on where the assets are located. There are no significant differences between the geographical locations of assets, operations and the associated external revenues.

	Segment revenue from external customers	Segment assets	Capital expenditure on intangible assets, property and equipment and deferred acquisition costs
	£m	£m	£m
At 31 December 2005			
United Kingdom	14,310	100,362	160
Canada	2,192	14,261	9
International	1,904	5,470	2
Unallocated items	-	167	7
Total	18,406	120,260	178
At 31 December 2004			
United Kingdom	11,261	86,528	544
Canada	1,976	11,626	67
International	1,340	3,809	265
Unallocated items	-	51	-
Total	14,577	102,014	876

2. Net investment return

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
(a) Financial instruments other than those at fair value through profit or loss		
Interest income		
Cash and cash equivalents	126	173
Loans and receivables	710	691
Held to maturity debt securities	9	11
Other	1	-
	846	875
Impairment losses (recognised)/reversed	(1)	2
	845	877
(b) Losses on foreign exchange	(6)	(26)
(c) Financial instruments at fair value through profit and loss		
Net unrealised gains/(losses)		
Equity securities	4,109	840
Debt securities	597	719
Derivative financial instruments	(45)	217
Other	-	(10)
	4,661	1,766
Net realised gains/(losses)		
Equity securities	4,756	4,071
Debt securities	2,643	2,194
Derivative financial instruments	(307)	(376)
Other	7	(5)
	7,099	5,884
(d) Investment property		
Rental income	587	600
Net unrealised gains	991	674
Net realised gains	200	117
	1,778	1,391
Total net investment return	14,377	9,892

Included within interest income is £1m (2004 : £1m) in respect of interest income accrued on impaired financial assets.

Included in net realised gains/(losses) on financial instruments at fair value through profit or loss are dividends on equity securities of £1,121m (2004 : £920m) and interest income on debt securities of £2,021m (2004 : £1,985m).

The Group holds certain derivatives to economically hedge part of its investment portfolio. The gains/(losses) of these derivatives have been included in the unrealised and realised gains/(losses) of the respective underlying assets.

3. Fee and commission income

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Fund management fee income on investment contracts at fair value	248	214
Fee income from third party funds under management	88	57
Reinsurance commission income	2	2
Other fee and commission income	22	23
Total fee and commission income	360	296

4. Other administration expenses

Notes	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Commission expenses	410	632
Interest expense on customer accounts related to banking activities and deposits by banks	205	242
Interest expense on debt securities issued and mortgage backed floating notes	324	260
Other interest expense	17	19
Staff costs and other employee related costs	545	624
Operating lease rentals	2	3
Other corporate expenses	29	8
Auditor's remuneration	17	5
Other administration expenses	490	491
Depreciation of property and equipment	13	17
Impairment losses on property and equipment	13	9
Reversal of impairment on property and equipment	13	(8)
Amortisation of intangible assets	8	7
	2,064	2,343
Acquisition costs deferred during the year	9	(70)
Amortisation of deferred acquisition costs	9	72
Impairment losses on deferred acquisition costs	9	-
Other*	-	239
Total other administration expenses	2,066	2,273

* Effective 31 December 2004 the Group domesticated a substantial portion of the Canadian business (Note 42). The impact of this was to reduce the deferred acquisition balance in Canada by £239m.

5. Staff costs and other employee related costs

Notes	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
The aggregate remuneration payable in respect of employees was:		
Wages and salaries	440	492
Social security costs	39	47
Other pension costs:		
Defined benefit scheme	26	63
Defined contribution scheme	26	3
Total staff costs and other employee related costs	545	624

	Group	
	12 months to 31 December 2005	13.5 months to 31 December 2004
The average number of staff employed by the Group during the year was:		
United Kingdom	8,324	10,032
Canada	2,352	2,265
International	644	932
Total average number of staff employed	11,320	13,229
Life and pensions	9,166	10,856
Healthcare and general insurance	671	776
Investment management	688	698
Banking	795	899
Total average number of staff employed	11,320	13,229

The information required to be disclosed under the Companies Act 1985 in respect of directors' remuneration is provided in the Report of the Remuneration Committee on pages 13 to 20.

6. Auditor's remuneration

	Notes	Group	
		12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Audit services			
Statutory audit		3.7	1.4
Audit related regulatory reporting		0.4	0.9
Other assurance services		10.8	1.8
Tax advisory services		2.2	1.3
Total auditor's remuneration	4	17.1	5.4

The auditors' remuneration in respect of statutory audit services for the Company was £2.1m (2004 : £0.6m).

Fees in respect of non-audit services performed in the UK were £12.5m (2004 : £3.0m), including £7.9m (2004 : £1.8m) in respect of the Strategic Review, preparation for the proposed demutualisation and the adoption of IFRS.

7. Tax expense

(a) Current year tax expense

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Current tax:		
United Kingdom	373	237
Canada and international	54	28
Adjustment to tax expense in respect of prior years	(1)	-
Total current tax	426	265
Deferred tax:		
Deferred tax expenses arising from the current period	105	88
Total deferred tax	105	88
Total tax expense	531	353

Unrecognised tax losses of previous years were used to reduce current and deferred tax expenses by £18m and £84m respectively (2004 : £29m).

(b) Tax expense taken to unallocated divisible surplus

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Deferred tax*	-	(76)
Aggregate tax effect of items credited directly to unallocated divisible surplus	-	(76)

* Includes the tax effect of adopting FRS 27 (refer Note 23).

7. Tax expense (continued)

(c) Reconciliation of tax expense

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Result before tax	1,515	371
Tax at 30%	455	111
Permanent differences	(72)	(36)
Different tax rates	(13)	(7)
Different tax base of mutual life assurance	270	203
Adjustment to tax expense in respect of prior years	(1)	-
Recognition of previously unrecognised tax credit	(102)	(29)
Deferred tax not recognised	(6)	94
Other	-	17
Total tax expense for the year	531	353

8. Intangible assets

Notes	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Beginning of period				
Cost	51	34	23	10
Accumulated amortisation and impairment	(24)	(18)	(3)	(2)
Opening net book amount	27	16	20	8
Additions	24	17	20	13
Amortisation charge	(7)	(6)	(4)	(1)
Closing net book amount	44	27	36	20
At 31 December				
Cost	75	51	43	23
Accumulated amortisation and impairment	(31)	(24)	(7)	(3)
Closing net book amount	44	27	36	20

Intangible assets relate to capitalised software development costs.

9. Deferred acquisition costs

	Notes	Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Beginning of period					
Cost		636	3,160	506	3,037
Accumulated amortisation and impairment		(367)	(1,160)	(296)	(1,093)
Opening net book amount		269	2,000	210	1,944
Exchange differences		6	(13)	-	(11)
Costs deferred	4	70	686	31	634
Impairment charge	4	-	(44)	-	(44)
Amortisation charge	4	(72)	(333)	(29)	(286)
Other*		17	(239)	-	(239)
FRS 27 adjustment	41	-	(1,788)	-	(1,788)
Closing net book amount		290	269	212	210
At 31 December					
Cost		692	636	537	506
Accumulated amortisation and impairment		(402)	(367)	(325)	(296)
Closing net book amount		290	269	212	210

Included in deferred acquisition costs above are costs deferred on investment contracts (known as deferred origination costs) amounting to £278m (2004 : £251m).

* Effective 31 December 2004 the Group domesticated a substantial portion of the Canadian business (Note 42). Following domestication the insurance liabilities were valued (in accordance with Group accounting policies) in accordance with CALM. An explicit deferred acquisition cost is not recognised under the CALM valuation basis. The impact of this was to reduce the deferred acquisition balance in Canada by £239m.

10. Investments in subsidiaries

	Company	
	2005 £m	2004 £m
Beginning of period	6,770	6,971
Fair value gains	2,135	637
Acquisition of controlling interest	17,994	1,199
Cessation of controlling interest or disposal of interest held	(1,574)	(2,732)
Impairment losses recognised	-	(27)
Other	(11)	722
At 31 December	25,314	6,770

Subsidiaries held at fair value amounted to £24,028m (2004 : £5,555m), those at cost amounted to £1,286m (2004 : £1,215m).

During 2005 the Company made changes to its investment mix that resulted in the transfer of £15,058m holdings in bonds and property to unit trusts. These unit trusts are accounted for as subsidiaries of the Company and included within 'acquisition of controlling interest' above. The remaining additions relate to further investment into subsidiaries. The 'cessation of controlling interest or disposal of interest held' relates primarily to disinvestment in subsidiaries.

In 2004 £722m of 'Other' related to the Canadian domestication (Note 42). The Company's investment in the Spanish subsidiary Prosperity was impaired by £27m in 2004 and subsequently disposed of in 2005.

The following are details of the Company's principal subsidiaries which are unlisted entities except where indicated:

Name of subsidiary	Country of incorporation or registration	% of interest held	Nature of business
The Standard Life Assurance Company of Canada	Canada	100	Life assurance
Standard Life Healthcare Limited	England	100	General insurance
Standard Life Investments Limited	Scotland	100	Investment management
Standard Life Bank Limited	Scotland	100	Banking
Standard Life Investment Funds Limited	Scotland	100	Life assurance
Standard Life Lifetime Mortgages Limited	Scotland	100	Mortgage finance
Standard Life Pension Funds Limited	Scotland	100	Life assurance
Standard Life Savings Limited	Scotland	100	Investment management
Standard Life European Private Equity Trust PLC* **	Scotland	51	Investment trust
Standard Life (Asia) Limited	Hong Kong	100	Life assurance
SL Finance PLC	England	100	Finance company
SL MACS PLC	England	100	Finance company
SL MACS (No. 2) PLC	England	100	Finance company
Standard Life Employee Services Limited	Scotland	100	Employee services

* Indicates listed entity.

** Indicates the entity has a different reporting date to the Group but has been consolidated consistently at 31 December.

In certain instances, the Group sponsors the formation of special purpose entities primarily for the purpose of securitisation of assets and for raising finance. The Group consolidates special purpose entities when the substance of the relationship is that it controls or has the power to control the entity. In assessing and determining if the Group controls such special purpose entities, judgement is made about the Group's exposure to the risks, benefits and the ability to control the operating and financial decisions of the entity.

11. Investments in associates and joint ventures

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Beginning of period	1,891	1,832	1,806	1,334
Income arising from associates and joint ventures	99	86	67	71
Net increase in investment vehicle holdings	648	61	294	329
Additions	48	-	40	-
Disposals	-	(54)	-	(54)
Dividends received	(90)	(63)	(72)	(48)
Other	12	29	2	(26)
At 31 December	2,608	1,891	1,937	1,606

Income arising from associates and joint ventures includes £90m (2004 : £69m) arising from associates accounted for at fair value through profit and loss in accordance with IAS 39.

Net increase in investment vehicle holdings relate to the purchase and sales of units in the Global Liquidity Funds. The majority of additions and disposals relate to the purchase and sale of non-principal associates and joint ventures.

(a) Investments in associates

The following are particulars of the Group's share of principal associates, all of which are held at fair value:

Name of associates	Country of incorporation or registration	% interest held	Year- end	Nature of business	Assets £m	Liabilities £m	Revenues £m	Profit / (Loss) £m
At 31 December 2005								
Standard Life Investments (Global Liquidity Funds) PLC	Ireland	44.0%	15 Nov*	OEIC	2,475	59	92	90
At 31 December 2004								
Standard Life Investments (Global Liquidity Funds) PLC	Ireland	42.0%	15 Nov*	OEIC	1801	35	71	69

* Indicates the entity has a different reporting date to the Group but has been accounted for consistently at 31 December.

The Group also owns certain investments where its holding exceeds 20% of the capital of the investees without being able to exercise significant influence over their financial and operating policies. Certain investments held by mutual funds, unit trusts and unit linked insurance funds are therefore not treated as associates and recorded within Investment Securities. Their operations are not significant in relation to the financial statements of the Group.

11. Investments in associates and joint ventures (continued)

(b) Investments in joint ventures

The following are particulars of the Group's principal joint ventures, all of which are unlisted:

Name of joint ventures	Country of incorporation or registration	% interest held	Current assets	Long term assets	Current liabilities	Long term liabilities	Income	Expenses
At 31 December 2005			£m	£m	£m	£m	£m	£m
Castan Waterfront Development Inc.*	Canada	50.0%	-	31	1	-	2	4
First Real Properties*	Canada	49.0%	5	48	7	14	15	5
HDFC Asset Management Company Limited**	India	49.9%	3	20	3	-	6	4
HDFC Standard Life Insurance Company Limited**	India	14.8%	2	37	2	31	-	2
Heng An Standard Life Insurance Company Limited	China	50.0%	-	65	1	18	9	10

Name of joint ventures	Country of incorporation or registration	% interest held	Current assets	Long term assets	Current liabilities	Long term liabilities	Income	Expenses
At 31 December 2004			£m	£m	£m	£m	£m	£m
Castan Waterfront Development Inc.*	Canada	50.0%	-	28	-	-	-	-
First Real Properties*	Canada	49.0%	7	34	5	14	6	6
HDFC Asset Management Company Limited**	India	49.9%	3	20	3	-	7	5
HDFC Standard Life Insurance Company Limited**	India	18.6%	3	24	2	21	-	-
Heng An Standard Life Insurance Company Limited	China	50.0%	1	50	-	9	9	8

* Owned by a subsidiary of the Company.

** The Company also has a 9.4% (2004 : 14.3%) interest in Housing Development Finance Corporation Limited ("HDFC Limited"). HDFC Limited owns 79.4% (2004 : 74.8%) and 50.1% (2004 : 50.1%) of HDFC Standard Life Insurance Company Limited and HDFC Asset Management Company Limited respectively. This gives the Group an effective interest in these entities of 22.2% (2004 : 25.5%) and 54.6% (2004 : 57.1%) respectively. The Company does not exercise significant influence over either of these joint ventures.

12. Investment property

	Notes	Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Beginning of period		8,779	7,094	6,005	5,248
Additions resulting from acquisitions		416	1,468	127	762
Additions resulting from subsequent expenditure		147	65	32	50
Transfers (to)/from property and equipment	13	209	(14)	188	-
Foreign exchange adjustment		54	(11)	14	(27)
Net unrealised gains/(losses)		953	680	(878)	608
Disposals		(622)	(517)	(1,069)	(642)
Other		(29)	14	(34)	6
At 31 December		9,907	8,779	4,385	6,005
The fair value of investment properties can be analysed as:					
Freehold		7,857	7,109	3,536	4,521
Long leasehold		1,976	1,608	780	1,426
Short leasehold		74	62	69	58
Fair value investment property		9,907	8,779	4,385	6,005

Investment property is stated at fair value. The properties in the UK, a sample of Canadian properties and certain properties in other regions were independently valued in accordance with the Royal Institution of Chartered Surveyors' guidelines on the basis of determining the open market value of such properties. All properties are revalued up to three months prior to the Balance Sheet date being 31 December.

The rental income arising from investment properties during the year amounted to £587m (2004 : £600m), which is included in net investment return. Direct operating expenses (included within other administration expenses) arising in respect of such properties during the year amounted to £125m (2004 : £124m).

13. Property and equipment

		Group			Company		
	Notes	Land and buildings £m	Equipment £m	Total £m	Land and buildings £m	Equipment £m	Total £m
Cost							
At 16 November 2003		481	228	709	406	219	625
Additions		157	16	173	142	15	157
Disposals		-	(52)	(52)	-	(51)	(51)
Transfers from investment property	12	14	-	14	-	-	-
Revaluations	23	16	-	16	16	-	16
Impairment losses recognised*	4	(18)	-	(18)	(11)	-	(11)
Foreign exchange adjustment		(1)	(2)	(3)	(1)	(3)	(4)
Transfer to Group subsidiary		-	-	-	(4)	(40)	(44)
Other		18	-	18	-	-	-
At 31 December 2004		667	190	857	548	140	688
Additions		75	9	84	42	1	43
Disposals		(11)	(7)	(18)	(11)	(129)	(140)
Transfers to investment property	12	(209)	-	(209)	(188)	-	(188)
Revaluations	23	11	-	11	7	-	7
Disposal of a subsidiary		-	(2)	(2)	-	-	-
Impairment losses recognised*	4	(1)	-	(1)	(5)	-	(5)
Foreign exchange adjustment		2	6	8	-	-	-
Other		33	-	33	17	-	17
At 31 December 2005		567	196	763	410	12	422
Accumulated depreciation							
At 16 November 2003		-	(175)	(175)	-	(172)	(172)
Depreciation charge for the year	4	-	(35)	(35)	-	(33)	(33)
Disposals		-	51	51	-	51	51
Foreign exchange adjustment		-	1	1	-	2	2
Transfer to Group subsidiary		-	-	-	-	37	37
At 31 December 2004		-	(158)	(158)	-	(115)	(115)
Depreciation charge for the year	4	-	(17)	(17)	-	(2)	(2)
Disposals		-	7	7	-	110	110
Acquisition of a subsidiary		-	1	1	-	-	-
Foreign exchange adjustment		-	(6)	(6)	-	-	-
At 31 December 2005		-	(173)	(173)	-	(7)	(7)
Carrying amount							
At 31 December 2004		667	32	699	548	25	573
At 31 December 2005		567	23	590	410	5	415

* Impairment losses recognised in the Income Statement were £1m (2004 : £18m). This arose due to reductions in the market value of a number of properties offset by the reversal of impairments on properties in the prior year.

Where the expected residual value of owner-occupied property is in line with the current fair value, no depreciation is charged.

Equipment primarily consists of computer equipment.

Land and Buildings consists of property occupied by the Group and property under development. The value of property under development at 31 December 2005 was £286m (£2004 : £394m).

The properties in the UK, a sample of Canadian properties and certain properties in other regions were independently valued in accordance with the Royal Institution of Chartered Surveyors' guidelines on the basis of determining the open market value of such properties. All properties are revalued up to three months prior to the Balance Sheet date being 31 December.

If the owner-occupied properties were measured using the cost model, the carrying values for Group and Company would be £284m (2004 : £287m) and £204m (2004 : £209m) respectively.

14. Tax assets and liabilities

	Notes	Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Current tax recoverable	18	12	8	2	2
Deferred tax assets		75	43	59	15
Total tax assets		87	51	61	17
Current tax liabilities		240	100	147	62
Deferred tax liabilities		559	428	399	381
Total tax liabilities		799	528	546	443

(a) Recognised deferred tax

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Deferred tax assets comprises:				
Actuarial liabilities	281	195	81	25
Losses carried forward	98	49	85	29
Realised losses on investments	-	10	-	2
Depreciable assets	22	21	8	11
Employee benefits	38	18	14	18
Tax acquisition expenses	93	96	48	61
Other	23	25	10	7
Gross deferred tax assets	555	414	246	153
Less: offset against deferred tax liabilities	(480)	(371)	(187)	(138)
Net deferred tax assets	75	43	59	15
Deferred tax liabilities comprises:				
Actuarial liabilities	-	63	-	63
Unrealised gains on investments	896	620	549	434
Deferred gains on realisation	90	47	16	-
Deferred acquisition costs	32	28	16	15
Other	21	41	5	7
Gross deferred tax liability	1,039	799	586	519
Less: offset against deferred tax assets	(480)	(371)	(187)	(138)
Net deferred tax liabilities	559	428	399	381
Movements in net deferred tax assets/(liabilities) comprise:				
Beginning of period	(385)	(365)	(366)	(364)
Transfer to Canadian subsidiary	-	-	-	12
Amounts (charged)/credited to net results	(105)	(88)	25	(57)
Amounts (charged)/credited to unallocated divisible surplus	-	76	(3)	50
Exchange differences	6	(8)	4	(7)
At 31 December	(484)	(385)	(340)	(366)

A deferred tax asset of £98m for the Group (2004 : £49m) and £85m for the Company (2004 : £29m) has been recognised in respect of the amount of losses of the German and Austrian branches and Canadian subsidiaries. Deferred tax assets are recognised in respect of tax losses carried forward to the extent that is probable that the losses will be capable of being offset against taxable profits in future periods. The value attributed to them takes into account the certainty or otherwise of their recoverability. Their recoverability is measured against anticipated taxable profits. The losses in Canada will expire between 2006 and 2015. The remaining losses do not have an expiry date. Current tax is expected to be settled/recovered within 12 months.

(b) Unrecognised deferred tax

Due to uncertainty regarding recoverability, deferred tax assets have not been recognised in respect of cumulative losses carried forward of £188m (2004 : £338m) for the Group and £167m (2004 : £318m) for the Company. These are losses of the Irish, German and Austrian branches of the Company, and in respect of the Overseas Life Assurance Business of the Company in the United Kingdom.

15. Loans and receivables

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Loans and receivables comprise:				
Loans secured by mortgages	12,301	11,831	540	634
Loans secured on policies	129	134	120	128
Other	67	207	51	176
Gross loans and receivables	12,497	12,172	711	938
Less: Allowance for impairment losses	(1)	(1)	-	-
Net loans and receivables*	12,496	12,171	711	938

* Group loans and receivables with variable interest rates and fixed interest rates are £7,637m and £4,852m respectively (2004 : £8,550m and £3,621m respectively). Company loans and receivables with variable interest rates and fixed interest rates are £606m and £105m respectively (2004 : £715m and £222m respectively).

Included in loans secured by mortgages are mortgages subject to securitisations of £4,968m (2004 : £3,945m).

The allowance for impairment losses on loans and receivables as at 31 December 2005 is unchanged from 2004 at £1m for Group and £nil for Company.

The amount of loans and receivables expected to be settled/recovered greater than twelve months is £11,617m (2004 : £10,779) and for the Company is £650m (2004 : £753m).

