

Registered Number 48340

**Legal & General Reinsurance Company Limited**  
**Report and Accounts 2016**

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## Company Information

### Board of Directors

Kerrigan Procter (Chairman)	appointed 04/12/2014
Derek Stapley (Independent)	appointed 26/06/2014
Bryan Blunt	appointed 01/12/2015
Troy Thompson	appointed 10/09/2015
Thomas Olunloyo	appointed 23/03/2017

Director resignation during the year was Manfred Maske (appointed 26/06/2014 and resigned 22/11/2016).

### Investment Committee

Kerrigan Procter	(Chairman)
Bryan Blunt	
Thomas Olunloyo	

### Audit, Risk and Compliance Committee

Derek Stapley	(Chairman)
Bryan Blunt	
Troy Thompson	

### General Management

Neil Burt	Head of Actuarial Reporting, Approved Actuary
Brendan Kemp	Chief Financial Officer
Thomas Olunloyo	Chief Executive Officer
Caspar Young	Chief Business Development Officer

### Registered Office

The Company's registered office is at Crown House, 3rd Floor, 4 Par-La-Ville Road, Hamilton, HM08, Bermuda and the Company is registered in Bermuda under registered number 48340 and domiciled in Bermuda.

### Corporate Secretary

Brendan Kemp

### Auditor

The Company has appointed PricewaterhouseCoopers Ltd. as independent auditors.

PricewaterhouseCoopers Ltd.  
Chartered Professional Accountants  
P.O. Box HM 1171  
Hamilton, HM EX  
Bermuda

### Bankers

HSBC Bank Bermuda Limited  
6 Front Street  
Hamilton, HM11  
Bermuda

HSBC Bank PLC  
8 Canada Square  
London, E14 5HQ  
United Kingdom

## Directors' Report

The board of directors are pleased to present their annual report along with the Audited Financial Statements for Legal & General Reinsurance Company Limited ('the Company') for the year ended 31 December 2016.

### Background and principal activities

The Company is a long-term class E reinsurer under Bermuda's Insurance Act of 1978 ('the Act'). The principal activity of the Company is the provision of life reinsurance solutions globally, focussing initially on pensions risk transfer in selected international markets.

The Company was capitalised in 2014 with £220m. Legal & General Re Holdings is the direct parent and Legal & General Group plc ('the Group') is the ultimate parent.

### Business Review

During 2016 the Company obtained two ratings from Standard & Poor's Rating Services ('S&P'), who assigned the Company an 'A+ - Stable' rating as well as Fitch Ratings ('Fitch') who rated the Company A+ - Stable'. Both ratings were a strategic priority of the Company due to its importance to the Group's international pension derisking strategy, shared management and branding.

In March 2016, the Company received notification from the De Nederlandsche Bank N.V. ('DNB'), that it has been granted 'Registered Reinsurer Status' and is free to provide reinsurance business to insurers in the Netherlands.

While 2016 has been a year of embedding and reporting the newly implemented Solvency II requirements, Legal & General Group has determined that it is preferable to use the Matching Adjustment ('the MA') for determining the Solvency II Financial Resources Requirement ('the FRR'). The Company has received approval of the MA application from the Prudential Regulatory Authority ('PRA') in 2015.

During the year, the Company continued to enhance governance, processes and procedures including the refinement of management level committees.

### Financial position and results

The results show International Financial Reporting Standard ('IFRS') profits before tax of £88m (2015: £95m) and release from operations of £75m (2015: £64m). These metrics are consistent with the Group's key metrics and ahead of expectations relative to the foundation business plan of the Company. Revenue for the Company as a result of the quota share transaction with Legal & General Assurance Society Limited ('LGAS') and the Dutch reinsurance agreement was £604m (2015: £173m) and £Nil (2015: £145m) respectively.

The Company holds £413m (2015: £349m) shareholders' equity to meet the Bermuda Solvency Capital Requirement ('BSCR') as at 31 December 2016. The Bermuda Monetary Authority ('the BMA') has implemented an Economic Balance Sheet ('EBS') regime which became effective on 1 January 2016.

### Dividend

A dividend of £25m was declared by the Company's Board of directors in November 2016 and paid to the Company's shareholder on 6 December 2016 (2015: £20m).

### Principal risks and uncertainties

A detailed review of the Company's exposure to risks, together with the framework for their management is set out in Note 22 of the financial statements. The Company prepares risk reports and has identified key risks as below:

#### 1) Regulatory change

There is a risk that the BMA makes further changes to the capital framework; and the Company has insufficient available capital to support a capital coverage ratio within risk appetite or cannot support new business growth.

The Company's business strategy is based upon prevailing legislation and regulation, and known/anticipated change. To mitigate this risk the Company engages with regulatory authorities via the Bermuda International Long-Term Insurers and Reinsurers ('BILTIR') association, of which the Company is an active member and lead working groups to refine the current regulatory framework as it applies to the Company. Sudden and/or retrospective changes in legislation, or the differing interpretation and application of regulation over time may, however, have a detrimental effect on the delivery of the Company's strategy and profitability.

The Company is exposed to additional regulatory risk because the Group is headquartered in the United Kingdom. Group regulation is conducted by the PRA and The Financial Conduct Authority ('The FCA'). The PRA could impose unfavourable conditions which could impact the ability of the Company to achieve its business strategy.

## 2) Solvency II

Emerging rules from European Union and guidance from European Insurance and Occupational Pensions Authority ('EIOPA') are unfavourable for retirement products in general. The Company's business could be exposed to unfavourable interpretations of Solvency II rules applied by the PRA. These interpretations could affect the Group's and the Company's regulatory surplus, thus impacting the capital available for the Company to achieve its growth aspirations. The Group's Internal Model was approved by the PRA in late 2015. Solvency II became effective on 1 January 2016.

Group has determined that it is preferable to use the MA for determining the Solvency II FRR. The MA reduces the FRR when approved for use. As a result, the Company's strategy and operations are constrained by the MA eligibility requirements including, for example, that assets be identified, organised and managed separately. The Group shall be required to increase the Solvency II technical provisions (liabilities) if it does not meet the MA requirements. The Company assets backing the annuities liabilities held by LGAS through funds withheld were successfully segregated in 2015 between those that are qualifying for the MA and those that are not eligible. The Company has also received approval of the MA application.

It is currently not clear how the United Kingdom's ('UK') exit from the European Union ('EU') will affect the UK's capital framework. The main impact of Brexit to the Company will be increased market volatility, the Company will monitor the situation closely and react accordingly. The Company's Registered Reinsurer status in the Netherlands is not dependent on the UK's membership with the EU.

## 3) Investment strategy

The Company is capitalised sufficiently to meet its ongoing business objectives from a local regulatory perspective. The shareholder funds supporting this business, as well as the assets that back the insurance liabilities, require a robust investment strategy that adheres to the BMA regulations. An investment strategy has been implemented that covers shareholder funds and assets backing liabilities covering both internal and external business. There is a risk that the investment strategy does not provide yields that allow the Company to be commercially successful and remain within risk appetite.

## 4) Financial market and economic conditions

The Company holds a broad range of investment assets to meet the obligations arising from its business. The performance and liquidity of investment markets and movements in interest rates, exchange rates and inflation can impact the value of these assets as well as the value of the underlying obligations. A potential mismatch of assets and liabilities may impact the earnings, profitability and the capital requirements of the Company.

The Company seeks to match the asset and liability cash flows to reduce the impact of changing economic conditions, in line with the prudent risk management principles applied by the Company and regulation. Additionally, a range of risk management strategies are used to manage volatility in returns from investment assets and the broader effects of adverse market conditions.

## 5) Counterparty and third party risks

The Company currently has two inwards reinsurance agreements in place and its long-term business success depends on these agreements and other new business opportunities that arise.

The Company is exposed to default risk in respect of the issuers of corporate debt and financial instruments, through the investment market and as part of its banking arrangements. Counterparty risk may also arise in the investment settlement process and from custodian services. Third party risk arises with regard to reliance upon external suppliers of certain administration and IT services.

The Company seeks to limit the potential exposure to loss from counterparty and third party failure through pre-selection criteria for those counterparties with which it will do business; the setting of pre-defined risk based exposure limits; and the active management of positions. Specific provisions are also made for defaults which provide a buffer if a counterparty fails. However, in extreme circumstances, an event causing widespread default may materially impact the Company's profitability, whilst the loss of crucial suppliers may impact operational effectiveness.

## 6) Mortality and other insurance assumption uncertainties

Assumptions are used to value the Company's liabilities, and given the long term nature, there is risk around the setting of these assumptions.

Mortality assumptions for base mortality and rates of mortality improvement are determined as part of the process to value the long term liabilities. The Company receives advice from a team of mortality specialists who recommend the assumptions using a rich database of relevant mortality data and industry models.

Economic assumptions including valuation interest rates and credit defaults within its investment portfolio are also used. The Company applies a prudent reduction to asset yield to allow for the risk of default for LGAS business and Dutch business respectively, overall this leads to a total default provision including additional default provision of c£285m (2015: c£229m). The Company believes the total default provision is sufficiently prudent to cover all reasonably foreseeable circumstances.

Processes are in place to ensure that assumptions are subject to a governance process that promotes critical challenge, including internal and external review. Analysis is performed to understand the impact of experience variances from best estimate assumptions as part of the Company's processes to assess solvency. Extreme shifts in financial markets may require changes to assumptions that impact the Company's long term profitability.

#### 7) Entry into new territories

A key component of the Company's strategy is to reinsure business originating from new territories which exposes the Company to a different regulatory regime. Obtaining licenses from the regulator and the conditions of approval could delay or impair the Company's growth aspiration. The Company has developed a robust pricing and valuation framework for markets where the Company already has a presence, and will develop further models for new international territories. The Company has used other highly rated reinsurers and external advisers to provide validation of the existing pricing basis, and a similar validation approach is expected in new territories. The Company will continually develop and assess existing models and frameworks, including the investment strategy, to ensure commercial success combined with a risk management approach that ensures exposures remain within Group risk appetite.

#### 8) Operational risk and people risk

Operational risk results from inadequate controls, systems, people or external events. Examples particularly relevant for the Company include inadequate contractual arrangements or insufficient technological or administrative capacity to manage and service inforce reinsurance agreements.

Resource constraints can lead to limited or slower growth aspirations. Insufficiently trained staff with inadequate capabilities in international markets could result in mispricing that could result in financial losses. The Company has recruited an experienced executive team that have employed suitably trained staff with experience in pension de-risking. The Company has constructed a framework of internal controls to minimise the risk of unanticipated loss or damage to our reputation. We seek to continually review and improve our framework.

