Registered Number 48340

Legal & General Reinsurance Company Limited
Report and Accounts 2017

Contents

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

Investment Committee

Kerrigan Procter	(Chairman)
Bryan Blunt	
Thomas Olunloyo	

Audit, Risk and Compliance Committee

Derek Stapley	(Chairman)
Bryan Blunt	
Troy Thompson	

General Management

Thomas Olunloyo	Chief Executive Officer (appointed 23/03/2017)
Brendan Kemp	Chief Financial Officer
Caspar Young	Chief Business Development Officer
Andrew Sooboodoo	Chief Risk Officer (appointed 23/03/2017)
Adrian Chapman	Chief Operating Officer (appointed 28/03/2018)
Michael Walsh	Chief Strategy Officer (appointed 28/03/2018)

Registered Office

The Company's registered office is Ground Floor, 19 Par-la-Ville Road, Hamilton, HM11, 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 2017.

Background and principal activities
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 ('PRT') in selected international markets.

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

Business Review
The Company holds Certified Reinsurer Status from Vermont (8 June 2017) and Maryland (3 February 2017) states and passporting approval from the National Association of Insurance Commissioners, which will reduce the administrative burden of achieving Certified Reinsurer Status in other US states.

The Company has consolidated its business strategy in 2017 to ensure the business is continuing to provide significant value for the shareholder. The Company has executed a related party general insurance treaty, which provides excess of loss coverage against United Kingdom ('UK') household insurance claims. However, the Company's primary source of revenue continues to be PRT business.

Financial position and results
The results show International Financial Reporting Standard ('IFRS') profits before tax of £100m (2016: £88m) and cash released from operations of £49m (2016: £75m). These metrics are consistent with the Group's key metrics. Revenue for the Company as a result of the quota share transaction with Legal & General Assurance Society Limited was £322m (2016: £604m) and the excess of loss coverage of Legal & General Insurance Limited was £4m (2016: N/A).

The Company holds £486m (2016: £413m) shareholder's equity to meet the Bermuda Solvency Capital Requirement ('BSCR') as at 31 December 2017.

Dividend
A dividend of £27m (2016: £25m) was declared by the Company's Board of directors in November 2017 and paid to the Company's shareholder on 14 December 2017.

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 23 of the financial statements. The Company has identified key risks as below:

<u>1) Regulatory change</u>
The markets in which the Company operates are highly regulated. Legislation and government fiscal policy influence the Company's product design. Regulation defines the overall framework for the structure and taxation of products and the capital that the Company holds. Significant changes in legislation or regulation may increase its cost base, reduce its future revenues and impact profitability or require it to hold more capital. The prominence of the risk increases where change is implemented without prior engagement with the sector. The nature of long–term business can also result in some changes in regulation, and the re-interpretation of regulation over time, having a retrospective effect on its in-force books of business, impacting the value of embedded future profits.

The Company bases its business strategy upon prevailing legislation and regulation, and known/anticipated change. To mitigate the risk the Company engages with legislative authorities where appropriate to assist in the evaluation of change on the sector and its stakeholders. However, sudden changes and/or retrospective changes in legislation and fiscal policy, or the differing interpretation and application of regulation over time, may have a detrimental effect on the delivery of the Company's strategy and profitability.

2) Financial market and economic conditions
2017 has seen volatility in financial markets as they have responded to uncertainties in the global economy and political events, such as the 2016 UK referendum on membership of the European Union ('Brexit').

There are not expected to be any primary impacts of Brexit for the Company. It is, however, probable that a potentially lengthy period of negotiation and an uncertain outcome will create ongoing uncertainty for financial markets and the broader global economy in which the Company operates, with potential for asset price shifts should uncertainty lead markets to reappraise their value.

The Company holds a broad range of investment assets to meet the obligations arising from writing insurance business. The performance and liquidity of investment markets, interest rate movements 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.

Interest rate expectations leading to falls in the risk free yield curve can also create a greater degree of inherent volatility to be managed in the local capital balance sheet, than the underlying economic position would dictate, potentially impacting capital requirements and surplus capital.

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

3) Counterparty and third party risks
The Company is exposed to default risk in respect of the issuers of corporate debt and financial instruments, through money market and reassurance transactions and as part of its banking arrangements. Third party risk arises with regard to reliance upon external suppliers of certain administration and information technology ('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. The Company also has the ability to withhold premiums on certain reassurance transactions to limit the exposure to counterparty failure. Specific reserves were also made, and continue to be, for defaults which help mitigate financial impacts should counterparties fail. Exposures against limits are actively monitored, with trigger levels being set and management action being taken to pre-empt loss from default events. However, in extreme circumstances, an event causing widespread default may impact the Company's profitability, whilst the loss of crucial suppliers may impact operational effectiveness.

4) Longevity and other assumption uncertainties
The Company writes significant levels of immediate and deferred annuities. The writing of long term insurance business necessarily requires the setting of assumptions for long term trends in factors such as mortality, persistency, valuation interest rates and credit defaults. Actual experience may result in the need to recalibrate these assumptions reducing profitability.

The Company uses its pricing capabilities to assess and charge an appropriate premium for known risk factors, with stress testing undertaken to validate the appropriateness of key assumptions. However, scenarios such as a dramatic advancement in medical science leading to unexpected changes in life expectancy, coupled with a reinsurer default may impact profitability and capital. Extreme shifts in financial markets and in the broader economic environment may also require other assumptions to be recalibrated.

5) Operational Risk
The Company's business processes can be complex, with significant reliance placed upon a combination of IT systems and manual processes. The Company has constructed a framework of internal controls to minimise the risk of unanticipated loss or damage to the Company's reputation. The Company seeks to continually review and improve its framework. The Group's Internal Audit function also provides independent assurance on the adequacy and effectiveness of its internal controls. However, no system of internal control can completely eliminate the risk of error, financial loss, fraudulent actions or reputational damage.

6) Digital Risk
As the Company increasingly digitises its business, the Company is inherently exposed to new risks. The Company is alive to cyber threats, in terms of protecting its customers' data, minimising damage to its reputation and potential for financial loss and works closely with its business partners to proactively manage emerging threats. As has been seen in other business sectors, it is possible that alternative digitally enabled providers of financial services products emerge with lower cost business models or innovative service propositions and capital structures and disrupt the current competitive landscape. The Company is executing a strategy that has digital at its heart.