16. Derivative financial instruments

The Group's insurance business uses derivative financial instruments in order to match contractual liabilities, to reduce the risk from potential movements in foreign exchange rates, equity indices, property indices and interest rates, or to achieve efficient portfolio management.

The Group's banking business uses derivative financial instruments in order to match or reduce the risk from potential movements in foreign exchange rates, equity indices and interest rates inherent in the banking book or to reduce credit risk.

The contract amount is the notional principal. Amounts included in the Balance Sheet are the fair value assets and liabilities.

Additional disclosures are provided in the risk management note (Note 31).

	Group					
	Contract amount	2005 Fair value assets	Fair value liabilities	Contract amount	2004 Fair value assets	Fair value liabilities
	£m	£m	£m	£m	£m	£m
Cash flow hedges	1,368	10	5	-	-	-
Fair value hedges	4,357	24	98	-	-	-
Held for trading	19,401	213	138	14,597	230	358
Total derivative financial instruments	25,126	247	241	14,597	230	358

From 1 January 2005, the Group designated certain derivative financial instruments as cash flow hedges and fair value hedges.

	Company					
	Contract amount	2005 Fair value assets	Fair value liabilities	Contract amount	2004 Fair value assets	Fair value liabilities
	£m	£m	£m	£m	£m	£m
Total derivative financial instruments	13,135	158	120	8,457	196	136

With respect to the Company, all derivative financial instruments are classified as held for trading.

(a) Cash flow hedges

The Group designates as cash flow hedges those currency forwards and currency swaps used to reduce the exposure to variability in cash flows arising from the foreign exchange risk associated with foreign currency borrowings.

Cash flows in respect of these transactions are expected to occur at various dates between the Balance Sheet date and October 2008.

The Group also designates as cash flow hedges those interest rate swaps used to reduce the exposure to variability in cash flows arising from the interest rate risk associated with floating rate borrowings.

Cash flows in respect of these transactions are expected to occur at various dates between the Balance Sheet date and July 2010.

	Group			Company		
	Contract amount	2005 Fair value assets	Fair value liabilities	Contract amount	2005 Fair value assets	Fair value liabilities
	£m	£m	£m	£m	£m	£m
Foreign exchange derivatives:						
Forwards	918	10	1	-	-	-
Interest rate derivatives:						
Interest rate swaps	450	-	4	-	-	-
Total cash flow hedges	1,368	10	5	-	-	-

16. Derivative financial instruments (continued)

(b) Fair value hedges

The Group designates as portfolio fair value hedges those interest rate swaps used to hedge changes in the fair value of the Group's fixed rate mortgage book arising from interest rate risk.

The Group also designates as fair value hedges those currency swaps used to hedge changes in the fair value of foreign currency borrowings arising from exchange rate risk.

	Group			Company		
	Contract amount	Fair value assets	Fair value liabilities	Contract amount	Fair value assets	Fair value liabilities
	£m	£m	£m	£m	£m	£m
Foreign exchange derivatives:						
Cross currency swaps	2,079	21	83	-	-	-
Interest rate derivatives:						
Interest rate swaps	2,278	3	15	-	-	-
Total fair value hedges	4,357	24	98	-	-	-

At 31 December 2005, the fixed interest rates vary from 3.85% to 6.69%.

(c) Held for trading

Derivative financial instruments that are not accounted for as effective hedging instruments are classified as held for trading.

Held for trading includes derivative financial instruments that the Group holds as economic hedges of financial instruments that are measured at fair value. Held for trading also includes derivative financial instruments that the Group holds to match contractual liabilities that are measured at fair value or to achieve efficient portfolio management in respect of instruments measured at fair value.

	Group					
	Contract amount	Fair value assets	Fair value liabilities	Contract amount	Fair value assets	Fair value liabilities
	£m	£m	£m	£m	£m	£m
Equity derivatives:						
Equity swaps	4	-	-	4	-	1
Futures	2,796	5	35	1,395	5	22
Options	1,800	54	4	1,606	61	-
Interest rate derivatives:						
Interest rate swaps	7,982	41	28	3,471	8	15
Forward rate agreements	60	-	-	60	-	-
Futures	1,202	8	3	401	2	2
Options	541	35	-	555	28	-
Foreign exchange derivatives:						
Cross currency swaps	533	54	1	2,721	80	208
Forwards	4,025	16	53	3,895	46	101
Futures	28	-	-	-	-	-
Options	247	-	-	255	-	-
Other derivatives:						
Property index swaps	126	-	12	117	-	4
Property index forwards	49	-	2	117	-	5
Credit default swaps	8	-	-	-	-	-
Total derivative financial instruments held for trading	19,401	213	138	14,597	230	358

16. Derivative financial instruments (continued)

	Company					
	Contract amount £m	2005 Fair value assets £m	Fair value liabilities £m	Contract amount £m	2004 Fair value assets £m	Fair value liabilities £m
Equity derivatives:						
Futures	2,706	4	35	1,370	1	22
Options	1,559	8	-	1,489	43	-
Interest rate derivatives:						
Interest rate swaps	4,016	34	24	614	8	5
Futures	1,202	8	-	378	2	2
Options	541	35	-	555	28	-
Foreign exchange derivatives:						
Cross currency swaps	517	54	-	534	79	-
Forwards	2,164	15	47	3,028	35	99
Options	247	-	-	255	-	-
Other derivatives:						
Property index swaps	126	-	12	117	-	3
Property index forwards	49	-	2	117	-	5
Credit default swaps	8	-	-	-	-	-
Total derivative financial instruments held for trading	13,135	158	120	8,457	196	136

The amount of derivative fair value assets expected to be settled/recovered greater than twelve months is £201m (2004 : £131m) and for the Company £128m (2004 : £112m).

The amount of derivative fair value liabilities expected to be settled/recovered greater than twelve months is £145m (2004 : £255m) and for the Company £44m (2004 : £50m).

17. Investment securities

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Equity securities and interests in pooled investment funds:				
Listed	42,747	34,754	28,346	24,876
Unlisted	854	740	6,721	5,362
Equity securities and interests in pooled investment funds	43,601	35,494	35,067	30,238
Debt securities at fair value through profit and loss:				
Listed	37,366	32,596	21,555	30,472
Unlisted	6,386	4,834	434	364
Held to maturity debt securities:				
Listed	78	132	-	-
Debt securities	43,830	37,562	21,989	30,836
Total investment securities	87,431	73,056	57,056	61,074

Included in the equity securities and interests in pooled investment funds of the Company are amounts relating to investment contracts with Standard Life Investment Funds, which is a subsidiary of the Group.

The amount of debt securities expected to be settled greater than twelve months is £41,918m (2004 : £35,360m) and for the Company £21,211m (2004 : £29,446m).

18. Other debtors

	Notes	Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Insurance business:					
Amounts receivable on direct insurance business		108	120	28	35
Amounts receivable on reinsurance contracts		4	5	4	1
		112	125	32	36
Investment securities:					
Outstanding sales of investment securities		111	177	51	121
		111	177	51	121
Other:					
Current tax recoverable	14	12	8	2	2
Due from related parties		-	-	41	90
Prepayments		24	15	-	-
Accrued income		710	677	411	561
Other		373	390	170	229
		1,119	1,090	624	882
Total other debtors		1,342	1,392	707	1,039

The carrying amounts disclosed above reasonably approximate the fair values as at the year-end.

The amount of other debtors expected to be received greater than twelve months is £12m (2004 : £11m) and for the Company is £11m (2004 : £11m).

19. Cash and cash equivalents

		Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Cash at bank and in hand		320	177	147	26
Balance with central bank		7	7	-	-
Money at call and short notice		742	691	24	54
Demand and term deposits with original maturity of <3 months		1,808	1,068	1,470	959
Debt investments with original maturity of <3 months		1,574	897	788	176
Total cash and cash equivalents		4,451	2,840	2,429	1,215

	Notes	Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Cash and cash equivalents		4,451	2,840	2,429	1,215
Bank overdrafts	24	(105)	(144)	(68)	(124)
Total cash and cash equivalents for cash flow		4,346	2,696	2,361	1,091

Balances with the central bank includes mandatory reserve deposits of £7m (2004 : £7m) which are not available for use in the Group's day-to-day operations.

Cash in hand and balances with the central bank and mandatory reserve deposits are non-interest bearing. Money at call and short notice and deposits are subject to variable interest rates.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods

Insurance and investment contract liabilities include unitised, non unitised, conventional and annuity business. Unitised contracts are those where the contractual benefits are determined with reference to units allocated to the contract; non-unitised contracts consist primarily of bonds where the benefits are linked to chosen indices although no units are allocated; annuity contracts are those where regular payments are made depending on the survival of live(s) or for a certain period of time and all other contracts are classed as conventional business.

The following sections give details of these main classes of business:

1. (a) UK Insurance and investment contract liabilities - terms

This section describes the terms of the Life and Pensions business in the UK. It also gives details on significant options and guarantees that have the potential to increase the benefits paid to policyholders. Under some options and guarantees the benefits paid depend on the behaviour of financial variables such as interest rates and equity returns. The significant options and guarantees that are not valued at fair value are disclosed below.

Unitised pensions business

This class of business comprises single or regular premium contracts under which a percentage of the premium is used to allocate units in one or more internal linked funds, or on a participating basis. Most of this business is classified as investment contracts although there are some contracts that are classified as insurance, for example those with guaranteed minimum pensions. The major unitised pension products include Individual and Group Personal Pension business, Executive Pensions, Stakeholder, and Self Invested Personal Pensions.

Provision for additional death benefits may be provided by cancellation of units or through supplementary term assurance contracts.

The Company recovers costs out of policies invested in internal linked funds by a fund management charge. Under Stakeholder contracts, this fund management charge has a maximum limit.

The most significant options and guarantees under these contracts are the following:

- participating contracts where, subject to specified conditions, it is guaranteed either that the unit price will rise at an annual rate of at least 4% a year or that the unit price will not fall, and, that there will be no unit price adjustment (UPA) at specified retirement dates or death;
- certain participating Trustee Investment Plan policies where, subject to specified conditions and limits, it is guaranteed that there will be no UPA when units are encashed;
- single premium pension policies where a minimum pension is guaranteed. Under these contracts a minimum investment in the participating fund is stipulated at inception with any excess over this minimum being available for investment in internal linked funds. The total investment is available to meet the guaranteed pension.

At 31 December 2005 the value of those single premium pension policies with a guaranteed minimum pension is £662m, where £83m relates to non-participating policies and £579m relates to participating policies. This represents about 1.5% of the total UK pension business. These pensions are valued on the regulatory basis if non-participating and on the realistic basis if participating.

If the market moves in line with the adverse scenario II as shown in the Sensitivity Analysis, Note 22 (market value of equities -15%, change in property values -12.5%, change in yields on 15 year gilt fixed interest bonds of -17.5%) then the impact on the unallocated divisible surplus from these contracts and the corresponding assets is -£14m i.e. a reduction in surplus.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

Conventional pensions business

Conventional pension business comprises contracts where a minimum level of benefit is set at outset and applies at the date(s) specified in the policy, for example Pure Endowment contracts. Regular bonuses may be added to this initial minimum over the term of the policy and in addition, a final bonus may be paid. These contracts are classified as insurance contracts.

Guaranteed annuity options providing for payment of a minimum annuity, in lieu of a cash sum, are available under pure endowment contracts. Under some of these contracts the guarantee applies only at the maturity date.

Under other contracts, the option also applies for a specified period proceeding the maturity date in which case, the sum assured and bonuses are reduced by specified factors and different guaranteed annuity rates apply.

Unitised life business

Unitised life business comprises single or regular premium endowment and whole life contracts under which a percentage of the premium is used to allocate units in one or more internal linked funds or on a participating basis. Some of this business is classified as insurance contracts, for example Homeplan and With Profits Bonds. Others are classified as investment contracts, for example Capital Investment Bonds.

The most significant options and guarantees under these contracts are the following:

- participating contracts where, subject to specified conditions, it is guaranteed on death and maturity either that the unit price will rise at an annual rate of at least 3% a year or that the unit price will not fall, and, that there will be no unit price adjustment (UPA) at maturity;
- for participating bonds it is guaranteed that no UPA will apply on regular withdrawals up to certain specified limits.

The death benefit under regular premium contracts is the greater of the bid value of units allocated and sum assured under the contract. Some contracts also contain critical illness cover providing for payment of a critical illness sum assured on diagnosis of certain defined serious illnesses. Under single premium contracts, the death benefit equals 101% or 100.1% of the bid value of units depending on the type of contract and when it is taken out.

Under contracts effected in connection with house purchase the death benefit is guaranteed. Under other contracts, at any time after the first ten years, the Company may review the status of the contract and, if it deems it necessary, reduce the sum assured within the limits permitted.

Under some contracts effected in connection with house purchase, provided the original contract is still in force the following options can normally be exercised at any time before the 55th birthday of the life assured:

- Future insurability option under which a new contract can be effected on then current premium rates, in connection with a further loan, up to the level of life and basic critical illness cover available on the original contract, without any further evidence of health;
- Term extension option on then current premium rates under which the term of the contract may be extended by an integral number of years if the lender agrees.

Non unitised life business

The non unitised business largely comprises single premium policies where the maturity value is linked to increases in the FTSE 100 Index subject to minimum maturity values established when the policies commenced. These bonds are classified as investment contracts.

The potential value of the minimum maturity values has been determined at amortised cost.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

Conventional life business

Conventional business consists of single or regular premium endowment, whole life and term assurance contracts where guaranteed benefits are payable on death and under some products on permanent and total disability or on diagnosis of a critical illness. These contracts are classified as insurance contracts. Under participating contracts, regular bonuses may be added to the guaranteed sum assured over the term of the policy and in addition, a final bonus may be paid on death and maturity. Certain endowment assurances have minimum surrender value provisions and minimum paid-up values.

Annuities

This class of business consists of single premium contracts that provide guaranteed annuity payments and are classified as insurance contracts. The payments depend on the survival of a life or lives with or without a guaranteed period and may reduce on a specified death or increase each year at a predefined rate or in line with the increase in the UK Retail Price Index (RPI).

For those annuities which increase at a predefined rate the total liability at 31 December 2005 is £3,485m and this represents about 30% of the total UK annuity business. These are valued on the regulatory basis with allowance for the predefined rate of increase.

If the market moves in line with the adverse Scenario II as shown in the Sensitivity Analysis, Note 22, (market value of equities -15%, change in property values -12.5%, change in yields on 15 year gilt fixed interest bonds of -17.5%) then the impact on the unallocated divisible surplus from those annuities with a predefined rate of increase and the corresponding assets is £15m i.e. an increase in surplus.

There is a subset of annuities where the RPI linked annuity payment cannot fall or is guaranteed to increase at a minimum rate; the majority of such annuities are those whose payment cannot fall.

The total liability at 31 December 2005 for RPI linked annuities (including any guaranteed minimum rate of escalation) is £1,994m and this represent about 17% of the total UK annuity business. These are valued on the regulatory basis with allowance for a positive rate of RPI escalation (greater than 0%).

The RPI annuities are backed by index linked securities and so if the market moves in line with the adverse scenario II as shown in the Sensitivity Analysis, then the impact on the unallocated divisible surplus from these annuities is not significant.

However if the rate of RPI increase is -1% for a year then for most RPI linked annuities the payment would not fall and in these circumstances there would be an additional cost of approximately £1m. If the rate of RPI increase continued negatively over a longer period then the cost would increase significantly.

For some participating deferred annuity policies, at maturity the annuity income can be converted to cash on guaranteed minimum terms.

The Participating Pension annuity is an annuity contract under which changes to the level of annuity are based on a rate of return declared by the Company but reductions in the level of the annuity are limited.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

1. (b) UK Insurance and investment contract liabilities – methods

Calculation of liabilities

The FSA's realistic reporting regime seeks to place a realistic and market consistent value on both assets and liabilities for participating insurance and investment contracts. In particular, the liabilities reflect discretionary benefits such as future bonuses as well as both the intrinsic value and the time value of options and guarantees and allow for possible future management actions. The assets include the value inherent in the existing in force policies.

The realistic liabilities are based on the aggregate value of individual policy asset shares that reflect the actual premium, expense and charge history of each policy. For example the investment return credited to the asset shares is consistent with the return achieved on the assets backing participating business; any mortality deductions are based on published mortality tables; for those asset shares on an expense basis the allowance attributed to the asset share is as far as practical the appropriate share of the actual expenses; for those on a charges basis the allowance is consistent with that for an equivalent unit linked policy.

Other components of the realistic liability reflect policy related liabilities such as policy guarantees, options and future bonuses, which are calculated using a stochastic model that simulates future investment returns, asset mix and bonus strategies. In these financial statements these liabilities also reflect the present value of future profits on non-participating insurance and investment contracts written in the participating fund.

The liabilities for non-participating conventional insurance contracts are calculated using the gross premium method. The method brings into account full premiums receivable under the contracts, estimated renewal and maintenance costs and contractually guaranteed benefits.

The liabilities for annuity contracts are calculated by discounting the expected future annuity payments together with an appropriate estimate of future expenses at an assumed rate of interest derived from the yields on the underlying assets. The liabilities include allowances for changes to maximum pension limits due to expected changes in the UK pension regulations (A-day).

For contracts with guaranteed insurability options, the calculated liabilities have been subjected to minimum values on a contract-by-contract basis that exceed those required on the assumption that the options are foregone by those experiencing the select mortality of newly underwritten lives. For Lifetime Protection Series term assurance business, the liabilities include an allowance for whichever options the policyholder has exercised.

For unithised non-participating insurance contracts and investment contracts the liability is based on the value of the underlying assets supporting the contracts. For non unithised non-participating investment contracts, the liability is measured at amortised cost using the effective interest method. The effective interest rate is that which discounts estimated future cash flows through the expected life of the liability. The estimation of cash flows incorporates all contractual terms relating to the instrument.

Participating contracts allocations

Regular bonuses are declared at the discretion of the Board in accordance with the Company's Regulations and are set at levels, which aim to achieve a gradual build-up in guaranteed participating policy benefits whilst not unduly constraining investment freedom and the prospects for final bonuses. In setting these rates, the financial position (both current and projected) of the Company is taken into account. Were it necessary, regular bonus rates would be set to zero. Regular bonus rates are set for each relevant class of participating policy and/or internal fund and reflect its characteristics, including any guaranteed rates.

For some contracts final bonuses may also be paid. These bonuses are not guaranteed and can be withdrawn at any time.

The Board is not required by Standard Life's Regulations to pay out, use, transfer or allocate any part of the available (or expected) surplus. The Board is entitled to decide that the whole or any part of the available (or expected) surplus be left in the fund.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

Participating contracts payouts

The Company's aim is that, subject to meeting all contractual obligations and maintaining adequate financial strength, payouts on a participating policy (including any final bonus applying) should fairly reflect the experience of the Company applicable to such a policy, after any adjustments for smoothing.

When setting payout levels, the Company seeks to ensure fair treatment between those participating policyholders who choose to withdraw and those who remain.

Asset shares are used as a tool to determine fair treatment. The calculation of asset shares varies between products, for example calculations can be on the basis of representative policies or on an individual policy basis. The calculation of asset shares is described in more detail in the Company's *Principles & Practices of Financial Management (PPFM)*.

The methodology and parameters used in payout calculations may, of necessity, involve some measure of approximation. The Company reviews regularly the methodology and parameters used and sets parameters on bases appropriate for the participating class and/or internal fund concerned.

In normal circumstances the Company seeks to offer some smoothing of investment returns to participating policyholders at the time of claims due to maturity for life policies or for pension policies where the Company has no right to reduce benefits as defined in the relevant contractual terms and conditions. The Company may, at its discretion, also provide some smoothing of investment returns for death claims and some types of withdrawal at the time of payment. The Company aims to operate smoothing of investment returns in such a way as to be neutral for participating policyholders as a whole over time. The Board monitors the anticipated cost of smoothing on a regular basis and, in some circumstances, it may be appropriate to reflect the costs in asset shares and/or adjust the approach to smoothing.

When calculating asset shares, the Company may at its discretion make fair deductions to reflect its assessment of the cost of guarantees. In April 2004 the Company announced that it would take an allowance for the assessed costs of guarantees when determining final bonuses payable on claims, calculating policy switch values and calculating surrender and transfer values. These allowances vary between types of policies, reflecting the nature of the guarantees provided. This was in line with the intention to reflect the costs of guarantees, should they become significant, in the returns credited to participating policies. In the past, these costs had been relatively insignificant and had been met from the fund's capital. These allowances are kept under review.

If the Board considers it necessary then fair deductions may be taken from the asset shares of participating policies in order to maintain the inherited estate at a size appropriate for existing and future financial and business conditions and obligations.

It has been the Company's practice to enhance payouts through the addition of discretionary amounts, known as benefits of mutuality. This practice was reviewed during 2004 and as a result it was announced that these discretionary payments would be reduced and that it was expected that these would be phased out over the two years from October 2004. Phasing out these payments will help protect the financial position of the Company and balance the interests of all of the Company's policyholders.

In assessing the affordability of payouts and, in particular, the degree to which the Company should make discretionary adjustments to them (including but not limited to smoothing), the Board will look at the financial position of the Company. The Board will take into account the existence of any regulatory capital issued by the Company, its terms and conditions and the degree to which such regulatory capital is intended to be subordinated to the Company's obligations to policyholders (including the requirement to treat customers fairly).

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

Mortgage endowment policies

The Company announced in September 2000 that, subject to certain conditions being satisfied, it would top up the payouts at maturity on certain policies where there is a shortfall between the claim value and the mortgage amount originally targeted. One condition is that there is sufficient growth in the capital of the Company for it to set aside regular provisions to meet possible top up payments. The provisions held by the Company at 15 November 2003 were £393m.

