LEGAL & GENERAL GROUP PLC
ANNUAL REPORT AND ACCOUNTS 2009

EVERY DAY.

We help make financial security easier to achieve for millions of people.

RISK. SAVINGS.
INVESTMENT MANAGEMENT.

Legal & General

WE COMBINE STRATEGIC CLARITY, OPERATIONAL EXCELLENCE AND FINANCIAL STRENGTH TO DELIVER SUSTAINABLE BENEFITS FOR CUSTOMERS, BUSINESS PARTNERS, SHAREHOLDERS AND EMPLOYEES.

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OTHER INFORMATION

* These sections make up the Directors' Report.
This section of the Annual Report sets out information on the Group's principal activities together with a review of the development and performance of the Group, including financial performance, in accordance with Section 417 Companies Act 2006.

MORE INFORMATION

www.legalandgeneralgroup.com
For more information visit our website.

HIGHLIGHTS.

KEY HIGHLIGHTS

- Net cash generation[1] 118% higher at £699m (2008: £320m)
- Annual cost reduction £69m against a target of £50m
- Final Dividend increased by 33% to 2.73p per share
- Worldwide EEV new business contribution up 10% to £328m (2008: £297m)
- Legal & General Investment Management assets under management £315bn (2008: £264bn)
- International IFRS operating profit doubled to £127m (2008: £59m)

TOTAL NET CASH GENERATION

£699m (2008: £320m)

IFRS PROFIT FOR THE YEAR

£844m (2008: loss of £1,130m)

FULL YEAR DIVIDEND

3.84p (2008: 4.06p)

FINANCIAL STRENGTH[2]

AA-

KEY PERFORMANCE INDICATORS

Key Performance Indicators (KPIs) are measures of financial performance of the Group which help us to evaluate progress towards our strategic imperatives.

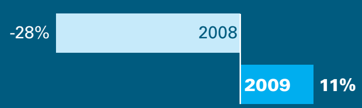
See pages 10 and 11 for more information.

IGD CAPITAL SURPLUS[3] (AS AT 31.12.09)

£3.1bn (2008: £1.8bn)

TOTAL SHAREHOLDER RETURN (TSR)

11%



(2008: Negative 28%)

IFRS OPERATING PROFIT BEFORE TAX[4†]

£1,109m

(2008: £592m restated†)

RETURN ON EQUITY (ROE)

22.2% 2008: (negative 23.6%)

EEV OPERATING PROFIT BEFORE TAX[5]

£1,319m

(2008: £875m restated)

1 Net cash generation is defined as operational cash generation less new business strain for the UK non profit Risk and Savings businesses.
Operational cash generation is defined as the expected release from in-force business for the UK non profit Risk and Savings businesses, the shareholders' share of bonuses on With-profits business, the post-tax IFRS operating profit on other UK businesses, dividends remitted from our international businesses from sustainable cash generation and expected investment return (excluding expected gains/losses on equities) on Group Capital and Financing invested assets.

2 Standard & Poor's Financial Strength rating for Legal & General Assurance Society Limited. As at 22 March 2010.

3 EU Insurance Groups Directive. Figures after accrual of proposed dividend, based on draft unaudited regulatory returns.

4 International Financial Reporting Standards.

5 European Embedded Value.

† We have reviewed the definition of operating profit on the IFRS basis. Accordingly the 2008 figures have been restated. A reconciliation is provided on page 17 of this report.

WHAT WE DO: OUR BUSINESSES.

WE ARE A LEADING PROVIDER OF RISK, SAVINGS AND INVESTMENT MANAGEMENT PRODUCTS IN THE UK, WITH MORE THAN SEVEN MILLION CUSTOMERS AND OVER 9,000 EMPLOYEES WORLDWIDE. THE GROUP'S PRIMARY FOCUS TODAY IS ON THE UK, BUT WE CONTINUE TO EXPAND INTERNATIONALLY IN ATTRACTIVE NEW MARKETS.

RISK

SAFEGUARDS CUSTOMERS AGAINST FINANCIAL RISKS

Our Risk businesses assume customers' financial risks from defined events such as death, injury or household damage, whilst our annuities business protects individuals from the risk of outliving their savings in retirement.

Products

- Individual protection
- Group protection
- Housing network
- Corporate annuities
- Individual annuities
- General insurance

£366m

Protection and annuities APE
(2008: £488m)

4.6m

Total number of customers protected by risk businesses
(2008: 4.4m) Excluding Bulk Purchase Annuity (BPA) customers

For more information see pages 20 to 23.

SAVINGS

FINANCIAL PLANNING, SAVINGS AND INVESTMENTS

Our Savings business is an investment management led manufacturer and assembler of modern, flexible products, allowing individuals to save to meet the costs of specific future events or to give a planned income in retirement.

Products

- Unit trusts
- Individual savings accounts (ISAs)
- Investment bonds
- Pensions
- With-profits

£907m

Savings APE
(2008: £879m)

£54.8bn

Total savings assets under administration
(2008: £45.8bn)

For more information see pages 24 to 27.

INVESTMENT MANAGEMENT

INVESTING ON BEHALF OF INSTITUTIONAL AND RETAIL CUSTOMERS

LGIM is the largest manager of UK sourced pension assets and one of the largest investors in the UK stock market; with responsibility for approximately 4.5% of all London-listed equities on behalf of its customers.

Products

- Index funds
- Fixed income
- Actively-managed equity funds
- Private equity
- Property
- Risk management solutions

£33.3bn

Gross new institutional funds received
(2008: £33.1bn)

£315bn

Total funds under management (FUM)
(2008: £264bn)

For more information see pages 28 to 31.

INTERNATIONAL

OUR OVERSEAS PRESENCE

Our international businesses combine our mature existing international businesses in the United States, France and the Netherlands, with selective participation in the fast-growing middle class wealth of emerging markets.

Products

- Individual protection
- Group protection
- Savings – wholesale, retail and individual
- Investment management

£115m

International APE
(2008: £119m APE)

£127m

IFRS operating profit
(2008: £59m)

For more information see pages 32 to 35.

CHAIRMAN'S STATEMENT.

"IN TAKING OVER FROM SIR ROB MARGETTS I AM CONFIDENT THAT I HAVE JOINED A COMPANY THAT IS STRATEGICALLY WELL-POSITIONED TO DELIVER PROFITABLE GROWTH IN THE UK AND INTERNATIONALLY WHILE ALSO FULFILLING A BROADER, SOCIALLY USEFUL, REMIT."

To see a video of John Stewart please visit **www.legalandgeneralgroup.com**

A CHALLENGING YEAR

This is my first communication with you, our shareholders, as the new Chairman of your Company. I have known and worked with Legal & General for many years and have found the company to have huge strengths, including its balance sheet, cash-generative capacity, strong brand and commitment to customers.

In the 2008 Annual Report, your previous Chairman indicated that we expected continuing recession in the UK in 2009 and, sadly, he was not wrong. In the first quarter of 2009 financial markets were left reeling after narrowly avoiding a systemic failure of the banking system and entering one of the sharpest, deepest recessions on record. However, over the course of one of the most difficult years in my memory, a financial meltdown was avoided and a feared 1930's style depression did not materialise.

Through this period of extreme uncertainty, no major UK-listed insurer was forced to cease trading, ask for taxpayer funding or go to the stock market to raise fresh capital. Most importantly, no promises to policyholders were reneged upon. Investment performance suffered with falling markets, but customers' claims and pensions continued to be paid as normal. This is testament to the strength and importance of the life industry in the UK.

Throughout the course of the year, policy makers undertook extraordinary measures to rebuild confidence in the financial system and stimulate economic activity. I am pleased that these actions, alongside the steady stewardship of your Board, have had a positive impact on our share price and on your returns, ensuring that we entered 2010 in a strong position.

SHAREHOLDER RETURN AND DIVIDEND

By the end of the year, the FTSE All-Share Index saw a recovery to 2761, 25% above its 2209 at the start of last year. Our total shareholder return (TSR) for 2009 was 11% (2008: negative 28%).

This year, in line with improved market conditions, but recognising the need to retain a strong capital base, the Board is recommending an increase in the final dividend of 33% to 2.73p per share. With the interim dividend of 1.11p, this will bring total dividends for 2009 to 3.84p.

FULL YEAR DIVIDEND

3.84p

(2008: 4.06p)

IFRS OPERATING PROFIT

£1,109m

(2008: £592m restated)

EEV OPERATING PROFIT

£1,319m

(2008: £875m restated)

ANNUAL GENERAL MEETING (AGM)

This year's AGM will be held on Wednesday 26 May at the Institution of Engineering and Technology, Savoy Place, London WC2R 0BL.

BOARD CHANGES

In addition to my appointment there have been a number of changes to the Board this year. In June we welcomed Dame Clara Furse, formerly Chief Executive of London Stock Exchange Group, as a Non-Executive Director of the Group and in September Dr. Nigel Wilson joined the Board as Group Chief Financial Officer in succession to Andrew Palmer.

I would like to thank Andrew for the contribution he made to Legal & General over his long period with the Company and to formally welcome Nigel and Dame Clara to the Board.

Full details of all changes can be found on page 45 of the report.

OUR STAFF

As a result of the economic situation, fiscal changes and our pursuit of increased efficiency we reduced resource levels across the Group this year. This resulted in redundancies in several areas.

Notwithstanding these changes our employees have continued to perform at their normal high standard and I am very grateful to them for their hard work and commitment.

OUTLOOK

As we head into 2010, economic indicators have started to improve and financial markets have responded slowly. Over the next twelve months we anticipate only modest growth in the UK economy and activity in the housing market is likely to remain subdued. However, fresh signs of improvement in the manufacturing sector should help restore economic growth in 2010 and we believe the Company is well positioned to seize the opportunities offered by this recovery.

JOHN STEWART
CHAIRMAN

SIR ROB MARGETTS

Rob Margetts joined Legal & General's Board in June 1996 and became Chairman in February 2000. An industrialist by background, he brought a wealth of experience to bear during his long tenure at the helm of our Board of Directors.

He also brought a strong commitment to reinforcing the Company's clear values and ethics.

He was a leading 'green entrepreneur' long before the concept became fashionable, and was the driving force behind Legal & General's leadership in the environmental and CSR fields.

During Sir Rob's decade of service as Chairman, he has consistently demonstrated his ability to provide wise counsel and clear board leadership for Legal & General.

We value hugely and thank him for his extraordinary commitment both to the success of Legal & General and to our strong ethic as a responsible provider of financial services. We wish him well in the next stage of his career.

SIR DAVID WALKER
VICE CHAIRMAN

GROUP CHIEF EXECUTIVE'S REVIEW.

"IN LAST YEAR'S REPORT WE OUTLINED OUR STRATEGIC DIRECTION AND THE FIVE IMPERATIVES KEY TO REALISING OUR ASPIRATION OF BECOMING THE UK'S LEADING RISK, SAVINGS AND INVESTMENT MANAGEMENT BUSINESS. I AM PLEASED TO REPORT THAT IN 2009 WE HAVE ACCELERATED OUR PROGRESS IN THESE AREAS AND DELIVERED SOME STRONG RESULTS."

To see a video of Tim Breedon please visit
www.legalandgeneralgroup.com

DELIVERING OUR STRATEGY

In March 2009 I set out our intention to accelerate the net cash generation of the Group. We set targets to deliver £450 million of net cash and £50 million of annual cost savings in 2009. Both of these targets were exceeded by the end of September, and end of year net cash generation was £699 million and annual cost savings were £69 million.

Legal & General is a balanced manufacturer of Risk, Savings, and Investment management products. In Risk, market leading positions in protection and annuities are generating significant, sustainable cash flows and continue to perform well despite a weakened UK housing market. Our General insurance business is now delivering healthy returns.

The turnaround in our Savings business is ahead of schedule. New business sales have been strong in 2009 with emergence of sustainable cash flow and profit in the second half of 2009.

Legal & General Investment Management (LGIM) has continued to receive strong new business flows and has established a top ranked position in the UK pensions fund market. Our International businesses are now poised to become a significant source of future profit growth.

Our diverse mix of distribution channels puts us in a good position ahead of the implementation of the Retail Distribution Review (RDR). New distribution arrangements with SAGA, Skipton Building Society and Northern Rock, amongst others, will contribute to overall sales in 2010.

We have also worked closely with industry associations and relevant Government bodies to highlight the impacts of regulation and policy, particularly the potential unintended consequences of the European Solvency II Directive and its impact on UK savers.

FINANCIAL HIGHLIGHTS

Worldwide new business sales for 2009 were £1,388 million on an annual premium equivalent (APE) basis (2008: £1,486 million). In part this reflects more difficult economic conditions, and low investor confidence in

FINAL DIVIDEND PAYABLE

£160m
(2008: £120m)

IFRS PROFIT FOR THE YEAR

£844m
(2008: loss of £1,130m)

OUR PURPOSE

"I strongly believe insurance can be a catalyst for economic improvement, and a force for good. We can take on new responsibilities to benefit our policyholders, investment customers, shareholders and society at large. Having proved we can survive the financial crisis, it is now up to us to prove our value in the recovery, but we will need the right regulatory framework and the right spirit of partnership with Government to do so.

We need to deliver on our promises and meet our obligations where it is right to do so. We must not forget that our products should be designed to meet the real needs of customers, not be driven by our own preferences or those of our distributors."
Tim Breedon, Business In the Community (BITC) AGM, 3 December 2009.

In recognition of this important aspect of our role, a new section has been added to this year's report and can be found on page 36.

Our CSR Report contains further details and can be found at www.legalandgeneralgroup.com/csr.

the first half of the year. However it is also the result of a deliberate strategy on our part to focus more selectively on higher quality, higher return new business. International Financial Reporting Standards (IFRS) operating profit was £1,109m (2008: £592m restated).

In Risk, individual annuities recorded double digit sales growth and individual protection outperformed the falls in gross mortgage lending reflecting sector leadership and breadth of distribution. The pensions buyout market, after an extraordinary 2008, returned to the levels seen in previous years and Legal & General took a broadly consistent share of this market in 2009.

The strategy of focusing on the small scheme market coupled with a highly selective approach to larger transactions has been maintained. Total APE in the Risk business fell 25% to £366 million.

In Savings, a strategy of reducing volumes in traditional capital-intensive life and pensions products in favour of more capital efficient Self Invested Personal Pensions (SIPPs) and unit trusts continues to drive growth. Overall UK Savings APE was 3% higher than last year at £907 million, boosted by a 69% growth in unit trusts sales.

Investment management received gross inflows of funds of £33.3 billion for the year. Of this LGIM inflows accounted for £31.5 billion, our second highest annual level of gross funds ever, as UK Corporate pensions trustees and institutional clients continue to be attracted to our range of indexed, fixed income and liability driven investment (LDI) products combined with high levels of service.

International sales were down 3%, as businesses in the United States, France and the Netherlands performed well in challenging market conditions. New joint ventures in India and the Gulf began trading during the fourth quarter.

BALANCE SHEET AND CAPITAL

Financial strength was a major focus in 2008 and continued to be so in 2009. Our balance sheet is stronger and our estimated IGD surplus at the end of the year was £3.1 billion (2008: £1.8bn). This is more than double the required level of regulatory capital, resulting in a coverage ratio of 224%, up from 169% at the end of December 2008.

OUTLOOK

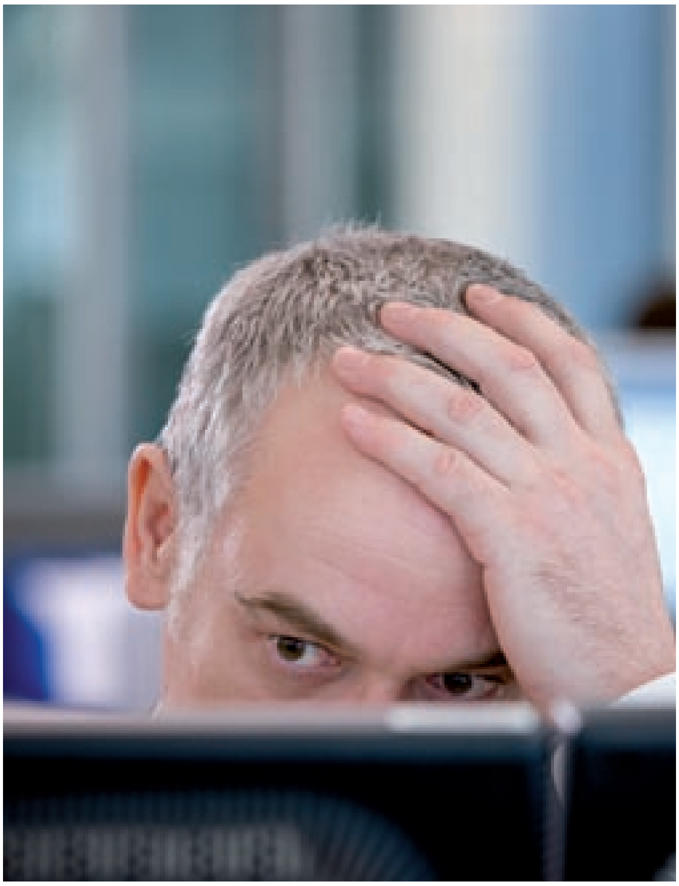
These results demonstrate the significant progress we continue to make in transforming the Group into a lower cost, capital efficient, cash generative business. Our business outlook is exciting. Confidence is slowly returning to the economy and I believe the actions that we have taken this year leave our businesses well placed to continue delivering growth going forward. We have a clear strategy based on strong cash generation and profit growth, an efficient manufacturing capability, and proven distribution strength.

TIM BREEDON
GROUP CHIEF EXECUTIVE

MARKET ENVIRONMENT.

"THE ECONOMIC CRISIS STARTED AS AN ISSUE OF BANK LIQUIDITY, THEN BECAME AN ISSUE OF BANK SOLVENCY, AND ENDED AS A CRISIS OF CONFIDENCE FROM WHICH WE ARE STILL RECOVERING. RESTORING CONFIDENCE IS CRUCIAL TO THE SUCCESS OF THE INDUSTRY GOING FORWARD."

TIM BREEDON
GROUP CHIEF EXECUTIVE



INDUSTRY AND MARKETS

In 2009 the UK entered one of the sharpest, deepest recessions on record. Throughout the course of the year policy makers undertook extraordinary measures to rebuild confidence in the financial system and stimulate economic activity.

In the first quarter of 2010 economic data has begun to improve and financial markets have started to respond. The UK economy continues to lag behind other major developed economies, although officially exiting recession at the end of 2009. However, signs of confidence returning to the housing market and improvement in the manufacturing sector should help restore moderate economic growth during 2010.

FROM DEBT TO SAVINGS

After a decade of debt accumulation amongst consumers, what we are seeing, post-crash, are the beginnings of a welcome and necessary rebuilding of savings.

At present, the new money being saved largely reflects short-term, precautionary savings. As the economy slowly stabilises, though, a proportion of precautionary saving should transform into long-term investments designed to meet the costs of specific future events or to give a planned income in retirement.

For this to happen, confidence in financial services and financial products needs to return. One important aspect of this will be stability of regulatory and tax treatment. Savers need to know that they can plan, and that taxation of savings products will not be subject to unexpected changes. The further erosion of this principle in December's pre-budget report (PBR) was therefore disappointing. Importantly, savings product manufacturers need to be confident that they will not also be the victims of retrospective policy changes.

BULK ANNUITY MARKET	INCREASE IN FUNDS UNDER MANAGEMENT IN 2009	GROWTH IN UK LIFE MARKET
over 10	**£119bn**	**120%**
New firms entering market since 2006	(2008: IMA FUM fell by £107bn)	ABI Life and pensions APE since 1995

Savers and investors also need to know that, while the regulatory system protects consumers' interests, it is the customers themselves who ultimately bear the costs of compliance. This must remain at a reasonable level, ensuring protection of the consumer, but not reducing the value of the investment from day one as a result of excessive and unnecessary bureaucratic processes.

REGULATION AND POLITICAL ENVIRONMENT

There is a risk that the EU's Solvency II proposals, if implemented in the wrong way, may increase the volatility of insurance companies' balance sheets and force them to raise capital levels. Capital is a raw material used in the manufacture of our products. If more is needed, prices go up, and value for the customer is eroded. The value of UK pension savings could be cut substantially and the price of insurance products rise as companies pass on the costs of carrying extra capital. Capital hording also reduces available investment in the broader economy.

We are at the vanguard of seeking changes to the proposed prudential regulatory regime in order to secure the best possible outcome for UK pension savers.

Another key area for focus is Conduct of Business regulation in UK financial services. A clear regulatory approach which does not rely on hindsight judgements is required. It should also provide single accountability for regulation, ensuring consumer access, experience and outcomes are at the heart of regulation. In turn this will enable the Financial Ombudsman Service (FOS) to focus on its role as an arbitration service, providing a fast and high quality service to consumers and a fairer framework for consumer protection, without excessive regulatory costs.

OUTLOOK

Consolidation across both the insurance and banking sectors has impacted the distribution landscape, reducing the number of brands available to consumers both on the high street and through intermediaries. We expect the FSA's Retail Distribution Review to further impact the market, particularly the availability of advice from independent financial advisers.

We anticipate a relatively subdued period of growth. As a result, central banks are likely to keep official interest rates on hold, potentially until 2011. Given the anaemic outlook for economic growth and the labour market we do not see any significant underlying inflationary pressures building or any need for the Bank of England to increase official interest rates. However there is a need to remain watchful given the extraordinary monetary stimulus injected into the economy through low interest rates and quantitative easing.

STRATEGIC OVERVIEW.

OUR AIM

TO DELIVER SUSTAINABLE GROWTH IN CASH FLOWS IN ORDER TO REWARD OUR SHAREHOLDERS.

WE WILL DO THIS BY ENSURING THAT:

AT GROUP LEVEL WE:

APPLY SUPERIOR FINANCIAL MANAGEMENT

Capital is a key ingredient for our business and effective capital management is an important objective. We aim to ensure that we have the right amount of the right type of capital to meet our business requirements. We have built a reputation as a low-cost manufacturer. As well as immediate margin enhancement, cost leadership provides the agility to react to changing circumstances quickly.

BUILD A DIVERSIFIED BUSINESS

We manage our portfolio of businesses to deliver Group targets against our key metrics. We scan the market to identify new opportunities and invest to grow the business and build profitable returns.

EACH BUSINESS PROVIDES:

HIGH QUALITY PRODUCTS AND BROAD DISTRIBUTION

Central to our business model is the maintenance of diversified distribution capability. The benefits of this strategy are that we are able to build scale in diversified markets and maintain growth as distribution patterns shift. Together with this, we will produce products which offer demonstrable value to customers, distributors and us, maintaining quality and ensuring a stable stream of high quality new business.

A POSITIVE CUSTOMER EXPERIENCE

We recognise our customers are at the heart of our business and consequently work hard to develop relationships with our key customer segments and distributors on mutually acceptable terms. We aim to deliver a positive experience for our existing customer base; treating our customers fairly and meeting, or beating, the performance assumptions made in terms of persistency, cost, claims and mortality.

A HIGH EXPECTATION CULTURE

Our people are key to our continued long term success. We aim to maintain a strong management team and continually to grow the breadth and depth of our management capability. Our organisational culture already yields benefits in terms of behaviour, low turnover and cost, but we recognise the need to evolve in the current marketplace, injecting greater energy into the business to improve on our successes.

RETURN ON EQUITY (RoE)

Definition: RoE measures the return earned by shareholders on shareholder capital retained within the business. RoE is calculated as IFRS profit after tax divided by average IFRS shareholders' funds.

Purpose: RoE provides a link between performance and balance sheet management and ensures that an appropriate balance is maintained between the two.

IFRS OPERATING PROFIT

Definition: The Group's primary financial statements (see Financial Statements) are prepared on an International Financial Reporting Standards (IFRS) basis which all EU listed companies are required to follow. IFRS operating profit measures the pre-tax result using a smoothed longer term investment return. Any variance between actual and smoothed investment return is reported below operating profit.

Purpose: IFRS operating profit gives an insight into the Group's ability to generate cash flows to support dividends during a period.

HOW WE MEASURE SUCCESS:	PERFORMANCE
We do this in five ways*: • Return on equity • IFRS operating profit • Insurance group directive (IGD) surplus and coverage ratio • Total shareholder return (TSR) • EEV operating profit * The definitions and purpose of these measures can be found at the bottom of this page.	• Both IFRS and EEV operating profits showed a healthy improvement on 2008 numbers. Our focus on cash generation has yielded a significant improvement in IFRS profits • Our balance sheet proved resilient to extreme market conditions and year end estimated IGD surplus was £3.1bn • TSR has improved in 2009 to 11% from negative 28% in 2008 • Consequently group return on equity was a healthy 22%.
Segmented IFRS profit	• Risk is a highly cash generative business which benefits from high scale and leading market positions. IFRS operating profit in 2009 was £735m • Savings has continued to turn around its performance with changes to costs, products and distribution yielding an IFRS operating profit of £55m • Investment management has a leading position in its UK markets, and is developing internationally. IFRS operating profit was £167m • We are building our international portfolio with the launch of new businesses in the Gulf States and India in 2009. International IFRS operating profit was £127m.
• Persistency measures • Awards in recognition of good products	• We have continued to execute our multi distribution strategy well during 2009. We signed distribution agreements with SAGA, Northern Rock, and Skipton Building Society amongst others • Our product range continues to attract customers and distributors to us. During the year we launched a range of new products across our businesses.
• Customer experience report • Customer satisfaction surveys	• Extreme market conditions have affected customers during the year. Many savings and investment management customers have seen their asset values fall. This has had an impact on customer perceptions of Legal & General • We continue to deliver high quality service to our customers and win many awards for service. We continually strive to improve the quality of service we offer.
• Annual staff survey • Staff engagement in 'What Matters?' programme	• We have continued to make good progress in the evolution of our culture. We have recruited a number of high quality leaders to the Board and to individual businesses. Our managers have been trained on improving performance management, leadership and communications. There is still more to do but we are pleased with the progress we have made in 2009.

INSURANCE GROUPS DIRECTIVE (IGD) SURPLUS*

Definition: The IGD surplus is an FSA regulatory measure which calculates surplus capital within the Group. IGD surplus is defined as Group regulatory capital employed less the Group regulatory capital requirement. Surplus capital held within our Society Long Term Fund cannot be included in the IGD definition of capital employed.

Purpose: IGD surplus is the Group level regulatory surplus capital measure. IGD surplus is after accrual of proposed dividend.

* Figures extracted from draft unaudited regulatory returns.

TOTAL SHAREHOLDER RETURN (TSR)

Definition: TSR is a measure used to compare the performance of different companies' stocks and shares over time. It combines the share price appreciation and dividends paid to show the total return to the shareholder. The TSR shown is the change in share price over a three year performance period, plus the value of reinvested dividends, relative to the performance of all the other companies in the FTSE 100.

Purpose: TSR measures total return to shareholders over the medium term.

EEV OPERATING PROFIT

Definition: Legal & General provides supplementary financial statements prepared on the European Embedded Value (EEV) basis for long term insurance contracts (see Supplementary Financial Statements). The EEV basis provides an assessment of the value which has been generated by the business during a period. Operating profit on the EEV basis reports the change in embedded value in a period, but excludes fluctuations from assumed longer term investment return.

Purpose: In the Board's opinion, EEV operating profit provides shareholders with a good understanding of the value which is being created on the Group's long term insurance contracts.

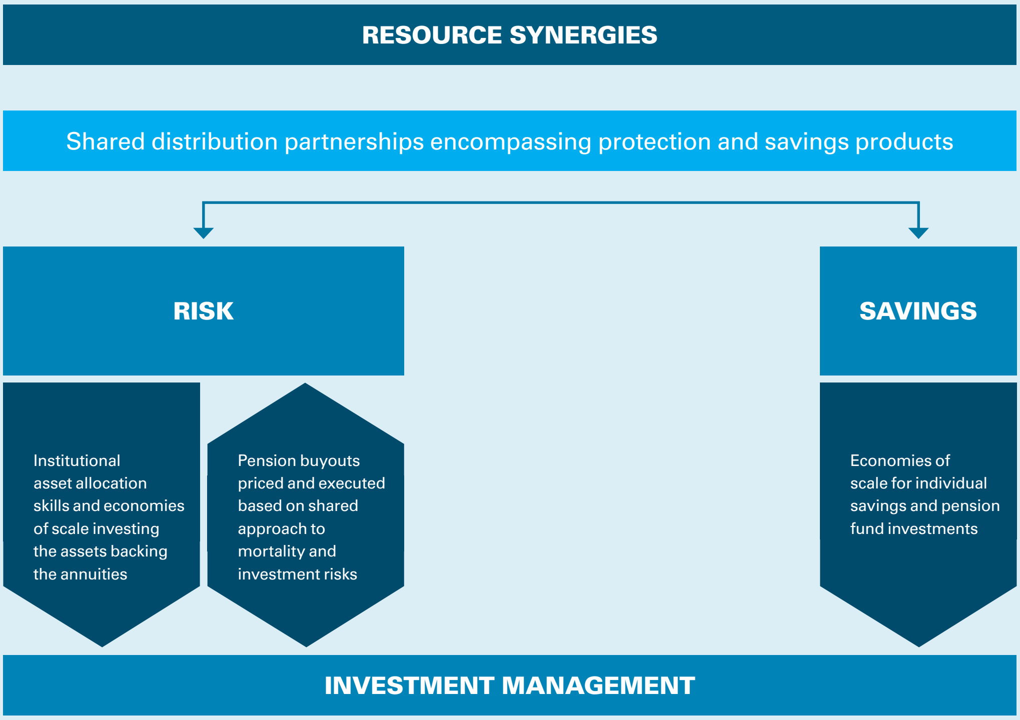
SYNERGIES BETWEEN OUR BUSINESSES.

"WE BELIEVE THAT OUR COMBINATION OF RISK, SAVINGS AND INVESTMENT MANAGEMENT WORKS BETTER TOGETHER, AND ADDS MORE VALUE AS A WHOLE THAN ANY OF THE THREE COMPONENTS COULD ON ITS OWN."

TIM BREEDON
GROUP CHIEF EXECUTIVE

Synergy matters because it enables us to deliver better products, making best use of all the resources which exist across the Company, and deliver better services and returns for customers and shareholders, for each individual customer or corporate client. Individuals and companies do not necessarily compartmentalise their various financial requirements. They benefit from dealing with an organisation like ours which can understand and address the broader picture.

Utilising synergies benefits all parties. For example, individual customers of our Savings division benefit from LGIM's institutional fund management expertise.



42%

of bulk purchase annuity business comes from LGIM clients

67%

of maturing pension schemes purchase L&G annuity

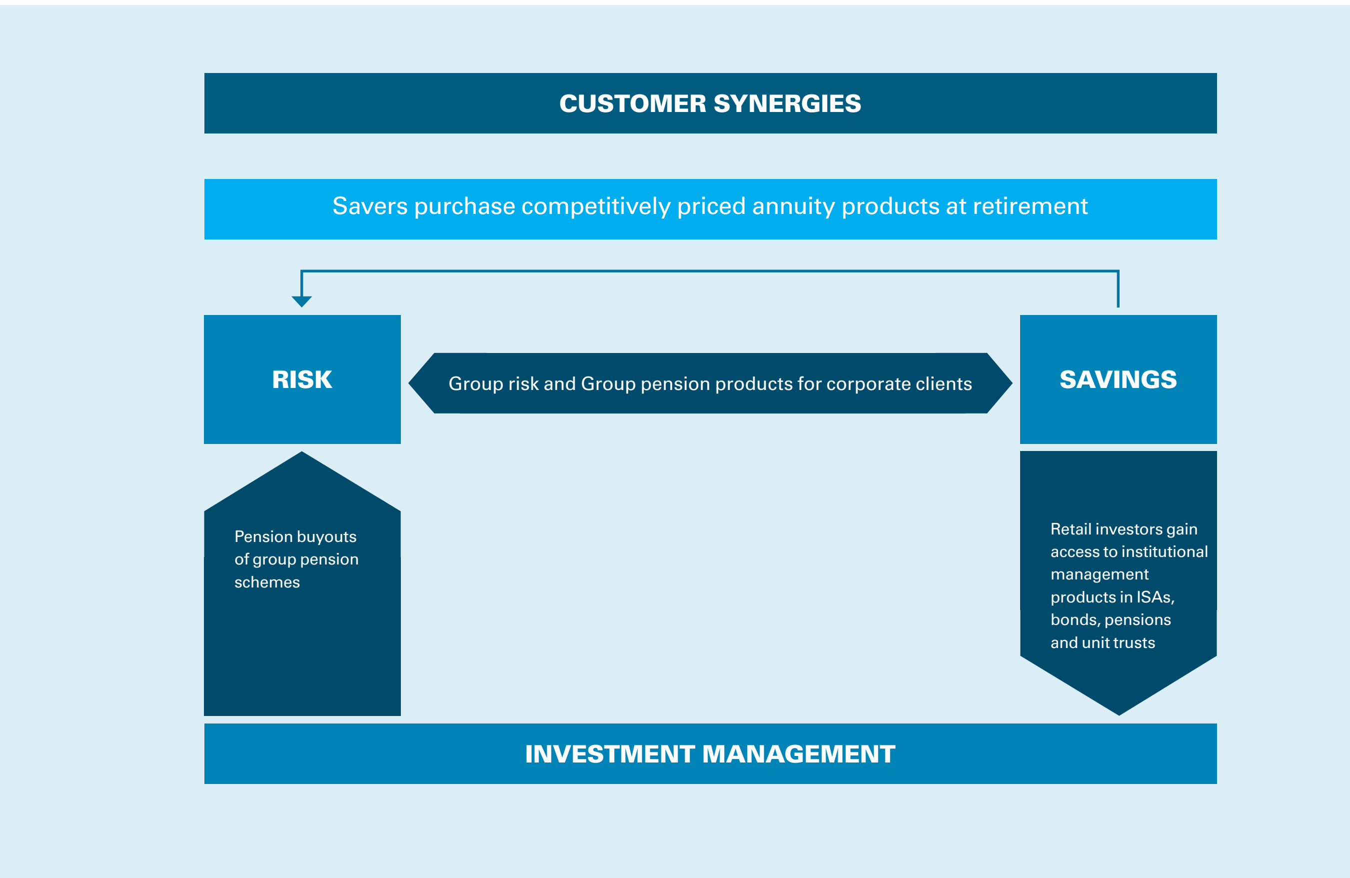
25%

of group new business APE comes from internal introductions

Customers who have had a positive pensions experience with our Savings division are likely to look favourably on an annuity proposition from our Risk division when the time comes to annuitise.

Corporate customers looking to execute a pension buyout benefit from the combination of Risk's longevity expertise and LGIM's investment skills: a package which we can deliver as a result of utilising synergies and sharing skills and resources across our business divisions.

Synergies also exist between each operating division and the corporate centre. Each business benefits from shared central resources: the strength of the balance sheet and risk management, and our powerful brand being prime examples. Each of our businesses can and does help the others, and this adds value to the Group as a whole.



OUR PERFORMANCE

GROUP RESULTS.

"THE ACCELERATION OF OUR STRATEGY IN 2009 GENERATED SIGNIFICANT IMPROVEMENTS IN PROFITABILITY, CAPITAL AND CASHFLOW TO SUPPORT A SUSTAINABLE DIVIDEND."

TIM BREEDON GROUP CHIEF EXECUTIVE

IFRS PROFIT FOR THE YEAR

£844m

(2008: loss of £1,130m)

GROUP PERFORMANCE

IFRS[1] basis

	2009	2008
Operating profit before tax[2]	**£1,109m**	£592m*
Return on Equity (ROE)	**22.2%**	(23.6)%
Ordinary shareholders' equity	**£4,196m**	£3,588m
Dividend cover[3]	**3.6**	1.8
Worldwide new business APE[4]	**£1,388m**	£1,486m
New institutional funds	**£33.3bn**	£33.1bn
Worldwide FUM[5]	**£334bn**	£280bn

EEV[6] basis

	2009	2008
Operating profit before tax	**£1,319m**	£875m
Contribution from new business	**£328m**	£297m
Ordinary shareholders' equity	**£6,695m**	£6,521m
Dividend cover[3]	**4.2**	2.7

* Restated. See page 17 for more information.
[1] International Financial Reporting Standards.
[2] Supplementary operating profit before tax from continuing operations.
[3] Dividend cover is calculated as operating profit after tax divided by the current year interim dividend plus the proposed final dividend.
[4] Annual Premium Equivalent (APE) is total new annual premiums plus 10% of single premiums. Excludes institutional investments in unit trust funds which are disclosed under institutional funds.
[5] Funds Under Management.
[6] European Embedded Value.

AREAS OF FOCUS FOR 2009

In March 2009 we set out a course of action for the year centred on:

1. Improving net cash generation and reducing capital tied up in new business

2. Reducing costs

	2009 actual	2009 target	2008
Net cash	**£699m**	**£450m**	£320m
Cost savings	**£69m**	**£50m**	–

3. Improving balance sheet resilience

	2009	2008
IGD Surplus*	**£3.1bn**	£1.8bn

* Figures after accrual of final dividend, based on draft unaudited regulatory returns

The financial model on the adjacent page separately identifies the Group's capital stock and operational cashflows. Operational cash generation is defined as the flow of cash expected to be generated by the business each year and is available to:
– replenish the capital stock;
– reinvest back into the business; and
– finance the dividend.

The capital stock is represented by the Group's IGD surplus and is available to provide financial strength to absorb experience variances and reserve changes incurred by the Group.

The IGD surplus is also available to support solvency capital required to be held for regulatory purposes in the businesses.

FOCUS ON VALUE OF IN-FORCE (VIF) BUSINESS

A key component of future operational cash generation is the monetisation of the in-force business. This consists of the expected release in the non profit business, the shareholders' share of with-profits bonuses, and dividends from the international businesses. At the end of 2009, the undiscounted value of the worldwide VIF was £10.2bn. The profile in the adjacent table shows that £860m of the VIF is expected to monetise in 2010.

When reconciling to operational cash for 2010, we remove identifiable short term variances and assumption changes which are charged directly to the capital stock.

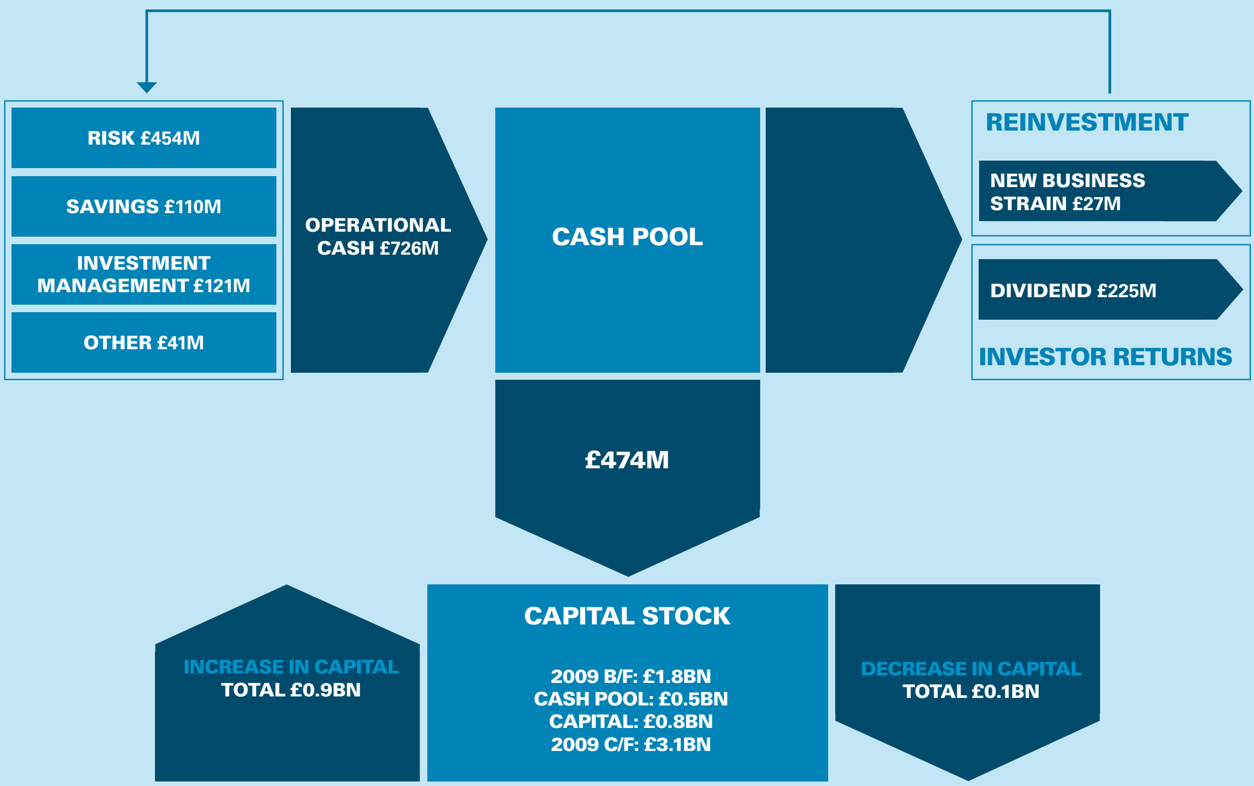
The resultant expected release from non profit business forms the operational cash generated by the non profit business.

Estimated monetisation of worldwide VIF (undiscounted)[1]

£m	Total	2010	2011	2012
Business in-force at start of year[2]	7,200	700	630	560
2009 new business cash flows	700	70	50	50
UK VIF monetisation	7,900	770	680	610
International VIF monetisation	2,300	90	90	80
	10,200	860	770	690

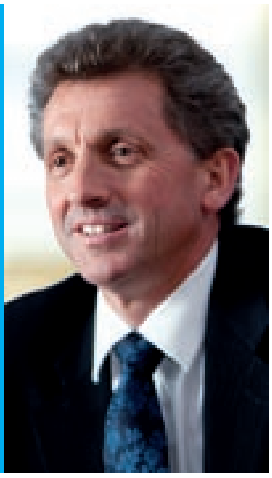
[1] Management estimates.
[2] Based on 2009 assumptions.

FINANCIAL MODEL



GROUP RESULTS.

> **"2009 WAS A YEAR IN WHICH WE SET OURSELVES CHALLENGING TARGETS AND EXCEEDED THEM COMPREHENSIVELY."**
>
> **DR. NIGEL WILSON**
> **GROUP CHIEF FINANCIAL OFFICER.**



During 2009 material progress has been made in generating cash and improving cost management. Actions to reduce Groupwide costs, including a 17% reduction in total headcount, led to an overall annual reduction in costs of £69 million.

Furthermore, action to reduce commission and focus on capital efficient new business led to a material reduction in new business strain to only £27m (2008: £334m). These effects, together with improvements in the operating profit of LGIM, General insurance and Retail investments led to net cash generation of £699m during 2009, a significant improvement on 2008 (£320m) and the £450m target set in March 2009. Operational cash generated in 2009 increased by 11% to £726m (2008: £654m) primarily as a result of the release of the mature in-force risk business.

One of the principal aims of the Group is to optimise the cash profile of its products. Regardless of financial reporting methodology, total cash earned by a product over its lifetime will be the same.

Reported profit relating to non profit Risk and Savings products can be volatile in any particular year – being impacted by non-recurring items such as reserving changes, large investment variances and non cash items which may be significant. We therefore focus on the expected cash profile of our products to give us a better understanding of the Group's ability to sustain dividend payments to shareholders and finance new business over the medium term.

The Group's ability to generate cash is considerable and is supported by our Risk, Savings, Investment management and International businesses.

Reconciliation of operational cash generation to IFRS profit

The table below provides an analysis of the operational cash generated by each of the Group's business segments, together with a reconciliation to IFRS profit.

Net cash generation is calculated net of tax and forms an integral component of IFRS profit. IFRS profit in the year also includes the non-recurring items described above which are managed with the intention of delivering positive experience over the medium term.

Reconciliation of operational cash generation to IFRS profit

Year ended 31 December 2009	Operational cash generation £m	New business strain £m	Net cash £m	International £m	Variances £m	Investment gains and losses £m	Other £m	IFRS profit/(loss) after tax £m	Tax expense/ (credit) £m	IFRS profit/(loss) before tax £m
Total Risk	**454**	50	**504**	–	27	–	–	**531**	204	**735**
Total Savings	**110**	(77)	**33**	–	16	–	(8)	**41**	14	**55**
Investment management	**121**	–	**121**	–	–	–	–	**121**	46	**167**
International	**8**	–	**8**	78	–	–	–	**86**	41	**127**
Group capital and financing	**33**	–	**33**	–	–	16	–	**49**	8	**57**
Investment projects	**–**	–	**–**	–	–	–	(23)	**(23)**	(9)	**(32)**
Operating profit	**726**	(27)	**699**	**78**	43	16	(31)	**805**	304	**1,109**
Investment variance	**–**	–	**–**	–	–	58	–	**58**	(74)	**(16)**
Minority interests	**–**	–	**–**	–	–	–	(19)	**(19)**	–	**(19)**
Total	**726**	(27)	**699**	78	43	74	(50)	**844**	230	**1,074**

NEW BUSINESS

Group APE for 2009 of £1.4bn was 7% lower than last year. This in part reflects trading conditions during the year but also management action to overhaul the product mix. As markets contracted and commissions were cut volumes declined in most markets. However, Legal & General Investment Management new funds and demand for SIPPs, unit trusts, ISAs and products with an element of guarantee continued to grow.

Changes to the definition of supplementary IFRS operating profit

Supplementary IFRS operating profit is one of the key performance indicators for the Group. We believe this measure gives shareholders a better understanding of the underlying performance of the business. We have changed its definition to enhance its clarity and insight into the factors driving Group profitability, in particular to remove the impact of economic volatility from the underlying performance of the business.

The new definition extends our use of expected investment returns to the non profit Risk and Savings results, bringing this business into line with our other UK segments. It is also more closely aligned with the basis used for European Embedded Value (EEV) reporting.

The change in definition does not affect the underlying performance, the economics of our business, the profit before tax attributable to shareholders or the profit for the year. It only changes the allocation of profit between operating and non-operating elements.

The key changes to our definition of IFRS operating profit are:

i. Operating profit for the Risk and Savings businesses is now based on the investment returns that the Group expects to make on the financial investments which back the non profit business over the reporting period, rather than the actual returns on these investments. The difference between the expected return and the actual return on investments, and the corresponding impact on liabilities, is shown below the operating profit line. This adjustment includes the removal of accounting volatility arising from the mismatch of asset and liability valuations for deferred tax balances within unit linked funds under IFRS.

ii. Group capital and financing operating profit now excludes the profit or loss arising from actuarial gains and losses on annuities held by the Group's defined benefit pension schemes. As this is driven by bond market yields the effect has also been classified as variation from longer term investment return.

iii. The profit impact arising from the elimination of own debt holdings is reflected below operating profit. In previous reporting periods this amount has been nil.

The following table sets out the effect of the above changes to IFRS operating profit for the year ended 31 December 2008:

	As reported 2008 £m	Effect of restating the definition of IFRS operating profit £m	Restated 2008 £m
Operating profit			
Risk	(603)	825	222
Savings	66	(59)	7
Investment management	165	–	165
International	59	–	59
Group capital and financing	124	15	139
Operating profit	**(189)**	**781**	**592**
Variation from longer term investment return	(1,239)	(781)	(2,020)
Property losses attributable to minority interests	(63)	–	(63)
Profit/(loss) from continuing operations before tax attributable to equity holders of the Company	**(1,491)**	**–**	**(1,491)**
Tax credit attributable to equity holders of the Company	361	–	361
Profit/(loss) from ordinary activities after tax	**(1,130)**	**–**	**(1,130)**
Loss attributable to minority interests	**63**	**–**	**63**
(Loss)/profit attributable to equity holders of the Company	**(1,067)**	**–**	**(1,067)**

IFRS operating profit increased by 87% to £1,109m in 2009 (2008: £592m) reflecting the significant growth in net cash generated.

GROUP RESULTS.

CREDIT RATINGS

During 2009 and early 2010, Standard & Poor's, Moody's, and AM Best, the credit rating agencies, reviewed credit ratings across the sector due to the continuing deterioration in economic and market conditions.

Our credit ratings as at 22 March 2010 are:

Rating type	Standard & Poor's[1]	Moody's[2]	AM Best[2]
Financial strength rating*	AA-	Aa2	A+
Long term	A	A2	a
Short term	A-1	P1	n/a
Subordinated	BBB+	A3	a-

* For Legal & General Assurance Society (Legal & General Assurance Society is the principal operating company of the Group). All other ratings for Legal & General Group Plc/Legal & General Finance PLC (guaranteed by Legal & General Group Plc).
[1] Stable outlook.
[2] Negative outlook.

Society remains one of the highest rated European life insurance funds by both Standard & Poor's and Moody's.

BALANCE SHEET AND CAPITAL

At the end of 2009, the estimated IGD surplus was £3.1bn (2008: £1.8bn), after accruing for the final dividend. This represents a capital coverage ratio of 224%, up from 169% at the end of December 2008.

IGD surplus[1] £bn	2009	2008
Group capital resources	**5.6**	4.4
Group capital resources requirement	**2.5**	2.6
IGD surplus	**3.1**	1.8
Coverage ratio	**224%**	169%

[1] After accrual of the final dividend of £160m (2008: £120m).

CREDIT DEFAULT RESERVE

In the first half of 2009, the bonds backing the non profit annuity liabilities experienced downgrades, mainly as a consequence of the deteriorating outlook for UK and Irish banks. This led to an increase in the long term default provision to 36 basis points (bps) (2008: 30 bps) to reflect continuing economic uncertainty.

The second half of the year saw a significant improvement in sentiment in the credit markets and a narrowing of spreads. There was a limited reversal of the downgrade experience, but despite this the long term default provision was maintained at 36 bps.

Despite challenging financial conditions in 2009, the actual default cost was only £1m after expected recoveries.

Given the markets have not completely normalised, there have been no material releases of the provisions established at the end of 2008. As a consequence of strengthening the long term provision and market movements, the total credit default provision has increased to £1.5bn from £1.2bn at end 2008. This is equivalent to 68 bps (2008: 68 bps) of defaults per annum over the term of the non profit annuity credit portfolio.

ASSET QUALITY

Shareholders have exposure to just 9% of the Group's total assets under management, or £30bn. The portfolio of investments remains of high quality.

Shareholders' exposure to UK and overseas equities was £0.9bn at 31 December 2009, and is largely limited to assets held within the shareholders' funds of Legal & General Assurance Society Limited.