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 the Company is responsible for the preparation of the financial statements contained in this report. These financial statements have been prepared in accordance with IFRS.

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 and 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 28 March 2018 and were signed on their behalf by:

B Blunt
Director

D Stapley
Non-executive Director

T Olunloyo
Director

Independent auditor's report

To the Board of Directors and Shareholder of Legal & General Reinsurance Company Limited

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 December 31, 2017 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 December 31, 2017;
- the statement of financial position as at December 31, 2017;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; 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.

PricewaterhouseCoopers Ltd., Chartered Professional Accountants, P.O. Box HM 1171, Hamilton HM EX, Bermuda
T: +1 (441) 295 2000, F:+1 (441) 295 1242, www.pwc.com/bermuda

Other information

Management is responsible for the other information. The other information comprises the Directors' Report on page 4 to 6 (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.

Responsibilities of management 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.

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.

PricewaterhouseCoopers Ltd.

Chartered Professional Accountants

Hamilton, Bermuda

March 28, 2018

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 December 2017

	Notes	**2017 £m**	2016 £m
Revenue			
Gross written premiums	1F/2	**326**	604
Net change in provision for unearned premiums	1F	**(2)**	-
Net premium earned		**324**	604
Investment return	1I/1L/1Q/3	**308**	767
Total revenue		**632**	1,371
Expenses			
Claims and change in insurance liabilities	1F/4	**524**	1,277
Acquisition costs	1F	**1**	1
Other expenses	1R/5	**7**	5
Total expenses		**532**	1,283
Profit for the year attributable to equity holders of the Company		**100**	88
Total comprehensive income for the year attributable to equity holders of the Company		**100**	88

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

Statement of Financial Position
As at 31 December 2017

	Notes	2017 £m	2016 £m
Assets			
Investment in subsidiary	1D/19/20	1	1
Funds withheld	1H/9	5,547	5,242
Financial investments	1I/1L/10/11	578	551
Other assets	12	9	-
Cash and cash equivalents	1K/13	27	21
Total assets		6,162	5,815
Equity			
Share capital	1N/14	-	-
Contributed surplus		220	220
Retained earnings		266	193
Total shareholder's equity		486	413
Liabilities			
Insurance contract liabilities	1F/1G/15/16	5,654	5,376
Payables and other financial liabilities	1L/1O/1P/11/17	22	26
Total liabilities		5,676	5,402
Total equity and liabilities		6,162	5,815

The Notes on pages 14 to 40 are an integral part of these financial statements.

The financial statements on pages 10 to 13 were approved by the board of directors on 28 March 2018 and were signed on their behalf by:

B Blunt
Director

D Stapley
Non-executive Director

T Olunloyo
Director

Statement of Changes in Equity

For the year ended 31 December 2017

For the year ended 31 December 2017	Notes	Share capital £m	Contributed Surplus £m	Retained earnings £m	Total equity £m
As at 1 January		**-**	**220**	**193**	**413**
Total comprehensive income for the year		**-**	**-**	**100**	**100**
Dividend	8	**-**	**-**	**(27)**	**(27)**
As at 31 December 2017		**-**	**220**	**266**	**486**
For the year ended 31 December 2016					
As at 1 January		-	220	130	350
Total comprehensive income for the year		-	-	88	88
Dividend	8	-	-	(25)	(25)
As at 31 December 2016		-	220	193	413

Statement of Cash Flows
For the year ended 31 December 2017

	Notes	**2017 £m**	2016 £m
Cash flows from operating activities			
Profit for the year		**100**	88
Adjustments for non-cash movements in profit for the year			
Unrealised gains on financial investments		**(10)**	(30)
Accrued dividends and interest income		**(1)**	-
Foreign exchange gain		**(1)**	(4)
Net (increase) / decrease in operating assets			
Funds withheld (increase)		**(305)**	(1,028)
Net decrease / (increase) in non profit non-unit linked investments		**1**	(43)
Net (increase) in other assets		**(9)**	-
Net increase / (decrease) in operating liabilities			
Net increase in insurance contract liabilities		**278**	1,076
Net (decrease) / increase in payables and other financial liabilities		**(4)**	16
Net cash flows from operating activities		**49**	75
Cash flows from investing activities			
Purchases of financial investments		**(540)**	(338)
Proceeds from sales and maturities of financial investments		**521**	298
Dividends received		**3**	2
Net cash flows used in investing activities		**(16)**	(38)
Cash flows from financing activities			
Dividend distributions to ordinary equity holder of the Company during the year	8	**(27)**	(25)
Net cash flows used in financing activities		**(27)**	(25)
Net increase in cash and cash equivalents		**6**	12
Cash and cash equivalents at the beginning of the year		**21**	9
Cash and cash equivalents at 31 December	13	**27**	21

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 Act'). The principal activity of the Company is the provision of life reinsurance solutions globally, focussing initially on pensions risk transfer ('PRT') in selected international markets.

The Company's financial statements have been prepared in accordance with International Financial Reporting Standard ('IFRS') issued by the International Accounting Standards Board ('IASB'). The Company's financial statements also comply with International Financial Reporting Interpretations Committee ('IFRIC') interpretations as issued by the IASB. The financial statements have been prepared under the historical cost convention, with the exception of financial assets, financial liabilities and investments in subsidiaries which are reported 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 Statement of Profit or Loss and Other Comprehensive Income 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 1H, 1I, 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.

Estimation of deferred acquisition costs

Costs are incurred in connection with acquiring new business, such as initial commission and the indirect costs of obtaining and processing new business. These costs are capitalised and amortised in accordance with the Company's accounting policies. The recoverability of these assets is assessed and impaired if the projected future margins are less than the carrying value of the assets. To the extent that the future margins differ from those anticipated, an adjustment to the carrying value of the deferred acquisition cost assets will be necessary.

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.

Non-participating insurance contract liabilities (Notes 1F, 1G, 15, 16) 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 16.

1. Accounting policies (cont'd)

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 cost.