During 2004 the Company concluded that the capital growth condition required for the promise had not been met, and a detailed review of the Company's financial position concluded that it would be in the best interests of the Company, taking into account the interests of all its participating policyholders, not to make further provision unless and until the capital growth condition was actually met. Therefore no further provision was made for 2004.

An assessment of the appropriateness of the provision continues to be conducted annually. During 2005 the Company again concluded that the capital growth condition had not been met and therefore no further provision has been made for 2005. It is the Company's intention that the provisions already held will be used to provide top up payments to affected policyholders, as long as this is considered fair and prudent.

Appropriate provision has been made for potential compensation payments due to policyholders arising from the Company's review of past sales of mortgage endowment policies.

The incidence and magnitude of payments will be influenced by the requirements of the FSA and by the actions of industry bodies and policyholders. It is therefore not possible to estimate with certainty the final costs which will arise.

1. (c) UK Insurance and investment contract liabilities – assumptions

Most guarantees on participating contracts and future bonuses are valued prospectively using a stochastic model, which generates future investment returns. Within the projections, allowance is made for future bonus reflecting projected investment conditions and the Company's PPFM. For guarantees on participating contracts not valued using the stochastic model, the liability is calculated by applying the ratio of guarantee costs to the asset share for the product most similar in nature with appropriate adjustments.

The economic assumptions for the calculation of the present value of future profits on non-participating insurance and investment contracts are shown in the table below:

	2005	2004
Risk Discount Rate	6.72%-7.07%	7.35%
Investment returns		
Equities	4.22%	7.10%
Property	4.22%	7.10%
Fixed Interest – Gilts	4.19%-4.22%	4.55%-4.59%
Fixed Interest – Corporate	4.22%-4.87%	5.17%-5.35%
Expense Inflation	3.83%	3.80%
RPI	2.85%	2.80%

The table above shows the changes in the basis between 2005 and 2004. The 2005 risk discount rate is calculated on a market consistent basis and is set equal to the risk free rate plus a margin to allow for the non market risks inherent in the cash flows being discounted.

The investment returns for 2005 are the risk free rate of return that are used to value the non-participating business on a market consistent basis.

The non-economic assumptions include expenses, mortality and withdrawals.

The expense and mortality assumptions are best estimate assumptions determined from the Company's recent analyses. They are consistent with the assumptions for non-participating insurance contracts with the explicit margins for prudence removed.

A withdrawal investigation is carried out each year and assumptions are set with reference to recent levels taking into account any trends evident. However, in general the results for participating business are not particularly sensitive to the overall level of withdrawals. For non-participating business, appropriate allowances are made for withdrawals only where this would lead to an increase in the insurance and investment contract liabilities.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

For non-participating insurance contracts, the assumptions used to determine the liabilities are updated at each reporting date to reflect the latest experience. Material judgement is required in calculating these liabilities and, in particular, in the choice of assumptions about which there is uncertainty over future experience. These assumptions are determined as appropriate estimates at the date of valuation. The basis is considered prudent in each aspect. In particular, options and guarantees have been provided for on prudent bases and no credit is taken for possible beneficial effects on liabilities of voluntary withdrawals.

The principal assumptions for the main UK non-participating insurance contracts are as follows:

Valuation interest rates

The valuation interest rates used are determined in accordance with the FSA Integrated Prudential Sourcebook.

The process used to determine the valuation interest rates used in the calculation of the liabilities comprises three stages: determining the current yield on the assets held after allowing for risk and tax, hypothecating the assets to various types of policy and determining the discount rates from the hypothecated assets.

For equity assets, the current earnings and dividends are considered and, if necessary, a deduction is made to reflect sustainability. Similarly, a deduction to the yields on property assets is made where necessary, to allow for the possibility of rental defaults. For corporate bonds, a deduction is made for the risk of default. The yield for each category of asset is taken as the average adjusted yield weighted by the market value of each asset in that category.

The valuation interest rates used are:

Non-participating	2005	2004
1. Assurances		
Pensions	3.75%	4.25%
Other	3.00%	3.25%
2. Annuities		
Individual/Group		
- life	4.00%	4.25%
- pension	4.50%	4.90%
- linked to RPI	1.30%	1.70%

Mortality rates

The future mortality assumptions are based on historical experience with an allowance for future mortality improvement in annuities. The Company's own mortality experience is regularly assessed and analysed, and the larger industry-wide investigations are also taken into account.

Mortality tables used	2005	2004
1. Assurances	AM92 ult - 3.5 years	AM92 ult - 4 years
2. Annuities		
Individual and group in deferment	AM92 ult - 3.5 years	AM92 ult - 4 years
Individual after vesting	103% IMA 92 M04 / 105% IFA 92 M04	73% IMA92 C10 ult / 89% IFA92 C10 ult
Group after vesting	104% PMA 92 M04 / 123% PFA 92 M04	80% PMA92 C10 ult / 91% PFA92 C10 ult

A significant assumption is the rate at which future mortality is expected to improve for annuitants. The mortality improvement factors assumed for the males are in line with the projection basis underlying the above tables published by the CMI with a minimum improvement of 1.5% per annum. The improvement factors assumed for females also reflect the projection basis underlying the above tables published by the CMI but to a lesser extent and with a different underpin.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

Expenses

The assumptions for future policy expense levels are determined from the Company's recent expense analyses. No allowance has been made for potential expense improvement, and the costs of projects to improve expense efficiency have been ignored. The assumed future expense levels incorporate an annual inflation rate allowance of 3.83% for UK business derived from the expected Retail Price Index (RPI) implied by current investment yields and an additional allowance for earnings inflation.

For non-participating immediate and deferred annuity contracts, an expense loading is made in respect of renewal expenses, an explicit allowance is made for termination expenses and an implicit allowance is made for fund management expenses, by reducing the valuation rate used.

For conventional non-participating insurance contracts, an explicit allowance for renewal, and termination expenses is included in the liabilities. An allowance for investment expenses is reflected in the valuation rate of interest.

In calculating the liabilities for unitised life contracts, the administration expenses are assumed to be identical to the expense charges made against each policy. Similar assumptions are made, where applicable, in respect of mortality, morbidity and the risk benefit charges made to meet such costs.

2. (a) Canadian business - terms

Annuities

These contracts are similar to those issued in the UK and provide a guaranteed annuity payment based on the survival of a life or for a specified period. The majority of the portfolio are life contingent annuities and are classified as life insurance. However there are some term certain annuities classified as investment contracts. Most of the annuity portfolio is written on a non-participating basis. The benefits may increase each year at a pre-defined rate or in line with increases in the Canadian Consumer Price Index (CPI) and will not decrease in periods of deflation.

For those annuities which increase at a predefined rate the total liability at 31 December 2005 is £389m and these represent about 11% of the total Canadian annuity business. The liability for annuities linked to CPI-index is approximately £265m. This represents about 7% of the total Canadian annuity business.

The annuity liabilities, including these guarantees, are valued using the Canadian Asset Liability Method (CALM). The value held is the maximum of various economic scenarios including changes in the interest rate environment and inflation rates. For CPI-linked annuities, a 1% increase in the RPI would increase liabilities by £7m. However, inflation risk on these annuities is managed with assets linked to inflation.

Universal Life insurance

The main Universal Life product written by the Company is named Perspecta and is a non-participating life insurance product. Perspecta are whole life assurance contracts, under which premiums may be invested on both an index linked and non-linked basis. Premiums invested on a non-linked basis are placed on deposit at rates of interest guaranteed for periods from 1 day to 20 years. The rate offered is determined with reference to the financial conditions at the time of premium payment. The contract provides life cover, and in addition, on death the value of the index linked funds is guaranteed never to be less than 75% of premiums deposited into those funds, adjusted for expense charges and any withdrawals. The liability for these policies is £425m at 31 December 2005.

Perspecta contracts issued up to November 2003 provided the following interest rate guarantees:

- 0% for the Daily Interest Fund.
- For each term investment fund (TIF), the greater of 90% of the Government of Canada Bond rate for the same term, less 1.75%, and:
- 0% for the 1-year TIF
 - 1% for the 3-year TIF
 - 2% for the 5-year TIF
 - 3% for the 10, 15 and 20-year TIF.

Furthermore, it was guaranteed that at least one TIF at a minimum guaranteed interest rate of 3% would be offered as long as the policy is in force.

Perspecta contracts issued after November 2003 provide lower interest rate guarantees for terms of at least 3 years, there is no guarantee that a term with a 3% minimum guaranteed rate will be offered and the TIF investment option can be withdrawn.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

In addition, on all Perspecta policies the value of the investment account may increase on guaranteed terms at specified policy anniversaries. The level of increase depends upon various conditions, including when the contract was effected.

Perspecta policyholders have the option to switch into TIFs some or all of their investments in the other investment options and can increase their premiums up to statutory limits. The guarantees that then apply are those set when the contract was effected.

These options and guarantees are valued using the Canadian regulatory basis. Under this basis, the actuarial liabilities provide for the sensitivity of the liabilities to changes in the interest rate environment by scenario testing. A reduction of 0.50% in the yields curve would increase the value of the guarantee to £24m. At 31 December 2005, the liability for all the TIFs (i.e. pre and post November 2003) is £59m.

Accumulation contracts

This category comprises savings products that are classified as non-participating investment contracts. The major individual product is Ideal Solution for Savings and the major group product is SLX. Deposits can be invested on a non-linked basis at guaranteed interest rate for a given period. New market conditions apply if the plan renews after maturity.

Also included in this category are unit linked products sold on an individual or group basis. The individual product is non-participating and offers a death benefit guarantee of the greater of the fund value and 100% of the net deposits.

Provided that the monies have been invested for a minimum of 10 years, the maturity benefit is the greater of the fund value and 75% of deposits at the annuity commencement date less any cash values previously paid out. Otherwise the maturity benefit is the fund value. The cost of the guarantee has been calculated in accordance with local regulations and results in no provision being required.

The group version of this product differs in that it does not offer a guarantee upon death or maturity.

Registered Retirement Income Fund (RRIF) and Life Income Fund (LIF) products

RRIF and LIF products are non-participating investment account contracts into which single premiums are invested on a linked or non-linked basis. Non-linked premiums are placed on deposit at rates of interest guaranteed for a selected term. The rate offered depends on financial conditions at the time of deposit. Proceeds at the end of a guarantee period may be reinvested at the then current rates. Regular withdrawals are made from the account to provide an income during retirement. The policyholder may vary the amounts withdrawn subject to the regulatory minimum. The unit linked version offers guarantees on death and maturity similar to the individual product described above.

Conventional life business

Conventional business consists of participating or non-participating single or regular premium endowment, whole life and term assurance contracts where the guaranteed benefit is payable on death. Participating whole life and endowment assurance contracts contain scales of minimum guaranteed surrender values and paid-up policy amounts. Participating whole of life contracts issued prior to 1985 include a guaranteed annuity rate option where the lump sum death benefit can be converted into an annuity on guaranteed terms or retained by the Company whereupon the value accumulates at an annual interest rate of at least 2.5%. For some participating whole life policies it is guaranteed that the interest on policy loans will not exceed 6%. There are some participating policies where it is guaranteed that the annual interest rate credited will be at least 4%.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

2. (b) Canadian business - methods

The liabilities for participating insurance contracts are calculated on a realistic basis consistent with the methodology and assumptions used to calculate liabilities for the UK participating business.

The liabilities in respect of non-participating business are determined in accordance with methods prescribed by Canadian regulations, adjusted where appropriate to comply with UK accounting principles.

Under Canadian regulations, liabilities are determined according to the Canadian Asset Liability Method (CALM). The Company's assets and liabilities are projected under a number of different economic scenarios. These scenarios include the current yield curve as at the valuation date and a number of various rising and falling interest rate environments. Under each scenario the assets required to support the liabilities are the value of assets which will achieve zero surplus at the end of the projection period. The liability is set equal to greatest value across all scenarios of the required assets.

2. (c) Canadian business - assumptions

The Canadian economic environment at 31 December 2005 is used to determine the expected interest rates for the current valuation. The expected experience scenario of risk free rates is derived from the yield curve of Canadian federal bonds at that date, as summarised below:

Yield curve – by duration	2005	2004
6 months	3.65%	2.54%
1 year	3.91%	2.69%
2 years	3.81%	3.00%
3 years	3.84%	3.20%
5 years	3.89%	3.68%
7 years	3.92%	4.00%
10 years	3.94%	4.31%
20 years	4.07%	4.74%
30 years	4.02%	4.85%

The following table shows the other key investment returns used in the asset and liability projections under CALM:

Investment returns	2005	2004
Equities	7.00%	7.04%
Property	6.91%	6.91%

These investment returns are net of investment expenses and are prudent assumptions as they include risk margins determined in line with Canadian standards of practice. A further drop in the asset values of 30% for equities and 25% for property is applied to allow for adverse deviations in projecting cash flows for non-fixed income assets.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

Mortality assumptions have a significant impact on the liabilities and are shown below:

Mortality tables used	2005	2004
1. Assurances		
Perspecta Universal Life and Term Life	65%-120% of base table (where base table is 71%-83% of CIA 86-92)	65%-120% of base table (where base table is 75%-85% of CIA 86-92)
Participating and non-participating Life, closed to new business	69%-83% of CIA 86-92	65%-85% of CIA 86-92
2. Annuities		
Individual - after vesting	86%-88% of IAM83M / IAM83F with projection scale AA	87%-92% of IAM83M / IAM83F with projection scale AA
Group - after vesting	75%-124% of GAM83M / GAM83F with projection scale AA	77%-124% of GAM83M / GAM83F with projection scale AA

Mortality assumptions are derived from studies performed during 2004 and 2005 using a blend of industry and Company experience. The rates are expressed as a percentage per the tables shown. For assurance business the percentages vary depending on the underwriting classification and the duration of the contracts. For annuity business the percentages vary depending on whether the contract is in payout or in deferment, and on the gender of the annuitant.

Margins for adverse deviation are added and vary depending on the nature of the products and the strength of the underwriting criteria. These margins are consistent with Canadian actuarial standards of practice for use in local regulatory reporting.

3. European Business - terms, methods and assumptions

Republic of Ireland

The contracts issued in the Republic of Ireland have features similar to those in the UK. The contracts issued are mainly participating business. The options and guarantees are also similar to those in the UK, including guaranteed sums assured on some conventional life business, no unit price adjustments (UPA) at maturity or on regular withdrawals on some unitised participating contracts and guaranteed annuity options on some pension business.

The liabilities are calculated using a methodology and basis consistent with the UK approach but using assumptions appropriate to the market.

The value of options and guarantees on the Irish business are measured using a methodology consistent with the UK. However, the basis used is calibrated for the Irish market.

Germany

The contracts issued in Germany mainly consist of unitised participating endowment assurances and deferred annuities, under which a percentage of each premium is applied to purchase units in the German With Profits Fund. Certain unit prices in the German With Profits Fund are guaranteed not to decrease. The death benefit under endowment assurances is the greater of the sum assured on death or 105% of the current surrender value. The death benefit under deferred annuities is the greater of the sum assured on death, 100% of the current surrender value and, for regular premium paying contracts and certain single premium contracts, a refund of premiums.

Provided all premiums have been received to date, the maturity value, and for certain contracts the surrender benefits, are subject to guaranteed minimum amounts. For some participating unitised policies it is guaranteed that there will be no UPA on claims on or after the surrender option date. Some of these policies guarantee that the premium required for a given level of benefit will not exceed a specified amount. Deferred annuities have a guaranteed annuity at the Selected Benefit Date and the annuity start date. In addition certain contracts are subject to guaranteed annuity amounts.

The liabilities are calculated using a methodology basis consistent with the UK approach but using assumptions appropriate to the markets.

The value of options and guarantees on the German business are measured using a methodology consistent with the UK. However, the basis used is calibrated for the German market.

20. Insurance contract liabilities, investment contract liabilities and reinsurance assets – terms, assumptions and methods (continued)

4. Healthcare business - terms, methods and assumptions

The contracts issued by Standard Life Healthcare mainly consist of individual and corporate private medical insurance products that include a range of benefit options. All contracts are written on an annual renewal basis and accordingly are accounted for on an annual premium income basis. A provision for unearned premiums is calculated on a daily basis as the most accurate method for calculating the proportion of premium accounted for in periods up to the accounting date that is attributable to subsequent periods.

Claims incurred comprise claims paid in the year and changes in the provision for outstanding claims, whether reported or not, together with any other adjustment to claims from previous years.

Outstanding claims comprise provisions for the claims incurred up to, but not paid at, the Balance Sheet date, whether reported or not.

Commission payable is deferred on the same basis as unearned premiums.

5. Reinsurance – terms, methods and assumptions

The Group limits its exposure to loss within insurance operations through participation in reinsurance arrangements. The majority of the business ceded is placed on a quota-share basis with retention limits varying by product line and territory. Amounts recoverable from reinsurers are estimated in a manner consistent with the methods and assumptions used for ascertaining the underlying policy benefits and are presented in the Balance Sheet as reinsurance assets.

Even though the Group may have reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to reinsurance ceded, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements.

The Group is not dependent on a single reinsurer nor are the operations of the Group substantially dependent upon any reinsurance contract.

21. Insurance contract liabilities, non-participating investment contract liabilities, participating investment contract liabilities and reinsurance assets

Participating insurance contract liabilities primarily includes conventional life and pension products and unitised life (With Profit Bonds and Homeplan).

Non-participating insurance contract liabilities consist primarily of conventional term assurances (Lifetime Protection Series or LPS), life contingent annuities, Perspecta universal life in Canada, and a small amount of linked Homeplan business.

Participating investment contract liabilities include unitised pension products, both individual and group, including Self invested Personal Pension (SIPP).

Non-participating investment contract liabilities consist primarily of unit linked business, including Investment Bonds (Capital Investment Bonds), non-linked bonds including Canadian Ideal Solution for Savings and SLX, and term certain annuities.

- (a) The movement during the year in insurance contract liabilities, participating investment contract liabilities and reinsurance assets is as follows:

	Group					Net 2005
	Participating insurance contract liabilities	Non-participating insurance contract liabilities	Participating investment contract liabilities	Total insurance and participating contracts	Reinsurers share of liabilities (reinsurance asset)	
	£m	£m	£m	£m	£m	£m
At 1 January 2005	18,264	18,854	15,929	53,047	(617)	52,430
Expected change	(430)	(275)	(161)	(866)	(62)	(928)
Methodology/modelling changes	202	(46)	(71)	85	22	107
Effect of changes in:						
Economic assumptions	336	679	336	1,351	(12)	1,339
Non-economic assumptions	(95)	186	(66)	25	(46)	(21)
Effect of:						
Economic experience	1,131	342	931	2,404	(28)	2,376
Non-economic experience	205	(62)	1,062	1,205	29	1,234
New business	30	781	152	963	(15)	948
Total change in insurance contract liabilities	1,379	1,605	2,183	5,167	(112)	5,055
Foreign exchange adjustment	(10)	699	(36)	653	(50)	603
At 31 December 2005	19,633	21,158	18,076	58,867	(779)	58,088

	Company					Net 2005
	Participating insurance contract liabilities	Non-participating insurance contract liabilities	Participating investment contract liabilities	Total insurance and participating contracts	Reinsurers share of liabilities (reinsurance asset)	
	£m	£m	£m	£m	£m	£m
At 1 January 2005	18,264	14,761	15,929	48,954	(978)	47,976
Expected change	(430)	(130)	(161)	(721)	(60)	(781)
Methodology/modelling changes	202	(90)	(71)	41	22	63
Effect of changes in:						
Economic assumptions	336	627	336	1,299	(12)	1,287
Non-economic assumptions	(95)	238	(66)	77	(46)	31
Effect of:						
Economic experience	1,131	243	931	2,305	(28)	2,277
Non-economic experience	205	(62)	1,062	1,205	31	1,236
New business	30	308	152	490	(15)	475
Total change in insurance contract liabilities	1,379	1,134	2,183	4,696	(108)	4,588
Foreign exchange adjustment	(10)	39	(36)	(7)	(18)	(25)
At 31 December 2005	19,633	15,934	18,076	53,643	(1,104)	52,539

21. Insurance contract liabilities, non-participating investment contract liabilities, participating investment contract liabilities and reinsurance assets (continued)

Economic assumptions reflect changes in fixed income yields, leading to lower valuation rates on non-participating business, and other market movements. Experience changes in 2005 primarily represent higher than expected investment returns, increasing the participating liabilities.

Non-economic assumptions cover mortality, persistency and expenses. Experience changes in 2005 primarily represent lower than expected claims (including deaths, surrenders, maturities and lapses).

Changes in methodology and models include refinement of the realistic liability models, including enhanced modelling of the cost of guarantees for Germany.

(b) Change in the present value of future results on non-participating contracts:

	Group	Company
	2005	2005
	£m	£m
At 1 January 2005	1,041	1,041
Expected change, including unwind of discount	(25)	(25)
Methodology/modelling changes	303	303
Effect of changes in economic and non-economic assumptions	(122)	(122)
Effect of economic and non-economic experience	88	88
New business	244	244
Foreign exchange adjustment	(1)	(1)
At 31 December 2005	1,528	1,528

(c) Change in non-participating investment contract liabilities:

	Group	Company
	Non-participating investment contract liabilities	Non-participating investment contract liabilities
	£m	£m
At 1 January 2005	30,597	25,055
Contributions	6,952	5,893
Initial charges and reduced allocations	(7)	(7)
Account balances paid on surrender and other terminations in the year	(3,407)	(2,518)
Investment return credited and related benefits	5,996	5,380
Foreign exchange adjustment	913	21
Other	71	97
Recurring management charges	(186)	(186)
At 31 December 2005	40,929	33,735

Refer to Note 31 – Risk Management policies for an indication of the term to contracted maturity/repricing date for insurance and investment contract liabilities. Reinsurance contracts are generally structured to match liabilities on a class of business basis. This has a mixture of terms. The reinsurance assets are therefore broadly expected to be realised in line with the settlement of liabilities (as per the terms of the particular treaty) within a reinsured class of business.