DIVIDEND POLICY

Due to the unprecedented adverse market conditions in 2008 and early 2009, the Board took the decision to cut the 2008 final dividend by 50% (final dividend: 2.05p per share, total dividend paid £120m, full year dividend 4.06p, total dividend paid of £239m). Although the Group's cash generation was sufficient to maintain the dividend at the 2007 level, the principal concern was to sustain the strength of the Group's capital base at a time when financial markets were in turmoil. In August, we also announced a reduction in the 2009 half year dividend of 45% (£65m) from the 2008 level. Total cash payment to shareholders fell from £367m in 2008 to £185m in 2009.

During the second half of 2009, investment markets have recovered and shown more stability, and whilst many remain cautious about the recovery, the financial and economic outlook is now more optimistic. The Group has generated £726m of operational cash, whilst incurring £27m of strain in writing new business, resulting in £699m of net cash. The IGD surplus is estimated to have increased from £1.8bn at end 2008 to £3.1bn at the end 2009 after accrual of the dividend, reflecting improved financial strength. The Board has therefore recommended that the 2009 final dividend be based on a 33% step-up from 2008 levels resulting in a final dividend per share of 2.73p. With the half year dividend of 1.11p, this will bring total dividends for 2009 to 3.84p.

In arriving at future dividend recommendations, the Board will continue to take account of market conditions, cash generation within the businesses and the stability of the Group's capital base. We expect to demonstrate continued progress in the ability of the Group to generate cash and, as a result, we envisage that we will grow the dividend in line with medium term cash generation. We anticipate that the dividend will be comfortably covered by net cash generation.

OUTLOOK

Recovery in the UK economy in 2010 is likely to be slow and we expect the UK housing market to remain subdued. Nonetheless we expect our core UK Risk and Savings markets to recover in 2010 from depressed levels in 2009. We are optimistic about the Group's medium term growth prospects. We aim to capitalise on our market leading positions in Risk, build the LGIM franchise in the UK and overseas, deliver further improvements in Savings and continue to develop our existing international portfolio whilst exploring opportunities to expand into other attractive markets.

SOLVENCY II

Solvency II is the new risk-based regulatory approach which the EU is introducing for all insurance organisations operating in the European Union. It covers both capital adequacy and risk management, with the key objective of improving protection for policyholders. Currently the planned implementation date is 31 October 2012.

Solvency II will impact Legal & General directly in its UK, French and Dutch businesses, as well as at Group level.

The outline requirements of Solvency II are reasonably clear, but many important specific requirements remain under discussion with the European Commission and its advisors. These specific requirements will determine the impact of Solvency II on the Group. We are engaging actively to ensure a satisfactory outcome to these negotiations, to ensure that capital requirements are sufficient but not excessive and will protect consumers without increasing the cost to them of our insurance products.

We also set up a major programme to implement the Solvency II requirements. This will be an expensive and resource intensive undertaking over a period of three years, involving all of the Group's insurance subsidiaries.

RISK BUSINESSES.

"OUR RISK BUSINESSES SERVE AN IMPORTANT SOCIAL PURPOSE: WE TAKE ON CUSTOMERS' FINANCIAL RISKS FROM DEFINED EVENTS LIKE DEATH, ILLNESS, INJURY OR HOUSEHOLD DAMAGE. OUR ANNUITIES BUSINESS PROTECTS PENSIONERS FROM THE RISK OF OUTLIVING THEIR SAVINGS."

JOHN POLLOCK GROUP EXECUTIVE DIRECTOR (RISK)

OUR PERFORMANCE

	2009			2008		
	APE £m	Contribution* £m	Margin %	APE £m	Contribution* £m	Margin %
Protection	**180**	**68**	**7.9**	207	62	6.2
Annuities	**186**	**217**	**11.7**	281	209	7.4
Total	**366**	**285**	**10.4**	488	271	7.1

* From new business on an EEV basis

RISK – NET CASH GENERATION

£504m

(2008: £206m)

RISK – IFRS OPERATING PROFIT

£735m

(2008: £222m)

STRATEGY IN ACTION

Our five strategic imperatives* are applied across all business units. The following illustrates them in action in the Risk division.

IMPERATIVE	ACTIVITY
FINANCIAL MANAGEMENT	Net cash generated by the Risk business increased to £504m in 2009 (2008: £206m)
DIVERSIFIED BUSINESS	In Individual protection our product range continues its expansion into High Net Worth markets and family and business protection products.
HIGH QUALITY PRODUCTS, BROAD DISTRIBUTION	Bancassurance channel strengthened by the addition of exclusive distribution deals with Northern Rock and Skipton Building Society, amongst others.
A POSITIVE CUSTOMER EXPERIENCE	In Group protection our centres of excellence and employee specialism continue to improve experience and return to work rates for claimants.
HIGH EXPECTATION CULTURE	Market leading performance continues to be recognised in the attainment of several industry awards.

*As outlined on page 10.

FOCUS ON LONGEVITY

Success in risk markets requires skills which combine investment, longevity expertise and excellence in risk selection. During 2009 we have made progress in extending the concept of more granular and tailored pricing based on an individual's circumstances. Our Annuity Solutions service offered customers a conventional annuity with the ability to achieve extra income by providing their postcode when it was launched in 2008. In 2009 this service has been extended to improve our enhanced annuity proposition and now covers an extensive range of lifestyle and medical health risks. Our extensive and statistically credible longevity database is enhanced by our relationship with UCL and the support of the Longevity Science Advisory Panel, headed by Sir Derek Wanless. This relationship helps to inform our views on future UK life expectancy.

OUR STRENGTHS

- Risk pricing and underwriting expertise.
- Accurate statistical modelling enabled by extensive in-house database.
- Particular expertise in medical underwriting and mortality/morbidity.
- Technological investment facilitates interactive underwriting and rapid data loading.
- Economies of scale and administrative excellence.
- Leading rapid intervention-based Group protection product enables corporate clients to secure faster returns to work for sick employees.
- Synergies with LGIM facilitate pricing and execution of pension buyout and bulk annuity business.
- Wide ranging distribution through independent financial advisers (IFAs), sole-tie business partners and bank and building society partnerships.
- Housing network drives protection and GI sales by providing access to customers at point of sale.

OUR PRODUCTS

Individual protection
Covers individuals or families against financial losses arising from defined events such as death, disability or critical illness.

Group protection
Products which are designed for employers to offer as a benefit to their employees. They protect employers, employees and their families by assuming the risks and associated costs of an employee falling ill or dying while in employment.

Annuities
Bought by people converting a lump sum (often money saved in a pension scheme) into a lifelong income.

Bulk purchase annuities (BPAs) or Pension buyouts
BPAs are offered to companies wishing to transfer all or part of the responsibility and risk from company pension schemes to an insurance company for a negotiated price.

General insurance (GI)
Focusing on the household sector, we insure the fabric of properties and their contents.

Housing network
Our network of mortgage advisers provides a link with mortgage lenders, sourcing mortgages for clients and facilitating sales of Protection and GI products.

RISK BUSINESSES.

OUR RISK BUSINESSES MAINTAIN A MARKET LEADING POSITION IN KEY SEGMENTS, WITH HIGH QUALITY CUSTOMER SERVICE, SUPERIOR TECHNOLOGY AND ECONOMIES OF SCALE. WE HAVE MAINTAINED OUR MARKET LEADING POSITION DESPITE A SUBDUED HOUSING MARKET.

WE CONTINUE TO DIVERSIFY OUR PRODUCT OFFERING AND INCREASE OUR DISTRIBUTION PARTNERSHIPS WHILST FOCUSING ON PRODUCTS THAT CONTRIBUTE CASH TO THE BUSINESS THROUGHOUT 2009.

We distribute our risk products through four channels: independent financial advisers and consultants; bank and building society partnerships; through our housing network; and via direct distribution.

We continue to improve quality and service in our individual protection business, ensuring that customer fairness is at the centre of our business model. The number of critical illness claims declined due to non-disclosure has reduced to just 1.8% from 4% in 2008. This is due to improvements in our underwriting processes which increase disclosure at the point of sale rather than at the point of claim. Steps have also been taken to make joint life policies fairer. Single life policies will now be offered to people who would previously have had their joint life policy cancelled as a result of non-disclosure from their partner.

The improved technology of our online service helps advisers to sell protection as they can quote, apply and complete applications online resulting in reduced approval time for clients. The benefits of this system have now been rolled out to Yorkshire Building Society, allowing them to solve a wider range of protection needs than was previously possible. Our expertise in tele-underwriting has allowed us to speed up the application process and immediate decisions can be made for 85% of applications which go through this process.

The addition of three new life insurance plans for the over 50s further expands and diversifies our product offering. These products are only available on a direct basis, limiting distribution costs.

Continued improvements were rewarded with four awards at the Financial Adviser Life & Pensions Awards. These were Best Life Assurance Provider, Best Term Assurance Provider, Best Critical Illness and Income Replacement Provider and Best Protection Provider.

There has been further consolidation of the group protection market in 2009 which has offered us opportunities due to our size and scale. Group protection continues to support UK companies by providing and protecting employee benefits and lobbying relevant bodies to ensure that any proposed legislation has no negative impact on provision.

Group protection written premiums were maintained at over £291m despite high levels of re-quoting in 2009 as companies looked for cost reduction opportunities. We continue to explore new opportunities to expand the scope of the customer base for these products and have had some success with entry to the public sector arena, reducing our reliance on the traditional market.

Centres of excellence in musculoskeletal, cardiovascular, oncological, neurological and psychological conditions contribute to improving return to work rates. Improved results, service standards and increased levels of professional qualifications by our employees were rewarded with the attainment of both Best Group Life Provider at the Cover Excellence Awards 2009 and Rehabilitation Initiative of The Year Award at The Rehabilitation First Awards 2009.

In our annuities business, we maintain a defined appetite for longevity risk. The strategic focus of generating cash from the business means that we are not prepared to bid for business that will not deliver an appropriate return on capital. Our flexible approach to writing business means that although we continue to hold the capital and capability to write further annuity business, our appetite can be limited if prices are not attractive.

Following a successful pilot in 2008, the Annuity Plus service will be offered to all advisers. This simplified enhanced annuity product focuses on the five most common health risks affecting the retiring population – smoking, diet-controlled diabetes, high blood pressure, high cholesterol and high or low body mass.

Our annuity business is working with SAGA, a brand synonymous with the retirement market, to offer a new service for consumers wishing to buy their pension annuity on a direct basis. The SAGA service is based on our successful Annuity Solutions service and will give customers access to our non profit pension annuities, as well as a range of annuity features and payment options.

We also anticipated shifts in the distribution landscape and launched our direct to consumer annuity service which has proved very successful. We have offered this capability to other providers, increasing the potential of this product.

While it was an incredibly tough year for the mortgage market as a whole, individual protection outperformed falls in gross mortgage lending. It has become much harder for customers to secure funding for house purchases which has made it a challenging environment for advisers.

This has resulted in consolidation across the market. However, we have added partners to our housing proposition including Tyler Mortgage Management and Honister Capital, Bank of China and Ahli United Bank. This adds strength to our distribution and increases the breadth of our product offering. 2010 marks the fifteenth anniversary of the Legal & General Mortgage Club, which was one of the first clubs of its kind in the UK.

We continue to see strong improvements in the performance of our General insurance (GI) business following a thorough review and restructuring of the operation in 2008. The review focused on improving core underwriting and operational efficiency. Profits of £17m (2008: operating loss £2m) were driven by a significant improvement in the combined operating ratio, 96% (2008 108%). This has been achieved with year on year comparable weather claims experience and despite the economic backdrop of reduced mortgage related new business opportunities.

These changes have established a robust platform and provide a basis to build our GI contribution. We aim to extend our distribution range by enhancing product covers and offering access to complementary insurance products, combining these with our established expertise in offering a mortgage related proposition. In 2009 we achieved 8% premium growth despite the significant fall in mortgage transactions and GI were voted 'Personal Touch (PT) Best Buildings and Contents Provider' in 2009.

CORPORATE SOCIAL RESPONSIBILITY

OUR WORK WITH SHELTER

Our Risk business benefits from a strong housing market, through our own products and our partnerships across the market. We sell insurance to cover the homes these mortgages buy and cover the life insurance needs of the people and the families who buy these homes.

We felt it was important to put something back into this market. Our partnership with Shelter is the way we have chosen to do this. Earlier this year, we sponsored a major new report by Shelter called 'Groundbreaking'. This report is being used to lobby government and local authorities into looking at new ways of providing quality housing across all the housing tenures.

We are also supporting a project in Gloucestershire to prevent teenage homelessness and helping Shelter develop regional housing support services across the South West and North East of England. By partnering with Shelter, we are introducing them to market information they would not naturally have access to and in return they provide us access to researchers, think tanks and people we would not ordinarily meet, helping us to identify new opportunities in typically unexplored markets.

Shelter

For more information see pages 40 to 41.

OUTLOOK

New systems implementations will drive further efficiency gains in the Risk businesses and build on the cost savings delivered in 2009. We expect operating profit to be in line with 2009 after excluding the impact of a return to more normal annuity pricing conditions.

SAVINGS.

"SAVINGS DELIVERED A STRONG UNDERLYING PERFORMANCE DURING 2009, DELIVERING A TURNAROUND IN CASH GENERATION WITH GROWTH OF NEW BUSINESS, INCREASED NET FUND FLOWS AND SIGNIFICANT GROWTH IN ASSETS UNDER ADMINISTRATION."

MARK GREGORY GROUP EXECUTIVE DIRECTOR (SAVINGS)

OUR PERFORMANCE

New business APE £m

	2009	2008	% Change
Retail investments	375	229	64%
Non profit	341	459	(26%)
With-profits	191	191	0%
Total savings	**907**	879	3%

Assets under administration £bn

	2009	2008	% Change
Retail investments	13.0	9.1	43%
Non profit	20.4	17.3	18%
With-profits	21.4	19.4	10%
Total savings	**54.8**	45.8	20%

SAVINGS – NET CASH GENERATION

£33m

(2008: loss of £23m)

SAVINGS – IFRS OPERATING PROFIT

£55m

(2008: £7m restated)

STRATEGY IN ACTION

Our five strategic imperatives* are applied across all business units. The following illustrates them in action in the Savings division.

IMPERATIVE	ACTIVITY
FINANCIAL MANAGEMENT	Significant costs have been taken out of the business, commissions reduced and products re-designed to reduce strain of writing new business.
DIVERSIFIED BUSINESS	Transformation of the mix of products sold with increased focus on retail investments and Self Invested Personal Pension (SIPP) products.
HIGH QUALITY PRODUCTS, BROAD DISTRIBUTION	Savings products distributed to individuals and companies via a broad range of bank and building society partners, IFAs and direct to consumer.
A POSITIVE CUSTOMER EXPERIENCE	Charging structures of some products changed to reward and encourage customer loyalty, aligning what is best for the customer and the business.
HIGH EXPECTATION CULTURE	Several awards won in 2009 including Group SIPP provider of the year.

*As outlined on page 10.

FOCUS ON WORKPLACE SAVINGS

In the corporate market our WorkSave platform, which combines Group SIPP and our new Group ISA, appeals to employers looking to establish holistic savings opportunities for their employees. Major FTSE companies including First Group, Morrisons and BG Group took advantage of this offering in 2009.

Workplace Savings won two awards at the 2009 Pensions Management Technology, Administration and Service awards (TAS) – Group SIPP provider of the year and Group Pensions provider of the year as well as Group SIPP Provider at the Pension & Investment Provider Awards.

OUR STRENGTHS

- Wide product range to suit different maturity and asset allocation preferences.
- Broad distribution, with direct and intermediated sales through IFAs and bank and building society partners.
- Legal & General Investment Management (LGIM) synergy gives access to expert fund management.
- Adaptable approach to technology evidenced by partnership with Cofunds platform.
- Financial strength and asset allocation skills within With-profits enables us to balance expectations and risk management for customers and shareholders.

OUR PRODUCTS

Unit trusts
A relatively simple form of collective investment, which enable customers to invest in a wide variety of different securities and indices.

Individual savings accounts
Enable customers to invest in cash or securities, up to a defined annual limit on a tax efficient basis.

Investment bonds
Combine life assurance features and the facility for the customer to invest in a variety of investment funds.

Pensions
Pensions products enable individuals to save for retirement in a tax efficient way, either through a personal pension, or as part of an employer's scheme.

Structured products
Investments that aim to minimise the risk of capital loss whilst still offering some equity exposure.

With-profits
With-profits products pool customers' investments. Policies share the characteristic that investors receive bonuses as a result of direct participation in surplus profits.

SAVINGS.

OUR SAVINGS BUSINESS IS AN INVESTMENT MANAGEMENT LED MANUFACTURER AND ASSEMBLER OF MODERN, FLEXIBLE AND CAPITAL LIGHT PRODUCTS.

THE BUSINESS HOLDS £54.8BN OF CUSTOMER ASSETS UNDER ADMINISTRATION, AN INCREASE OF 20% (2008: £45.8BN), STRENGTHENING OUR POSITION AS AN ASSET GATHERER.

OUR SAVINGS BUSINESS OFFERS A WIDE RANGE OF FLEXIBLE PRODUCTS AND INVESTMENT OPTIONS WHICH ENABLE CUSTOMERS TO SAVE FOR RETIREMENT AND OTHER LIFE EVENTS.

Savings products are distributed through bank and building society partners, IFAs and direct sales.

During 2009 we have continued to implement the strategy outlined in 2008 and accelerated many of these initiatives. The focus has been on increased net cash flow and profit rather than higher sales volumes. Product mix has shifted towards modern, less capital intensive products to achieve this objective. Significant cost savings have been made across the business in 2009 and underlying net cash flow has improved.

There has been continued improvement in financial management; reducing commissions paid to intermediaries, increasing fees on some products and withdrawing products which had high reserving costs. As anticipated, the steps taken to reduce reliance on products with high levels of commission and long payback periods has resulted in a reduction in sales of unit linked bonds and stakeholder pensions.

Alongside this product redesign strategy, a cost rationalisation programme was rolled out in 2009. Year on year operating costs were reduced significantly through a reduction in headcount and a review of all non value adding expenditure.

Overall, net fund flows for retail investments increased substantially to £2.1bn versus £0.4bn in 2008, with Assets under Administration (AuA) growth of 43% to £13bn.

Interest in capital protected products has increased as customers search for security in response to a less certain financial landscape. This has included significant increases in the sale of With-profits bonds, up 96% to £55m (2008: £28m).

There has been a substantial growth in unit trust sales which have increased by 69% at £269m APE and an increase in ISA sales of 51% to £106m APE. The strong growth in sales reflects the continued success of our distribution arrangement with Nationwide Building Society and our campaign to sell more products via specialist IFAs and direct sales channels.

The charging structures of some products have been changed to reward and encourage customer loyalty. This is an example of alignment of what is best for the customer and what is best for the business, reducing costs whilst encouraging long term investment.

We continue to hold a 25% stake in Cofunds, the UK's largest independent investment platform. We now also have scale on our own platform which has seen significant growth throughout the year and now holds £1 to £1.5bn of assets. Our fund of funds products also continue to perform well.

Unit linked bond sales were 48% lower at £68m (2008: £131m), reflecting the impact of the strategic decision to reduce the capital strain of sales. Tax changes continue to reduce customer appeal for this product.

Individual SIPP sales grew by 9% in 2009. SIPP sales now represent 75% of all non profit individual pension sales. However, total APE sales of non profit pensions were 17% lower at £273m (2008: £328m) reflecting management action to limit volume in the older style stakeholder products.

Sales in Group SIPP products have remained resilient with sales 6% higher than last year and new business tender activity has been strong. Changes have been made to initial commission structures, with increased sales volumes coming via fee based intermediaries.

Overall sales of With-profits products were flat year on year at £191m. However, With-profits bonds sales remain strong, rising 96% in the year.

The awards Workplace Savings won at the 2009 Pensions Management awards reflect the Group's commitment to a high performing culture and positive customer experience. They are a strong external endorsement of the way we support our customers, deliver on our promises and give a positive customer experience on a complex savings product.

At the same awards ceremony Suffolk Life, part of the Specialised Savings division, won the award for Income Drawdown and Phased Retirement provider of the year and were also commended as runners up in the Bespoke SIPP category.

OUTLOOK

The medium-term prospects for our Savings business are good. Economic recovery, coupled with further rollback of state support, will stimulate private saving. In the shorter-term we expect increased business activity, there is strong demand for our range of pension and unit trust products, and in the workplace, our market leading Group SIPP proposition continues to attract a significant interest from employers.

CORPORATE SOCIAL RESPONSIBILITY

OUR WORK WITH A4e

Recent economic turbulence has increased the need for many families to look for financial advice and assistance. In recognition of this we have worked with a third sector organisation called A4e to provide practical support for a Money Guidance pilot in the North West of England.

Expertise was provided by staff from our employed sales force (ESF) to support this important initiative. This included advice on the differences between guidance and regulated advice, knowledge of the basic ranges of products and services open to clients in the market and providing an understanding of the way consumers can be referred to specialists in mortgages, protection, wealth and taxation.

Working with A4e gives us an understanding of how organisations such as ours can help people to get out of debt and into saving. Our ESF will be working with A4e Money Guiders over the next few months to see if there are areas of expertise where we can support them.

A4e
improving people's lives

For more information see pages 40 to 41.

INVESTMENT MANAGEMENT.

"LGIM HAS BEEN SUCCESSFUL IN ITS STRATEGY TO DIVERSIFY BY GROWING ITS CORE ACTIVE MANAGEMENT CAPABILITY AND RISK MANAGEMENT SOLUTIONS ALONGSIDE ITS MARKET LEADING INDEX TRACKING BUSINESS."

PETER CHAMBERS CHIEF EXECUTIVE OFFICER, LGIM

OUR PERFORMANCE

	2009	2008
Total funds under management (FUM)	**£315bn**	£264bn
Gross new funds*	**£33.3bn**	£33.1bn
Fee-to-fund ratio	**10.3bps**	10.6bps
Operating profit*	**£167m**	£165m

*LGIM and institutional investments in unit trusts

OPERATIONAL CASH GENERATION

£121m

(2008: £115m)

IFRS OPERATING PROFIT

£167m

(2008: £165m)

STRATEGY IN ACTION

Our five strategic imperatives* are applied across all business units. The following illustrates them in action in the Investment management division.

IMPERATIVE	ACTIVITY
FINANCIAL MANAGEMENT	Scalable business model displays high profitability, strong cash flow and high return on capital.
DIVERSIFIED BUSINESS	Successful diversification, growing core active management capability and risk management solutions alongside index tracking business.
HIGH QUALITY PRODUCTS, BROAD DISTRIBUTION	New business inflows into LGIM's active fixed income funds of £2.7bn in 2009 (excluding cash), more than double the £1.1bn received in 2008.
A POSITIVE CUSTOMER EXPERIENCE	In 2009, 24% of new business inflows came from non-index fund clients, up from 14% in 2008.
HIGH EXPECTATION CULTURE	LGIM has a strong team based culture and won many awards in 2009 including the Financial News Client Service Team of the Year.

*As outlined on page 10.

FOCUS ON GOVERNANCE

LGIM's governance approach is focused on protecting shareholders' interests. Since many of our investments are held as part of an index-tracking mandate, individual stocks cannot be sold or assigned a reduced weighting. Instead, if we see a potential problem emerging in an investee company, our approach is to work with that company to ensure the best interests of its shareholders are maintained. To achieve this, we engage in dialogue with the company and if our differences are not reconciled, we will follow up with a vote which reinforces our position at the company's Annual General Meeting. During the course of 2009, LGIM held 136 meetings with company chairmen and non-executive directors on a variety of governance issues. Our approach is steered by our adherence to the Combined Code of Corporate Governance and by the ABI's Principles for Social, Ethical and Environmental investment.

OUR STRENGTHS

- LGIM's leading market position enables us to deliver the benefits of economies of scale and excellent execution for both retail and institutional clients.
- A wide range of index funds enables investors to gain exposure to equity, government and corporate fixed income markets across the globe.
- Rigorous market analysis and selection enables active fund managers to invest in the securities and sectors they believe offer superior investment opportunities.
- Technical skill and experience in the institutional pension fund market mean LGIM is well placed to execute complex strategies for clients.

OUR PRODUCTS

Index funds

LGIM currently has some £208bn of index funds under management (2008: £176bn). Rather than making individual stock picks or assigning particular weightings to certain sectors, index funds aim to replicate the return of an equity-tracking or fixed income index.

Fixed income

LGIM provides actively managed equity and fixed income funds which aim to produce a higher return than the market over the medium to longer term.

Risk management solutions

LGIM provides a range of derivative-based investment approaches, such as liability driven investment (LDI) and equity risk management, aimed at helping pension funds meet payments to members when they fall due.

Property

LGIM is a significant investor in UK commercial property and is active as a landlord and in site developments on behalf of property fund investors.

Private equity

LGV Capital is a well established provider of private equity in the UK mid-market and has a 20 year history of successfully backing management teams in growing the value of their businesses.

INVESTMENT MANAGEMENT.

OUR INVESTMENT MANAGEMENT BUSINESS, (LGIM), IS ONE OF THE LARGEST INVESTORS IN THE UK STOCK MARKET AND THE LARGEST MANAGER OF UK SOURCED PENSION ASSETS; WITH RESPONSIBILITY FOR ALMOST 4.5% OF ALL LONDON-LISTED EQUITIES ON BEHALF OF ITS CUSTOMERS. LGIM IS ALSO ONE OF THE LARGEST LONDON-BASED INVESTORS IN OVERSEAS STOCK MARKETS.

LGIM OFFERS A FULL RANGE OF FUND AND PENSIONS MANAGEMENT SERVICES FROM INDEX AND ACTIVE EQUITIES THROUGH TO FIXED INTEREST AND CASH; IN ADDITION LGIM HAS PROPERTY AND PRIVATE EQUITY BUSINESSES.

LGIM clients include pension funds, private investors, companies, charities, life companies, friendly societies and subsidiaries within the Group.

LGIM continued to attract strong new business in 2009. Whilst maintaining its position as one of the largest providers of UK index tracking funds, LGIM has continued to diversify its offering to ensure continued growth and profitability. Active management capability and risk management solutions have been expanded, and new business inflows coming from non-index fund clients accounted for 24% of total inflows in 2009 (2008: 14%). Higher fee generating active products were successfully developed to complement strong growth in passive business. New business inflows into LGIM's active fixed income funds amounted to £2.7bn in 2009, more than double the amount received in 2008 (£1.1bn).

Consolidation amongst competitors, including Black Rock's acquisition of Barclays Global Investors (BGI), has increased the element of global competition in this market. LGIM continues to expand its global reach in the US, Europe and the Middle East and is well positioned to respond to this challenge as a powerful active and passive investment manager. Legal & General Investment Management America (LGIMA) took on its first external mandate in the United States in 2009 and is now in a position to market active fixed income and liability driven investment (LDI) funds to US institutional investors. LGIM also won its first European investment grade corporate bond mandate and received a significant passive mandate from the Gulf during the year. The ambition is to diversify in both products and markets and further opportunities will be explored in other international locations.

Against a backdrop of reduced asset prices, Investment management delivered a very strong performance in the generation of gross new business. 80% of new investments were made by existing clients (2008: 74%). It is encouraging that LGIM has significantly increased inflows into active fixed income and LDI mandates, with 95% and 61% respective growth year on year. These asset classes typically generate higher fee income than traditional index mandates.

LGIM has achieved record assets under management of £315bn as at 31 December 2009 (2008: £264bn) as a result of strong new business flows and recovering markets. In 2009, LGIM attracted £31.5bn in new fund inflows (2008: £30.9bn). LGIM is strongly cash generative and in 2009 IFRS operating profit was stable at £172m (2008: £172m) despite the impact of market volatility in early 2009.

LGIM is highly rated by its many institutional clients and their investment advisers for providing quality investment and client services. This has been recognised with a number of industry awards in 2009. Legal & General UK Property Trust was awarded Best Property Fund at the Money Observer Fund Awards. At the Financial News awards LGIM was awarded Client Service Team of the Year and Best Client Administration. Hedge Funds Review: awarded the LGIM Global Macro Fund the Best Newcomer award and Professional Pensions named LGIM Fixed Interest Manager of the Year and Pooled Manager of the Year.

2009 was a 'year of two halves' for the UK commercial property market as the trend of declining capital values in 2008 gave way to a strong recovery in the second half of the year. Legal & General Property (LGP) successfully stayed ahead of the market correction when values were falling, and positioned the business for re-entry into the market early in the second quarter.

Timely acquisitions during the year enabled Legal & General Property's Funds to secure assets at historically low pricing. Between April and December, LGP successfully invested in over £600 million of assets on behalf of their open-ended funds and ended the year with gross FUM of £8.3bn (2008: £8.6bn).

During 2009 LGP's investment performance track record has been strong, showing outperformance relative to benchmark in the majority of funds. This has already been acknowledged in several awards received during the year.

OUTLOOK

Market volatility has meant there is a growing appetite amongst pension plan sponsors and trustees to de-risk their schemes. LDI solutions enable the matching of investment portfolios to the payments required and LGIM is well placed to benefit from this trend. Looking into 2010 the pipeline of new business enquiries remains very healthy as our offering of index and lower risk active products allied to high levels of customer service continues to appeal to UK pension fund trustees and, increasingly, international clients.

CORPORATE SOCIAL RESPONSIBILITY

OUR WORK WITH WHIZZ-KIDZ

Our work with Whizz-kidz is teaching us about the challenges of mobility and accessibility in our Commercial Property Portfolio particularly for our shopping centres.

This project took the format of a mystery shopper campaign with Whizz-Kidz young ambassadors carrying out accessibility assessments at Legal & General Property's four largest shopping centres across the UK. The young ambassadors, aged from 9-18yrs, were at the forefront of the campaign from the outset, helping to design the project by feeding into the assessment criteria by which the centres would be measured.

Working with Whizz-Kidz on the issue of accessibility has allowed us to benefit from their expertise and has also provided some valuable work experience to the young ambassadors. This is a good example of how businesses and charities can work together in a mutually beneficial way.

Whizz-Kidz
move a life forward

For more information see pages 40 to 41.

INTERNATIONAL.

"OUR INTERNATIONAL BUSINESS WILL BECOME INCREASINGLY IMPORTANT AS WE EXPORT LEGAL & GENERAL'S CORE SKILLS AND VALUES TO NEW MARKETS."

GARETH HOSKIN GROUP INTERNATIONAL DIRECTOR

OUR PERFORMANCE

2009

	APE £m	New business margin %	IFRS Operating Profit £m
US	49	4.9	86
Netherlands	22	2.7	42
France	44	0.1	4
Other*			(5)
Total	**115**	**2.6**	**127**

*Other includes our joint venture operations in Egypt, the Gulf and India.

2008

	APE £m	New business margin %	IFRS Operating Profit £m
US	51	6.3	39
Netherlands	29	3.1	6
France	39	0.5	14
Total	**119**	**3.6**	**59**

INTERNATIONAL IFRS OPERATING PROFIT

£127m

(2008: £59m)

STRATEGY IN ACTION

Our five strategic imperatives* are applied across all business units. The following illustrates them in action in the International division.

IMPERATIVE	ACTIVITY
FINANCIAL MANAGEMENT	Established businesses paid increased dividends to the Group.
DIVERSIFIED BUSINESS	Business model is adapted to best suit market in each country, drawing on the Group's established strengths and capabilities.
HIGH QUALITY PRODUCTS, BROAD DISTRIBUTION	Focus on protection in developed markets and Bancassurance mass market savings in developing markets.
A POSITIVE CUSTOMER EXPERIENCE	Legal & General Netherlands (LGN) won best insurer in eight of the last nine years and Legal & General America (LGA) is well recognised for underwriting expertise.
HIGH EXPECTATION CULTURE	Led by a central team, local businesses are run by local management to the Group's highest standards of conduct.

*As outlined on page 10.

FOCUS ON AMERICA

Legal & General America (LGA) holds a strong market share in its chosen segments and is a growing operation, with approximately 400 employees across the US in three locations; our main office in Maryland, near Washington DC, and smaller operations in New York and Chicago.

The US market offers potential for expansion with many individuals either not insured at all or without adequate cover. There are therefore opportunities both to increase the number of individuals with life cover and to increase the amounts individuals are covered for. The ambition is for LGA to become an invaluable part of the growing Legal & General International portfolio.

OUR STRENGTHS

- Tailoring of product offering to fit new markets.
- Term underwriting expertise in UK, US and Netherlands.
- Group insurance presence in France, Egypt, Gulf.
- Local partners who bring access to high quality distribution and strong brand recognition.
- Bancassurance expertise in the UK has been well replicated through joint venture partnerships in Egypt, the Gulf and India.
- Intermediary channel management.
- Multi-country Takaful and conventional insurance capability.
- Product innovation.
- Strong local management teams.

OUR PRODUCTS

Term insurance
Covers individuals or families against financial losses arising from defined events such as death, disability or critical illness.

Group protection
Products which are designed for use by employers to offer as a benefit to their employees. They assume the risks and associated costs of an employee falling ill or dying while in employment.

Wealth management
A variety of long-term savings products tailored to the requirements of savers and investors in specific markets.

Unit-linked savings
A core Legal & General product set finding increasing resonance in selected international markets.

INTERNATIONAL.

WE BALANCE OUR EXISTING INTERNATIONAL BUSINESSES IN THE UNITED STATES, FRANCE AND THE NETHERLANDS WITH SELECTIVE PARTICIPATION IN THE FAST GROWING MIDDLE CLASS WEALTH OF EMERGING MARKETS.

The profitability of our established international businesses has continued to improve in 2009 and new ventures have been launched successfully during the year. Total international IFRS operating profit in sterling terms was £127m (2008: £59m) more than double that achieved in 2008. Our International businesses achieved premium income of £1,128m, (2008: £961m).

The International businesses contribution to operational cash is represented by dividends remitted from sustainable operational cash flows. In 2009 the USA paid a preference dividend of $6 million and the Netherlands also paid a dividend of €5 million.

OUR ESTABLISHED BUSINESSES

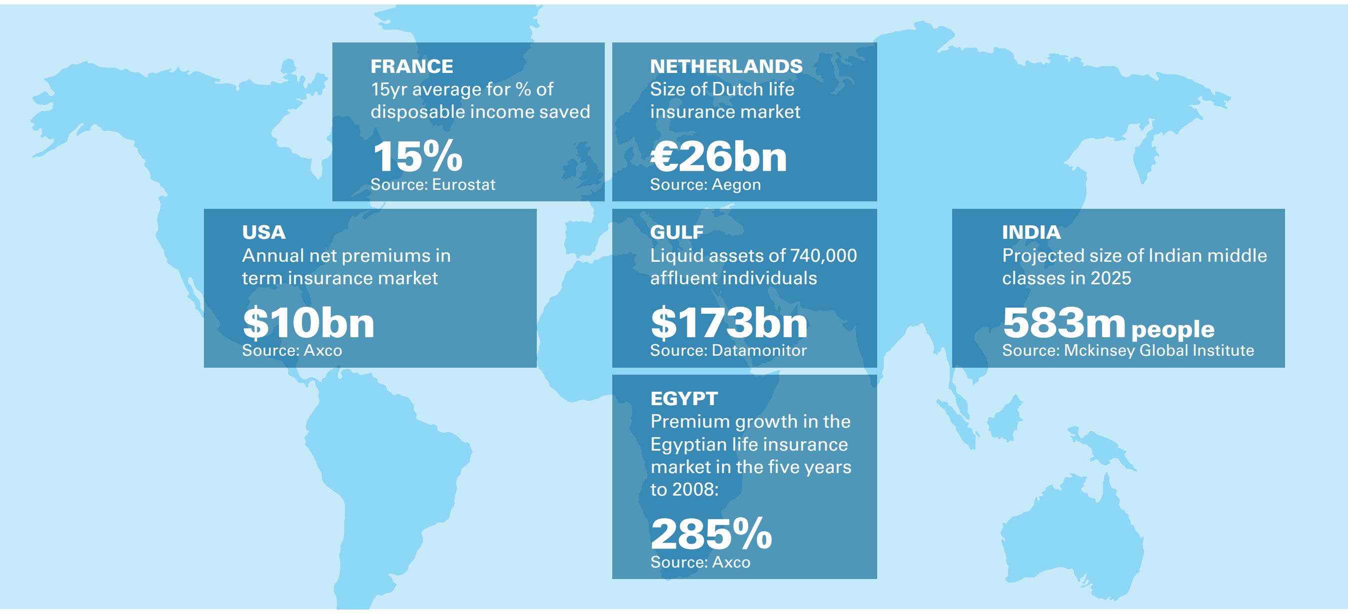
Legal & General America (LGA) is going through a period of change and transformation. More efficient use of the capital supporting LGA has allowed the business to pay dividends to the Group for 2009. This sustainable dividend stream back to the Group should be followed by our other mature businesses in 2010.

Our business in the Netherlands continues to maintain a strong position in its chosen markets, holding 5% of the term life assurance market and 22% of the single premium unit linked market. We are the eighth largest insurer in the Netherlands where we have been voted the Best Insurer in eight of the last nine years by independent brokers. However, regulatory impacts are depressing volumes in unit linked products and in local currency terms.

Legal & General France maintains its attractive position in high net worth markets. Savings written premiums are up 25% on 2008. The strong Group protection business maintained premiums at 2008 levels despite tough market conditions and has maintained profitability.

In 2010 we celebrate the tenth anniversary of the launch of CIL, our joint venture with CIB Bank in Egypt. This was

OUR GLOBAL PRESENCE



our first international bancassurance venture, and is now the largest private life insurer in the Egyptian market.

NEW VENTURES LAUNCHED

IndiaFirst Life Insurance, our joint venture in India in which we own a 26% stake, was given a licence to trade by the Indian Regulatory and Development Authority in 2009. The company initially launched with three products; IndiaFirst Savings Plan, IndiaFirst Education Plan and IndiaFirst Future Plan, a pension product. Plans to expand the product offering are well developed and include further individual and group protection policies.

Legal & General Gulf and Takaful companies have been authorised by the Central Bank of Bahrain (CBB) to sell a mixture of unit linked savings plans and pure protection products. Legal & General Gulf is the parent company with Gulf Takaful as a 100% subsidiary. Both companies have their head offices in the Kingdom of Bahrain.

Ahli United Bank, our partner in the Gulf, is the third largest bank in Bahrain with one of the most extensive networks in the Gulf Co-operation Council, offering a multi-national presence in this area. Products released at launch included Regular Savings, Flexible Savings, and Wedding, Education, Retirement, and Family Protection plans. All of the products are Sharia compliant and have been approved by the company's Sharia Board, prior to receiving regulatory approval.

Both of these new ventures represent exciting opportunities to combine our considerable insurance experience and proven bancassurance capabilities with the exclusive distribution and brand recognition of our banking partners. The new ventures will enable the development of customer centric insurance operations delivering value over the medium term for both the distributor and insurer. These represent a very attractive alternative to the high cost agency distribution model which is prevalent in the emerging markets.

OUTLOOK

Our presence in international markets continues to grow at a controlled and manageable pace in areas where we see potential for profitable growth. This will see the International businesses making a growing contribution to Group profits and cashflow in the future.

INDIAFIRST CASE STUDY

In November our Indian joint venture, IndiaFirst Life Insurance, was launched with two of the country's strongest public sector banks, Bank of Baroda and Andhra Bank. This has given IndiaFirst instant national bank branch coverage of the world's second largest population and access to a growing affluent middle class.

Legal & General worked closely with its partners, and IndiaFirst was set up as a 'Greenfield' insurance operation in record time, recruiting and training over 800 sales persons and managers as well as training and licensing bank branch employees.

The initial response has been very strong with over 45,000 policies, primarily regular premium savings, being issued in the first four months of trading through over 3,000 activated branches.

"INDIAFIRST LIFE INSURANCE, THROUGH ITS AVOWED VALUE OF PUTTING THE CUSTOMER FIRST, IS WELL ON COURSE TO ACHIEVING THE VISION AND ASPIRATIONS OF ITS PROMOTING ORGANISATIONS OF BEING INDIA'S MOST PREFERRED LIFE INSURANCE PROVIDER."

M D MALLAYA
CHAIRMAN AND MANAGING DIRECTOR
BANK OF BARODA
MUMBAI, INDIA
22 MARCH 2010

OUR PURPOSE

OUR ROLE.

INSURANCE PRODUCTS HELP TO PROTECT INDIVIDUALS AND BUSINESSES AGAINST A WIDE RANGE OF RISKS – EVERYTHING FROM POOR HEALTH AND NATURAL DISASTERS TO THE RISK OF OUTLIVING SAVINGS IN OLD AGE. BY REDUCING THE IMPACT OF THESE PROBLEMS, THE INSURANCE INDUSTRY ALLOWS PEOPLE TO BEAR RISKS WITH GREATER PEACE OF MIND AND REDUCES POTENTIAL RELIANCE ON THE STATE.

OUR PURPOSE

Finance plays a role in everybody's life, and good financial companies are those which connect with customers' lives accordingly. They facilitate household budgeting and long term saving, enable people to get through the financial consequences of unfortunate or catastrophic events and are there for customers when they are needed.

In addition to our role of delivering returns for our shareholders and customers we believe that as a business, we have a responsibility to take a position of leadership in broader society. We must ensure that we relate to the day-to-day lives and concerns of our customers, and as a shareholder we must set new and higher standards of stewardship and engagement with the businesses in which we invest.

THE ROLE OF INSURANCE

Industry and the Government share the provision of cover for what is known as 'addressable risk' in the UK. This means each side picks up its part of the costs of ill-health, healthcare, unemployment and pensions. At present, the Government is responsible for 65% of all addressable risk through its various benefit systems and 35% is covered by the insurance industry through the products provided to clients.

July 2009 saw the publication of 'Vision for the Insurance Industry in 2020' a joint report by an Insurance Industry Working Group (IIWG) consisting of the Chancellor of the Exchequer and insurance sector leaders. Our Group Chief Executive, Tim Breedon, was a member of the group, and the final report picks up several of our themes and thoughts for the future direction of the industry. The report could play a role in the economic recovery and is welcome evidence of long term thinking by the industry, despite the many immediate pressures it had to face in 2008 and 2009.

The insurance industry plays a unique role within the economy, by providing a mechanism to allow people to cope when a risk is realised. In 2008 the UK insurance industry paid out £239 million to customers every day in pension and life insurance benefits. The industry also paid out almost £9 million per day to householders in general insurance claims and £7.5 million daily for liability claims including those arising from accidents at work and professional liabilities.

OUR PURPOSE

Our product range is designed to reflect the risk, savings and investment needs of our customers at various key stages of their lives. In return, we provide benefits to our customers and our wider society as a whole.

CUSTOMERS	BUSINESSES	PRODUCTS	BENEFITS TO CUSTOMERS	PUBLIC POLICY BENEFIT
INDIVIDUALS AND CORPORATES	**RISK** – SAFEGUARDING CUSTOMERS AGAINST FINANCIAL RISKS	Customers pay up front premiums in return for insurance, individual protection and annuities.	Deliver on our promise to customers and pay claims that enable individuals to cope with the financial consequences of unforeseen events, such as bereavement, illness, damage to property and running out of savings in old age.	**The provision of these benefits reduces the likelihood of people having to fall back on the state as a result of loss of income, homelessness or poverty in retirement. This in turn benefits society by reducing pressure on strained public finances.**
	SAVINGS – FINANCIAL PLANNING, SAVINGS AND INVESTMENTS **INVESTMENT MANAGEMENT** – INVESTING ON BEHALF OF INSTITUTIONAL AND RETAIL CUSTOMERS	Customers invest funds through unit trusts, ISAs, investment funds, pensions, index funds.	Our products enable people to save for the medium and long term, either individually or through employer schemes, and to build funds which provide a secure income in retirement. We act as a steward of our customers' money.	

Our core purpose as an industry is to provide our customers with 'safety in numbers', enabling the pooling of premiums and sharing of risks to spread the financial impact of the negative events that will happen to some of them. Without our industry each of those individuals would have to provide for their own future independently without the benefits of sharing the burden of the risk with others. For the majority, this just would not be possible.

THE IMPORTANCE OF GOOD GOVERNANCE

As institutional shareholders, on behalf of pension and other funds for whom we invest, we speak for over 4.5% of the FTSE and are committed to living up to our responsibilities. We believe that companies such as ourselves which do these things responsibly are genuinely 'socially useful', and they also provide the institutional investment for businesses which in turn create jobs and pay taxes.

We play a leading role as we move towards the 'virtuous circle' described in the IIWG Paper: a business model where an increasingly customer-friendly, business-efficient insurance sector delivers a 'triple win' for customers, shareholders and taxpayers. The research supported by us and undertaken by Business in the Community (BITC) last year made a convincing case that those companies who perform well against environmental, social and governance (ESG) criteria also tend to outperform in investment terms. We want to understand this link better and we will be supporting further BITC research in this area.

Engagement requires resources: time, effort, and investment in clever and dedicated people. So if pension funds, and politicians, rightly expect a higher degree of engagement by institutions, they have to recognise that this comes at a price. We are already one of the most active institutions on environment, social and governance (ESG) engagement, and the breadth and depth of our activity is likely to increase further. It is equally important for others to step up their activity on these issues.

Our industry needs to do more to encourage high standards of governance and corporate behaviour, as well as supporting the managers of those companies which do successfully deliver benefits to customers and shareholders. As part of our 'socially useful' role, this needs to be facilitated by creating the right mechanisms for institutional shareholders to work together, and by adjusting business models so that the costs of intervention are met by the ultimate beneficiaries.

OUTLOOK

It will take the UK several years to recover from the economic crisis of 2008/2009 and for consumers' trust in financial institutions to be regained. Long term financial institutions such as Legal & General are able to play a valuable and worthwhile role in the recovery process, in channelling investment for growth, jobs and returns. We will do so as guardians of savings, managers of risk, and stewards of the assets in which we invest.

PEOPLE AND OPERATIONAL RESOURCES.

“IN 2010 WE WANT TO FURTHER IMPROVE EMPLOYEES’ UNDERSTANDING OF AND ENGAGEMENT WITH OUR STRATEGY AND VISION.”

TIM BREEDON
GROUP CHIEF EXECUTIVE

It has been a challenging year at Legal & General as it has for the UK financial services industry as a whole. We have had to make changes to address these challenges, recognising that our operating costs needed to be decisively lowered; savings of £69 million have been achieved. In many parts of the business redundancies have resulted from these difficult decisions.

Support and assistance in finding a new role was provided to all employees facing redundancy. Unite, the Union with which we continue to have a strong relationship, was fully consulted and involved throughout this difficult process, as was our Managers’ Consultation Forum (MCF). It is a credit to our staff that they have continued to perform so effectively during such a challenging period.

As outlined in last year’s report, we anticipated further economic contraction in 2009 and set challenging cost reduction targets which reflected the increasing need for efficiencies. These targets have been achieved without a negative impact on customer service.

STRATEGY IN ACTION

Our employee survey continues to play a vital role in enabling understanding and acknowledgment of how employees feel about working at Legal & General. It also highlights key areas requiring focus to enable us to achieve our goals and ambitions for next year and beyond. This year saw the highest level of feedback, with a response rate of 79% (2008: 77%).

Results showed increased co-operation between departments and improved confidence in employees feeling safe to speak up and challenge the way things are done in their division. However, results indicated that decision making and taking action were two areas that need improvement.

In addition to our employee survey, we have introduced a programme called ‘What Matters’ to help us to identify and align what is important to our customers, our employees and our business. The objectives of the programme are to empower our employees to identify what they can change, provide employees with a more external focus and to create a plan of action for change at Legal & General. This progress is integral to encouraging greater employee engagement with Company strategy and developing a high performing culture across the organisation.

Changes have already been made to some of our working policies and practices in response to feedback. Programmes are underway to improve the quality and visibility of our leadership and the articulation of our strategy alongside practical measures including the introduction of a new print management system across all sites. Our ‘Ideas in Action’ programme continues to encourage employee suggestions for continuous improvement to our business and our customers’ experience of dealing with us.

Our management development team are supporting these changes through the leadership programme being run with management teams. This focuses on the core skills a manager needs in leadership and motivation, setting goals linked to strategy, developing high performing teams and building on people’s strengths to maximise their talent. This is closely linked to our focus on improving employee engagement.

Our policy is to treat employees without discrimination and to operate equal opportunity employment practices designed to achieve this end. The Group’s policy on diversity includes giving full and fair consideration to applications for employment made by disabled persons; to continue, wherever possible, the employment of staff who become disabled and to provide equal opportunities for the training and career development of disabled employees.

In 2009 our Equality and Diversity Committee has focused on disability and on how to encourage further application and recruitment. This has included looking at how and where we advertise vacancies.

OUR SOCIAL ROLE

As a large employer we encourage our staff to be involved in their communities, either through financial contribution or with their time and expertise.

EMPLOYEES WORLDWIDE

9,324

Average number of employees during the year. (2008: 9,777)

Another way we support local communities is through volunteering. This gives our staff the opportunity to develop new skills whilst helping their community. In what has been a very difficult year, our employees have remained committed to helping these causes and undertook over 650 days of volunteering in 2009 on community projects and fundraising activities (2008: 881 days).

SUPPLY CHAIN

Management of our supply chain is an important aspect of running our business efficiently and in a sustainable way. Terms and conditions for business transactions are agreed with suppliers and payment is made in accordance with these terms provided the supplier's obligations are met. The Company has no trade creditors. As at 31 December 2009, the average number of days of payments outstanding for the Legal & General Group of companies was 33 (2008: 34).

Suppliers are regularly assessed to ensure that they comply with our environmental, social and ethical policies, as outlined in the case study on this page.

ACHIEVEMENTS

Our employees continue to perform well in difficult circumstances and this was recognised externally at this year's eg awards where four managers were shortlisted for the national finals. eg solutions is an operations management software company, and their awards recognise outstanding contributions made by individuals towards operational best practice.

Our learning and development team was also recognised with a bronze award for their Fraud Awareness Computer Based Training (CBT) in the 'Excellence in the Production of Learning Content – Private Sector' category at the 2009 e-Learning Awards. 2009 has been a successful year for our learning and development team, who also recently won joint silver at the 2009 Learning in Practise Awards in October for the work done with The Learning Network (TLN).

OUTLOOK

There are three key areas of focus for employee engagement in 2010; to improve all of our employees' understanding of the company strategy, the vision for their business area and the company as a whole; to set clear, meaningful objectives in-line with Legal & General's goals for 2010; and to communicate clearly where we are making changes and improvements for our business.

CORPORATE SOCIAL RESPONSIBILITY

OUR WORK WITH SUPPLIERS

Since 2007 our purchasing team has been sharing knowledge and expertise with a number of procurement professionals from organisations across the financial services industry. The Financial Services Purchasing Forum (FSPF) includes HSBC, Lloyds, Aviva and American Express as well as many of our strategic Business Partners.