#### 9) Financial reporting risk

Financial reporting risk may result from a lack of understanding of the complexity or impact on financial reporting of executed deals. Risk also arises if the data, processes and procedures associated with new transactions are not fully documented or controlled leading to errors in the financial statements. Delayed reporting or incorrect results may occur if the data provided by a cedant is incorrect, of poor quality, incomplete or late. The Company maintains a close relationship with its cedants to ensure accurate and timely data is received.

A financial reporting framework has been implemented, ensuring both actuarial and finance function are fully engaged in month end reporting. The robust framework reduces the risk of inaccurate financial reporting within the control of the Company.

#### **Statement of Directors' responsibilities**

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

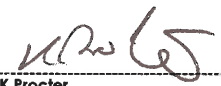
The management of Legal & General Reinsurance Company Limited is responsible for the preparation of the financial statements contained in this report. These financial statements have been prepared in accordance with International Financial Reporting Standards.

Management has established and maintains a system of financial reporting and internal controls to provide reasonable assurance that transactions are properly authorised and recorded. These controls include the careful selection, training, supervision of qualified employees, the establishment of well-defined responsibilities and the communication of policies relating to good conduct and business practice.

#### **Auditors**

The shareholder's independent auditors, PricewaterhouseCoopers Ltd. have audited the financial statements of the Company in accordance with International Standards on Auditing and have expressed their opinion in their report to the Company's shareholder. The auditors have unrestricted access to and meet periodically with the Audit, Risk & Compliance Committee to review its findings regarding internal controls over the financial reporting process, auditing matters and reporting issues.

These financial statements have been authorised for issue by the Board of Directors on 23 March 2017 and were signed on their behalf by:

  
K Procter  
Chairman  
23 March 2017

  
D Stapley  
Non-executive Director  
23 March 2017

  
T Oluwole  
Director  
23 March 2017



## Independent auditor's report

To the Shareholder of Legal & General Reinsurance Company Limited

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### **Our opinion**

In our opinion, the financial statements present fairly, in all material respects, the financial position of Legal & General Reinsurance Company Limited (the Company) as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

### **What we have audited**

The Company's financial statements comprise:

- the statement of profit or loss and other comprehensive income for the year ended 31 December 2016;
- the statement of financial position as at 31 December 2016;
- the statement of changes in equity for the year ended 31 December 2016;
- the statement of cash flows for the year ended 31 December 2016; and
- the notes to the financial statements, which include a summary of significant accounting policies.

### **Basis for opinion**

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Independence**

We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Chartered Professional Accountants of Bermuda Rules of Professional Conduct (CPA Bermuda Rules) that are relevant to our audit of the financial statements in Bermuda. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the CPA Bermuda Rules.

### **Other information**

Management is responsible for the other information. The other information comprises the Directors' Report (but does not include the financial statements and our auditor's report thereon).

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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### **Responsibilities of management and those charged with governance for the financial statements**

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

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### **Auditor's responsibilities for the audit of the financial statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's



report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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*PricewaterhouseCoopers Ltd.*

**Chartered Professional Accountants**  
Hamilton, Bermuda

**March 23, 2017**

**Statement of Profit or Loss and Other Comprehensive Income**

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
<b>Revenue</b>			
Gross written premiums	1F/2	604	318
<b>Net premium earned</b>			
Investment return / (loss)	1I/1L/1Q/3	767	(38)
Total revenue		1,371	280
<b>Expenses</b>			
Claims and change in insurance liabilities	1F/4	1,277	179
Acquisition costs	1F	1	1
Other expenses	1R/5	5	5
Total expenses		1,283	185
Profit for the year attributable to equity holders of the Company		88	95
Total comprehensive income for the year attributable to equity holders of the Company		88	95

All of the profit for the year is attributable to continuing activities.

**Statement of Financial Position**

As at 31 December 2016

	Notes	2016 £m	2015 £m
<b>Assets</b>			
Investment in subsidiary	1D/18/19	1	-
Funds Withheld	1H/9	5,242	4,214
Financial investments	1I/1L/10/11	551	436
Cash and cash equivalents	1K/12	21	9
<b>Total assets</b>		<b>5,815</b>	<b>4,659</b>
<b>Equity</b>			
Share capital	1N/13	-	-
Contributed Surplus		220	220
Retained earnings		193	130
<b>Total shareholders' equity</b>		<b>413</b>	<b>350</b>
<b>Liabilities</b>			
Non-participating contract liabilities	14/15	5,376	4,300
Payables and other financial liabilities	1L/1O/11/16	26	9
<b>Total liabilities</b>		<b>5,402</b>	<b>4,309</b>
<b>Total equity and liabilities</b>		<b>5,815</b>	<b>4,659</b>

The Notes on pages 14 to 38 are an integral part of these financial statements.

Signed on behalf of the board of directors:

  
K Procter  
Chairman  
23 March 2017

  
D Stapley  
Non-executive Director  
23 March 2017

  
T Olunloyo  
Director  
23 March 2017

**Statement of Changes in Equity**

For the year ended 31 December 2016

	Notes	Share capital £m	Contributed Surplus £m	Retained earnings £m	Total equity £m
<b>For the year ended 31 December 2016</b>					
<b>As at 1 January</b>		-	220	130	350
Total comprehensive income for the year		-	-	88	88
Dividend	8	-	-	(25)	(25)
<b>As at 31 December 2016</b>		-	220	193	413
<b>For the year ended 31 December 2015</b>					
As at 1 January		-	220	55	275
Total comprehensive income for the year		-	-	95	95
Dividend		-	-	(20)	(20)
<b>As at 31 December 2015</b>		-	220	130	350

**Statement of Cash Flows**

For the year ended 31 December 2016

	Notes	2016 £m	2015 £m
<b>Cash flows from operating activities</b>			
<b>Profit for the year</b>		<b>88</b>	95
<b>Adjustments for non-cash movements in profit for the year</b>			
Realised and unrealised gains on financial investments		<b>(30)</b>	-
Foreign exchange loss		<b>(4)</b>	(2)
<b>Net (increase) / decrease in operational assets</b>			
Funds Withheld (non-cash item)		<b>(1,028)</b>	139
Net (increase) in operational investments		<b>(43)</b>	(139)
<b>Net increase / (decrease) in operational liabilities</b>			
Non-participating contracts (non-cash item)		<b>1,076</b>	(34)
Payables and other financial liabilities		<b>16</b>	5
<b>Net cash flows from operating activities</b>		<b>75</b>	64
<b>Cash flows from investing activities</b>			
Purchases of financial investments		<b>(338)</b>	(146)
Proceeds from sales and maturities of financial investments		<b>298</b>	94
Dividends received		<b>2</b>	-
<b>Net cash flows (used in) investing activities</b>		<b>(38)</b>	(52)
<b>Cash flows from financing activities</b>			
Dividend distributions to ordinary equity holders of the Company during the year	8	<b>(25)</b>	(20)
<b>Net cash flows (used in) financing activities</b>		<b>(25)</b>	(20)
Net increase / (decrease) in cash and cash equivalents		<b>12</b>	(8)
Cash and cash equivalents at the beginning of the year		<b>9</b>	17
<b>Cash and cash equivalents at 31 December</b>		<b>21</b>	9

The Company's statement of cash flows includes all cash and cash equivalent flows.

## 1. Accounting policies

### A Basis of preparation

The Company is a long-term class E reinsurer under Bermuda's Insurance Act of 1978. The principal activity of the Company is the provision of life reinsurance solutions globally, focussing initially on pensions risk transfer in selected international markets.

The Company's financial statements have been prepared in accordance with IFRSs issued by the International Accounting Standards Board ('IASB'). The Company's financial statements also comply with IFRS and International Financial Reporting Interpretations Committee ('IFRIC') interpretations as issued by the IASB. The financial statements have been prepared under the historical cost convention, and financial assets and financial liabilities (including derivative instruments) at fair value through profit and loss.

These separate financial statements contain information about Legal & General Reinsurance Company Limited as an individual company and does not contain consolidated financial information. The Company is included in the group accounts of Legal & General Group Plc, a UK domiciled publicly traded company.

The Company presents its statement of financial position in order of liquidity. This is considered to be more relevant than a before and after 12 months presentation, given the long term nature of the Company's core business. However for each asset and liability line item which combines amounts expected to be recovered or settled before and after 12 months from the Statement of Financial Position date, disclosure of the split is made by way of a note.

Financial assets and financial liabilities are disclosed gross in the Statement of Financial Position unless a legally enforceable right of offset exists and there is an intention to settle recognised amounts on a net basis. Income and expenses are not offset in the income statement unless required or permitted by any accounting standard or IFRIC interpretation, as detailed in the applicable accounting policies of the Company.

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

### B Use of estimates

The preparation of the financial statements includes the use of estimates and assumptions which affect items reported in the Statement of Financial Position and the Statement of Profit or Loss and Other Comprehensive Income at the date of the financial statements. Although these estimates are based on management's best knowledge of current circumstances and future events and actions, actual results may differ from those estimates, possibly significantly. This is particularly relevant to the following:

#### The determination of fair values of unquoted and illiquid financial investments (Notes 11, 9, 10 and 11)

For unquoted financial investments, the Company obtains pricing information from a range of pricing services and brokers. Where there are indications that there is no active market, the Company seeks further evidence of the fair value from alternative pricing sources and market information. Priority is given to publicly available prices from independent sources when available, but overall, the source of pricing and/or the valuation technique is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The valuation techniques include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and, if applicable, enterprise valuation and may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments.

#### Non-participating insurance contract liabilities (Notes 1F, 1G, 14, 15) and associated balances

Long term business liabilities can never be definitive as to their timing or the amount of claims and are therefore subject to regular reassessment. The significant estimates and assumptions used in calculating insurance liabilities are disclosed in Note 15.

#### Tax balances

Under current Bermuda law the Company is not required to pay any taxes in Bermuda on either income or capital gains. The Company has received an undertaking from the Minister of Finance in Bermuda that in the event of any such taxes being imposed the Company will be exempted from taxation until the year 2035.

### C Summary of significant accounting policies

The Company has selected accounting policies which state fairly its financial position and financial performance for a reporting year. The accounting policies have been consistently applied to all years presented, unless otherwise stated.

The principal accounting policies adopted in preparing these financial statements are set out below.

### D Investments in subsidiary undertaking

Shares in subsidiary undertaking are carried at fair value.

## Notes to the Financial Statements

For the year ended 31 December 2016

Legal & General Reinsurance Company Limited  
Report and Accounts 2016

### 1. Accounting policies (cont'd)

#### E Product classification

The Company's products are classified for accounting purposes as non-participating insurance contracts. Insurance contracts are contracts which transfer significant insurance risk to the insurer at the inception of the contract.

#### F Long term insurance contracts

##### Premium income

Premiums are recognised as revenue when due for payment.