E Product classification

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

F Insurance contract liabilities

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

Non-participating insurance contract liabilities

Premiums are recognised as revenue when due for payment. Claims and surrenders are accounted for when payment is due. Claims payable include the direct costs of settlement. Acquisition costs comprise direct costs, such as initial commission, and the indirect costs of obtaining and processing new business. These costs are charged to the Statement of Profit or Loss and Other Comprehensive Income when incurred.

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.

General insurance contracts

Premiums are accounted for in the period in which the risk commences as gross written premium. For all these contracts, premiums are recognised as revenue (earned premiums) proportionally over the period of coverage. The portion of gross written premium on in-force contracts that related to unexpired risks at the balance sheet date is reported as the provision for unearned premium. Premiums are shown before deduction of commission.

Unearned premiums represent the proportion of premiums written in the year that relate to unexpired terms of policies in force at the balance sheet date, calculated on a time-apportioned basis. A proportion of commission and other acquisition expenses relating to unearned premiums is carried forward as deferred acquisition costs ('DAC'). DAC are deferred over the period in which the related premiums are earned. All other costs are recognised as expenses when incurred.

Claims incurred comprise of claims and related expenses paid in the year and changes in the provisions for outstanding claims. This includes provisions for claims incurred but not reported ('IBNR') and related expenses, together with any other adjustments to claims from previous years.

Provision is made at the balance sheet date for the estimated cost of claims and related insurance recoveries incurred but not settled at that date, including the costs of claims incurred but not yet reported to the Company. The estimated costs of claims include expenses to be incurred in settling claims and a deduction for the expected value of salvage and other recoveries. The Company takes all reasonable steps to ensure that it has appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

G Liability adequacy tests (Note 15)

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 Statement of Profit or Loss and Other Comprehensive Income by establishing a provision for losses.

H Funds Withheld (Note 9)

Funds withheld represent amounts contractually withheld by Legal & General Assurance Society Limited ('LGAS') in accordance with the reinsurance agreement. The value of the assets withheld and interest income are recorded in accordance with specific treaty terms.

1. Accounting policies (cont'd)

H Funds Withheld (Note 9) (cont'd)

As part of the reinsurance agreement, LGAS contractually withholds assets equal to 101% (2016: 101%) of their IFRS 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, although it does not directly own them. 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. To mitigate this risk, the Company helps set the investment guidelines followed by LGAS and monitors compliance thereto.

I Investments (Note 10,11,12)

Financial Assets

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 classified as HFT and FVTPL are measured at fair value with gains and losses reflected in the Statement of Profit or Loss and Other Comprehensive Income. Transaction costs are expensed as incurred.

Certain 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 insurance contract liabilities investments 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.

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 Français 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.

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

The shareholder is 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. The shareholder of the Company is directly exposed to market, credit and currency risk on these assets.

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 Statement of Profit or Loss and Other Comprehensive Income. 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. Impairment is only recognised if the loss event has an impact on the estimated future cash flows of assets held at amortised cost.

Assets which are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

1. Accounting policies (cont'd)

K Cash and cash equivalents (Note 13)

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 (Note 10,11,17)

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 Statement of Profit or Loss and Other Comprehensive Income over the borrowing period using the effective interest method.

N Share capital (Note 14)

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.

Dividend recognition

A dividend distribution to the Company's shareholder 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 (Note 17)

Payables and other financial liabilities comprise derivative liabilities, collateral received from banks and other liabilities. The derivative liabilities comprise a variety of exchange traded and over-the-counter derivative financial instruments, including, futures, options, 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 currency monetary assets and liabilities are translated at the spot rate at period end. 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 (Note 3)

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 and liabilities.

Investment income includes dividends and interest. Dividends are accrued on an ex-dividend basis. Interest is 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 (Note 5)

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

1. Accounting policies (cont'd)

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 2017 but which the Company has not adopted early, as follows:

- **IFRS 15 – Revenue from Contracts with Customers**
  IFRS15, '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. The standard does not apply to business classified as insurance contracts, and therefore no impact is expected on the effective date.

- **IFRS 16 - Leases**
  In January 2016, the IASB issued IFRS 16, "Leases", effective for annual periods beginning on or after 1 January 2019, subject to European Union ('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 Statement of Financial Position. 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 2018 however no impact is expected as the Company has no leases. The Company does not intend to early adopt this standard.

- **IFRS 17 – Insurance Contracts**
  IFRS 17, 'Insurance Contracts' was issued in May 2017 and is effective for annual periods beginning on or after 1 January 2021 (subject to EU endorsement). The standard will be applied retrospectively, subject to the transitional options provided for in the standard, and provides a comprehensive approach for accounting for insurance contracts including their valuation, Statement of Profit or Loss and Other Comprehensive Income presentation and disclosure. The Company has mobilised a project to assess the financial and operational implications of the standard and work will continue throughout 2018 to ensure technical compliance and to develop the required system capability to implement the standard.

- **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. IFRS 4 has been amended to include the option to defer IFRS 9 until the earlier of the implementation of the new insurance standard or 1 January 2021. Management has met the criteria to qualify for the temporary deferral until the implementation of the new insurance standard.

  For an insurer to apply this deferral,
  1. Total liabilities related to insurance must exceed 90%; or
  2. Total liabilities related to insurance are greater than 80% but less than 90% so long as the insurer does not engage in significant activity unconnected to insurance.

  Total liabilities connected to insurance within the company at 31 December 2017 were 99% and the company will therefore apply the deferral of IFRS 9.

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 amounts to £326m (2016: £604m). £322m (2016: £604m) relates to inward reinsurance premiums of long term business classified as non-participating premiums. In July 2017 the Company entered into an excess of loss treaty with Legal & General Insurance Limited ('LGIL') for £4m (2016: £Nil). All premium is sourced in the UK (2016: UK).

3. Investment return

	2017 £m	2016 £m
Financial investment return [1 2]	**308**	767
Total Investment return	**308**	767

1. Financial investment return includes fair value gains and losses, dividends and interest. Investment return is stated net of investment management fees and rebates.
2. Net gain (including interest and dividend income) of £279m (2016: gain £722m) arose in the year on the funds withheld (see Note 9). Net gains of £19m (2016: £47m) arose on financial investments designated as FVTPL and £10m (2016: loss £2m) arose on derivative contracts classified as HFT.