Last year, a sub-group of this forum was formed specifically to share current best practices and build a consistent approach to the management of corporate responsibility (CR) issues within financial services supply chains. All the members have worked together on delivering initiatives and common tools designed to engage and assess suppliers and increase the knowledge of CR within organisations.

The results of the collaboration include the production of 'buying guides', a set of questions to help buyers consider corporate responsibility when purchasing goods or services. This work has recently seen this sub-group shortlisted as a finalist for the 2009 Chartered Institute of Purchasing and Supply's 'Best Contribution for Corporate Responsibility' Award.

Corporate procurement regularly issues these buying guides to all our purchasing employees at half-yearly CR Forums.

Our Sustainable Procurement Policy clearly states our CR requirements for suppliers and how we will support them in managing their social and environmental impacts. We continue to ask suppliers about how and where things were produced; if they are ethically sourced, meet environmental standards, and even the standards of working conditions.

In 2009, we spent £333m (2008: £431m) with our suppliers.

CORPORATE SOCIAL RESPONSIBILITY.

"IN ADDITION TO OUR ROLE OF DELIVERING RETURNS FOR OUR SHAREHOLDERS AND CUSTOMERS WE BELIEVE THAT AS A BUSINESS, WE HAVE A RESPONSIBILITY TO TAKE A POSITION OF LEADERSHIP IN BROADER SOCIETY."

TIM BREEDON
GROUP CHIEF EXECUTIVE

A RESPONSIBLE BUSINESS

Corporate social responsibility (CSR) is about how we behave as a business, whether we trade ethically, how we influence the way other organisations manage themselves and the efforts we make to reduce our own and the industry's environmental impacts.

Companies are increasingly evaluated by their shareholders, customers and employees on non-financial measures such as CSR metrics. We continue to see year on year improvement in our performance in the Business In the Community (BITC) CR Index. In 2009 our overall award increased from silver to gold, and we maintained our platinum award for the environment.

We also maintained our gold mark from the Charities Aid Foundation (CAF) for our Give As You Earn (GAYE) scheme. We also continue to value our inclusion in the Dow Jones Sustainability Index and FTSE4Good Index.

In last year's report we outlined how we had further integrated our corporate social responsibility initiatives into our day-to-day business. This year, to highlight the success of this alignment, there are case studies in each business review section explaining how our charitable involvement reflects our broader corporate strategy.

SUPPORTING OUR EMPLOYEES

2009 has been a year in which our employees have really risen to the fundraising challenge. This is reflected in the achievement of our GAYE target of 15% of employees using the benefits offered by the GAYE scheme with 16% doing so in 2009 (2008: 13.6%) and the high number of employees utilising their charity £750 matching allowance.

A team of 38 employees from across the Group took part in the 2009 Flora London Marathon, running for The Children's Trust. Through hard work, sponsorship and other fundraising activities, the team managed to raise an impressive £87,000 (including Legal & General's matching).

PARTNERSHIPS

In addition to the partnerships highlighted in the business sections, we have relationships with the following third sector organisations:

Our Group Protection business has worked with the British Heart Foundation (BHF) for several years, concentrating on the promotion of workplace health. BHF are one of the leading researchers on heart health, and our partnership helps us understand longevity and health issues that could affect future customers.

Our Group Protection business is working with Macmillan to help us to understand how people affected by cancer are affected financially. Together we are investigating how we can make improvements to policies to improve customer experience at this difficult time.

For more information on CSR and for more case studies and interviews:
www.legalandgeneralgroup.com

ENVIRONMENT

Our approach to managing our environmental impacts remains consistent and we continue to understand and reduce rather than offset our environmental impact. To increase awareness of environmental issues, a Computer Based Training (CBT) module was rolled out to all employees this year, which 75% of employees have now completed.

We have made progress in reducing our CO_2 emissions and the amount of waste we produce, with CO_2 emissions down 9.5% and waste production reduced by 32%, meaning that we are on track to achieve our 2012 targets. We have now established our Carbon Reduction Commitment (CRC) Committee and assessed the impact across the Business, both from our own facilities and from our commercial property portfolio. We are well-positioned for the introduction of CRC.

An area of particular focus in 2009 has been reducing the amount of paper we use as a business. Increased efficiencies have resulted in a reduction of 17% of paper used, despite an increase in the number of customer policies. For more information on our environmental results please see our online CSR report, www.legalandgeneralgroup.com

GOVERNANCE

Legal & General's CSR Committee is chaired by Tim Breedon, Group Chief Executive. The CSR Committee is supported by the Environment Committee, Charity Committee, Health & Safety Committee, Equality and Diversity Committee and the Business Ethics Committee. For further information see the report on the CSR Committee on page 71.

UNITED KINGDOM DONATIONS

During 2009, charitable donations totalling over £2.8m (2008: £3.2m) were made by the company and by employees through approved schemes. As in 2008, no political donations were made during the year.

OUTLOOK

We remain committed to our CSR strategy of aligning third party relationships with our business objectives and responsibilities whilst supporting employees in their individual fundraising efforts and will continue embedding this approach in 2010.

MEND is childhood obesity charity which helps young people and their families become fitter, healthier and happier by offering free healthy living programmes in the local community. They are helping our Risk business to understand health and longevity issues caused by childhood obesity.

We believe that basic numeracy is key to understanding and managing finances. This is why we have been supporting a programme to help Maths teachers encourage their students to take more of an interest in the subject.

As a financial services organisation, we believe we should help prevent financial crime. We have supported Crimestoppers in the development of various community programmes including educating young people about crime.

Our Savings business is working with the East and West Sussex Credit Unions to help them market their products in their local communities. In return they are helping us to understand how we can adapt our products to encourage people to save.

Our partnership with Help the Aged has introduced HandyVans across the UK. These vans highlight the importance of home security amongst vulnerable communities, installing appropriate devices to improve security whilst providing insight to our General Insurance business.

GOVERNANCE

BOARD OF DIRECTORS.

CORPORATE GOVERNANCE AT A GLANCE

Core principles
We support the Combined Code on Corporate Governance 2008 (the Code). For the year ended 31 December 2009, the Board believes that the Company complied with the principles and provisions of the Code to the extent that they apply to the Company.

Board structure
The Board comprises:
- Non-executive Chairman.
- Non-executive vice Chairman and senior independent director.
- Six other non-executive directors.
- Four executive directors.

The Board held nine scheduled meetings in 2009 (2008: nine) and one ad hoc meeting.

Committees
The Board is assisted by the following committees:
1. Audit Committee – held four meetings (2008: four).
2. Nominations Committee – held two meetings (2008: two).
3. Chairman's Succession Committee – held six meetings.
4. Remuneration Committee – held three meetings (2008: five).
5. Risk Committee – the Group Risk and Compliance Committee met four times during 2009. The non-executive chaired Risk Committee was established in early 2010.
6. Corporate Social Responsibility Committee – held four meetings (2008: four).

Changes
Board member changes are set out on page 46.

Each of the non-executive directors is considered to be independent for the purposes of the Code.

Geoffrey Timms
Company Secretary

KEY TO COMMITTEE MEMBERSHIP
[1] Member of the Audit Committee
[2] Member of the Nominations Committee
[3] Member of the Remuneration Committee


1 2


3 4

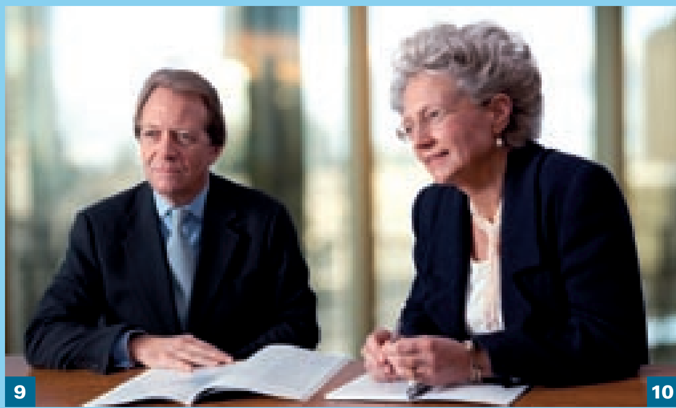
1. NIGEL WILSON, GROUP CHIEF FINANCIAL OFFICER. Nigel was appointed to the Board on 1 September 2009. Prior to joining Legal & General, Nigel was Chief Financial Officer of United Business Media Limited (from 2001) and appointed Deputy Chief Executive in 2008. Nigel is a non-executive director of Halfords Group Plc. Previous appointments include Group Finance Director at Waste Management International Plc, Chief Executive, Corporate, Guinness Peat Aviation (G.P.A.), Head of Corporate Finance and Group Commercial Director of Dixons Group Plc, Managing Director of Stanhope Properties Plc and a consultant at McKinsey & Co.

2. JOHN STEWART, CHAIRMAN. John was appointed Chairman of the Company on 1 March 2010. He is a non-executive director of Telstra Corporation, a Member of Scottish Enterprise's International Advisory Board, a member of the Court of the Bank of England and a member of the Australian Federal Attorney General's Business – Government Advisory Group on national security. Former roles include: Chief Executive of Woolwich (1996-2000), Deputy CEO of Barclays (2000-2003) and Chief Executive of National Australia Bank (2004-2008). He was also a Member of the Australian Prime Minister's Task Group on Emissions Trading.[2,3]

3. TIM BREEDON, GROUP CHIEF EXECUTIVE. Tim was appointed to the Board in January 2002 as Group Director (Investments) and became Group Chief Executive in January 2006. He joined Legal & General in 1987 and former roles include Managing Director (Index Funds) and Director (Index Funds). Tim is a director of the Association of British Insurers. Former directorships include The Investment Management Association and The Financial Reporting Council. Tim is Chairman of the Corporate Social Responsibility Committee.

4. SIR DAVID WALKER, VICE CHAIRMAN AND SENIOR INDEPENDENT NON-EXECUTIVE DIRECTOR. Sir David was appointed to the Board in March 2002. Former roles include: Chairman and Chief Executive of Morgan Stanley International Limited; executive director of the Bank of England; Chairman of the London Investment Banking Association; Chairman of the Securities and Investments Board and Deputy Chairman of Lloyds Bank.[2,3]

5 6



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5. DR RONALDO SCHMITZ, INDEPENDENT NON-EXECUTIVE DIRECTOR. Ronaldo was appointed to the Board in October 2000. He is also non-executive director of Cabot Corporation, Sick AG, and was recently appointed Vice-Chairman of the Vatican bank, Istituto per Le Opere di Religione. Former roles include: Executive Director of Deutsche Bank AG; non-executive director of GlaxoSmithKline plc and Rohm & Haas Company.[2,3]

6. RUDY MARKHAM, INDEPENDENT NON-EXECUTIVE DIRECTOR. Rudy was appointed to the Board in October 2006. He is also a non-executive director of Standard Chartered Plc and Chair of its Audit and Risk Committees, a non-executive director of the Financial Reporting Council, Moorfields Eye Hospital NHS Foundation Trust, United Parcel Service Inc, UCL Partners Ltd and AstraZeneca Plc. Former roles include: Chief Financial Officer, Director of Strategy and Technology and Treasurer of Unilever Plc; Chair and CEO of Unilever Japan, Chair of Unilever Australia.[1,2,3]

7. MARK GREGORY, GROUP EXECUTIVE DIRECTOR (SAVINGS). Mark was appointed to the Board in January 2009. He joined Legal & General in 1998 and has held a variety of divisional finance director roles and served as Group Financial Controller, Communications and Resources Director, Resources and International Director and UK Service Operations Director. From 2006, he was Managing Director, With-Profits. Prior to joining Legal & General, he had worked in senior financial and business development roles at companies including Kingfisher Plc and ASDA.

8. JOHN POLLOCK, GROUP EXECUTIVE DIRECTOR (PROTECTION AND ANNUITIES). John was appointed to the Board in December 2003, having joined Legal & General in 1980. John's former roles include: Director, UK Operations; Managing Director, Legal & General Asia and various posts in Customer Services and IT.

9. JAMES STRACHAN, INDEPENDENT NON-EXECUTIVE DIRECTOR. James was appointed to the Board in December 2003. He is a non-executive director of the Financial Services Authority (FSA), Care UK Plc, Welsh Water Limited, Sarasin & Partners LLP, JPMorgan Asian Investment Trust Plc and Social Finance, and a visiting fellow at the London School of Economics. Former roles include: Member of the Court of Directors of the Bank of England, Chairman of the Audit Commission, Managing Director of Merrill Lynch, Trustee of Somerset House and Chairman of RNID.[1,2,3]

10. DAME CLARA FURSE, INDEPENDENT NON-EXECUTIVE DIRECTOR. Clara was appointed to the Board in June 2009. She is also a non-executive director of Nomura Europe Holdings Plc and Nomura International Plc. Former roles and directorships include: Chief Executive of London Stock Exchange, non-executive director of LCH. Clearnet, Euroclear and Fortis.[1,2]

11. FRANCES HEATON, INDEPENDENT NON-EXECUTIVE DIRECTOR. Frances was appointed to the Board in July 2001. She is also a non-executive director of Jupiter Primadona Growth Trust Plc and chairman of Schroders Pension Trustees Limited. Former roles include: non-executive director AWG Plc, member of the Court of Directors of the Bank of England, Deputy Chairman of WS Atkins Plc and executive director of Lazard Brothers & Co. Limited.[1,2]

12. HENRY STAUNTON, INDEPENDENT NON-EXECUTIVE DIRECTOR. Henry was appointed to the Board in May 2004. He is a non-executive director of Ladbrokes Plc, Standard Bank Plc, The Merchants Trust Plc and New Look Retailers Limited. Former roles include: Finance Director of ITV Plc and Granada Group Plc; Chairman of Ashtead Group Plc and non-executive director of EMAP Plc, Independent Television News Limited and Vector Hospitality Plc.[1,2]

INTRODUCTION.

"THE BOARD BELIEVES THAT GOOD CORPORATE GOVERNANCE AND A SUCCESSFUL COMPANY GO HAND IN HAND."

Rob Margetts

SIR ROB MARGETTS

2009 was a challenging year for Boards of financial services companies. The events that shook financial markets last year have focussed attention on the governance of major companies and the role of the Board in providing leadership. The Board of Legal & General has steered the Company through these recent difficult times ensuring continuing stability whilst striving for better performance for our shareholders.

The Board is committed to the highest standards of corporate governance and is determined that the Group is recognised as a leader in responsible business. The Board believes that good corporate governance and a successful company go hand in hand.

The Board sits at the peak of the Company's governance structure. In the words of the Combined Code, the Board's role is to provide entrepreneurial leadership within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board achieves this through its own work and the work of its committees.

I hope this report, together with the other reports in this section, provide you with an understanding of our governance framework and how the Company complies with the principles and provisions of the Combined Code.

It has been an honour to serve the Company, the Board and shareholders for the last 13 years. I wish John and the Board all the best for 2010 and beyond.

OVERVIEW OF OUR CORPORATE GOVERNANCE FRAMEWORK

LEGAL & GENERAL GROUP PLC

AUDIT	NOMINATIONS	REMUNERATION	RISK	CORPORATE SOCIAL RESPONSIBILITY
Advises the Board on financial reporting matters and the effectiveness of the Group's internal control environment. More details can be found on page 52.	Leads the process for the appointment of new directors to the Board. More details can be found on page 50.	Advises the Board on remuneration philosophy and overall reward policy. More details can be found on page 55.	Advises the Board on matters of risk management and oversight. More details can be found on page 72.	Develops the Group's CSR strategy and policies and engages with key stakeholders on CSR matters. More details can be found on page 71.

"THE BOARD HAS CLOSELY FOLLOWED THE DEVELOPMENTS IN CORPORATE GOVERNANCE PRACTICE DURING 2009."

JOHN STEWART CHAIRMAN

Much is demanded of the directors of the Boards of major companies. It is imperative that a Board comprises the right balance of skills and experience to provide effective stewardship of the Company through good times and bad. During 2009, the Board welcomed Dame Clara Furse as non-executive director, and Nigel Wilson as executive director. All of our non-executive directors contribute their diverse business experience and wide range of skills to the Company. With two of our most experienced non-executive directors, Frances Heaton and Dr. Ronaldo Schmitz, planning to retire this year, our focus is on identifying successors with skills and experience aligned to the Group's strategy.

The Board has closely followed the developments in corporate governance practice during 2009, in particular the commentary on the Board's role in risk governance. In line with emerging best practice, the Board determined that, in future, its risk committee should be chaired by a non-executive director. Like the executive chaired Group Risk and Compliance Committee, the non-executive chaired risk committee will have responsibility for providing advice and oversight to the Board on current risk exposures and future risk strategy. More information about the committee and how we manage risk can be found at page 72.

Each year the Board participates in a formal evaluation of its performance, the performance of its committees and that of individual directors. The evaluation process is considered a valuable exercise. The Board undertook the evaluation for 2009 in January of this year. Use of an external facilitator was considered however, as the timing of the exercise coincided with the transition from Sir Rob Margetts to myself, it was agreed that the evaluation should be facilitated internally by myself and supported by externally established online tools. The evaluation comprised a confidential online questionnaire, which sought directors' views on Board relationships, the role of the Board and its committees, its effectiveness (in particular in developing and testing strategy), and individual directors' views on their own contribution during the year. The questions also examined whether the Board meets regularly enough, provides an atmosphere for candid discussion and debate, and devotes the right amount of time to the right things. I have met with all Board members individually to discuss their responses and will be developing an action plan to be agreed by the Board and implemented this year. Overall, I am satisfied that the Board operates well.

We recognise that engagement between the Board and the Company's shareholders is critical to ensure an alignment of interests. During 2009, the Company was particularly focussed on ensuring the channel of engagement was open and that the messages being communicated by the Company to its investors were clear and understandable. Meetings with institutional investors and analysts were undertaken during the year on behalf of the Board by the Group Chief Executive and Group Chief Financial Officer. The Board is supported by our Investor Relations department, which is in regular contact with institutional investors and analysts. A report on the activities of the Investor Relations department, and the feedback received from investors and analysts, is provided to the Board at each meeting by the Group Chief Financial Officer. This ensures that the Board is kept regularly appraised of the key issues and concerns of the Company's major shareholders. This year, we are continuing our focus on engagement with a comprehensive schedule of regular investor and analyst meetings. Sir David Walker, as the Senior Independent Director, and myself are available to meet or speak with major shareholders on request if they have any concerns that are not able to be addressed through the usual channels.

The Board views the Annual General Meeting (AGM) as an important opportunity to engage with the Company's private investors. All Board members attend the AGM and are available to meet shareholders and answer any questions. We endeavour to make attendance at our AGM a rewarding experience for investors in terms of meeting the Board and developing a better understanding of our business. I would encourage as many shareholders as possible to attend on 26 May 2010. We also now provide a dedicated contact in the Company for our private investors to raise any concerns or queries that they might have.

I look forward to meeting many of you at the AGM and through our Investor Relations programme.

CORPORATE GOVERNANCE REPORT.

THE BOARD MET TEN TIMES DURING 2009 AND HELD A TWO DAY EVENT OFF-SITE FACILITATED BY THE EXECUTIVE AND SENIOR MANAGEMENT TO REVIEW AND DEBATE STRATEGY.

The Board's involvement in developing and agreeing the Group's future strategy has been effective in driving the strategic direction of the Group during the recent financial turmoil and delivering strong financial performance. The two day strategy event and specific agenda items at meetings held throughout the year helps the Board to plan the strategic focus for the Group and establish the foundations for long term growth. Additional Board meetings were called as required, and in total the Board met ten times during the year.

THE BOARD

The Board comprises a non-executive Chairman, seven non-executive directors and four executive directors. The details of the current directors, including biographies, are on pages 42 and 43. During 2009, there were a number of Board changes:

- Mark Gregory was appointed as Group Executive Director (Savings) on 28 January 2009 following the resignation of Kate Avery as a director of the Company.
- Dame Clara Furse joined the Board as a non-executive director on 1 June 2009.
- Andrew Palmer retired from the Board and Nigel Wilson was appointed as Group Chief Financial Officer and a director of the Company with effect from 1 September 2009.
- John Stewart was appointed as Chairman Designate on 1 January 2010. Sir Rob Margetts retired from the Board and John Stewart formally took over as Chairman on 1 March 2010.

Appointments to the Board are the responsibility of the Board as whole, acting on the advice and recommendations of the Nominations Committee. The non-executive members of the Board contribute their diverse business experience and wide range of skills to the Company. The composition of the Board is regularly reviewed to ensure the right combination of skills is in place to successfully drive the Company forward. Most recently, this took place as part of our Board evaluation exercise, as described on page 45. Experience and qualities from other industries, and other aspects of commercial and public life, that will contribute to the driving forward of the Company's strategy are valued however, the time commitments of all our non-executive directors are carefully assessed to ensure that the Company continues to derive the benefit whilst avoiding time commitments on the non-executives that are unduly onerous. Succession planning is considered on an ongoing basis for all Board members and senior management, and arrangements are in place to identify the right people when the time comes.

The Combined Code, as well as the Company's Articles of Association, require that on appointment to the Board, a director is subject to election by the Company's shareholders at the first AGM after their appointment, and then to re-election every three years.

Dame Clara Furse, John Stewart and Nigel Wilson will all offer themselves for election at this year's AGM as they have been appointed since the last AGM. Rudy Markham, John Pollock, Henry Staunton and James Strachan retire by rotation at this year's AGM and will offer themselves for re-election. Each of the non-executive directors offering themselves for re-election have been reappointed by the Company for further three year terms. The Board is satisfied that those directors retiring and seeking re-election are properly qualified for their reappointment by virtue of their skills and experience and their contribution to the Board and its committees. The Notice for this year's AGM confirms that the performance of the directors being proposed for election and re-election continues to be effective and they continue to show commitment to their role.

If any director is not elected or re-elected at the AGM, their appointment will terminate automatically with immediate effect.

Following appointment to the Board, directors undertake a formal induction programme aimed at familiarising them with the Company, its products and services, the markets in which it operates and the Company's senior management. The programme includes meetings with the executive directors, the Group General Counsel and senior management responsible for Investor Relations, Internal Audit, Strategy, International, Communications, Human Resources and Group Compliance.

Board and committee meetings attended by each director during 2009

Director	Board (10)	Audit committee (4)	Nominations committee (8)	Remuneration committee (3)
Sir R Margetts	10 (10)	n/a	2 (2)	3 (3)
J Stewart[1]	n/a	n/a	n/a	n/a
T J Breedon	10 (10)	4 (4)	n/a	3 (3)
Dame C Furse[2]	5 (5)	2 (2)	2 (2)	n/a
M J Gregory[3]	9 (9)	n/a	n/a	n/a
F A Heaton	10 (10)	4 (4)	6 (8)	n/a
R Markham	8 (10)	4 (4)	6 (8)	2 (3)
A W Palmer[4]	7 (7)	3 (3)	n/a	n/a
J B Pollock	10 (10)	n/a	n/a	n/a
Dr. R Schmitz	9 (10)	n/a	6 (8)	2 (3)
H S Staunton	10 (10)	4 (4)	8 (8)	n/a
J Strachan	10 (10)	4 (4)	6 (8)	2 (3)
Sir D Walker	10 (10)	n/a	8 (8)	3 (3)
N D Wilson[5]	3 (3)	1 (1)	n/a	n/a

Figures in brackets indicate the maximum number of meetings that could have been attended by that director.

[1] Appointed to the Board in 2010
[2] Appointed to the Board on 1 June 2009
[3] Appointed to the Board on 28 January 2009
[4] Retired from the Board on 1 September 2009
[5] Appointed to the Board on 1 September 2009
Note: C R Avery resigned on 28 January 2009 and therefore did not attend any meetings in 2009

Ongoing training is provided to the Board through the Business Awareness Programme and ad hoc training sessions are conducted on topical issues as they arise. Sessions during 2009 included the Turner Review and the Retail Distribution Review.

The terms of appointment of the non-executive directors are available for inspection at the Company's registered office, on the Company's website and will be available at the AGM.

The service contracts for the executive directors all provide for termination on notice by the executive director or the Company on 12 months' or less. In relation to John Pollock, who will offer himself for re-election at this year's AGM, the termination notice period is six months and on termination, he would become entitled to six months' salary in addition to the payment of pension contributions and car allowance. The service contract of Nigel Wilson, who will offer himself for election at the AGM, is terminable on 12 months' notice.

The Board has determined that throughout 2009 the majority of the non-executive directors (excluding the Chairman) were independent in character and judgment. Dr. Ronaldo Schmitz has served on the Board since October 2000 and he intends to retire at this year's AGM. The Board remained satisfied of Dr. Schmitz's independence of character and judgment during 2009. Although Sir Rob Margetts first joined the Board in 1996, the Board believes that his knowledge and experience were of great value to the Board and the Company in 2009 during which time the Nominations Committee worked to identify his successor.

The Board and committee meetings attended by each director during 2009 are shown in the table above. Non-attendance at a meeting is rare and only arises if a director has an unexpected commitment or, for a newly appointed director, an unavoidable existing commitment that cannot be rearranged.

The activities of the Board are guided by the principles of the Combined Code. There is a formal list of matters specifically reserved for decision by the Board which includes all decisions on strategic matters, capital expenditure, dividend policy and major contracts. The Board regularly reviews the performance of the Group and its businesses against plan and receives regular reports from each executive director and the Group General Counsel. The Board also receives detailed briefings from senior managers on the key business areas, which are aimed at enhancing Board members' understanding of the business and provide the Board

CORPORATE GOVERNANCE REPORT.

with the opportunity to question and review strategy and develop working relationships with senior managers. The Board also receives an annual report from the Group Risk and Compliance Director on regulatory compliance matters and the Company's relationship with its regulator, the Financial Services Authority.

The Chairman and non-executive directors meet formally in the absence of the executive directors at least twice per year. The Chairman also regularly meets the non-executive directors on a one to one basis to discuss any concerns they may have about the Board or the running of the Company. The Senior Independent Director is also available to the non-executive directors should they have any concerns about the performance of the Chairman. The non-executive directors formally met in 2009 without the Chairman present to appraise the Chairman's performance. In addition to the annual Board performance evaluation, executive directors participate in regular performance reviews with the Group Chief Executive and are subject to a formal annual appraisal. The Chairman conducts regular performance reviews of the Group Chief Executive.

The Board has defined the roles of the Chairman, the Group Chief Executive and the Senior Independent Director and the division of responsibilities between them so that no one individual has unfettered powers of decision. The Chairman is responsible for the leadership and effective performance of the Board, effective communication by the Board with the Company's shareholders and, through the Company Secretary, ensuring that Board members have the information they require in order to discharge their responsibilities.

The Group Chief Executive is responsible for leading the day to day management of the Group within the strategy approved by the Board. The Group Chief Executive chairs the Executive Committee of which all executive directors are members together with the Chief Executive Officer (Investments) and Head of International. The Group Risk and Compliance Director, the Investor Relations and Strategy Director, the Human Resources Director and the Group General Counsel are all in regular attendance.

Sir David Walker is the vice Chairman and Senior Independent Director. He is available to shareholders if they have any concerns that cannot be resolved through the usual channels.

The Company Secretary is responsible for advising the Board, through the Chairman, on all governance matters. Directors have access to the advice and services of the Company Secretary as and when required, as well as to independent professional advice at the expense of the Company. The appointment and removal of the Company Secretary is a matter reserved specifically for the Board.

INTERNAL CONTROL

The Board has overall responsibility for the Group's internal control systems and for monitoring their effectiveness. Implementation and maintenance of the internal control systems are the responsibility of the executive directors and senior management. The effectiveness of the internal control systems is reviewed regularly by the Audit Committee, the main operating boards, the Group Risk and Compliance Committee during 2009 and the Risk Committee going forwards.

The Board regularly reviews actual and forecast performance of its businesses against their one year plans and other key performance indicators. Lines of responsibility and delegated authorities are clearly defined. The Group's control policies and procedures are published on a dedicated intranet site, which is regularly updated and accessible throughout the Group. Senior managers are required to confirm compliance with these policies throughout the year. The results of this confirmation process are considered by the Audit Committee on behalf of the Board.

The Combined Code requires directors to review and report to shareholders on the Group's internal control systems, which include financial, operational and compliance controls, and risk management.

The Board has controls in place to identify, evaluate and manage significant risks faced by the Group on an ongoing basis and for determining the effectiveness of the system of internal controls. Where failings or weaknesses are identified, actions are taken to remedy those failings or weaknesses. Established procedures, including those already described, are in place to comply with the Code. The Board assesses the effectiveness of internal control systems on the basis of:

- Regular reports by management to the main operating boards and the Audit Committee on the adequacy and effectiveness of internal control systems and significant control issues.

- The Group Risk and Compliance Committee's review of the process for formally identifying, evaluating and managing the significant risks to the achievement of the Group's objectives. In 2010, the Risk Committee will also have a role in this review.

- The regular compliance reports from the Group Risk and Compliance Director.

- Reports from the Group Chief Internal Auditor to the Audit Committee on the results of internal audits.

The Board takes regular account of the significance of social, environmental and ethical matters to the businesses of the Group. The work of the CSR Committee, which is chaired by the Group Chief Executive, is outlined on page 71.

The Group's internal control systems are designed to manage, rather than eliminate, the risk of failure to meet business objectives and can only provide reasonable, but not absolute, assurance against material misstatement or loss. In assessing what constitutes reasonable assurance, the Board has regard to materiality and to the relationship between the cost of, and benefit from, internal control systems.

For 2009, the Board was able to conclude, with reasonable assurance, that appropriate internal control systems were maintained throughout the year.

ANNUAL GENERAL MEETING

The Annual General Meeting will be held at 11.30am on Wednesday, 26 May 2010 at The Institution of Engineering and Technology, Savoy Place, London, WC2R 0BL. Both electronic and written proxy appointment facilities are available for shareholders. Full details on the AGM, including explanatory notes, are contained in the Notice which will be sent to shareholders at least 20 working days before the meeting. The Notice sets out the resolutions to be proposed at the AGM and an explanation of each. All documents relating to the AGM are available on the Company's website **www.legalandgeneralgroup.com**.

The Notice of AGM also sets out the deadlines for exercising voting rights and appointing a proxy (or proxies) to vote in relation to the resolutions to be proposed at the meeting. All proxy votes are recorded and counted, and the numbers for, against or withheld in relation to each resolution are announced at the AGM and published on the Company's website after the meeting. Details of voting at the AGM, including votes withheld, will be available on the Company's website directly after the meeting.

COMPLIANCE WITH THE COMBINED CODE

For the year ended 31 December 2009, the Board believes that the Company complied with the principles and provisions of the Combined Code to the extent they apply to the Company. A copy of the Code can be obtained from the Company Secretary at the registered office of the Company and is available on the Financial Reporting Council's website www.frc.org.uk.

NOMINATIONS COMMITTEE REPORT.

DURING 2009, THE COMMITTEE LED THE PROCESS FOR THE APPOINTMENT OF A NEW NON-EXECUTIVE DIRECTOR AND A SUCCESSOR FOR ANDREW PALMER, THE GROUP DIRECTOR (FINANCE). UNDER THE CHAIRMANSHIP OF THE VICE CHAIRMAN, SIR DAVID WALKER, THE COMMITTEE MANAGED THE PROCESS FOR IDENTIFYING A SUCCESSOR FOR SIR ROB MARGETTS.

The Nominations Committee leads the process for the appointment of new directors to the Board and reviews on a regular basis whether the Chairman and the non-executive directors continue to be able to meet their commitments to the Company.

Members	
John Stewart (Chairman)	Rudy Markham
Sir David Walker	Dr. Ronaldo Schmitz
Dame Clara Furse	Henry Staunton
Frances Heaton	James Strachan

The Committee is chaired by the Chairman, and all non-executive directors are members of the Committee. The executive directors, as well as the Group General Counsel and Group HR Director, may attend meetings by invitation. The Committee is chaired by the vice Chairman when it is considering matters relating to the Chairman.

The Committee meets formally once a year to review the succession plans in place for the executive directors and key senior management. Otherwise the Committee meets periodically when required.

All directors may serve on a number of other Boards, provided they can demonstrate that any such appointment will not interfere with their time commitment to the Company and that they obtain the agreement of the Chairman to the appointment before accepting. Executive directors must also obtain the permission of the Group Chief Executive. This ensures that any potential conflicts of interest or any other concerns around the proposed appointment are considered and addressed. The major commitments of our non-executive directors are outlined in their biographies on pages 42 and 43. Currently, non-executive directors are expected to commit 25 to 30 days per year. The Committee remains satisfied that all non-executive directors have sufficient time to meet their commitments to the Company. All of the non-executive directors are considered to be independent. The Committee was also satisfied that during 2009 the Chairman's other commitments did not interfere with the day to day performance of his duties for the Company.

During 2009, under the leadership of Sir Rob Margetts, the Committee was active in the appointment of a new non-executive director and in identifying a successor for Andrew Palmer, the Group Director (Finance).

Early in 2009, based on an assessment of the size of the Board and the balance of its composition, the Board decided to seek an additional non-executive director. The balance of skills, knowledge and experience on the Board was evaluated, and the Committee developed an appointment specification. The specification included a desire for the appointee to have recent executive experience. The Committee instructed external advisers to assist in the identification and shortlisting of potential candidates. All Committee members and the Group Chief Executive met the short listed candidates and unanimously resolved in April to recommend to the Board that Dame Clara Furse be appointed. Dame Clara formally joined the Board as a non-executive director on 1 June.

Following Andrew Palmer's indication that he intended to retire during 2009, the Committee commenced the search for a replacement. Taking into consideration the views of the Group Chief Executive and the other executive directors, the Committee decided to consider external candidates as well as the internal candidates identified in the Company's succession plan. A detailed specification for the role of Group Chief Financial Officer was developed and with the assistance of an external search consultancy, candidates with the requisite skills and experience were identified. These candidates were considered by the Committee together with the internal candidates. In May, the Committee resolved to recommend to the Board that a formal offer be made to Nigel Wilson to join the Company as Group Chief Financial Officer. Nigel joined on 1 September.

In early 2009, Sir Rob Margetts indicated to the Board his intention to retire once a suitable successor was identified. A sub committee of the Nominations Committee was formed of all of the non-executive directors (NEDs) except for the Chairman. The sub committee under the chairmanship of the vice Chairman, Sir David Walker, commenced the process of identifying a successor. The sub committee engaged an external search consultancy and prepared a job specification, which included desired experience, leadership skills, personal qualities and the expected time commitment. A shortlist of candidates was prepared and members of the sub committee, together with the Group Chief Executive, met the candidates. The sub committee met six times during the year and in between times, the vice Chairman and Company Secretary kept all members fully appraised of progress. In November 2009, the sub committee recommended to the Board that John Stewart be appointed as successor to Sir Rob Margetts. John Stewart's appointment as Chairman Designate from 1 January 2010 and formal appointment as Chairman from 1 March 2010, was announced in December. The sub committee was satisfied that John Stewart was independent on appointment and of his ability to meet the requirements of Chairman taking into account his other significant commitments. Sir Rob Margetts was not involved in the selection and appointment of his successor.

RESPONSIBILITIES

- Regularly review the structure, size and composition of the Board and make recommendations to the Board on any changes.
- In relation to new appointments to the Board, lead the process for the identification and nomination of candidates to fill Board vacancies. The Committee considers potential candidates on merit and against objective criteria, and also considers a candidate's ability to devote sufficient time to the job.
- Review the time commitment required from non-executive directors.
- Consider succession planning for directors and senior management to ensure the continued ability of the Company to implement its strategy and compete effectively in the markets in which it operates.

The Committee adopted updated terms of reference during 2009. The terms of reference can be viewed on our website.

AUDIT COMMITTEE REPORT.

"A PRINCIPAL RESPONSIBILITY OF THE COMMITTEE IS TO MONITOR THE INTEGRITY OF THE GROUP'S FINANCIAL STATEMENTS."

HENRY STAUNTON
AUDIT COMMITTEE CHAIRMAN

THE COMMITTEE

Members of the Audit Committee:

Members	
Henry Staunton (Chairman)	Rudy Markham
Dame Clara Furse	James Strachan
Frances Heaton	

Membership of the Audit Committee currently comprises four non-executive directors and myself as Chairman. The Combined Code requires at least one financially qualified member (as recognised by the Consultative Committee of Accountancy Bodies). Currently, two members of the Committee fulfil this requirement. All members of the Committee are required to be financially literate and to have relevant corporate finance experience. New Committee members participate in training upon joining the Committee, which covers the role of the Committee, its terms of reference and key current issues relevant to the matters considered by the Committee.

The Committee invites the Chairman, Group Chief Executive, Group Chief Financial Officer, Group Financial Controller, Group Chief Internal Auditor, UK Actuary and representatives of the external auditors, PricewaterhouseCoopers LLP, to attend all of its meetings, although it reserves the right to request that they withdraw at any time during the meeting. Other senior management are invited to present reports as required by the Committee to discharge its duties. The Committee regularly holds private meetings with the Group Chief Internal Auditor and representatives of the external auditors.

The Committee met four times during 2009. Agendas for meetings are linked to events in the Group's financial calendar. The Committee also participated in a detailed training session in March designed to assist Committee members in understanding financial reporting matters relevant to the preparation of the 2008 annual financial statements.

The Committee operates under formal terms of reference and these are reviewed annually. The Committee's terms of reference include all matters required by the Combined Code. During 2009, the Group Risk and Compliance Committee, which reports to the Board, was responsible for reviewing the internal control and risk management system. The new Board risk committee described on page 72 will assume this responsibility in future.

The Chairman of the Committee reports back to the Board on the outcome of meetings, and the Board receives the minutes of all Committee meetings.

ACTIVITIES

A principal responsibility of the Committee is to monitor the integrity of the Group's financial statements. As part of this, the Committee reviewed the areas requiring judgment as part of the preparation of the Group's financial statements during 2009. These areas change over time. With input from the Group's external auditors, including their assessment of the Group's financial reporting and control risks, the Committee reviewed the significant financial reporting issues and judgments as well as the key disclosures to be included in the financial statements published during the course of 2009. The market announcements which accompanied the financial statements were also reviewed to ensure consistency with the contents of the financial statements.

A sound system of internal controls is essential for reliable financial reporting and for the effective management of the Group. To assess the quality of the control environment of the Group, the Committee received regular reports during the year from the external auditors, as well as from the Internal Audit department, following their work in reviewing and auditing the Group's control environment. The Committee also invited senior managers from business areas across the Group to report to the Committee on the quality of the controls in their business area. This was usually linked to a report from the Group's external auditors or the Internal Audit department on their findings on the control framework in that business area.

In this way, the Committee obtains the fullest picture possible to enable it to be satisfied with the effectiveness of the Group's internal control environment. The Committee also received the minutes of the meetings of the Group Risk and Compliance Committee held during the year.

The Committee is responsible for monitoring the Group's relationship with its external auditors including their effectiveness and independence. The Committee reviewed and agreed the audit plan for 2009, and any variations to this that were proposed during the year; evaluated the quality of input, perceptiveness and robustness of representatives of the external auditors through their reports to the Committee and their participation in discussion at Committee meetings. The Committee also reviewed and agreed the fees payable to the auditors for their audit work. On the basis of this review, the Committee has recommended to the Board that it recommend that shareholders support the reappointment of PricewaterhouseCoopers as the Group's external auditors at this year's Annual General Meeting.

The Committee regularly reviews the amount and nature of non-audit work undertaken by the auditors and the associated fees, and did so in 2009. The Group has adopted a policy setting out the types of non-audit work that may and may not be provided to the Group by the auditors. This policy requires the Committee to approve the engagement of the auditors to undertake non-audit work. Non-audit work in excess of £250,000 must be subject to competitive tender. If the auditors are selected, the Committee is responsible for agreeing the fees for the work. The policy also restricts the employment by the Group of former staff of the external auditors, and precludes the employment of any audit partner if that partner was involved in providing audit services to the Group in the last three years.

The Group's Internal Audit function makes an important contribution to the Committee in the discharge of its responsibilities. The Committee reviewed and agreed the internal audit plan for 2009 and evaluated the function's performance through the quality of reports provided to the Committee, management response to audit findings and the timeliness of the implementation of recommendations. The level of skills and expertise of the individuals in the Internal Audit function and the resources available to the Internal Audit department, including staff numbers, were also reviewed.

RESPONSIBILITIES

- Advise the Board on external financial reporting matters including significant financial reporting issues and judgments and the Group's accounting principles and policies, and any changes to them.
- Review the half year and annual financial statements prior to publication including related market announcements.
- Advise the Board on the effectiveness of the Group's internal control environment and risk management systems.
- Consider and make recommendations to the Board on the appointment of external auditors.
- Monitor the relationship with the Group's external auditors including audit expertise and effectiveness, terms of engagement and fees and their independence.
- Review the extent of non-audit services provided by the external auditors.
- Monitor the role and effectiveness of Internal Audit including resourcing, annual internal audit plans, key findings and management response.

The full terms of reference for the Committee can be found on our website.

AUDIT COMMITTEE REPORT.

SUMMARY OF WORK OVER THE LAST 12 MONTHS

- Reviewed the financial statements in the 2008 Annual Report and Accounts and 2009 Half Year report, and received reports from the external auditors on those statements.
- Reviewed the basis for the preparation of the Group's accounts on a going concern basis.
- Reviewed the significant disclosures contained in the financial statements.
- Reviewed the effectiveness of the Group's internal controls based on reports received from management, Internal Audit and the external auditors and reviewed the proposed disclosures for the 2008 Annual Report and Accounts.
- Reviewed the Principal Risks and Uncertainties disclosed in the 2008 Annual Report and Accounts and 2009 Half Year report.
- Reviewed the market announcements which accompanied the 2008 Annual Report and Accounts and 2009 Half Year Report, as well as the 17 February 2009 market announcement relating to IGD Capital Surplus.
- Agreed the scope of audit work to be undertaken by the Group's external auditors and the fees to be paid to the auditors for this audit work. Reviewed the non-audit work undertaken by the external auditors during the year and the non-audit fees paid to the auditors.
- Undertook a comprehensive review of the external auditors' performance.
- Received quarterly reports from the Group Chief Internal Auditor on internal audit work undertaken, key findings, management response and the implementation of recommended actions.
- Reviewed the terms of reference for Internal Audit and evaluated the performance of the Internal Audit function.
- Received annual reports from the Group Tax Director and Group Treasurer.
- Reviewed the Committee's terms of reference.
- Participated in training on key financial reporting matters relating to the preparation of the 2008 Annual Report and Accounts and received regular updates on developments in accounting and financial reporting matters.

On behalf of the Audit Committee

Henry Staunton
Audit Committee Chairman

DIRECTORS' REPORT ON REMUNERATION.

SUMMARY

DIRECTORS' REPORT ON REMUNERATION.

LETTER FROM SIR DAVID WALKER, CHAIRMAN OF THE REMUNERATION COMMITTEE

Dear shareholder

I am pleased to present the Remuneration Committee's report on directors' remuneration for 2009, the forthcoming financial year and, subject to ongoing review, subsequent years.

The Committee has reviewed all of the Company's key remuneration policies in the light of the draft code of practice issued by the FSA, the Walker Review and other publications and guidance from the ABI, NAPF and RiskMetrics. The review confirmed that current arrangements for the overall structure of remuneration for the executive directors remains largely appropriate. However, during 2010, we will continue to review the shape of the directors' remuneration to ensure it remains competitive and continues to be fit for purpose with a view to any appropriate changes being made for 2011.

Last year the Committee decided to freeze the salaries for the executive directors and senior management except to reflect promotions, awarding no bonuses to the executive directors and reducing Performance Share Plan (PSP) awards for the executive directors from the normal policy level of 200% of salary to 150%.

The Committee continues to take a cautious position and does not feel it appropriate to change the basic shape of the remuneration framework in current economic conditions. Accordingly, the Committee envisages continuing within this basic framework in 2010 but with a return to pre-2009 incentive potential, reflecting the greater stability in the market.

Salaries have been reviewed and adjusted in line with the budget agreed for senior management below Board level (around 2%) or in line with our policy of progression towards mid-market where appropriate. Under the annual bonus plan, bonuses of between 40% and 80% of the maximum potential (125%) were awarded to the executive directors. PSP awards at the normal level of 200% of salary were also agreed for 2010.

The Committee takes seriously the issue of balancing risk and reward, an area that has received much scrutiny by regulatory authorities. During 2009, the Committee commissioned a detailed internal review of all bonus plans operating below Board level to ensure that the schemes did not expose the Company to any excessive risk and were appropriately managed. The review determined that the schemes were broadly appropriate in terms of their application. To ensure sound future governance, a Bonus Steering Committee (BSC) has been established to review any proposed new schemes and any changes to existing schemes below Board level to ensure they support business strategy and do not encourage any inappropriate risk taking. Scheme metrics, the quantum of potential award and eligibility to participate (in relation to participants below Board level) will also be reviewed to ensure they continue to be appropriate. The BSC will report to the Remuneration Committee. The Remuneration Committee retains ultimate approval for all bonus plans across the Company and has final discretion as to how they are applied.

The Committee also reviewed its current remuneration structure in relation to tax changes outlined in the April 2009 Budget. The Committee aims to ensure that its remuneration policies are appropriate in light of market conditions, legislation and are perceived as valuable to employees. The Committee agreed to consider the use of approved and unapproved nil cost options as an alternative to deferred shares.

A resolution to vote for this Directors' Remuneration Report (pages 55 to 70) will be put to the Annual General Meeting (AGM). I hope that you will support this resolution.

Sir David Walker
Chairman of the Remuneration Committee

THE REMUNERATION COMMITTEE'S GOVERNANCE AND APPROACH

GENERAL GOVERNANCE

The report of the Remuneration Committee has been prepared in accordance with the requirements of the Companies Act 2006 and Schedule 8 of the Large and Medium sized Companies and Groups (Accounts and Reports) Regulations 2008. It also describes the Group's compliance with the Combined Code on Corporate Governance in relation to remuneration. The Company is an active member of the ABI and the Committee, consistent with its approach of operating within the highest standards of corporate governance, takes significant account of guidelines issued by the ABI and other shareholder bodies (such as the NAPF) when setting the remuneration strategy for the Company. It also seeks to maintain an active and productive dialogue with investors on developments in the remuneration aspects of corporate governance generally and any changes to the Company's executive pay arrangements in particular.

Terms of reference

The Committee's terms of reference are available on our website or on request. The terms of engagement between the Company and the Committee's independent adviser Hewitt New Bridge Street (HNBS) are available on request.

Audit

During the year the Committee undertook a self evaluation of its performance in conjunction with HNBS, the Committee's independent adviser. The conclusion was that the Committee has operated effectively in determining and overseeing the implementation of remuneration policies and that all applicable regulatory requirements are being met.

REMUNERATION COMMITTEE MEETINGS

The Committee met three times during 2009 and the main issues discussed are shown on page 58.

Remuneration committee members and attendees

Remuneration Committee Member	Position	Comments
Sir David Walker	Chairman of Remuneration Committee	Independent
Sir Rob Margetts	Chairman of the Company and Member until his retirement	Independent upon appointment. Retired as Chairman from 1 March 2010
Rudy Markham	Member	Independent
Dr. Ronaldo Schmitz	Member	Independent
James Strachan	Member	Independent
John Stewart	Chairman of the Company and Member since appointment	Independent upon appointment. Appointed as Chairman from 1 March 2010.
Remuneration Committee Attendee	**Position**	**Comments**
Tim Breedon	Group Chief Executive	Attends by invitation
Elaine MacLean	Group HR Director	Attends as an executive responsible for advising on the remuneration policy
Rosemary Lemon	Group Head of Remuneration	Attends as an executive responsible for advising on the remuneration policy
Representatives of Hewitt New Bridge Street (HNBS)		Attend by invitation as the Committee's independent adviser. HNBS does not provide any other services to the Company.

No person is present during any discussion relating to their own remuneration.

DIRECTORS' REPORT ON REMUNERATION.

Remuneration committee meetings

MEETING	STANDARD AGENDA ITEMS	ITEMS DISCUSSED IN ADDITION TO THE STANDARD AGENDA
MARCH The March meeting mainly focused on remuneration issues relating to the previous and forthcoming year.	• Recommendations to the Board in respect of the Chairman's fee and executive directors' salaries. • Setting annual bonus targets for the executive directors for 2009 and determining bonuses to be paid for 2008. • Determining the 2009 Performance Share Plan (PSP) awards and performance conditions for the executive directors and approving proposed PSP awards granted to senior executives within the Group. The Committee also measured the performance condition applying to the 2006 PSP awards. This award did not vest. • Performing an oversight role on remuneration for other senior executives within the Group. The Committee reviews all pay, bonus and share award recommendations for employees whose salaries are £100,000 or above. It also reviews the remuneration for the 'oversight departments' that is, the employees in Human Resources, Finance, Group Compliance and Risk. • Review and approval of new bonus plans or amendments to existing schemes. • Approving the 2008 directors' remuneration report. • Approval to grant any Freeshares to employees based on Company performance. Freeshares are discussed twice a year. No Freeshares were granted to employees in 2009 due to economic circumstances and Company performance. • Approval of any share grants under the Share Bonus Plan (SBP).	• The March Remuneration Committee meeting also discussed an initial review of bonus schemes below Board level in light of the FSA review of remuneration guidelines. This included establishing an initial framework for future corporate governance for the approval of bonus awards. • The Committee also agreed to establishing greater clarity over bonus potential for the senior leadership group.
JULY The July meeting mainly focused on the strategic direction of reward.	• The annual review of the remuneration strategy, policy and approach for all staff. The Committee considers the policy in relation to senior executive remuneration in the context of remuneration structures across the Group as a whole. • Reviewing the terms of reference of the Committee. • Regular items include the review of any bonus plans and share grants.	• The July meeting specifically discussed tax related considerations arising from the 2009 budget.
DECEMBER The December meeting focused on the pay review budgets and the approval of bonus plans for the forthcoming year.	• Review of proposed pay, bonus and share scheme budgets for the managers' pay review. • Review of bonus schemes.	• The December meeting also discussed the final report concerning the review of all bonus schemes below Board level and the establishment of a formal Bonus Steering Committee reporting to the Remuneration Committee. This included principles and good practice in writing bonus plans. • Agreement was given at the meeting to exercise discretion over the timing of the vesting of the 2007 Share Bonus Plan to allow employees to choose whether to vest their deferred bonus in the 2009-2010 tax year. • Agreement was also given to look at the use of approved and unapproved options in relation to deferred bonus to give employees more flexibility in tax planning on the basis that such arrangements would not result in any adverse tax consequences for the Company.