22. Impact of assumption changes on unallocated divisible surplus

The unallocated divisible surplus and the value of corresponding assets and liabilities depend on a number of key assumptions and any variation in these assumptions could significantly change the unallocated divisible surplus – this is illustrated in the tables in this section.

The subordinated debt and the subordinated members' accounts are valued in these statements on an amortised cost basis and so are independent of assumptions. The value of these will vary with exchange rates.

Changes in assumptions which impact insurance and investment contract liabilities could impact the unallocated divisible surplus. Whether and how much of an impact each change has depends on the methodology and key assumptions of the liability.

For participating business, the liability calculated on a realistic basis consists primarily of the inherent value in the policy (for example, the asset share), and the assets supporting it, which are not impacted by changes to non-economic assumptions such as mortality, lapses and expenses. However, other components of the realistic liability, such as policy guarantees, options and future bonuses, are impacted by changes in these assumptions.

Four key assumptions in the calculation of non-participating insurance contract liabilities are mortality, interest rates, expenses and lapse/withdrawal rates.

Mortality

For non-participating business the main insurance risk results from changes in mortality. The risk depends on the assumptions made and the type of contract involved. The mortality rates are based on published mortality tables, adjusted to reflect actual, and expected future, experience. If mortality rates were assumed to be lower this would lead to an increase in the insurance contract liability for annuities and a decrease in that for assurance.

Valuation interest rates

For non-participating business the valuation interest rates used to discount liabilities are determined in accordance with the FSA Integrated Prudential Sourcebook. The valuation interest rates are determined with reference to market rates and so changes in the market rates will impact the value of both assets and liabilities.

Expenses

For non-participating business the current level of expenses adjusted for inflation is taken as the appropriate expense base. An increase in the level of expenses would result in fewer assets being available to meet obligations and so would reduce the unallocated surplus.

Withdrawal and lapse rates

For non-participating business, although lapses and withdrawals prior to the original contract end date do impact on the timing of our cash flows, the value placed on non-participating liabilities is mostly independent of these considerations. This is because the values represent the greater of the prospective reserve or the surrender value (withdrawal value).

For participating policies (both insurance and investment contracts) the realistic value includes an explicit assumption for lapses and withdrawals. Our Principles and Practices of Financial Management (PPFM) state that when setting payouts the Company will seek to ensure fair treatment between those participating policyholders who choose to withdraw and those who remain, so changes in volumes of withdrawals do not necessarily impact on our available capital.

The table below demonstrates the effect of change in key assumptions, including market movement, on the unallocated divisible surplus whilst other assumptions remain unchanged. Only first order effects are shown.

22. Impact of assumption changes on unallocated divisible surplus (continued)

The market movement scenarios affect the value of both assets and liabilities, whereas the other movements only impact the liabilities. The change in the liabilities allowing for Scenario I is £305m and under Scenario II is (£156m).

Sensitivity analysis – Insurance Contracts	Change in assumption %	2005	
		Impact on unallocated divisible surplus £m	Impact on unallocated divisible surplus £m
		Group	Company
Insurance contracts (direct written and reinsurance accepted):			
Market movement (see note below)	Scenario I	352	352
	Scenario II	(293)	(293)
Expense assumptions	+ 10%	(95)	(84)
	- 10%	87	76
Morbidity/mortality assumptions	+ 10%	280	282
	- 10%	(345)	(344)
Withdrawal and lapse rate assumptions	+ 10%	19	3
	- 10%	(27)	(11)
Reinsurance contracts (ceded):			
Market movement (see note below)	Scenario I	(8)	(8)
	Scenario II	9	9
Expense assumptions	+ 10%	1	2
	- 10%	(1)	(2)
Morbidity/mortality assumptions	+ 10%	24	91
	- 10%	(17)	(91)
Withdrawal and lapse rate assumptions	+ 10%	4	-
	- 10%	(4)	-
Net insurance contracts:			
Market movement (see note below)	Scenario I	343	343
	Scenario II	(283)	(283)
Expense assumptions	+ 10%	(91)	(81)
	- 10%	83	73
Morbidity/mortality assumptions	+ 10%	438	373
	- 10%	(508)	(434)
Withdrawal and lapse rate assumptions	+ 10%	15	3
	- 10%	(23)	(11)
<hr/>			
Sensitivity analysis – Investment Contracts	Change in assumption %	2005	
		Impact on unallocated divisible surplus £m	Impact on unallocated divisible surplus £m
		Group	Company
Participating investment contracts:			
Market movement (see note below)	Scenario I	205	205
	Scenario II	(291)	(291)
Expense assumptions	+ 10%	(45)	(45)
	- 10%	45	45
Morbidity/mortality assumptions	+ 10%	-	-
	- 10%	-	-
Withdrawal and lapse rate assumptions	+ 10%	(4)	(4)
	- 10%	5	5
Non-participating investment contracts:			
Market movement (see note below)	Scenario I	(10)	(10)
	Scenario II	11	11
Expense assumptions	+ 10%	-	-
	- 10%	-	-
Morbidity/mortality assumptions	+ 10%	-	-
	- 10%	-	-
Withdrawal and lapse rate assumptions	+ 10%	-	-
	- 10%	-	-

22. Impact of assumption changes on unallocated divisible surplus (continued)

Market movement note

Since unallocated divisible surplus is impacted by economic conditions, two scenarios are considered reflecting the movement in the underlying asset values in the analysis. Scenario I allows for the combined impact of three components – a change in market value of equities of +15%, a change in property values of +12.5% and a change in yields on 15-year gilt fixed interest bonds of +17.5% and scenario II allows for the negative combination of these changes. These changes do not impact the various valuation interest rates to the same extent but can be broadly translated to an +/- 0.75% change in valuation interest rates where applicable. It has also been assumed that the valuation interest rates have moved in line with the movements in asset values.

This movement is similar in nature to the risk capital margin calculation required by the FSA. This calculation allows for certain management actions and for consistency, allowance for these actions, is also included in this analysis.

In calculating the above figures the following main management actions have been assumed for participating business:

- Regular bonuses are modelled dynamically, where the decision algorithm allows for the projected affordability of the bonuses in the portfolio and takes into account policyholders' reasonable expectations with respect to movements in the regular bonus rates over time.
- Investment mixes are dynamically controlled within the model. Fixed interest assets are assumed to be held broadly reflecting the nature of the underlying liabilities. Exposure to equities and property is gradually reduced as adverse scenarios unfold.
- Additional payments from the capital set aside under the Mortgage Endowment Promise may cease under certain adverse conditions, with payment only being resumed once the capital growth condition under the Promise had been met.
- The size of the deduction for guarantees taken from asset shares currently varies depending on the business being valued. However under stressed conditions it is assumed that an additional uniform deduction would be applied to all relevant contracts subject to certain limitations to reflect the loss arising under such conditions.

It should be noted that these sensitivities are non-linear and larger or smaller impacts should not be derived from these results. Also it should be noted that the sensitivity analysis represents a snap shot of the impact that the changes in assumptions can have.

The sensitivity analysis does not take into account the fact that the assets and liabilities are actively managed and may vary at the time that any actual market movement occurs. Other limitations in the above analysis include the use of hypothetical market movements to demonstrate potential risk.

23. Movement in components of unallocated divisible surplus, net assets attributable to unit holders and minority interest

Group	Notes	Revaluation of land and buildings	Cash flow hedges	Foreign currency translation	Remaining components	UDS* before Income Statement recognition	Total income/ (expense) recognised in the Income Statement	UDS*	Net assets attributable to unit holders	Minority interest	Total
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
2005											
Beginning of period		16	-	(89)	3,751	3,678	-	3,678	77	250	4,005
Fair value losses on cash flow hedges	16	-	(4)	-	-	(4)	-	(4)	-	-	(4)
Actuarial gains on defined benefit pension schemes	26	-	-	-	22	22	-	22	-	-	22
Revaluation of land and buildings	13	11	-	-	-	11	-	11	-	-	11
Exchange differences on translating foreign operations		-	-	218	-	218	-	218	10	(3)	225
Aggregate tax effect of items not recognised in the Income Statement	14	-	-	-	-	-	-	-	-	-	-
Other		-	-	-	1	1	-	1	-	-	1
Income/(expense) not recognised in the Income Statement during the period		11	(4)	218	23	248	-	248	10	(3)	255
Change in liability for third party interest in consolidated funds		-	-	-	-	-	-	-	43	-	43
Increase in net assets attributable to minority interest		-	-	-	-	-	-	-	83	-	83
Transfer to unallocated divisible surplus		-	-	-	-	-	901	901	-	-	901
Net contributions during the year		-	-	-	-	-	-	-	246	24	270
Contributions to subsidiary holdings		-	-	-	-	-	-	-	-	33	33
Distributions from subsidiary holdings		-	-	-	-	-	-	-	(3)	(47)	(50)
Transfer to associate status		-	-	-	-	-	-	-	(15)	-	(15)
At 31 December 2005		27	(4)	129	3,774	3,926	901	4,827	358	340	5,525

* Unallocated divisible surplus.

23. Movement in components of unallocated divisible surplus, net assets attributable to unit holders and minority interest (continued)

Group	Notes	Revaluation of land and buildings	Cash flow hedges	Foreign currency translation	Remaining components	UDS* before Income Statement recognition	Total income/ (expense) recognised in the Income Statement	UDS*	Net assets attributable to unit holders	Minority interest	Total
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
2004											
Beginning of period		-	5	-	4,887	4,892	-	4,892	50	139	5,081
Fair value losses on cash flow hedges transferred to the Income Statement	16	-	(5)	-	-	(5)	-	(5)	-	-	(5)
Actuarial losses on defined benefit pension schemes	26	-	-	-	(42)	(42)	-	(42)	-	-	(42)
Revaluation of land and buildings	13	16	-	-	-	16	-	16	-	-	16
Exchange differences on translating foreign operations	-	-	-	(93)	-	(93)	-	(93)	(2)	2	(93)
Aggregate tax effect of items not recognised in the Income Statement	14	-	-	-	4	4	-	4	-	-	4
Income/(expense) not recognised in the Income Statement during the period		16	(5)	(93)	(38)	(120)	-	(120)	(2)	2	(120)
Change in liability for third party interest in consolidated funds	-	-	-	-	-	-	-	-	16	-	16
Increase in net assets attributable to minority interest	-	-	-	-	-	-	-	-	-	33	33
Transfer (from) unallocated divisible surplus	-	-	-	-	-	-	(15)	(15)	-	-	(15)
Transfer to subsidiary status	-	-	-	-	-	-	-	-	-	50	50
Contributions to subsidiary holdings	-	-	-	-	-	-	-	-	-	32	32
Distributions from subsidiary holdings	-	-	-	-	-	-	-	-	-	(6)	(6)
Transfer on consolidation of Unit Trusts	-	-	-	-	-	-	-	-	13	-	13
Adoption of FRS 27	41	-	-	-	(1,155)	(1,151)	-	(1,151)	-	-	(1,151)
Tax effect of adoption of FRS 27	14,41	-	-	4	72	72	-	72	-	-	72
At 31 December 2004		16	-	(89)	3,766	3,693	(15)	3,678	77	250	4,005

* Unallocated divisible surplus.

23. Movement in components of unallocated divisible surplus, net assets attributable to unit holders and minority interest (continued)

Company	Notes	Revaluation of land and buildings	Cash flow hedges	Foreign currency translation	Remaining components	UDS* before Income Statement recognition	Total income/ (expense) recognised in the Income Statement	UDS*
		£m	£m	£m	£m	£m	£m	£m
2005		16	-	(46)	3,760	3,730	-	3,730
Beginning of period								
Actuarial gains on defined benefit pension schemes	26	-	-	-	45	45	-	45
Revaluation of land and buildings	13	7	-	-	-	7	-	7
Exchange differences on translating foreign operations		-	-	29	-	29	-	29
Aggregate tax effect on items not recognised in the Income Statement	14	-	-	-	(3)	(3)	-	(3)
Other		-	-	-	3	3	-	3
Income/(expense) not recognised in the Income Statement during the period		7	-	29	45	81	-	81
Transfer to unallocated divisible surplus		-	-	-	-	-	786	786
At 31 December 2005		23	-	(17)	3,805	3,811	786	4,597

* Unallocated divisible surplus.

23. Movement in components of unallocated divisible surplus, net assets attributable to unit holders and minority interest (continued)

Company	Notes	Revaluation of land and buildings	Cash flow hedges	Foreign currency translation	Remaining components	UDS* before Income Statement recognition	Total income/ (expense) recognised in the Income Statement	UDS*
		£m	£m	£m	£m	£m	£m	£m
2004								
Beginning of period		-	-	-	4,814	4,814	-	4,814
Actuarial losses on defined benefit pension schemes	26	-	-	-	(37)	(37)	-	(37)
Revaluation of land and buildings	13	16	-	-	-	16	-	16
Exchange differences on translating foreign operations		-	-	(50)	-	(50)	-	(50)
Aggregate tax effect of items not recognised in the Income Statement	14	-	-	-	4	4	-	4
Other		-	-	-	5	5	-	5
Income/(expense) not recognised in the Income Statement during the period		16	-	(50)	(28)	(62)	-	(62)
Transfer from unallocated divisible surplus		-	-	-	-	-	(6)	(6)
Adoption of FRS 27	41	-	-	4	(1,066)	(1,062)	-	(1,062)
Tax effect of adoption of FRS 27	14,41	-	-	-	46	46	-	46
At 31 December 2004		16	-	(46)	3,766	3,736	(6)	3,730

* Unallocated divisible surplus.

24. Borrowings

	Notes	Group		Company	
		2005 £m	2004 £m	2005 £m	2004 £m
Certificates of deposit, commercial paper and medium term notes	24(a)	1,963	2,221	-	-
Securitisations	24(b)	4,025	3,204	-	-
Bank overdrafts	19	105	144	68	124
Other		140	132	-	-
Total borrowings		6,233	5,701	68	124

(a) Certificates of deposit, commercial paper and medium term notes

The Group has issued sterling denominated certificates of deposit through a subsidiary into the UK market. The Group has also issued commercial paper and medium term notes through Standard Life Funding B.V., a wholly owned subsidiary of Standard Life Bank. Standard Life Bank has guaranteed the liabilities of its subsidiary in relation to the issuance of this debt. The guarantee is in respect of notes issued and is for a maximum of US\$2bn and Euro 4bn in relation to the US commercial paper and Euro commercial paper programmes respectively, and Euro 4bn in respect of the medium term note programme. Generally, borrowings are short term variable rate instruments.

	Group		Carrying amount	
	Average interest rates 2005	2004	2005 £m	2004 £m
Due within 1 year				
Standard Life Bank certificates of deposit – GBP	4.45%	4.80%	789	933
Standard Life Funding B.V. Commercial Paper – GBP	4.60%	4.90%	196	30
Standard Life Funding B.V. Commercial Paper – USD	4.43%	2.40%	440	150
Standard Life Funding B.V. Commercial Paper – JPY	0.09%	-	20	-
Standard Life Funding B.V. Commercial Paper – EUR	2.45%	2.20%	341	515
Standard Life Funding B.V. Medium term notes – GBP	5.60%	5.00%	15	201
Standard Life Funding B.V. Medium term notes – USD	4.58%	-	58	-
Standard Life Funding B.V. Medium term notes – EUR	-	2.30%	-	211
			1,859	2,040
Due between 1 and 5 years				
Standard Life Funding B.V. Medium term notes – GBP	4.80%	5.20%	12	27
Standard Life Funding B.V. Medium term notes – USD	-	2.60%	-	52
Standard Life Bank certificates of deposit – GBP	4.54%	4.90%	5	15
			17	94
Due after 5 years				
Standard Life Funding B.V. Medium term notes – EUR	2.70%	2.40%	83	87
Standard Life Funding B.V. Medium term notes – GBP	4.63%	-	4	-
			87	87
Total certificates of deposit, commercial paper and medium term notes			1,963	2,221

The carrying amounts disclosed above reasonably approximate the fair values as at the year-end.

24. Borrowings (continued)

(b) Securitisations

Loans are issued by the Group which are secured by mortgages subject to securitisation (Note 15). Under this arrangement, the beneficial interest in these mortgages is transferred to special purpose entities. The issue of mortgage backed floating rate notes by the special purpose entities has funded the purchase of the mortgages. The Company and its subsidiaries are not obliged to support any losses suffered by the note holders and do not intend to provide such support. The notes were issued on the basis that note holders are only entitled to obtain payment, of both principal and interest, to the extent that the available resources of the respective special purpose entities including funds due from customers in respect of the securitised mortgages, are sufficient and that note holders have no recourse whatsoever to the Company or its subsidiaries. This has been clearly stated in the legal agreements with note holders.

The mortgage backed floating rate notes at year-end are as follows:

	Group		Carrying amount	
	Average interest rates 2005	2004	2005 £m	2004 £m
Lothian Mortgages No. 1 PLC – USD – Maturity 2017	4.62%	2.40%	215	252
Lothian Mortgages No. 1 PLC – GBP – Maturity 2035	5.09%	5.30%	570	568
Lothian Mortgages No. 2 PLC – USD – Maturity 2018	-	2.30%	-	80
Lothian Mortgages No. 2 PLC – GBP – Maturity 2038	4.93%	5.10%	202	201
Lothian Mortgages No. 2 PLC – USD – Maturity 2038	4.56%	2.30%	333	382
Lothian Mortgages No. 2 PLC – EUR – Maturity 2038	2.62%	2.50%	522	537
Lothian Mortgages No. 3 PLC – USD – Maturity 2019	4.49%	2.30%	295	400
Lothian Mortgages No. 3 PLC – GBP – Maturity 2039	4.95%	5.30%	786	784
Lothian Mortgages No. 4 PLC – USD – Maturity 2006	4.41%	-	57	-
Lothian Mortgages No. 4 PLC – EUR – Maturity 2040	2.33%	-	476	-
Lothian Mortgages No. 4 PLC – GBP – Maturity 2040	4.81%	-	569	-
Total securitisations			4,025	3,204

25. Subordinated liabilities

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Subordinated guaranteed bonds				
6.75% £500,000,000 Fixed rate perpetual reset subordinated guaranteed bonds 2027	505	505	505	505
6.375% €750,000,000 Fixed/floating rate subordinated guaranteed bonds 2022	527	542	527	542
Subordinated members' accounts				
6.546 % £300,000,000 Mutual Assurance Capital Securities	319	299	319	299
5.314 % €360,000,000 Mutual Assurance Capital Securities	260	254	260	254
Subordinated notes				
6.14% £265,000,000 Fixed rate undated subordinated notes 2015	267	-	-	-
Total subordinated liabilities and members' accounts	1,878	1,600	1,611	1,600

Subordinated guaranteed bonds

The 6.75% Sterling Fixed rate perpetual reset subordinated guaranteed bonds and the 6.375% Euro Fixed/floating rate subordinated guaranteed sterling bonds 2022 were issued on 12 July 2002 by SL Finance PLC, a wholly owned subsidiary of the Company. The payment of principal and interest in respect of the bonds has been irrevocably and unconditionally guaranteed by the Company. The claims of the bondholders to payment under the guarantee will rank below the claims of all senior creditors of the Company including policyholders.

The Sterling bonds are redeemable at par at the option of the issuer on 12 July 2027 and on every fifth anniversary thereafter. If the Sterling bonds are not redeemed on 12 July 2027, the interest rate payable will be reset to 2.85% over the gross redemption yield on the appropriate 5-year benchmark gilt on the reset date.

The Euro bonds are redeemable at par at the option of the issuer on 12 July 2012 and on any interest payment date thereafter until maturity. From 12 July 2012 the Euro bonds will bear interest quarterly in arrears at a floating rate determined by the 3 month Euro deposit rate.

25. Subordinated liabilities (continued)

Subordinated members' accounts

During 2004, SL MACS PLC and SL MACS (No.2) PLC ("the Issuers"), subsidiaries of the Company, raised finance through the issue of Mutual Assurance Capital Securities (MACS). The MACS are perpetual securities of the Issuers and as such have no fixed date for redemption. The gross proceeds of the issue of MACS were made available to the Company pursuant to two Subordinated Members' Account (SMA) agreements between the Company and the Issuers. The obligations of the Company under the SMA agreements constitute direct, unsecured and, save as to subordination, unconditional obligations of the Company. The claims of the Issuers would, on a winding up of the Company, be subordinated and rank junior to the full satisfaction of the claims of (i) all unsubordinated creditors of the Company, including all policyholders, and (ii) the subordinated Guaranteed Bonds shown above.

There is no fixed date for the repayment of the amounts under the SMA agreements and accordingly there is no fixed due date for redemption of the MACS. Under the respective SMA agreements, the Company may elect to repay all amounts payable together with the accrued interest up to (but excluding) the first redemption date of 6 January 2020 for the sterling denominated MACS and 6 January 2015 for the euro denominated MACS or any interest payment date thereafter. In certain circumstances the Company may also elect to repay all amounts payable under the respective SMA agreements prior to the applicable first optional redemption date noted above.

The sterling denominated MACS started accruing interest from 4 November 2004 and bear interest at a rate of 6.546% per annum payable annually in arrears on 6 January each year, commencing on 6 January 2006. From and including 6 January 2020 and every fifth anniversary thereafter, these MACS will bear interest annually in arrears based on the aggregate of a margin plus the gross redemption yield of the specific gilts.