4. Claims and change in insurance liabilities

From continuing operations	**2017 £m**	2016 £m
Claims paid - gross	**253**	237
Change in insurance liabilities [1] - gross	**271**	1,040
Total claims and change in insurance liabilities	**524**	1,277

1. The change in reserves includes an increase of £271m (2016: increase of £1,011m) from the LGAS quota share, an increase of £4m (2016: increase of £4m) from the expense reserves and a decrease of £4m (2016: increase of £25m) from the Dutch business. The Company has not paid claims on the excess of loss coverage LGIL treaty. The roll-forward of the insurance contract liabilities is provided in Note 15.

5. Other expenses

	2017 £m	2016 £m
Other administrative expenses [1]	**7**	5
Total other expenses	**7**	5

1. 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 (2016: 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 20(vi) & 20(vii) Related party transactions.

7. Foreign exchange and exchange rates

Investment income for the year includes a foreign exchange loss of £2m (2016: loss £30m) arising on conversion of foreign currency monetary assets and liabilities to functional currency. Foreign exchange includes gains realised during the year from foreign currency financial investments amounting to £1m (2016: loss £4m).

Principal rates of exchange used for translation are:

	2017 Average	**2017 Year-End**	2016 Average	2016 Year-End
United States Dollar	**1.289**	**1.353**	1.355	1.236
Canadian Dollar	**1.687**	**1.695**	1.779	1.657
Euro	**1.142**	**1.127**	1.224	1.172

8. Dividend

	Dividend Per share 2017 £	**Total 2017 £m**	Dividend Per share 2016 £	Total 2016 £m
Ordinary share dividends paid in the year				
- Current year dividend	**108**	**27**	100	25
Total Dividend	**108**	**27**	100	25

On 14 December 2017 the Company paid a dividend of £27m (2016: £25m) to its parent company, Legal & General Re Holdings Limited.

9. Funds Withheld

Investment gains on funds withheld represented 44.1% (2016: gains of 52.2%) of the Company's revenue in 2017. Funds withheld totaled £5,547m (2016: £5,242m) at 31 December 2017.

Funds withheld comprised 90.0% (2016: 90.2%) of the Company’s total assets as of 31 December 2017. All of the Company’s funds withheld balance is associated with its reinsurance of LGAS annuity contracts.

Income accrues on the withheld assets according to the terms defined in the reinsurance treaty and the Company estimated the return was approximately 5.0% (2016: 13.7%) for the year ended 31 December 2017. The ratings of the assets underlying the funds withheld are shown in Note 23 Table 2.

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 15(iii).

10. Financial investments

(i) Financial investments at fair value

	Notes	Shareholder 2017 £m	Non profit non-unit linked 2017 £m	Total 2017 £m
Financial investments at fair value designated as:				
Fair value through profit or loss		**351**	**222**	**573**
Held for trading		**1**	**4**	**5**
Total financial investments	10(ii)	**352**	**226**	**578**
Expected to be received within 12 months				**10**
Expected to be received after 12 months				**568**

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

The risks associated with financial investments are outlined in Note 23.

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 £136.4m (2016: £143.8m) of debt securities pledged as collateral against ASR Levensverzekering N.V. The assets used as collateral are AAA, AA, A, BBB Corporate Bonds (2016: AAA, AA, A, BBB Corporate Bonds) having a residual maturity of up to 28 years (2016: 30 years). 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.

Private equity investments are included within equity securities and debt securities. A profit of £2.4m (2016: £0.6m) has been recognised in the Statement of Profit or Loss and Other Comprehensive Income in respect of the movement in fair value of these investments (Note 10(ii) b)).

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:

As at 31 December 2017	Total £m	Level 1 £m	Level 2 £m	Level 3 £m
Shareholder				
Equity securities	**314**	**276**	**-**	**38**
Debt securities	**37**	**25**	**2**	**10**
Derivative assets	**1**	**1**	**-**	**-**
Non profit non-unit linked				
Equity securities	**3**	**3**	**-**	**-**
Debt securities	**217**	**26**	**191**	**-**
Accrued interest	**2**	**-**	**2**	**-**
Derivative assets	**4**	**-**	**4**	**-**
Total financial investments	**578**	**331**	**199**	**48**

As at 31 December 2016	Total £m	Level 1 £m	Level 2 £m	Level 3 £m
Shareholder				
Equity securities	290	264	-	26
Debt securities	28	-	28	-
Non profit non-unit linked				
Equity securities	2	2	-	-
Debt securities	221	28	193	-
Accrued interest	2	-	2	-
Derivative assets	8	-	8	-
Total financial investments	551	294	231	26

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 the Company's pricing providers and a number of their contributing brokers, the Company has considered that these prices are not from a suitably active market and have classified them as level 2.

10. Financial investments (cont'd)

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 the shareholder is exposed and reflect unquoted equities including investments in private equity, property vehicles, 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.

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. Level 3 assets, where internal models are used, represent a small proportion of assets to which shareholders are exposed. These comprise property, unquoted equities, untraded debt securities and securities where the broker methodology is unknown. Unquoted securities include suspended securities excluding investments in private equity and property vehicles. Untraded debt securities include private placements, commercial real estate loans, income strips and lifetime mortgages.

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 within Level 3.

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.

(a) Assets measured at fair value based on level 3

	Equity securities 2017 £m	**Debt securities 2017 £m**	**Total 2017 £m**	Equity securities 2016 £m	Debt securities 2016 £m	Total 2016 £m
As at 1 January	**26**	**-**	**26**	-	-	-
Total gains or losses for the period:						
- unrealised gains/(losses) in profit and loss	**4**	**(2)**	**2**	1	-	1
Purchases / Additions	**8**	**-**	**8**	25	-	25
Sales / Disposals	**-**	**(16)**	**(16)**	-	-	-
Transfers into Level 3	**-**	**28**	**28**	-	-	-
As at 31 December	**38**	**10**	**48**	26	-	26

The Company holds regular discussion with pricing providers to determine whether transfers or classifications between levels of the fair value hierarchy have occurred.