##### Claims

Claims and surrenders are accounted for when payment is due. Claims payable include the direct costs of settlement.

##### Acquisition costs

Acquisition costs comprise direct costs, such as initial commission, and the indirect costs of obtaining and processing new business.

##### Non-participating Insurance contract liabilities

Under current IFRS requirements, non-participating insurance contract liabilities are measured using UK Generally Accepted Accounting Principles ('GAAP'), as permitted by IFRS 4, 'Insurance contracts'.

The liabilities are calculated on the basis of current information using the gross premium valuation method. This brings into account the full premiums receivable under contracts written, having prudent regard to expected lapses and surrenders, estimated renewal and maintenance costs and contractually guaranteed benefits.

#### G Liability adequacy tests (Note 14)

The Company performs liability adequacy testing on its insurance liabilities to ensure that the carrying amount of liabilities is sufficient to cover current estimates of future cash flows. When performing the liability adequacy test, the Company discounts all contractual cash flows and compares this amount with the carrying value of the liability. Any deficiency is immediately charged to the income statement by establishing a provision for losses.

#### H Funds Withheld (Note 9)

Funds withheld represent amounts contractually withheld by LGAS in accordance with the reinsurance agreement. The value of the assets withheld and interest income are recorded in accordance with specific treaty terms.

As part of the reinsurance agreement, LGAS contractually withholds assets equal to 101% of their IFRS reserves (2015: net statutory reserves) and are managed according to an agreed investment policy set by the Company. The Company reflects these assets as funds withheld on the Company's Statement of Financial Position. In the event that LGAS was to become insolvent, the Company would need to assert a claim on the assets supporting its reserve liabilities. The Company attempts to mitigate its risk of loss by offsetting amounts for claims or allowances that it owes LGAS with amounts that LGAS owes to the Company. The Company is subject to the investment performance of the withheld assets. The Company sets and monitors compliance with the investment guidelines followed by LGAS. The Company's risk of loss could increase if the investment guidelines are inappropriate or LGAS does not adhere to such guidelines. This could have a material adverse impact on the Company's financial condition and operations result.

#### I Investments

##### Financial Investments

The Company classifies its financial investments on initial recognition as held for trading (HFT), designated at fair value through profit or loss (FVTPL), or receivables. Initial recognition of financial investments is on the trade date. The Company's policy is to measure financial investments at FVTPL. All derivatives other than those designated as hedges are classified as HFT.

Financial investments held by the Company are designated as FVTPL as their performance is evaluated on a total return basis, consistent with asset performance reporting to the Group Investment and Market Risk Committee and the Company's investment strategy. Assets designated as FVTPL include debt securities and equity instruments which would otherwise have been classified as Available for Sale ('AFS') under IAS 39, 'Financial instruments: recognition and measurement'. Assets backing non-participating policyholder liabilities are designated as FVTPL. The Company's non-participating investment contract liabilities are measured on the basis of current information and are designated as FVTPL to avoid an accounting mismatch in the Statement of Profit or Loss and Other Comprehensive Income.

The fair values of quoted financial investments are based on current bid prices. If the market for a financial investment is not active, the Company establishes fair value by using valuation techniques such as recent arm's length transactions, consensus market pricing, reference to similar listed investments, discounted cash flow models or option pricing models.

## 1. Accounting policies (cont'd)

### Financial Investments (cont'd)

Private equity investments are valued in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which represent current best practice, developed by the Association Française des Investisseurs en Capital, the British Venture Capital Association and the European Private Equity and Venture Capital Association. The techniques used for determining fair value include earnings multiples, the price of a recent investment or a net asset basis.

Financial investments classified as HFT and FVTPL are measured at fair value with gains and losses reflected in the income statement. Transaction costs are expensed as incurred.

Receivables are initially measured at fair value plus acquisition costs, and subsequently measured at amortised cost using the effective interest method.

The Company has categorised its financial investments in accordance with the level of shareholder or policyholders exposure to risks and rewards. The two categorisations presented are:

#### *Non profit non-unit linked*

Shareholders are exposed to the risks and rewards of the underlying market, credit and currency of the assets backing policyholder's liabilities.

#### *Shareholder*

All other assets are classified as shareholder assets. Shareholders of the Company are directly exposed to market, credit and currency risk on these assets.

On incorporation the Company adopted IFRS 13 'Fair Value Measurement'. This Standard defines fair value, sets out in a single IFRS a framework for measuring fair value, and requires disclosure about fair value measurements.

## **J Impairment policy**

The Company reviews the carrying value of its financial assets (other than those held at FVTPL) at each Statement of Financial Position date. If there is an indication that a financial asset is impaired, the carrying value is reduced through a charge to the income statement. There must be objective evidence of impairment as a result of one or more events which have occurred after the initial recognition of the asset.

## **K Cash and cash equivalents**

Cash and cash equivalents include cash at banks and other short term highly liquid investments with original maturities of 3 months or less.

## **L Derivative financial instruments**

The Company's activities expose it to the financial risks of changes in foreign exchange rates and interest rates. The Company uses derivatives such as foreign exchange forward contracts, interest rate swaps and cross currency basis swaps contracts to hedge these exposures.

Where the risks and characteristics of derivatives embedded in other contracts are not closely related to those of the host contract and the whole contract is not carried at fair value, the derivative is separated from that host contract and measured at fair value, with fair value movements reflected within investment return, unless the embedded derivative itself meets the definition of an insurance contract.

## **M Borrowings**

Borrowings are recognised initially at fair value, net of transaction costs. Borrowings classified as liabilities are subsequently stated at amortised cost. The difference between the net proceeds and the redemption value is recognised in the income statement over the borrowing period using the effective interest method.

## **N Share capital**

### *Equity instruments*

An equity instrument is any contract which evidences a residual interest in the net assets of an entity. It follows that a financial instrument is treated as equity if:

- there is no contractual obligation to deliver cash or other financial assets or to exchange financial assets or liabilities on unfavourable terms; and
- the instrument is either a non-derivative which contains no contractual obligation to deliver a variable number of own equity instruments, or is a derivative which will be settled only by the Company exchanging a fixed amount of cash, or other financial assets, for a fixed number of its own equity instruments.



## 1. Accounting policies (cont'd)

### Dividend recognition

A dividend distribution to the Company's shareholders is recognised as a liability in the period in which the dividends are authorised and are no longer at the discretion of the Company. Final dividends are accrued when approved by the Company's directors.

### **O Payables and other financial liabilities**

Payables and other financial liabilities comprise derivative liabilities and other liabilities. The derivative liabilities comprise a variety of exchange traded and over-the-counter derivative financial instruments, including forward currency contracts and swaps such as interest rate swaps and cross currency basis swaps measured at fair value.

### **P Foreign currency transactions**

Foreign currency transactions are translated into the functional currency ('Sterling') using the exchange rate prevailing at the date of the transactions. Foreign exchange gains and losses are recognised in the Statement of Profit or Loss and Other Comprehensive Income, except when recognised in equity as qualifying cash flow or net investment hedges.

### **Q Investment return**

The reporting of investment return comprises investment income, unrealised gains and losses from financial investments held at FVTPL and realised gains and losses from all financial assets.

Investment income includes dividends, interest and rent. Dividends are accrued on an ex-dividend basis. Interest and rent are included on an accruals basis. Interest income for financial assets which are not classified as FVTPL is recognised using the effective interest method. Investment income is presented net of investment management fees.

### **R Other expenses**

Other expenses comprise administrative expenses, management fees payable, corporate expenses and other charges. Other costs are accounted for as they arise.

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

Certain standards, amendments and interpretations to existing standards have been published which are mandatory for the Company's accounting periods beginning on or after 1 January 2016 or later periods but which the Company has not adopted early, as follows:

- Amendment to IFRS 9, 'Financial Instruments' In July 2014, the IASB issued IFRS 9, 'Financial Instruments' which is effective for annual periods beginning on or after 1 January 2018, subject to the IASB's consideration of its exposure draft, "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance contracts". On adoption, IFRS 9 contains three key elements:
  - a principle-based model for classification and measurement of financial instruments driven by cash flow characteristics and the business model in which an asset is held. Financial assets are classified under either amortised cost, fair value through other comprehensive income (FVOCI) or fair value through profit and loss;
  - a single expected loss impairment model that will require more timely recognition of expected credit losses on assets classified as amortised cost or FVOCI. Specifically, the new Standard requires entities to account for expected credit losses from when financial instruments are first recognised, and it lowers the threshold for recognition of full lifetime expected losses;
  - a substantially-reformed model for hedge accounting with enhanced disclosures about risk management activities, enabling entities to better reflect these activities in their financial statements

The impact of IFRS 9 on the Company's financial statements will depend on the interaction of the asset classification and measurement with the insurance contract measurement at the date of transition, particularly for liabilities which are measured using locked in discount rates. The IASB have given insurers the opportunity to apply for a deferral of IFRS 9 until the earlier of the implementation of the new insurance standard or 1 January 2021. Management intends to defer until the implementation of the new insurance standard.

- Amendment to IFRS 15, 'Revenue from Contracts with Customers' issued in May 2014 is effective for annual periods beginning on or after 1 January 2018. This standard provides clear guidance over when and how much revenue should be recognised. It provides a principles-based approach for revenue recognition, and introduces the concept of recognising revenue for obligations as they are satisfied. An assessment is currently on-going to determine the impact upon the Company. The standard does not apply to business classified as insurance contracts. The Company does not intend to early adopt this standard.
- IFRS 16, "Leases", effective for annual periods beginning on or after 1 January 2019, subject to EU endorsement. IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts, bringing commitments in relation to operating leases (as currently defined in IAS 17, "Leases") onto the balance sheet. The impact of the standard on lessor accounting is significantly smaller with the provisions remaining closely aligned to those in IAS 17 although the IASB have issued updated guidance on the definition of a lease. An assessment of the impacts of the standard on the Company's financial statements will be carried out in 2016. The Company does not intend to early adopt this standard.

There are no other IFRS standards, amendments and interpretations that are not yet effective that would be expected to have a material impact on the Company.

## 2. Analysis of revenue

Total premium written in the year of £604m (2015: £318m) relates to reinsurance premiums inward of long term business classified as non-participating premiums. In December 2015, the Company completed its first Dutch bulk annuity reinsurance transaction for €200m (£145m).

	2016 £m	2015 £m
United Kingdom	604	173
Netherlands	-	145
<b>Gross written premium</b>	<b>604</b>	<b>318</b>

## 3. Investment return

	2016 £m	2015 £m
Financial investment return <sup>1 2</sup>	767	(38)
<b>Investment return</b>	<b>767</b>	<b>(38)</b>

1. Financial investment return includes fair value gains and losses, dividends, rent and interest. Investment return is stated net of investment management fees and rebates.