The Euro denominated MACS started accruing interest from 4 November 2004 and bear interest at a rate of 5.314% per annum payable annually in arrears on 6 January, commencing on 6 January 2006. From and including 6 January 2015, these MACS will bear interest quarterly in arrears, commencing 6 April 2015, at a floating rate of interest to be calculated quarterly based on the aggregate of a margin plus the rate for three month euro deposits.

Each SMA agreement effectively provides that interest is payable by the Company to the applicable Issuer at the same rate and in the same amount as that paid by that Issuer in respect of the MACS.

The payment of interest by the Company to the Issuers under the SMA agreements may be deferred in certain circumstances, in which case the payment of interest by the Issuers under the MACS would also be deferred. If interest is deferred under the SMA agreement, the Company may elect to capitalise the amount deferred in certain circumstances and in other circumstances, this occurs automatically. If such deferred interest is capitalised under the SMA agreement then a corresponding amount would be capitalised under the applicable MACS.

If a demutualisation takes place, the SMA agreements contain provision for conversion into a replacement instrument, or under certain circumstances provides that the Company will repay the SMA, resulting in the redemption of the MACS.

Subordinated notes

On 29 June 2005, Standard Life Funding B.V. ("SLF B.V."), a wholly owned subsidiary of Standard Life Bank ("SLB"), issued £265m of undated subordinated notes (the "Subordinated Notes"). Within a Subordinated Deed of Guarantee, SLB guarantees the payment of all sums payable by SLF B.V. under the Subordinated Notes. The rights and claims of all Subordinated Noteholders are subordinated to the claims of all senior creditors of both SLF B.V. and SLB.

The Subordinated Notes are redeemable at par at the option of the issuer on 29 June 2015, but if they are not redeemed on 29 June 2015, then the interest rate payable will be reset to 2.80% over the gross redemption yield on the appropriate benchmark gilt on the reset date.

26. Pension and other post retirement benefit provisions

The Group operates defined contribution and defined benefit schemes for staff employed by the Group.

Defined contribution schemes

In the UK with effect from 16 November 2004, new employees are eligible to join a defined contribution scheme. The assets of the scheme are held separately from those of the Company in an independently administered fund. In Canada employees have the option to have their current year of service credited on a defined contribution basis. The contributions under this option are equivalent to the amount that the Group would have otherwise determined using the projected unit credit valuation method under the defined benefit scheme. £3m (2004 : £3m) is included as an expense in the Income Statement in respect of defined contribution schemes.

Defined benefit schemes

The Group operates defined benefit schemes for its employees in Europe and Canada. Within Europe defined benefit schemes operate in the UK, Ireland and Germany with the vast majority relating to the UK. With effect from 16 November 2004 the UK scheme was closed to new entrants. Updates to the valuations on which the pension liability of £386m (2004 : £472m) was based were at 31 December 2005 for all schemes. The European schemes accounted for £217m (2004 : £349m) of the total pension liability and £169m (2004 : £123m) related to the Canadian scheme. The Group expects to contribute £46m to its defined benefit pension schemes in 2006 and the Company expects to contribute £43m.

In Canada certain of the scheme plans provide employees with post retirement medical benefits. A one percentage point increase or decrease in the assumed medical cost trend rates on the accumulated post-employment benefit obligation for medical cost is £3m (2004 : £2m) and £2m (2004 : £2m) respectively.

(a) Analysis of amounts recognised in the Income Statement

The amounts recognised in the Group Income Statement for defined contribution and defined benefit schemes are as follows:

Notes	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Current service cost	(61)	(72)
Interest cost on benefit obligation	(68)	(68)
Expected return on plan assets	63	51
Past service cost	-	(11)
Gains on curtailment	-	15
Expense recognised in the Income Statement	5	(85)

(b) The reconciliation of actuarial gains and losses:

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Actual return less expected return on plan assets	137	23
Experience gains arising on schemes' liabilities	15	9
Changes in assumptions underlying schemes' liabilities	(130)	(74)
Actuarial gains/(losses) in the Statement of Recognised Income and Expenses	22	(42)

26. Pension and other post retirement benefit provisions (continued)

(c) Analysis of amounts recognised in the Balance Sheet

The amounts recognised in the Balance Sheet of the Group are as follows:

	Group					
	2005 £m			2004 £m		
	Europe	Canada	Total	Europe	Canada	Total
Present value of funded obligation	(1,265)	(126)	(1,391)	(1,082)	(90)	(1,172)
Fair value of plan assets	1,051	-	1,051	735	-	735
Present value of unfunded obligations	(3)	(43)	(46)	(2)	(33)	(35)
Net liability on the Balance Sheet	(217)	(169)	(386)	(349)	(123)	(472)

The definition of plan assets excludes non-transferable financial instruments issued by the reporting entity. Investments that do not meet the definition of plan assets are not deducted from the defined benefit pension scheme obligation. In 2005 certain of these non-transferable financial instruments relating to the Europe scheme were amended to enable transferability. The remaining excluded assets relate to the Canadian scheme.

The present value of the defined benefit obligation including all assets backing the scheme is as follows:

	Group	
	2005 £m	2004 £m
Defined benefit pension deficit recognised on the Balance Sheet	(386)	(472)
Investment by pension scheme in non-transferable financial instruments	111	181
Present value of the defined benefit obligation less the fair value of gross scheme assets	(275)	(291)

The amounts recognised in the Balance Sheet of the Company are as follows:

	Company					
	2005 £m			2004 £m		
	Europe	Canada	Total	Europe	Canada	Total
Present value of funded obligation	(1,265)	-	(1,265)	(1,081)	-	(1,081)
Fair value of plan assets	1,051	-	1,051	735	-	735
Present value of unfunded obligations	(2)	-	(2)	(2)	-	(2)
Net liability on the Balance Sheet	(216)	-	(216)	(348)	-	(348)

(d) Defined benefit obligation

The movement in the present value of defined benefit obligation is as follows:

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Beginning of period	1,207	1,063	1,083	1,063
Exchange differences	18	(6)	(1)	(6)
Service cost	58	80	58	70
Interest cost	68	68	60	67
Actuarial (gains)	115	65	93	60
Gains on curtailments	-	(15)	-	(15)
Benefits paid	(29)	(48)	(26)	(37)
Transfer on Canadian domestication	-	-	-	(119)
At 31 December	1,437	1,207	1,267	1,083

26. Pension and other post retirement benefit provisions (continued)

(e) Plan assets

The changes in the fair value of plan assets are as follows:

	Group		Company	
	2005	2004	2005	2004
	£m	£m	£m	£m
Beginning of period	735	635	735	635
Recognition of plan assets	96	-	96	-
Expected return	63	51	63	51
Actuarial gains	137	23	137	23
Contributions by employer	46	63	46	63
Benefits paid	(26)	(37)	(26)	(37)
At 31 December	1,051	735	1,051	735

The difference between the Group benefits paid disclosed in Table d and Table e is due to the exclusion of Canadian assets in Table e.

In 2005 the Group entered into futures contracts in order to increase exposure to bonds and reduce exposure to equities.

The distribution of the fair value of the plan assets at year-end is as follows:

	Group	
	2005	2004
	£m	£m
Equities	871	628
Bonds	99	80
Other	81	27
	1,051	735

The expected return on plan assets is based on market expectations at the beginning of the period for returns over the entire life of the related benefit obligations. The actual return on plan assets during 2005 was £200m (2004 : £74m).

(f) Principal assumptions

The principal assumptions used in determining defined benefit pension obligations for the Group's schemes are as follows:

	Group	
	12 months to 31 December 2005	13.5 months to 31 December 2004
Rate of increase in salaries	2.85% - 4.00%	4.50% - 5.00%
Rate of increase in pensions	2.25% - 2.85%	2.25% - 2.75%
Discount rate	4.80% - 5.25%	5.50% - 6.00%
Inflation assumption	2.25% - 2.85%	2.25% - 2.75%
Rate of return on plan assets	6.45%	7.45%

Mortality tables used for the UK defined benefit pension obligations:

Post-retirement - males	PMA92	PMA92
Post-retirement - females	PFA92	PFA92
Pre-retirement - males	AM92 - 5 years	AM92 - 5 years
Pre-retirement - females	AF92 - 5 years	AF92 - 5 years

The change in the assumption rate for the increase in salaries reflects management action regarding future salary increases which impact the UK scheme.

27. Deferred income

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Beginning of period	234	232	221	220
Additions during the year	39	40	31	35
Released to the Income Statement as fee income	(35)	(38)	(29)	(34)
At 31 December	238	234	223	221

28. Customer accounts related to banking activities and deposits by banks

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Current/demand accounts	2,217	2,283	-	-
Term deposits	2,040	2,000	-	-
Deposits by banks	877	864	-	-
Total customer accounts related to banking activities and deposits by banks	5,134	5,147	-	-

Current/demand accounts are subject to variable interest rates. Term deposits are subject to fixed interest rates.

The carrying amounts disclosed above reasonably approximate the fair values as at the year-end.

Interest rates on current/demand accounts ranged between 3.40% and 5.95% and those on term deposits ranged between 3.75% and 5.35%.

All amounts are expected to be settled within 12 months.

29. Other liabilities

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Insurance business:				
Amounts payable on direct insurance business	452	451	409	411
Deposits received from reinsurers	54	47	37	25
Amounts payable on reinsurance contracts	12	12	43	5
	518	510	489	441
Investment securities:				
Outstanding purchases of investment securities	204	185	128	165
	204	185	128	165
Other:				
Due to related parties	-	-	87	84
Accruals	276	177	106	104
Provisions	16	5	10	4
Other	544	489	227	271
	836	671	430	463
Total other liabilities	1,558	1,366	1,047	1,069

Provisions comprise obligations in respect of compensation, litigation, staff entitlements and reorganisation that are uncertain as to the amount and timing of outflow. Additional provisions made during the year were £11m (2004 : £3m) and £6m (2004 : £3m) for Group and Company respectively. The amount of other liabilities expected to be settled greater than twelve months is £171m (2004 : £266m) and for the Company £84m (2004 : £176m).

30. Net increase/(decrease) in operating assets and liabilities

	Group		Company	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
(Increase)/decrease in operating assets:				
Deferred acquisition costs	(87)	(448)	(32)	(424)
Investment in subsidiaries*	-	-	(947)	1,649
Investment in associates*	(558)	(2)	(222)	(281)
Investment property	(919)	(1,455)	(522)	(1,084)
Reinsurance assets	(50)	(99)	(29)	(713)
Loans and receivables	(108)	(1,393)	237	124
Derivatives net assets/(liabilities)	21	(456)	40	(331)
Investment securities	(12,857)	(8,359)	(10,818)	(8,759)
Other debtors	(79)	132	12	(26)
	(14,637)	(12,080)	(12,281)	(9,845)
Increase/(decrease) in operating liabilities:				
Insurance contract liabilities	2,947	1,373	2,482	1,570
Investment contract liabilities	11,634	8,180	10,832	7,694
Certificate of deposits, commercial paper and medium term notes	287	908	-	-
Current, demand and term deposits and deposits by banks	13	610	-	-
Pension and other post retirement benefit provisions	(28)	48	(46)	40
Deferred income	6	2	3	4
Customer accounts related to banking activities	(26)	(316)	-	-
Other liabilities	156	140	461	258
Change in liability for third party interest in consolidated funds	43	16	-	-
	15,032	10,961	13,732	9,566
Net (increase)/decrease in operating assets and liabilities	395	(1,119)	1,451	(279)

* Investment in Standard Life Investments (Global Liquidity Funds) PLC and certain unit trusts have been classified as operating activities due to the nature of the underlying transactions.

31. Risk management policies

(a) Governance framework

Standard Life's Group Risk Management Policy ensures that the risks taken in meeting the Group's corporate, financial and regulatory objectives are identified and managed in accordance with the approved risk framework.

The Group takes and manages risks to achieve its corporate, financial and regulatory objectives. The types of risk inherent in the pursuit of these objectives and the extent of exposure to these risks form the Group risk profile. The risk profile of the individual business units within the Group is similarly set by reference to its objectives.

The Group manages risks through the group risk management framework, which allows for the identification, assessment, control and monitoring of risks across the Group. The Group and each individual business unit establish effective risk management systems and controls within the framework for the following high-level categories of risk: insurance, credit, liquidity, market and operational.

The Board annually approves a separate Group Risk Policy for each category of risk specifying the procedures to be taken across the Group to identify, assess, control and monitor the risk. The governing body of each individual business unit also approves, as applicable, its own risk policies in line with the applicable Group Risk Policy. Each Group Risk Policy sets out minimum standards to which each individual business unit should adhere in constructing its own risk policies and procedures.

The Board delegates responsibility for the implementation of the day-to-day process to manage risk across the Group, to the Group Chief Executive. The Group Chief Executive is supported in this role by the Group Executive Committee and assisted by the Group Technical Risk Committee and the Group Operational Risk Committee. These committees are constituted with formal terms of reference.

The Group has an established risk management function whose role is to support the Board, the Group Chief Executive and the risk committees in meeting their risk management responsibilities. This centralised function is headed by the Director, Group Risk & Compliance, who reports directly to the Group Finance Director and is the FSA Approved Person charged with reporting to the Board on setting and controlling risk exposure across the Group.

A consolidated Board report is prepared on a quarterly basis summarising the information reported to the Group Risk Management Committees. The report comprises detailed sections on:

- Business Unit Risk Profiles;
- Strategic Risks;
- Group-wide Project Risks;
- Operational Risks;
- Technical Risks.

(b) Insurance risk

Insurance risk arises from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities. It is the risk of adverse deviations from the cash flows assumed when pricing or reserving for insurance contracts.

Sensitivity to the main assumptions underlying insurance risk e.g. mortality, longevity, persistency and expenses, can be seen in Note 22.

The Group sets the acceptable level of insurance risk through the Group Insurance Risk Policy.

The main features of the policy are:

- Insurance risk is only incurred in the pursuit of the Group's corporate and financial objectives, in particular to grow the business subject to maintaining adequate financial strength
- The writing of business only on approved rates, which have regard to experience of significant factors such as expenses, persistency, mortality and morbidity
- The use of reinsurance
- The monitoring of the adequacy of reserves to cover insurance liabilities
- Regular monitoring of the overall capital of the Group and of the appropriate individual business units.

Insurance risk is only undertaken within the permitted activities of each business unit.

31. Risk management policies (continued)

(b) Insurance risk (continued)

Each business unit defines the classes and characteristics of insurance business that it is prepared to accept.

Insurance liabilities are assessed in accordance with the Group's obligation to treat customers fairly. Where policy benefits are subject to discretion, the valuation of liabilities and pricing of policies will reflect any restriction on that discretion arising from published documents such as The Principles and Practices of Financial Management.

New business is written in accordance with approved pricing assumptions. Underwriting criteria is defined and aligned to the approved pricing assumptions and to the identification of aggregations of risk with the policyholder.

Every product open to new business is reviewed annually to confirm, or otherwise, that pricing assumptions remain appropriate.

The approach to the use of reinsurance or other means of risk transfer is defined.

Claim values and reinsurance reclaims are calculated using rigorously tested systems and well-documented procedures. Controls over the claims process to mitigate invalid claims and claim payment errors, including reinsurance recoveries, is considered under the Group Operational Risk Policy. Inefficiencies in the settlement of claims is reflected in the periodic, but at least annual, analyses of expenses and claims.

Each business unit must ensure that relevant stress testing is carried out to help ensure that only acceptable levels of insurance risk are undertaken.

The Group's concentration of insurance risk, measured by insurance liabilities, before and after reinsurance by territory in relation to the type of insurance contract is as follows:

	Group					
	Life & Pensions	Healthcare & General Insurance	Total	Life & Pensions	Healthcare & General Insurance	Total
	2005 £m	2005 £m	2005 £m	2004 £m	2004 £m	2004 £m
United Kingdom						
Gross liabilities	32,115	153	32,268	30,277	163	30,440
Net liabilities	31,811	131	31,942	30,036	146	30,182
Canada						
Gross liabilities	5,987	-	5,987	4,640	-	4,640
Net liabilities	5,560	-	5,560	4,307	-	4,307
International						
Gross liabilities	2,473	63	2,536	1,961	77	2,038
Net liabilities	2,471	39	2,510	1,951	61	2,012
Total gross liabilities	40,575	216	40,791	36,878	240	37,118
Total net liabilities	39,842	170	40,012	36,294	207	36,501

The Company's concentration of insurance liabilities is similar to that of the Group, with a significant concentration of insurance risk in the United Kingdom.

Where an embedded derivative is an insurance contract in its own right or is closely related to the host insurance contract then separation is not required and the whole contract is treated as an insurance contract. At the year-end all embedded derivatives were either insurance contracts in their own right or were closely related to the host insurance contract and did not require separation.

31. Risk management policies (continued)

(c) Credit risk

Credit risk is the risk incurred whenever the Group or individual business units are exposed to loss if a counterparty fails to perform its contractual obligations, including failure to perform those obligations in a timely manner. The Group sets the acceptable level of credit risk through the Group Credit Risk Policy.

The overriding prudential requirement of the policy, which covers all assets beneficially owned by the Group excluding assets held in respect of linked liabilities, is that all assets are of sufficient quality and are sufficiently well diversified to represent appropriate backing for its liabilities, capital and reserves. The policy also requires compliance with all applicable legislation and regulation and sets further limits under specific types of financial instruments, as summarised below.

Cash and cash equivalents

Maximum exposure limits are set with reference to long-term credit ratings issued by Standard & Poor's and Moody's.

Derivative financial assets

Maximum exposure limits, net of collateral, are set with reference to long-term credit ratings issued by Standard & Poor's and Moody's. The forms of collateral that may be accepted are also specified and minimum transfer amounts in respect of margin deposits are also set by reference to the counterparty's rating.

Debt securities

Maximum exposure limits are set on the proportions of the total portfolio of debt securities, excluding those secured on specific assets, which may be placed with counterparties rated below certain agreed long-term ratings levels.

Loans and receivables

Portfolio limits are set by the individual business units. These limits specify the proportion of the value of the total portfolio of mortgage loans and mortgage bonds that are represented by a single or group of related counterparties, geographic area, employment status, economic sector, risk rating and loan to value percentage.

Reinsurance assets

The Group's policy is to place reinsurance only with highly rated counterparties. The credit ratings are assessed on an ongoing basis. Furthermore, the policy restricts the Group from assuming concentrations of risk with few individual reinsurers by specifying certain limits on ceding and the minimum conditions for acceptance and retention of reinsurers.

Other financial instruments

Property leases are entered into only after an assessment of the prospective tenant's ability to pay the rent. The credit quality of the portfolio is monitored on an ongoing basis.

All intermediaries must meet minimum requirements defined by the business units. Standard terms of business permit commission due to intermediaries to be netted off against amounts to be reclaimed.

Credit risk in respect of customer balances, incurred on non-payment of premiums or contributions will only persist during the grace period specified in the policy document or trust deed, on the expiry of which the policy is either paid-up or terminated.

Credit risk in respect of loans issued to holders of long-term business policies is mitigated by holding the policy as security against the loan.

31. Risk management policies (continued)

(c) Credit risk (continued)

Master netting arrangements

The Group has entered into a number of master netting arrangements with counterparties with which it transacts significant volumes of transactions. Such arrangements do not generally result in the offset of Balance Sheet liabilities against Balance Sheet assets as transactions are usually settled on a gross basis. However, the credit risk associated with such balances is reduced in the event of default when assets held under the arrangement are realised and balances settled on a net basis.

The extent to which the Group's overall exposure to credit risk is reduced through a master netting arrangement may change substantially within a short period following the Balance Sheet date because the exposure is affected by each transaction subject to the arrangement.

Credit ratings

The following tables provide information regarding the credit risk exposure of the Group at 31 December 2005, by classifying the following financial assets, excluding those backing unit linked business, according to credit ratings of the counterparties. AAA is the highest possible rating. Rated financial assets that fall outside the range of AAA to BBB are classified as Below BBB.

31 December 2005	Group						Total
	Credit rating					Not rated	
	AAA	AA	A	BBB	Below BBB		
	£m	£m	£m	£m	£m		
Reinsurance assets	210	265	180	-	11	113	779
Debt securities	25,277	3,604	5,426	1,334	124	1,536	37,301
Derivative financial assets	-	223	23	-	-	-	246
Cash and cash equivalents	697	2,666	300	1	-	-	3,664
Off-balance sheet financial assets*	-	-	-	-	-	2,299	2,299

31 December 2004	Group						Total
	Credit rating					Not rated	
	AAA	AA	A	BBB	Below BBB		
	£m	£m	£m	£m	£m		
Reinsurance assets	183	213	144	-	10	67	617
Debt securities	22,177	2,798	4,610	1,429	89	1,421	32,524
Derivative financial assets	-	204	17	-	-	1	222
Cash and cash equivalents	519	1,316	314	4	-	-	2,153
Off-balance sheet financial assets*	-	-	-	-	-	2,311	2,311

* Mortgage lending commitments.

The Company has a similar risk profile to that of the Group, with a significant concentration of AAA debt securities.

For reinsurance assets, in the above tables, where a rating does not exist for a counterparty's subsidiary company then the rating of that subsidiary's parent company has been used.

At 31 December 2005, credit risk is primarily concentrated in the United Kingdom within the Government and Financial Services Industry sectors. Counterparty risk is monitored in accordance with the Group Credit Risk Policy.

Included in the Investments in associates and joint ventures (Note 11) is the Group's investment in the Standard Life Investments (Global Liquidity Funds) PLC, which is accounted for at fair value through the profit and loss in accordance with IAS 39. This fund is rated as AAA.

Assets amounting to £7,317m (2004 : £5,733m) backing unit linked business have been excluded from these tables as the credit risk on such financial assets is borne by the policyholders.