10. Financial investments (cont'd)

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

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	**Current fair value 2017 £m**	**Reasonably possible alternative assumptions Increase in fair value 2017 £m**	**Reasonably possible alternative assumptions Decrease in fair value 2017 £m**	Current fair value 2016 £m	Reasonably possible alternative assumptions Increase in fair value 2016 £m	Reasonably possible alternative assumptions Decrease in fair value 2016 £m
Assets							
Shareholder							
- Unquoted investments in Unconsolidated Property Vehicles [1]	Prices supplied by property pricing team	**38**	**2**	**(2)**	26	2	(2)
- Debt Securities where broker methodology is unknown [2]	Prices sourced directly from brokers	**10**	**-**	**-**	-	-	-
Total		**48**	**2**	**(2)**	26	2	(2)

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, Pemberton European Mid-Market Debt Fund I('Pemberton'): Fund investing in senior secured unlisted loans, structured as a Luxembourg Limited Partnership and Built to Rent: a property fund structured as an English Limited Partnership investing in U.K. rental residential developments with a valuation methodology based on RICS property surveys.
2. Includes a direct investment in Ahana Operations LLC: a private placement senior secured infrastructure loan. Valuations are provided independently from broker.

11. Derivative assets and liabilities

	Fair values Assets 2017 £m	**Liabilities [1] 2017 £m**	Fair values Assets 2016 £m	Liabilities [1] 2016 £m
Shareholder				
Interest rate contracts - held for trading	**-**	**-**	-	-
Equity/ index derivatives - held for trading	**1**	**(1)**	-	-
Total shareholder	**1**	**(1)**	-	-
Non profit non-unit linked derivatives:				
Interest rate contracts - held for trading	**4**	**(5)**	8	(3)
Forward foreign exchange contracts - held for trading	**-**	**-**	-	(1)
Currency swap contracts - held for trading	**-**	**-**	-	(7)
Total non profit non-unit linked derivatives	**4**	**(5)**	8	(11)
Total derivative assets and liabilities	**5**	**(6)**	8	(11)

1. Derivative liabilities are reported in the Statement of Financial Position within Note 17 Payables and other financial liabilities.

11. Derivative assets and liabilities (cont'd)

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

		Maturity profile of undiscounted cash flows					
As at 31 December 2017	**Fair values £m**	**Within 1 year £m**	**1-5 years £m**	**5-15 years £m**	**15-25 years £m**	**Over 25 years £m**	**Total £m**
Cash inflows							
Shareholder							
Derivative assets	**1**	**34**	**1**	**-**	**-**	**-**	**35**
Derivative liabilities	**(1)**	**19**	**2**	**2**	**-**	**-**	**23**
Non profit non-unit linked derivatives							
Derivative assets	**4**	**22**	**54**	**88**	**13**	**6**	**183**
Derivative liabilities	**(5)**	**7**	**20**	**45**	**74**	**24**	**170**
Total	**(1)**	**82**	**77**	**135**	**87**	**30**	**411**
Cash outflows							
Shareholder							
Derivative assets	**1**	**(33)**	**(1)**	**-**	**-**	**-**	**(34)**
Derivative liabilities	**(1)**	**(20)**	**(2)**	**(2)**	**-**	**-**	**(24)**
Non profit non-unit linked derivatives							
Derivative assets	**4**	**(24)**	**(55)**	**(87)**	**(12)**	**(6)**	**(184)**
Derivative liabilities	**(5)**	**(8)**	**(25)**	**(54)**	**(76)**	**(24)**	**(187)**
Total	**(1)**	**(85)**	**(83)**	**(143)**	**(88)**	**(30)**	**(429)**
Net shareholder derivatives cashflows		**-**	**-**	**-**	**-**	**-**	**-**
Net non profit non-unit linked derivatives cash flows		**(3)**	**(6)**	**(8)**	**(1)**	**-**	**(18)**

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

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 13).

12. Other assets

	Shareholder 2017 £m	Non profit non-unit linked 2017 £m	Total 2017 £m	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m
Other receivables [1]	**3**	**6**	**9**	-	-	-
Total other assets	**3**	**6**	**9**	-	-	-
Due within 12 months			**9**			-
Due after 12 months			**-**			-

1. Includes receivables from brokers.

13. Cash and cash equivalents

	Shareholder 2017 £m	Non profit non-unit linked 2017 £m	Total 2017 £m	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m
Cash at bank and in hand [1]	**11**	**16**	**27**	1	20	21
Total cash and cash equivalents	**11**	**16**	**27**	1	20	21

1. Cash at bank includes £2m (2016: £11m) 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.

14. Share capital

	Number of shares	2017 £	2016 £
Issued share capital:			
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 holder of the Company's ordinary shares is entitled to receive dividends as declared and is entitled to one vote per share at shareholder meetings of the Company.

15. Insurance contract liabilities

(i) Analysis of insurance contract liabilities

	Notes	Gross 2017 £m	Reinsurance 2017 £m	Gross 2016 £m	Reinsurance 2016 £m
Non-participating insurance contracts	15(iii)	**5,652**	-	5,376	-
General insurance contracts[1]		**2**	-	-	-
Total insurance contract liabilities		**5,654**	-	5,376	-

[1]General insurance contracts provision for unearned premiums

15. Insurance contract liabilities (cont'd)

(ii) Expected insurance contract liability cash flows

As at 31 December 2017	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	**1,456**	**2,686**	**1,968**	**1,732**	**7,843**	**5,652**
General insurance contracts	**2**	**-**	**-**	**-**	**-**	**2**
Non-participating insurance contract liabilities	**1,458**	**2,686**	**1,968**	**1,732**	**7,843**	**5,654**

Insurance contract undiscounted cash flows are based on the expected date of settlement. The weighted average discount rate applied for the carrying value is 2.23%.

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
Non-participating insurance contract liabilities	1,383	2,590	1,951	1,821	7,745	5,376

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%.

(iii) Movement in non-participating insurance contract liabilities

	Note	Gross 2017 £m	Gross 2016 £m
As at 1 January		**5,376**	4,300
New liabilities in the period		**397**	561
Liabilities discharged in the year		**(314)**	(284)
Unwinding of discount rates		**132**	147
Effect of change in non-economic assumptions	16	**(48)**	1
Effect of change in economic assumptions	16	**132**	684
Other		**(22)**	(33)
As at 31 December		**5,652**	5,376
Expected to be settled within 12 months		**292**	278
Expected to be settled after 12 months		**5,360**	5,098

(iv) Movement in general insurance contract liabilities

	Note	Gross 2017 £m	Gross 2016 £m
As at 1 January		**-**	-
Earned in the year		**-**	-
Gross written premiums in respect of future periods		**2**	-
As at 31 December		**2**	-
Expected to be settled within 12 months		**2**	-
Expected to be settled after 12 months		**-**	-

16. 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 Prudential Regulatory Authority ('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 the Company's 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.