2. Net gain (including interest and dividend income) of £722m (2015: loss £36m) arose in the year on the funds withheld (see Note 9). The remainder of the gain relates to shareholder funds and Euro Long Term Fund investments.

## 4. Net claims and change in insurance liabilities

From continuing operations	2016 £m	2015 £m
Claims paid - gross	237	213
	237	213
Change in insurance liabilities <sup>1</sup> - gross	1,040	(34)
<b>Net claims and change in insurance liabilities</b>	<b>1,277</b>	<b>179</b>

1. The change in reserves includes an increase of £1,015m (2015: release of £172m) from the LGAS quota share and an increase of £25m (2015: increase of £138m) from the Dutch business.

## 5. Other expenses

	2016 £m	2015 £m
Other administrative expenses <sup>1</sup>	5	5
<b>Total other expenses</b>	<b>5</b>	<b>5</b>

<sup>1</sup>. The Company does not have direct staff costs. Other group entities contract staff for the needs of the Company's activities and then recharge a proportion of those costs to the Company. The recharged costs are part of 'Other administrative expenses' above. See Note 6 Employee information.

## 6. Employee information

The Company does not have direct employees (2015: Nil) since they are employed by fellow subsidiaries of Legal & General Group Plc. The Company is recharged the staff costs by the fellow subsidiaries. Please refer to Note 19(v) & 19(vi) Related party transactions.

## 7. Foreign exchange and exchange rates

Investment income for the year includes a foreign exchange loss of £30m (2015: loss £2m) arising on conversion of monetary assets and liabilities to functional currencies. Foreign exchange includes losses realised during the year from investing financial investments amounting £4m (2015: loss £2m).

Principal rates of exchange used for translation are:

	2016 Average	2016 Year-End	2015 <sup>1</sup> Average	2015 <sup>1</sup> Year-End
United States Dollar	1.355	1.236	1.528	1.474
Canadian Dollar	1.779	1.657	1.969	2.047
Euro	1.224	1.172	1.378	1.357

<sup>1</sup>. Restated

## 8. Dividends

	Dividend Per share 2016 £	Total 2016 £m	Dividend Per share 2015 £	Total 2015 £m
Ordinary share dividends paid in the year / period - Current year dividend	100	25	80	20
<b>Ordinary share dividend</b>	<b>100</b>	<b>25</b>	<b>80</b>	<b>20</b>

On 6 December 2016 the Company paid a dividend of £25m (2015: £20m) to its parent company, Legal & General Re Holdings Limited.

## 9. Funds Withheld

Investment gains on funds withheld represented 52.2% (2015: losses of 12.9%) of the Company's revenue in 2016. Funds withheld totaled £5,242m (2015: £4,214m) at 31 December 2016.

Funds withheld comprised 90.2% (2015: 90.4%) of the Company's total assets as of 31 December 2016. All of the Company's funds withheld balance is associated with its reinsurance of LGAS annuity contracts.

The reinsurance agreement is written on a funds withheld basis, the assets equal to 101% of LGAS IFRS reserves (2015: net statutory reserves) are contractually withheld by LGAS and are managed according to an agreed investment policy set by the Company and LGAS. The assets are reflected as funds withheld on the Company's statement of financial position. In the event of LGAS's insolvency, the Company would need to assert a claim on the assets supporting its reserve liabilities. However, the risk of loss to the Company is mitigated by its ability to offset amounts it owes LGAS for claims or allowances with amounts owed by LGAS.

## 9. Funds Withheld (cont'd)

Income accrues on the withheld assets according to the terms defined in the reinsurance treaty and the Company estimated the return was approximately 13.7% (2015: -0.9%) for the year ended 31 December 2016. Additionally, under the treaty the Company is exposed to the investment performance on the withheld assets, although it does not directly own them. These assets are primarily fixed maturity investment securities. To mitigate this risk, the Company helps set the investment guidelines followed by LGAS and monitors compliance thereto. The ratings of the assets underlying the funds withheld are shown in Note 22 Table 4.

Funds Withheld expected to be settled within 12 months and after 12 months in line with the expected settlement of the backed liabilities as per Note 14(iii).

## 10. Financial investments

### (i) Financial investments at fair value

	Shareholder	Non profit non-unit linked	Total
Notes	2016 £m	2016 £m	2016 £m
<b>Financial investments at fair value designated as:</b>			
Fair value through profit or loss	318	225	543
Held for trading	-	8	8
Financial investments at fair value	318	233	551
<b>Total financial investments</b>	10(ii)	233	551
Expected to be received within 12 months			10
Expected to be received after 12 months			541
	Shareholder	Non profit non-unit linked	Total
Notes	2015 £m	2015 £m	2015 £m
<b>Financial investments at fair value designated as:</b>			
Fair value through profit or loss	297	139	436
Financial investments at fair value	297	139	436
<b>Total financial investments</b>	10(ii)	139	436
Expected to be received within 12 months			9
Expected to be received after 12 months			427

The risks associated with financial investments are outlined in Note 22.

Financial investments have been allocated between those expected to be settled within 12 months and after 12 months in line with the expected settlement of the backed liabilities.

Financial investments include £143.8m (2015: £Nil) of debt securities pledged as collateral against ASR Levensverzekering N.V. The assets used as collateral are AAA, AA, A, BBB Corporate Bonds (2015: Nil) having a residual maturity of up to 30 years (2015: Nil). The Company is entitled to receive all of the cash flows from the assets during the period when they are pledged as collateral. The Company can decide to substitute an asset which is designated as collateral at any time, provided the relevant terms and conditions of the Security Deed is met.

Financial investments include equity securities in unquoted investments in property vehicles and unquoted securities. A profit of £0.6m (2015: £Nil) has been recognised in the income statement in respect of the movement in fair value of these investments.

## 10. Financial investments (cont'd)

### (ii) Fair value hierarchy

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value measurements are based on observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's view of market assumptions in the absence of observable market information. The Company utilises techniques that maximise the use of observable inputs and minimise the use of unobservable inputs.

The levels of fair value measurement bases are defined as follows:

Level 1: fair values measured using quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: fair values measured using valuation techniques for all inputs significant to the measurement other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: fair values measured using valuation techniques for any input for the asset or liability significant to the measurement that is not based on observable market data (unobservable inputs).

The following table presents the Company's assets by IFRS 13 hierarchy levels:

	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
<b>As at 31 December 2016</b>					
<b>Shareholder</b>					
Equity securities	290	264	-	26	-
Debt securities	28	-	28	-	-
<b>Non profit non-unit linked</b>					
Equity securities	2	2	-	-	-
Debt securities	221	28	193	-	-
Accrued interest	2	-	2	-	-
Derivative assets	8	-	8	-	-
<b>Total financial investments</b>	<b>551</b>	<b>294</b>	<b>231</b>	<b>26</b>	<b>-</b>
<b>As at 31 December 2015</b>					
<b>Shareholder</b>					
Equity securities	297	297	-	-	-
<b>Non profit non-unit linked</b>					
Debt securities	137	23	114	-	-
Accrued interest	2	-	2	-	-
<b>Total financial investments</b>	<b>436</b>	<b>320</b>	<b>116</b>	<b>-</b>	<b>-</b>

All of the Company's level 2 assets have been valued using standard observable market data and market pricing sources, such as iBoxx, IDC, and Bloomberg. However, following consultation with our pricing providers and a number of their contributing brokers, we have considered that these prices are not from a suitably active market and have classified them as level 2.

Level 3 assets, where internal models (that are not based on observable market data) and external models (where there is insufficient information on the methodology used) are used to represent a small proportion of assets to which shareholders are exposed and reflect unquoted equities including investments in private equity, property vehicle, suspended securities, manually priced derivatives and some broker priced assets.

In many situations, inputs used to measure the fair value of an asset or liability may fall into different levels of the fair value hierarchy. In these situations, the Company determines the level in which the fair value falls based upon the lowest level input that is significant to the determination of the fair value. As a result, both observable and unobservable inputs may be used in the determination of fair values that the Company has classified with level 3.

## 10. Financial investments (cont'd)

The Company determines the fair values of certain financial assets and liabilities based on quoted market prices, where available. The Company also determines fair value based on estimated future cash flows discounted at the appropriate current market rate. As appropriate, fair values reflect adjustments for counterparty credit quality, the Company's credit standing, liquidity and risk margins on unobservable inputs.

Where quoted market prices are not available, fair value estimates are made at a point in time, based on relevant market data, as well as the best information about the individual financial instrument. Illiquid market conditions have resulted in inactive markets for certain of the Company's financial instruments. As a result, there is generally no or limited observable market data for these assets and liabilities. Fair value estimates for financial instruments deemed to be in an illiquid market are based on judgments regarding current economic conditions, liquidity discounts, currency, credit and interest rate risks, loss experience and other factors. These fair values are estimates and involve considerable uncertainty and variability as a result of the inputs selected and may differ significantly from the values that would have been used had a ready market existed, and the differences could be material. As a result, such calculated fair value estimates may not be realisable in an immediate sale or settlement of the instrument. In addition, changes in the underlying assumptions used in the fair value measurement technique could significantly affect these fair value estimates.

Fair values are subject to a control framework designed to ensure that input variables and outputs are assessed independent of the risk taker. These inputs and outputs are reviewed and approved by a valuation committee.

### (a) Significant transfers between level 1, level 2 and level 3:

There have been no significant transfers between levels during the year (2015: no significant transfers).

### (b) Assets measured at fair value based on level 3:

	Equity securities 2016 £m	Other financial investments 2016 £m	Investment property 2016 £m	Total 2016 £m	Equity securities 2015 £m	Other financial investments 2015 £m	Investment property 2015 £m	Total 2015 £m
<b>As at 1 January</b>	-	-	-	-	-	-	-	-
Total gains or losses for the period: - unrealised gains/(losses) in profit and loss	1	-	-	1	-	-	-	-
Purchases/ Additions	25	-	-	25	-	-	-	-
<b>As at 31 December</b>	<b>26</b>	-	-	<b>26</b>	-	-	-	-

As a Company we hold regular discussion with our pricing providers to determine whether transfers or classifications between levels of the fair value hierarchy have occurred.

## 10. Financial investments (cont'd)

### (c) Effect of changes in significant unobservable inputs (level 3) to reasonably possible alternative assumptions

As discussed above, the fair values of financial instruments are, in certain circumstances measured using valuation techniques that incorporate assumptions that are not evidenced by prices from observable current market transactions in the same instrument and are not based on observable market data. The following table shows the level 3 financial instruments carried at fair value as at the balance sheet date, the valuation basis, main assumptions used in the valuation of these instruments and reasonably possible increases or decreases in fair value based on reasonably possible alternative assumptions.