31. Risk management policies (continued)

(d) Liquidity or funding risk

Liquidity risk is the risk that the Group or individual business units, although solvent, do not have sufficient financial resources available to meet their obligations as they fall due, or can secure them only at excessive cost.

The Group sets the acceptable level of liquidity risk through the Group Liquidity Risk Policy. The methods used to manage liquidity risk include:

- Limits on the volume of financial assets held which are both not quoted and not regularly traded on a recognised exchange
- Committed third party funding facilities
- Establishing contingency funding plans to ensure adequate liquid financial resources are in place to meet obligations as they fall due in the event of reasonably foreseeable abnormal circumstances.

The central Group Treasury function has responsibility for mitigating liquidity, interest rate and foreign exchange risks across the Group and for arranging external financing.

(e) Market risk

Market risk is the risk that as a result of market movements the Group or individual business units may be exposed to fluctuations in the value of its assets, the amount of its liabilities or the income from its assets. Sources of general market risk include movements in interest rates, equities and foreign exchange rates.

Sensitivity to market risk can be seen in Note 22.

The Group sets the acceptable level of market risk through the Group Market Risk Policy.

The main features of the policy are:

- Market risk is only incurred in the pursuit of the Group's corporate and financial objectives, in particular, its investment objectives
- Asset allocation and portfolio limit structures are established for each asset class
- Adequately diversified benchmarks set and approved
- Control over derivatives and hedging activities
- Aggregate exposure limits that are in line with the regulatory requirements.

Asset Liability Matching

Each quarter, an analysis is carried out to quantify the market risk that the Group is exposed to. The sensitivity of the published statutory surplus to changes in market conditions is analysed, and consideration is given as to whether the current investment strategy remains appropriate. Where necessary, changes to the current investment strategy are recommended to the Board.

A market risk and investment strategy paper is prepared and presented to the Board each quarter setting out the results of the above analysis and any recommendations to be made.

The market risk paper examines market changes that are considered to be significant, but reasonably foreseeable, rather than worst-case scenarios. Worst-case scenarios, defined as scenarios that have a 1 in 200 year chance of occurring over a one-year period, are considered as part of the process to produce the Company's Individual Capital Assessment.

In addition, the financial position of the Group, including exposure to changes in market conditions, is monitored on an ongoing basis.

Use of derivatives

Derivative instruments are employed by the Group to not only match the liabilities but also for efficient portfolio management in reducing market risk and currency risk. Such derivatives are either listed on regulated markets or are with approved counterparties. At inception, the Group documents the purpose of the derivative instrument. For derivatives whose purpose it is to hedge existing risk, this documentation includes the identification of the hedged item and the risk being mitigated. During the life of the derivative instrument, the purpose the instrument fulfils and its continued relevance is monitored. For derivatives whose purpose is to hedge existing risk, this monitoring includes an assessment of the effectiveness of the risk mitigation. Further information on derivative financial instruments can be found in Note 16.

31. Risk management policies (continued)

(e) Market risk (continued)

Currency risk

The Group'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. 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, and net investment in foreign operations when these are incorporated in the consolidated financial statements of the Group.

The Group's market risk policy specifies that no more than 25% of the total assets and loans representing local currency liabilities or capital and reserves will be denominated in currencies other than the local currency. This policy does not apply to unit linked contracts where the currency risk is borne by the policyholder.

The tables below summarises the Group's exposure to foreign currency exchange rate risks at 31 December 2005 and 2004 by categorising the carrying value of assets and liabilities by major currencies. Within other are a wide range of other currencies due to the Group's investment strategy. These are stated after excluding exposures related to unit linked business.

	2005 Group				
	GBP £m	Euro £m	CAD £m	Other £m	Total £m
Loans and receivables	10,734	1	1,638	2	12,375
Investment securities					
Equity securities and interests in pooled investment funds	11,847	2,835	433	5,025	20,140
Debt securities	29,401	2,435	4,924	541	37,301
Other financial assets	4,135	305	406	146	4,992
Non-financial assets	909	1,364	551	1,081	3,905
Total assets excluding unit linked assets	57,026	6,940	7,952	6,795	78,713
Unit linked assets					41,547
Total Group assets					120,260
Minority interest	229	111	-	-	340
Subordinated liabilities	1,091	787	-	-	1,878
Non-participating contract liabilities					
Non-participating insurance contracts	13,772	410	4,464	26	18,672
Non-participating investment contracts	244	5	2,175	2	2,426
Participating contract liabilities					
Participating insurance contracts	17,056	2,101	476	-	19,633
Participating investment contracts	16,812	1,258	6	-	18,076
Present value of future results on non-participating contracts	(1,505)	(23)	-	-	(1,528)
Net assets attributable to unit holders	279	-	79	-	358
Other financial liabilities	9,186	1,782	291	1,476	12,735
Non-financial liabilities	1,008	113	173	2	1,296
Total liabilities excluding unit linked liabilities and unallocated divisible surplus	58,172	6,544	7,664	1,506	73,886
Unit linked liabilities					41,547
Unallocated divisible surplus					4,827
Total Group liabilities and minority interest					120,260

31. Risk management policies (continued)

(e) Market risk (continued)

Currency risk (continued)

	2004 Group				
	GBP £m	Euro £m	CAD £m	Other £m	Total £m
Loans and receivables	10,350	31	1,565	-	11,946
Investment securities					
Equity securities and interests in pooled investment funds	10,479	2,018	288	5,085	17,870
Debt securities	26,024	2,476	3,773	251	32,524
Other financial assets	2,556	316	455	150	3,477
Non-financial assets	2,363	1,590	1,024	190	5,167
Total assets excluding unit linked assets	51,772	6,431	7,105	5,676	70,984
Unit linked assets					31,030
Total Group assets					102,014
Minority interest	145	105	-	-	250
Subordinated liabilities	804	796	-	-	1,600
Non-participating contract liabilities					
Non-participating insurance contracts	12,927	415	3,545	9	16,896
Non-participating investment contracts	275	4	2,010	-	2,289
Participating contract liabilities					
Participating insurance contracts	16,322	1,601	341	-	18,264
Participating investment contracts	14,906	1,020	3	-	15,929
Present value of future results on non-participating contracts	(995)	(46)	-	-	(1,041)
Other financial liabilities	8,419	1,836	203	1,338	11,796
Net assets attributable to unit holders	31	-	46	-	77
Non-financial liabilities	949	157	140	-	1,246
Total liabilities excluding unit linked liabilities and unallocated divisible surplus	53,783	5,888	6,288	1,347	67,306
Unit linked liabilities					31,030
Unallocated divisible surplus					3,678
Total Group liabilities and minority interest					102,014

Financial assets and liabilities exclude items falling outside the disclosure requirements of the relevant IFRS standard. Items such as investments in associates and reinsurance assets are included in non-financial assets.

The unallocated divisible surplus by nature is not attributed to currency categories.

31. Risk management policies (continued)

(e) Market risk (continued)

Interest rate risk

Interest rate risk refers to the potential variability in the Group's financial condition as a result of changes in interest rates.

Assets backing the fixed term insurance and investment liabilities may include those without fixed terms like equities and property, included in N/A, as well as fixed term assets.

Liabilities without fixed terms such as most annuity business, may be backed by assets with fixed terms.

The following table sets out the time to contractual maturity or repricing date, whichever is the earliest, for the Group's assets and liabilities exposed to interest rate risk:

	Group							N/A	Total
	Within 1 year	1-5 years	5-10 years	10-15 years	15-20 years	> 20 years	No fixed term		
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets:									
Financial assets:									
Fair value interest rate risk	3,831	13,423	10,554	4,476	2,915	6,677	1,117	-	42,993
Cash flow interest rate risk	9,407	52	15	-	349	566	124	-	10,513
Non-interest bearing financial instruments	-	-	-	-	-	-	-	21,302	21,302
Non-financial assets	-	-	-	-	-	-	-	3,905	3,905
Total assets excluding unit linked assets	13,238	13,475	10,569	4,476	3,264	7,243	1,241	25,207	78,713
Unit linked assets									41,547
Total Group assets									120,260
Minority interest	-	-	-	-	-	-	-	340	340
Liabilities:									
Insurance and investment contract liabilities:									
Fair value interest rate risk:									
Insurance contracts	1,323	4,885	6,543	2,353	712	1,071	21,392	26	38,305
Investment contracts	1,626	4,949	3,774	3,017	2,813	4,247	76	-	20,502
Present value of future results on non-participating contracts	-	-	-	-	-	-	-	(1,528)	(1,528)
Unallocated divisible surplus	-	-	-	-	-	-	-	4,827	4,827
Other financial liabilities:									
Fair value interest rate risk	11	88	347	-	3	-	4	9	462
Cash flow interest rate risk	11,229	73	758	300	-	489	-	66	12,915
Net assets attributable to unit holders	-	-	-	-	-	-	-	358	358
Non-interest bearing financial instruments	-	-	-	-	-	-	-	1,236	1,236
Non-financial liabilities	-	-	-	-	-	-	-	1,296	1,296
Total liabilities excluding unit linked liabilities	14,189	9,995	11,422	5,670	3,528	5,807	21,472	6,630	78,713
Unit linked liabilities									41,547
Total Group liabilities and minority interest									120,260
Total assets less liabilities and minority interest	(951)	3,480	(853)	(1,194)	(264)	1,436	(20,231)	18,577	-

31. Risk management policies (continued)

(e) Market risk (continued)

Interest rate risk (continued)

31 December 2004

	Group							N/A	Total
	Within 1 year	1-5 years	5-10 years	10-15 years	15-20 years	>20 years	No fixed term		
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets:									
Financial assets:									
Fair value interest rate risk	2,134	11,691	6,774	5,053	3,810	5,235	914	-	35,611
Cash flow interest rate risk	9,960	112	14	-	390	499	166	-	11,141
Non-interest bearing financial instruments	-	-	-	-	-	-	-	19,065	19,065
Non-financial assets	-	-	-	-	-	-	-	5,167	5,167
Total assets excluding unit linked assets	12,094	11,803	6,788	5,053	4,200	5,734	1,080	24,232	70,984
Unit linked assets									31,030
Total Group assets									102,014
Minority interest	-	-	-	-	-	-	-	250	250
Liabilities:									
Insurance and investment contract liabilities:									
Fair value interest rate risk:									
Insurance contracts	975	3,978	5,612	2,226	803	1,046	20,116	404	35,160
Investment contracts	1,142	4,084	3,941	3,107	2,321	3,314	356	(47)	18,218
Unallocated divisible surplus	-	-	-	-	-	-	-	3,678	3,678
Present value of future profits on non-participating contracts	-	-	-	-	-	-	-	(1,041)	(1,041)
Other financial liabilities:									
Fair value interest rate risk	-	31	89	-	3	(1)	4	-	126
Cash flow interest rate risk	10,798	61	788	300	-	489	-	62	12,498
Net assets attributable to unit holders	-	-	-	-	-	-	-	77	77
Non-interest bearing financial instruments	-	-	-	-	-	-	-	772	772
Non-financial liabilities	-	-	-	-	-	-	-	1,246	1,246
Total liabilities excluding unit linked liabilities	12,915	8,154	10,430	5,633	3,127	4,848	20,476	5,401	70,984
Unit linked liabilities									31,030
Total Group liabilities and minority interest									102,014
Total assets less liabilities and minority interest	(821)	3,649	(3,642)	(580)	1,073	886	(19,396)	18,831	-

The interest rate risk profile of the Company is similar to that of the Group.

Included in non-financial assets is the Group's investment in the Standard Life Investment (Global Liquidity Funds) PLC, which is accounted for at fair value through the profit and loss in accordance with IAS 39. This investment, disclosed in Note 11 – Investments in associates and joint ventures, will expose the Group to both fair value and cash flow interest risk as the underlying investments within the fund are a mixture of fixed and floating rate cash investments.

31. Risk management policies (continued)

(e) Market risk (continued)

Interest rate risk (continued)

Financial assets subject to interest rate risk include debt securities, loans and receivables and derivative financial instruments. Non-interest bearing financial instruments include equity securities. Insurance and investment contract liabilities exposed to interest rate risk comprise with and without participating non-unit linked liabilities. Other financial liabilities subject to interest rate risk include bank customer accounts, derivative financial instruments, subordinated liabilities and borrowings.

Financial instruments classified as exposed to fair value interest rate risk are those with a fixed rate of interest. Financial instruments classified as exposed to cash flow interest rate risk are those with a floating interest rate, which is reset as market rates change. For those contracts where part of the liability is exposed to fair value interest rate risk then the whole contract is considered to be exposed to fair value interest rate risk.

The Group is also exposed to interest rate risk as a result of off-balance sheet credit commitments and guarantees as detailed in Note 32. Under such arrangements, the Group is contractually obliged to extend financing facilities to such counterparties at agreed terms and conditions. Such commitments are subject to counterparties continuing to satisfy certain conditions and are normally renewed on an annual basis.

The Group's range for weighted average effective interest rates is shown for selected assets and liabilities valued at amortised cost. These weighted averages represent the weighted average interest rates across all currencies in which the Group's business is conducted. The applicable rates are as follows:

	Group	
	2005 %	2004 %
Assets		
Mortgage loans	6.04	6.73
Loans secured on policies	5.91	6.37
Loans secured by mortgages subject to securitisation	5.76	6.55
Held to maturity debt securities	7.33	7.79
Cash and cash equivalents	4.44	4.49
	Group	
	2005 %	2004 %
Liabilities		
Customer accounts related to banking activities	4.11	4.28
Borrowings	4.18	4.58
Subordinated liabilities	6.51	6.57
Investment contracts at amortised cost:	5.41	5.45
Annuities	7.77	8.16
Term deposits	3.94	4.19
Guaranteed bonds	3.78	3.72

Unit linked contracts

For unit linked contracts, the unit prices (i.e. obligation to the policyholders) are based on fair values of investments and other assets within the portfolio. Therefore, there is no interest rate risk for these contracts. However, the Group's exposure to such contracts is the risk of volatility in asset management fees due to the impact of interest rate and market price movements on the fair value of assets held in the linked funds, on which asset management fees are based.

Within this category of contracts there are insurance contracts with guaranteed minimum death benefits that expose the Group to the risk of a reduction in the value of underlying investments as a result of changes in interest rates.

All such contracts have embedded surrender options and unit linked features. These derivatives vary in response to the change in financial variables (such as market interest rates). The Group is therefore required to separate and fair value these derivatives when the instrument is not designated to be measured at fair value through income and the embedded derivatives are not closely related to the host contract. At year-end, all embedded derivatives within these liabilities were closely related to the host contract and did not require separation.

31. Risk management policies (continued)

(f) Operational risk

Operational risk is defined as the risk of loss, or adverse consequences for the business, resulting from inadequate or failed internal processes, people and systems, or from external events.

The Group sets an acceptable level of operational risk through the Group Operational Risk Policy. The Policy also requires compliance with applicable legislation and regulations.

The types of operational risk the Group is exposed to are identified using the following operational risk categories: fraud or irregularities; regulatory or legal; customer treatment; business interruption; supplier failure; planning; process execution; and people. Activities undertaken to ensure the practical operation of controls over financial risks (i.e. market, credit, liquidity and insurance risk) are treated as an operational risk.

A strategy to control the operational risk exposures identified is based on a combination of one or all of the following: modify operations such that there is no exposure to the risk; accept exposure to the risk and choose not to control the risk; or accept exposure to the risk and control the exposure by risk transfer or risk treatment.

The level of control and nature of the controls implemented is based on, amongst other things the:

- Potential cause and impact of the risk
- Likelihood of the risk happening in the absence of any controls
- Ease with which the risk could be insured against
- Cost of implementing controls to reduce the likelihood of the risk occurring
- Operational risk appetite.

Existing or newly implemented controls are identified, including key controls, documented and their performance subject to self-assessment by business managers at least quarterly. A conclusion as to the adequacy of these controls is documented and subject to ongoing self-assessment by business managers.

The assessment of operational risk exposures is performed on a quantitative and qualitative basis using a combination of likelihood and customer, financial and reputational impact. As part of the development of their business plan each Group company ensures that relevant stress testing is carried out, at least annually, to help identify the exposure to operational risk.

The operational risks faced by each Group company and its exposure to these risks forms its operational risk profile. Each Group company is required to understand and review its profile by monitoring its key operational risk exposures, compliance with approved thresholds, loss experience and the results of control self-assessment.

The impact of a new product, a significant change, or any one-off transaction on the operational risk profile of each Group company is assessed and managed in accordance with established guidelines or standards.

32. Contingencies

(a) Legal proceedings and regulations

The Group and Company like other insurers are subject to legal proceeding in the normal course of business. While it is not practicable to forecast or determine the final results of all pending or threatened legal proceedings, management does not believe that such proceedings (including litigations) will have a material effect on the results and financial position of the Group and Company.

The Group and Company are subject to insurance solvency regulations in all the territories in which they issue insurance and investment contracts, and they have complied with all the local solvency regulations. There are no contingencies associated with the Group or Company's compliance or lack of compliance with these regulations.

(b) Guarantees

Subordinated guaranteed bonds were issued by SL Finance PLC, a wholly owned subsidiary of the Company, and are the subject of a subordinated guarantee from the Company (refer to Note 25). Under the terms of the financial guarantee, the payment and interest in respect of the bonds has been irrevocably and unconditionally guaranteed by the Company.

A Group subsidiary, Standard Life Bank Limited has guaranteed the liabilities of its subsidiary undertaking, Standard Life Funding B.V., in connection with the subsidiary undertakings issuance of commercial paper and medium term notes. The guarantee is in respect of notes issued and is for a maximum of US \$2bn (2004 : US \$2bn) and €4bn (2004 : €4bn) in relation to the US commercial paper and Euro commercial paper programmes respectively, and €4bn (2004 : €4bn) on respect of the medium term note programme.

(c) Warranties

The Company has potential obligations in relation to certain warranties given in connection with the disposal of a book of business during the 2005 financial year. The Company's total liability in respect of all relevant claims under these warranties is limited to a total of €30m and extends to a maximum period of 30 months from 30 September 2005. The likelihood of payments being made under these warranties is considered to be low.

(d) Joint ventures and associates

The Group has entered into agreements to share in the assets and liabilities of joint venture and associate investments. The directors do not anticipate any material losses from such investments, and the operations of such investments are not material in relation to the operations of the Group.

The Group's share of contingent liabilities of the joint ventures and associates is not significant in relation to the operations of the Group.

33. Commitments

(a) Capital commitments

The Group's capital commitments as at the year-end are:

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Authorised and contracted for but not provided and incurred:				
Investment properties	264	411	128	36
Property and equipment	55	74	54	74
Total capital commitments	319	485	182	110

£249m (2004 : £386m) and £15m (2004 : £1m) relates to the contractual obligations to purchase, construct, or develop investment property and repair, maintain, or enhance investment property, respectively.

(b) Off-balance sheet financial instruments

The following indicates the contractual amounts of the Group's off-balance sheet financial instruments that commit it to customers and third parties, as at the year-end:

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Guarantees and letters of credit	8	8	-	-
Commitments to extend credit; maturity one year or less	2,299	2,311	-	-
Other commitments	505	390	357	482
Total off-balance sheet financial instruments	2,812	2,709	357	482

Included in 'Other commitments' is £296m (2004 : £192m) committed by certain of the Group's subsidiaries which are not fully owned by the Group. These commitments are funded through (contractually agreed) additional investments in the subsidiary by the Group and the minority interests. The levels of funding are not necessarily in line with the relevant percentage holdings.

(c) Operating lease commitments

The Group has entered into commercial non-cancellable leases on certain property and equipment. Such leases have varying terms, escalation clauses and renewal rights.

The future aggregate minimum lease payments under non-cancellable operating leases are:

	Group		Company	
	2005 £m	2004 £m	2005 £m	2004 £m
Less than one year	9	8	1	8
Between one and five years	15	22	2	21
More than five years	6	7	6	7
Total operating lease commitments	30	37	9	36

(d) Other commitments

On 20 September 2005 Standard Life Healthcare (SLH) announced that it was purchasing the private medical insurance business of FirstAssist. As at 31 December 2005 the Group was committed to this purchase, however the purchase was still subject to a Part VII transfer, under the Financial Services and Markets Act 2000, as well as High Court approval.

34. Related party transactions

(a) Transactions with and balances due from/to related parties

In the normal course of business, the Group enters into transactions with related parties that relate to insurance, banking and investment management business. Such related party transactions are at arms length.

Details of significant transactions with related parties during the year are as follows:

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Sales to:		
Associates	5,478	5,318
Joint ventures and other related parties	53	21
Total sales	5,531	5,339
Purchases from:		
Associates	6,037	5,376
Joint ventures and other related parties	51	63
Total purchases	6,088	5,439

Transactions shown above relate primarily to the sale and purchase of holdings in a unit trust, Standard Life Investments (Global Liquidity Funds) PLC, which is an associate of the Group.

At the year-end £241m (2004 : £191m) was due from related parties, primarily relating to the Group's defined benefit pension scheme.

(b) Compensation of key management personnel

Key management personnel, comprising 21 people (2004 : 22 people) of the Group, include all directors, both executive and non-executive and the direct reports of the Chief Executive Officer. Detailed disclosures of directors' remuneration for the year and transactions in which the directors are interested are contained within the audited section of the Remuneration Committee Report on pages 13 to 20.

Compensation of key management personnel is:

	Group	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Salaries and other short-term employee benefits	9	5
Post-employment benefits	5	5
Other	1	2
Total compensation of key management personnel	15	12

The 12-month equivalent figure for total compensation in 2004 is £11m.

(c) Transactions with and balances due from/to key management personnel

All transactions between the key management and the Group during the year are on commercial terms which are equivalent to those available to all employees of the Group.