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 c33bps (2016: 33bps) and c40bps (2016: 40bps) per annum 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 £287m (2016: £273m) and £15m (2016: £12m) respectively.

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.

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:

	2017 UK	**2017 Dutch**	2016 UK	2016 Dutch
(i) Rate of interest/discount rate[1]				
Annuities in deferment	**2.26% pa**	**1.53% pa**	2.47% pa	1.69% pa
Annuities in deferment (RPI linked; net rate after allowance for inflation)	**-1.20% pa**		-1.10% pa	
Vested annuities	**2.26% pa**	**1.53% pa**	2.47% pa	1.69% pa
Vested annuities (RPI linked; net rate after allowance for inflation)	**-1.20% pa**		-1.10% pa	
(ii) Mortality Tables				
Annuities in deferment [3]	**75.6% - 84.2% PCXA00/PNXA00**[2]	**76.0%-83.0% M/F AG2014**	81.3% - 83.4% PCXA00/PNXA00[2]	76.0%-83.0% M/F AG2014
Vested annuities [3]				
- Bulk purchase annuities	**76.4% - 84.2% PCMA00/PCFA00**	**76.0%-83.0% M/F AG2014**	82.2% - 83.4% PCMA00/PCFA00	76.0%-83.0% M/F AG2014
- Other annuities	**60.9% - 115.5% PCMA00/PCFA00**		60.7% - 129.1% PCMA00/PCFA00	

1. Until 2017 the Company utilised a rate of interest/discount rate equal to 10% of that used by the cedants as an approximation. During the year, the Company refined their estimate to approximate the rate of interest/discount rate on the specific assets backing the Company's portion of the liabilities assumed from the cedant.
2. Table created by blending PCXA00 with PNXA00 tables. The base table to be used for bulk purchase annuity policies in deferment is PNMA00 up to and including age 55 and PCMA00 for age 65 and above for males. The identical method is applied to females using PNFA00 and PCFA00.
3. For vested and deferred annuities, mortality rates are assumed to reduce according to an adjusted CMI's mortality improvement model. The model reflects population experience and projects current rates of mortality improvements to a user defined Long Term Rate. The Long Term Rate has been determined using a combination of the Company's internal Cause of Death model and expert judgment with the following parameters:

   -Males: Long Term Rate – UK 2.0% (2016: 2.0%) p.a. / Dutch 2.0% (2016: 2.0%) up to age 85 tapering to 0% at 120.
   -Females: Long Term Rate – UK 1.5% (2016: 1.5%) p.a. / Dutch 2.0% (2016: 2.0%) up to age 85 tapering to 0% at 120.

16. Long term insurance valuation assumptions (cont'd)

Additional period smoothing is applied for males only by age-specific constant additions to initial rates.
In aggregate, assumptions regarding future longevity improvement at the end of 2017 have developed in line with emerging experience.
Different business classes have different effective dates for applying improvers.
For certain annuities, a further allowance is made for the effect of initial selection.
The basis above is applicable up to age 90. After age 90 the basis is blended towards a bespoke table from age 105 onwards (2016: After age 90 the basis is blended towards a bespoke table from age 105 onwards).

17. Payables and other financial liabilities

	Notes	**Shareholder 2017 £m**	**Non profit non-unit linked 2017 £m**	**Total 2017 £m**	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m
Derivative liabilities	11	**1**	**5**	**6**	-	11	11
Other liabilities		**3**	**4**	**7**	-	-	-
Collateral received from banks		**-**	**2**	**2**	-	8	8
Intercompany balances due	20(vi)	**-**	**7**	**7**	-	7	7
Payables and other financial liabilities		**4**	**18**	**22**	-	26	26
Settled within 12 months				**17**			19
Settled after 12 months				**5**			7

Payables and other financial liabilities settled after 12 months are expected to be settled within five years with the exception of derivative liabilities, as disclosed in Note 11.

Fair value hierarchy

As at 31 December 2017	**Total £m**	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Amortised cost £m**
Derivative liabilities	**6**	**1**	**5**	**-**	**-**
Other liabilities	**7**	**1**	**-**	**-**	**6**
Collateral received from banks	**2**	**2**	**-**	**-**	
Intercompany balances due [1]	**7**	**7**	**-**	**-**	**-**
Payables and other financial liabilities	**22**	**11**	**5**	**-**	**6**

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	-	-	-	-	-
Collateral received from banks	8	8	-	-	-
Intercompany balances due [1]	7	7	-	-	-
Payables and other financial liabilities	26	16	10	-	-

1. See Note 20(vi) Related party transactions.

There have been no significant transfers between levels (2016: No significant transfers).

18. Contingent liabilities, guarantees and indemnities

Provisions for the liabilities arising under contracts with policyholders is based on certain assumptions. The variance between actual experience from that assumed may result in those liabilities differing from the provisions made for them. Liabilities may also arise in respect of claims relating to the interpretation of policyholder contracts, or the circumstances in which policyholders have entered into them. The extent of these liabilities is influenced by a number of factors including the actions and requirements of the regulators.

In 2017, a liquidity facility ('LF') provided by the Group to LGIL was increased to enable LGIL to accept transfers of assets in specie from the Company in place of cash settlements. The Company agreed to pay LGIL's increased LF commitment fee and margin costs to allow LGIL to make drawings from the LF if required.

The Company did not have any other contingent liabilities, guarantees or indemnities in 2017 (2016: nil) arising as part of its normal course of business.

19. 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, 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$0.12m (£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 cost.

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.

20. Related party transactions

(i) Reinsurance
The Company is acting as reinsurer to its sister entity, LGAS. The Company accepted £322m (2016: £604m) of reinsurance premium for reinsuring non-participating insurance business, paid £0.8m (2016: £1.3m) in commission and paid £243m (2016: £228m) in claims during the year. A non-participating insurance liability of £5,419m (2016: £5,146m) is held to cover this business.