	Main Assumption	Reasonably possible alternative assumptions			Reasonably possible alternative assumptions		
		Current fair value 2016 £m	Increase in fair value 2016 £m	Decrease in fair value 2016 £m	Current fair value 2015 £m	Increase in fair value 2015 £m	Decrease in fair value 2015 £m
<b>Assets</b>							
<b>Shareholder</b>							
- Unquoted investments in Property Vehicles <sup>1</sup>	Property yield: occupancy	21	2	(2)	-	-	-
- Unquoted securities <sup>2</sup>		5	-	-	-	-	-
<b>Total</b>		<b>26</b>	<b>2</b>	<b>(2)</b>	<b>-</b>	<b>-</b>	<b>-</b>

1. Includes Industrial Property Investment Fund ('IPIF'): Property fund structured as a Jersey Property Unit Trust (JPUT). Valuation methodology is based on RICS property surveys.

2. Includes Pemberton European Mid-Market Debt Fund II ('Pemberton'): Fund investing in senior secured unlisted loans, structured as a Luxembourg Limited Partnership.

## 11. Derivative assets and liabilities

	Contract/ notional amount 2016 £m	Fair values Assets 2016 £m	Liabilities <sup>1</sup> 2016 £m	Contract/ notional amount 2015 £m	Fair values Assets 2015 £m	Liabilities <sup>1</sup> 2015 £m
<b>Non profit non-unit linked derivatives:</b>						
Interest rate contracts - held for trading	374	8	3	203	-	2
Forward foreign exchange contracts - held for trading	-	-	1	-	-	1
Currency swap contracts - held for trading	156	-	7	-	-	-
<b>Total non profit non-unit linked derivatives</b>	<b>530</b>	<b>8</b>	<b>11</b>	<b>203</b>	<b>-</b>	<b>3</b>
<b>Total derivative assets and liabilities</b>	<b>530</b>	<b>8</b>	<b>11</b>	<b>203</b>	<b>-</b>	<b>3</b>

1. Derivative liabilities are reported in the balance sheet within Note 16 Payables and other financial liabilities.

The notional amounts of some derivative instruments provide a basis for comparison with instruments recognised on the balance sheet. However, these amounts do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Company's exposure to credit or price risks.

### 11. Derivative assets and liabilities (cont'd)

The contractual undiscounted cash flows in relation to non-unit linked derivatives have the following maturity profile.

As at 31 December 2016	Fair values £m	Maturity profile of undiscounted cash flows					Total £m
		Within 1 year £m	1-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	
<b>Cash inflows</b>							
<b>Non profit non-unit linked derivatives</b>							
Derivative assets	8	17	19	38	16	11	101
Derivative liabilities	(11)	49	47	84	87	20	287
<b>Total</b>	<b>(3)</b>	<b>66</b>	<b>66</b>	<b>122</b>	<b>103</b>	<b>31</b>	<b>388</b>
<b>Cash outflows</b>							
<b>Non profit non-unit linked derivatives</b>							
Derivative assets	8	(15)	(12)	(37)	(17)	(9)	(90)
Derivative liabilities	(11)	(53)	(62)	(89)	(80)	(19)	(303)
<b>Total</b>	<b>(3)</b>	<b>(68)</b>	<b>(74)</b>	<b>(126)</b>	<b>(97)</b>	<b>(28)</b>	<b>(393)</b>
<b>Net non profit non-unit linked derivatives cash flows</b>		(2)	(8)	(4)	6	3	(5)

As at 31 December 2015	Fair values £m	Maturity profile of undiscounted cash flows					Total £m
		Within 1 year £m	1-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	
<b>Cash inflows</b>							
<b>Non profit non-unit linked derivatives</b>							
Derivative assets	-	-	3	5	-	-	8
Derivative liabilities	(3)	122	10	29	-	-	161
<b>Total</b>	<b>(3)</b>	<b>122</b>	<b>13</b>	<b>34</b>	<b>-</b>	<b>-</b>	<b>169</b>
<b>Cash outflows</b>							
<b>Non profit non-unit linked derivatives</b>							
Derivative assets	-	(1)	(3)	(4)	-	-	(8)
Derivative liabilities	(3)	(123)	(9)	(32)	-	-	(164)
<b>Total</b>	<b>(3)</b>	<b>(124)</b>	<b>(12)</b>	<b>(36)</b>	<b>-</b>	<b>-</b>	<b>(172)</b>
<b>Net non profit non-unit linked derivatives cash flows</b>		(2)	1	(2)	-	-	(3)

The Company uses derivatives to reduce market risk. The most widely used derivatives are over the counter interest rate swaps. The Company may use futures to facilitate efficient asset allocation. In addition, derivatives are used to improve asset-liability matching and to manage interest rate and foreign exchange risk. It is the Company's policy that all derivative transactions are on a covered basis against underlying holdings of assets. Derivative counterparty risk is managed by the posting of collateral on a daily basis (Note 12).



## 12. Cash and cash equivalents

	Shareholder 2016 £m	non-unit linked 2016 £m	Total 2016 £m	Shareholder 2015 £m	non-unit linked 2015 £m	Total 2015 £m
Cash at bank and in hand <sup>1</sup>	1	20	21	-	9	9
Cash and cash equivalents	1	20	21	-	9	9

1. Cash at bank includes £11.2m (2015: £Nil) pledged as collateral against derivative liabilities. The Company can decide to substitute an asset which is designated as collateral at any time, provided the relevant terms and conditions of the International Swap Dealers Association and CSA agreements are met.

## 13. Share capital

	Number of shares	2016 £	2015 £
<b>Issued share capital:</b>			
Fully paid ordinary shares of US\$1 each	250,000	150,465	150,465

In 2014, 250,000 authorised and issued ordinary shares of US\$1.00 were subscribed to by Legal & General Re Holdings Limited. There is one class of ordinary shares. All shares issued carry equal voting rights.

The holders of the Company's ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at shareholder meetings of the Company.

## 14. Non-participating insurance contract liabilities

### (i) Analysis of non-participating insurance contract liabilities

	Notes	Gross 2016 £m	Reinsurance 2016 £m	Gross 2015 £m	Reinsurance 2015 £m
Non-participating insurance contracts	14(iii)	5,376	-	4,300	-
<b>Non-participating insurance contract liabilities</b>		<b>5,376</b>	<b>-</b>	<b>4,300</b>	<b>-</b>

### (ii) Expected insurance contract liability cash flows

As at 31 December 2016	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Non-participating insurance contracts	1,383	2,590	1,951	1,821	7,745	5,376
<b>Non-participating insurance contract liabilities</b>	<b>1,383</b>	<b>2,590</b>	<b>1,951</b>	<b>1,821</b>	<b>7,745</b>	<b>5,376</b>

Insurance contract undiscounted cash flows are based on the expected date of settlement. The weighted average discount rate applied for the carrying value is 2.44%.

#### 14. Non-participating insurance contract liabilities (cont'd)

As at 31 December 2015	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Non-participating insurance contracts	1,241	2,332	1,786	1,696	7,055	4,300
<b>Non-participating insurance contract liabilities</b>	<b>1,241</b>	<b>2,332</b>	<b>1,786</b>	<b>1,696</b>	<b>7,055</b>	<b>4,300</b>

Insurance contract undiscounted cash flows are based on the expected date of settlement. The weighted average discount rate applied for the carrying value is 3.419%.

#### (iii) Movement in non-participating insurance contract liabilities

	Note	Gross 2016 £m	Gross 2015 £m
<b>As at 1 January</b>		<b>4,300</b>	4,334
New liabilities in the period		561	333
Liabilities discharged in the year		(284)	(227)
Unwinding of discount rates		147	125
Effect of change in non-economic assumptions	15	1	40
Effect of change in economic assumptions	15	684	(264)
Acquisitions		-	-
Other		(33)	(41)
<b>As at 31 December</b>		<b>5,376</b>	4,300
Expected to be settled within 12 months		278	249
Expected to be settled after 12 months		5,098	4,051

#### 15. Long term insurance valuation assumptions

##### Non-participating business

The Company writes only non-participating business and it seeks to make prudent assumptions about its future experience based on current market conditions and recent experience. The basis used to set technical provisions follows the UK PRA statutory basis, which is an acceptable basis under IFRS, subject to the amendment of certain assumptions which differ from the UK PRA basis and are more prudent. The assumptions incorporate prudent margins in excess of our best estimate assumptions to minimise the possibility of actual experience being less favourable than assumed.

##### Valuation rates of interest and discount rates

The valuation interest rate for the underlying annuity business is based on the modified internal rate of return on the portfolio of assets backing the liabilities. The current dividend yield is used for equity investments and the rental income yield is used for property holdings within the funds withheld.

For the valuation interest rate assumption, asset yields are adjusted to reflect the risk of default associated with the investments held. The Company applies a prudent reduction to asset yield to allow for the risk of default for LGAS business and Dutch business respectively, overall this leads to a total default provision including additional default provision of c£285m (2015: c£229m).

The Company believes the total default allowance is prudent to cover all reasonably foreseeable circumstances.

##### Mortality

Mortality assumptions are set with reference to standard tables drawn up by the Continuous Mortality Investigation ('CMI') of the Institute and Faculty of Actuaries. These tables are based on industry wide mortality experience for insured lives. Mortality improvement rates are based on the CMI's mortality projections model and reflect expected improvements in longevity in the future.

The majority of internal statistical investigations are carried out at least annually to determine the extent to which the Company's experience differs from that of the industry and suggest appropriate adjustments which need to be made to derive the valuation assumptions.

## 15. Long term insurance valuation assumptions (cont'd)

### Expenses

The Company monitors its expense experience and carries out detailed investigations regularly to determine the expenses incurred in writing and administering the different products and classes of business. An allowance for expense inflation in the future is also made, taking account of both salary and price information. The expense assumptions also include an appropriate allowance for prudence.