The detailed disclosures of transactions with directors during the year and year-end balances arising from such transactions are contained within the audited section of the Remuneration Committee Report on pages 13 to 20.

During the period to 31 December 2005 key management personnel contributed £6.3m (2004 : £0.8m) to products sold by the Group. This primarily relates to investments in SIPP products with the transfer of funds from an external provider.

At 31 December 2005 key management personnel had outstanding loans of £39,592 (2004 : £75,857).

34. Related party transactions (continued)

(d) Company's related party transactions and balances

Transactions between the Company and its subsidiaries have been eliminated on consolidation. However, for presentation within the Company's separate financial statements, the following are details of significant transactions with related parties (including subsidiaries) during the year:

Such related party transactions are at arms length.

	Company	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Sales to:		
Subsidiaries - Insurance contracts	-	17
Subsidiaries	1,291	2,615
Associates, joint ventures and other related parties	4,719	4,278
Total sales	6,010	6,910
Purchases from:		
Subsidiaries - Investment contracts	547	273
Subsidiaries - Insurance contracts	24	-
Subsidiaries	18,042	1,097
Associates, joint ventures and other related parties	4,975	4,664
Total purchases	23,588	6,034

Amounts shown under 'Sales to: Subsidiaries' relate primarily to the disposal of and dividends received from subsidiary unit trusts.

Amounts shown under 'Purchases from: Subsidiaries' relate primarily to the transfer of holdings in bonds and property to unit trusts.

The year-end balances arising from transactions with related parties are as follows:

	Company	
	12 months to 31 December 2005 £m	13.5 months to 31 December 2004 £m
Due from related parties:		
Subsidiaries	1,555	1,369
Other related parties	119	97
Total due from related parties	1,674	1,466
Due to related parties:		
Subsidiaries	1,943	1,684
Total due to related parties	1,943	1,684

Amounts due to/from related parties include loans to/from subsidiaries, intercompany receivables/payables and amounts due from the defined benefit pension scheme.

35. Events after the Balance Sheet date

There are no significant post Balance Sheet date events.

36. Restructuring and demutualisation expenses

Included within administration expenses are restructuring and demutualisation expenses of £84m (2004 : £75m).

The 2005 expenses were mainly incurred in association with work undertaken preparing for the demutualisation and public listing of the Group in 2006 (£68m). A portion of the additional costs (£16m) relate to implementation of the 2004 strategic review, in particular redundancy costs.

The 2004 expenses were incurred in relation to the repositioning of UK L&P, focusing on more profitable lines of business. This resulted in expenditure of £45m, consisting mainly of redundancy and pension augmentation payments. The remaining costs were incurred as part of the strategic review and related mainly to redundancy costs, lease expiry costs and preliminary demutualisation costs.

37. Collateral

Collateral is accepted from and provided to certain market counterparties to mitigate counterparty risk in the event of default. The use of collateral in these circumstances is governed by formal bilateral agreements between the parties. The amount of collateral required by either party is calculated daily based on the value of derivative transactions in accordance with these agreements and collateral is moved on a daily basis to ensure there is full collateralisation. Any collateral moved under the terms of these agreements is transferred outright. With regard to either collateral pledged or accepted the Group may request the return of, or be required to return, collateral to the extent it differs from that required under the daily margin calculations. Furthermore alternative collateral may be provided if acceptable to both parties.

At the year-end, the Group had pledged £184m (2004 : £131m), of which the Company pledged £155m (2004 : £92m), of cash as collateral for liabilities.

At the year-end, the Group had accepted £1,801m (2004 : £434m) of cash and £6,900m (2004 : £1,684m) of securities as collateral of which the Company accepted £1,114m (2004 : £434m) of cash and £3,042m (2004 : £1,548m) of securities as collateral. Included within these amounts is collateral which has been accepted in relation to stock lending. At year-end the Group had accepted £1,749m (2004 : £367m) of cash and £6,878m (2004 : £1,681m) of securities in relation to stock lending. None of the above securities were sold or repledged at the year-end.

Where there is an event of default under the terms of the agreements, any collateral balances will be included in the close-out calculation of net counterparty exposure.

38. Fair value of financial assets and liabilities

The estimated carrying values and fair values of financial assets and liabilities are as follows:

	Notes	Group		Company	
		2005 Carrying value £m	2005 Fair value £m	2005 Carrying value £m	2005 Fair value £m
Financial assets					
Loans secured by mortgages	15	7,333	7,455	540	512
Loans secured by mortgages subject to securitisation	15	4,968	4,989	-	-
Financial liabilities					
Loan notes backing securitisations	24	4,025	4,041	-	-
Subordinated guaranteed bonds	25	1,032	1,169	1,032	1,169
Subordinated notes	25	267	277	-	-
Subordinated member accounts	25	579	588	579	588

	Notes	Group		Company	
		2004 Carrying value £m	2004 Fair value £m	2004 Carrying value £m	2004 Fair value £m
Financial assets					
Loans secured by mortgages	15	7,886	7,979	634	604
Loans secured by mortgages subject to securitisation	15	3,945	3,910	-	-
Financial liabilities					
Loan notes backing securitisations	24	3,204	3,358	-	-
Subordinated guaranteed bonds	25	1,047	1,154	1,047	1,154
Subordinated member accounts	25	553	578	553	578

The estimated fair values are calculated by discounting the expected future cash flows at current market rates.

It is not possible to reliably calculate the fair value of investment contract liabilities because any fair value measurement would have to include a share of the unallocated divisible surplus. The assumptions and methods used in the calculation of these liabilities are set out in the accounting policies and Note 20. The carrying value of investment contract liabilities at the 31 December 2005 was £59,005m (2004 : £46,526m).

The carrying value of all other financial assets and liabilities approximates their fair value.

39. UK GAAP Restatement

On conversion from UK GAAP to IFRS a number of prior period errors, that in aggregate are considered material, were identified. The impact of these items on the transfer to unallocated divisible surplus in 2004 was a decrease of £170m. The total impact on the Balance Sheet and Income Statement is shown below.

The comparative amounts for certain line items have been restated to correct errors in the 2004 and 2003 UK GAAP financial statements. The result of the restatement is an increase to unallocated divisible surplus of £17m in 2004 and £194m in 2003 prior to conversion to IFRS. This includes a foreign exchange impact of £7m in 2004.

The comparative amounts for deferred tax expense and deferred tax liability in 2004 have been restated to correct errors in the taxation calculations for the Canadian structured settlement business and technical provisions. The tax effect of all corrections is a decrease in deferred tax assets of £133m and a decrease in deferred tax liabilities of £71m.

The comparative amounts for Canadian insurance contract liabilities and change in insurance contracts liabilities have been restated to correct an error in the calculation of reserves to reflect the UK GAAP value of Canadian assets and the corresponding increase to insurance liabilities and to correct an error of omission of certain liabilities. The result of this restatement is a decrease in insurance contracts liabilities of £20m in 2003 and an increase of £109m in 2004.

The comparative amounts as at December 2003 for investment contract liabilities have been reduced and the unallocated divisible surplus increased by £188m to reflect errors in respect of processing issues in the liability systems.

The effect of these restatements on the 2003 and 2004 financial statements is as follows:

	Effect on 2004	Effect on 2003
	£m	£m
Income Statement*		
Increase in change in insurance contract liabilities	(125)	-
Decrease in operating result before tax	(125)	-
Increase in income tax expense	(45)	-
Decrease in transfer to unallocated divisible surplus	(170)	-
Balance Sheet		
Decrease in deferred tax assets	(133)	-
(Increase)/decrease in deferred tax liabilities	71	(14)
(Increase)/decrease in insurance contract liabilities	(109)	20
Decrease in investment contract liabilities	188	188
Increase in unallocated divisible surplus	17	194

* The restatement of the 2003 Income Statement is not required.

40. Capital statement

The Financial Services Authority (FSA) requires all insurance companies to maintain Capital Resources (CR) in excess of their Capital Resources Requirement (CRR). Capital Resources comprise assets in excess of liabilities, valued on a regulatory basis. Also, certain items that are classified as liabilities in the Balance Sheet such as subordinated guaranteed bonds and members' accounts, are included as components of Capital Resources. The Capital Resources Requirement represents the total of the Individual Capital Resources Requirement (ICRR) of each regulated company in the Group.

The Company is a mutual organisation and is the principal insurance company in the Group. It's with profits fund owns all the subsidiaries of the Group. All business, including non-participating business, is written within this fund. The Capital Resources of the regulated subsidiaries are included when calculating the Company's Capital Resources and Capital Resources Requirement, and the Company's capital supports the Group's business. For these reasons the Group's capital position is presented below in a single column.

	Group	
	2005	2004
	£m	£m
Available capital resources		
Unallocated divisible surplus	4,827	3,678
Adjustments onto regulatory basis		
<i>Changes to the valuation of contract liabilities</i>	2,012	476
<i>Exclusion of the present value of future results on non-participating contracts</i>	(1,528)	(1,041)
<i>Exclusion of deferred acquisition costs and other inadmissible assets</i>	(347)	(276)
<i>Exclusion of deferred income</i>	223	221
<i>Changes to the valuation of other assets and liabilities</i>	(191)	391
	169	(229)
Other qualifying capital		
<i>Subordinated guaranteed bonds</i>	1,032	971
<i>Subordinated members' accounts</i>	579	548
<i>Subordinated notes</i>	263	-
<i>Implicit item for future profits</i>	200	500
	2,074	2,019
Total available Capital Resources to meet regulatory requirement	7,070	5,468
<i>Life capital not subject to constraints</i>	4,667	3,800
<i>Other capital available to meet the requirement of the life assurance business</i>	1,518	1,234
<i>Capital readily available to meet the requirement of the life assurance business</i>	6,185	5,034
<i>Other capital not available to meet the requirement of the life assurance business</i>	381	68
	6,566	5,102
<i>Life capital subject to constraints</i>	504	366
Total available Capital Resources	7,070	5,468
Regulatory Capital Resources Requirement	2,898	2,513
Excess of available Capital Resources over regulatory requirement	4,172	2,955
Analysis of contract liabilities		
Participating		
<i>Insurance contracts</i>	19,633	18,264
<i>Investment contracts</i>	18,076	15,929
	37,709	34,193
Unit linked		
<i>Insurance contracts</i>	2,486	1,958
<i>Investment contracts</i>	38,503	28,483
	40,989	30,441
Other non-participating		
<i>Insurance contracts</i>	18,672	16,896
<i>Investment contracts</i>	2,426	2,114
	21,098	19,010
	99,796	83,644
Total contract liabilities in Balance Sheet		
<i>Life</i>	99,678	83,482
<i>Non-life</i>	118	162
	99,796	83,644

40. Capital statement (continued)

The Company's regulatory solvency position is determined using the FSA's "twin peaks" approach, which requires liabilities to be valued on both a realistic and a regulatory basis. The realistic basis removes some of the margins for prudence included in calculations under the regulatory basis. However, it requires discretionary benefits that are not considered under the regulatory basis, such as final bonuses, to be valued. Essentially, the higher of these two peaks is used to determine the Capital Resources Requirement. At 31 December 2005, the regulatory peak exceeded the realistic peak by £791m (2004 : £919m).

In addition to the requirement to maintain Capital Resources in excess of its Capital Resources Requirement, the FSA requires that each regulated company in the Group identifies the major risks it faces and, if appropriate, quantifies the amount and type of capital it believes is appropriate to mitigate those risks. This individual capital assessment reflects the company's own view of the adequacy of its Capital Resources. The determination of the liabilities includes various actuarial and other assumptions including potential changes in market conditions and the actions management might take as a result of those changes.

Changes in market conditions and other variables have the potential to affect significantly the capital position. Poor investment returns would depress Capital Resources, but this could be mitigated by changing the asset portfolio and by the level of bonuses declared. Future annuitant mortality could be significantly different from that assumed in the calculation of the liabilities. The interaction between the 'twin peaks' under the FSA's approach and European Union developments on solvency requirements could also have a significant impact on the future capital position.

The non-life Capital Resources exceed the Capital Resources Requirement for the non-life business by £1,518m (2004 : £1,234m), and can therefore be used to meet the requirements of the life assurance business.

The Group, through subsidiaries and joint ventures, provides insurance and other financial services in the UK, Canada, India and China, and through branches provides such services in Canada, Ireland and Germany. There are no formal arrangements to provide capital to particular funds or business units. Any allocations of capital would need to be approved on a case-by-case basis by the Board.

The Capital Resources of the Canadian branch are subject to constraints. Canadian legislation requires sufficient assets to be held in trust by an external Canadian financial institution to provide an adequate margin of those assets over Canadian liabilities. Consequently the total Capital Resources are not readily available to meet all the requirements of the Group.

Contract liabilities

The process used to determine the assumptions that have the greatest effect on the measurement of contract liabilities (including options and guarantees), the quantified disclosure of those assumptions, and the terms and conditions of options and guarantees relating to life assurance contracts that could in aggregate have a material effect on future cash flows are disclosed in Note 20.

The sensitivity of contract liabilities to changes in market conditions, key assumptions and other variables, and assumptions about management actions in response to changes in market conditions, are disclosed in Note 22.

40. Capital statement (continued)

Movements in capital

The movement in the total Capital Resources includes the investment surplus, new business strains and changes in regulatory requirements.

The investment surplus arises from changes in market conditions, and reflects the total returns earned on the assets compared with the valuation interest rates previously assumed. It also reflects the change in the yield currently available on the assets and therefore the current valuation interest rates, and the differences in the assumptions under the resilience tests.

Strains of writing new business and supporting bonus rates arise under the regulatory peak. An example of where a strain can result is where the maturity value is in excess of the provision that is included in the Balance Sheet.

There have been no changes in management policy during the year. Changes in assumptions used to measure contract liabilities and other items have no significant impact on Capital Resources.

The Capital Resources at 31 December 2004 were based on the UK GAAP financial statements as published prior to the UK GAAP restatement set out in Note 39. The unallocated divisible surplus represents the amount included in the IFRS financial statements after the UK GAAP restatement. Consequently, each adjustment onto regulatory basis in the table above reflects an element of restatement of the unallocated divisible surplus to the amount included in the UK GAAP financial statements at 31 December 2004. This restatement accounts for £305m of the 'changes to other assets and liabilities' in the table above.

Regulatory requirements have changed with regard to the treatment of Standard Life Bank in the calculation of Capital Resources. Transitional rules were applied at 31 December 2004, that resulted in the assets and liabilities of this subsidiary being included at the carrying value included in its financial statements and its Individual Capital Resources Requirement not forming part of the Capital Resources Requirement. At 31 December 2005, the assets and liabilities of Standard Life Bank have been reflected in Capital Resources on a regulatory basis, and its Individual Capital Resources Requirement forms part of the Capital Resources Requirement.

Capital management policies and risk management objectives

Managing capital is the on-going process of determining and maintaining the quantity and quality of capital appropriate for the Group, and ensuring capital is deployed in a manner consistent with the expectations of the Group's stakeholders. For these purposes, the Group considers our key stakeholders to be the FSA and the providers of capital (our members and holders of our subordinated liabilities).

There are two primary objectives of capital management within the Group. The first objective is to ensure that capital is, and will continue to be, adequate to maintain the required level of safety and stability of the Group and hence to provide an appropriate degree of security to our customers. The second objective is to support the development of the business by ensuring that the returns generated on capital investment are sufficient to provide adequate compensation to the providers of capital, after allowing for the risks to which that capital is exposed.

The capital requirements of each business unit are routinely forecast on a periodic basis, and the requirements are assessed against both the forecast available capital and the internal rate of return expected to be achieved from planned activities. In addition, internal rates of return achieved on capital invested are assessed against hurdle rates, which are intended to represent the minimum acceptable return given the risks associated with each investment.

The capital planning process is the responsibility of the Group Actuarial Director; capital plans are ultimately subject to approval by the Board.

The formal procedures for identifying and assessing risks that could affect the capital position of the Group are described in the risk management policies set out in Note 31.

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27)

(a) Group reconciliation of the Consolidated Balance Sheet at 31 December 2004 and 16 November 2003

	31 December 2004			16 November 2003		
	As reported under UK GAAP Restated £m	Adjustments £m	IFRS £m	As reported under UK GAAP Restated £m	Adjustments £m	IFRS £m
Assets						
Intangible assets	-	27	27	-	16	16
Deferred acquisition costs	1,352	(1,083)	269	1,063	937	2,000
Investments in associates and joint ventures	296	1,595	1,891	644	1,188	1,832
Investment property	-	8,779	8,779	-	7,094	7,094
Property and equipment	5,477	(4,778)	699	5,340	(4,806)	534
Deferred tax assets	123	(80)	43	164	(58)	106
Reinsurance assets	641	(24)	617	539	16	555
Loans and receivables	9,940	2,231	12,171	9,215	1,792	11,007
Derivative financial assets	-	230	230	-	253	253
Investment securities						
Equity securities and interests in pooled investment funds	15,986	19,508	35,494	21,376	15,645	37,021
Debt securities	30,041	7,521	37,562	21,405	6,426	27,831
	46,027	27,029	73,056	42,781	22,071	64,852
Assets held to cover linked liabilities	33,366	(33,366)	-	27,134	(27,134)	-
Other debtors	1,858	(466)	1,392	1,482	31	1,513
Cash and cash equivalents	109	2,731	2,840	203	2,781	2,984
Total assets	99,189	2,825	102,014	88,565	4,181	92,746
Minority interest	145	105	250	74	65	139
Liabilities						
Non-participating contract liabilities						
Non-participating insurance contracts*	-	18,854	18,854	-	-	-
Non-participating investment contracts*	-	30,597	30,597	-	-	-
	-	49,451	49,451	-	-	-
Participating contract liabilities						
Participating insurance contracts*	-	18,264	18,264	-	-	-
Participating investment contracts*	-	15,929	15,929	-	-	-
Present value of future results on non- participating contracts*	-	(1,041)	(1,041)	-	-	-
Unallocated divisible surplus	4,473	(795)	3,678	4,474	418	4,892
	4,473	32,357	36,830	4,474	418	4,892
Insurance contract liabilities	83,951	(83,951)	-	74,622	(39,404)	35,218
Investment contract benefits	-	-	-	-	38,816	38,816
Third party interest in consolidated funds	-	77	77	-	50	50
Borrowings	3,280	2,421	5,701	2,573	2,162	4,735
Subordinated liabilities	1,519	81	1,600	970	60	1,030
Pension and other post retirement benefit provisions	-	472	472	-	428	428
Deferred income	244	(10)	234	219	13	232
Deferred tax liabilities	337	91	428	266	205	471
Current tax liabilities	68	32	100	138	10	148
Customer accounts related to banking activities and deposits by banks	4,262	885	5,147	4,577	276	4,853
Derivative financial liabilities	-	358	358	-	535	535
Other liabilities	910	456	1,366	652	547	1,199
Total liabilities and minority interest	99,189	2,825	102,014	88,565	4,181	92,746

* The Group is not required to restate the Balance Sheet as at 16 November 2003 for FRS 27.