On July 2017 the Company entered into an excess of loss reinsurance treaty with its sister entity LGIL. The Company accepted £4m (2016: N/A) of reinsurance premium of which £2m is unearned (2016: N/A), incurred £0.4m (2016: N/A) in commission of which £0.2m is deferred (2016: N/A) and paid no claims (2016: N/A) during the year. In 2017, a liquidity facility ('LF') provided by the Group to LGIL was increased to enable LGIL to accept transfers of assets in specie from the Company in place of cash settlements. The Company agreed to pay LGIL's increased LF commitment fee and margin costs to allow LGIL to make drawings from the LF if required.

(ii) Investments in Group unit trusts and the Group liquidity funds
The Company held £244m (2016: £223m) of investments in unit trusts, controlled and managed by Group companies that are classified as other related parties. The Company made losses of £13m (2016: gain £28m) from those trusts.

(iii) Investments in Funds withheld
The Company held £5,547m (2016: £5,242m) in funds withheld by its sister entity LGAS. Net gain of £279m (2016: gain of £722m) arose in the year on the funds withheld (See Note 9).

(iv) Investment in subsidiary
The Company held a £529k (2016: £528k) investment in its subsidiary L&G SAC (see note 19).

20. Related party transactions (cont'd)

(v) Other assets

As at 31 December	2017 £m	2016 £m
Due from other related party:		
- Premium receivable	**2**	-
- Deferred acquisition costs [1]	**-**	-
Total	**2**	-

1. Deferred acquisition costs from the LGIL treaty amount to £0.2m (2016: N/A).

(vi) Payables and other financial liabilities

As at 31 December	2017 £m	2016 £m
Due to other related party:		
- Management charges due [1]	**7**	7
Total	**7**	7

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.

(vii) Other charges

For the year ended 31 December	2017 £m	2016 £m
Management charges [1]	**7**	6
Total charges	**7**	6

1. See note under table 20(vi). £4m (2016: £4m) of management charges are staff related costs.

(viii) Dividends
On 14 December 2017, the Company paid a dividend of £27m (2016: £25m) to its parent company, Legal & General Re Holdings Limited.

21. 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.

21. Management of capital resources (cont'd)

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. 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 Bermudian statutory accounts prepared due to its status as a class E reinsurer. The Company's total capital resources of £486m (2016: £413m) comprise capital contribution from the ultimate parent of £220m (2016: £220m) and £266m (2016: £193m) in respect of retained earnings after payment of a £27m dividend (2016: £25m).

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.

22. 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
The Shareholder is 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. The shareholder of the Company is 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 23 (Risk management and control) have been provided using this categorisation.

	Shareholder 2017 £m	**Non profit non-unit linked 2017 £m**	**Total 2017 £m**	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m
Assets						
Investment in subsidiary	**-**	**1**	**1**	-	1	1
Funds Withheld	**-**	**5,547**	**5,547**	-	5,242	5,242
Financial Investments	**352**	**226**	**578**	318	233	551
Other assets	**3**	**6**	**9**	-	-	-
Cash and cash equivalents	**11**	**16**	**27**	1	20	21
Total assets	**366**	**5,796**	**6,162**	319	5,496	5,815
Liabilities						
Insurance contract liabilities	**-**	**5,654**	**5,654**	-	5,376	5,376
Payables and other financial liabilities	**4**	**18**	**22**	-	26	26
Total liabilities	**4**	**5,672**	**5,676**	-	5,402	5,402

23. 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.

Governance Framework
A key part of the risk management process is a robust governance framework. The Company operates a three lines of defense governance structure. The first line is represented by risk owners 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 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 are 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.

The Group'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 funds withheld investment risk policy, as noted below, to LGAS. The Company manages market risk using the following methods:

<u>Asset liability matching</u>
The Company manages its assets and liabilities in accordance with relevant regulatory requirements, reflecting the differing types of liabilities it has on the Company Statement of Financial Position.

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.

23. Risk management and control (cont'd)

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

Derivatives
The Company uses derivatives to reduce the market risk arising in the 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.

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 3 on page 40.

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 has minimal exposure to currency risk from financial instruments held in currencies other than their functional currencies, as nearly all such holdings are backing either insurance or investment contract liabilities or hedging.

The Company operates internationally and as a result is exposed to foreign currency exchange risk arising from fluctuations in exchange rates of various currencies, of which the largest is Euro. The Company does not hedge foreign currency revenues as these are substantially retained locally to support the growth of the Group's business and meet local regulatory and market requirements.

The Company aims to maintain sufficient assets in local currency to meet local currency liabilities however movements may impact the value of the Company's shareholder's equity which is expressed in sterling. This aspect of foreign exchange risk is monitored and managed, against pre-determined limits. These exposures are managed by aligning the deployment of regulatory capital by currency with the Company's regulatory capital requirements by currency. Currency borrowings and derivatives are used to manage exposures within the limits that have been set.

As at 31 December 2017, the Company held 19% (2016: 1%) of its total equity attributable to the shareholder in currencies, mainly US dollar and Euro, other than the functional currency. The exchange risks inherent in these exposures are mitigated through the use of derivatives, mainly forward currency contracts, cross currency basis swaps and futures.

The Company's management of currency risk reduces the shareholder's exposure to exchange rate fluctuations. The Company's exposure to a 10% exchange movement in the US Dollar and Euro on an IFRS basis, where the values of economic hedging instruments are reflected at their carrying value as opposed to their notional amounts, are reflected below. A 10% appreciation in the US Dollar to Sterling period-end foreign exchange rate would have a £2.6m (2016: -£3.2m) impact on shareholder equity and a 10% appreciation in the Euro to Sterling period-end foreign exchange rate would have a £4.3m (2016: £2.7m) impact on shareholder equity respectively.

23. Risk management and control (cont'd)

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 geographical 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.

Table 1 indicates the Company's exposure to different equity markets around the world.

Table 1 – Exposure to worldwide equity markets

	Shareholder 2017 £m	**Non profit non-unit linked 2017 £m**	**Total 2017 £m**	Shareholder 2016 £m	Non profit non-unit linked 2016 £m	Total 2016 £m
UK	**-**	**26**	**26**	-	24	24
Listed equities	**-**	**26**	**26**	-	24	24
Holdings in unit trusts	**314**	**3**	**317**	290	2	292
Total equities	**314**	**29**	**343**	290	26	316

The funds withheld by LGAS includes non-unit linked property investments totaling £423m (2016: £360m) and equities totaling £26m (2016: £24m), which are all located in the UK.