OUR REMUNERATION POLICIES

Directors' remuneration for financial year ended 31 December 2009

	Salary/fees £'000	Benefits[5] £'000	Cash in lieu of pension £'000	Annual bonus Cash £'000	Annual bonus Deferred £'000	Total **2009 £'000**	Total 2008 £'000
Executive:							
Tim Breedon	770	20	169	481	289	**1,729**	1,006
Nigel Wilson[4]	175	7	–	97	59	**338**	n/a
John Pollock	370	20	81	183	110	**764**	490
Mark Gregory[2]	285	18	–	157	94	**554**	n/a
Andrew Palmer[3]	297	11	–	153	–	**461**	480
Kate Avery[1]	20	1	–	–	–	**21**	405
	1,917	77	250	1,071	552	**3,867**	2,381
Non-executive:							
Sir Rob Margetts	325	2.6	–	–	–	**327.6**	326
Sir David Walker	110	0.1	–	–	–	**110.1**	110
Henry Staunton	90	0.4	–	–	–	**90.4**	90.6
James Strachan	65	0.3	–	–	–	**65.3**	65.3
Rudy Markham	65	–	–	–	–	**65.0**	65
Dr. Ronaldo Schmitz	65	17	–	–	–	**82.0**	80
Frances Heaton	65	0.4	–	–	–	**65.4**	66
Dame Clara Furse	38	–	–	–	–	**38.0**	n/a
	823	20.8	–	–	–	**843.8**	802.9
Total	2,740	97.8	250	1,071	552	**4,710.8**	3,183.9

1. In January 2009, Kate Avery stood down from the Board. On cessation of employment she was paid statutory and contractual entitlements only. Her remuneration above reflects 20 working days in January (1 – 28). However, she left the Company on 31 August 2009 and was paid in total £256,667 up to that date. Following termination of employment she was paid a further £135,000 as the first stage of her contractual and statutory entitlements in relation to loss of office. The second and final payment of £135,000 is due in April 2010. Kate Avery's unvested Share Bonus Plan awards lapsed on her cessation of employment. No amounts were paid in lieu of bonus or share incentives.
2. Mark Gregory was appointed to the Board on 28 January 2009. His remuneration above reflects the period 28 January to 31 December 2009 (240 working days).
3. Andrew Palmer stood down from the Board on 1 September 2009. His pay reflects 168 working days (from 1 January to 1 September 2009). However, he left the Company on 31 December 2009 and his base salary was in total £460,000 up to that date. His bonus payment is pro-rated for the period 1 January to 1 September 2009. No additional bonus was paid for the period after 1 September.
4. Nigel Wilson was appointed to the Board on 1 September 2009. His bonus is pro-rated to reflect four months of employment from September to December 2009.
5. Benefits include car allowances, medical insurance and travel expenses for work purposes.

The information in this table has been audited by the independent auditors, PricewaterhouseCoopers LLP.

1) GENERAL REMUNERATION POLICY

The Group's remuneration policy is broadly consistent for all employees and is designed to support recruitment, motivation and retention as well as reward high performance in the context of appropriate risk management. Remuneration is considered within the overall context of the Group's sector and the markets in which the divisions operate. The policy for the majority of employees continues to be to pay around the relevant mid-market level with a package designed to align the interests of employees with those of shareholders, with an appropriate proportion of total remuneration dependent upon performance. Management seeks to ensure that our pay policies and practices are free from unfair bias. This is monitored by an annual equal pay audit. The policy for directors is described in more detail on the following pages.

2) REMUNERATION POLICY FOR NON-EXECUTIVE DIRECTORS

Non-executive directors (NEDs) are appointed for a period of three years. Their performance is reviewed annually. NEDs may be reappointed for a further three-year period and subsequently, if considered appropriate, for a final period of three years after which such NEDs shall be subject to annual re-election in accordance with the Company's Articles of Association and the Combined Code. Appointments may be terminated by either party without notice. Fees for the non-executive directors are determined by the Board, based on a range of external information and advice set within the aggregate limits contained in the Articles of Association.

DIRECTORS' REPORT ON REMUNERATION.

During 2009, the fees of the NEDs, including the Chairman, were reviewed and no increases were made. For 2010, it has been determined that no change would be made to fees until the new Chairman, John Stewart, has had time to consider the members of the Board committees and whether the roles and responsibilities of the NEDs have broadened in scope and time commitment given the added emphasis being placed on corporate governance and risk oversight. As a result the following fees continue to apply:

NED fees	
Chairman	£325,000
Chairman of the Remuneration Committee, Vice Chairman and Senior Independent Director	£110,000
Chairman of the Audit Committee	£90,000
All other non executive directors	£65,000

NEDs must use at least 50% of their fees, after UK tax, to buy Legal & General shares. Fees paid to non-executive directors are non-pensionable. In addition to their fees, directors are entitled to be reimbursed for expenses properly and reasonably incurred in respect of their office and shown as benefits within the emoluments table. No further remuneration is payable.

NED	Current letter of appointment start date	Current letter of appointment end date
Sir Rob Margetts	May 2008	Retired 1st March 2010
John Stewart	January 2010	AGM 2013
Sir David Walker	February 2008	February 2011
Henry Staunton	May 2007	May 2010
James Strachan	December 2009	AGM 2013
Rudy Markham	October 2009	AGM 2013
Dr. Ronaldo Schmitz	September 2006	AGM 2010
Frances Heaton	June 2007	AGM 2010
Dame Clara Furse	June 2009	May 2012

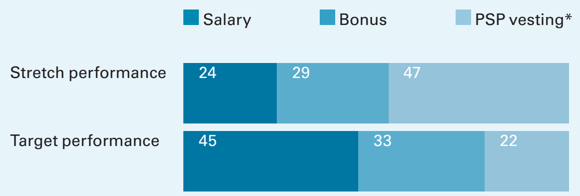
3) REMUNERATION PACKAGE FOR EXECUTIVE DIRECTORS

The remuneration of the Group's executive directors comprises salary, participation in an annual bonus plan (paid partly in cash and partly in deferred shares) and the Group's Performance Share Plan (PSP), which is a long term incentive plan, plus pension and ancillary benefits.

When setting remuneration for the executive directors, the Committee takes into account the market sector, function, job size, and individual and Company performance. In addition, the pay, employment conditions and salary budgets set for the other employees in the Company are taken into consideration. Data is obtained from a variety of independent sources (including HNBS, Watson Wyatt (now Towers Watson) and Monks Partnership, which is part of PricewaterhouseCoopers, our auditors). Where possible, the practice is to use at least two independent sources of information for each individual role.

The chart illustrates that a significant proportion of both target and stretch pay is performance-related and paid in shares.

Relative split of salary, bonus and PSP for executive directors at target and stretch performance (%) in line with current policy



* Share price growth is ignored.

Summary of key features of executive directors' remuneration

ELEMENT OF REMUNERATION PACKAGE	PURPOSE	POLICY	SUMMARY OF HOW IT OPERATES
BASE SALARY	• Help recruit and retain key employees. • Reflect the individual's experience and role within the Group.	• To pay at around the mid-market level relative to the FTSE 100, with particular regard to other relevant financial institutions. • Regard given to individual skills and experience. • In specific circumstances (for example, a new appointment) may set salaries below mid-market, with a view to reaching mid-market level within two to three years. • Increases in salary for executive directors broadly follow the salary budgets for the rest of the organisation, unless, for example, salary progression to mid-market is agreed as referred to above.	• Paid monthly in cash. • Normally reviewed by the Committee annually and fixed for the 12 months commencing 1 January. • Salary is supplemented with normal benefits available to senior managers including car allowance and medical insurance. Legal & General products can be acquired by executive directors on the terms available to other members of staff. • For 2010, increases for the executive directors are in line with the budget set for the general management pay review below Board level (2%) and our policy of salary progression towards mid-market.
ANNUAL BONUS	• Incentivise executives to achieve specific, predetermined goals during a one-year period. • Reward ongoing stewardship and contribution to core values. • Deferred proportion of bonus, awarded in shares, provides a retention element.	• Maximum bonus potential set by reference to market comparators (currently 125% of base salary). • On-target bonus of 75% of base salary (60% of maximum) for all executive directors. • Percentage of bonus deferred and awarded in shares.	• All executive directors have objectives related to Group key performance indicators (KPIs), plus individual (where relevant) divisional and strategic targets. • Bonus result is determined by the Committee after year end, based on performance against targets. • Normally, 62.5% of the bonus paid in cash and 37.5% paid in deferred shares to be held for three years. • The deferred element may be subject to forfeiture if the performance which led to a bonus being paid is found to be incorrect. • For 2009, bonuses of between 50% and 100% of base salary were awarded.
PERFORMANCE SHARE PLAN	• Incentivise executives to achieve superior returns to shareholders. • Align interests of executives and shareholders through building a shareholding. • Retain key executives over a three-year performance period.	• Awards of conditional shares made annually, with vesting dependent on relative total shareholder return (TSR) measured over the three subsequent years. • Executive directors normally receive annual grants of 200% of salary. • For 2010, awards to executive directors have been set at 200% of salary.	• Vesting condition for half of the award measures the Group's TSR versus the FTSE 100. Vesting condition for the other half measures TSR versus the insurance constituents in the FTSEurofirst 300 plus any FTSE 350 Life Insurance companies not in the FTSEurofirst 300. • The two conditions are measured independently. • The awards will vest in full if Legal & General is ranked at or above the 20th percentile. One quarter of awards will vest if TSR is at median. No awards vest below median. • The Remuneration Committee will also assess whether the TSR out-turn is reflective of the underlying financial performance of the Company and may scale back vesting.

DIRECTORS' REPORT ON REMUNERATION.

Summary of key features of executive directors' remuneration (continued)

ELEMENT OF REMUNERATION PACKAGE	PURPOSE	POLICY	SUMMARY OF HOW IT OPERATES
PENSION	• Reward sustained contribution.	• Provide competitive post-retirement benefits. • No compensation for public policy or tax changes.	• Participation in a Group pension scheme. • Accrue benefits according to length of service up to retirement. • From 2009, pensionable salary for the defined benefit pension plan has been limited to a maximum increase of 2.5% each year. • Cash alternative for executive directors opting for enhanced protection above the lifetime allowance. • New executive directors receive 15% of base salary into the defined contribution pension plan (they contribute 5%).
SHARE OWNERSHIP GUIDELINES	• To align the interests of executive directors and shareholders.	• The Group Chief Executive is required to build and maintain a shareholding of 200% of base salary and, for other executive directors, 100% of base salary.	• Executives are expected to build a shareholding through the vesting of shares under the Group's share incentive plans. Existing shareholdings and shares acquired in the market are also taken into account.

Salary

The policy is generally to pay salaries around the mid-market level for the individual's performance within the context of the relevant market for the job. However, when setting salaries, judgement is also exercised by the Committee, having regard to individual experience and responsibility.

Salary is the only pensionable remuneration and it is normally reviewed annually with effect from January.

Accordingly, particularly when a new appointment is made, salary levels may be set at a lower level than the mid-market position, with a view to increasing towards this position over the two to three years following promotion.

For 2010, the salary increases for Tim Breedon and Nigel Wilson have followed the broad budget set for the general management population in the annual pay review of around 2%. The salaries for John Pollock and Mark Gregory reflect their salary progression towards the mid-market position in line with the policy.

Accordingly, the base salaries for the executive directors for the financial year beginning on 1 January 2010 are as follows:

Name	Salary for 2010	% Increase over 2009
Tim Breedon	£785,000	1.9%
Nigel Wilson	£536,000	2.0%
John Pollock	£400,000	8.0%
Mark Gregory	£360,000	16.0%

Annual bonus

Maximum bonus levels and the proportion payable for on-target performance are considered in the light of market bonus levels for the job in other FTSE 100 financial services sector companies and the FTSE 100 as a whole. The maximum bonus payment for the executive directors remains at 125% of salary. The proportion of bonus payable for on-target performance is 60% of the maximum for all the executive directors (that is 75% of salary). 62.5% of any bonus earned will normally be paid in cash, with the balance being paid in shares under the Share Bonus Plan (SBP) described below.

In setting bonus targets, the Committee seeks to link targets to areas of the business in which the executive has particular influence and responsibility, while also seeking to maintain a keen team ethos. The executive directors' bonuses are based on a variety of targets, including Group KPIs (which for 2009 comprised 40% of the total bonus and were common to all executive directors), performance of the business unit for which the individual is responsible (where applicable), and strategic targets. The bonus that resulted from the delivery of these objectives was reviewed by the Committee based on its view of the executive's overall performance and regulatory compliance. In reviewing results, approach to risk is monitored.

For 2009, the Group KPI targets were met in full. Performance against the other Financial and Strategic targets were partially met and bonus awards ranged from 50% to 100% of salary (out of a maximum bonus potential of 125% of salary).

The bonus structure for the executive directors for 2010 was reviewed and it was felt appropriate to change the weighting for Tim Breedon and Nigel Wilson to place greater emphasis on the Group KPIs. There is no change to maximum bonus potential which remains at 125% of salary. The bonus structure for 2010 is summarised below:

Name	Group KPIs	Other financial targets	Other strategic targets	Core targets for 2010
Tim Breedon	60%	20%	20%	Deliver returns to shareholders.
Mark Gregory	40%	30%	30%	Pro-actively manage Savings financial performance, continually deliver improvements in standards of products and services to customers, ensure business efficiency.
Nigel Wilson	60%	20%	20%	Pro-active management of financial performance, manage capital requirements, strengthen the control environment, embed new metrics, mitigate commercial risks.
John Pollock	40%	30%	30%	Pro-actively manage the Protection and Annuities financial performance, ensure high standards of customer experience and improve business efficiency.

4) REMUNERATION POLICY FOR OTHER SENIOR EXECUTIVES

The remuneration policy for executives below Board level is broadly consistent with that followed at executive director level. There are 159 executives in the UK whose salaries exceed £100,000.

Salary range	Number of executives
£100,000 – £124,999	83
£125,000 – £149,999	39
£150,000 – £174,999	24
£175,000 – £199,999	4
£200,000 – £224,999	7
£225,000 – £249,999	1
£250,000+	1

SHARE PLANS

SHARE BONUS PLAN (SBP)

As stated above, 37.5% of any bonus earned is normally deferred into shares under the SBP, under which restricted shares are awarded and held in a trust for three years. The release of shares is not subject to further performance conditions; however, executives are normally required to remain in employment during the three-year vesting period. As the shares have been earned prior to award, any dividends occurring on these shares are paid to the executives during the vesting period. The value of the shares awarded to directors is reported in the year of performance and shown in the directors' remuneration table on page 59.

Should the performance which led to the payment of a bonus subsequently be found to be misstated, the Committee has discretion to withhold some or all of the SBP awards paid to executive directors relating to the relevant year's performance.

PERFORMANCE SHARE PLAN (PSP)

Executive directors are entitled to participate in the Group's PSP. The PSP was approved by shareholders in 2004. In March 2007 the Committee approved the introduction of a specific long term incentive plan for LGIM senior executives (none of whom are executive directors). The PSP remains the sole long term incentive arrangement for all other senior executives.

DIRECTORS' REPORT ON REMUNERATION.

Under the PSP, awards of conditional shares are made to top managers. The Committee reviews the quantum of awards made each year to ensure that it is in line with the market. The maximum annual award possible in 2010 remains at 200% of salary, and it is generally the Committee's policy to make awards of this level to executive directors annually. However, when making awards, it will also consider wider factors such as company performance in determining whether to grant at this normal policy level. In view of the exceptional economic and financial situation, the Committee decided to reduce the size of awards for 2009 to 150% of salary (with the exception of operating the normal 200% limit for the award granted on recruitment to the new Group Chief Financal Officer (CFO) as outlined below). Given the return to greater market stability, the Committee intends to return to a policy of granting awards worth 200% of salary in 2010.

The number of shares that vest is dependent on Legal & General's relative TSR performance over a three-year period as follows:

Legal & General's TSR relative to the comparator group at the end of the performance period	Percentage of award which vests
Below median	0%
Median	25%
Between median and 20th percentile	25%-100%
20th percentile or above	100%

Until 2007, the FTSE 100 was used to measure relative TSR performance. For the awards made in 2008 onwards, two distinct performance measures are used: half is measured relative to the FTSE 100 constituents (as at the grant date), with the balance being measured against the insurance constituents of the FTSEurofirst 300 plus any FTSE 350 Life Insurers not in the FTSEurofirst 300. Performance under the two elements is assessed independently.

The Committee considers that the measures and targets remain appropriate. They endorse consistency in the remuneration policy and provide a clear alignment of interests with shareholders. In addition they ensure a degree of risk management as TSR (through share price) reflects both underlying financial performance and the market's assessment of the quality and sustainability of those earnings.

Additionally, the Committee assesses whether the underlying performance of the Company is reflective of the TSR out-turn. The Committee may exercise its discretion to scale back the vesting of awards if it was felt that the Company's financial performance did not justify the level of vesting. The parameters which the Committee uses in making this assessment include market share, partnerships entered into and maintained, cost constraint, capital management, risk and shareholder perception.

Performance against TSR conditions is independently reviewed by Hewitt New Bridge Street.

Appointment of new Group Chief Financial Officer (CFO)

Nigel Wilson was appointed CFO on 1 September 2009. His ongoing remuneration package is consistent with the standard structure for executive directors as outlined above. He had a starting salary of £525,000. Additionally, in order to facilitate his recruitment, Nigel Wilson received the following share awards on 16 October 2009:

- an award of shares worth 200% of salary under the PSP; and
- a one-off award of shares to compensate for existing share awards that Nigel Wilson forfeited with his previous employer upon joining Legal & General. Most of the value in those awards was either subject to no pre-vest performance conditions or subject to conditions which were considered to be likely to vest. The terms of the one-off award were structured, therefore, mindful of the Committee's duty to fairly compensate the executive without including any additional value which is not necessary to secure his recruitment.

Nigel Wilson purchased 760,948 Legal & General shares worth £675,000 on 16 October 2009 and in return he was granted an award of 760,948 shares. This award vests in three equal tranches on the second, third and fourth anniversary of grant subject normally to continued employment and continued holding of the purchased shares. Nigel Wilson will not receive the value of any dividends occurring on the awarded shares between grant and vesting. Details of the awards are shown on page 67.

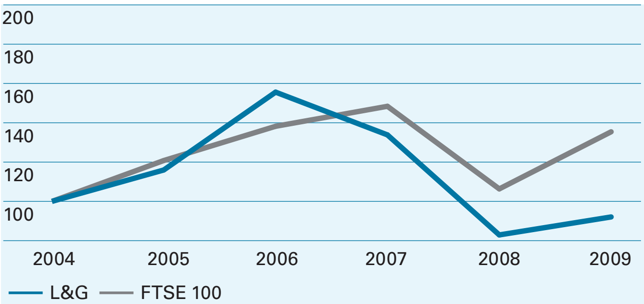
If, prior to the normal vesting date, Nigel Wilson ceases to be an employee then the share award will lapse unless his departure is by reason of death, retirement, redundancy, ill health, disability or in other circumstances at the Committee's discretion, in which case the award shall vest. Awards will also vest early in the event of a change of control of the Company. This award, which is not pensionable, was granted under the terms of Listing Rule 9.4.2R(2) and the terms of the award will be available for inspection by shareholders at the Company's registered office and at the Annual General Meeting.

The basis for determining Nigel Wilson's entitlement to shares in the event of a capitalisation issue, rights issue or open offer, sub-division or consolidation of shares, reduction of capital or any other variation of capital cannot be altered to his advantage without the prior approval of shareholders at a general meeting (except for minor amendments to benefit the administration of the scheme, to take account of a change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for Nigel Wilson or Legal & General).

Five-year total shareholder return

The chart below shows the value, as at 31 December 2009, of a £100 investment in Legal & General shares on 31 December 2004, compared with £100 invested in the FTSE 100 on the same date. The other points plotted are the values at intervening financial year-ends. The FTSE 100 index was chosen as the Company is a member of this index.

Total shareholder return (at 31 December 2009)



Source: Thompson Reuters.

ALL EMPLOYEE SHARE SCHEMES

There are share schemes for all UK employees. Executive directors are entitled to participate on the same terms as all UK employees in the Savings-Related Share Option Scheme and the Employee Share Plan, both of which are approved by HMRC.

DILUTION LIMITS

The PSP and the SBP operate with market-purchased shares that are held in an Employee Benefit Trust. The Company's all-employee plans may be satisfied using either new-issue or market-purchased shares.

The Company's all-employee plans and the now-closed Executive Share Option Scheme operate within the ABI's dilution limit of 5% in ten years for executive schemes and all its plans operate within the 10% in ten years limit for all schemes. As at 31 December 2009, the Company had 4.56% share capital available under the 5% in ten years limit, and 8.03% share capital available under the 10% in ten years limit.

At 31 December 2009 27,893,949 shares were held by the Employee Benefit Trust to hedge outstanding awards of 43,755,398 for the PSP and SBP. This means that the Trust holds 63.7% of outstanding awards.

SHAREHOLDINGS AND BENEFITS

Share ownership guidelines

In order to further align the interests of the executive directors and shareholders, the executive directors are required to build a significant personal shareholding in the business. The Group Chief Executive is expected to build a holding of shares valued at twice salary while the other executive directors are expected to build towards a holding valued at one times their salary.

As at 31 December 2009, the executive directors' share ownership against the guidelines were:

Director	Actual share ownership at 31st December 2009	Guideline on share ownership as a percentage of salary	Guideline met?
Tim Breedon	202%	200%	Yes
Nigel Wilson	234%	100%	Yes
John Pollock	129%	100%	Yes
Mark Gregory	136%	100%	Yes

Share Price used at 31st December 2009 of 80.6 pence.

Although share ownership guidelines are not contractually binding, the Committee retains the discretion to withhold future grants under the PSP if executives do not comply with the guidelines.

DIRECTORS' REPORT ON REMUNERATION.

DIRECTORS' SHARES INTERESTS

The holdings of directors in office at the end of the year in the shares of the Company, including unvested shares awarded under the Employee Share Plan and Share Bonus Plan are shown below. These exclude unvested awards made by the Company under the Performance Share Plan.

Name	31 December 2009	1 January 2009
Tim Breedon	**1,927,045**	**1,924,195**
Mark Gregory	**521,593**	**477,505**
John Pollock	**590,578**	**609,602**
Nigel Wilson	**1,521,896**	**0**
Dame Clara Furse	**13,067**	**0**
Frances Heaton	**136,988**	**106,140**
Sir Rob Margetts	**882,802**	**620,627**
Rudy Markham	**122,409**	**49,993**
Dr. Ronaldo Schmitz	**304,349**	**117,617**
Henry Staunton	**207,020**	**137,600**
James Strachan	**159,754**	**92,087**
Sir David Walker	**419,109**	**333,730**

SHARE OPTIONS

Executive directors' options outstanding under the Company Share Option Plan (CSOP), Executive Share Option Scheme (ESOS) and/or under the Savings-Related Share Option Scheme (SAYE) comprise:

MOVEMENTS IN YEAR

Name		Share options 1 Jan 2009	Options (exercised/ lapsed) granted	Share options 31 Dec 2009	Exercise price (p)	Earliest exercise date	Latest exercise date
Tim Breedon	SAYE	**9,220**		**9,220**	101.4	1.10.09	31.3.10
	CSOP	**545**		**545**	158.47	11.4.03	10.4.10
	ESOS	**78,115**	(78,115)	**0**	162.36	24.4.02	22.4.09
Mark Gregory	SAYE	**9,220**		**9,220**	101.4	1.10.09	31.3.10
	CSOP	**545**		**545**	158.47	11.4.03	10.4.10
	SAYE	**0**	27,767	**27,767**	56	1.10.14	31.3.15
Andrew Palmer	SAYE	**18,585**		**18,585**	98.6	31.12.09	30.6.10
	CSOP	**545**		**545**	158.47	11.4.03	10.4.10
	CSOP	**19,589**		**19,589**	148.62	10.4.04	31.12.10
	ESOS	**307,710**		**307,710**	148.62	10.4.04	31.12.10
	ESOS	**436,400**		**436,400**	147.48	10.4.05	31.12.10
John Pollock	SAYE	**17,038**		**17,038**	98.6	1.5.13	31.10.13
	CSOP	**545**		**545**	158.47	11.4.03	10.4.10

The SAYE scheme is approved by HMRC and, in accordance with the relevant legislation, has no performance conditions.

One option over 78,115 shares lapsed in 2009. As at 31 December 2009, there were 819,942 options outstanding for executive directors where the exercise price exceeded the market price of 80.6 pence. The range of middle market closing share prices during 2009 was 23.0 pence to 88.8 pence.

Andrew Palmer retired on 31 December 2009. His outstanding options crystallised on his retirement date, with exercise periods of 12 months for his CSOP and ESOS options and six months for his SAYE option.

Kate Avery's outstanding options lapsed in full on cessation of her employment on 31st August 2009.

All outstanding ESOS awards for the above have now met their performance conditions and are exercisable.

The Company's register of directors' interests, which is open to inspection, contains full details of directors' shareholdings and share options.

No share options were exercised by executive directors during 2009.

The information in this table has been audited by the independent auditors, PricewaterhouseCoopers LLP.

SHARE BONUS PLAN

Awards made since 2005 have been included within the directors' remuneration table in the year to which the bonus relates – see page 59.

Nigel Wilson Recruitment Award

The following shares were granted – see page 64

Date of Award	Number of shares	Date of Vesting
16th October 2009	253,649	16th October 2011
16th October 2009	253,649	16th October 2012
16th October 2009	253,650	16th October 2013

PERFORMANCE SHARE PLAN

Name	Awards granted[1]	Maximum award receivable for stretch performance	Awards vesting[2]	Awards lapsing	**Maximum outstanding awards as at 31 December 2009**
Tim Breedon	24 April 2006	960,304		(960,304)	**0**
	25 April 2007	950,544			**950,544**
	29 April 2008	1,210,688			**1,210,688**
	6 May 2009	1,984,536			**1,984,536**
Mark Gregory	24 April 2006	256,080		(256,080)	**0**
	25 April 2007	231,212			**231,212**
	29 April 2008	274,212			**274,212**
	6 May 2009	798,969			**798,969**
Andrew Palmer[2]	24 April 2006	569,068		(569,068)	**0**
	25 April 2007	565,188		(565,188)	**0**
	29 April 2008	723,268		(723,268)	**0**
	6 May 2009	1,185,567	259,613	(925,954)	**0**
John Pollock	24 April 2006	348,551		(348,551)	**0**
	25 April 2007	411,044			**411,044**
	29 April 2008	581,760			**581,760**
	6 May 2009	953,608			**953,608**
Nigel Wilson	16 October 2009	1,194,359			**1,194,359**

The table shows the maximum number of shares that could be released if awards were to vest in full. Participants do not receive dividends on unvested awards.

1. The share price on the date of grant was 58.2p for the 6 May 2009 awards and 87.9p for 16 October 2009 award. These awards vest on the third anniversary of the award date subject to the satisfaction of performance conditions as described on page 64.
2. Andrew Palmer's 2007 and 2008 awards lapsed, having failed to meet their performance conditions when tested on his retirement date. His 2009 award met its performance condition in full and vested in accordance with the Plan rules. 259,613 shares vested and 925,954 lapsed as a result of the reduced performance period. The share price on 31 December 2009 was 80.6 pence.
3. Kate Avery's outstanding awards lapsed in full on the cessation of her employment. Her unvested awards under the Share Bonus Plan also lapsed on cessation of employment. Awards that reached maturity before 31 August 2009 vested in accordance with the rules.

The information in this table has been audited by the independent auditors, PricewaterhouseCoopers LLP.

DETAILS OF HOW AWARDS VESTED AND LATEST POSITION FOR OUTSTANDING AWARDS

Grant date	Performance period	TSR ranking versus FTSE 100	Percentage of award vesting
24 April 2006 – actual performance	24 April 2006 to 23 April 2009	68	zero

Grant date	31 December 2009 vesting projection (% of award)
25 April 2007 – performance to 31 December 2009	zero
29 April 2008 – performance to 31 December 2009	zero
6 May 2009 – performance to 31 December 2009	100%

DIRECTORS' REPORT ON REMUNERATION.

In 2010, the Remuneration Committee decided that executive directors should be granted awards of performance shares to the following values: Tim Breedon £1,570,000 Mark Gregory £720,000 John Pollock £800,000 and Nigel Wilson £1,072,000.

OTHER SHARE PURCHASES

The changes in the directors' share interests between 31 December 2009 and 23 March 2010 are outlined in the tables below. The executive directors' share purchases were made pursuant to their participation in the Employee Share Plan:

2010 Name	4 January	1 February	1 March
Tim Breedon	183	188	195
Nigel Wilson	–	186	195
John Pollock	184	187	195
Mark Gregory	183	188	195

The following non-executive directors acquired shares pursuant to the regular monthly purchase of shares as part of their remuneration:

2010 Name	4 January	1 February	1 March
John Stewart	–	–	21,039
Sir Rob Margetts	20,107	20,238	20,626
Dame Clara Furse	1,993	2,046	2,086
Frances Heaton	1,993	2,046	2,086
Rudy Markham	1,993	2,046	2,086
Dr. Ronaldo Schmitz	1,993	2,046	2,086
Henry Staunton	5,554	5,297	5,399
James Strachan	1,993	2,046	2,086
Sir David Walker	4,476	4,596	4,684

BENEFITS

Other benefits for executive directors provided by the Group are:

- pension scheme
- car allowance
- medical insurance; and
- staff discounts.

Our products can be acquired by executive directors on the terms available to members of staff.

Pensions

Three of the executive directors (Tim Breedon, John Pollock and Mark Gregory) are members of the Group UK Senior Pension Scheme ('the Plan'), details of which are given in the Pension Entitlements section on page 69.

Executives who elected solely for primary protection in response to the lifetime allowance introduced as part of the reforms to pensions legislation in 2006, remain in the Plan. For those executives who elected for enhanced protection, they have opted out of the Plan for future service accrual. Consistent with the legislation, affected executives will be entitled to a pension determined by reference to pensionable earnings at retirement, provided this does not breach the enhanced protection requirements.

From 1 January 2009 onwards, the increases in pensionable salary under the Plan have been capped at a maximum of 2.5% each year for active members (including relevant executive directors). For Tim Breedon and John Pollock, both of whom opted for enhanced protection and no longer accrue pension within the Plan, their non-bonusable salary supplement is now 22% of the equivalent of the 'capped pensionable salary' had they remained members of the Plan from 1 January 2009, reflecting a broadly equivalent benefit to the application of a 2.5% per annum pensionable salary increase cap. In addition, their basic salary at retirement will no longer be used to determine their ultimate pension entitlement.

In accordance with the benefit changes made with effect from 1 January 2009, accrued pension to 31 December 2008 based on final pensionable salary at 31 December 2008 will increase by:

a) for pension earned before 6 April 2006 the greater of the retail price index (RPI) and national average earnings (NAE), with a maximum of 5% in any year; and
b) in respect of service from 6 April 2006 to 31 December 2008 the lesser of 5% per annum over the whole period and the RPI.

Retirement

On retirement from Legal & General at age 60 and subject to statutory limits, executive directors are entitled to pensions as follows:

Andrew Palmer: two-thirds of his annual 'capped' pensionable salary at retirement.

Mark Gregory: one-sixtieth of his eligible pensionable salary for each year of eligible service.

(From 1 January 2009 onwards, the increases in pensionable salary under the Plan are capped at a maximum of 2.5% each year for active members, including relevant executive directors).

Tim Breedon and John Pollock: one-sixtieth of eligible salary for each year of service through to the date they opted for enhanced protection. Since opting for enhanced protection on 6 April 2006 they have received a cash supplement in lieu of pension accrual as shown in the Directors' Remuneration table on page 59. Consistent with the legislation, their pension entitlement at retirement remained linked to their salary; however, this linkage ceased at 31 December 2008.

Nigel Wilson: Nigel Wilson is a member of the Company's defined contribution arrangements, the Legal & General Staff Pension Plan. He is entitled to a company contribution of 15% of his pensionable salary.

Bonus sacrifice into pension

Directors, like all managers, may elect, before its award, to sacrifice all or part of their cash bonus into pension. Bonus sacrifice is at the discretion of the Company each year.

Death in service

On death in service, a capital sum equal to four times salary is payable, together with a spouse's pension of four-ninths of the member's annualised salary. Protection is also offered in the event of serious ill health. This latter benefit has no transfer value in the event of the member leaving service.

Pension entitlements

Name	Age at 31 December 2009	Increase in accrued pension in 2009 £'000	Accumulated accrued pension at 31 December 2009 £'000	Transfer value of accrued benefits at 31 December 2009 £'000	Transfer value of accrued benefits at 31 December 2008 £'000	Increase/ (decrease) net of employee contributions in 2009 £'000
Tim Breedon	51	13	279	5,810	5,291	518
John Pollock	51	8	174	3,587	3,251	336
Mark Gregory	46	5	30	521	404	114
Nigel Wilson[1]	53	0	0	0	0	0
Andrew Palmer	56	25	287	6,615	5,811	798
Kate Avery	49	10	49	890	673	212

The increase in accrued pension during the year excludes any increase for inflation.

1. Nigel Wilson is a member of the defined contribution arrangement. The Company contributed £27,296 into his fund in 2009.

The information in this table has been audited by the independent auditors, PricewaterhouseCoopers LLP.

DIRECTORS' REPORT ON REMUNERATION.

Change in transfer value (TV): the increase in the accrued benefit, which is the actual benefit for the affected executives, increased by between £5,000 and £25,000 for each individual. This is consistent with the calculation of the entitlement as explained in the Benefits section on page 68. The above table also shows the increase in transfer value (being the current capital value now of the pension ultimately due). In the case of Tim Breedon and John Pollock this level of increase did not arise as a result of extra accrual - they ceased accruing any additional pension entitlement with effect from 31 December 2008. The reasons for the increase in transfer value are primarily a combination of the revaluation of their deferred pension entitlements at 31 December 2008 in line with the National Average Earnings (NAE) index, which was was 5% in 2009, and the fact that the transfer value factors increase with age.

DIRECTORS' LOANS

At 31 December 2009 there were no outstanding loans made to directors.

SERVICE CONTRACTS

The termination period for Tim Breedon and John Pollock is six months and on termination they would be entitled to an additional six months' salary, pension and car allowance entitlement. These entitlements may be mitigated and/or spread over the period of notice.

Mark Gregory and Nigel Wilson have termination periods of 12 months. However, they have no entitlement to any additional contractual payment on termination of employment. Any payment in lieu of notice will consist solely of base salary and the cost of providing benefits for the outstanding notice period and will be subject to deductions for income tax and national insurance as appropriate. These entitlements may be mitigated and/or spread over the period of notice.

Copies of the executive directors' service contracts are available for inspection at the Company's registered office.

EXTERNAL APPOINTMENTS

The Company considers that certain external appointments can help to broaden the experience and capability of the executive directors. Any such appointments are subject to annual agreement by the Remuneration Committee and must not be with competing companies. Subject to the Committee's agreement, any fees may be retained by the individual. Tim Breedon is an unpaid Board member of the ABI. While a director, Andrew Palmer received fees of £50,000 as a non-executive director of SEGRO plc and was also Chairman of their Audit Committee, Chairman of the ABI Financial Regulation and Taxation Committee and Chairman of the ABI Financial Reporting Committee. Nigel Wilson is a non-executive director of Halfords Group Plc and receives a fee of £66,000 p.a. Mark Gregory is an unpaid Director of Westdown Park Management Company Ltd.

The Directors' Report on Remuneration was approved by the directors on 22 March 2010.

Sir David Walker
Chairman of the Remuneration Committee

INDEPENDENT VERIFICATION REVIEW

Hewitt New Bridge Street (HNBS) act as advisers to the Remuneration Committee. In addition, they were asked to verify that the 2009 remuneration practice for executive directors followed the Remuneration Policy put to the 2009 AGM. In conducting this work, HNBS reviewed the elements of executive director remuneration during 2009, as detailed in the policy statements of the Directors' Report on Remuneration 2008 (DRR 2008). They confirmed that they were satisfied that the remuneration practice during 2009 had been in line with the stated policy set out in the DRR 2008.

CSR COMMITTEE REPORT.

THE COMMITTEE'S ROLE IS TO DEVELOP THE GROUP'S CSR STRATEGY AND POLICIES, TO MONITOR PROGRESS IN IMPLEMENTING THAT STRATEGY AND TO ENGAGE WITH KEY STAKEHOLDERS ON CSR MATTERS. THE COMMITTEE REPORTS TO THE BOARD.

Corporate social responsibility (CSR) is a key priority for the Company. As one of the UK's largest life and pensions providers, the Company is committed to aligning its corporate purpose with the needs of its customers and the wider community. The Company is also uniquely positioned as one of the UK's largest investors to influence the companies in which it invests on CSR issues. The CSR Committee is chaired by the Group Chief Executive, and is supported by the committees listed on page 41.

2009 FOCUS

GUIDING PRINCIPLES	THE COMMITTEE'S FOCUS IN 2009	GOVERNED BY
OUR CUSTOMERS	• Providing good value, fit for purpose products which meet or exceed our customers' expectations. • When the customer circumstances dictate, provide a pension the day a customer retires after a lifetime of saving, pay out valid claims when a customer gets ill or when an unexpected event leaves them unable to work, pay valid claims quickly when unexpected events affect our customers' homes and livelihoods, provide investments which pay out what was planned for at outset.	Ethics Committee
OUR PEOPLE	• Ensure our employees understand and adopt correct ethical behaviour. • Work in close partnership with our recognised trade union, Unite, on key decisions affecting our employees. • Adopt policies and practices which encourage an appropriate work/life balance and provide a flexible, supportive, healthy and safe working environment.	Equality and Diversity Committee Group Health and Safety Committee
OUR ENVIRONMENT	• Reduce, rather than offset, the impact on the environment arising from our business activities. • Integrate environmental legislation into our business.	Group Environment Committee
OUR COMMUNITIES	• Support the community as a whole particularly on grass roots issues where we can make a difference in those communities where our main offices are based in the UK and overseas. • Social investment through partnering with third sector organisations to campaign for the issues that matter to our markets and businesses.	Group Charity Committee
OUR SUPPLIERS	• Compliance by our key suppliers with our Sustainable Procurement Policy. • Support those suppliers who do not comply with our CSR standards in making improvements.	Group Environment Committee
SOCIALLY RESPONSIBLE INVESTMENT	• Promote responsible ESG business practices in the companies in which we invest. • Promote sustainable business practices in our commercial property portfolio to create better investor returns and relationships with occupiers.	Group CSR Committee

SUPPORTING THE GENERATION OF SHAREHOLDER VALUE

RISK MANAGEMENT.

THE EFFECTIVE MANAGEMENT OF RISK IS ESSENTIAL TO DELIVERY OF THE GROUP'S STRATEGY AND THE GENERATION OF SHAREHOLDER VALUE

RISK MANAGEMENT AT A GLANCE

Identification
We understand the risks inherent in our business and we continuously review them as the business develops and markets change. Identified risks are recorded and responsibility is allocated to an owner to assess and manage the risk.

Analysis
Risks are assessed and analysed so that there is a full understanding of the nature of the risk, its probability, and its likely impact on the business area and the Group's overall strategy. We stress test our risks to understand their impact on the business in the event of extreme market conditions.

Mitigation
Risk mitigation plans are developed and implemented to manage or respond to risks so that we continue to operate within our chosen risk appetite.

These plans are kept under regular review to ensure that they remain robust and appropriate as the nature, probability or impact of risks may change over time.

Reporting
Regular reporting of risks and the mitigation strategies occurs through the individual business level risk committees to the executive level risk committees, and ultimately to the Board committees.

RISK MANAGEMENT

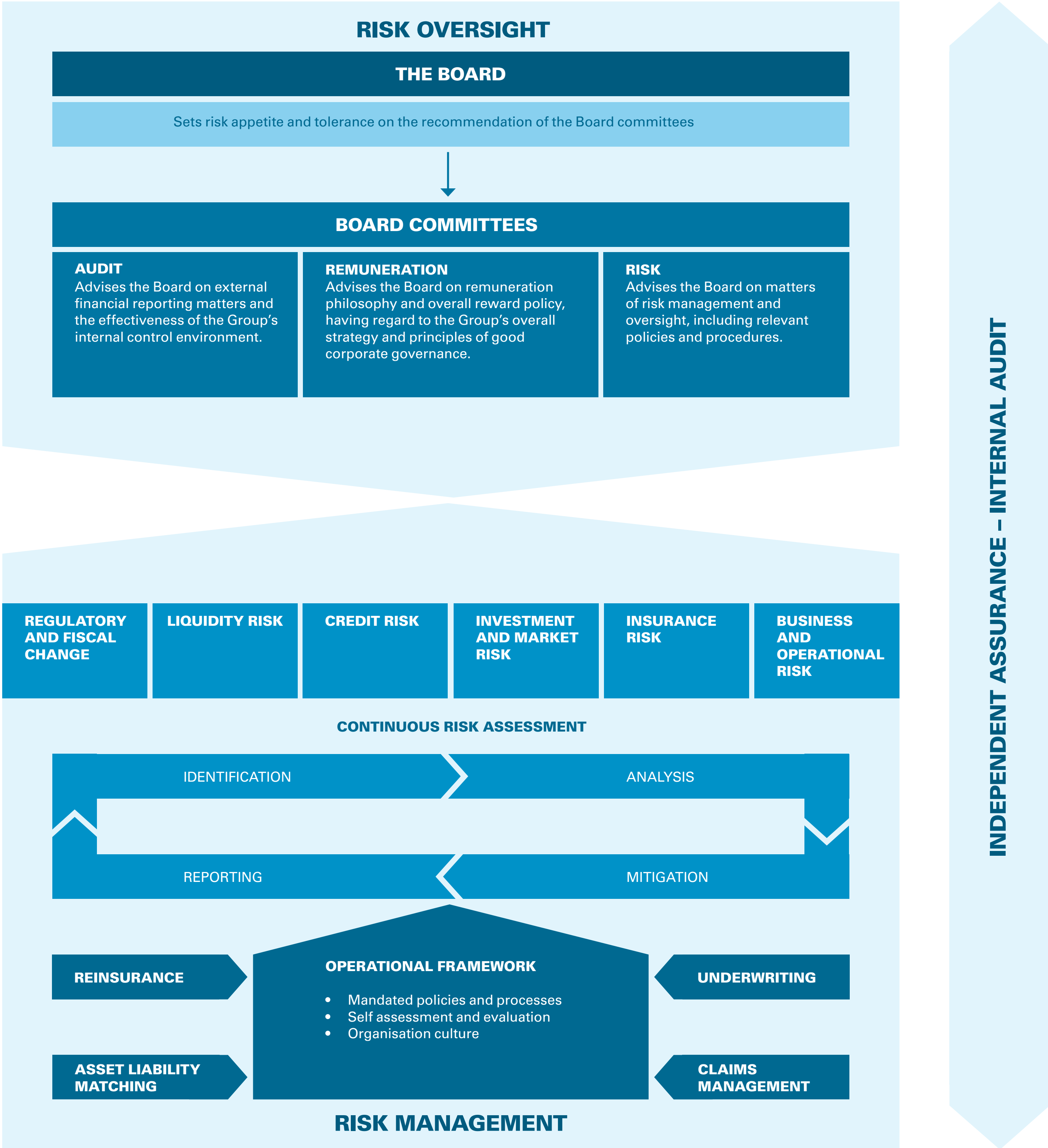
The Group's approach to risk management is aimed at the early identification of key risks to the Group's businesses and the Group's overall strategy, followed by a full understanding of the nature of those risks, the probability of them occurring and their likely impact or effect if they did occur. Robust mitigation action plans are developed and implemented with the aim of reducing or removing the likelihood of the risk occurring or managing the impact if the risk cannot be avoided.

The management of risk, particularly a full understanding of the risks inherent in the business areas, markets and geographies in which the Group operates, is linked to the development and implementation of the Group's strategy.

The Board has overall responsibility for setting the risk appetite and tolerance for the Group. The Board is assisted by advice and recommendations received from the Board committees.

Subsequent to the year end, the Company carried out a review of its corporate governance arrangements with particular regard to recent commentary on the Board's role in risk governance. The Board agreed that it would be in the best interests of shareholders and the Company for the Group risk committee to be chaired by a non-executive director. Due to Board changes expected to take place in the first half of 2010 as a result of director retirements, the Group risk committee will initially be chaired by the Chairman and membership will comprise the Chairman and up to four other non-executive directors. The risk committee will operate under formal terms of reference approved by the Board, copies of which will be available on the Company's website following approval. It is expected that the non-executive chaired risk committee will meet in early 2010. Risk management and oversight will be delegated by the Board to the risk committee.

RISK MANAGEMENT GOVERNANCE



RISK MANAGEMENT.

	OVERVIEW	MITIGATION
REGULATION AND LEGISLATION	**Changes in regulation or legislation may have a detrimental effect on our strategy or profitability.** Regulation defines the overall framework for the design, marketing and distribution of our products; the acceptance and administration of business; and the prudential capital that we hold. Current areas of significant regulatory change include Solvency II and the Retail Distribution Review. In addition to these known areas of change, there remains potential for new regulation in response to recent market events as well as possible changes in the regulatory landscape following the 2010 general election. Legislation and government fiscal policy can also influence our product design, the retention of existing business and our required reserves for future liabilities. Areas of new insurance law include that being developed by the Law Commission. Potential changes to personal and corporate taxation also present uncertainty with respect to the profitability and continued attractiveness of our products.	The Group bases its business strategy upon prevailing regulation and legislation, and known/anticipated change. To mitigate the risk of legislation or regulation adversely impacting the sectors in which we operate, the Group seeks to engage with regulatory and legislative authorities to assist in the evaluation of change and develop outcomes that meet the needs of all stakeholders.
FINANCIAL MARKET AND ECONOMIC CONDITIONS	**Investment market performance or conditions in the broader economy may adversely impact our results.** The Group 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. The income derived by our investment management activities can also be impacted by significant falls in investment asset values, whilst broader economic conditions can influence the purchase by customers of retail financial services products and how long they are retained. Whilst 2009 has seen a recovery of major markets from their position in 2008, broader economic conditions remain less certain, with possible consequences to investment values. Investment markets may also suffer considerable disruption should a significant macro-economic event, for example a sovereign debt crisis, occur within a developed world economy.	The Group seeks to reduce the impact of these risks through ensuring the profile of cash flows of our assets and liabilities are appropriately matched. Matching techniques include using financial instruments as part of formal risk management strategies to reduce volatility in returns from investment assets, the effect of changes in interest rates and inflation, and the broader effects of adverse market conditions. We seek to reduce the impact of market and economic conditions upon our investment businesses through the utilisation of a low cost scalable business model and by maintaining a diversified portfolio of products.
COUNTERPARTY AND THIRD PARTY RISKS	**In dealing with issuers of debt and other types of counterparty, the Group is exposed to the risk of default.** As part of our strategies to appropriately match long term assets and liabilities, exposures can arise to the issuers of corporate debt and other financial instruments. As part of our day to day business we also have exposures to banking, money market and reinsurance counterparties, as well as the providers of investment settlement and custody services. Third party risks also arise through reliance upon external suppliers for certain administration and IT development services.	Recent market events have demonstrated the importance of sound counterparty management. In this context the Group seeks to limit the potential exposure to loss from counterparty and third party failure through setting robust selection criteria and exposure limits covering factors such as counterparty financial strength, sectors and geography. Exposures against limits are actively monitored, with trigger levels being set and management action being taken to pre-empt loss from default events.
UK FINANCIAL SERVICES SECTOR CONTAGION RISKS	**As a UK based Group, earnings are influenced by the perception of the UK financial services sector as a whole.** Factors such as investment market performance, actions by regulators against organisations operating in the sector and shock events, including matters such as significant market failures, can impact the confidence of retail investors in the sector as a whole and their purchase or retention of financial service products.	2009 has seen a general downturn in business volumes across the sectors in which the Group operates. We continue to seek to differentiate our business model from that of our competitors. This includes a diversified portfolio of risk, savings and investment management businesses in the UK, further details of which are set out on pages 2 and 3, and a broad distribution mix. In addition, as set out on page 32, we are focused on developing our international businesses, with joint ventures in India and the Gulf being established in 2009, complementing our existing portfolio of overseas activities, as well as our investment management business winning its first mandates in the US.
MORTALITY CATASTROPHE AND OTHER ASSUMPTION UNCERTAINTIES	**Revisions to assumptions may require adjustments to reserves.** 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. The writing of household insurance business also requires assumptions to be set for factors such as extreme weather and other catastrophic events. Whilst a prudent approach is taken to evaluating required reserves for these risks, extreme events, such as a rapid advance in medical science leading to significantly enhanced annuitant longevity or an event causing widespread mortality/morbidity, coupled with a reinsurer default may require assumptions to be recalibrated impacting profitability and capital.	The Group uses its pricing capabilities and the significant experience data it has accumulated to assess and charge an appropriate premium for known risk factors, and to ensure that reserves remain appropriate on an ongoing basis. The evaluation of reserves is supported by stress and scenario testing which seeks to validate the appropriateness of key assumptions to combinations of extreme events, including economic conditions, investment performance and product specific matters.
INDUSTRY CHANGE	**The Group may not maximise opportunities from structural changes within the financial services sector.** The financial services sector is going through a period of change and consolidation. This presents a range of challenges as well as opportunities to providers of sufficient scale such as Legal & General. Recent examples have included the merger of banks and building societies resulting in a change to the distribution landscape. The emergence of niche product providers with new business models continues to drive innovation within a number of the sectors in which the Group operates.	We seek to ensure it has market leading expertise in the core fields in which it operates, and actively focuses on retaining the best personnel with the knowledge to design and support our products, and manage their evolution as market and consumer expectations change. In response to consolidation by banks and building societies, we have established a number of new distribution partnerships. Within our annuities business, a disciplined and selective approach to pension buyout business was maintained throughout 2009, and whilst we continue to lead in the traditional smaller schemes bulk purchase market, increased product and pricing sophistication and increased distribution opportunities helped individual annuities sales to grow. Our savings business has seen a transformation of the mix of products sold towards more modern, less capital intensive offerings.

OTHER STATUTORY AND REGULATORY INFORMATION.

ARTICLES OF ASSOCIATION

The Company's Articles of Association may only be amended by a special resolution at a general meeting of shareholders. At the Company's AGM to be held on 26 May 2010, a resolution will be put to shareholders proposing amendments to the existing Articles of Association to incorporate changes introduced by the Companies Act 2006.