### The principal assumptions are:

	2016 UK	2016 Dutch	2015 <sup>1</sup> UK	2015 <sup>1</sup> Dutch
<b>(i) Rate of interest/discount rate</b>				
Annuities in deferment	UK 2.47% pa	Dutch 1.69% pa	UK 3.43% pa	Dutch 3.21% pa
Annuities in deferment (RPI linked; net rate after allowance for inflation)	-1.10% pa		0.12% pa	
Vested annuities	UK 2.47% pa	Dutch 1.69% pa	UK 3.43% pa	Dutch 3.21% pa
Vested annuities (RPI linked; net rate after allowance for inflation)	-1.10% pa		0.12% pa	
<b>(ii) Mortality Tables</b>				
Annuities in deferment <sup>2</sup>	81.3% - 83.4% PCXA00/PNXA00	Dutch 76.0%-83.0% M/F Dutch AG2014	UK 81.3% - 86.7% PCXA00/PNXA00	Dutch 76.0%-83.0% M/F Dutch AG2014
Vested annuities <sup>2</sup>				
- Bulk purchase annuities	82.2-83.4% PCMA00/PCFA00	Dutch 76.0%-83.0% M/F Dutch AG2014	UK 82.2% - 86.7% PCMA00/PCFA00	Dutch 76.0%-83.0% M/F Dutch AG2014
- Other annuities	60.7% - 129.1% PCMA00/PCFA00		63.9% - 133.5% PCMA00/PCFA00	

1. Restated.

2. For vested and deferred annuities, mortality rates are assumed to reduce according to an adjusted CMI's mortality improvement model. The model reflects experience from the England and Wales population and projects current rates of mortality improvements to a defined Long Term Rate. The Long Term Rate has been determined using a combination of Group's internal Cause of Death model and expert judgment. CMI 2014 has the following parameters:

-Males: Long Term Rate of 2.0% (2015: 2.0%) p.a. up to age 85 tapering to 0% at 120. Dutch 2.0% (2015: 2.0%) based on CMI 2011  
-Females: Long Term Rate of 1.5% (2015: 1.5%) p.a. up to age 85 tapering to 0% at 120. Dutch 2.0% (2015: 2.0%) based on CMI 2011

## 16. Payables and other financial liabilities

	Notes	2016 £m	2015 £m
Derivative liabilities	11	11	3
Other liabilities		8	-
Intercompany balances due	19(v)	7	6
<b>Payables and other financial liabilities</b>		<b>26</b>	<b>9</b>
Settled within 12 months		19	8
Settled after 12 months		7	1

### Fair value hierarchy

As at 31 December 2016	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
Derivative liabilities	11	1	10	-	-
Other liabilities	8	8	-	-	-
Intercompany balances due <sup>1</sup>	7	7	-	-	-
<b>Payables and other financial liabilities</b>	<b>26</b>	<b>16</b>	<b>10</b>	<b>-</b>	<b>-</b>

## 16. Payables and other financial liabilities (cont'd)

As at 31 December 2015	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
Derivative liabilities	3	1	2	-	-
Intercompany balances due <sup>1</sup>	6	6	-	-	-
<b>Payables and other financial liabilities</b>	<b>9</b>	<b>7</b>	<b>2</b>	<b>-</b>	<b>-</b>

1. See Note 19(v) Related party transactions.

There have been no significant transfers between levels (2015: No significant transfers).

## 17. Contingent liabilities, guarantees and indemnities

The Company does not have any contingent liabilities, guarantees or indemnities (2015: Nil) arising as part of its normal course of business.

## 18. Parent companies and fellow subsidiaries

The immediate parent company of Legal & General Reinsurance Company Limited is Legal & General Re Holdings Limited, a company incorporated in England and Wales. The ultimate holding company for both of those entities is Legal & General Group Plc. These accounts provide information about Legal & General Reinsurance Company Limited as an individual undertaking. Copies of the accounts of the ultimate holding company, Legal & General Group Plc, are available, at the Registered Office, One Coleman Street, London, EC2R 5AA, on the Group website at [www.legalandgeneral.com](http://www.legalandgeneral.com), or from the Company Secretary.

On 15 January 2015 Legal & General SAC Limited ('L&G SAC') (License No. 49929) was incorporated as a Bermuda exempted company limited by shares, was subsequently licensed on 12 October 2015 as a Class C Insurer under the Insurance Act 1978 and as a Segregated Accounts Company under the Segregated Accounts Companies Act 2000.

In June 2015 the Company subscribed to L&G SAC's 250,000 authorised and issued ordinary shares of US\$1.00. There is one class of ordinary shares and all shares issued carry equal voting rights. In October 2015 the Company completed a US\$0.65m (£0.43m) capital injection into L&G SAC as required by local Bermuda requirements. Furthermore, in November 2016 the Company completed a US\$0.12 (£0.10m) capital injection into L&G SAC.

L&G SAC is a wholly owned subsidiary of the Company set up to provide alternative de-risking solutions to pension scheme trustees in the UK and other territories worldwide by direct access to the reinsurance market without intermediation with an insurer. L&G SAC reflects the Group's strategic plan to expand its longevity and asset risk business internationally. L&G SAC has not written any business since inception. Shares in L&G SAC are carried at fair value.

Legal & General Re Holdings Limited fully owns Legal & General Resources Bermuda Limited ('LGRB'), a company incorporated in Bermuda providing administrative services to the Company and L&G SAC.

## 19. Related party transactions

### (i) Reinsurance

The Company is acting as reinsurer to its sister entity, LGAS. The Company accepted £604m (2015: £173m) of reinsurance premium for reinsuring non-participating insurance business, paid £1.3m (2015: £0.5m) in commission and paid £228m (2015: £213m) in claims during the year. A non-participating insurance liability of £5,146m (2015: £4,130m) is held to cover this business.

### (ii) Investments in Group unit trusts and the Group liquidity fund

The Company held £223m (2015: £260m) of investments in unit trusts, controlled and managed by Group companies that are classified as other related parties. In the year ended 31 December 2016 the Company made gains of £28m (2015: £0.3m) from those trusts.

### (iii) Investments in Funds Withheld

The Company held £5,242m (2015: £4,214m) in funds withheld by its sister entity LGAS. Net gain of £722m (2015: loss of £36m) arose in the year on the funds withheld (See Note 9).

### (iv) Investment in Subsidiary

The Company held a £528k investment in subsidiary (2015: £429k) in L&G SAC.

**19. Related party transactions (cont'd)**

**(v) Payables**

As at 31 December	2016 £m	2015 £m
To other related party: - Management charges due <sup>1</sup>	7	6
<b>Total</b>	<b>7</b>	<b>6</b>

1. The management charges due relate to expenses owed by the Company, to Legal & General group entities, namely LGRB and Legal & General Resources Limited. These charges have accrued over the year and relate to the operation costs including employee benefits. Legal & General Resources Limited which employs all UK staff, charges all of its costs pertaining to secondees to LGRB from the UK offices. LGRB employs Bermuda based staff and incurs all costs of operation, 100% of which is recharged to the Company.

**(vi) Other charges**

For the year ended 31 December	2016 £m	2015 £m
Interest charges on loan due to L&G Finance Plc <sup>1</sup> Management charges <sup>2</sup>	6	5
<b>Total charges</b>	<b>6</b>	<b>5</b>

1. In 2015 the Company received a short term borrowing from Legal & General Finance Plc totaling €200m (£145m). The loan was repaid prior to year end at a cost of £0.01m.

2. See note under table 19(v). For the year charges of £4m are staff related costs (2015: £3m).

**(vii) Dividends**

During December 2016, the Company paid a dividend of £25m (2015: £20m) to its parent company, Legal & General Re Holdings Limited.

**20. Management of capital resources**

**Capital management policies and objectives**

The Company aims to manage its capital resources to maintain financial strength, policyholder security, local requirements and the Group's relative external financial strength ratings advantage.

**Capital measures**

The Company measures its capital on a number of different bases, including those which comply with the regulatory framework within which the Company operates, and those which the directors consider most appropriate for managing the business. The measures used by the Company include:

**Accounting bases**

Management use the primary financial statements prepared on an IFRS basis to manage capital and cash flow usage and to determine dividend paying capacity.

**Bermuda statutory requirements**

The Company is licensed as a class E long term reinsurer under the Bermuda's Insurance Act 1978. Under the Act, the Company is required to maintain a minimum capital and surplus of £89m as at 31 December 2016 (2015: £72m). There are no statutory restrictions on the payment of dividends from retained earnings of the Company as the minimum statutory capital and surplus requirements are satisfied by the share capital and additional paid in capital. However, approval from the Bermuda Monetary Authority must be obtained before the statutory capital is reduced in excess of 15% of the previous year's statutory filing. In all cases, the Approved Actuary needs to approve any proposed dividends.

**Capital resources**

The financial strength of the Company is measured by reference to its Bermudan statutory accounts prepared due to its status as a class E reinsurer. The Company's total capital resources of £413m (2015: £349m) comprise capital contribution from the ultimate parent of £220m (2015: £220m) and £193m (2015: £129m) in respect of retained earnings inclusive of a £25m dividend (2015: £20m).

## 20. Management of capital resources (cont'd)

### Available regulatory capital resource risks

The Company's available capital resources are sensitive to changes in market conditions, due to both changes in the value of the assets and to the effect that changes in investment conditions may have on the value of the liabilities. Capital resources are also sensitive to assumptions and experience relating to mortality and morbidity and, to a lesser extent expenses.

The most significant sensitivities arise from the following two risks:

- Credit risk which would crystallise if the credit quality deteriorated and defaults within the asset backing liabilities exceeded the assumptions used for reserving.
- Mortality risk which would crystallise if the mortality of annuitants was lower than the assumptions used for reserving.

### 21. Assets analysis

The Company has categorised its assets and liabilities in accordance with the level of shareholder or policyholders exposure to risks and rewards. The two categorisations presented are:

#### Non profit non-unit linked

Shareholders are exposed to the risks and rewards of the underlying market, credit and currency of the assets backing policyholder's liabilities.

#### Shareholder

All other assets are classified as shareholder assets. Shareholders of the Company are directly exposed to market, credit and currency risk on these assets.

The table below presents an analysis of the statement of financial position by category. All of the quantitative risk disclosures in Note 22 (Risk management and control) have been provided using this categorisation.

	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m	Shareholder <sup>1</sup> 2015 £m	Non profit <sup>1</sup> non-unit linked 2015 £m	Total <sup>1</sup> 2015 £m
<b>Assets</b>						
Funds Withheld	-	5,242	5,242	-	4,214	4,214
Investment in subsidiary	-	1	1	-	-	-
Financial Investments	318	233	551	297	139	436
Cash and cash equivalents	1	20	21	-	9	9
<b>Total assets</b>	<b>319</b>	<b>5,496</b>	<b>5,815</b>	<b>297</b>	<b>4,362</b>	<b>4,659</b>
<b>Liabilities</b>						
Non-participating contract liabilities	-	5,376	5,376	-	4,300	4,300
Other liabilities	-	26	26	-	9	9
<b>Total liabilities</b>	<b>-</b>	<b>5,402</b>	<b>5,402</b>	<b>-</b>	<b>4,309</b>	<b>4,309</b>

1. Restated

## 22. Risk management and control

This section describes the Company's approach to risk management. It covers the overall approach that applies to all risks and includes a detailed review of risks within the Company's business.

### Risk management objectives

The Company's primary objective in undertaking risk management activity is to manage risk exposures in line with risk appetite, minimising its exposure to unexpected financial loss and limiting the potential for deviation from anticipated outcomes. In this respect, a framework of limits and qualitative statements are in place for material exposures.