Credit risk

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

The Group'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 2. 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.

23. Risk management and control (cont'd)

Table 2 – Exposure to credit risk including funds withheld

As at 31 December 2017 Shareholder	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated other £m	Total £m
Government securities	4	11	4	6	-	-	25
Other fixed rate securities	-	2	-	-	-	10	12
Total debt securities	4	13	4	6	-	10	37
Derivative assets	-	-	-	-	-	1	1
Cash and cash equivalents	-	-	-	-	-	11	11
Financial assets	4	13	4	6	-	22	49
Other assets	-	-	2	-	-	1	3
Total shareholder	4	13	6	6	-	23	52
Non profit non-unit linked[1]							
Government securities	101	676	7	18	1	-	803
Other fixed rate securities	76	259	1,236	1,301	53	-	2,925
Variable rate securities	-	198	260	76	27	-	561
Total debt securities	177	1,133	1,503	1,395	81	-	4,289
Accrued interest	2	6	18	20	1	-	47
Loans and receivables	22	56	277	269	8	-	632
Derivative assets	-	-	-	-	-	198	198
Cash and cash equivalents	156	-	-	-	-	16	172
Financial assets	357	1,195	1,798	1,684	90	214	5,338
Investment in subsidiary	-	-	-	-	-	1	1
Other assets	-	-	1	4	-	423	428
Total non profit non-unit linked[1]	357	1,195	1,799	1,688	90	638	5,767
Per previous accounting policy[1]							
Total non profit non-unit linked	157	1,080	1,471	1,860	404	795	5,767

1 The accounting policy on the presentation of the non profit non-unit linked portfolio's credit ratings has been changed. The table now shows a harmonised method for calculating the credit rating average across the non profit non-unit linked funds. The Company believes this provides more reliable and relevant information as the data across the funds is more consistently measured. The accounting policy change has been applied retrospectively to 2016. The 2016 table has been represented. The impact of the new accounting policy on 2016 and 2017 on the non profit non-unit linked portfolio is presented to illustrate the adjustment.

There are no impaired or past due financial assets within the portfolios in 2017.

23. Risk management and control (cont'd)

Table 2 – Exposure to credit risk including funds withheld

As at 31 December 2016	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated other £m	Total £m
Shareholder							
Other fixed rate securities	-	-	28	-	-	-	28
Total debt securities	-	-	28	-	-	-	28
Cash and cash equivalents	-	-	-	-	-	1	1
Total shareholder	-	-	28	-	-	1	29
Non profit non-unit linked [1]							
Government securities	103	791	6	16	3	-	919
Other fixed rate securities	75	296	1,181	1,249	59	-	2,860
Variable rate securities	-	244	266	72	22	-	604
Total debt securities	178	1,331	1,453	1,337	84	-	4,383
Accrued interest	2	7	18	20	1	-	48
Loans and receivables	-	64	220	156	9	-	449
Derivative assets	-	-	-	-	-	210	210
Cash and cash equivalents	-	-	-	-	-	20	20
Financial assets	180	1,402	1,691	1,513	94	230	5,110
Investment in subsidiaries	-	-	-	-	-	1	1
Other assets	-	-	-	-	-	359	359
Total non profit non-unit linked[1]	180	1,402	1,691	1,513	94	590	5,470
Per previous accounting policy[1]							
Total non profit non-unit linked	163	1,174	1,482	1,747	314	590	5,470

[2] The accounting policy on the presentation of the non profit non-unit linked portfolio's credit ratings has been changed. The table now shows a harmonised method for calculating the credit rating average across the non profit non-unit linked funds. The Company believes this provides more reliable and relevant information as the data across the funds is more consistently measured. The accounting policy change has been applied retrospectively to 2016. The 2016 table has been represented. The impact of the new accounting policy on 2016 and 2017 on the non profit non-unit linked portfolio is presented to illustrate the adjustment.

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

23. 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.

The Group'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.

Weather catastrophe: Potential for liquidity risk arises from claims on the reinsurance of LGIL insurance policies.

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, the Group's treasury function. The Group 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.

The Group'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.

<u>Internal process failure</u>
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.

23. Risk management and control (cont'd)

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 the human resource (HR) functions. Recruitment is managed centrally by HR functions, and all new recruits are required to sign all the 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.

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 the 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 reassurance 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 Group's 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. The Group's formal 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.

23. Risk management and control (cont'd)

Sensitivity analysis

Table 3 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 2017 £m	**Impact on equity net of reinsurance 2017 £m**	Impact on pre-tax Profit net of reinsurance 2016[1] £m	Impact on Equity net of reinsurance 2016[1] £m
Sensitivity test				
1% increase in interest rates	**5**	**5**	12	12
0.5% decrease in interest rates1	**(4)**	**(4)**	(8)	(8)
Credit spread widens by 100 bps with no change in expected defaults	**(4)**	**(4)**	(4)	(4)
0.5% increase in inflation1	**(4)**	**(4)**	6	6
15% Rise in property1	**20**	**20**	10	10
15% fall in property1	**(23)**	**(23)**	(10)	(10)
25% Rise in Equity Value1	**5**	**5**	5	5
25% Fall in Equity Value1	**(5)**	**(5)**	(5)	(5)
Annuity: +10bps in credit default assumption	**(50)**	**(50)**	(45)	(45)
Annuity: -10bps in credit default assumption	**49**	**49**	44	44
1% decrease in annuitant mortality	**(19)**	**(19)**	(21)	(21)
1% Increase in Annuitant Mortality	**18**	**18**	20	20

1 For 2017 the Group has aligned sensitivity analysis disclosure requirements across various reported metrics, primarily for interest rate, equity, property value, and annuitant mortality. The current disclosure also reflects management's perception of key risks in current economic conditions.

- 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 100/50 basis point change in the gross redemption yield on fixed interest securities together with a 100/50 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 0.5% p.a. increase in inflation resulting in a 0.5% p.a. reduction in real yield and no change to the nominal yield. In addition the expense inflation rate is increased by 0.5% p.a.
- 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).