CONFLICTS OF INTEREST

During 2008, provisions in the Companies Act 2006 concerning a director's duties in dealing with actual or potential conflicts of interest became effective. In accordance with these provisions, shareholders approved changes to the Company's Articles of Association at the 2008 AGM to allow directors to authorise such conflicts.

The Board has adopted a policy and procedure for the disclosure and authorisation (if appropriate) of conflicts of interest, and these have been followed during 2009.

POWERS OF DIRECTORS

The directors may exercise all powers of the Company subject to applicable legislation and regulation and the Company's Articles of Association.

SHARE CAPITAL

As at 31 December 2009, the Company's issued share capital comprised 5,862,216,780 Ordinary shares each with a nominal value of 2.5p. Details of the Ordinary share capital can be found in Note 28 to the Financial Statements on page 128.

At the 2009 AGM, the Company was granted authority by shareholders to purchase up to 586,167,936 Ordinary shares, being 10% of the issued share capital of the Company as at 24 March 2009. In the year to 31 December 2009, no shares were purchased by the Company. This authority will expire at this year's AGM. As such, a special resolution is proposed in the Notice of AGM seeking shareholder approval to renew this authority.

At the 2009 AGM, the directors were given the power to allot shares up to an amount of £48,358,855, being 33% of the issued share capital of the Company as at 24 March 2009. This authority will also expire at this year's AGM. As such, a special resolution is proposed in the Notice of AGM seeking shareholder approval to renew this authority.

A further resolution is proposed, as set out in the Notice of AGM, that will, if approved by shareholders, authorise the directors to issue shares up to the equivalent of 5% of the Company's issued share capital as at 22 March 2010 for cash without offering the shares first to existing shareholders in proportion to their holdings.

Detailed explanatory notes to these resolutions are set out in the Notice of AGM.

Other than the above, the directors have no current intention of issuing further share capital and no issue will be made which would effectively alter control of the Company without prior approval of shareholders in a general meeting.

SUBSTANTIAL SHARE INTERESTS

As at 22 March 2010, the Company had been advised of the following significant direct and indirect interests in the issued share capital of the Company:

	Number of Ordinary shares of 2.5p with direct voting rights	Number of Ordinary shares of 2.5p with indirect voting rights	Total interest in issued share capital
AXA S.A and its group of companies	3.04%	1.27%	4.31%
Swiss Reinsurance Company Ltd	3.93%	0%	3.93%
Aviva Plc & its subsidiaries	2.86%	0%	2.86%
Schroders Plc	0%	5.04%	5.04%
Blackrock Inc	0%	5.21%	5.21%

DIVIDEND

The Company may, by ordinary resolution in a general meeting, declare dividends in accordance with the respective rights of the members, but no dividend can exceed the amount recommended by the Board. An interim dividend of 1.11p per share was paid on 1 October 2009. The directors propose a final dividend of 2.73p per Ordinary share. Subject to shareholder approval, the final dividend will be paid on 1 June 2010 to shareholders on the share register on 16 April 2010.

RELATED PARTY TRANSACTIONS

Details of related party transactions are set out in Note 40 to the Financial Statements on page 147.

OTHER STATUTORY AND REGULATORY INFORMATION.

RIGHTS AND OBLIGATIONS ATTACHING TO SHARES

The rights and obligations relating to the Company's Ordinary shares are set out in the Articles of Association. A copy of the Articles of Association can be requested from the Company Secretary at the Company's registered office.

Holders of Ordinary shares are entitled to attend, speak and vote at general meetings. In a vote on a show of hands, every member present in person or every proxy present, who has been duly appointed by a member, will have one vote and on a poll every member present in person or by proxy shall have one vote for every Ordinary share held. These rights are subject to any special terms as to voting upon which any shares may be issued or may at the relevant time be held and to any other provisions of the Company's Articles of Association. Under the Companies Act 2006 and the Articles of Association, directors have the power to suspend voting rights and, in certain circumstances, the right to receive dividends in respect of shares where the holder of those shares fails to comply with a notice issued under section 793 of the Companies Act 2006.

The Board can decline to register a transfer of any share which is not a fully paid share. In addition, registration of a transfer of an uncertificated share may be refused in the circumstances set out in the uncertificated securities rules and where the number of joint holders exceeds four. The Board may also refuse to register the transfer of a certificated share unless:
(a) the instrument of transfer is duly stamped and is left at the Company's registered office or such other place as the Board may from time to time determine accompanied by the certificate for the share to which it relates and such evidence as the Board may reasonably require to show the right of the transferor to make the transfer;
(b) the instrument of transfer is in respect of only one class of share; and
(c) the number of joint holders does not exceed four.

Subject to the provisions of the Companies Act, all or any of the rights attaching to an existing class of shares may be varied from time to time either with the consent in writing of the holders of not less than three-fourths in nominal value of the issued shares of that class (excluding any treasury shares) or with the sanction of a special resolution passed at a separate general meeting of the holders of those shares.

Shares acquired through the employee share schemes rank equally with all other Ordinary shares in issue. Barclays Private Bank & Trust (Isle of Man) Limited, as trustee of the Legal & General Employees' Share Ownership Trust, holds 0.47% of the issued share capital of the Company as at 22 March 2010 in trust for the benefit of the executive directors, senior executives and managers of the Group. This includes shares held as nominee on behalf of Legal & General Share Scheme Trustees Limited, as trustee of the Legal & General Employee Share Trust, which is in the process of being wound up. The voting rights in relation to these shares are exercised by the trustee. The trustee may vote or abstain from voting, or accept or reject any offer relating to shares, in any way it sees fit, without incurring any liability and without being required to give reasons for its decision.

Under the rules of the Legal & General Group Employee Share Plan (Plan), eligible employees are entitled to acquire shares in the Company. Plan shares are held in trust for participants by Equiniti Share Plan Trustees Limited, which holds 0.43% of the issued share capital of the Company as at 22 March 2010. Voting rights are exercised by the trustees on receipt of the participants' instructions. If a participant does not submit an instruction to the trustees, no vote is registered. In addition, the trustees do not vote on any unawarded shares held under the Plan as surplus assets.

The Company is not aware of any agreements between shareholders which may result in restrictions on the transfer of securities and/or voting rights.

CHANGE OF CONTROL

There are no agreements between the Company and its directors or employees for compensation providing for loss of office or employment (whether through resignation, purported redundancy or otherwise) in the event of a takeover bid, except for those relating to normal notice periods. The rules of the Company's share plans contain provisions under which options and awards to participants, including executive directors, may vest on a takeover or change of control of the Company or transfer of undertakings.

The Company has a committed circa £1bn bank syndicated credit facility which is terminable if revised terms cannot be agreed with the syndicate of banks in a 30 day period following a change of control.
As at 22 March 2010, the Company has no borrowings under this facility.

There are no change of control conditions in the terms of any of the Company's outstanding debt securities. The terms of the Company's agreements with its banking counterparties, under which derivative transactions are undertaken, include the provision for termination of transactions upon takeover/merger if the resulting merged entity has a credit rating materially weaker than the Company. There are no other committed banking arrangements either drawn or undrawn that incorporate any change of control conditions.

USE OF FINANCIAL INSTRUMENTS

Information on the Group's risk management process is set out on pages 72 to 74. More details on risk management and the financial instruments used are set out in Note 48 of the Financial Statements on page 159.

INDEMNITIES

The Company has agreed to indemnify, to the extent permitted by law, each of the directors against any liability incurred by a director in respect of acts or omissions arising in the course of their office. Qualifying pension scheme indemnities (as defined in section 235 of the Companies Act 2006) have been granted, to the extent permitted by law, to certain trustees of the Company's pension schemes. The indemnities were in force throughout 2009 and remain so. Copies of the deeds of indemnity are available for inspection at the Company's registered office and will also be available at the AGM.

CHARITABLE DONATIONS

During the period, the Group made charitable donations amounting to £2.8 million. Details of the Company's charitable activities are set out on pages 40 to 41.

POLITICAL DONATIONS

No political donations were made during 2009.

FORWARD-LOOKING STATEMENTS

The Directors' Report is prepared for the members of the Company and should not be relied upon by any other party or for any other purpose. Where the Directors' Report includes forward-looking statements, these are made by the directors in good faith based on the information available to them at the time of their approval of this report. Such statements should be treated with caution due to the inherent uncertainties underlying such forward-looking statements.

INSURANCE

The Company has arranged appropriate Directors' and Officers' Liability insurance for directors. This is reviewed annually.

INDEPENDENT AUDITORS

The Company's auditors have expressed their willingness to continue in office and the Audit Committee has recommended their reappointment to the Board. A resolution to re-appoint PricewaterhouseCoopers LLP as auditors to the Company and to authorise the directors to determine their remuneration is proposed for the forthcoming AGM.

DIRECTORS' INTERESTS

The Directors' Report on Remuneration on pages 55 to 70 provides details of the interests of each director, including details of current incentive schemes and long term incentive schemes, the interests of directors in the share capital of the Company and details of their share options, as at 31 December 2009 and the changes in those interests that have occurred between 1 January 2010 and 22 March 2010 (being the last practicable date prior to publication of the Notice of the AGM).

DISCLOSURE OF INFORMATION TO AUDITORS

Each of the directors who held office at the date of approval of this Directors' Report confirms that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware and each of the directors have taken all reasonable steps they ought to have taken as directors to ascertain any relevant audit information and to ensure that the Company's auditors are aware of such information. This confirmation is given in accordance with section 418(2) of the Companies Act 2006.

GOING CONCERN STATEMENT

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Directors' Report on pages 1 to 35, 38 to 39 and 42 to 78. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Group Results on pages 14 to 19. Principal risks are detailed on page 74. In addition, the financial statements include, amongst other things, notes on the Group's objectives, policies and processes for managing its capital (page 152), its financial risk management objectives (page 159), details of its financial instruments and hedging activities (page 115) and its exposures to credit risk (page 166) and liquidity risk (page 171).

The 2010 economic climate remains uncertain. However, based on the available information on the future, the directors consider that the Group has the plans and resources to manage its business risks successfully, as it has a diverse range of businesses and remains financially strong.

OTHER STATUTORY AND REGULATORY INFORMATION.

The directors have a reasonable expectation that the Company and the Group have adequate resources to continue operational existence for the foreseeable future. For that reason, they continue to adopt the going concern basis in preparing the accounts.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Directors' Report, including the Directors' Remuneration Report, and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Group Financial Statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and the parent company financial statements in accordance with UK Accounting Standards (UK Generally Accepted Accounting Principles) and applicable law. The Group and parent company Financial Statements are required by law to give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period.

In preparing those Financial Statements, the directors are required to:
- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state that the Group Financial Statements comply with IFRS as adopted by the European Union and IFRS issued by the IASB, and with regard to the parent company financial statements, that applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Financial Statements; and
- prepare the Group and parent company financial statements on the going concern basis unless it is inappropriate to presume that the Group and parent company will continue in business, in which case there should be supporting assumptions or qualifications as necessary.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and parent company and to enable them to ensure that the Directors' Remuneration Report and the Financial Statements comply with the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Group and for taking such reasonable steps to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the information included on the Group's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Responsibility statement

Each of the directors listed on pages 42 and 43 confirms that to the best of their knowledge:

(a) the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the Group as a whole; and

(b) the directors' report includes a fair review of the development and performance of the business and the position of the Company and Group as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

G J Timms
Company Secretary
22 March 2010

GROUP CONSOLIDATED FINANCIAL STATEMENTS

SUPPLEMENTARY FINANCIAL STATEMENTS – EUROPEAN EMBEDDED VALUE BASIS

COMPANY FINANCIAL STATEMENTS

INDEPENDENT AUDITORS' REPORT

To the Members of Legal & General Group Plc

We have audited the group financial statements of Legal & General Group Plc for the year ended 31 December 2009 which comprise the Consolidated Income Statement, Consolidated Statement of Comprehensive Income, Consolidated Balance Sheet, Consolidated Statement of Changes in Equity, Consolidated Cash Flow Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the group financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion the group financial statements:

- give a true and fair view of the state of the group's affairs as at 31 December 2009 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

Separate opinion in relation to IFRSs as issued by the IASB

As explained in note 1 to the group financial statements, the group in addition to complying with its legal obligation to apply IFRSs as adopted by the European Union, has also applied IFRSs as issued by the International Accounting Standards Board (IASB).

In our opinion the group financial statements comply with IFRSs as issued by the IASB.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, the information given in the Directors' Report for the financial year for which the group financial statements are prepared is consistent with the group financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

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

- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement on going concern included in the corporate governance statement; and
- the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

Other matter

We have reported separately on the parent company financial statements of Legal & General Group Plc for the year ended 31 December 2009 and on the information in the Directors' Remuneration Report that is described as having been audited.

Richard Keers

Richard Keers (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
22 March 2010

Notes:

a) The financial statements are published on the website of Legal & General Group Plc, www.legalandgeneralgroup.com. The maintenance and integrity of the Legal & General Group Plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2009	Notes	2009 £m	2008 £m
Revenue			
Gross written premiums	1F,G,H/3(iv)	**5,275**	5,895
Outward reinsurance premiums	1J	**(574)**	(569)
Net change in provision for unearned premiums	1H	**11**	1
Net premiums earned		**4,712**	5,327
Fees from fund management and investment contracts	1G	**786**	740
Investment return	1Z/5	**38,201**	(37,749)
Operational income	1AA	**91**	38
Total revenue	3(ii)	**43,790**	(31,644)
Expenses			
Claims and change in insurance liabilities		**7,614**	3,287
Reinsurance recoveries		**(520)**	(587)
Net claims and change in insurance liabilities	1F,H/6	**7,094**	2,700
Change in provisions for investment contract liabilities	1G	**33,186**	(33,313)
Acquisition costs	1F,G,H	**780**	776
Finance costs	1Q	**179**	379
Other expenses	1AA	**882**	773
Transfers to/(from) unallocated divisible surplus	1F	**430**	(806)
Total expenses		**42,551**	(29,491)
Profit/(loss) before income tax	9	**1,239**	(2,153)
Income tax (expense)/credit attributable to policyholder returns	11	**(165)**	662
Profit/(loss) from continuing operations before income tax attributable to equity holders of the Company		**1,074**	(1,491)
Total income tax (expense)/credit	1R/11	**(395)**	1,023
Income tax expense/(credit) attributable to policyholder returns	11	**165**	(662)
Income tax (expense)/credit attributable to equity holders	11	**(230)**	361
Profit/(loss) for the year		**844**	(1,130)
Attributable to:			
Minority interests	29	**(19)**	(63)
Equity holders of the Company		**863**	(1,067)
Dividend distributions to equity holders of the Company during the year	1U/12	**185**	367
Dividend distributions to equity holders of the Company proposed after the year end	1U/12	**160**	120
		p	p
Earnings per share			
Based on profit/(loss) attributable to equity holders of the Company	1AB/13	**14.82**	(17.88)
Diluted earnings per share			
Based on profit/(loss) attributable to equity holders of the Company	1AB/13	**14.73**	(17.88)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2009	Notes	2009 £m	2008 £m
Profit/(loss) for the year		**844**	(1,130)
Other comprehensive income after tax			
Exchange differences on translation of overseas operations		**(63)**	139
Actuarial (losses)/gains on defined benefit pension schemes	36	**(154)**	18
Actuarial losses/(gains) on defined benefit pension schemes transferred to unallocated divisible surplus	32	**62**	(8)
Net change in financial investments designated as available-for-sale		**66**	(56)
Total comprehensive income/(expense) for the year		**755**	(1,037)
Total comprehensive income/(expense) attributable to:			
Minority interests	29	**(19)**	(63)
Equity holders of the Company		**774**	(974)

CONSOLIDATED BALANCE SHEET

As at 31 December 2009

	Notes	2009 £m	2008 £m
Assets			
Investment in associates	1D/44	**45**	14
Plant and equipment	1M/17	**61**	75
Investment property	1L/18	**3,839**	3,969
Financial investments	1L/19	**276,016**	234,514
Reinsurers' share of contract liabilities	1J/21	**2,093**	1,997
Purchased interest in long term businesses and other intangible assets	1K/22	**146**	227
Deferred acquisition costs	1F,G,H/23	**1,957**	2,112
Deferred tax asset	1R/24	**796**	988
Income tax recoverable	1R/25	**1**	8
Other assets	26	**1,440**	2,135
Cash and cash equivalents	1O/27	**10,650**	10,688
Total assets	3(iii)	**297,044**	256,727
Equity			
Share capital	1U/28	**147**	147
Share premium	28	**936**	936
Employee scheme shares	1U/28	**(38)**	(46)
Capital redemption and other reserves		**41**	(42)
Retained earnings		**3,110**	2,593
Shareholders' equity		**4,196**	3,588
Minority interests	29	**2**	144
Total equity	3(iii)	**4,198**	3,732
Liabilities			
Subordinated borrowings	1Q/35	**1,870**	1,657
Participating insurance contracts	1F/30	**9,404**	9,384
Participating investment contracts	1G/31	**7,139**	6,992
Unallocated divisible surplus	1F/32	**1,284**	913
Value of in-force non-participating contracts	1F/33	**(367)**	(171)
Participating contract liabilities		**17,460**	17,118
Non-participating insurance contracts	1F,H/30	**28,583**	25,841
Non-participating investment contracts	1G/31	**234,502**	196,698
Non-participating contract liabilities		**263,085**	222,539
Senior borrowings	1Q/35	**1,407**	2,314
Provisions	1T,W/36	**757**	555
Deferred tax liabilities	1R/24	**303**	259
Income tax liabilities	1R/25	**140**	5
Payables and other financial liabilities	37	**5,003**	6,799
Other liabilities	38	**892**	997
Net asset value attributable to unit holders	39	**1,929**	752
Total liabilities	3(iii)	**292,846**	252,995
Total equity and liabilities		**297,044**	256,727

The notes on pages 87 to 183 form an integral part of these financial statements.

The financial statements on pages 81 to 183 and the supplementary financial statements on pages 184 to 204 were approved by the directors on 22 March 2010 and were signed on their behalf by:

John Stewart
Chairman

Tim Breedon
Group Chief Executive

Nigel Wilson
Group Chief Financial Officer

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2009	Share capital £m	Share premium £m	Employee scheme shares £m	Capital redemption and other reserves £m	Retained earnings £m	Total £m	Minority interests £m	Total equity £m
As at 1 January	**147**	**936**	**(46)**	**(42)**	**2,593**	**3,588**	**144**	**3,732**
Profit/(loss) for the year	–	–	–	–	863	863	(19)	844
Exchange differences on translation of overseas operations	–	–	–	(63)	–	(63)	–	(63)
Actuarial (losses) on defined benefit pension schemes	–	–	–	–	(154)	(154)	–	(154)
Actuarial losses on defined benefit pension schemes transferred to unallocated divisible surplus	–	–	–	–	62	62	–	62
Net change in financial investments designated as available-for-sale	–	–	–	66	–	66	–	66
Total comprehensive income/(expense) for the year	–	–	–	3	771	774	(19)	755
Options exercised under share option schemes:								
– Executive share option schemes	–	–	–	–	–	–	–	–
– Savings related share option scheme	–	–	–	–	–	–	–	–
Shares purchased	–	–	(2)	–	–	(2)	–	(2)
Shares vested	–	–	10	(18)	–	(8)	–	(8)
Employee share schemes:								
– Value of employee services	–	–	–	21	–	21	–	21
Transfer to retained earnings	–	–	–	–	8	8	–	8
Dividends	–	–	–	–	(185)	(185)	–	(185)
Movement in third party interests	–	–	–	–	–	–	(123)	(123)
Currency translation differences	–	–	–	77	(77)	–	–	–
As at 31 December	**147**	**936**	**(38)**	**41**	**3,110**	**4,196**	**2**	**4,198**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (CONTINUED)

For the year ended 31 December 2008	Share capital £m	Share premium £m	Employee scheme shares £m	Capital redemption and other reserves £m	Retained earnings £m	Total £m	Minority interests £m	Total equity £m
As at 1 January	157	927	(42)	59	4,345	5,446	178	5,624
Loss for the year	–	–	–	–	(1,067)	(1,067)	(63)	(1,130)
Exchange differences on translation of overseas operations	–	–	–	139	–	139	–	139
Actuarial gains on defined benefit pension schemes	–	–	–	–	18	18	–	18
Actuarial (gains) on defined benefit pension schemes transferred to unallocated divisible surplus	–	–	–	–	(8)	(8)	–	(8)
Net change in financial investments designated as available-for-sale	–	–	–	(56)	–	(56)	–	(56)
Total comprehensive income/(expense) for the year	–	–	–	83	(1,057)	(974)	(63)	(1,037)
Share buyback[1]	(11)	–	–	11	(523)	(523)	–	(523)
Options exercised under share option schemes:								
– Executive share option schemes	–	1	–	–	–	1	–	1
– Savings related share option scheme	1	8	–	–	–	9	–	9
Shares purchased	–	–	(10)	–	–	(10)	–	(10)
Shares vested	–	–	6	(17)	–	(11)	–	(11)
Employee share schemes:								
– Value of employee services	–	–	–	14	–	14	–	14
Transfer to retained earnings	–	–	–	–	3	3	–	3
Dividends	–	–	–	–	(367)	(367)	–	(367)
Movement in third party interests	–	–	–	–	–	–	29	29
Currency translation differences	–	–	–	(192)	192	–	–	–
As at 31 December	147	936	(46)	(42)	2,593	3,588	144	3,732

1. During 2008, shares were repurchased and cancelled under a share buyback programme at a cost of £523m including expenses.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2009

	Notes	2009 £m	2008 £m
Cash flows from operating activities			
Profit/(loss) for the year		**844**	(1,130)
Adjustments for non-cash movements in net profit/(loss) for the year			
Realised and unrealised (gains)/losses on financial investments and investment properties		**(29,180)**	48,376
Investment income		**(8,813)**	(10,086)
Interest expense		**179**	379
Income tax expense/(credit)		**395**	(1,023)
Other adjustments		**104**	77
Net (increase)/decrease in operational assets			
Investments designated as held for trading or fair value through profit or loss		**(5,822)**	2,161
Investments designated as available-for-sale		**(61)**	(93)
Other assets		**477**	(1,702)
Net increase/(decrease) in operational liabilities			
Insurance contracts		**3,143**	(1,479)
Transfer to/(from) unallocated divisible surplus		**368**	(798)
Investment contracts		**29,337**	(43,485)
Value of in-force non-participating contracts		**(196)**	105
Other liabilities		**1,121**	541
Cash used in operations		**(8,104)**	(8,157)
Interest paid		**(160)**	(377)
Interest received		**5,074**	5,214
Income tax received/(paid)		**52**	(208)
Dividends received		**3,896**	4,614
Net cash flows from operating activities		**758**	1,086
Cash flows from investing activities			
Net acquisition of plant and equipment		**(7)**	(14)
Acquisitions (net of cash acquired)	16	**–**	1,004
Capital injection into overseas joint ventures	44	**(36)**	–
Net cash flows from investing activities		**(43)**	990
Cash flows from financing activities			
Dividend distributions to ordinary equity holders of the Company during the year		**(185)**	(367)
Proceeds from issue of ordinary share capital		**–**	10
Purchase of employee scheme shares		**(2)**	(9)
Purchase of shares under share buyback programme	28	**–**	(523)
Proceeds from borrowings		**2,124**	3,568
Repayment of borrowings		**(2,629)**	(2,960)
Net cash flows from financing activities		**(692)**	(281)
Net increase in cash and cash equivalents		**23**	1,795
Exchange (losses)/gains on cash and cash equivalents		**(61)**	156
Cash and cash equivalents at 1 January		**10,688**	8,737
Cash and cash equivalents at 31 December	27	**10,650**	10,688

The Group's consolidated cash flow statement includes all cash and cash equivalent flows, including those relating to the UK long term fund policyholders.

NOTES TO THE FINANCIAL STATEMENTS

1 ACCOUNTING POLICIES

A Basis of preparation

The Group financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) as adopted by the European Union, and with those parts of the UK Companies Act 2006 applicable to companies reporting under IFRS. The Group's financial statements also comply with IFRS as issued by the IASB.

The Group presents its balance sheet broadly in order of liquidity. This is considered to be more relevant than a before or after 12 months presentation, given the long term nature of the Group'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 balance sheet date, disclosure of the split is made by way of a note.

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

The Group has adopted the revised presentation under IAS 1 (revised), 'Presentation of financial statements' and accordingly included a separate consolidated statement of comprehensive income. The revision prohibits the presentation of items of income and expenses in the consolidated statement of changes in equity and requires changes in equity attributable to shareholders to be presented separately to those that are not attributable to shareholders. The changes are purely presentational and the comparatives have been restated to reflect the new presentation.

In 2009, the Group adopted amendments to IFRS 2, 'Share-based payments' and IAS 23, 'Borrowing costs' with no impact to the Group's results. Amendments to IFRS 7, 'Financial instruments: disclosures' have also been adopted and the additional disclosures required by the amendment have been provided in Notes 19 and 48.

B Use of estimates

The preparation of the financial statements includes the use of estimates and assumptions which affect items reported in the consolidated balance sheet and income statement and the disclosure of contingent assets and liabilities 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 investment property (Notes 1L and 18)

Investment property in the UK is valued bi-annually by external chartered surveyors at open market values in accordance with the 'Appraisal and Valuation Manual' of The Royal Institution of Chartered Surveyors or using internal valuations and estimates during the intervening period. Outside the UK, valuations are produced in conjunction with external qualified professional valuers in the countries concerned. In the event of a material change in market conditions between the valuation date and balance sheet date, an internal valuation is performed and adjustments made to reflect any material changes in fair value.

The determination of fair values of unquoted and illiquid financial investments (Notes 1L, 19 and 20)

For unquoted financial investments, the Group obtains pricing information from a range of pricing services and brokers. Where there are indications that there is no active market, the Group 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 (Notes 1F, 1G and 23)

Significant costs are incurred in connection with acquiring new insurance business, such as initial commission and the indirect costs of obtaining and processing new business. These costs, which vary with, and are primarily related to, the production of new business, are capitalised and amortised against margins in future revenues on the related insurance policies. The recoverability of the asset is measured and the asset is deemed impaired if the projected future margins are less than the carrying value of the asset. To the extent that the future margins differ from those anticipated, an adjustment to the carrying value of the deferred acquisition cost asset will be necessary.

For participating contracts, acquisition costs are charged to the income statement when incurred.

Tax balances (Notes 1R, 24 and 25)

The current tax expense is based on the taxable profits for the year, after any adjustments in respect of prior years. The judgements made, and uncertainties considered, in arriving at tax balances in the financial statements are discussed in Notes 24 and 25.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 ACCOUNTING POLICIES (CONTINUED)

B Use of estimates (continued)

Insurance and investment contract liabilities (Notes 1F, 1G, 30 and 31) 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 34.

C Summary of significant accounting policies

The Group has selected accounting policies which fairly state its financial position and financial performance for a reporting period. 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 Consolidation principles

Subsidiary undertakings

The consolidated financial statements incorporate the assets, liabilities, equity, revenues, expenses and cash flows of the Company and of its subsidiary undertakings drawn up to 31 December each year. All intra-group balances, transactions, income and expenses are eliminated in full. Subsidiaries are those entities (including special purpose entities, mutual funds and unit trusts) over which the Group directly or indirectly has the power to govern the operating and financial policies in order to gain economic benefits (Note 43). Profits or losses of subsidiary undertakings sold or acquired during the period are included in the consolidated results up to the date of disposal or from the date of gaining control. The interests of parties, other than the Group, in investment vehicles, such as unit trusts, are classified as liabilities and appear as 'Net asset value attributable to unit holders' in the consolidated balance sheet.

Acquisitions

The Group applies the purchase method in its accounting for the acquisition of subsidiaries. The cost of an acquisition is measured as the fair value of the assets transferred, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the Group's share of the net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the Group's share of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Associates and joint ventures

Associates are entities over which the Group has significant influence but which it does not control. Consistent with IAS 28, 'Investments in associates', it is presumed that the Group has significant influence where it has between 20% and 50% of the voting rights in the investee. Joint ventures are entities where the Group and other parties undertake an activity which is subject to joint control.

The Group has interests in associates and joint ventures which form part of an investment portfolio held through private equity partnerships, mutual funds, unit trusts and similar entities. In accordance with the choices permitted by IAS 28 and IAS 31, 'Interests in joint ventures', these interests have been classified as fair value through profit or loss and measured at fair value within financial investments, with changes in fair value recognised in the income statement.

Associates which do not form part of an investment portfolio are initially recognised in the balance sheet at cost. The carrying amount of the associate is increased or decreased to reflect the Group's share of the profit or loss after the date of the acquisition.

E Product classification

The Group's products are classified for accounting purposes as either insurance contracts (participating and non-participating) or investment contracts (participating and non-participating). Insurance contracts are contracts which transfer significant insurance risk to the insurer at the inception of the contract. Contracts which do not transfer significant insurance risk to the insurer are classified as investment contracts. Hybrid contract types, containing both insurance and investment features, have been treated as investment contracts when accounting for premiums, claims and other revenue.

A number of insurance and investment contracts contain discretionary participating features (DPF) which entitle the policyholders to receive guaranteed benefits as well as additional benefits:

- the amount or timing of which is contractually at the discretion of the Group; and
- which are contractually based on:
  - the performance of a specified pool of contracts or a specified type of contract;
  - realised and/or unrealised investment returns on a specified pool of assets held by the issuer; or
  - the profit or loss of the Company, fund or other entity which issues the contract.

Contracts with DPF are referred to as participating contracts. With-profits contracts in the UK and most Guarantie Long Terme contracts in France are classified as participating.

F Long term insurance contracts

Premium income

Premiums are recognised as revenue when the liabilities arising from them are created.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Claims

Death claims are accounted for on notification of death. Surrenders for non-linked policies are accounted for when payment is made. Critical illness claims are accounted for when admitted. All other claims and surrenders are accounted for when payment is due. Claims payable include the direct costs of settlement.

Acquisition costs

Acquisition costs comprise direct costs, such as initial commission, and the indirect costs of obtaining and processing new business. Acquisition costs relating to non-participating insurance contracts written outside the with-profits part of the UK Long Term Funds (LTFs) which are incurred during a financial year are deferred by use of an asset which is amortised over the period during which the costs are expected to be recoverable, and in accordance with the expected incidence of future related margins. For participating contracts, acquisition costs are charged to the income statement when incurred.

Insurance contract liabilities

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

UK

In the UK, insurance contract liabilities are determined following an annual investigation of the LTFs in accordance with regulatory requirements.

For non-participating insurance contracts, the liabilities are calculated on the basis of current information using the gross premium valuation method. This brings into account the full premiums receivable under contracts written, having prudent regard to expected lapses and surrenders, estimated renewal and maintenance costs and contractually guaranteed benefits. For unit linked insurance contract liabilities the provision is based on the fund value together with an allowance for any excess of future expenses over charges where appropriate.

For participating contracts, the liabilities to policyholders are determined on a realistic basis in accordance with Financial Reporting Standard (FRS) 27, 'Life assurance'. This includes an assessment of the cost of any future options and guarantees granted to policyholders valued on a market consistent basis. The calculation also takes account of bonus decisions which are consistent with Legal & General Assurance Society Limited's (Society's) Principles and Practices of Financial Management (PPFM). The shareholders' share of the future cost of bonuses is excluded from the assessment of the realistic liability.

In determining the realistic value of liabilities for participating contracts, the value of future profits on non-participating business written in the with-profits part of the fund is accounted for as part of the calculation. The present value of future profits (VIF) for this business is separately determined and its value is deducted from the sum of the liabilities for participating contracts and the unallocated divisible surplus.

Unitised liabilities are recognised when premiums are received and non-unitised liabilities are recognised when premiums are due.

Overseas

The long term insurance contract liabilities for business transacted by overseas subsidiaries are determined on the basis of recognised actuarial methods which reflect local supervisory principles or, in the case of the US, on the basis of US GAAP.

Unallocated divisible surplus

The nature of benefits for participating contracts is such that the allocation of surpluses between ordinary equity holders and participating policyholders is uncertain. The amount of surplus which has not been allocated at the balance sheet date is classified within liabilities as the unallocated divisible surplus. Adjustments made to comply with FRS 27 are charged to the unallocated divisible surplus.

G Investment contracts

Premium income

For investment contracts, amounts collected as premiums are not included in the income statement but are reported as contributions to investment contract liabilities in the balance sheet.

Revenue from investment contracts

Fees charged for investment management services are recognised as revenue as the services are provided. Initial fees, which exceed the level of recurring fees and relate to the future provision of services, are deferred and amortised over the anticipated period in which the services will be provided.

Fees charged for investment management services for institutional and retail fund management are also recognised on this basis.

Claims

Claims are not included in the income statement but are deducted from investment contract liabilities. The movement in investment contract liabilities consists of claims incurred in the period less the corresponding elimination of the policyholder liability originally recognised in the balance sheet and the investment return credited to policyholders.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 ACCOUNTING POLICIES (CONTINUED)

G Investment contracts (continued)

Acquisition costs

For participating investment contracts, 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 income statement when incurred.

For non-participating investment contracts, only directly related acquisition costs which vary with, and are related to, securing new contracts and renewing existing contracts, are deferred and amortised over the period during which the costs are expected to be recoverable from future revenue. All other costs are recognised as expenses when incurred.

Trail commission

The Group operates distribution agreements with intermediaries where further commission costs are payable in each period which a relevant policy remains in-force. For relevant non-participating investment contracts, a liability for the present value of this future commission cost is recognised in the balance sheet on inception of the contract. The present value of future commission costs is deferred as an asset and amortised over the period during which the related revenue will be recognised. At each subsequent reporting date, the liability is remeasured to fair value because this financial liability is part of a portfolio of unit linked assets and liabilities whose performance is evaluated on a fair value basis. Any increase in the liability is recognised as an additional deferred cost. Any change in lapse assumptions or revisions to the underlying assumptions for future cash flows will be reflected in the fair value movement for a period. If the future commission liability decreases, a corresponding adjustment is made to the amortisation of the asset.

Investment contract liabilities

Under current IFRS requirements, participating investment contract liabilities are measured using local GAAP, as permitted by IFRS 4 (see above for insurance contract liabilities). In the UK, participating investment contract liabilities are determined in accordance with FRS 27, including a value for guarantees, in the same way as insurance contracts.

Non-participating investment contracts are unit linked contracts. Unit linked liabilities are measured at fair value by reference to the value of the underlying net asset values of the Group's unitised investment funds at the balance sheet date.

Unitised liabilities are recognised when premiums are received and non-unitised liabilities are recognised when premiums are due.

H General insurance business

Results for the General insurance business are determined after taking account of unearned premiums, outstanding claims and unexpired risks using the annual basis of accounting.

Premium income

Premiums are accounted for in the period in which the risk commences. Estimates are included for premiums not notified by the year end and provision is made for the anticipated lapse of renewals not yet confirmed. Those proportions of premiums written in a year which relate to periods of risk extending beyond the end of the year are carried forward as unearned premiums.

Acquisition costs

A proportion of commission and other acquisition costs relating to unearned premiums is carried forward as deferred acquisition costs or, in respect of reinsurance outwards, as deferred income.

Technical liabilities

Liabilities, together with related reinsurance recoveries, are established on the basis of current information. Such liabilities can never be definitive as to their timing or the amount of claims and are therefore subject to subsequent reassessment on a regular basis.

Claims and related reinsurance recoveries are accounted for in respect of all incidents up to the year end. Provision is made on the basis of available information for the estimated ultimate cost, including claims settlement expenses, claims reported but not yet settled and claims incurred but not yet reported. An unexpired risk provision is made for any overall excess of expected claims and deferred acquisition costs over unearned premiums and after taking account of investment return.

I Liability adequacy tests

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

J Reinsurance

The Group's insurance subsidiaries cede insurance premiums and risk in the normal course of business in order to limit the potential for losses and to provide financing. Outwards reinsurance premiums are accounted for in the same accounting period as the related premiums for the direct or inwards reinsurance business being reinsured. Reinsurance assets include balances due from reinsurers for paid and unpaid losses and loss adjustment expenses, ceded unearned premiums and ceded future life policy benefits. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Reinsurance is recorded as an asset in the consolidated balance sheet unless a right of offset exists, in which case the associated liabilities are reduced commensurately.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

K Intangible assets

Goodwill

Goodwill on the acquisition of subsidiaries prior to 1998 has been charged directly to reserves. On disposal, goodwill held in reserves is transferred directly to retained earnings. From 1998, the Group's policy is to recognise goodwill on the balance sheet as an intangible asset, measured at cost less any accumulated impairment losses.

Purchased interest in long term businesses and other intangible assets

Portfolios of in-force insurance or investment contracts acquired either directly or through the acquisition of a subsidiary undertaking are capitalised at fair value. The value of business acquired represents the present value of anticipated future profits in acquired contracts. These amounts are amortised over the anticipated lives of the related contracts in the portfolio. Other intangible assets acquired via business combinations are recognised at fair value and are subsequently amortised over their useful life in line with the expected emergence of profit from the business.

L Investments

Investment property

Investment property comprises land and buildings which are held for long term rental yields and capital growth. It is carried at fair value with changes in fair value recognised in the income statement within investment return.

Financial investments

The Group classifies its financial investments on initial recognition as held for trading (HFT), designated at fair value through profit or loss (FVTPL), available-for-sale (AFS) or loans and receivables. Initial recognition of financial investments is on the trade date.

The Group's policy is to measure investments at FVTPL except for certain overseas assets where the related liability is valued on a passive basis (not using current information), in which case investments are classified as AFS. All derivatives other than those designated as hedges are classified as HFT.

Certain financial investments held by the Group 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 Group's investment strategy. Assets designated as FVTPL include debt securities and equity instruments which would otherwise have been classified as AFS under IAS 39, 'Financial instruments: recognition and measurement'. Assets backing participating and non-participating policyholder liabilities outside the US are designated as FVTPL. For participating contracts the assets are managed on a fair value basis to maximise the total return to policyholders over the contract life. The Group's non-participating investment contract liabilities outside of the US are measured on the basis of current information and are designated as FVTPL to avoid an accounting mismatch in the income statement.

The fair values of quoted financial investments are based on current bid prices. If the market for a financial investment is not active, the Group 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.

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

Financial investments classified as AFS are measured at fair value with unrealised gains and losses recognised in a separate reserve within equity. Realised gains and losses, impairment losses, dividends, interest and foreign exchange movements on non-equity instruments are reflected in the income statement.

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

M Plant and equipment

The initial cost of an item of plant or equipment is capitalised where it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The cost is then depreciated on a straight line basis over the item's estimated useful working life.

N Impairment policy

The Group reviews the carrying value of its financial assets (other than those held at FVTPL) at each balance sheet date. If the carrying value of a financial asset is impaired, the carrying value is reduced through a charge to the income statement. There must be objective evidence of impairment as a result of one or more events which have occurred after the initial recognition of the asset. Impairment is only recognised if the loss event has an impact on the estimated future cash flows of assets held at amortised cost or fair value of assets classified as AFS.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 ACCOUNTING POLICIES (CONTINUED)

N Impairment policy (continued)

Non-financial assets which have an indefinite useful life are not subjected to amortisation and are tested annually for impairment. 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.

O Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, treasury bills and other short term highly liquid investments with original maturities of three months or less.

P Derivative financial instruments and hedge accounting

The Group's activities expose it to the financial risks of changes in foreign exchange rates and interest rates. The Group uses derivatives such as foreign exchange forward contracts and interest rate swap contracts to hedge these exposures. The Group uses hedge accounting, provided the prescribed criteria in IAS 39 are met, to recognise the offsetting effects of changes in the fair value or cash flow of the derivative instrument and the hedged item. The Group's principal uses of hedge accounting are to:

(i) recognise in shareholders' equity the changes in the fair value of derivatives designated as hedges of a net investment in a foreign operation. Any cumulative gains and/or losses are recognised in the income statement on disposal of the foreign operation;

(ii) defer in equity the changes in the fair value of derivatives designated as the hedge of a future cash flow attributable to a recognised asset or liability, a highly probable forecast transaction, or a firm commitment until the period in which the future transaction affects profit or loss or is no longer expected to occur; and

(iii) hedge the fair value movements in loans due to interest rate and exchange rate fluctuations. Any gain or loss from remeasuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement.

The relationship between the hedging instrument and the hedged item, together with the risk management objective and strategy for undertaking the hedge transaction, are documented at the inception of the transaction. The effectiveness of the hedge is documented and monitored on an ongoing basis. Hedge accounting is only applied for highly effective hedges (between 80% and 125% effectiveness) with any ineffective portion of the gain or loss recognised in the income statement, within other expenses, in the current period.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instruments which do not qualify for hedge accounting are recognised immediately in the income statement.

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.

Q Borrowings

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

Borrowings comprise unsecured subordinated debt such as tier 1 and tier 2 bond issues, short and long term unsecured senior debt such as long dated bond issues, commercial paper issuance and bank borrowings under both committed and uncommitted debt facilities including bank overdrafts. Borrowings raised from individual banks, syndicated banks and capital markets secured on specific assets/cash flows such as Triple X securitisations and property partnerships' assets are included as non recourse borrowings, as are mortgage loans raised by SIPP clients secured on their properties invested in their portfolio of linked SIPP investments which we manage on their behalf.

R Income taxes

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement except where it relates to an item which is recognised in other comprehensive income.

Current tax is the expected tax payable on the taxable profit for the period and any adjustment to the tax payable in respect of previous periods.

The total income tax expense for the period includes income tax paid by Society in respect of UK life policyholder returns, which is not related to profits earned by equity holders for the period. The income tax charge in the income statement has therefore been apportioned between the element attributable to policyholder returns and the element attributable to equity holders' profits (equity holder tax).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Deferred income tax

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Deferred tax is measured using tax rates expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled, based on tax rates and law which have been enacted or substantively enacted at the balance sheet date.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Deferred tax assets and liabilities are not discounted.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future (or if it will, then it will not generate any incremental tax liability for the Group).

S Leases

Where a significant proportion of the risks and rewards of ownership is retained by the lessor, leases are classified as operating leases. Payments made as lessees under operating leases (net of any incentives from the lessor) are charged to the income statement on a straight line basis over the period of the lease.

T Employee benefits

Pension obligations

The Group operates a number of defined benefit and defined contribution pension schemes in the UK and overseas. The assets of all UK defined benefit schemes are held in separate trustee administered funds which are subject to regular actuarial valuation every three years, updated by formal reviews at reporting dates.

The liability recognised in the balance sheet in respect of defined benefit pension schemes is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets. Plan assets exclude any insurance contracts issued by the Group. The defined benefit obligation is actuarially calculated each year using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows. The discount rate is based on market yields of high quality corporate bonds which are denominated in the currency in which the benefits will be paid, and that have terms to maturity which approximate to those of the related pension liability.

Where the unallocated divisible surplus or equity holders' funds are affected as a result of actuarial gains and losses on the defined benefit pension scheme, the charge or credit is not recognised in the income statement but through the statement of comprehensive income.

The Group pays contractual contributions in respect of defined contribution schemes. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expenses when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available. Obligations under defined benefit pension schemes are included within provisions.

Share-based payments

The Group operates a number of share-based payment schemes. The fair value at the date of grant of the equity instrument is recognised as an expense, spread over the vesting period of the instrument. The total amount to be expensed is determined by reference to the fair value of the awards, excluding the impact of any non-market vesting conditions. At each balance sheet date, the Group revises its estimate of the number of equity instruments which are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment is made to equity. On vesting or exercise, the difference between the expense charged to the income statement and the actual cost to the Group is transferred to retained earnings. Where new shares are issued, the proceeds received are credited to share capital and share premium.

U Share capital and employee scheme shares

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 Group exchanging a fixed amount of cash or other financial assets, for a fixed number of its own equity instruments.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 ACCOUNTING POLICIES (CONTINUED)

U Share capital and employee scheme shares (continued)

Share issue costs

Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. An incremental share issue cost is one which would not have arisen if shares had not been issued.

Legal & General shares

Where any Group entity purchases the Company's equity share capital, the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to shareholders. Where such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity attributable to shareholders, net of any directly attributable incremental transaction costs and the related income tax effects. Shares held on behalf of employee share schemes are disclosed as such on the balance sheet.

Where shares are cancelled under the share buyback programme, the consideration paid, including any directly attributable incremental costs, is deducted from equity attributable to shareholders. As required by Companies Act 2006, the equivalent of the nominal value of shares cancelled is transferred to a capital redemption reserve.

Dividend recognition

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

V Fiduciary activities

Assets associated with fiduciary activities and the income arising from those assets, together with associated commitments to return such assets to customers, are not included in these financial statements. Where the Group acts in a fiduciary capacity, for instance as a trustee or agent, it has no contractual rights over the assets concerned.

W Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The Group recognises a provision for onerous contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

X Payables and other financial liabilities

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, cross-currency swaps and credit default swaps measured at fair value.

Y Foreign currency translation

Foreign currency transactions

Foreign currency transactions are translated into the functional currency using the exchange rate prevailing at the date of the transactions. The functional currency of the Group's foreign operations is the currency of the primary economic environment in which these entities operate. Foreign exchange gains and losses are recognised in the income statement, except when recognised in equity as qualifying cash flow or net investment hedges.

Overseas subsidiaries

The assets and liabilities of all of the Group's foreign operations are translated into sterling, the Group's presentational currency, at the closing rate at the date of the balance sheet. The income and expenses for each income statement are translated at average exchange rates. On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to a separate component of shareholders' equity.

Z Investment return

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

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

AA Operational income and expenses

Operational income comprises fee income from estate agency operations, agency fee income relating to distribution services and revenue from consolidated private equity investments. Operational income is accounted for when due.

Other expenses comprise primarily the expenses incurred in estate agency operations, institutional fund management and retail investment business, together with unallocated corporate expenses. Other costs are accounted for as they arise.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

AB Earnings per share

Earnings per share

Earnings per share is calculated by dividing net income attributable to ordinary equity holders by the weighted average number of ordinary shares in issue during the year, excluding employee scheme shares and shares acquired under the share buyback programme prior to cancellation. For this purpose, net income is defined as the profit after tax derived from continuing operations, or as the profit after tax derived from both continuing and discontinued operations.

Diluted earnings per share

For diluted earnings per share, the weighted average number of ordinary shares in issue, excluding employee scheme shares, is adjusted to assume conversion of all dilutive potential ordinary shares, such as share options granted to employees. Potential or contingent share issuances are treated as dilutive when their conversion to shares would decrease net earnings per share.

AC Segmental reporting

Under the requirements of IFRS 8 'Operating segments', operating and reportable segments are presented in a manner consistent with the internal reporting provided to the chief operating decision maker, which has been identified as the Board of Legal & General Group Plc.

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

Certain new standards, amendments and interpretations to existing standards have been published which are mandatory for the Group's accounting periods beginning on or after 1 January 2010 or later periods but which the Group has not adopted early, as follows:

- Revised IFRS 3, 'Business combinations' issued in January 2008 (effective for annual periods commencing on or after 1 July 2009). The standard continues to apply the acquisition method to business combinations, with some significant changes e.g. all payments to purchase a business are to be recorded at fair value at the acquisition date, with some contingent payments subsequently re-measured at fair value through income. Goodwill may be calculated based on the parent's share of net assets or may include goodwill related to the minority interest. All transaction costs will be expensed. The requirements of this standard will be considered for any future business acquisitions.
- Revised IAS 27, 'Consolidated and separate financial statements' issued in January 2008 (effective for annual periods commencing on or after 1 July 2009). This standard requires the effect of all transactions with non-controlling interests to be recorded in equity if there is no change in control. It also specifies the accounting when control is lost – any remaining interest in the entity is re-measured to fair value and a gain or loss is recognised in profit or loss. The Group does not consider that this amendment will result in any significant impact on the financial statements.
- IFRIC 17, 'Distributions of non-cash assets to owners' issued in November 2008 (effective for annual periods commencing on or after 1 July 2009). The interpretation clarifies that a dividend payable should be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity; an entity should measure the dividend payable at the fair value of the net assets to be distributed; an entity should recognise the difference between the dividend paid and the carrying amount of the net assets distributed in profit or loss; and an entity will provide additional disclosures if the net assets being held for distribution to owners meet the definition of a discontinued operation. The IFRIC is not expected to have a material impact on the Group's financial statements.
- IFRIC 18, 'Transfers of assets from customers' issued in January 2009 (effective for annual periods commencing on or after 1 July 2009). This IFRIC clarifies the requirements of IFRSs for agreements in which an entity receives from a customer an item of property, plant, and equipment that the entity must then use either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services (such as a supply of electricity, gas or water). This IFRIC is not relevant to the Group's operations as the Group does not have such agreements with customers.
- There are various amendments resulting from the IASB's annual improvements project issued in April 2009 (effective for annual periods commencing on or after both 1 July 2009 and 1 January 2010), these are unlikely to have a material impact on the Group accounts.
- Amendment to IFRS 1, 'First-time adoption of International Financial Reporting Standards' issued in July 2009 (effective for annual periods commencing on or after 1 January 2010). These amendments exempt entities using the full cost method from retrospective application of IFRSs for oil and gas assets and exempt entities with existing leasing contracts from reassessing the classification of those contracts in accordance with IFRIC 4. The amendments are not relevant to the Group's financial statements.
- Amendments to IFRS 2, 'Group cash-settled share-based payment transactions' issued in June 2009 (effective for annual periods commencing on or after 1 January 2010). The amendments provide a clear basis to determine the classification of share-based payment awards in both consolidated and separate financial statements. The definitions section has also been amended to remove the inconsistencies between Appendix A, defined terms and the main body of the standard. The Group does not consider that this amendment will result in any significant impact on the financial statements.
- IFRS 9, 'Financial instruments' on classification and measurement, issued in November 2009 (effective for annual periods commencing on or after 1 January 2013). This is the first part of a new standard on classification and measurement of financial assets that will replace IAS 39. IFRS 9 has two measurement categories: amortised cost and fair value. All equity instruments are measured at fair value. A debt instrument is at amortised cost only if the entity is holding it to collect contractual cash flows and the cash flows represent principal and interest, otherwise it must be measured at fair value through profit or loss. The Group does not intend to early adopt this standard.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

2 SUPPLEMENTARY OPERATING PROFIT INFORMATION

Supplementary IFRS operating profit is one of the Group's key performance indicators. We provide this measure because we believe it gives shareholders a better understanding of the Group's underlying performance. In order to further enhance this understanding, we have amended the definition of IFRS operating profit to remove the impact of investment volatility from the non profit Risk and Savings and the Group capital and financing results.