### Risk Management

A significant part of the Company's business involves the acceptance and management of risk. The Company operates a formal risk management framework to ensure that all risks are managed within risk appetite. The Company seeks to manage its exposure to risk through control techniques which ensure that the residual risk exposures are within acceptable tolerances agreed by the Board. The key control techniques for the major categories of risk exposure are summarised further in this note. Overall responsibility for the management of the Company's exposure to risk is vested in the Board.

## **22. Risk management and control (cont'd)**

### **Governance Framework**

A key part of the risk management process is a robust governance framework. The Company operates a three lines of defence governance structure. The first line is represented by governance within the Company, the second line is represented by the Risk team within the Company and/or at the divisional level, and the third line is represented by the Group Internal Audit function.

The risks to which the Company are exposed are mentioned below, but this should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties.

### **Insurance risk**

*Exposure to loss arising from claims experience being different to that anticipated.*

Insurance risk is implicit in the Company's insurance business and arises as a consequence of the type and volume of business written and the concentration of risk in particular policies or groups of policies subject to the same risks. Insurance risk is managed using policies and delegated authorities for underwriting, pricing and reinsurance. The Legal & General Group insurance risk policy sets out the overall framework for the management of insurance risk. Areas where the Company is primarily exposed to insurance risk is mortality and, rates of mortality improvement. Insurance risk also arises from incomplete scheme demographic data, specifically where information concerning spouses is unavailable (spouse risk).

Pricing is based on a fixed set of assumptions, such as mortality, which consider past experience, recent trends, and expert opinion. Actual experience may vary from the pricing assumptions, leading to profits or losses. Insurance exposures are limited through reinsurance for specific cohorts of business. Overall, the Company seeks to be conservative in its acceptance of insurance risks by establishing strict underwriting criteria and limits.

### **Market risk**

*Exposure to loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets.*

The Company's exposure to market risk is influenced by one or more external factors, including changes in specified interest rates, financial instrument prices, foreign exchange rates and indices of prices or rates.

Significant areas where the Company is exposed to these risks are:

- assets backing insurance contracts;
- assets and liabilities denominated in foreign currencies; and
- other financial assets and liabilities.

Legal & General Group Plc's market risk policy sets out the overall framework for the management of market risk. The policy is reinforced by more granular investment policies for long term and other business, which have due regard to the nature of liabilities and guarantees and other embedded options given to policyholders.

The Company is ultimately responsible for the management of market risk. The Company has chosen to outsource the execution of the investment risk policy, as noted below, to LGAS (2015: Legal & General Pensions Limited ('LGPL') which novated in 2015 to LGAS). The Company manages market risk using the following methods:

#### Asset liability matching

The Company manages its assets and liabilities in accordance with relevant regulatory requirements, reflecting the differing types of liabilities it has.

For business such as immediate annuities, which is sensitive to interest rate risk, analysis of the liabilities is undertaken to create a portfolio of securities, the value of which changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits from changing interest rates. Interest rate risk cannot be completely eliminated, due to the nature of the liabilities and early redemption options contained in the assets.

LGAS holds a range of asset types to meet liabilities and it uses stochastic models to assess the impact of a range of future return scenarios on investment values and associated liabilities. This allows the Company with LGAS to devise an investment strategy which maximises risk-adjusted returns to its shareholders.

#### Derivatives

The Company uses derivatives to reduce the market risk arising in the long term funds. The most widely used derivatives are exchange-traded swaps. The Company may use futures to facilitate efficient asset allocation within the long term funds. In addition, derivatives within the long term fund are used to improve asset liability matching and to manage interest rate, foreign exchange and inflation risks. It is the Company's policy that amounts at risk through derivative transactions are covered by cash or corresponding assets and that swaps are collateralised as appropriate to reduce counterparty risk.

#### Interest rate risk

Interest rate risk is the risk that the Company is exposed to lower returns or loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets and liabilities arising from changes in underlying interest rates.

## 22. Risk management and control (cont'd)

The Company is exposed to interest rate risk on the investment portfolio it maintains to meet the obligations and commitments under its non-linked insurance contracts, in that the proceeds from the assets may not be sufficient to meet the Company's obligations to policyholders.

To mitigate the risk that guarantees and commitments are not met, the Company purchases financial instruments, which broadly match the expected non-participating policy benefits payable, by their nature and term. The composition of the investment portfolio is governed by the nature of the insurance liabilities, the expected risk-adjusted rate of return and the expected impact on the capital requirement.

Asset liability matching significantly reduces LGAS's and consequently the Company's exposure to interest rate risk. Sensitivity to interest rate changes is included in Table 5 on page 38.

### Inflation risk

Inflation risk is the potential for loss as a result of relative or absolute changes in inflation rates. The Company is directly exposed to inflation risk in respect of inflation-linked contracts. Contracts in payment may also include an annual adjustment for movements in prices indices, subject to an annual floor. The Company seeks to manage the risk of movements in price indices through the use of inflation swaps within funds withheld assets.

### Currency risk

The Company is potentially exposed to loss as a result of fluctuations in the value of, or income from, assets denominated in foreign currencies. The Company manages its currency risk exposure in respect of assets denominated in currencies other than the liability currency by backing obligations with investments in the same currency and through hedging using derivatives.

Table 1 summarises the Company's net exposure to foreign currency exchange risk, in sterling.

**Table 1 – Currency risk  
As at 31 December 2016**

Shareholder	Euro £m	US Dollar £m	Sterling £m	Carrying value £m
<b>Assets</b>				
Financial Investments	5	-	313	318
Cash and cash equivalents	1	-	-	1
<b>Total assets</b>	<b>6</b>	<b>-</b>	<b>313</b>	<b>319</b>
<b>Non profit non-unit linked</b>				
<b>Assets</b>				
Funds Withheld	48	-	5,194	5,242
Financial Investments	199	34	-	233
Cash and cash equivalents	10	-	10	20
Investment in subsidiary	-	-	1	1
<b>Total assets</b>	<b>257</b>	<b>34</b>	<b>5,205</b>	<b>5,496</b>
<b>Liabilities</b>				
Non-participating contract liabilities	234	43	5,099	5,376
Payables and other financial liabilities	1	16	9	26
<b>Total liabilities</b>	<b>235</b>	<b>59</b>	<b>5,108</b>	<b>5,402</b>



## 22. Risk management and control (cont'd)

**Table 1 – Currency risk**  
As at 31 December 2015 <sup>1</sup>

Shareholder	Euro £m	US Dollar £m	Sterling £m	Carrying value £m
<b>Assets</b>				
Financial Investments	-	35	262	297
<b>Total assets</b>	-	35	262	297
<b>Non profit non-unit linked</b>				
<b>Assets</b>				
Funds Withheld	41	-	4,173	4,214
Financial Investments	139	-	-	139
Cash and cash equivalents	9	-	-	9
<b>Total assets</b>	189	-	4,173	4,362
<b>Liabilities</b>				
Non-participating contract liabilities	177	32	4,091	4,300
Payables and other financial liabilities	-	6	3	9
<b>Total liabilities</b>	177	39	4,094	4,309

1. Restated

The Company's management of currency risk reduces shareholders' exposure to exchange rate fluctuations. The Company's exposure to a 10% exchange movement in the US Dollar and Euro on an IFRS basis, net of hedging activities, is detailed in Table 2.

**Table 2 – Currency risk analysis**

Currency sensitivity test	Euro 2016 £m	US 2016 £m	Restated Euro 2015 £m	Restated US 2015 £m
10% appreciation impact on profit post tax / equity	2.7	(3.2)	1.1	(1.0)

### Other price risk

Other price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices, other than those arising from interest rate risk or currency risk. These changes may be as a result of features of the individual instrument, its issuer, or factors affecting all similar financial instruments traded in the market.

The Company controls its exposure to geographic price risks by using internal country credit ratings. These ratings are based on macroeconomic data and key qualitative indicators. The latter take into account economic, social and political environments.

## 22. Risk management and control (cont'd)

Table 3 indicates the Company's exposure to different equity markets around the world.

Table 3 – Exposure to worldwide equity markets

	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m	Shareholder 2015 £m	Non profit non-unit linked 2015 £m	Total 2015 £m
UK	-	24	24	-	29	29
<b>Listed equities</b>	-	24	24	-	29	29
Unlisted non UK Equities	68	-	68	-	-	-
Holdings in unit trusts	221	2	223	297	-	297
<b>Total equities</b>	<b>289</b>	<b>26</b>	<b>315</b>	<b>297</b>	<b>29</b>	<b>326</b>

The funds withheld by LGAS includes non-unit linked property investments totaling £360m (2015: £314m) and equities totaling £24m (2015: £29m), which are all located in the UK.

### Credit risk

*Exposure to loss if another party fails to perform its financial obligations to the Company.*

Legal & General Group Plc's credit risk policy defines the overall framework for the management of credit risk. Credit risk exposures primarily arise in relation to corporate bonds.

The Company holds fixed and variable rate securities within the financial investments and funds withheld to back part of its insurance liabilities. Significant exposures are managed by the application and regular review of concentration limits, with allowance being made in the actuarial valuation of the insurance liabilities for possible defaults.

The funds withheld includes property lending and sale & leaseback investments. The Company is inherently exposed to the risk of default by a borrower or tenant. Each property lending and sale & leaseback investment transaction is subject to a due diligence process to assess the credit risks implicit in the transaction and confirm that the risk of default has been appropriately mitigated. The Company protects its interests through taking security over the underlying property associated with the investment transaction.

The credit profile of the Company's financial investments and funds withheld exposed to credit risk is shown in Table 4. The credit rating bands are provided by independent rating agencies. For unrated assets, such as cash and derivatives, not exposed to credit risk, the Company maintains internal ratings which are used to manage exposure to these counterparties.

The carrying amount of assets included in the statement of financial position represents the maximum credit exposure. No impairment provisions have been made.

22. Risk management and control (cont'd)

Table 4 – Exposure to credit risk including funds withheld

As at 31 December 2016 Shareholder	Notes	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated other £m	Total £m
Other fixed rate securities		-	-	28	-	-	-	28
<b>Total debt securities</b>		-	-	28	-	-	-	28
Cash and cash equivalents		-	-	1	-	-	-	1
<b>Financial assets</b>		-	-	29	-	-	-	29
<b>Non profit non-unit linked</b>								
Government securities	9/10/11	92	802	6	16	3	-	919
Other fixed rate securities	9/10/11	69	209	1,108	1,361	113	-	2,860
Variable rate securities	9/10/11	-	157	288	128	31	-	604
<b>Total debt securities</b>		161	1,168	1,402	1,505	147	-	4,383
Accrued interest	9/10/11	2	6	16	22	2	-	48
Loans and receivables	9/10/11	-	-	64	220	165	-	449
Derivative assets	9/10/11	-	-	-	-	-	210	210
Cash and cash equivalents	9/10/11	-	-	-	-	-	20	20
<b>Financial assets</b>		163	1,174	1,482	1,747	314	230	5,110
Other assets	10	-	-	-	-	-	360	360
		163	1,174	1,482	1,747	314	590	5,470

There are no impaired or past due financial assets within the portfolios in 2016.