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27) (continued)

Group analysis of adjustments to the Consolidated Balance Sheet as at 31 December 2004

	Investments and loans valuation	Investment contract liabilities	Insurance contract liabilities	Employee benefits	Consolidation of additional entities	Unit linked asset	DAC & DIR	Deferred taxation	Other adjust ments	Sub total	Adoption of FRS 27	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets												
Intangible assets	-	-	-	-	-	-	-	-	27	27	-	27
Deferred acquisition costs	-	-	-	-	-	-	-	-	-	-	-	-
Investments in associates and joint ventures	(10)	-	-	-	1,080	525	705	-	-	705	(1,788)	(1,083)
Investment property	-	-	-	-	434	3,534	-	-	-	1,595	-	1,595
Property and equipment	10	-	-	-	(68)	158	-	-	4,811	8,779	-	8,779
Deferred tax assets	-	-	-	-	-	-	-	(27)	(4,878)	(4,778)	-	(4,778)
Reinsurance assets	-	-	-	-	-	-	-	-	-	(27)	(53)	(80)
Loans and receivables	164	-	(30)	-	3,181	428	-	-	(1,542)	(30)	6	(24)
Derivative financial assets	205	-	-	-	19	6	-	-	-	2,231	-	2,231
Investment securities	-	-	-	-	-	-	-	-	-	230	-	230
Equity securities and interests in pooled investment funds	468	-	20	-	(1,487)	21,038	-	-	(531)	19,508	-	19,508
Debt securities	(779)	-	-	-	323	8,048	-	-	(71)	7,521	-	7,521
Assets held to cover linked liabilities	-	-	-	-	-	(33,366)	-	-	-	(33,366)	-	(33,366)
Other debtors	(156)	-	-	-	38	84	-	-	(432)	(466)	-	(466)
Cash and cash equivalents	1	-	-	-	279	307	-	-	2,144	2,731	-	2,731
Total assets	(97)	-	(10)	-	3,799	762	705	(27)	(472)	4,660	(1,835)	2,825
Minority interest	-	-	-	-	105	-	-	-	-	105	-	105
Liabilities												
Non-participating contract liabilities	-	-	-	-	-	-	-	-	-	-	-	-
Non-participating insurance contracts	-	-	-	-	-	-	-	-	-	-	18,854	18,854
Non-participating investment contracts	-	-	-	-	-	-	-	-	-	-	30,597	30,597
Participating contract liabilities	-	-	-	-	-	-	-	-	-	-	-	-
Participating insurance contracts	-	-	-	-	-	-	-	-	-	-	-	-
Participating investment contracts	-	-	-	-	-	-	-	-	-	-	-	-
Present value of future results on non-participating contracts	-	-	-	-	-	-	-	-	-	-	-	-
Unallocated divisible surplus	(116)	464	21	(274)	-	-	346	(245)	88	284	(1,041)	(1,041)
Insurance contract liabilities	-	(2)	(19,825)	-	-	(27,753)	112	-	(2)	(47,470)	(36,481)	(795)
Investment contract benefits	-	(462)	19,658	(183)	-	27,823	-	-	(82)	46,754	(46,754)	-
Third party interest in consolidated funds	-	-	-	-	77	-	-	-	-	77	-	77
Borrowings	(1,000)	-	-	-	3,470	6	-	-	(55)	2,421	-	2,421
Subordinated liabilities	-	-	-	-	81	-	-	-	-	81	-	81
Pension and other post retirement benefit provisions	-	-	-	472	-	-	-	-	-	472	-	472
Deferred income	-	-	-	-	3	-	(13)	-	-	(10)	-	(10)
Deferred tax liabilities	-	-	-	-	6	5	-	209	(5)	215	(124)	91
Current tax liabilities	-	-	-	-	1	25	-	6	-	32	-	32
Customer accounts related to banking activities and deposits by banks	909	-	-	-	-	-	-	-	(24)	885	-	885
Derivative financial liabilities	358	-	-	-	-	-	-	-	-	358	-	358
Other liabilities	(248)	-	136	(15)	56	656	260	3	(392)	456	-	456
Total liabilities and minority interest	(97)	-	(10)	-	3,799	762	705	(27)	(472)	4,660	(1,835)	2,825

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27) (continued)

Group analysis of adjustments to the Consolidated Balance Sheet as at 16 November 2003

	Investments and loans valuation £m	Investment contract liabilities £m	Insurance contract liabilities £m	Employee benefits £m	Consolidation of additional entities £m	Unit linked asset £m	DAC & DIR £m	Deferred taxation £m	Other adjustments £m	Total £m
Assets										
Intangible assets	-	-	-	-	-	-	-	-	16	16
Deferred acquisition costs	-	-	-	-	-	-	937	-	-	937
Investments in associates and joint ventures	(7)	-	-	-	738	457	-	-	-	1,188
Investment property	-	-	-	-	-	2,034	-	-	5,060	7,094
Property and equipment	(4)	-	-	-	(43)	37	-	-	(4,796)	(4,806)
Deferred tax assets	-	-	-	-	-	19	-	(77)	-	(58)
Reinsurance assets	-	-	-	-	-	8	-	-	-	16
Loans and receivables	12	-	8	-	-	655	-	-	(1,209)	1,792
Derivative financial assets	249	-	-	-	-	4	-	-	-	253
Investment securities	-	-	-	-	2,334	-	-	-	-	-
Equity securities and interests in pooled investment funds	503	-	-	-	(802)	16,669	-	-	(725)	15,645
Debt securities	(557)	-	-	-	-	7,234	-	-	(251)	6,426
Assets held to cover linked liabilities	-	-	-	-	-	(27,134)	-	-	-	(27,134)
Other debtors	(111)	-	-	-	92	189	-	5	(144)	31
Cash and cash equivalents	2	-	-	-	424	327	-	-	2,028	2,781
Total assets	87	-	8	-	2,743	499	937	(72)	(21)	4,181
Minority interest	-	-	-	-	65	-	-	-	-	65
Liabilities										
Insurance contract liabilities	-	-	(18,278)	-	-	(21,231)	105	-	-	(39,404)
Investment contract benefits	-	(380)	18,041	(165)	-	21,289	-	-	31	38,816
Unallocated divisible surplus	(234)	380	91	(245)	-	-	583	(278)	121	418
Third party interest in consolidated funds	-	-	-	-	50	-	-	-	-	50
Borrowings	(312)	-	-	-	2,451	-	-	-	23	2,162
Subordinated liabilities	7	-	-	-	53	-	-	-	-	60
Pension and other post retirement benefit provisions	-	-	-	428	-	-	-	-	-	428
Deferred income	(71)	-	-	-	-	-	97	-	(13)	13
Deferred tax liabilities	-	-	-	-	-	-	-	205	-	205
Current tax liabilities	-	-	-	-	4	3	-	3	-	10
Customer accounts related to banking activities and deposits by banks	276	-	-	-	-	-	-	-	-	276
Derivative financial liabilities	535	-	-	-	-	-	-	-	-	535
Other liabilities	(114)	-	154	(18)	-	438	152	(2)	(183)	547
Total liabilities and minority interest	87	-	8	-	2,743	499	937	(72)	(21)	4,181

* The Group is not required to restate the Balance Sheet as at 16 November 2003 for FRS 27.

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27) (continued)

(b) Group reconciliation of the consolidated Income Statement for the period ended 31 December 2004

	2004		
	As reported under UK GAAP Restated £m	Adjustments £m	IFRS £m
Revenue			
Gross earned premium	10,219	(5,868)	4,351
Premium ceded to reinsurers	(109)	13	(96)
Net earned premium	10,110	(5,855)	4,255
Net investment return	9,167	725	9,892
Income arising from associates and joint ventures	-	86	86
Fee and commission income	-	296	296
Other income	790	(742)	48
Total net revenue	20,067	(5,490)	14,577
Expenses			
Claims and benefits paid	8,097	(2,985)	5,112
Claim recoveries from reinsurers	(53)	(8)	(61)
Change in reinsurance assets	-	(41)	(41)
Change in insurance and participating liabilities	10,277	(7,437)	2,840
Change in investment contract liabilities	-	3,912	3,912
Administration expenses			
Restructuring and demutualisation expenses	75	-	75
Other administration expenses	1,149	1,124	2,273
	1,224	1,124	2,348
Change in liability for third party interest in consolidated funds	-	16	16
Operating expenses	19,545	(5,419)	14,126
Finance costs	80	-	80
Result before tax	442	(71)	371
Tax expense/(benefit)	369	(16)	353
Transfer to/(from) unallocated divisible surplus	41	(56)	(15)
Increase in net assets attributable to minority interest	32	1	33
Balance on the Income Statement	-	-	-

The result after tax for the period of £33m represents the increase in net assets attributable to minority interest.

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27) (continued)

Reconciliation of the Company unallocated divisible surplus as at 16 November 2003 and 31 December 2004

	16 November 2003 FFA / UDS £m	Transfer to UDS £m	Foreign currency translation £m	Pensions reserve £m	Revaluation reserve £m	FRS 27 £m	Other £m	31 December 2004 FFA / UDS £m
As reported under UK GAAP								
Prior year adjustment	(4,280)	(211)	35	-	-	-	-	(4,456)
Restated UK GAAP	(189)	170	7	-	-	-	-	(12)
	(4,469)	(41)	42	-	-	-	-	(4,468)
Adjustments								
Investments and loans valuation	286	(172)	-	-	-	-	-	114
Investment contract liabilities	(380)	(73)	-	-	-	-	-	(453)
Insurance contract liabilities	(91)	70	-	-	-	-	-	(21)
Employee benefits	245	(8)	-	37	-	-	-	274
Deferred acquisition costs and deferred income	(583)	237	-	-	-	-	-	(346)
Deferred taxation	275	(1)	-	-	-	-	-	274
Other	(97)	(6)	8	-	(16)	-	(5)	(116)
Adoption of FRS 27	-	-	(4)	-	-	1,016	-	1,012
	(4,814)	6	46	37	(16)	1,016	(5)	(3,730)

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27) (continued)

Explanation of reconciling items between UK GAAP and IFRS

The UK GAAP Balance Sheet and Income Statement has been presented in a format consistent with International Financial Reporting Standards (IFRS). Each of the significant adjustments is described below.

Investments and loans valuation

Under UK GAAP listed investments are valued at fair value using a mid-market value. Under IFRS listed investments are designated at fair value through profit or loss and valued at fair value using the bid price.

Unlisted investment securities were previously stated at directors' valuation under UK GAAP. Under IFRS, unlisted securities are designated at fair value through profit or loss and are required to be valued at fair value using a technique that complies with the requirements of IAS 39. The value of unlisted investments has been amended where the directors' valuation was not consistent with the IAS fair value.

Under IFRS, loans and receivables, subordinated debt and borrowings are carried at amortised cost as calculated using the effective interest rate ('EIR') method. This method effectively records through net interest income, a constant return over the relevant period of lending transactions. It spreads components such as interest, discounts, and fees payable/receivable over the effective life of the loan. These items have been adjusted to the extent that the UK GAAP measurement basis differed from that prescribed under IFRS.

Derivatives were previously valued on either an amortised cost basis or at the mid-market price under UK GAAP. In addition, many derivatives were netted off against their associated hedged items. Under IFRS, all derivatives are required to be held at their fair value. Netting is also specifically prohibited. Where derivatives were used to hedge risks on a cash flow basis under UK GAAP, the transitional arrangements contained in IFRS1 have been applied. The cash flow hedge reserve was therefore brought onto the transitional Balance Sheet in 2003 and recycled through the profit and loss account during 2004.

On a Group basis these adjustments have resulted in a decrease in UDS of £116m as at 31 December 2004 (2003 : £234m). The net profit transferred to UDS increased by £123m for the period ended 31 December 2004. £5m was released from the cash flow hedge reserve in 2004. For the Company the impact was a decrease in UDS of £114m at 31 December 2004 (2003 : £286m) with a £172m increase in the transfer to UDS for the period ended 31 December 2004.

Investment contract liabilities

Product classification

Under UK GAAP all contracts written by an insurance company are accounted for on a similar basis. IFRS 4 requires products to be classified for accounting purposes as either insurance or investment contracts depending on whether there has been a transfer of significant insurance risk. Insurance contracts and those that have a discretionary participating feature continue to be accounted for using UK GAAP. Under IFRS, non-participating investment contract liabilities are measured at either amortised cost or at fair value (in the case of linked liabilities).

Accounting for non-participating investment contracts

Under UK GAAP the liability under unit linked contracts is equal to the market value of the underlying linked assets plus a prudential regulatory reserve. Under IFRS these liabilities are carried at fair value and continue to be measured on a basis that is consistent with the valuation of the underlying assets. Consequently, under IFRS the unit linked liability is calculated as the fair value of the underlying assets on a bid value basis but excludes any prudential reserves.

The Group measures non-linked non-participating investment contract liabilities at amortised cost using the effective interest rate method. An adjustment is required to the extent that the UK GAAP valuation basis is not compliant with the IFRS amortised cost basis.

These adjustments have resulted in an increase in UDS of £464m for Group and £453m for Company as at 31 December 2004 (2003 : £380m for Group and Company). The net profit transferred to UDS increased by £84m for Group and £73m for the Company for the period ended 31 December 2004.

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (including FRS 27) (continued)

Deposit accounting

Under UK GAAP all premiums receivable and claims payable are recognised in the Income Statement (revenue accounting). IFRS requires the application of deposit accounting whereby amounts receivable under Investment contracts without DPF are no longer shown as premiums in the Income Statement but are treated as deposits and added to investment contract liabilities in the Balance Sheet. Similarly claims payable on Investment contracts without DPF are no longer shown as claims in the Income Statement but treated as a repayment of a deposit and are accounted for as a reduction in the investment contract liability in the Balance Sheet. The impact is to reduce income and expenses by £5,595m. There is no impact to UDS.

Insurance contract liabilities

Under UK GAAP insurance contracts and participating investment contracts are valued using a prospective discounted cash flow basis. The discount rate applied to contractual cash flows is determined on a basis that is consistent with the valuation of the assets backing the contracts. Under IFRS the backing assets are measured on a different basis than under UK GAAP and therefore a corresponding adjustment is made to the liabilities.

The effect of this adjustment has resulted in an increase in UDS of £21m for Group and Company as at 31 December 2004 (2003 : £91m). The net profit transferred to UDS decreased by £70m for the period ended 31 December 2004.

Employee benefits

Under UK GAAP the expected cost of providing pension obligations over the projected period of the employees' service was recognised in the Income Statement. There was no upfront recognition of the pension fund deficit in the Balance Sheet. Under IFRS, the defined benefit pension deficit is recognised as a liability in the Group's Balance Sheet. The amount recognised is the present value of the defined benefit obligation reduced by the fair value of scheme assets. Certain assets (which are classified as non-transferable financial instruments) do not meet the definition of plan assets and are not deducted from the pension scheme obligation; however, they are offset by a reduction to the corresponding liability to the scheme. This has the effect of increasing the headline pension deficit balance by £181m on a Group and Company basis but does not impact the UDS. For 2005 onwards a transferability agreement was put in place for UK and Ireland, this recognises all of the assets backing the pension obligation as plan assets thereby reducing the headline pension deficit balance.

The Group has elected to recognise all actuarial gains and losses outside of the Income Statement in the Statement of Recognised Income and Expense. The amount recognised as Pensions and other post retirement benefit provisions on a Group basis comprises the following:

	2004 £m
Gross pension obligation included in pensions and other post retirement benefit provisions	472
Non-transferable financial assets backing obligations	(181)
Defined benefit pension scheme deficit	291

On a Group and Company basis, recognition of the defined benefit pension scheme deficit, net of tax, resulted in a decrease in the UDS at 31 December 2004 of £274m (2003 : £245m). The pension liability recognised for Group and Company was £472m and £348m respectively at 31 December 2004 (2003 : £428m and £423m). Actuarial losses recognised in the Statement of Recognised Income and Expense for Group and Company at 31 December 2004 were £42m and £37m respectively and the adjustment resulted in £13m of additional expenses in the Income Statement for Group and £8m for Company.

Consolidation of additional entities

IFRS requires the consolidation of certain other investment vehicles which did not require consolidation under UK GAAP. This is due to a stricter definition of when an entity is deemed to be under the control of an investor. The Group now consolidates several open-ended investment companies, unit trusts and other investment vehicles on a line-by-line basis.

Under IFRS, joint ventures and associates are accounted for using the equity method of accounting. The effect of the adjustments is the reclassification and recognition of Investments in Associates and Joint Ventures of £1,080m (2003 : £738m) and an additional share of profit after tax of associates and joint ventures of £72m being recognised for the period ended 31 December 2004.

41. Reconciliations of Balance Sheet and Income Statement reported under UKGAAP and IFRS (including FRS 27) (continued)

Unit linked asset explosion

Assets held to cover linked liabilities of £33,550m (2003 : £27,318m) are no longer disclosed in the single line 'Assets held to cover linked liabilities' but are consolidated on a line-by-line basis under IFRS. This has resulted in the recognition of additional debt securities and equity securities of £8,048m and £21,038m respectively (2003 : £7,234m and £16,669m). There is no impact on UDS as a result of this change.

Linked liabilities are also separately disclosed according to the nature of the contract, being insurance or investment contract liabilities.

Deferred acquisition costs (DAC) and deferred income reserve (DIR)

Under UK GAAP front-end fees on investment management service contracts are recognised as received. IFRS requires these fees to be recognised as services are provided over the life of the contract. Therefore under IFRS an explicit deferred income reserve is recognised for any front-end fees received that relate to services to be provided in future periods.

Incremental costs that directly relate to the cost of acquiring new investment management business are deferred as an asset and amortised in line with the associated revenue as the services are provided.

Both the life and pensions and investment management segments contain investment management service contracts.

The Group has elected to make certain improvements to its accounting for deferred acquisition costs. Under the revised policy all costs associated with acquisition are deferred and deferral extends to single as well as regular premium business.

Overall the net impact of the DAC/DIR adjustment for Group and Company is an increase to UDS of £346m as at 31 December 2004 (2003 : £583m). The net profit transferred to UDS decreased by £237m for the period ended 31 December 2004.

Deferred taxation

IFRS requires deferred tax to be calculated on temporary differences rather than timing differences under UK GAAP. Under IFRS where any asset or liability has a temporary timing difference and that temporary timing difference is increased or decreased in the IFRS financial statements by making an adjustment to its carrying value on transition to IFRS, then an adjustment will be required to deferred tax provisions recognised in the UK GAAP financial statements. Furthermore, IAS 12 does not permit discounting of deferred tax provisions whereas UK GAAP did.

The net impact of these adjustments on the Group is a decrease in the UDS at 31 Dec 2004 of £245m (2003 : £278m). The net profit transferred to UDS increased by £29m for the period ended 31 December 2004 and the tax effect of adjustments taken directly to UDS is £4m. The impact on the Company is to decrease UDS by £274m at 31 Dec 2004 (2003 : £275m) which results in a £1m increase in the transfer to UDS.

Other adjustments

The other adjustments that arise as a result of the transition to IFRS include the following:

- Software development costs that meet the requirements for recognition as an intangible asset under IFRS must be capitalised and recognised as an intangible asset. Under UK GAAP the Group had been writing off development expenditure in the year of the expenditure. The UDS has increased by £24m (2003 : £13m) as a result.
- The Group has opted to reclassify some of its properties as investment properties, which are shown as a separate asset component in the IFRS financial statements and are held at fair value under IFRS. Fair value is determined without any deduction for transaction costs. Gains or losses arising from changes in fair value are accounted for in income rather than through the revaluation reserves as under UK GAAP. Owner-occupied properties under UK GAAP were valued on a vacant possession basis whereas under IFRS they are valued at fair value. The effect of the property valuation has resulted in an increase in UDS of £84m (2003 : £80m).

41. Reconciliations of Balance Sheet and Income Statement reported under UK GAAP and IFRS (continued)

- Under IFRS lease incentives are recognised as a reduction in rental income over the lease term. Since the Group are acting as lessors, payment of the lease incentive is recognised as an asset and the cost of the incentive as a reduction of rental income over the lease term on a straight-line basis. UK GAAP requires incentives to be spread over the shorter of the lease term and a period ending on a date on which the rent is first adjusted to prevailing market rates. The effect of this has resulted in an increase in UDS of £31m (2003 : £28m).
- 'Cash equivalents' is a newly defined term under IFRS and results in more assets falling into the scope of 'Cash and Cash Equivalents'. Approximately £2bn of assets has been classified into Cash and Cash Equivalents in both 2003 and 2004.
- All Group entities that have a functional currency different from the Group presentation currency are translated as follows:
 - assets and liabilities for each balance are translated at the closing rate at Balance Sheet date. This means that the opening balances are retranslated at closing rate to obtain the exchange difference between opening and closing rate;
 - income and expenses are translated at average exchange rates.The translation differences are recognised in a separate component of equity, known as the translation reserve.
The Group has taken advantage of the exemption on first-time adoption of IFRS that permits it to not recalculate the cumulative translation reserve at the date of transition. As a result the opening reserve at transition date is reset to zero. The impact of the adjustment is to decrease UDS by £51m at 31 December 2004.

The overall impact of the above adjustments on the Company is an increase in UDS of £116m as at 31 December 2004 (2003 : £97m).

Explanation of material adjustments to the Cash Flow Statement for 2004

In the financial statements prepared under UK GAAP, Standard Life availed itself of the exemption outlined in paragraph 5(b) of FRS 1 *Cash Flow Statements* and consequently no Cash Flow Statement was presented. A full Cash Flow Statement is presented in these financial statements for the period ended 31 December 2004 and 2005 for IFRS.

Adoption of FRS 27

As explained in the accounting policies, insurance contracts and participating investment contracts are accounted for using accounting policies that were applied prior to the transition to IFRS. As permitted by IFRS 4 an improvement to these policies has been reflected in these financial statements. This improvement relates to the implementation of the UK accounting standard FRS 27 *Life Assurance* which deals with accounting for liabilities to policyholders under participating contracts. As acknowledged within FRS 27 its retrospective application is difficult. The Group has assessed that it is impracticable to restate the Balance Sheet at 16 November 2003 and the Income Statement for the period to 31 December 2004 for the impact of FRS 27. The Balance Sheet at 31 December 2004 has been restated.

In accordance with FRS 27 participating contract liabilities are determined on a realistic basis and are reduced by the PVFP on non-participating contracts written in the with profits fund. DAC is only held on non-participating investment contracts to the extent of the DIR recognised. This has resulted in an increase in participating contract liabilities of £409m and a reduction in deferred acquisition costs of £1,788m at 31 December 2004. The participating contract liabilities are offset by the present value of future profits on non-participating contracts of £1,041m. The effect of these adjustments is to decrease deferred tax liabilities by £124m and deferred tax assets by £53m, offset by an increase to reinsurance assets of £6m. Corresponding amounts have been adjusted to the unallocated divisible surplus in accordance with FRS 27 resulting in a decrease of £1,079m at 31 December 2004 for Group. The impact for Company is a decrease to unallocated divisible surplus of £1,012m at 31 December 2004. FRS 27 requires insurance contracts to be classified into their participating and non-participating components and reflected as such on the Balance Sheet. A presentational adjustment has been made to reflect this classification for insurance and investment contracts.

FRS 27 requires cost of guarantees to be valued on a fair value approach. FRS 27 permits the PVFP on the non-participating business written within the with profits fund to be deducted from the realistic liability as this value is included within the realistic liability calculation.

42. Domestication of Canadian non-participating business

On 31 December 2004 substantially all of the non-participating liabilities of The Standard Life Assurance Company Canadian Branch were assumed by The Standard Life Assurance Company of Canada (SLCC), a wholly owned subsidiary undertaking of The Standard Life Assurance Company. Most of the remaining non-participating business of the Branch was reinsured with SLCC on 31 December 2004. All Canadian participating business has remained in the Branch and has not been assumed or reinsured by SLCC.

SLCC issued shares and subordinated debt in exchange for the domesticated business. This is reflected by a corresponding increase in the value of the investment recognised by The Standard Life Assurance Company in respect of this subsidiary.

43. Undated intercompany financial instrument

The Company entered into loan agreements during the year to borrow US\$397m and US\$13m. The balance outstanding at year end was £245m. The payment of the principal and interest in respect of these loan agreements is at the full discretion of the Company, therefore the loan agreements have been classified as equity instruments.