The key changes to our definition of IFRS operating profit are:

i. Operating profit for the Risk and Savings businesses is now based on the investment returns that the Group expects to make on the financial investments that back the non profit business over the reporting period, rather than the actual returns on these investments. The difference between the expected return and the actual return on investments, and the corresponding impact on liabilities, is shown below the operating profit line. This adjustment includes the removal of accounting volatility arising from the mismatch of asset and liability valuations for deferred tax balances within unit linked funds under IFRS.
ii. Group capital and financing operating profit now excludes the profit or loss arising from actuarial gains and losses on annuities held by the Group's defined benefit pension schemes. As this is driven by bond market yields the effect has been classified as variation from longer term investment return.
iii. The profit or loss impact arising from the elimination of own debt holdings is reflected below operating profit. In previous reporting periods this amount has been £nil.

The amended definition more closely aligns the results of non profit Risk and Savings and Group capital and financing with our other UK businesses and is closer to the European Embedded Value (EEV) definition of operating profit. It changes the allocation of profit between operating and non-operating elements, but it does not affect underlying performance, the economics of our business, the profit before tax attributable to shareholder or the profit for the year.

The table below sets out the effect of the above changes to IFRS supplementary operating profit for the year ended 31 December 2008, and the six months ended 30 June 2009:

	As reported 2008 £m	**Effect of restating the definition of IFRS operating profit £m**	**Restated 2008 £m**	As reported 30.06.09 £m	Effect of restating the definition of IFRS operating profit £m	Restated 30.06.09 £m
From continuing operations						
Risk	**(603)**	**825**	**222**	(128)	351	223
Savings	**66**	**(59)**	**7**	(5)	26	21
Investment management	**165**	**–**	**165**	70	–	70
International	**59**	**–**	**59**	65	–	65
Group capital and financing	**124**	**15**	**139**	29	(4)	25
Operating (loss)/profit	**(189)**	**781**	**592**	31	373	404
Variation from longer term investment return	**(1,239)**	**(781)**	**(2,020)**	(154)	(373)	(527)
Property losses attributable to minority interests	**(63)**	**–**	**(63)**	(20)	–	(20)
Loss from continuing operations before tax attributable to equity holders of the Company	**(1,491)**	**–**	**(1,491)**	(143)	–	(143)
Tax credit attributable to equity holders of the Company	**361**	**–**	**361**	52	–	52
Loss for the period	**(1,130)**	**–**	**(1,130)**	(91)	–	(91)
Loss attributable to minority interests	**63**	**–**	**63**	20	–	20
Loss attributable to equity holders of the Company	**(1,067)**	**–**	**(1,067)**	(71)	–	(71)

Operating profit for the Risk segment represents the net capital invested/released from the non profit Risk businesses (individual and group protection, and individual and bulk purchase annuities) and the profit of our General insurance business. Operating profit reflects the investment returns that the business expects to make on the financial investments that back the business and on shareholder funds retained within our General insurance business.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Operating profit for the Savings segment represents the net capital invested/released from the non profit Savings businesses (non profit investment bonds and non profit pensions (including SIPPs)), the with-profits transfer and the operating profit of our core retail investments business. Operating profit reflects the investment returns that the business expects to make on the financial investments that back this business.

Operating profit for the Investment management and International segments reflects the profits from these organisations and includes a longer term expected investment return on the shareholders' funds within the Investment management and Netherlands' operations.

Investment return on Group capital incorporates a longer term expected investment return using longer term investment return assumptions applied to the average balance of Group invested assets (including interest bearing intra-group balances) calculated on a quarterly basis. Profits or losses arising from actuarial movements on annuities held by the Group's defined benefit pension schemes are excluded from operating profit. Profit and losses arising on the elimination of own debt holdings are also excluded from operating profit.

The table below sets out the effect of the above changes to IFRS operating profit for the year ended 31 December 2009:

(i) Reconciliation between operating profit and profit from ordinary activities after income tax

	Notes	2009 £m	2008 Restated £m
From continuing operations			
Risk	(ii)	**735**	222
Savings	(iii)	**55**	7
Investment management	(iv)	**167**	165
International	(v)	**127**	59
Group capital and financing	(vi)	**57**	139
Investment projects[1]		**(32)**	–
Operating profit		**1,109**	592
Variation from longer term investment return		**(16)**	(2,020)
Property losses attributable to minority interests		**(19)**	(63)
Profit/(loss) from continuing operations before tax attributable to equity holders of the Company		**1,074**	(1,491)
Tax (expense)/credit attributable to equity holders of the Company	11	**(230)**	361
Profit/(loss) for the year		**844**	(1,130)

1. Investment projects relate to strategic investments including Solvency II.

(ii) Risk

(a) Risk operating profit

	Notes	2009 £m	2008 Restated £m
Non profit Risk	(b)	**717**	223
General insurance	(f)	**17**	(2)
Other[1]		**1**	1
Total Risk operating profit		**735**	222

1. Other comprises estate agencies and housing related business conducted through our regulated mortgage network. It also includes Nationwide Life Risk business and business unit costs of £3m (2008: £3m) allocated to the Risk business.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

2 SUPPLEMENTARY OPERATING PROFIT INFORMATION (CONTINUED)

(ii) Risk (continued)

(b) Analysis of net capital released from non profit Risk business

	Notes	2009 £m	2008 Restated £m
Non profit business operating profit comprises:			
Operational cash generation		**438**	376
New business strain		**50**	(173)
Net cash generation		**488**	203
Experience variances	(c)	**113**	2
Changes to valuation assumptions	(d)	**169**	(42)
Changes to FSA reporting and capital rules		**15**	–
Movements in non-cash items	(e)	**(229)**	16
Other		**(41)**	(20)
		515	159
Tax gross-up		**202**	64
Non profit Risk operating profit		**717**	223

Non profit business operational cash generation represents the capital and profit expected to be generated in the period from the in-force non profit business if the embedded value and valuation assumptions are borne out in practice. The experience variances are calculated with reference to embedded value assumptions, including the apportionment of investment return and tax in the EEV model.

The 2008 net capital released analysis has been restated in accordance with the new definition of operating profit (see the beginning of this note).

Both new business strain and operational cash generation exclude required solvency margin from the liability calculation as is required by the ABI SORP.

In 2006 the FSA introduced a more realistic reserving framework for certain non profit business (Policy statement (PS) 06/14). In July 2009, a Part VII transfer of the Nationwide Life Risk business to Society took place and the Group chose to adopt PS06/14 for this business. The impact of this, offset by the amortisation of associated intangible assets, is reflected within changes to FSA reporting and capital rules above.

An analysis of the experience variances, valuation assumption changes and non-cash items, all net of tax, is provided below:

(c) Experience variances

	2009 £m	2008 Restated £m
Persistency	**(9)**	(5)
Mortality/morbidity	**(9)**	26
Expenses	**1**	18
BPA data loading	**48**	22
Project and development costs[1]	**(21)**	(53)
Tax[2]	**79**	(15)
Other	**24**	9
	113	2

1. Project and development costs relate to continued investment in internal and other customer facing systems (£15m) and redundancy costs (£6m).
2. The current tax charge was lower than expected due to the utilisation of brought forward tax losses.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(d) Changes to valuation assumptions

	2009 £m	2008 Restated £m
Persistency	**(5)**	4
Mortality/morbidity	**101**	(25)
Expenses	**54**	(55)
Other	**19**	34
	169	(42)

(e) Movements in non-cash items

	2009 £m	2008 Restated £m
Deferred tax[1]	**(221)**	19
Other	**(8)**	(3)
	(229)	16

1. The movement in deferred tax reflects the profitability of the non profit Risk business in 2009 and the consequent utilisation of brought forward losses from 2008.

(f) General insurance operating profit, underwriting result and combined operating ratios

	Operating profit 2009 £m	Under-writing result 2009 £m	Combined operating ratio 2009 %	Operating (loss)/profit 2008 £m	Under-writing result 2008 £m	Combined operating ratio 2008 %
From continuing operations						
Household	**12**	**1**	**98**	(12)	(26)	110
Other business	**5**	**4**	**79**	10	8	86
	17	**5**	**96**	(2)	(18)	108

The combined operating ratio is:

$$\left[\frac{\text{Net incurred claims}}{\text{Net earned premiums}} + \frac{\text{Expenses + Net commission}}{\text{Net written premiums}}\right] \times 100$$

(iii) Savings

(a) Savings operating profit

	Notes	2009 £m	2008 Restated £m
Non profit Savings[1]	(b)	**(4)**	(79)
With-profits business[2]		**64**	107
		60	28
Core retail investments		**9**	–
Other[3]		**(14)**	(21)
Total Savings operating profit		**55**	7

1. Non profit Savings business includes non profit investment bonds and non profit pensions (including SIPPs).
2. With-profits business operating profit is the shareholders' share of total with-profits bonuses.
3. Other includes Suffolk Life, International (Ireland), Nationwide Life Savings business and business unit costs of £3m (2008: £3m), allocated to the Savings business.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

2 SUPPLEMENTARY OPERATING PROFIT INFORMATION (CONTINUED)

(iii) Savings (continued)

(b) Analysis of net capital released from non profit Savings business

	Notes	2009 £m	2008 Restated £m
Non profit business operating profit comprises:			
Operational cash generation		**58**	77
New business strain		**(77)**	(161)
Net cash generation		**(19)**	(84)
Experience variances	(c)	**(1)**	(35)
Changes to valuation assumptions	(d)	**9**	32
Changes to FSA reporting and capital rules		**50**	–
Movements in non-cash items	(e)	**(64)**	(14)
Other		**22**	45
		(3)	(56)
Tax gross-up		**(1)**	(23)
Non profit Savings operating profit		**(4)**	(79)

Non profit business operational cash generation represents the capital and profit expected to be generated in the period from the in-force non profit business if the embedded value and valuation assumptions are borne out in practice. The experience variances are calculated with reference to embedded value assumptions, including the apportionment of investment return and tax in the EEV model.

The 2008 net capital released analysis has been restated in accordance with the new definition of operating profit (see the beginning of this note).

Both new business strain and operational cash generation exclude required solvency margin from the liability calculation as is required by the ABI SORP.

In 2006, the FSA introduced a more realistic reserving framework for certain non profit business (PS06/14). In 2009, the Group has chosen to implement PS06/14 rule changes relating to the calculation of the regulatory sterling reserves on non profit unit linked contracts. The impact of this is reflected within changes to FSA reporting and capital rules above. However, sterling reserves on investment contracts are eliminated from IFRS reporting and the corresponding reduction is reported through non-cash items.

An analysis of the experience variances, valuation assumption changes and non-cash items, all net of tax, is provided below:

(c) Experience variances

	2009 £m	2008 Restated £m
Persistency	**(1)**	12
Mortality/morbidity	**–**	(1)
Expenses	**–**	(7)
Project and development costs[1]	**(23)**	(42)
Tax[2]	**22**	3
Other	**1**	–
	(1)	(35)

1. Project and development costs relate to continued investment in internal and other customer facing systems (£16m) and redundancy costs (£7m).
2. The current tax change was lower than expected due to the utilisation of brought forward tax losses.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(d) Changes to valuation assumptions

	2009 £m	2008 £m
Persistency	**1**	8
Mortality/morbidity	**(2)**	(1)
Expenses	**(1)**	(2)
Other	**11**	27
	9	32

(e) Movements in non-cash items

	2009 £m	2008 Restated £m
Deferred tax	**(33)**	16
Deferred acquisition costs	**(5)**	20
Deferred income liabilities	**35**	30
Other[1]	**(61)**	(80)
	(64)	(14)

1. In 2009, Other includes the elimination of £55m of sterling reserves following the adoption of PS06/14.

(iv) Investment management

	2009 £m	2008 £m
Managed pension funds	**128**	117
Private equity	**(1)**	(1)
Property	**4**	4
Other income[1]	**41**	52
Legal & General Investment Management	**172**	172
Institutional unit trusts[2]	**(5)**	(7)
Total Investment management operating profit	**167**	165

1. Other income includes £28m of profits arising from the provision of investment management services charged to the Group's Risk and Savings businesses (2008: £35m).
2. Investment management operating profit excludes core retail investments of £9m (2008: £nil), which has been disclosed as part of Savings.

(v) International

	2009 £m	2008 £m
USA	**86**	39
Netherlands	**42**	6
France	**4**	14
Other[1]	**(5)**	–
Total International operating profit	**127**	59

1. Other includes our joint venture operations in Egypt, the Gulf and India.

Exchange rates are provided in Note 10.

(vi) Group capital and financing

	2009 £m	2008 Restated £m
Investment return[1]	**191**	298
Interest expense[2]	**(127)**	(145)
Investment expenses	**(3)**	(5)
Unallocated corporate expenses	**(4)**	(9)
Total Group capital and financing operating profit	**57**	139

1. The longer term expected investment return of £191m (2008: £298m) reflects an average return of 6% (2008: 7%) on the average balance of invested assets of £3.0bn (2008: £4.5bn), held within Group capital and financing calculated on a quarterly basis. The invested assets held within Group capital and financing amounted to £2.8bn at 31 December 2009 (31 December 2008: £3.9bn).
2. Interest expense excludes interest on non recourse financing (see Note 35).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

2 SUPPLEMENTARY OPERATING PROFIT INFORMATION (CONTINUED)

(vii) Earnings per share

	Notes	Profit/ (loss) before tax 2009 £m	Tax (credit)/ expense 2009 £m	Profit after tax 2009 £m	Number of shares[1] 2009 m	Earnings per share 2009 p
Operating profit from continuing operations	(i)	**1,109**	**(304)**	**805**	**5,824**	**13.82**
Variation from longer term investment return	(i)	**(16)**	**74**	**58**		**1.00**
Loss attributable to equity holders/EPS[2]		**1,093**	**(230)**	**863**	**5,824**	**14.82**

	Notes	Profit/ (loss) before tax 2008 Restated £m	Tax (credit)/ expense 2008 Restated £m	Profit/ (loss) after tax 2008 Restated £m	Number of shares[1] 2008 m	Earnings per share 2008 Restated p
Operating profit from continuing operations	(i)	592	(163)	429	5,968	7.19
Variation from longer term investment return	(i)	(2,020)	524	(1,496)		(25.07)
Profit attributable to equity holders/EPS[2]		(1,428)	361	(1,067)	5,968	(17.88)

1. Weighted average number of shares.
2. Earnings per share.

The number of shares in issue at 31 December 2009 was 5,862,216,780 (31 December 2008: 5,861,627,994).

3 SEGMENTAL ANALYSIS

The Group has five reporting segments comprising Risk, Savings, Investment management, International, and Group capital and financing.

The Risk segment comprises individual and group protection, individual and bulk purchase annuities, and general insurance, together with estate agencies and the housing related business conducted through our regulated mortgage network.

The Savings segment comprises non profit investment bonds, non profit pensions (including SIPPs), ISAs, retail unit trusts, and all with-profits products.

The Investment management segment comprises institutional fund management and institutional unit trust business.

The International segment comprises businesses in the United States, France, the Netherlands and emerging markets.

Shareholders' equity supporting the non profit Risk and Savings businesses is held within Legal & General Assurance Society Limited and Legal & General Pensions Limited and is managed on a groupwide basis within Group capital and financing. This also includes capital within the Group's treasury function, and unit trust funds and property partnerships, which are managed on behalf of clients but are required to be consolidated under IFRS, which do not constitute a separately reportable segment.

Transactions between reportable segments are on normal commercial terms, and are included within the reported segments.

The Group assesses performance and allocates resources on the basis of IFRS operating profit before tax (set out in Note 2). Segmental IFRS operating profit before tax is reconciled to the consolidated profit from continuing operations before tax attributable to equity holders and consolidated profit from ordinary activities after income tax.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(i) Operating profit

For the year ended 31 December 2009	Risk £m	Savings £m	Investment management £m	International £m	Group capital and financing[1] £m	Total £m
Operating profit	**735**	**55**	**167**	**127**	**25**	**1,109**
Variation from longer term investment return[2,3]	**(218)**	**127**	**(4)**	**26**	**53**	**(16)**
Property losses attributable to minority interests	**–**	**–**	**–**	**–**	**(19)**	**(19)**
Profit from continuing operations before tax attributable to equity holders of the Company	**517**	**182**	**163**	**153**	**59**	**1,074**
Tax (expense)/credit attributable to equity holders of the Company	**(142)**	**(49)**	**(45)**	**(49)**	**55**	**(230)**
Profit for the year	**375**	**133**	**118**	**104**	**114**	**844**

1. For segmental purposes, the Investment projects have been included in Group capital and financing.
2. At half-year 2009, non profit Risk business reflected a small reduction in yield from action taken to sell some of the Group's holdings of tier 1 and upper tier 2 bank securities. These actions have contributed £75m to the negative investment variance. The cash and overlay strategy executed on the portfolio resulted in adverse effects on the assumed yields at the half-year which are reflected within IFRS profit. As expected, these half-year yield impacts have been reversed by action taken in further diversifying the credit portfolio in the second half of the year. The impact of strengthening assumptions for reinvestment of cashflows, variability in currency hedging costs and inflation is also reflected here, in addition to the negative impact from default provisioning of £50m. The 2008 Risk investment return variance includes £(650)m relating to the increase in the non profit annuity credit default reserve.
3. Savings investment variances reflect management action taken in the second half of the year to optimise the tax position of unit linked business.

For the year ended 31 December 2008	Risk Restated £m	Savings Restated £m	Investment management £m	International £m	Group capital and financing Restated £m	Total Restated £m
Operating profit	222	7	165	59	139	592
Variation from longer term investment return	(854)	59	7	4	(1,236)	(2,020)
Property losses attributable to minority interests	–	–	–	–	(63)	(63)
(Loss)/profit from continuing operations before tax attributable to equity holders of the Company	(632)	66	172	63	(1,160)	(1,491)
Tax credit/(expense) attributable to equity holders of the Company	172	(7)	(52)	(21)	269	361
(Loss)/profit for the year	(460)	59	120	42	(891)	(1,130)

(ii) Revenue

For the year ended 31 December 2009	Risk £m	Savings £m	Investment management £m	International £m	Group capital and financing £m	Total £m
Internal revenue	**117**	**136**	**103**	**–**	**(356)**	**–**
External revenue	**5,809**	**7,200**	**28,992**	**1,527**	**262**	**43,790**
Total revenue	**5,926**	**7,336**	**29,095**	**1,527**	**(94)**	**43,790**

For the year ended 31 December 2008	Risk £m	Savings £m	Investment management £m	International £m	Group capital and financing £m	Total £m
Internal revenue	132	133	119	–	(384)	–
External revenue	2,648	(6,008)	(28,229)	741	(796)	(31,644)
Total revenue	2,780	(5,875)	(28,110)	741	(1,180)	(31,644)

Total revenue includes investment gains of £38,201m (2008: losses of £37,749m).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

3 SEGMENTAL ANALYSIS (CONTINUED)
(iii) Consolidated balance sheet

As at 31 December 2009	Risk £m	Savings £m	Investment management £m	International £m	Group capital and financing £m	Total £m
Assets						
Investment in associates	**–**	**14**	**–**	**31**	**–**	**45**
Investment property	**–**	**1,965**	**497**	**7**	**1,370**	**3,839**
Financial investments	**22,416**	**40,857**	**206,753**	**6,400**	**(410)**	**276,016**
Reinsurers' share of contract liabilities	**1,558**	**687**	**–**	**272**	**(424)**	**2,093**
Deferred acquisition costs	**45**	**999**	**16**	**984**	**(87)**	**1,957**
Other assets	**1,380**	**477**	**956**	**1,453**	**(1,822)**	**2,444**
Cash and cash equivalents	**568**	**2,619**	**3,314**	**516**	**3,633**	**10,650**
Total assets	**25,967**	**47,618**	**211,536**	**9,663**	**2,260**	**297,044**
Shareholders' equity	**120**	**79**	**339**	**1,372**	**2,286**	**4,196**
Minority interests	**–**	**–**	**–**	**–**	**2**	**2**
Total equity	**120**	**79**	**339**	**1,372**	**2,288**	**4,198**
Liabilities						
Subordinated borrowings	**–**	**–**	**–**	**–**	**1,870**	**1,870**
Participating contract liabilities	**–**	**15,084**	**–**	**2,376**	**–**	**17,460**
Non-participating contract liabilities	**22,102**	**30,078**	**207,963**	**3,523**	**(581)**	**263,085**
Senior borrowings[1]	**9**	**199**	**2**	**535**	**662**	**1,407**
Other liabilities	**3,736**	**2,178**	**3,232**	**1,857**	**(1,979)**	**9,024**
Total liabilities	**25,847**	**47,539**	**211,197**	**8,291**	**(28)**	**292,846**
Total equity and liabilities	**25,967**	**47,618**	**211,536**	**9,663**	**2,260**	**297,044**

1. Includes non recourse financing.

As at 31 December 2008	Risk £m	Savings £m	Investment management £m	International £m	Group capital and financing £m	Total £m
Assets						
Investment in associates	–	14	–	–	–	14
Investment property	–	2,866	273	7	823	3,969
Financial investments	19,119	34,160	173,255	6,250	1,730	234,514
Reinsurers' share of contract liabilities	1,479	474	–	302	(258)	1,997
Deferred acquisition costs	51	1,018	18	1,100	(75)	2,112
Other assets	2,199	518	1,471	1,427	(2,182)	3,433
Cash and cash equivalents	412	3,941	3,376	618	2,341	10,688
Total assets	23,260	42,991	178,393	9,704	2,379	256,727
Shareholders' equity	101	73	322	1,272	1,820	3,588
Minority interests	–	–	–	–	144	144
Total equity	101	73	322	1,272	1,964	3,732
Liabilities						
Subordinated borrowings	–	–	–	–	1,657	1,657
Participating contract liabilities	–	14,829	–	2,289	–	17,118
Non-participating contract liabilities	19,001	25,917	174,469	3,691	(539)	222,539
Senior borrowings[1]	–	161	9	676	1,468	2,314
Other liabilities	4,158	2,011	3,593	1,776	(2,171)	9,367
Total liabilities	23,159	42,918	178,071	8,432	415	252,995
Total equity and liabilities	23,260	42,991	178,393	9,704	2,379	256,727

1. Includes non recourse financing.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(iv) Gross written premiums on insurance contracts

	2009 £m	2008 £m
From continuing operations		
Risk		
Non-participating Risk business	**3,057**	4,038
General insurance		
– Household	**247**	267
– Other business	**26**	29
Total Risk	**3,330**	4,334
Savings		
Non-participating Savings business	**45**	49
Participating business	**772**	551
Total Savings	**817**	600
International		
USA	**487**	397
Netherlands	**270**	278
France	**371**	286
Total International	**1,128**	961
Total gross written premiums	**5,275**	5,895

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

4 NEW BUSINESS (GROSS OF REINSURANCE)

New business premiums reflect income arising from the sale of new contracts during the reporting period and any changes to existing contracts, which were not anticipated at the outset of the contract. This is presented below for all long term business written by the Group including both insurance and investment contracts.

New annual premiums arise where the terms and conditions of a policy anticipate more than one premium being paid over its lifetime; new single premiums comprise all premiums which are not categorised as new annual premiums.

	Annual 2009 £m	Single 2009 £m	Annual 2008 £m	Single 2008 £m
Protection	180	–	207	–
Annuities[1]	–	1,862	–	2,806
Total Risk	180	1,862	207	2,806
Core retail investments[2]				
– ISAs	22	838	29	413
– Unit trusts	10	2,595	12	1,466
Unit linked bonds	–	677	–	1,306
Pensions, stakeholder and other non profit	144	1,289	181	1,468
With-profits	103	879	108	838
Total Savings	279	6,278	330	5,491
International				
USA	49	–	51	–
Netherlands	8	142	13	157
France	14	293	17	227
	530	8,575	618	8,681
Investment management				
UK managed pension funds[3]				
– Pooled funds		25,606		26,733
– Segregated funds		3,381		841
		28,987		27,574
Limited partnerships		34		51
Other funds[2]	1	4,262	1	5,465
	1	33,283	1	33,090
Total new business	531	41,858	619	41,771
Comprising:				
Insurance contracts				
Risk and Savings				
– Participating	2	1,217	1	855
– Non-participating	246	1,340	284	2,394
Investment contracts				
Risk and Savings				
– Participating	3	308	4	237
– Non-participating	247	2,221	288	3,253
Core retail investments (including France)	32	3,489	41	1,942
Investment management	1	33,283	1	33,090
Total new business	531	41,858	619	41,771

1. Risk annuity new business includes those premiums written in the with-profits fund of £17m (2008: £27m). For segmental profit reporting these contracts are incorporated with all other with-profits business in the Savings segment on the basis of materiality.
2. Core retail investments excludes institutional investments which are disclosed with segregated property, property partnerships, private equity partnerships and institutional clients funds which are disclosed as part of institutional fund management. Other funds comprise new business from Legal & General Investment Management (2009: £2,464m; 2008: £3,249m) and from Legal & General Retail Investments (2009: £1,799m; 2008: £2,218m).
3. Excludes £7.9bn (2008: £7.4bn) which is held on a temporary basis, generally as part of portfolio reconstructions.

The UK pooled managed funds of £25.6bn (2008: £26.7bn) reported above are classified as fund management contracts. The increase in the fair value of the investment contract liabilities is shown in the income statement. There are three classes of new business for conventional individual protection where there is a material difference between gross and net of reinsurance annualised new business premiums: term assurance, which is 53.7% reinsured (2008: 52.9%); whole of life assurance, which is 12.4% reinsured (2008: 2.5%); and income protection, which is 39.1% reinsured (2008: 28.4%).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

5 INVESTMENT RETURN

	2009 £m	2008 £m
Financial investment return[1]	**37,905**	(36,603)
Property investment return[2]	**296**	(1,146)
Investment return	**38,201**	(37,749)

1. Financial investment return includes fair value gains and losses, excluding fair value movements attributable to AFS investments, dividends and interest. Net gains/(losses) (excluding interest and dividend income) of £27,303m (2008: £(46,072)m) arose on financial investments designated as FVTPL and £1,851m (2008: £(866)m) arose on derivative contracts classified as HFT. Interest income of £93m (2008: £77m) arose on financial investments designated as AFS. There were no impairments on assets classified as AFS during the year (2008: £17m). Investment income of £144m (2008: £545m) arose on loans and receivables.
2. Property investment return includes £283m (2008: £294m) of rental income.

6 NET CLAIMS AND CHANGE IN INSURANCE LIABILITIES

From continuing operations	Long term insurance 2009 £m	General insurance 2009 £m	Total 2009 £m	Long term insurance 2008 £m	General insurance 2008 £m	Total 2008 £m
Claims paid						
– gross	**4,359**	**178**	**4,537**	4,429	235	4,664
– reinsurance recoveries	**(419)**	**(2)**	**(421)**	(406)	(7)	(413)
	3,940	**176**	**4,116**	4,023	228	4,251
Change in insurance liabilities						
– gross	**3,096**	**(19)**	**3,077**	(1,333)	(44)	(1,377)
– reinsurance recoveries	**(100)**	**1**	**(99)**	(182)	8	(174)
Net claims and change in insurance liabilities	**6,936**	**158**	**7,094**	2,508	192	2,700

The roll-forward of the insurance contract liabilities is provided in Note 30.

7 AUDITORS' REMUNERATION

	2009 £m	2008 £m
Remuneration receivable by the Company's auditor for the audit of the consolidated and Company financial statements	**1.5**	1.6
Remuneration receivable by the Company's auditor and its associates for the supply of other services to the Company and its associates, including remuneration for the audit of the financial statements of the Company's subsidiaries:		
Audit of the Company's subsidiaries, pursuant to legislation	**2.0**	1.9
	3.5	3.5
Other services supplied pursuant to legislation	**0.6**	0.5
Tax services	**0.7**	0.4
Other services not covered above	**0.8**	1.5
Total remuneration	**5.6**	5.9

The 2008 comparatives include final fees billed in respect of the 2008 audit.

In addition to the above, fees payable to the Company's auditor and its associates for audit services supplied to the Company's associated pension schemes amounted to £nil (2008: £nil).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

8 EMPLOYEE INFORMATION

	2009	2008
Average number of staff employed during the year:		
UK	**8,143**	8,999
Europe	**380**	360
USA	**417**	418
Total excluding consolidated private equity investment vehicles	**8,940**	9,777
Consolidated private equity investment vehicles[1]	**384**	–
Worldwide employees	**9,324**	9,777

	Notes	2009 £m	2008 £m
Salaries		**310**	330
Social security costs		**38**	39
Share-based incentive awards		**20**	23
Defined benefit pension costs	36	**62**	58
Defined contribution pension costs	36	**34**	25
Total excluding consolidated private equity investment vehicles		**464**	475
Consolidated private equity investment vehicles[1]		**8**	–
		472	475

1. The private equity investment vehicle is controlled by virtue of a 100% holding owned by the with-profits part of the LTF. The £8m costs of employment for private equity investment subsidiaries in 2009 primarily comprise wages and salaries.

9 PROFIT BEFORE INCOME TAX

	Notes	2009 £m	2008 £m
The following items have been included in arriving at profit before income tax:			
– Depreciation on plant and equipment	17	**(19)**	(23)
– Amortisation of purchased interest in long term businesses and other intangibles	22	**(66)**	(30)
– Operating lease rentals		**(24)**	(24)
– Reinsurance commissions		**11**	10
– Direct operating expenses arising from investment properties which generate rental income		**(34)**	(19)
– Redundancy costs		**(26)**	–

During the year, the Group entered into prospective reinsurance arrangements which resulted in a profit of £142m (2008: £130m). This profit has been reflected in the consolidated income statement for the year.

10 FOREIGN EXCHANGE AND EXCHANGE RATES

Profit for the year includes foreign exchange gains on financial instruments. The gain for the year also includes foreign exchange losses of £10m (2008: gains of £11m) arising on conversion of monetary assets and liabilities to functional currencies.

Principal rates of exchange used for translation are:

	01.01.09-31.12.09 Average	2009 Year end	01.01.08-31.12.08 Average	2008 Year end
US Dollar	**1.57**	**1.62**	1.85	1.44
Euro	**1.12**	**1.13**	1.26	1.03

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

11 INCOME TAX EXPENSE/(CREDIT)

	2009 £m	2008 £m
Current tax		
– Current tax for the year	**112**	103
– Adjustments in respect of prior years	**(8)**	1
Total current tax	**104**	104
Deferred tax		
– Origination and reversal of temporary differences	**291**	(1,127)
Total income tax expense/(credit)	**395**	(1,023)
Represented by:		
Income tax expense/(credit) attributable to policyholder returns	**165**	(662)
Income tax expense/(credit) attributable to equity holders	**230**	(361)
Total income tax expense/(credit)	**395**	(1,023)

The Group uses estimates to apportion the income tax expense of Society between the elements attributable to policyholder returns and equity holders' profits. The net equity holders' profit from UK long term business has borne tax at the effective equity holder tax rate. For participating business and certain non profit business this is sufficiently close to the standard rate of UK corporation tax for that rate to be used in the financial statements. For the remaining non profit business, the effective equity holder tax rate is used. For equity holders' funds within Society's LTF, the equity holder income tax is the income tax attributed to the return on those funds. The balance of income taxes associated with UK long term business profits is then classified as income tax attributable to policyholders' returns.

There is no definitive method of calculating the effective equity holder tax rate. A number of alternative methods are consistently used in order to assess the validity of using the standard rate of UK corporation tax.

The tax assessed for the year is higher (2008: lower) than the standard corporation tax rate applicable to companies operating in the UK of 28% (2008: 28.5%). The differences are explained below:

	2009 £m	2008 £m
Income tax expense/(credit) calculated at standard UK corporation tax rate	**347**	(614)
Effects of:		
Income tax expense/(credit) relating to policyholder returns	**119**	(474)
Disallowable expenditure	**–**	5
Non taxable income including dividends	**(4)**	(15)
Adjustments in respect of prior years	**(8)**	1
Differences between taxable and accounting investment gains/losses	**(36)**	7
Difference between taxable and accounting acquisition costs	**–**	(6)
Unrelieved tax losses	**–**	47
Overseas tax	**7**	6
No tax in respect of property losses attributable to minority interests	**5**	18
(Lower)/higher tax on Shareholder Retained Capital (SRC) investment return	**(33)**	2
Difference between tax relief and accounting expense for share releases and option exercises	**1**	(1)
Reduction in UK corporate tax rate	**–**	3
Other	**(3)**	(2)
Total income tax expense/(credit)	**395**	(1,023)

	2009 £m	2008 £m
Deferred tax recognised directly in equity		
Relating to net gains or losses recognised directly in equity	**(25)**	(19)
Exchange (losses)/gains	**(29)**	77
Deferred tax recognised directly in equity	**(54)**	58

A surplus of £469m has been declared in the period by Society's LTF, which represents the full balance of the SRC. As such, no deferred tax liability exists at the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

12 DIVIDENDS AND OTHER DISTRIBUTIONS

	Per share 2009 p	Total 2009 £m	Per share 2008 p	Total 2008 £m
Ordinary share dividends paid in the year				
– Prior year final dividend	**2.05**	**120**	4.10	248
– Current year interim dividend	**1.11**	**65**	2.01	119
	3.16	**185**	6.11	367
Ordinary share dividend proposed[1]	**2.73**	**160**	2.05	120

1. The proposed current year dividend has not been included as a liability in the balance sheet.

13 EARNINGS PER SHARE

Earnings per share have been calculated using the weighted average number of ordinary shares in issue and the profits/(losses) for the financial year. Reconciliations of the earnings and weighted average numbers of shares used in the calculations are set out below:

Based on profit/(loss) attributable to equity holders

	Profit after tax 2009 £m	Number of shares[1] 2009 m	Earnings per share 2009 p	Loss after tax 2008 £m	Number of shares[1] 2008 m	Earnings per share 2008 p
Profit/(loss) attributable to equity holders of the Company	**863**	**5,824**	**14.82**	(1,067)	5,968	(17.88)
Net shares under options allocable for no further consideration[2]	**–**	**33**	**(0.09)**	–	22	–
Diluted earnings per share	**863**	**5,857**	**14.73**	(1,067)	5,990	(17.88)

1. Weighted average number of shares.
2. At 31 December 2008, net shares under options allocable for no further consideration were anti-dilutive and were therefore excluded from the diluted earnings per share calculation.

The number of shares in issue at 31 December 2009 was 5,862,216,780 (2008: 5,861,627,994).

14 DISCLOSURE OF TAX EFFECTS RELATING TO EACH COMPONENT OF OTHER COMPREHENSIVE INCOME

	Before tax 2009 £m	Tax credit/ (expense) 2009 £m	After tax 2009 £m	Before tax 2008 £m	Tax (expense)/ credit 2008 £m	After tax 2008 £m
Exchange differences on translation of overseas operations	**(63)**	**–**	**(63)**	139	–	139
Actuarial (losses)/gains on defined benefit pension schemes	**(213)**	**59**	**(154)**	26	(8)	18
Actuarial losses/(gains) on defined benefit pension schemes transferred to unallocated divisible surplus	**86**	**(24)**	**62**	(11)	3	(8)
Net change in financial investments designated as available-for-sale	**101**	**(35)**	**66**	(83)	27	(56)
Other comprehensive income	**(89)**	**–**	**(89)**	71	22	93

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

15 SHARE-BASED PAYMENTS

The fair values of the share grants made during the year have been calculated using the following assumptions:

	SAYE	SAYE	PSP	PSP
Award date	**20 Apr 09**	**17 Sep 09**	**6 May 09**	**16 Oct 09**
Weighted average share price	**49p**	**75p**	**65p**	**86p**
Weighted average exercise price	**36p**	**56p**	**n/a**	**n/a**
Expected volatility	**45%**	**45%**	**n/a**	**n/a**
Expected life	**3 – 7 years**	**3 – 7 years**	**3 years**	**3 years**
Risk free investment rate	**2.2 – 2.7%**	**2.1 – 3.2%**	**n/a**	**n/a**
Dividend yield	**7.0%**	**4.2%**	**n/a**	**n/a**

Expected volatility is a measure of the tendency of a security price to fluctuate in a random, unpredictable manner. Expected volatility is determined by calculating the historical volatility of the Group's share price over the previous ten years. The expected life has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

The Group provides the following equity settled share-based long term incentive plans for directors and eligible employees:

Savings related share option scheme (SAYE)

The SAYE allows employees to enter into a regular savings contract over either three, five or seven years, coupled with a corresponding option over shares of the Group. The grant price is equal to 80% of the quoted market price of the Group shares on the invitation date. Options are normally forfeited if the employee leaves the Group.

	Options 2009	Weighted average exercise price 2009 p	Options 2008	Weighted average exercise price 2008 p
Outstanding at 1 January	**29,189,645**	**90**	36,140,337	82
Granted during the year	**89,516,287**	**37**	24,847,859	92
Forfeited during the year	**(24,932,172)**	**84**	(1,367,401)	97
Exercised during the year	**(568,786)**	**49**	(14,557,902)	60
Expired during the year	**(2,963,195)**	**84**	(15,873,248)	102
Outstanding at 31 December	**90,241,779**	**39**	29,189,645	90
Exercisable at 31 December	**754,593**	**94**	763,190	88

The fair values of the SAYE options granted during the year have been estimated using the Black-Scholes model. The assumptions used in the model are shown above. The weighted average fair value of each SAYE option granted during the year was 14p (2008: 29p). The Group recognised total expenses of £3m (2008: £2m) relating to the SAYE scheme. The intrinsic value of vested SAYE options was £nil (2008: £nil) at the year end. Intrinsic value of a share option is calculated as the current share price less the option price. The options outstanding at 31 December 2009 had a weighted average remaining contractual life of 4 years.

Company share option scheme (CSOP)/Executive share option scheme (ESOS)

The CSOP, approved by HM Revenue & Customs (HMRC), and unapproved ESOS were designed to provide a long term incentive to directors and managers of the Group. The number of options granted is based on the manager's level, salary and performance. The options have a ten year life but do not normally vest in the first three years. In order to exercise the options, the Legal & General Total Shareholder Return (TSR) must exceed the median TSR of the FTSE 100 for a period of at least three years commencing on the date of the grant. Options are normally forfeited if the employee leaves the Group.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

15 SHARE-BASED PAYMENTS (CONTINUED)

Company share option scheme (CSOP)/Executive share option scheme (ESOS) (continued)

	Options 2009	Weighted average exercise price 2009 p	Options 2008	Weighted average exercise price 2008 p
Outstanding at 1 January	**34,441,666**	**139**	38,365,089	138
Granted during the year	**–**	**–**	–	–
Forfeited during the year	**(5,246,662)**	**145**	(2,911,495)	146
Exercised during the year	**(20,000)**	**78**	(640,846)	86
Expired during the year	**(3,643,965)**	**160**	(371,082)	149
Outstanding at 31 December	**25,531,039**	**134**	34,441,666	139
Exercisable at 31 December	**25,531,039**	**134**	34,441,666	139

The fair values of the options granted under the CSOP/ESOS are estimated using a binomial model, reflecting the historic exercise patterns. The assumptions used in the model are disclosed on page 111. No options have been granted since 2004 under these schemes.

The Group recognised total expenses of £nil (2008: £nil) related to the CSOP and ESOS. The intrinsic value of vested share options at the year end was £nil (2008: £nil). The options outstanding at 31 December 2009 had a weighted average remaining contractual life of 2 years.

Share bonus plan (SBP)

SBP grants restricted shares which vest with employees three years after the grant date; recipients are entitled to both vote and receive dividends. The rights associated with SBP grants are normally forfeited on leaving the Group.

The fair value of the shares awarded has been calculated as the market value on the grant date.

During the year, 14,546,572 shares (2008: 9,512,807 shares) were awarded under the SBP. The weighted average fair value of the shares issued was 60p (2008: 124p). The Group recognised a total expense of £8m (2008: £11m) relating to the SBP.

Performance share plan (PSP)

Conditional shares can be granted to top managers under the PSP, based upon individual and Company performance. Under the PSP, the number of performance shares transferred to the individual at the end of the three year vesting period is dependent on the Group's relative TSR. The award will vest in full for upper quintile performance. One quarter of the award will vest for median performance. Awards will vest on a straight line prorated basis for performance between the median and upper quintile.

For awards made prior to 2008, the performance condition is based upon the FTSE 100. For awards made during or after 2008, half of each award will be measured using the existing FTSE 100 test, the remaining half is measured against a bespoke group of UK and European insurance companies. The group comprises all UK-listed life insurers that are constituents of the FTSE 350, plus all members of the insurance sector of the FTSE Eurotop 300. The two halves are measured independently, thus it is possible that one half may vest, whilst the other does not.

For both comparator groups, the companies used are members of the relevant indices as at the date of award.

Additionally, the Remuneration Committee assesses whether the underlying performance of the Company is reflective of the TSR result. In exceptional circumstances, the Remuneration Committee may exercise their discretion to scale back the vesting of awards, if it is felt that the Company's performance did not justify the level of vesting. The parameters which the Remuneration Committee use in making this assessment include market share, partnerships gained and maintained, cost constraint, capital management and shareholder perception.

During the year, 14,819,263 performance shares (2008: 2,036,380) were awarded. The weighted average fair value of each award issued was 41p (2008: 232p). The Group recognised a total expense of £4m (2008: £5m) relating to the PSP during the year.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Employee share plan (ESP)

Under the ESP, approved by HMRC, permanent UK employees may elect to purchase Group shares from the market at the prevailing market price on a monthly basis. The Group supplements the number of shares purchased by matching the first £20 of the employees' contributions. From time to time, the Group may make a grant of free shares. Both the free and matching shares must be held in trust for three years before they may vest to the employee. After vesting the shares remain within the Trust until they are transferred to the employee or the employee leaves the Group. The Trust is consolidated into the results of the Group with the unvested shares disclosed as employee scheme shares.

The fair value of the granted shares is equal to the market value at the grant date.

During the year, 1,526,549 shares (2008: 4,329,878 shares) were granted under the ESP. The weighted average fair value of the shares issued was 60p (2008: 117p). The Group recognised a total expense of £5m (2008: £5m) relating to the ESP during the year.

Total recognised expense

The total recognised expense relating to share-based payments in 2009 was £20m (2008: £23m) before tax, all of which related to equity settled share schemes.

Total options

Options over 115,772,818 shares are outstanding under CSOP, ESOS and SAYE at 31 December 2009 as shown below:

Option price pence per share	Number of shares	Option period ending in	Option price pence per share	Number of shares	Option period ending in
30.01 – 40.00	**80,497,865**	**2012 – 2016**	**100.01 – 110.00**	**1,180,480**	**2010 – 2015**
40.01 – 50.00	**–**	**–**	**110.01 – 120.00**	**680,824**	**2010 – 2014**
50.01 – 60.00	**6,626,981**	**2010 – 2017**	**120.01 – 130.00**	**28,631**	**2010**
60.01 – 70.00	**–**	**–**	**130.01 – 140.00**	**–**	**–**
70.01 – 80.00	**5,181,247**	**2010 – 2013**	**140.01 – 150.00**	**12,887,532**	**2011 – 2012**
80.01 – 90.00	**784,283**	**2010 – 2016**	**150.01 – 160.00**	**5,744,462**	**2010**
90.01 – 100.00	**2,160,513**	**2010 – 2015**	**160.01 – 170.00**	**–**	**–**

16 ACQUISITIONS

Company name	Date of acquisition	Cash paid £m	Transaction costs £m	Total cost £m	Total net assets acquired £m
Nationwide Life Limited	31/01/08	250	2	252	252
Nationwide Unit Trust Managers Limited	31/01/08	49	1	50	50
Suffolk Life Group Plc	06/05/08	62	1	63	63

On 31 January 2008, the Group acquired 100% of the shares of Nationwide Life Limited and Nationwide Unit Trust Managers Limited. In addition, on 6 May 2008 the Group acquired 100% of the shares of Suffolk Life Group Plc. The total cost of these acquisitions was £365m. Full details are provided in the 2008 full year financial statements.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

17 PLANT AND EQUIPMENT

	2009 £m	2008 £m
Cost		
As at 1 January	**156**	147
Additions	**10**	18
Disposals	**(19)**	(9)
As at 31 December	**147**	156
Depreciation		
As at 1 January	**81**	68
Provided during the year	**19**	23
Disposals	**(14)**	(10)
As at 31 December	**86**	81
Net book value at 31 December	**61**	75

18 INVESTMENT PROPERTY

	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Unit linked 2009 £m	Total 2009 £m
Fair value at 1 January	**188**	**–**	**1,632**	**2,149**	**3,969**
Additions	**11**	**–**	**133**	**533**	**677**
Improvements	**–**	**–**	**3**	**1**	**4**
Disposals	**(63)**	**–**	**(479)**	**(294)**	**(836)**
Fair value gain/(loss)	**3**	**–**	**48**	**(25)**	**26**
Exchange revaluation	**(1)**	**–**	**–**	**–**	**(1)**
Fair value at 31 December	**138**	**–**	**1,337**	**2,364**	**3,839**

	Notes	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Fair value at 1 January		408	27	2,638	2,896	5,969
Additions		11	–	1	127	139
Improvements		2	–	85	18	105
Disposals		(58)	(27)	(485)	(515)	(1,085)
Fair value loss		(177)	–	(607)	(880)	(1,664)
Exchange revaluation		2	–	–	–	2
Acquisitions	16	–	–	–	503	503
Fair value at 31 December		188	–	1,632	2,149	3,969

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

19 FINANCIAL INVESTMENTS

	Notes	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Unit linked 2009 £m	Total 2009 £m
Financial investments at fair value designated as:						
Fair value through profit or loss		**2,938**	**21,628**	**16,546**	**227,845**	**268,957**
Available-for-sale		**1,862**	**–**	**–**	**5**	**1,867**
Held for trading		**257**	**1,269**	**63**	**2,160**	**3,749**
Financial investments at fair value	(i)	**5,057**	**22,897**	**16,609**	**230,010**	**274,573**
Loans and receivables	(ii)	**130**	**1**	**296**	**1,016**	**1,443**
Total financial investments		**5,187**	**22,898**	**16,905**	**231,026**	**276,016**
Expected to be settled within 12 months						**47,187**
Expected to be settled after 12 months						**228,829**

	Notes	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Financial investments at fair value designated as:						
Fair value through profit or loss		3,305	17,995	15,593	187,718	224,611
Available-for-sale		1,896	–	–	5	1,901
Held for trading		304	1,994	40	3,764	6,102
Financial investments at fair value	(i)	5,505	19,989	15,633	191,487	232,614
Loans and receivables	(ii)	98	–	282	1,520	1,900
Total financial investments		5,603	19,989	15,915	193,007	234,514
Expected to be settled within 12 months						40,742
Expected to be settled after 12 months						193,772

Investment risks on unit linked assets are borne by the policyholders. The remaining risks are outlined in the risk management note (see Note 48).

Financial investments include £714m (2008: £690m) of debt securities pledged as collateral against derivative liabilities. The assets used as collateral are Treasury Gilts, Foreign Government Bonds, AAA Supranational Bonds, and AAA, AA and BBB rated bonds (2008: Treasury Gilts, AAA Supranational Bonds, and AAA and AA rated bonds) having a residual maturity of over 18 years (2008: over 16 years). The Group is entitled to receive all of the cash flows from the asset during the period when it is pledged as collateral. Further, there is no obligation to pay or transfer these cash flows to another entity. The Group 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 agreement are met.

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. Assets in excess of the insurance and investment contract liabilities have been classified as expected to be settled after 12 months.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

19 FINANCIAL INVESTMENTS (CONTINUED)
(i) Financial investments at fair value

	Notes	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Unit linked 2009 £m	Total 2009 £m
Equity securities		**856**	**–**	**4,461**	**140,308**	**145,625**
Debt securities		**3,897**	**21,264**	**11,838**	**86,512**	**123,511**
Accrued interest		**47**	**364**	**247**	**1,030**	**1,688**
Derivative assets	20	**257**	**1,269**	**63**	**2,160**	**3,749**
Total investments at fair value		**5,057**	**22,897**	**16,609**	**230,010**	**274,573**

	Notes	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Equity securities		1,317	69	4,121	107,357	112,864
Debt securities		3,827	17,591	11,195	79,400	112,013
Accrued interest		56	335	251	965	1,607
Derivative assets	20	305	1,994	66	3,765	6,130
Total investments at fair value		5,505	19,989	15,633	191,487	232,614

Private equity investments are included within equity securities. A gain of £10m (2008: loss of £19m) has been recognised in the income statement in respect of the movement in fair value of these investments.

Property investments which are held via partnerships or unit trust vehicles are also included within equity securities. A loss of £3m (2008: loss of £9m) has been recognised in the income statement in respect of the movement in fair value of these investments.

Included within unit linked equity securities are £172m (2008: £172m) of debt instruments which incorporate an embedded derivative linked to the value of the Group's share price.

CDOs
The Group holds collateralised debt obligations (CDOs) with a market value of £1,212m at 2009 (2008: £1,004m).

These holdings include £108m (2008: £126m) in traded CDOs and £41m (2008: £34m) exposure to an equity tranche of a bespoke CDO.

The balance of £1,063m (2008: £844m) relates to a further four CDOs that were constructed in 2007 and 2008 in accordance with terms specified by Legal & General as part of a strategic review of the assets backing the annuity portfolio. These CDOs mature in 2017 and 2018. The Group selected at outset and manages the reference portfolios underlying the CDOs to give exposure to globally diversified portfolios of investment grade corporate bonds. The Group is able to substitute the constituents of the original reference portfolios with new reference assets, allowing the management of the underlying credit risk although substitutions in 2009 were limited. A breakdown of the underlying CDO reference portfolio by sector is provided below:

Sector	2009 %	2008 %
Technology & Telecoms	**9**	9
Oil & Gas	**6**	6
Utilities	**10**	10
Insurance	**6**	6
Industrials	**20**	20
Health Care	**3**	3
Financial Services	**6**	6
Banks	**14**	13
Consumer Services & Goods	**26**	27
	100	100

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The CDOs are termed as super senior since default losses on the reference portfolio have to exceed 27%, on average across the four CDOs, before the CDOs incur any default losses. Assuming an average recovery rate of 30%, then over 39% of the reference names would have to default before the CDOs incur any default losses.

Beyond 27% of default losses on the reference portfolio, losses to the CDO would occur at a rate that is a multiple of the loss rate on the reference portfolio. For illustration a £200m loss could be incurred if default losses to the reference portfolios exceeded 30% or if 43% of the names in the diversified global investment grade portfolio defaulted, with an average 30% recovery rate. (All figures are averages across the four CDOs.)

Despite the difficult financial conditions in early 2009, the underlying reference portfolio has had no reference entity defaults in 2009.

Losses are limited under the terms of the CDOs to assets and collateral invested.