Table 4 – Exposure to credit risk including funds withheld

As at 31 December 2015	Notes	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated other £m	Total £m
<b>Non profit non-unit linked</b>								
Government securities	9/10/11	99	479	12	15	3	-	608
Other fixed rate securities	9/10/11	61	171	862	1,160	87	-	2,341
Variable rate securities	9/10/11	-	140	252	128	32	-	552
<b>Total debt securities</b>		160	790	1,126	1,303	122	-	3,501
Accrued interest	9/10/11	2	6	14	22	2	-	46
Loans and receivables	9/10/11	-	1	74	132	104	-	311
Derivative assets	9/10/11	-	-	-	-	-	92	92
Cash and cash equivalents	9/10/11	-	-	-	-	-	69	69
<b>Financial assets</b>		162	797	1,214	1,457	228	161	4,019
Other assets	10	-	-	-	-	-	314	314
		162	797	1,214	1,457	228	475	4,333

There are no impaired or past due financial assets within the portfolios in 2015.

## 22. Risk management and control (cont'd)

### Liquidity risk

*The risk that the Company, though solvent, either does not have sufficient financial resources available to enable it to meet its obligations as they fall due, or can secure them only at excessive cost.*

Legal & General Group Plc's liquidity risk policy defines the overall framework for the management of liquidity risk. The Company does not seek exposure to liquidity risk in its own right, but recognises that exposure to liquidity risk can arise as a consequence of the markets in which it operates, the products that it writes and through the execution of investment management strategies.

The liquidity risks to which the Company's business may be exposed, primarily stem from low probability events that if not adequately planned for, may result in unanticipated liquidity requirements.

A limited level of contingent liquidity risk is an accepted element of writing contracts of insurance. However, the Company's insurance business seeks to maintain sufficient liquid assets and standby facilities to meet a prudent estimate of the cash outflows that may arise from contingent events. The level of required liquidity to be maintained by insurance funds is identified using techniques including cash flow analysis for ranges of extreme scenarios and stress tests for shock events.

To ensure an appropriate pool of liquid assets are maintained in line with a prudent estimate of cash outflows, the profile of investment assets held to meet future liabilities from writing insurance business are structured to include an appropriate proportion of cash and other readily realisable assets. The required profile is formally defined as part of asset benchmarks provided to the investment managers, with regular management information provided by the investment manager on the actual holding relative to the fund benchmark.

Specific liquidity risks associated with the Company's core product lines and the risk mitigation techniques are as follows:

Annuities: Potential for liquidity risk arises within two specific aspects of the Company's annuity business (i) changes in future pension commitments and (ii) collateral requirements risk hedging strategies.

(i) Changes in future pension commitments - once business has been written, cash outflows for pensions in payment are generally predictable, enabling the Company to structure the liquidity, income and maturity profile of investment assets backing long term liabilities to meet projected cash outflows. Although variations in longevity can alter the duration of outflows over the long term, trends are gradual, providing opportunity to respond with appropriate risk mitigation strategies.

(ii) Collateral requirements for risk hedging strategies - as part of the investment asset management strategy for the Company's annuity business, financial instruments are utilised to manage exposure to fluctuations in interest rates, inflation and foreign currency, which may otherwise result in long term liabilities being unmatched. The use of such financial instruments can require the posting of liquid collateral with counterparties, and as such an appropriate pool of the asset types specified by counterparties must either be held or readily available.

The Company manages its banking relationships, capital raising activities, overall cash and liquidity position and the payment of dividends, with support from its ultimate holding company, Legal & General Group Plc's treasury function. Legal & General Group Plc seeks to manage its corporate funds and liquidity requirements on a pooled basis and to ensure the Group maintains sufficient liquid assets and standby facilities to meet a prudent estimate of its net cash outflows. In addition, it ensures that, even under adverse conditions, the Group has access to the funds necessary to cover surrenders, withdrawals and maturing liabilities.

### Operational Risk

*Exposure to loss arising from inadequate or failed internal processes, people, systems, or from external events.*

Legal & General Group Plc's Operational risk policy defines the overall framework for the management of operational risk. The company does not have any operational risk appetite, and so seeks to mitigate operational risk wherever possible. However, there is a recognition that operational risk events may occur due to human error and external events that are beyond the control of the company. Operational risk events are logged, with material items worthy of additional attention presented to the risk committee.

There are a number of categories under which operational risk and its management across the Company can be considered

#### Internal process failure

The Company is potentially exposed to the risk of loss from failure of the internal processes with which it transacts its business. The Company seeks to ensure the adequacy of the controls over its processes through regular reviews and assessment of their appropriateness and effectiveness.

#### People

The Company is potentially exposed to the risk of loss from inappropriate actions by its staff. The risk is managed by business management and human resource (HR) functions. Recruitment is managed centrally by HR functions, and all new recruits are required to sign all Company policies. Employees have job descriptions setting out their accountabilities and reporting lines, and are appraised annually in accordance with agreed performance management frameworks. Employees are provided with appropriate training to enable them to meet the relevant regulatory requirements. Risks relating to health and safety and other legislation are managed through the provision of relevant training to all staff.

## **22. Risk management and control (cont'd)**

### **Outsourcing**

The Company is potentially exposed to the actions or failure of suppliers contracted to provide services on an outsourced basis. The required minimum standards of control for outsourced arrangements are set out in Legal & General Group's outsourcing and critical supplier policy.

### **Legal**

Legal risk is the risk of loss from unclear or deficient product documentation; inadequate documentation in support of material contracts such as reinsurance treaties; the incorrect interpretation of changes in legislation; employment related disputes and claims; and commercial disputes with suppliers. The risks are actively managed through the Legal & General Group legal risk framework, which defines minimum standards of control to be applied to minimise the risk of loss.

### **Compliance**

Compliance risk within the Company relates to the risk of non-adherence to legislative requirements, regulations and internal policies and procedures. Responsibility for ensuring adherence to relevant legal and regulatory requirements is vested in individual business managers.

### **Event**

Event risk relates to the potential for loss arising from significant external events such as terrorism, financial crisis and major changes in fiscal systems or disasters. Typically, such events have a low likelihood of occurrence, a material impact and can be difficult to prevent. The Company's risk mitigation focuses on minimising the business disruption and potential financial loss which may ensue from such an event. This includes maintaining a framework for the management of major incidents, the maintenance and regular testing of detailed business, technical and location recovery plans and the provision of insurance cover for the loss of buildings, contents and information technology systems and for the increased cost of working in the event of business disruption.

### **Fraud**

The Company is potentially exposed to the risk of internal fraud, claims-related fraud, and external action by third parties. The risk of internal fraud is managed through a number of processes including the screening of staff at recruitment, segregation of duties and management oversight. The activities of Internal Audit also act to counter the risk. Claims-related fraud is managed by ensuring business processes are designed to validate claims and ensure that only bona fide claims are settled. Anti-fraud techniques are regularly updated to mitigate risks and emerging threats. The Company's approach to mitigating fraud and other dishonest acts is supported by promoting an open and honest culture in all dealings between employees, managers and those parties with which the Company has contact. A formal Legal & General Group code of ethics sets out the Company's expectations in this respect. Effective and honest communication is essential if malpractice is to be effectively dealt with. The Company has defined whistle blowing procedures to enable all employees and those who work with the Company to raise matters of concern in confidence. Personnel independent of the business reporting line act as designated whistle blowing contacts.

### **Technology**

The Company places a high degree of reliance on IT in its business activities. The failure of IT systems could potentially expose the Company to significant business disruption and loss. To mitigate the risk, the Company works with its IT providers in ensuring appropriate standards and methodologies. Disaster recovery facilities enable IT operations to be conducted at remote locations in the event of the loss of computer facilities at a principal office site.

## 22. Risk management and control (cont'd)

### Sensitivity analysis

Table 5 shows the impact on pre-tax profit and equity, net of reinsurance, under each sensitivity scenario for the non-participating business.

	Impact on pre-tax profit net of reinsurance 2016 £m	Impact on equity net of reinsurance 2016 £m	Impact on pre-tax Profit net of reinsurance 2015 £m	Impact on Equity net of reinsurance 2015 £m
<b>Sensitivity test</b>				
10% decrease in equity values	-	-	-	-
7.5% decrease in property values	-	-	-	-
1% increase in interest rates	12	12	4	4
1% decrease in interest rates	(20)	(20)	(7)	(7)
Credit spread widens by 100 bps with no change in expected defaults	(4)	(4)	3	3
1% increase in inflation	(1)	(1)	5	5
10% fall in property	(8)	(8)	(5)	(5)
Annuity: +10bps in credit default assumption	(45)	(45)	(34)	(34)
Annuity: -10bps in credit default assumption	44	44	34	34
1% decrease in annuitant mortality	(21)	(21)	(16)	(16)
Default of largest reinsurer	-	-	-	-

- In calculating the alternative values, all other assumptions are left unchanged. In practice, items of the Company's experience may be correlated.
- The Company seeks to actively manage its asset and liability position. A change in market conditions may lead to changes in the asset allocation or charging structure which may have a more, or less, significant impact on the value of the liabilities. The analysis also ignores any second order effects of the assumption change, including the potential impact on the Company asset and liability position.
- These stresses use the assets that back the liabilities. Any excess assets have not been stressed in these calculations.
- The sensitivity of the profit to changes in assumptions may not be linear. They should not be extrapolated to changes of a much larger order.
- The change in interest rate test assumes a 100 basis point change in the gross redemption yield on fixed interest securities together with a 100 basis point change in the real yields on variable securities. Valuation interest rates are assumed to move in line with market yields adjusted to allow for the impact of PRA regulations.
- In the sensitivity for credit spreads corporate bond yields have increased by 100bps, gilt and approved security yields unchanged, and there has been no adjustment to the default assumptions.
- The inflation stress adopted is a 1% pa increase in inflation resulting in a 1% pa reduction in real yield and no change to the nominal yield.
- In addition the expense inflation rate is increased by 1% pa.
- The annuitant mortality stress is a 1% reduction in the mortality rates for immediate and deferred annuitants with no change to the mortality improvement rates (so for example a rate that was 80% of a standard table would become 79% of that standard table).