These CDOs also incorporate features under which, in certain circumstances, the Group can choose either to post additional cash collateral or to allow wind up of the structures. These features are dependent on the portfolios' weighted average spreads, default experience to date and time to maturity. No additional collateral was posted to any of the CDOs in 2009 (2008: £155m).

These CDOs are valued using an internal valuation which is based on observable market inputs. This is then validated against the counterparty valuation and, at the year end, validated by independent external consultants.

For the purposes of valuing the non profit annuity regulatory and IFRS liabilities, the yield on the CDOs is included within the calculation of the yield used to calculate the valuation discount rate for the annuity liabilities. An allowance for the risks, including default, is also made. For EEV purposes, the yield on the CDOs, reduced by the realistic default assumption, is similarly included in assumed future investment returns.

(ii) Loans and receivables

	Shareholder 2009 £m	**Non profit non-unit linked 2009 £m**	**With-profits 2009 £m**	**Unit linked 2009 £m**	**Total 2009 £m**
Deposits with credit institutions	**50**	**1**	**295**	**1,016**	**1,362**
Policy loans	**75**	**–**	**–**	**–**	**75**
Other loans	**5**	**–**	**1**	**–**	**6**
Total loans and receivables	**130**	**1**	**296**	**1,016**	**1,443**

	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Deposits with credit institutions	11	–	107	1,520	1,638
Policy loans	62	–	23	–	85
Other loans	25	–	152	–	177
Total loans and receivables	98	–	282	1,520	1,900

There are no material differences between the carrying values reflected above and the fair value of these loans.

(iii) Fair value hierarchy

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable willing parties in an arm's length transaction.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

19 FINANCIAL INVESTMENTS (CONTINUED)

(iii) Fair value hierarchy (continued)

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 Group's assets by IFRS 7 hierarchy levels:

	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
Shareholder					
Equity securities	856	654	99	103	–
Debt securities	3,897	950	2,932	15	–
Accrued interest	47	18	29	–	–
Derivative assets	257	2	255	–	–
Loans and receivables	130	–	–	–	130
Non profit non-unit linked					
Debt securities	21,264	945	20,319	–	–
Accrued interest	364	10	354	–	–
Derivative assets	1,269	46	1,223	–	–
Loans and receivables	1	–	–	–	1
With-profits					
Equity securities	4,461	3,966	2	493	–
Debt securities	11,838	3,930	7,908	–	–
Accrued interest	247	61	186	–	–
Derivative assets	63	5	58	–	–
Loans and receivables	296	–	–	–	296
Unit linked					
Equity securities	140,308	140,027	84	197	–
Debt securities	86,512	51,885	34,625	2	–
Accrued interest	1,030	355	675	–	–
Derivative assets	2,160	364	1,796	–	–
Loans and receivables	1,016	–	–	–	1,016
Total financial investments	276,016	203,218	70,545	810	1,443

In current market conditions, the liquidity of financial instruments is less than it has been in the past. All of the Group's level 2 assets have been valued using standard market pricing sources, such as iBoxx, IDC and Bloomberg except for bespoke CDO and swaps holdings (see below). In normal market conditions, we would consider these market prices to be observable market prices. However, following consultation with our pricing providers and a number of their contributing brokers, we have considered that these prices are not from a suitably active market and have prudently classified them as level 2.

Our holdings in bespoke CDOs and swaps are priced using industry standard internal models which utilise market assumptions. The CDO valuations have also been verified using externally provided prices. Accordingly, these assets have also been classified as level 2.

Level 3 assets, where internal models are used, represent a small proportion of assets to which shareholders are exposed and reflect unquoted equities including investments in private equity, property vehicles and suspended securities.

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 Group 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 Group has classified as level 3.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Group determines the fair values of certain financial assets and liabilities based on quoted market prices, where available. The Group 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 Group'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 Group'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 judgements regarding current economic conditions, liquidity discounts, currency, credit and interest rate risks, loss experience and other factors. These fair values are estimates and involve considerable uncertainty and variability as a result of the inputs selected and may differ significantly from the values that would have been used had a ready market existed, and the differences could be material. As a result, such calculated fair value estimates may not be realisable in an immediate sale or settlement of the instrument. In addition, changes in the underlying assumptions used in the fair value measurement technique could significantly affect these fair value estimates.

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

(a) Significant transfers between level 1 and level 2:

There have been no significant transfers between level 1 and level 2.

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

	Equity securities £m	Debt securities £m	Total £m
As at 1 January 2009	**743**	**20**	**763**
Total gains or losses for the period recognised:			
– in profit and loss	**(106)**	**1**	**(105)**
– in other comprehensive income	**–**	**1**	**1**
Purchases	**269**	**1**	**270**
Sales	**(113)**	**(6)**	**(119)**
As at 31 December 2009	**793**	**17**	**810**

There have been no significant transfers to or from level 3 during 2009.

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

As discussed above, the fair value 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 unobservable 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

19 FINANCIAL INVESTMENTS (CONTINUED)

Financial instruments	Main assumptions	Current fair value 2009 £m	Reasonably possible alternative assumptions: Increase in fair value 2009 £m	Reasonably possible alternative assumptions: Decrease in fair value 2009 £m
Assets				
Shareholder				
Private equity investment vehicles[1]	Price earnings multiple	**9**	**1**	**(1)**
Unquoted investments in property vehicles[2]	Property yield; occupancy	**94**	**10**	**(10)**
Asset backed securities	Cash flows; expected defaults	**15**	**9**	**(9)**
With-profits				
Private equity investment vehicles[1]	Price earnings multiple	**98**	**7**	**(7)**
Unquoted investments in property vehicles[2]	Property yield; occupancy	**395**	**40**	**(40)**
Unit linked				
Unquoted investments in property vehicles[2]	Property yield; occupancy	**193**	**15**	**(15)**
Suspended securities	Estimated recoverable amount	**6**	**–**	**–**
Total		**810**	**82**	**(82)**

1. Private equity investments are valued in accordance with the International Private Equity and Venture Capital Valuation Guidelines. Reasonably possible alternative valuations have been determined using alternative price earnings multiples.
2. Unquoted investments in property vehicles are valued by independent valuers on the basis of open market value as defined in the appraisal and valuation manual of the Royal Institute of Chartered Surveyors. Reasonably possible alternative valuations have been determined using alternative yield and occupancy assumption.

20 DERIVATIVE ASSETS AND LIABILITIES

	Contract/ notional amount 2009 £m	Fair values: Assets 2009 £m	Fair values: Liabilities[1] 2009 £m	Contract/ notional amount 2008 £m	Fair values: Assets 2008 £m	Fair values: Liabilities[1] 2008 £m
Shareholder derivatives:						
Interest rate contracts – fair value hedges	**600**	**68**	**–**	629	85	–
Interest rate contracts – held for trading	**1,684**	**24**	**80**	1,820	6	110
Forward foreign exchange contracts – net investment hedges	**733**	**10**	**–**	679	–	19
Forward foreign exchange contracts – held for trading	**531**	**138**	**1**	619	191	26
Equity/index derivatives – held for trading	**(46)**	**14**	**–**	(41)	12	1
Credit derivatives – held for trading	**179**	**3**	**6**	173	11	3
Total shareholder derivatives		**257**	**87**		305	159
Non profit non-unit linked derivatives:						
Interest rate contracts – held for trading	**21,783**	**654**	**962**	14,596	1,209	1,223
Forward foreign exchange contracts – held for trading	**–**	**38**	**160**	–	10	264
Equity/index derivatives – held for trading	**68**	**478**	**3**	50	716	–
Inflation swap contracts – held for trading	**5,913**	**70**	**152**	4,106	32	341
Credit derivatives – held for trading	**1,106**	**29**	**145**	1,855	27	392
Other derivatives – held for trading	**996**	**–**	**–**	–	–	–
Total non profit non-unit linked derivatives		**1,269**	**1,422**		1,994	2,220
With-profits derivatives:						
Interest rate contracts – held for trading	**952**	**35**	**42**	1,412	59	88
Forward foreign exchange contracts – held for trading	**–**	**3**	**6**	–	–	34
Equity/index derivatives – held for trading	**398**	**23**	**7**	(82)	7	3
Other derivatives – held for trading	**2**	**2**	**–**	–	–	–
Total with-profits derivatives		**63**	**55**		66	125
Unit linked derivatives:						
Interest rate contracts – held for trading	**20,322**	**663**	**706**	16,916	3,408	645
Forward foreign exchange contracts – held for trading	**–**	**339**	**341**	160	221	1,031
Equity/index derivatives – held for trading	**(650)**	**822**	**648**	419	25	2
Other derivatives – held for trading	**5**	**1**	**–**	–	1	–
Inflation rate contracts – held for trading	**13,275**	**335**	**318**	11,888	110	1,037
Total unit linked derivatives		**2,160**	**2,013**		3,765	2,715
Total derivative assets and liabilities		**3,749**	**3,577**		6,130	5,219

1. Derivative liabilities are reported in the balance sheet within Payables and other financial liabilities (see also Note 37).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

The contractual undiscounted cash flows in relation to non-unit linked derivatives have the following maturity profile. Unit linked derivatives have not been included as shareholders are not directly exposed to liquidity risks.

		Maturity profile of undiscounted cash flows					
As at 31 December 2009	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 derivatives**							
Derivative assets	257	884	223	623	1	–	1,731
Derivative liabilities	(87)	237	8	6	1	–	252
Non profit non-unit linked derivatives							
Derivative assets	1,269	3,063	1,777	3,933	3,201	3,785	15,759
Derivative liabilities	(1,422)	7,102	1,465	3,126	2,633	5,529	19,855
With-profits derivatives							
Derivative assets	63	289	93	84	28	4	498
Derivative liabilities	(55)	257	84	108	49	11	509
Total	25	11,832	3,650	7,880	5,913	9,329	38,604
Cash outflows **Shareholder derivatives**							
Derivative assets	257	(826)	(48)	(403)	–	–	(1,277)
Derivative liabilities	(87)	(284)	(183)	(78)	(1)	–	(546)
Non profit non-unit linked derivatives							
Derivative assets	1,269	(2,762)	(1,314)	(3,534)	(2,833)	(3,306)	(13,749)
Derivative liabilities	(1,422)	(7,464)	(1,905)	(4,155)	(2,844)	(4,520)	(20,888)
With-profits derivatives							
Derivative assets	63	(266)	(52)	(85)	(24)	(3)	(430)
Derivative liabilities	(55)	(271)	(122)	(111)	(54)	(13)	(571)
Total	25	(11,873)	(3,624)	(8,366)	(5,756)	(7,842)	(37,461)
Net shareholder derivatives cash flows		11	–	148	1	–	160
Net non profit non-unit linked derivatives cash flows		(61)	23	(630)	157	1,488	977
Net with-profits derivatives cash flows		9	3	(4)	(1)	(1)	6

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

20 DERIVATIVE ASSETS AND LIABILITIES (CONTINUED)

		Maturity profile of undiscounted cash flows					
As at 31 December 2008	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 derivatives**							
Derivative assets	305	40	151	642	–	–	833
Derivative liabilities	(159)	991	40	35	5	3	1,074
Non profit non-unit linked derivatives							
Derivative assets	1,994	416	791	1,787	1,746	3,961	8,701
Derivative liabilities	(2,220)	5,097	685	1,405	1,123	1,976	10,286
With-profits derivatives							
Derivative assets	66	40	79	110	40	10	279
Derivative liabilities	(125)	457	52	95	32	7	643
Total	(139)	7,041	1,798	4,074	2,946	5,957	21,816
Cash outflows **Shareholder derivatives**							
Derivative assets	305	(34)	(140)	(450)	–	–	(624)
Derivative liabilities	(159)	(1,040)	(48)	(28)	(9)	(5)	(1,130)
Non profit non-unit linked derivatives							
Derivative assets	1,994	(340)	(567)	(1,431)	(1,180)	(2,420)	(5,938)
Derivative liabilities	(2,220)	(5,494)	(1,251)	(1,939)	(1,542)	(2,540)	(12,766)
With-profits derivatives							
Derivative assets	66	(30)	(50)	(85)	(25)	(5)	(195)
Derivative liabilities	(125)	(507)	(87)	(126)	(58)	(14)	(792)
Total	(139)	(7,445)	(2,143)	(4,059)	(2,814)	(4,984)	(21,445)
Net shareholder derivatives cash flows		(43)	3	199	(4)	(2)	153
Net non profit non-unit linked derivatives cash flows		(321)	(342)	(178)	147	977	283
Net with-profits derivatives cash flows		(40)	(6)	(6)	(11)	(2)	(65)

Cash inflows and outflows are presented on a net basis where the Group is required to settle net or has a legally enforceable right of offset and the intention is to settle on a net basis.

Forward foreign exchange contracts – net investment hedges

The Group hedges part of the foreign exchange translation exposure on its net investment in its overseas subsidiaries, using forward foreign exchange contracts. It recognises the portion of the gain or loss which is determined to be an effective hedge through reserves within shareholders' equity, along with the gain or loss on translation of the foreign subsidiaries.

Interest rate swap contracts – fair value hedges

The Group uses interest rate swap contracts to hedge fixed rate loans in particular to hedge the movement in the fair value of a loan due to interest rates.

Fair value gains and losses arising from fair value hedging relationships are as follows:
Fair value losses of £21m arose on hedging instruments (2008: gains of £55m).
Fair value gains of £27m arose on the hedged item attributable to the hedged risk (2008: losses of £60m).

The total fair value gain on hedging instruments shown above excludes fair value gains arising from factors which are outside the designated hedging relationship of £5m (2008: losses of £20m).

Derivative contracts – held for trading

The Group uses certain derivative contracts which are effective hedges of economic exposures in accordance with the Group's risk management policy, but for various reasons are not designated within a formal hedge accounting relationship. Therefore, these contracts must be designated as held for trading, and gains and losses on these contracts are recognised immediately in the income statement.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

21 REINSURERS' SHARE OF CONTRACT LIABILITIES

	Notes	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Unit linked 2009 £m	Total 2009 £m
Reinsurers' share of:						
Insurance contract liabilities	30	**280**	**1,624**	**2**	**6**	**1,912**
Investment contract liabilities	31	**–**	**–**	**1**	**180**	**181**
Reinsurers' share of contract liabilities		**280**	**1,624**	**3**	**186**	**2,093**

	Notes	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Reinsurers' share of:						
Insurance contract liabilities	30	312	1,538	2	7	1,859
Investment contract liabilities	31	–	(1)	12	127	138
Reinsurers' share of contract liabilities		312	1,537	14	134	1,997

22 PURCHASED INTEREST IN LONG TERM BUSINESSES (PILTB) AND OTHER INTANGIBLE ASSETS

	PILTB insurance contracts 2009 £m	PILTB investment contracts 2009 £m	Other intangible assets 2009 £m	Total 2009 £m	PILTB insurance contracts 2008 £m	PILTB investment contracts 2008 £m	Other intangible assets 2008 £m	Total 2008 £m
Cost								
As at 1 January	**372**	**77**	**15**	**464**	173	–	–	173
Acquisition of subsidiaries	**–**	**–**	**–**	**–**	127	77	15	219
Net exchange difference	**(24)**	**–**	**–**	**(24)**	61	–	–	61
Other	**(13)**	**–**	**–**	**(13)**	11	–	–	11
As at 31 December	**335**	**77**	**15**	**427**	372	77	15	464
Amortisation								
As at 1 January	**(230)**	**(7)**	**–**	**(237)**	(154)	–	–	(154)
Amortisation for the year	**(55)**	**(10)**	**(1)**	**(66)**	(23)	(7)	–	(30)
Net exchange difference	**22**	**–**	**–**	**22**	(53)	–	–	(53)
As at 31 December	**(263)**	**(17)**	**(1)**	**(281)**	(230)	(7)	–	(237)
Net book value as at 31 December	**72**	**60**	**14**	**146**	142	70	15	227
To be amortised within 12 months				**21**				65
To be amortised after 12 months				**125**				162

The intangible assets above have finite useful economic lives.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

23 DEFERRED ACQUISITION COSTS

(i) Analysis of deferred acquisition

	Notes	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
Insurance contract deferred acquisition costs	(ii)	**983**	**(80)**	1,111	(90)
Investment contract deferred acquisition costs	(iii)	**974**	**–**	1,001	–
Deferred acquisition costs		**1,957**	**(80)**	2,112	(90)

(ii) Insurance contract deferred acquisition costs

	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January	**1,111**	**(90)**	734	(66)
Acquisition costs deferred	**147**	**(2)**	159	(1)
Amortisation charged to income	**(164)**	**7**	(142)	6
(Decrease)/increase due to currency translation	**(116)**	**10**	282	(25)
Other	**5**	**(5)**	78	(4)
As at 31 December	**983**	**(80)**	1,111	(90)
To be amortised within 12 months	**104**	**(3)**	118	(4)
To be amortised after 12 months	**879**	**(77)**	993	(86)

Of the total gross deferred acquisition costs, £907m (2008: £1,011m) relates to the US insurance business.

(iii) Investment contract deferred acquisition costs

	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January	**1,001**	**–**	962	–
Acquisition costs deferred	**157**	**–**	163	–
Amortisation charged to income	**(169)**	**–**	(95)	–
(Decrease)/increase due to currency translation	**(5)**	**–**	11	–
Other	**(10)**	**–**	(40)	–
As at 31 December	**974**	**–**	1,001	–
To be amortised within 12 months	**136**	**–**	138	–
To be amortised after 12 months	**838**	**–**	863	–

24 DEFERRED TAX ASSET/(LIABILITIES)

The deferred tax balances are as follows:

	As at 31 December 2009 £m	As at 31 December 2008 £m
Deferred tax liability arising in overseas entities	**(303)**	(259)
Deferred tax asset arising in UK entities	**796**	988
	493	729

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The movement in deferred tax asset/(liabilities) during the year is as follows:

	Net asset as at 31 December 2008 £m	(Charged)/ credited to the income statement £m	(Charged)/ credited to equity £m	Net asset as at 31 December 2009 £m
Unrealised gains and losses on investments and debt liabilities	**184**	**(215)**	**(34)**	**(65)**
Excess of depreciation over capital allowances	**41**	**1**	**–**	**42**
Temporary differences between the accounts and tax deduction for expenses	**71**	**(126)**	**28**	**(27)**
Temporary differences between the accounts and tax deduction for actuarial reserves	**(251)**	**54**	**20**	**(177)**
Tax losses carried forward	**685**	**(5)**	**(18)**	**662**
Temporary differences in relation to the pension fund deficit	**39**	**(19)**	**59**	**79**
Other temporary differences	**3**	**4**	**–**	**7**
Acquisition of Nationwide Life Limited, Nationwide Unit Trust Managers Limited and Suffolk Life Group Plc	**(43)**	**15**	**–**	**(28)**
Deferred tax asset/(liabilities)	**729**	**(291)**	**55**	**493**

	Net liability as at 31 December 2007 £m	Credited/ (charged) to the income statement £m	Credited/ (charged) to equity £m	Net asset as at 31 December 2008 £m
Unrealised gains and losses on investments and debt liabilities	(458)	624	18	184
Excess of depreciation over capital allowances	32	9	–	41
Temporary differences between the accounts and tax deduction for expenses	7	128	(64)	71
Temporary differences between the accounts and tax deduction for actuarial reserves	(163)	(66)	(22)	(251)
Tax losses carried forward	232	436	17	685
Temporary differences in relation to the pension fund deficit	51	(5)	(7)	39
Other temporary differences	3	–	–	3
	(296)	1,126	(58)	772
Acquisition of Nationwide Life Limited, Nationwide Unit Trust Managers Limited and Suffolk Life Group Plc	(44)	1	–	(43)
Deferred tax (liabilities)/asset	(340)	1,127	(58)	729

Included in the amounts credited/(charged) to income and equity in 2008 is £3m relating to the change in UK corporation tax rate from 30% to 28% in April 2008.

Following a change in UK tax law, all dividends paid on or after 1 July 2009 from L&G Group companies will be exempt from UK tax. No UK tax liability will therefore arise in respect of any remittance of earnings from overseas subsidiaries. As such, no deferred tax liability is recognised on these profits. Furthermore, it is expected that no foreign tax will arise on the earnings in the jurisdiction of the foreign entity upon distribution and as such no deferred tax has been provided in respect of foreign tax.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

24 DEFERRED TAX ASSET/(LIABILITIES) (CONTINUED)

Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

The Group has unrelieved trading losses carried forward as at 31 December 2009 of £25m (2008: £58m). No deferred tax asset has been recognised in respect of these losses as at 31 December 2009 (or 31 December 2008), as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these losses will only be obtained if it becomes probable that suitable profits will arise in future periods. The potential deferred tax asset unrecognised as at 31 December 2009 is £8m (2008: £17m).

The Group has unrelieved post-cessation trading losses carried forward as at 31 December 2009 of £15m (2008: £19m). No deferred tax asset has been recognised in respect of these losses as at 31 December 2009 (or 31 December 2008), as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these losses will only be obtained if it becomes probable that suitable post-cessation of trade profits will arise in future periods. The potential deferred tax asset unrecognised as at 31 December 2009 is £4m (2008: £5m).

The Group has surplus non-trading loan relationship deficits and management expenses carried forward as at 31 December 2009 of £17m (2008: £17m). No deferred tax asset has been recognised in respect of these deficits and expenses as at 31 December 2009 (or 31 December 2008), as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these deficits and expenses will only be obtained if it becomes probable that suitable profits will arise in future periods. The potential deferred tax asset unrecognised as at 31 December 2009 is £5m (2008: £5m).

The Group has capital losses carried forward as at 31 December 2009 of £77m (2008: £724m). No deferred tax asset has been recognised in respect of these losses as at 31 December 2009 (or 31 December 2008) as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these losses will only be obtained if it becomes probable that suitable profits will arise in future periods. The potential deferred tax asset unrecognised as at 31 December 2009 is £15m (2008: £155m).

25 INCOME TAX

	2009 £m	2008 £m
Due within 12 months	1	8
Due after 12 months	–	–
Income tax recoverable	**1**	8

	2009 £m	2008 £m
Due within 12 months	126	118
Due after 12 months	14	(113)
Income tax payable	**140**	5

At 31 December 2009, a partial provision is held for a dispute with HMRC relating to the basis of recognition of taxable profit within Society's LTF. The matter is being progressed through the Tax Tribunals Service. The maximum exposure in relation to this issue is £232m, plus interest of £98m.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

26 OTHER ASSETS

	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Unit linked 2009 £m	Total 2009 £m
Reinsurance receivables	35	9	–	–	44
Accrued interest and rent	2	7	41	82	132
Prepayments and accrued income	132	4	4	263	403
Other receivables	283	99	56	423	861
Other assets	452	119	101	768	1,440
Due within 12 months					1,418
Due after 12 months					22

	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Reinsurance receivables	35	2	–	–	37
Accrued interest and rent	2	–	36	101	139
Prepayments and accrued income	134	8	4	285	431
Other receivables	315	111	123	979	1,528
Other assets	486	121	163	1,365	2,135
Due within 12 months					2,098
Due after 12 months					37

27 CASH AND CASH EQUIVALENTS

	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Unit linked 2009 £m	Total 2009 £m
Cash at bank and in hand	199	98	62	1,153	1,512
Cash equivalents	1,382	484	1,271	6,001	9,138
Cash and cash equivalents	1,581	582	1,333	7,154	10,650

	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Unit linked 2008 £m	Total 2008 £m
Cash at bank and in hand	237	132	100	967	1,436
Cash equivalents	1,692	856	1,434	5,270	9,252
Cash and cash equivalents	1,929	988	1,534	6,237	10,688

Included within cash equivalents is £266m of collateral posted to CDOs which is not available for shareholder liquidity requirements.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

28 SHARE CAPITAL, SHARE PREMIUM AND EMPLOYEE SCHEME SHARES
(i) Share capital and share premium

Authorised share capital	2009 Number of shares	2009 £m	2008 £m
At 31 December: ordinary shares of 2.5p each	**9,200,000,000**	**230**	230

Issued share capital, fully paid	Notes	2009 Number of shares	Share capital £m	Share premium £m
As at 1 January 2009		**5,861,627,994**	**147**	**936**
Options exercised under share option schemes				
– Executive share option scheme	15	**20,000**	**–**	**–**
– Savings related share option scheme	15	**568,786**	**–**	**–**
As at 31 December 2009		**5,862,216,780**	**147**	**936**
As at 1 January 2008		6,296,321,160	157	927
Shares cancelled under share buyback programme[1]		(449,891,914)	(11)	–
Options exercised under share option schemes				
– Executive share option scheme	15	640,846	–	1
– Savings related share option scheme	15	14,557,902	1	8
As at 31 December 2008		5,861,627,994	147	936

1. During 2008, 449,891,914 shares were repurchased and cancelled under the share buyback programme representing 7.1% of opening issued share capital, at a cost of £523m including expenses.

There is one class of ordinary shares. All shares issued carry equal voting rights.

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

(ii) Employee scheme shares
The Group uses the Employee Share Ownership Trust (ESOT), Employee Share Trust (EST) and the Legal & General Group Employee Share Plan (ESP) to purchase and hold shares of the Group for delivery to employees under various employee share schemes. Shares owned by these vehicles are included at cost in the consolidated balance sheet and are shown as a deduction from shareholders' equity. They are disclosed as employee scheme shares until they vest to employees. Share-based liabilities to employees may also be settled via purchases directly from the market or by the issue of new shares.

The ESOT has waived its voting rights and its rights to some of the dividends payable on the shares it holds. Employees are entitled to dividends on the shares held on their behalf within the EST and the ESP.

	2009 Number of shares	2009 £m	2008 Number of shares	2008 £m
As at 1 January	**40,565,428**	**46**	38,176,859	42
Shares purchased	**3,140,535**	**2**	8,181,427	10
Shares vested	**(9,851,595)**	**(10)**	(5,792,858)	(6)
As at 31 December	**33,854,368**	**38**	40,565,428	46

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

29 MINORITY INTERESTS

Minority interests represent third party interests in property investment vehicles which are consolidated in the Group's results. The reduction in the minority interests in 2009 arises from the dilution of the Group's ownership of St Giles Limited Partnership and The Leisure Fund Limited Partnership, below 50%.

30 INSURANCE CONTRACT LIABILITIES

(i) Analysis of insurance contract liabilities

	Notes	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
Participating insurance contracts	(iii)	**9,404**	**(1)**	9,384	(1)
Non-participating insurance contracts[1]	(iv)	**28,353**	**(1,902)**	25,582	(1,847)
General insurance contracts	(v)	**230**	**(9)**	259	(11)
Insurance contract liabilities		**37,987**	**(1,912)**	35,225	(1,859)

1. Excluding General insurance contracts.

(ii) Expected insurance contract liability cash flows

	Date of undiscounted cash flow					
As at 31 December 2009	**0-5 years £m**	**5-15 years £m**	**15-25 years £m**	**Over 25 years £m**	**Total £m**	**Carrying value £m**
Participating insurance contracts	**5,807**	**3,949**	**1,152**	**462**	**11,370**	**9,404**
Non-participating insurance contracts	**8,450**	**14,047**	**12,128**	**15,026**	**49,651**	**19,029**
General insurance contracts[1]	**110**	**–**	**–**	**–**	**110**	**110**
Insurance contract liabilities	**14,367**	**17,996**	**13,280**	**15,488**	**61,131**	**28,543**

	Date of undiscounted cash flow					
As at 31 December 2008	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Life and pensions participating insurance contracts	5,849	3,757	867	326	10,799	9,384
Life and pensions non-participating insurance contracts	8,148	13,360	11,559	14,334	47,401	17,695
General insurance contracts[1]	128	–	–	–	128	128
Insurance contract liabilities	14,125	17,117	12,426	14,660	58,328	27,207

1. Excludes unearned premium reserve of £120m (2008: £131m) for which there are no cash flows.

Insurance contract undiscounted cash flows are based on the expected date of settlement.

Amounts under unit linked contracts are generally repayable on demand and the Group is responsible for ensuring there is sufficient liquidity within the asset portfolio to enable liabilities to unit linked policyholders to be met as they fall due. However, the terms of funds investing in less liquid assets permit the deferral of redemptions for predefined periods in circumstances where there are not sufficient liquid assets within the fund to meet the level of requested redemptions. Accordingly, unit linked liabilities have been excluded from the table.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 INSURANCE CONTRACT LIABILITIES (CONTINUED)
(iii) Movement in participating insurance contract liabilities

	Notes	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January		**9,384**	**(1)**	11,663	(1)
New liabilities in the year		**658**	**–**	333	–
Liabilities discharged in the year		**(1,157)**	**–**	(1,628)	–
Unwinding of discount rates		**92**	**–**	383	–
Effect of change in non-economic assumptions	34	**48**	**–**	58	–
Effect of change in economic assumptions	34	**430**	**–**	(1,348)	–
Other		**(51)**	**–**	(77)	–
As at 31 December		**9,404**	**(1)**	9,384	(1)
Expected to be settled within 12 months (net of reinsurance)		**1,366**		1,522	
Expected to be settled after 12 months (net of reinsurance)		**8,037**		7,861	

(iv) Movement in non-participating insurance contract liabilities

	Notes	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January		**25,582**	**(1,847)**	22,568	(1,302)
New liabilities in the year		**2,339**	**(312)**	3,020	(262)
Liabilities discharged in the year		**(2,004)**	**136**	(1,493)	79
Unwinding of discount rates		**1,233**	**(103)**	1,022	(88)
Effect of change in non-economic assumptions	34	**(319)**	**188**	(87)	121
Effect of change in economic assumptions[1]	34	**1,871**	**(2)**	(1,366)	(26)
Foreign exchange adjustments		**(363)**	**33**	946	(82)
Acquisitions		**–**	**–**	1,172	(286)
Other		**14**	**5**	(200)	(1)
As at 31 December		**28,353**	**(1,902)**	25,582	(1,847)
Expected to be settled within 12 months (net of reinsurance)		**1,927**		751	
Expected to be settled after 12 months (net of reinsurance)		**24,524**		22,984	

1. The economic assumptions changes in 2009 principally reflect the narrowing of credit spreads. Movements in credit spreads also increased the value of the corresponding backing assets.

In 2008, the Effect of changes in economic assumptions includes the impact arising from the prevailing interest rate environment and increased credit spreads reducing liabilities, partially offset by £650m of additional reserves for non profit annuity credit default.

(v) Analysis of General insurance contract liabilities

	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
Outstanding claims	**87**	**(3)**	99	(4)
Claims incurred but not reported	**23**	**–**	29	–
Unearned premiums	**120**	**(6)**	131	(7)
General insurance contract liabilities	**230**	**(9)**	259	(11)

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(vi) Movement in General insurance claim liabilities

	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January	**128**	**(4)**	172	(12)
Claims arising	**188**	**(1)**	231	(4)
Claims paid	**(177)**	**2**	(235)	6
Adjustments to prior year liabilities	**(29)**	**–**	(40)	6
As at 31 December	**110**	**(3)**	128	(4)
Expected to be settled within 12 months (net of reinsurance)	**79**		88	
Expected to be settled after 12 months (net of reinsurance)	**28**		36	

(vii) Unearned premiums

	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January	**131**	**(7)**	133	(7)
Earned in the period	**(131)**	**7**	(133)	7
Gross written premiums in respect of future periods	**120**	**(6)**	131	(7)
As at 31 December	**120**	**(6)**	131	(7)
Expected to be earned within 12 months (net of reinsurance)	**114**		124	
Expected to be earned after 12 months (net of reinsurance)	**–**		–	

(viii) Claims development – General insurance

Changes may occur in the amount of the Group's obligations at the end of a contract period. The top section of the following two tables illustrates how the estimate of total claims outstanding for each accident year developed over time. The bottom section of the tables reconciles the cumulative claims to the amount appearing in the balance sheet.

Gross of reinsurance

Accident year	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	Total £m
Estimate of ultimate claims costs:						
– At end of accident year	**209**	**205**	**294**	**191**	**164**	**1,063**
– One year later	**195**	**192**	**277**	**189**	**–**	**853**
– Two years later	**191**	**192**	**276**	**–**	**–**	**659**
– Three years later	**191**	**190**	**–**	**–**	**–**	**381**
– Four years later	**190**	**–**	**–**	**–**	**–**	**190**
Estimate of cumulative claims	**190**	**190**	**276**	**189**	**164**	**1,009**
Cumulative payments	**(185)**	**(183)**	**(271)**	**(176)**	**(90)**	**(905)**
Outstanding claims provision	**5**	**7**	**5**	**13**	**74**	**104**
Prior period outstanding claims						**2**
Claims handling provision						**4**
Total claims liabilities recognised in the balance sheet						**110**

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 INSURANCE CONTRACT LIABILITIES (CONTINUED)
(viii) Claims development – General insurance (continued)
Net of reinsurance

Accident year	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	Total £m
Estimate of ultimate claims costs:						
– At end of accident year	**205**	**200**	**280**	**189**	**162**	**1,036**
– One year later	**193**	**188**	**267**	**188**	**–**	**836**
– Two years later	**189**	**189**	**265**	**–**	**–**	**643**
– Three years later	**189**	**186**	**–**	**–**	**–**	**375**
– Four years later	**187**	**–**	**–**	**–**	**–**	**187**
Estimate of cumulative claims	**187**	**186**	**265**	**188**	**162**	**988**
Cumulative payments	**(184)**	**(180)**	**(262)**	**(176)**	**(89)**	**(891)**
Outstanding claims provision	**3**	**6**	**3**	**12**	**73**	**97**
Prior period outstanding claims						**7**
Claims handling provision						**3**
Total claims liabilities recognised in the balance sheet						**107**

31 INVESTMENT CONTRACT LIABILITIES
(i) Analysis of investment contract liabilities

	Notes	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
Participating investment contracts		**7,139**	**(1)**	6,992	(12)
Non-participating investment contracts	(iii)	**234,502**	**(180)**	196,698	(126)
Investment contract liabilities	(ii)	**241,641**	**(181)**	203,690	(138)
Expected to be settled within 12 months (net of reinsurance)		**43,675**		37,058	
Expected to be settled after 12 months (net of reinsurance)		**197,785**		166,494	

(ii) Movement in investment contract liabilities

	Gross 2009 £m	Reinsurance 2009 £m	Gross 2008 £m	Reinsurance 2008 £m
As at 1 January	**203,690**	**(138)**	232,368	(208)
Reserves in respect of new business	**37,618**	**(750)**	38,583	(741)
Amounts paid on surrenders and maturities during the year	**(32,382)**	**571**	(36,852)	504
Investment return and related benefits	**33,221**	**136**	(33,500)	307
Management charges	**(313)**	**–**	(378)	–
Foreign exchange adjustments	**(193)**	**–**	527	–
Acquisitions	**–**	**–**	2,942	–
As at 31 December	**241,641**	**(181)**	203,690	(138)

Fair value movements of £24,317m (2008: £32,743m) are included within the income statement arising from movements in investment contract liabilities designated as FVTPL.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

(iii) Non-participating investment contract liability fair value hierarchy

As at 31 December 2009	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
Non-participating investment contracts	**234,502**	**234,318**	**152**	**32**	**–**

The fair value of financial liabilities 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.

Non-participating unit linked investment contracts include £32m valued using significant unobservable inputs and have been classified as level 3. These liabilities have limited transactions and are backed by property investments.

There have been no significant transfers between any of the levels.

(iv) Expected investment contract liability cash flows

	Date of undiscounted cash flow					
As at 31 December 2009	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Participating investment contracts	**2,880**	**3,729**	**1,980**	**1,113**	**9,702**	**7,139**

	Date of undiscounted cash flow					
As at 31 December 2008	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Participating investment contracts	2,880	3,701	1,939	1,053	9,573	6,992

Investment contract undiscounted net cash flows are based on the expected date of settlement.

Amounts under unit linked contracts are generally repayable on demand and the Group is responsible for ensuring there is sufficient liquidity within the asset portfolio to enable liabilities to unit linked policyholders to be met as they fall due. However, the terms of funds investing in less liquid assets permit the deferral of redemptions for predefined periods in circumstances where there are not sufficient liquid assets within the fund to meet the level of requested redemptions. Accordingly unit linked liabilities have been excluded from the reported cash flows.

A maturity analysis based on the earliest contractual repayment date would present investment contract liabilities as due on the earliest period of the table because policyholders can exercise cancellation options at their discretion. In such a scenario, the liability would be reduced due to the application of surrender penalties.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

32 UNALLOCATED DIVISIBLE SURPLUS

	2009 £m	2008 £m
As at 1 January	**913**	1,721
Transferred from/(to) the income statement	**430**	(806)
Actuarial (losses)/gains on defined benefit pension schemes transferred from the statement of comprehensive income	**(62)**	8
Foreign exchange adjustments	**3**	(10)
As at 31 December	**1,284**	913

It is intended that the with-profits part of the LTF will be managed on the basis that it will remain open to new business and therefore there is no expectation of any distribution from the inherited estate.

33 VALUE OF IN-FORCE NON-PARTICIPATING CONTRACTS
(i) Movement in value of in-force non-participating contracts

	2009 £m	2008 £m
As at 1 January	**171**	276
Unwinding of the discount rates	**7**	14
Investment return	**193**	(149)
Other	**(4)**	30
As at 31 December	**367**	171
Expected to be settled within 12 months	**53**	17
Expected to be settled after 12 months	**314**	154

(ii) Expected net cash flows

	Date of undiscounted cash flow					
As at 31 December 2009	**0-5 years £m**	**5-15 years £m**	**15-25 years £m**	**Over 25 years £m**	**Total £m**	**Carrying value £m**
Value of in-force non-participating contracts	**250**	**224**	**108**	**57**	**639**	**367**

	Date of undiscounted cash flow					
As at 31 December 2008	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Value of in-force non-participating contracts	94	125	49	33	301	171

Value of in-force non-participating undiscounted net cash flows are based on the expected date of realisation.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

34 LONG TERM INSURANCE VALUATION ASSUMPTIONS

The Group's insurance assumptions, described below, relate exclusively to the UK insurance business. The non-UK businesses do not constitute a material component of the Group's operations and consideration of geographically determined assumptions is therefore not included.

Non-participating business

For its non-participating business the Group seeks to make prudent assumptions about its future experience based on current market conditions and recent experience. The approach used to set non-participating assumptions is generally similar to that used to determine the assumptions used for FSA statutory peak 1, although the actual assumptions may sometimes differ from those used for regulatory reporting purposes. These assumptions incorporate prudent margins in excess of our best estimate assumptions to reduce the possibility of actual experience being less favourable than assumed.

Valuation rates of interest and discount rates

The valuation interest rate for each contract type is based on the yield on the assets backing the contract adjusted for the risk that asset proceeds are not received by the Group. For some business, this yield is the gross redemption yield on fixed interest securities and the running yield on variable interest securities. For other business it is the Internal Rate of Return on the portfolio of backing assets.

In 2008 the Group established reserves to protect against a significant short term uplift in defaults. In 2009 the Group decided that it was prudent to have a short term uplift in default allowance and increase the long term default allowance to 36bps (2008: 30bps) per annum for unapproved securities backing non-profit business, 35bps (2008: 30bps) per annum for unapproved securities backing with-profits business, and to remain at 3bps per annum for approved securities and swaps. The total credit default allowances equate to £1.5bn, or 68bps per annum (2008: £1.2bn and 68bps repesctively) for unapproved securities backing non-profit annuity business when expressed over the duration of the assets held. A similar methodology has been used for assets backing with-profits business.

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

For equity investments, the yield is based on the current dividend yield, adjusted for prudence.
For property holdings, yields are based on the rental income payable calculated by considering different categories of tenant separately, adjusted for the possibility of default. Default rates used in the calculations vary by tenant category.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

34 LONG TERM INSURANCE VALUATION ASSUMPTIONS (CONTINUED)

Mortality and morbidity

Mortality and morbidity assumptions are set with reference to standard tables drawn up by the Continuous Mortality Investigation Bureau (CMIB) of the Institute and Faculty of Actuaries. These tables are based on industry-wide experience.

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

Persistency

The Group monitors its persistency experience and carries out detailed investigations annually. Persistency can be volatile and past experience may not be an appropriate future indicator.

The Group tries to balance past experience and future conditions by making prudent assumptions about the future expected long term average persistency levels.

For non-participating contracts where explicit persistency assumptions are not made, prudence is also incorporated into the liabilities by ensuring that they are sufficient to cover the more onerous of the two scenarios where the policies either remain in-force until maturity or where they discontinue at the valuation date.

Expenses

The Group 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. Adjustments may be made for known future changes in the administration processes, in line with the Group's business plan. An allowance for expense inflation in the future is also made, taking account of both salary and price information.

Participating business

For its participating business, the Group seeks to establish its liabilities at their realistic value in line with the requirements set out in FRS 27.

Non-economic assumptions are set to represent the Group's best estimates of future experience.

Economic assumptions

The FSA's realistic reporting regime requires a market consistent economic model. The model is calibrated using market data from a variety of market sources. This enables assumptions to be determined for the term structure of risk free interest rates, property and equity volatility. Risk free interest rates are determined with reference to the gilt yield curve on the valuation date increased by ten basis points.

Property volatility is set with reference to historic variations in property prices. Equity volatility is set so that the model reproduces observed market prices of traded equity derivatives. Correlations between asset classes are based on historic data.

Each investment scenario contains a consistent set of assumptions for investment returns and inflation.

Future bonuses

Future reversionary and terminal bonuses are consistent with the bonus policies set out in Society's Principles and Practices of Financial Management (PPFM).

Value of in-force non-participating contracts

The Group makes a deduction from the liabilities for the expected value of future profits arising on non-participating contracts written in the with-profits part of the Society LTF.

The economic assumptions used to calculate the value of these profits are consistent with those used to calculate liabilities for with-profits business, with the addition of a liquidity premium in respect of assets backing non-participating annuity business. Non-economic assumptions represent best estimates of expected future experience on this business.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Guaranteed annuity options
The guarantees are valued on a market consistent basis. The valuation methodology allows for the correlation between interest rates and the proportion of the policyholders who take up the option.

Guaranteed cash options
The liability is determined assuming that policyholders choose the most valuable alternative between the annuity and cash available at retirement.

The table below sets out the current valuation assumptions used to establish the long term liabilities for Society, Legal & General Pensions Limited (LGPL) and Legal & General Assurance (Pensions Management) Limited.

	2009	2008
Rate of interest/discount rates		
Non-participating business		
Life assurances	**2.25% pa and 7.60% pa[1]**	2.25% pa and 7.60% pa[1]
Pension assurances	**2.75 – 3.75% pa and 7.60% pa[1]**	2.50 – 3.75% pa and 7.60% pa[1]
Annuities in deferment	**5.49% pa**	6.50% pa
Annuities in deferment (RPI-linked; net rate after allowance for inflation)	**1.31% pa**	2.20% pa
Vested annuities	**5.05 – 5.49% pa**	5.54 – 6.50% pa
Vested annuities (RPI-linked; net rate after allowance for inflation)	**0.50 – 1.31% pa**	0.80 – 2.20% pa
Participating business		
Risk free rate (10 years)	**4.39% pa**	3.57% pa
Future bonuses	**Determined stochastically in line with bonus policy as stated in PPFM**	Determined stochastically in line with bonus policy as stated in PPFM
UK equity volatility (10 year option term)	**26.5%**	36.4%
Property volatility	**15.0%**	15.0%
Mortality tables		
Non-participating business		
Non-linked individual term assurances:		
Smokers	**105 – 114% TMS00/TFS00 Sel 5[2]**	109 – 123% TMS00/TFS00 Sel 5[2]
Non-smokers	**95 – 115% TMN00/TFN00 Sel 5[2]**	103 – 125% TMN00/TFN00 Sel 5[2]
Smoker status unknown	**129% TM00/TF00 Sel 5[2]**	138% TM00/TF00 Sel 5[2]
Non-linked individual term assurances with critical illness	**66 – 101% CIBT93M/F Ult Comb[2]**	66 – 99% CIBT93M/F Ult Comb[2]
Other non-linked non profit life assurances	**A67/70 suitably age adjusted[2]**	A67/70 suitably age adjusted[2]
Annuities in deferment	**67 - 70% AM92/AF92**	69 – 78% AM92/AF92
Vested annuities[3]		
Bulk purchase annuities	**90 – 94% PCMA00/PCFA00**	90 – 94% PCMA00/PCFA00
Other annuities	**60 – 88% PCMA00/PCFA00**	61 – 88% PCMA00/PCFA00

1. For product groups where liabilities are positive, the lower interest rate of 2.25% or 2.75 – 3.75% is used (2008: 2.25% or 2.50 – 3.75%). However, for product groups where liabilities are negative, the higher rate of 7.60% (2008: 7.60%) is used.
2. For term assurance with critical illness, morbidity rates are assumed to deteriorate at a rate of 0.50% pa for males and 0.75% pa for females (2008: 1.00% pa for males and 1.75% pa for females). An additional loading for guaranteed level term contracts of 0.85% multiplied by policy term less 5 years is applied. The corresponding loading for guaranteed decreasing term contracts is 0.65% multiplied by policy term less 5 years. No allowance is made for AIDS.
3. For vested annuities, mortality rates are assumed to reduce according to CMIB Working Paper 30 projection MC with a minimum of 2.0% (2008: 2.0%) pa up to age 90 tapering to a minimum of 0% (2008: 0%) pa at age 120 for males. For females, mortality rates are assumed to reduce according to 75% (2008: 75%) CMIB projection MC with a minimum of 1.5% (2008: 1.5%) pa up to age 90 tapering to a minimum of 0% (2008: 0%) pa at age 120. For certain annuities, a further allowance is made for the effect of initial selection.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

34 LONG TERM INSURANCE VALUATION ASSUMPTIONS (CONTINUED)

Premiums – non-participating business

For those contracts where the policyholder does not have the right to vary the amount of the premium paid, full credit is taken for the premiums contractually due at the valuation date. For contracts where the policyholder has the option to vary the rate of premium, the provision is taken as being the higher of the amount calculated as if the policyholder continues to make premium payments or, alternatively, ceases to pay premiums altogether.

Persistency – non-participating business

Lapse rates are used in the valuation of certain classes of long term business. Where this is the case, the valuation persistency basis is set by applying a prudential margin over the best estimate assumptions. The tables below show the major products where lapse rates have been used. In 2009, Whole of Life (conventional non profit) used lapse rates for the first time.

For term assurance business, the margin acts to increase the best estimate lapse rate in the early part of a policy's lifetime (when it is treated as an asset) but to reduce the best estimate lapse rate later in the policy's lifetime (when it is treated as a liability). The crossover point at which the margin changes direction is assessed for broad product groups but applied at a policy by policy level. Any liability to reinsurers on discontinuance within the first four years from inception is allowed for explicitly in the cash flows, using the valuation lapse basis, together with a prudent allowance for clawback of commission from agents upon lapse.

For unitised business, the margin acts to either increase or decrease the best estimate lapse rates, depending upon which approach results in the higher liability. The direction of the margin is assessed for unit life business and unit pensions business separately.

A summary of the lapse basis for major classes of business, as defined by the requirements of the annual returns to the FSA, is shown below:

	2009 Average lapse rate for the policy years			
Product	1 – 5 %	6 – 10 %	11 – 15 %	16 – 20 %
Level term	13.9	9.5	6.0	3.1
Decreasing term	14.2	9.7	6.5	6.0
Accelerated critical illness cover	20.0	10.6	5.4	5.0
Pensions term	12.5	8.6	5.7	5.1
Whole of Life (conventional non profit)	4.2	2.0	0.7	0.0
Savings endowment (unitised with-profits)	0.0	1.7	2.3	4.3
Target cash endowment (unitised with-profits)	3.7	3.4	3.7	2.9
Savings endowment (unit linked)	0.0	1.7	2.3	4.3
Target cash endowment (unit linked)	3.7	3.4	3.7	2.9
Bond (unitised with-profits)	1.2	3.0	2.9	3.0
Bond (unit linked)	2.4	6.3	3.9	3.7
Individual pension regular premium (unitised with-profits)	1.4	1.3	1.3	1.3
Individual pension regular premium (unit linked)	2.1	1.5	1.6	1.6
Group pension regular premium (unitised with-profits)	1.7	1.7	1.7	1.7
Group pension regular premium (unit linked)	1.4	1.4	1.2	1.2
Trustee Investment Plan regular premium (unitised with-profits)	0.4	0.4	0.4	0.4
Trustee Investment Plan regular premium (unit linked)	1.3	1.3	1.3	1.3
Individual pension single premium (unitised with-profits)	3.1	2.9	2.9	2.9
Individual pension single premium (unit linked)	3.6	3.2	2.5	2.5
Group pension single premium (unitised with-profits)	9.5	9.5	9.5	9.5
Group pension single premium (unit linked)	7.3	7.3	7.3	7.3
Trustee Investment Plan single premium (unitised with-profits)	9.3	9.0	8.6	8.6
Trustee Investment Plan single premium (unit linked)	6.4	5.5	4.1	4.1

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

	2008 Average lapse rate for the policy years			
Product	1 – 5 %	6 – 10 %	11 – 15 %	16 – 20 %
Level term	12.6	9.1	5.5	2.9
Decreasing term	12.6	9.1	5.8	5.3
Accelerated critical illness cover	18.4	10.5	5.3	4.9
Pensions term	11.9	8.8	5.4	4.8
Savings endowment (unitised with-profits)	0.0	2.3	3.0	3.6
Target cash endowment (unitised with-profits)	3.6	4.4	4.3	3.8
Savings endowment (unit linked)	0.0	2.3	3.0	3.6
Target cash endowment (unit linked)	3.6	4.4	4.3	3.8
Bond (unitised with-profits)	1.5	5.9	4.1	3.7
Bond (unit linked)	2.3	5.6	3.8	3.6
Individual pension regular premium (unitised with-profits)	1.1	1.1	1.1	1.1
Individual pension regular premium (unit linked)	1.6	1.1	1.1	1.1
Group pension regular premium (unitised with-profits)	2.3	2.3	2.3	2.3
Group pension regular premium (unit linked)	2.0	2.0	2.0	2.0
Trustee Investment Plan regular premium (unitised with-profits)	0.3	0.3	0.3	0.3
Trustee Investment Plan regular premium (unit linked)	1.2	1.2	1.2	1.2
Individual pension single premium (unitised with-profits)	3.2	3.2	3.2	3.2
Individual pension single premium (unit linked)	3.5	3.0	2.8	2.8
Group pension single premium (unitised with-profits)	7.7	7.7	7.7	7.7
Group pension single premium (unit linked)	6.5	6.5	6.5	6.5
Trustee Investment Plan single premium (unitised with-profits)	10.5	10.2	10.1	10.1
Trustee Investment Plan single premium (unit linked)	6.5	5.3	5.0	5.0

Endowment reserve

The endowment reserve has been set taking reasonable account of an assessment of the expected future population of complaints, the expected uphold rate for these complaints, the potential impact of any Financial Ombudsman Service decisions on referred complaints and the average compensation per complaint.

Overseas business

In calculating the long term business provisions for international long term business operations, local actuarial tables and interest rates are used.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

35 BORROWINGS

(i) Analysis by type

	Borrowings excluding unit linked borrowings 2009 £m	Unit linked borrowings 2009 £m	Total 2009 £m	Borrowings excluding unit linked borrowings 2008 £m	Unit linked borrowings 2008 £m	Total 2008 £m
Subordinated borrowings	**1,897**	**–**	**1,897**	1,657	–	1,657
Senior borrowings	**1,291**	**161**	**1,452**	2,134	180	2,314
Client fund holdings of Group debt[1]	**–**	**(72)**	**(72)**	–	–	–
Total borrowings	**3,188**	**89**	**3,277**	3,791	180	3,971

1. £72m of the Group's subordinated and senior debt (£27m and £45m respectively) is currently held by Legal & General customers through unit linked products. These borrowings are shown as a deduction from total borrowings in the table above. The prior year has not been restated.

Unit linked borrowings are excluded from the analysis below as the risk is retained by the policyholders.

(ii) Borrowings excluding unit linked borrowings – Analysis by nature

	Carrying amount 2009 £m	Coupon rate 2009 %	Fair value 2009 £m	Carrying amount 2008 £m	Coupon rate 2008 %	Fair value 2008 £m
Subordinated borrowings						
6.385% Sterling perpetual capital securities (Tier 1)	**666**	**6.39**	**473**	692	6.39	414
5.875% Sterling undated subordinated notes (Tier 2)	**425**	**5.88**	**326**	426	5.88	287
4.0% Euro subordinated notes 2025 (Tier 2)	**498**	**4.00**	**455**	539	4.00	283
10% Sterling subordinated notes 2041 (Tier 2)	**308**	**10.00**	**364**	–	–	–
Total subordinated borrowings	**1,897**		**1,618**	1,657		984
Senior borrowings						
Sterling medium term notes 2031-2041	**608**	**5.87**	**558**	608	5.87	493
Euro commercial paper 2010	**98**	**0.47**	**98**	609	3.69	610
Bank loans 2010	**9**	**0.51**	**9**	154	6.20	154
Non recourse financing						
– US Dollar Triple X securitisation 2025	**262**	**2.23**	**185**	369	2.94	369
– US Dollar Triple X securitisation 2037	**274**	**0.60**	**194**	308	2.25	308
– Sterling property partnership loans 2011	**–**	**–**	**–**	86	5.47	86
– LGV 6 Private Equity Fund Limited Partnership	**40**	**2.63**	**40**	–	–	–
Total senior borrowings	**1,291**		**1,084**	2,134		2,020
Total borrowings excluding unit linked borrowings	**3,188**		**2,702**	3,791		3,004
Total borrowings (excluding unit linked borrowings and non recourse financing)	**2,612**		**2,283**	3,028		2,241

£127m of interest expense was incurred during the period (2008: £145m) on borrowings excluding non recourse financing and unit linked borrowings.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Subordinated borrowings

6.385% Sterling perpetual capital securities
In 2007, Legal & General Group Plc issued £600m of 6.385% Sterling perpetual capital securities. Simultaneous with the issuance, the fixed coupon was swapped into six month LIBOR plus 0.94% pa. These securities are callable at par on 2 May 2017 and every three months thereafter. If not called, the coupon from 2 May 2017 will be reset to three month LIBOR plus 1.93% pa. For regulatory purposes these securities are treated as innovative tier 1 capital. These securities have been classified as liabilities as the interest payments become mandatory in certain circumstances.

5.875% Sterling undated subordinated notes
In 2004, Legal & General Group Plc issued £400m of 5.875% Sterling undated subordinated notes. These notes are callable at par on 1 April 2019 and every five years thereafter. If not called, the coupon from 1 April 2019 will be reset to the prevailing five year benchmark gilt yield plus 2.33% pa. These notes are treated as upper tier 2 capital for regulatory purposes. These securities have been classified as liabilities as the interest payments become mandatory in certain circumstances.

4.0% Euro subordinated notes 2025
In 2005, Legal & General Group Plc issued €600m of 4.0% Euro dated subordinated notes. The proceeds were swapped into sterling. The notes are callable at par on 8 June 2015 and each year thereafter. If not called, the coupon from 8 June 2015 will reset to a floating rate of interest based on prevailing three month Euribor plus 1.7% pa. These notes mature on 8 June 2025 and are treated as lower tier 2 capital for regulatory purposes.

10% Sterling subordinated notes 2041
On 16 July 2009, Legal & General Group Plc issued £300m of 10% dated subordinated notes. The notes are callable at par on 23 July 2021 and every five years thereafter. If not called, the coupon from 23 July 2021 will be reset to the prevailing five year benchmark gilt yield plus 9.325% pa. These notes mature on 23 July 2041 and are treated as lower tier 2 capital for regulatory purposes.

Non recourse financing

US Dollar Triple X securitisation 2025
In 2004, a subsidiary of Legal & General America Inc issued US$550m of non recourse debt in the US capital markets to meet the Triple X reserve requirements of part of the US term insurance written up to 2005. It is secured on the cash flows related to that tranche of business.

US Dollar Triple X securitisation 2037
In 2006, a subsidiary of Legal & General America Inc issued US$450m of non recourse debt in the US capital markets to meet the Triple X reserve requirements of part of the US term insurance written after 2005 and 2006. It is secured on the cash flows related to that tranche of business.

Sterling property partnership loans 2011
The property partnership loans were secured on specific properties.

LGV 6 Private Equity Fund Limited Partnership
These borrowings are non recourse bank borrowings.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

35 BORROWINGS (CONTINUED)

(iii) Borrowings excluding unit linked borrowings – Analysis by maturity

As at 31 December 2009	Carrying amount £m	Maturity profile of undiscounted cash flows: Within 1 year £m	1-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m
Subordinated borrowings							
6.385% Sterling perpetual capital securities (Tier 1)	**666**	**–**	**–**	**–**	**–**	**(600)**	**(600)**
5.875% Sterling undated subordinated notes (Tier 2)	**425**	**–**	**–**	**–**	**–**	**(400)**	**(400)**
4.0% Euro subordinated notes 2025 (Tier 2)	**498**	**–**	**–**	**–**	**(531)**	**–**	**(531)**
10% Sterling subordinated notes 2041 (Tier 2)	**308**	**–**	**–**	**–**	**–**	**(300)**	**(300)**
Senior borrowings							
Sterling medium term notes 2031-2041	**608**	**–**	**–**	**–**	**(590)**	**(10)**	**(600)**
Euro commercial paper 2010	**98**	**(98)**	**–**	**–**	**–**	**–**	**(98)**
Bank loans 2010	**9**	**(9)**	**–**	**–**	**–**	**–**	**(9)**
Non recourse financing							
– US Dollar Triple X securitisation 2025	**262**	**–**	**–**	**–**	**(266)**	**–**	**(266)**
– US Dollar Triple X securitisation 2037	**274**	**–**	**–**	**–**	**–**	**(278)**	**(278)**
– LGV 6 Private Equity Fund Limited Partnership	**40**	**(3)**	**(8)**	**(29)**	**–**	**–**	**(40)**
Total borrowings excluding unit linked borrowings	**3,188**	**(110)**	**(8)**	**(29)**	**(1,387)**	**(1,588)**	**(3,122)**
Contractual undiscounted interest payments		**(157)**	**(627)**	**(1,562)**	**(1,237)**	**(219)**	**(3,802)**
Total contractual undiscounted cash flows		**(267)**	**(635)**	**(1,591)**	**(2,624)**	**(1,807)**	**(6,924)**

As at 31 December 2008	Carrying amount £m	Maturity profile of undiscounted cash flows: Within 1 year £m	1-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m
Subordinated borrowings							
6.385% Sterling perpetual capital securities (Tier 1)	692	–	–	–	–	(600)	(600)
5.875% Sterling undated subordinated notes (Tier 2)	426	–	–	–	–	(400)	(400)
4.0% Euro subordinated notes 2025 (Tier 2)	539	–	–	–	(583)	–	(583)
Senior borrowings							
Sterling medium term notes 2031-2041	608	–	–	–	(590)	(10)	(600)
Euro commercial paper 2009	609	(611)	–	–	–	–	(611)
Bank loans 2009	154	(154)	–	–	–	–	(154)
Non recourse financing							
– US Dollar Triple X securitisation 2025	369	–	–	–	(375)	–	(375)
– US Dollar Triple X securitisation 2037	308	–	–	–	–	(313)	(313)
– Sterling property partnership loans 2011	86	–	(85)	–	–	–	(85)
Total borrowings excluding unit linked borrowings	3,791	(765)	(85)	–	(1,548)	(1,323)	(3,721)
Contractual undiscounted interest payments		(144)	(564)	(1,384)	(1,067)	(33)	(3,192)
Total contractual undiscounted cash flows		(909)	(649)	(1,384)	(2,615)	(1,356)	(6,913)

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

As at 31 December 2009, the Group had in place a £960m syndicated committed revolving credit facility provided by a number of its key relationship banks, maturing in December 2012.

The maturity profile above is calculated on the basis that a facility to refinance a maturing loan is not recognised unless the facility and loan are related. If refinancing under the Group's syndicated facility was recognised, then all amounts shown as repayable within one year would be reclassified as repayable between one and five years.

Undiscounted interest payments are estimated based on the year end applicable interest rate and spot exchange rates.

Short term assets available at the holding company level exceeded the amount of short term borrowings of £107m (Euro Commercial Paper and Bank Loans).

36 PROVISIONS

(i) Analysis of provisions

	Notes	2009 £m	2008 £m
Retirement benefit obligations[1]	(ii)	**746**	551
Other provisions		**11**	4
		757	555

1. Retirement benefit obligations are presented gross of £465m of annuity obligations insured by Society (2008: £411m).

(ii) Retirement benefit obligations

Defined contribution plans

The Group operates the following defined contribution pension schemes in the UK and overseas:

– Legal & General Group Personal Pension Plan (UK).
– Legal & General Staff Stakeholder Pension Scheme (UK).
– Legal & General America Inc. Savings Plan (US).
– Régime de Retraite Professionnel (France).
– Legal & General Nederland Stichting Pensioenfonds (Netherlands); replacing the early retirement scheme previously part of the defined benefit plan.
– Legal & General International (Ireland) Limited Retirement Solution Plan (Ireland).

Contributions of £34m (2008: £25m) were charged as expenses during the year in respect of defined contribution plans.

Defined benefit plans

The Group operates the following defined benefit pension schemes in the UK and overseas:

– Legal & General Group UK Pension and Assurance Fund (the Fund). The Fund was closed to new members from January 1995; last full actuarial valuation as at 31 December 2006.
– Legal & General Group UK Senior Pension Scheme (the Scheme). The Scheme was, with a few exceptions (principally transfers from the Fund), closed to new members from August 2000 and finally closed to new members from April 2007; last full actuarial valuation as at 31 December 2006.
– Legal & General America Inc. Cash Balance Plan; last full actuarial valuation as at 31 December 2008.
– Legal & General Nederland Stichting Pensioenfonds; last full actuarial valuation as at 31 December 2007.
– Régime de Retraite à Prestations Définies de Legal & General (France); last full actuarial valuation as at 31 December 2009.

The benefits paid from the defined benefit schemes are based on percentages of the employees' final pensionable salary for each year of credited service. The Group has no liability for retirement benefits other than for pensions, except for a small scheme in France (Indemnités de Fin de Carrière), which provides lump sum benefits on retirement. The Fund and Scheme account for virtually all of the UK and over 98% of worldwide assets of the Group's defined benefit schemes.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

36 PROVISIONS (CONTINUED)

(ii) Retirement benefit obligations (continued)

The principal actuarial assumptions for the UK defined benefit schemes were:

	Fund and Scheme 2009 %	Fund and Scheme 2008 %
Rate used to discount liabilities	**5.70**	6.50
Expected return on plan assets	**6.37**	6.71
Rate of increase in salaries[1]	**2.30**	2.30
Rate of increase in pensions in payment	**3.60**	3.20
Rate of increase in deferred pensions	**4.30**	3.75
Rate of general inflation (RPI)	**3.60**	2.70
Rate of wage inflation	**2.30**	2.30
Post retirement mortality		
– 2009: 100% (Fund) / 85% (Scheme) of PCMA/PCFA 00 with improvement at 100% MC males, 75% MC females, minimum improvement 1.5% pa males and 1.0% pa females, with tapering of minimum improvement rate linearly down to nil between ages 90 and 120		
– 2008: 100% (Fund) / 85% (Scheme) of PCMA/PCFA 00 with improvement at 100% MC males, 75% MC females, minimum improvement 1.5% pa males and 1.0% pa females		

1. On 1 December 2008, the conditions of the Fund and Scheme were amended to cap future pensionable salary increases at a maximum of 2.5% each year with effect from 1 January 2009.

	Fund and Scheme 2009 £m	**Overseas 2009 £m**	Fund and Scheme 2008 £m	Overseas 2008 £m
Movement in present value of defined benefit obligations				
As at 1 January	**(1,160)**	**(27)**	(1,365)	(19)
Current service cost	**(10)**	**(1)**	(17)	(1)
Past service cost	**–**	**–**	5	–
Interest expense	**(74)**	**(2)**	(77)	(1)
Plan participants' contributions	**–**	**–**	(3)	–
Actuarial (loss)/gain (recognised in statement of comprehensive income)	**(258)**	**(1)**	249	–
Benefits paid	**56**	**1**	48	1
Exchange differences	**–**	**2**	–	(7)
As at 31 December	**(1,446)**	**(28)**	(1,160)	(27)
Movement in fair value of plan assets				
As at 1 January	**609**	**27**	771	18
Expected return on plan assets	**41**	**2**	51	1
Actuarial gain/(loss) (recognised in statement of comprehensive income)	**46**	**–**	(222)	(1)
Employer contributions	**59**	**3**	54	4
Plan participants' contributions	**–**	**–**	3	–
Benefits paid	**(56)**	**(1)**	(48)	(1)
Exchange differences	**–**	**(2)**	–	6
As at 31 December	**699**	**29**	609	27
Gross pension obligations included in provisions	**(747)**	**1**	(551)	–
Annuity obligations insured by Society	**465**	**–**	411	–
Gross defined benefit pension deficit	**(282)**	**1**	(140)	–
Deferred tax on defined benefit pension deficit	**79**	**–**	39	–
Net defined benefit pension deficit	**(203)**	**1**	(101)	–

The total amount of actuarial (losses)/gains net of tax recognised in the statement of comprehensive income for the year was £(154)m; cumulative £(271)m (2008: £18m; cumulative £(117)m). Actuarial (losses)/gains net of tax relating to with-profits policyholders of £(62)m (2008: £8m) have been allocated to the unallocated divisible surplus.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The historic funding and experience adjustments are as follows:

	2009 £m	2008 £m	2007 £m	2006 £m	2005 £m
Present value of defined benefit obligations	**(1,474)**	(1,187)	(1,384)	(1,346)	(1,304)
Fair value of plan assets	**728**	636	789	778	722
Gross pension obligations	**(746)**	(551)	(595)	(568)	(582)
Experience adjustments on plan liabilities	**18**	3	(19)	(13)	(9)
Experience adjustments on plan assets	**46**	(222)	(32)	10	76

The fair value of the plan assets and expected return at the end of the year is made up as follows:

As at 31 December 2009	**UK £m**	**Expected return %**	**Overseas £m**	**Expected return %**
Equities	**351**	**7.0**	**8**	**8.2**
Bonds	**311**	**5.7**	**17**	**4.1**
Properties	**37**	**6.0**	**–**	**–**
Other investments	**–**	**–**	**4**	**2.8**
	699		**29**	

As at 31 December 2008	UK £m	Expected return %	Overseas £m	Expected return %
Equities	293	7.0	5	8.3
Bonds	280	6.5	18	4.1
Properties	36	6.0	–	–
Other investments	–	–	4	2.3
	609		27	

The average credit rating of the bond portfolio is AA (2008: AA).

The expected rate of return for bonds is based on the current yield on a medium to long term AA bond index. The expected rates of return on equities and properties are based on margins over bond yields reflecting risk premiums. In 2009, the return on plan assets, excluding annuity obligations, was £89m (2008: £(173)m).

Employer contributions increased to £62m (2008: £58m) including a pension deficit reduction payment of £41m (2008: £39m). Employer contributions of £29m are expected to be paid to the plan during 2010.

The following amounts have been charged/(credited) to the income statement:

	2009 £m	2008 £m
Current service costs	**11**	18
Interest expense	**76**	78
Expected return on plan assets	**(43)**	(52)
Total included in other expenses	**44**	44

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

37 PAYABLES AND OTHER FINANCIAL LIABILITIES

	Notes	2009 £m	2008 £m
Derivative liabilities	20	**3,577**	5,219
Collateral received from banks		**459**	668
Other		**967**	912
Payables and other financial liabilities		**5,003**	6,799
Settled within 12 months		**4,497**	6,116
Settled after 12 months		**506**	683

Other includes future commission payments which have contingent settlement provisions of £167m (2008: £186m). This liability has been determined using the net present value of the future commission which will be payable on fund values. This valuation technique uses assumptions which are consistent with the Group's effective rate of interest, investment return assumptions and persistency assumptions used in other valuations, but it is not determined by reference to published price quotations.

The undiscounted value which is expected to be paid at maturity in respect of such commission is £225m (2008: £229m).

Payables and other financial liabilities settled after 12 months are expected to be settled within five years.

(i) Fair value hierarchy

As at 31 December 2009	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
Derivative liabilities	3,577	2,184	1,393	–	–
Collateral received from banks	459	459	–	–	–
Other	967	–	60	167	740
Payables and other financial liabilities	**5,003**	**2,643**	**1,453**	**167**	**740**

Trail commissions are modelled using expected cash flows, incorporating expected future persistency. They have therefore been classified as level 3 liabilities. The entire movement in the balance has been reflected in the income statement during the year. A reasonably possible alternative persistency assumption would have the effect of increasing or decreasing the liability by £5m.

There have been no significant transfers between levels.

38 OTHER LIABILITIES

	2009 £m	2008 £m
Accruals	**216**	188
Reinsurers' share of deferred acquisition costs	**80**	90
Deferred income liabilities	**407**	463
Other	**189**	256
Other liabilities	**892**	997
Settled within 12 months	**422**	496
Settled after 12 months	**470**	501

Other liabilities settled after 12 months are expected to be settled within five years.

39 NET ASSET VALUE ATTRIBUTABLE TO UNIT HOLDERS

As at 31 December 2009	Total £m	Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m
Net asset value attributable to unit holders	**1,929**	**1,108**	**821**	**–**	**–**

Amounts attributable to unit holders are repayable on demand and the Group is responsible for ensuring there is sufficient liquidity within the corresponding asset portfolio to enable the liability to be met as it falls due. There have been no significant transfers between levels.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

40 RELATED PARTY TRANSACTIONS

There were no material transactions between directors or key managers and the Legal & General group of companies. All transactions between the Group, its directors and key managers are on commercial terms which are no more favourable than those available to employees in general. Contributions to the post-employment benefit plans are outlined in Note 36.

At 31 December 2009 and 31 December 2008 there were no loans outstanding to officers of the Company.

Key management personnel compensation

The aggregate compensation for key management personnel, including executive and non-executive directors, is as follows:

	2009 £m	2008 £m
Salaries	7	5
Social security costs	1	1
Post-employment benefits	1	1
Share-based incentive awards	3	3
Key management personnel compensation	12	10
Number of key management personnel	18	16

The UK defined benefit pension schemes have purchased annuity contracts issued by Society for consideration of £51m (2008: £49m) during the year, priced on an arm's length basis.

The Group's investment portfolio includes investments in venture capital, property and financial investments which are held via collective investment vehicles. Net investments in associate investment vehicles totalled £1,780m during the year (2008: £1,488m). The Group has outstanding loans to these associates of £7m (2008: £2m) and received investment management fees of £30m during the year (2008: £43m). Distributions from these investment vehicles to the Group totalled £57m (2008: £170m).

41 CONTINGENT LIABILITIES, GUARANTEES AND INDEMNITIES

Provision for the liabilities arising under contracts with policyholders is based on certain assumptions. The variance of actual experience from that assumed may result in such 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 FSA, ombudsman rulings, industry compensation schemes and court judgments.

Various Group companies receive claims and become involved in actual or threatened litigation and regulatory issues from time to time. The relevant members of the Group ensure that they make prudent provision as and when circumstances calling for such provision become clear, and that each has adequate capital and reserves to meet reasonably foreseeable eventualities. The provisions made are regularly reviewed. It is not possible to predict, with certainty, the extent and the timing of the financial impact of these claims, litigation or issues.

In 1975, Legal & General Assurance Society Limited (the Society) was required by the Institute of London Underwriters (ILU) to execute the ILU form of guarantee in respect of policies issued through the ILU's Policy Signing Office on behalf of NRG Victory Reinsurance Company Ltd (Victory), a company which was then a subsidiary of the Society. In 1990, Nederlandse Reassurantie Groep Holding NV (the assets and liabilities of which have since been assumed by Nederlandse Reassurantie Groep NV under a statutory merger in the Netherlands) acquired Victory and provided an indemnity to the Society against any liability the Society may have as a result of the ILU's requirement, and the ILU agreed that its requirement of the Society would not apply to policies written or renewed after the acquisition. Nederlandse Reassurantie Groep NV is now owned by Columbia Insurance Company, a subsidiary of Berkshire Hathaway Inc. Whether the Society has any liability as a result of the ILU's requirement and, if so, the amount of its potential liability, is uncertain. The Society has made no payment or provision in respect of this matter.

Group companies have given indemnities and guarantees as a normal part of their business and operating activities or in relation to capital market transactions. Legal & General Group Plc has provided indemnities and guarantees in respect of the liabilities of Group companies in support of their business activities.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

42 COMMITMENTS

(i) Capital commitments

	2009 £m	2008 £m
Authorised and contracted commitments not provided for in respect of investment property development, payable after 31 December		
– Long term business	**16**	35

(ii) Operating lease commitments

	2009 £m	2008 £m
The future aggregate minimum lease payments under non-cancellable operating leases are as follows:		
– Not later than 1 year	**27**	34
– Later than 1 year and not later than 5 years	**93**	130
– Later than 5 years	**201**	333
	321	497
Future aggregate minimum sublease payments expected to be received under operating subleases	**11**	10
The future aggregate minimum lease receivables under non-cancellable operating leases are as follows:		
– Not later than 1 year	**4**	2
– Later than 1 year and not later than 5 years	**11**	10
– Later than 5 years	**2**	3
	17	15

The Group leases offices and other premises under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

43 SUBSIDIARIES

(i) Operating subsidiaries

The principal operating subsidiaries consolidated in these financial statements are listed below. The Company holds, directly or indirectly, all of the ordinary share capital and voting rights of these companies.

Company name	Nature of business	Country of incorporation
Legal & General Finance PLC[1]	Treasury operations	England and Wales
Legal & General Resources Limited[1]	Provision of services	England and Wales
Legal & General Assurance Society Limited	Long term and general insurance	England and Wales
Legal & General Insurance Limited	General insurance	England and Wales
Legal & General Investment Management Limited	Institutional fund management	England and Wales
Legal & General Assurance (Pensions Management) Limited	Long term business	England and Wales
Legal & General Pensions Limited	Reinsurance	England and Wales
Legal & General Partnership Services Limited	Provision of services	England and Wales
Legal & General (Portfolio Management Services) Limited	Institutional fund management	England and Wales
Legal & General Property Limited	Property management	England and Wales
Legal & General (Unit Trust Managers) Limited	Unit trust management	England and Wales
Nationwide Life Limited	Long term business	England and Wales
Suffolk Life Annuities Limited	Long term business	England and Wales
Suffolk Life Pensions Limited	Long term business	England and Wales
LGV Capital Limited	Private equity	England and Wales
Legal & General (France) SA	Long term business	France
Legal & General Bank (France) SA	Financial services	France
Legal & General International (Ireland) Limited	Long term business	Ireland
Legal & General Nederland Levensverzekering Maatschappij NV	Long term business	Netherlands
Banner Life Insurance Company Inc	Long term business	USA
William Penn Life Insurance Company of New York Inc	Long term business	USA
Legal & General Investment Management America Inc	Institutional fund management	USA
First British American Reinsurance Company	Reinsurance	USA
First British American Reinsurance Company II	Reinsurance	USA
First British Bermudan Reinsurance Company	Reinsurance	Bermuda

1. Directly held by Legal & General Group Plc. All other subsidiaries are held through intermediate holding companies.

The main territory of operation of subsidiaries incorporated in England and Wales is the UK. For overseas subsidiaries the principal country of operation is the same as the country of incorporation. All subsidiaries have a 31 December year end reporting date.

The complete list of subsidiary undertakings can be obtained from the registered office at One Coleman Street, London, EC2R 5AA.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

43 SUBSIDIARIES (CONTINUED)

(ii) Investment vehicles

The following mutual funds and partnerships have been consolidated as a result of the Group's ability to exert control over the financial and operating activities of the investment vehicle so as to obtain economic benefits.

Vehicle name	Vehicle type	Territory	Year end reporting date	% of equity shares by the Group
Chineham Shopping Centre Limited Partnership	Property partnership	Jersey	31/12/2009	100.0
Ealing Shopping Centre Limited Partnership	Property partnership	Jersey	31/12/2009	100.0
Gresham Street Limited Partnership	Property partnership	Jersey	31/12/2009	100.0
Legal & General City Offices Limited Partnership	Property partnership	Jersey	31/12/2009	100.0
Legal & General Investment Management Global Opportunities Fixed Income Fund Plc	Open ended investment company	Ireland	31/12/2009	100.0
Legal & General Life Fund Limited Partnership	Property partnership	England and Wales	31/12/2009	100.0
Legal & General Spectrum (Jersey) Unit Trust	Property unit trust	Jersey	31/12/2009	100.0
Northampton Shopping Centre Limited Partnership	Property partnership	Jersey	31/12/2009	100.0
Legal & General Investment Management UK Smaller Companies Alpha Fund Plc	Open ended investment company	Ireland	31/12/2009	99.9
Legal & General Special Situations Trust	Equity unit trust	UK	14/09/2009	99.9
Legal & General Investment Management Global Macro Fund Plc	Open ended investment company	Ireland	31/12/2009	99.5
LGV 6 Private Equity Fund Limited Partnership	Private equity partnership	England and Wales	31/12/2009	99.4
Legal & General Asian Income Trust	Equity unit trust	UK	10/09/2009	90.9
Legal & General Japanese Trust	Equity unit trust	UK	17/10/2009	89.9
Legal & General Investment Management Liquidity Funds Plc	Open ended investment company	Ireland	31/12/2009	86.5
Legal & General North American Trust	Equity unit trust	UK	16/01/2009	86.0
Legal & General European Trust	Equity unit trust	UK	28/07/2009	83.9
ARC Property Fund Unit Trust	Property unit trust	Jersey	31/12/2009	80.0
Legal & General Pacific Growth Trust	Equity unit trust	UK	18/09/2009	80.0
Legal & General Diversified Absolute Return Trust	Equity unit trust	UK	25/09/2009	78.5
Legal & General Equity Trust	Equity unit trust	UK	15/08/2009	75.3
Legal & General Growth Trust	Equity unit trust	UK	15/05/2009	70.5
Legal & General Global Growth Trust	Equity unit trust	UK	15/01/2009	68.0
Legal & General High Income Trust	Fixed interest unit trust	UK	05/09/2009	67.0
Legal & General UK Smaller Companies Trust	Equity unit trust	UK	18/06/2009	66.8
Legal & General Pacific Index Trust	Equity unit trust	UK	25/03/2009	59.0
Lagoon Finance Limited[1]	Limited liability company	Ireland	31/12/2009	–
Trees SA[1]	Limited liability company	Luxembourg	30/06/2009	–

1. Lagoon Finance Limited and Trees SA are consolidated on the basis that the Group has the power to govern the financial and operating policies and has the rights to receive 100% of the economic benefits. Only the controlled cell of the Trees SA investment vehicle is consolidated.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

44 ASSOCIATES AND JOINT VENTURES

The Group has the following significant holdings which have been included as financial investments or investments in associates. The gross assets of these companies are in part funded by borrowings which are non recourse to the Group.

Company name	Country of incorporation	Accounting treatment	Year end reporting date	% of equity shares held by Group
Bracknell Property Unit Trust[1]	Jersey	FVTPL	31/03/2009	50.5
Central St Giles Unit Trust	Jersey	FVTPL	31/12/2009	50.0
Legal & General Gulf BSC[2]	Bahrain	Equity method	31/12/2009	50.0
Mithras Capital Fund Limited Partnership	Scotland	FVTPL	31/12/2009	50.0
Performance Shopping Centre Limited Partnership	England and Wales	FVTPL	31/12/2009	50.0
Warrington Retail Unit Trust	Jersey	FVTPL	31/12/2009	50.0
Meteor Industrial Partnership	England and Wales	FVTPL	31/12/2009	49.9
Legal & General UK Alpha Trust	England and Wales	FVTPL	18/06/2009	49.8
Legal & General European Index Trust Plc	England and Wales	FVTPL	31/07/2009	49.2
Legal & General Ethical Trust	England and Wales	FVTPL	12/12/2009	48.3
LGV 3 Private Equity Fund Limited Partnership	England and Wales	FVTPL	31/12/2009	46.6
LGV 1 Private Equity Fund Limited Partnership	England and Wales	FVTPL	30/11/2009	46.3
Legal & General Active Opportunities Trust	England and Wales	FVTPL	14/10/2009	45.7
Legal & General US Index Trust	England and Wales	FVTPL	05/12/2009	43.8
UK Logistics Fund Unit Trust	Jersey	FVTPL	31/12/2009	42.3
Arlington Business Parks Unit Trust	Jersey	FVTPL	31/12/2009	41.0
The Leisure Fund Unit Trust	Jersey	FVTPL	31/12/2009	39.8
English Cities Fund	England and Wales	FVTPL	31/12/2009	37.5
Legal & General Japanese Index Trust	England and Wales	FVTPL	24/10/2009	37.1
LGV 2 Private Equity Fund Limited Partnership	England and Wales	FVTPL	31/12/2009	37.1
LGV 4 Private Equity Fund Limited Partnership	England and Wales	FVTPL	31/12/2009	36.7
LGV 5 Private Equity Fund Limited Partnership	England and Wales	FVTPL	30/11/2009	36.0
Baroda L&G Life Insurance Company Limited[2]	India	Equity method	31/03/2009	26.0
Cofunds (Holdings) Limited	England and Wales	Equity method	31/12/2009	25.4
Legal & General Fixed Interest Trust	England and Wales	FVTPL	05/09/2009	23.0
Dunedin Capital Group Limited	Scotland	FVTPL	28/02/2009	22.6
Legal & General Distribution Trust	England and Wales	FVTPL	14/10/2009	21.2

1. The Bracknell Property Unit Trust is not consolidated as the Group does not have the power to control the entity.
2. Legal & General Gulf BSC and Baroda L&G Life Insurance Company Limited are joint venture operations.

Summarised financial information for associates which are classified as FVTPL is shown below.

2009	Private equity £m	Property partnerships £m	Unit trusts £m	Total £m
Aggregate revenues	30	82	512	624
Aggregate profit	24	40	137	201
Gross assets	152	2,441	4,677	7,270
Gross liabilities	3	1,337	104	1,444

2008	Private equity £m	Property partnerships £m	Unit trusts £m	Total £m
Aggregate revenues	68	141	198	407
Aggregate profit	60	79	144	283
Gross assets	187	3,225	4,717	8,129
Gross liabilities	6	1,559	99	1,664

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

45 GOODWILL RESULTING FROM ACQUISITIONS

The cumulative goodwill charged to reserves prior to 1998, arising from acquisition of subsidiaries which are still part of the Group, amounted to £70m (2008: £70m).

46 MANAGEMENT OF CAPITAL RESOURCES

Capital structure

The Group's total capital resources of £7.3bn (2008: £6.1bn) on an IFRS basis comprise equity holders capital, £4.2bn (2008: £3.6bn), subordinated debt, £1.8bn (2008: £1.6bn), and unallocated divisible surplus, £1.3bn (2008: £0.9bn).

From a regulatory perspective the Group is required to measure and monitor its capital resources on an ongoing basis and to comply with the minimum capital requirements of regulators in each territory in which we operate. At 31 December 2009, Legal & General's unaudited Insurance Group Directive (IGD) capital resources were £3.1bn in excess of capital requirements of £2.5bn, representing a solvency coverage ratio of 224%. This surplus capital is after accruing for a 2009 final dividend of £160m.

The Group writes a range of long term insurance and investment business in the long term fund (LTF) of its main operating insurance subsidiary, Legal & General Assurance Society Limited (Society). This fund is segregated from the Group's other assets. The fund includes participating (with-profits) business where policyholders and shareholders share in the risks and rewards, and non-participating (non profit) business, where the shareholders receive profits or incur losses. Capital in excess of the amount required to cover the liabilities is currently held within Society. This capital provides support for new and existing non profit business within our UK non profit Risk and Savings pensions businesses.

The non-linked non profit pensions and annuity business of Society is ceded, on arm's length terms, to a wholly owned Insurance Special Purpose Vehicle (ISPV), Legal & General Pensions Limited (LGPL). Whilst an ISPV is not required to segregate policyholder assets within a LTF, LGPL continues to manage policyholder and shareholder assets separately for internal purposes.

Managed pension fund business is written through Legal & General Assurance (Pensions Management) Limited (PMC), which is a life company writing predominantly non-participating group pension business effected by trustees of occupational schemes in the UK (or their equivalent overseas). The assets are held in a LTF and are separate from other assets within the Group.

In addition, the Group operates two UK long term insurance businesses acquired in 2008 (Nationwide Life Limited and Suffolk Life Annuities Limited). General insurance business is written in the UK by Legal & General Insurance Limited, and long term insurance business is written by subsidiaries in America, the Netherlands and France.

Capital management policies and objectives

The Group aims to manage its capital resources so as to maintain financial strength, policyholder security and relative external ratings advantage. The Group also seeks to maximise its financial flexibility by maintaining strong liquidity and by utilising a range of alternative sources of capital including equity, senior debt, subordinated debt and reinsurance.

Capital measures

The Group measures its capital on a number of different bases, including those which comply with the regulatory frameworks within which the Group operates and those which the directors consider most appropriate for managing the business. The measures used by the Group 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. In addition, the supplementary accounts prepared using EEV principles provide further insight into the value of the business to shareholders. Accordingly the Group's net asset value and total capital employed are also analysed and measured on this basis.

- Regulatory bases
  The financial strength of the Group's insurance subsidiaries is measured under various local regulatory requirements (see below). One of these regulatory measures, Individual Capital Assessment (ICA), measures capital using risk based stochastic techniques, and provides a measure of the level of economic capital required to run the Group's business.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Basis of regulatory capital and corresponding regulatory capital requirements

In each country in which the Group operates, the local insurance regulator specifies rules and guidance for the minimum amount and type of capital which must be held by long term insurance subsidiaries in excess of their insurance liabilities. The minimum required capital must be maintained at all times throughout the year. This helps to ensure that payments to policyholders can be made as they fall due.

The required capital is calculated by either assessing the additional assets which would be required to meet the insurance company's liabilities in specified, stressed financial conditions, or by applying fixed percentages to the insurance company's liabilities and risk exposures. The requirements in the different jurisdictions in which the Group operates are detailed below:

UK regulatory basis

Required capital for the life business is based on FSA rules. Society must hold assets in excess of the higher of two amounts, the first being calculated using the FSA rules specified by the Regulator (pillar 1), the second being an economic capital assessment by the Company which is reviewed by the FSA (pillar 2), otherwise known as Individual Capital Assessment (ICA).

The public pillar 1 capital calculation is calculated by applying fixed percentages to liabilities and sums assured at risk or setting aside a proportion of expenses (Peak 1). There are further stress tests for participating business, as measured in the Realistic Balance Sheet (Peak 2), which may increase the required capital under Peak 1 calculations.

The private pillar 2 capital calculation is an assessment of the economic capital required to ensure that the Company can meet its liabilities, with a high likelihood, as they fall due. This is achieved by application of stochastic modelling and scenario testing. The result is reviewed and may be modified by the FSA.

Regulatory capital for the general insurance business is also calculated using FSA pillar 1 and pillar 2 requirements. The pillar 1 calculation applies fixed percentages to premiums and claims. Pillar 2 creates a higher capital requirement and is therefore applied in this business.

US regulatory basis

Required capital is determined to be the Company Action Level Risk Based Capital (RBC) based on the National Association of Insurance Commissioners RBC model. RBC is a method of measuring the minimum amount of capital appropriate for an insurance company to support its overall business operations, taking into account its size and risk profile. The calculation is based on applying factors to various asset, premium, claim, expense and reserve items, with higher factors used for those items with greater underlying risk and lower factors for less risky items.

French and Dutch regulatory bases

The minimum required capital is defined by the French Ministry of Finance's 'Code des Assurances' and the 'De Nederlandsche Bank N.V.' (Dutch Supervisory Body) respectively. The basis of the calculation is a percentage of the liabilities plus a percentage of the sum assured at risk and, for some contracts, the premium. The percentages depend on the guarantees given and the amount of reinsurance cover.

Group regulatory basis

In addition to the regulatory capital calculations for the individual firms, the Group is required to comply with the requirements of the Insurance Group Directive (IGD).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

46 MANAGEMENT OF CAPITAL RESOURCES (CONTINUED)

Available regulatory capital resources

Capital resources available to meet regulatory UK capital requirements are determined using FSA valuation rules. The asset valuation rules are based on UK GAAP, adjusted for admissibility and counterparty exposure limits and specific valuation differences.

The Group's regulatory capital position statement in Table 1 sets out the different sources of capital held within the Group. The Group's total available capital resources, based on unaudited[1] FSA returns, are £5.1bn (2008: £4.0bn) of which £4.2bn (2008: £2.6bn) is held by the life businesses. The use of capital held by the UK and overseas life businesses is generally constrained by local regulatory requirements, and may not be available to provide funding for other businesses.

The total available capital resources of the Group's with-profits business (with-profits estate) is determined in accordance with the Realistic Balance Sheet rules prescribed by the FSA.

At 31 December 2009, the realistic value of the UK participating liabilities was £15.3bn (2008: £14.7bn) under the FSA realistic capital regime. The excess of realistic assets over realistic liabilities was £0.8bn (2008: £0.6bn). The capital resources reflect the surplus in that part of the fund which is in excess of any constructive obligation to policyholders. The liabilities within the consolidated balance sheet do not include the amount representing the shareholders' share of future bonuses.

1. The FSA returns are audited and filed subsequent to the publication of the Group's capital position.

Table 1 – Regulatory capital position statement

As at 31 December 2009	UK with-profits £m	UK non profit and SRC[1] £m	LPGL £m	Overseas and PMC £m	Total life £m	Shareholders' equity and other activities £m	Total £m
Ordinary shareholders' equity outside the LTF	–	157	703	1,553	2,413	492	2,905
Ordinary shareholders' equity in the LTF	–	1,291	–	–	1,291	–	1,291
Capital and reserves attributable to equity holders of the Company	–	1,448	703	1,553	3,704	492	4,196
Adjustments onto regulatory basis:							
Unallocated divisible surplus	1,249	–	–	35	1,284	–	1,284
Other[2]	(408)	(609)	–	(763)	(1,780)	(227)	(2,007)
Other qualifying capital:							
Subordinated borrowings	–	–	–	–	–	1,815	1,815
Internal loans[3]	–	–	981	–	981	(981)	–
Proposed dividend	–	–	–	–	–	(160)	(160)
Total available capital resources	841	839	1,684	825	4,189	939	5,128
IFRS liability analysis:							
UK participating liabilities on realistic basis:							
– Options and guarantees	723	–	–	–	723	–	723
– Other policyholder obligations	13,447	33	–	–	13,480	–	13,480
Overseas participating liabilities	–	–	–	2,340	2,340	–	2,340
Unallocated divisible surplus	1,249	–	–	35	1,284	–	1,284
Value of in-force non-participating contracts	(367)	–	–	–	(367)	–	(367)
Participating contract liabilities	15,052	33	–	2,375	17,460	–	17,460
Unit linked non-participating life assurance liabilities	554	491	–	1,404	2,449	–	2,449
Non-linked non-participating life assurance liabilities	1,953	21,878	–	2,073	25,904	–	25,904
Unit linked non-participating investment contract liabilities	8,152	18,341	–	208,009	234,502	–	234,502
General insurance liabilities	–	–	–	–	–	230	230
Non-participating contract liabilities	10,659	40,710	–	211,486	262,855	230	263,085

1. UK non profit and SRC includes Nationwide Life Limited and Suffolk Life Annuities Limited.
2. Other consists of shareholders' share in realistic liabilities of £307m and changes to the values of assets and liabilities on a regulated basis of £1,700m.
3. Internal loans wholly comprises the contingent loan (£981m) from Society shareholders' equity to LGPL, which is reflected in the value of LGPL for regulatory purposes.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

As at 31 December 2008	UK with-profits £m	UK non profit and SRC[1] £m	LPGL £m	Overseas and PMC £m	Total life £m	Shareholders' equity and other activities £m	Total £m
Ordinary shareholders' equity outside the LTF	–	166	(373)	1,466	1,259	1,236	2,495
Ordinary shareholders' equity in the LTF	–	1,093	–	–	1,093	–	1,093
Capital and reserves attributable to equity holders of the Company	–	1,259	(373)	1,466	2,352	1,236	3,588
Adjustments onto regulatory basis:							
Unallocated divisible surplus	950	–	–	(37)	913	–	913
Other[2]	(309)	(586)	–	(742)	(1,637)	(285)	(1,922)
Other qualifying capital:							
Subordinated borrowings	–	–	–	–	–	1,570	1,570
Internal loans[3]	–	–	938	–	938	(938)	–
Proposed dividend	–	–	–	–	–	(120)	(120)
Total available capital resources	641	673	565	687	2,566	1,463	4,029
IFRS liability analysis:							
UK participating liabilities on realistic basis							
– Options and guarantees	1,034	–	–	–	1,034	–	1,034
– Other policyholder obligations	12,976	39	–	–	13,015	–	13,015
Overseas participating liabilities	–	–	–	2,327	2,327	–	2,327
Unallocated divisible surplus	950	–	–	(37)	913	–	913
Value of in-force non-participating contracts	(171)	–	–	–	(171)	–	(171)
Participating contract liabilities	14,789	39	–	2,290	17,118	–	17,118
Unit linked non-participating life assurance liabilities	515	457	–	1,387	2,359	–	2,359
Non-linked non-participating life assurance liabilities	1,944	19,070	–	2,255	23,269	–	23,269
Unit linked non-participating investment contract liabilities	6,835	15,300	–	174,517	196,652	–	196,652
General insurance liabilities	–	–	–	–	–	259	259
Non-participating contract liabilities	9,294	34,827	–	178,159	222,280	259	222,539

1. UK non profit and SRC includes Nationwide Life Limited and Suffolk Life Annuities Limited acquired during 2008.
2. Other consists of shareholders' share in realistic liabilities of £179m and changes to the values of assets and liabilities on a regulated basis of £1,743m.
3. Internal loans wholly comprises the contingent loan (£938m) from Society shareholders' equity to LGPL, which is reflected in the value of LGPL for regulatory purposes.

Available regulatory capital resource risks

The Group's available capital resources are sensitive to changes in market conditions, both to changes in the value of the assets and to the impact which 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 and persistency. The most significant sensitivities arise from the following four risks:

- market risk in relation to UK participating business which would crystallise if adverse changes in the value of the assets supporting this business could not be fully reflected in payments to policyholders because of the effect of guarantees and options. The capital position of this business would also deteriorate if increases to the market cost of derivatives resulted in an increase in the liability for guarantees and options in the realistic balance sheet.

- market risk in relation to the UK annuity business, which would crystallise if the return from the fixed interest investments supporting this business were lower than that assumed for reserving.

- mortality risk in relation to the UK annuity business, which would crystallise if the mortality of annuitants improved more rapidly than the assumptions used for reserving.

- mortality risk in relation to the UK and US term assurance businesses, which would crystallise if mortality of the lives insured was higher than that assumed, possibly because of an epidemic.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

46 MANAGEMENT OF CAPITAL RESOURCES (CONTINUED)

A range of management actions is available to mitigate any adverse impact from changing market conditions and experience, including changes to with-profits bonus rates, changes to discretionary surrender terms and charging for guarantees. To the extent that management actions are expected only to offset partially adverse experience, then liabilities would be increased to anticipate the future impact of the adverse experience and total capital resources would be reduced.

Table 2 below provides management estimates of the impact on IGD surplus to changes in market conditions:

Table 2 – IGD sensitivity analysis

	Impact on surplus capital 2009 £m
Sensitivity test	
20% fall in equity values	**(0.3)**
40% fall in equity values	**(0.6)**
15% fall in property values	**(0.1)**
100bp increase in interest rates	**(0.3)**
100bp increase in credit spreads	**(0.1)**

Details of IFRS and EEV sensitivity analysis can be found in Tables 6 and 7 of Note 48.

Movements in life business regulatory capital resources

The movement in the life business regulatory capital resources is shown in Table 3.

Table 3 – Movements in life business regulatory capital resources

	UK with-profits £m	UK non profit and SRC[1] £m	LGPL £m	Overseas and PMC £m	Total life £m
As at 1 January 2009	**641**	**673**	**565**	**687**	**2,566**
Effect of investment variations	**241**	**75**	**(47)**	**3**	**272**
Effect of changes in valuation assumptions	**11**	**52**	**121**	**–**	**184**
Changes in regulatory requirements	**–**	**26**	**39**	**139**	**204**
New business	**(44)**	**(95)**	**67**	**(75)**	**(147)**
Cash distributions	**–**	**(108)**	**–**	**(87)**	**(195)**
Capital contributions	**–**	**–**	**600**	**48**	**648**
Other factors	**(8)**	**216**	**339**	**110**	**657**
As at 31 December 2009	**841**	**839**	**1,684**	**825**	**4,189**

1. UK non profit and SRC includes Nationwide Life Limited and Suffolk Life Annuities Limited acquired in 2008.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

	UK with-profits £m	UK non profit and SRC[1] £m	LGPL[2] £m	Overseas and PMC £m	Total life £m
As at 1 January 2008	1,047	1,130	1,210	562	3,949
Effect of investment variations	(279)	(449)	(250)	15	(963)
Effect of changes in valuation assumptions	(14)	118	(779)	–	(675)
New business	(38)	(187)	(147)	(75)	(447)
Cash distributions	–	(30)	(150)	(83)	(263)
Acquisitions	–	156	–	–	156
Other factors	(75)	(65)	681	268	809
As at 31 December 2008	641	673	565	687	2,566

1. UK non profit and SRC includes Nationwide Life Limited and Suffolk Life Annuities Limited acquired in 2008.
2. Effect of changes in valuation assumptions includes a £650m increase in credit default reserving. The corresponding deferred tax asset is included within Other factors.

47 ASSETS ANALYSIS

The Group has categorised its assets and liabilities in the following disclosure in accordance with the level of shareholder exposure to market and credit risks. The four categorisations presented are:

- **Unit linked**

For unit linked contracts, there is a direct link between the investments and the obligations. Unit linked business is written in both the Society LTF and in the LTF of PMC. The financial risk on these contracts is borne by the policyholders. The Group is, therefore, not directly exposed to any market risk, currency risk or credit risk for these contracts. Detailed risk disclosures have not been presented for unit linked assets and liabilities.

- **With-profits**

Policyholders and shareholders share in the risks and returns of the with-profits part of the Society LTF. The return to shareholders on virtually all participating products is in the form of a transfer to shareholders' equity, which is analogous to a dividend from the Society LTF and is dependent upon the bonuses credited or declared on policies in that year. The bonuses are broadly based on historic and current rates of return on equity, property and fixed income securities, as well as expectations of future investment returns. With-profits also includes participating business in the France operation which shares similar characteristics. The with-profits classification excludes unit linked contracts.

- **Non profit non-unit linked**

Shareholders are exposed to the risk and rewards of ownership of assets backing non profit non-unit linked business held within UK LTFs.

- **Shareholder**

All other assets are classified as shareholder assets. Shareholders of the Group are directly exposed to market and credit risk on these assets. This includes the assets and liabilities of our overseas insurance operations.

The table overleaf presents an analysis of the balance sheet by category. All of the quantitative risk disclosures in Note 48 (Risk management and control) have been provided using this categorisation.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

As at 31 December 2009	Shareholder £m	Non profit non-unit linked £m	With-profits £m	Unit linked £m	Total £m
Assets					
Investment in associates	**45**	**–**	**–**	**–**	**45**
Plant and equipment	**61**	**–**	**–**	**–**	**61**
Investments[1]	**6,906**	**23,362**	**19,575**	**240,544**	**290,387**
Purchased interests in long term business	**146**	**–**	**–**	**–**	**146**
Other operational assets	**2,580**	**2,468**	**260**	**979**	**6,287**
Total assets	**9,738**	**25,830**	**19,835**	**241,523**	**296,926**
Liabilities					
Subordinated borrowings	**1,897**	**–**	**–**	**(27)**	**1,870**
Participating contract liabilities	**–**	**34**	**17,218**	**208**	**17,460**
Non-participating contract liabilities	**1,716**	**22,465**	**1,953**	**236,951**	**263,085**
Senior borrowings	**1,242**	**9**	**40**	**116**	**1,407**
Other liabilities[1]	**2,525**	**1,570**	**577**	**4,232**	**8,904**
Total liabilities	**7,380**	**24,078**	**19,788**	**241,480**	**292,726**

As at 31 December 2008	Shareholder £m	Non profit non-unit linked £m	With-profits £m	Unit linked £m	Total £m
Assets					
Investment in associates	14	–	–	–	14
Plant and equipment	75	–	–	–	75
Investments[1]	7,720	20,589	19,080	201,394	248,783
Purchased interests in long term business	118	109	–	–	227
Other operational assets	2,927	2,405	393	1,515	7,240
Total assets	10,854	23,103	19,473	202,909	256,339
Liabilities					
Subordinated borrowings	1,657	–	–	–	1,657
Participating contract liabilities	–	39	16,890	189	17,118
Non-participating contract liabilities	2,514	19,070	1,944	199,011	222,539
Senior borrowings	2,031	29	74	180	2,314
Other liabilities[1]	2,237	2,761	456	3,525	8,979
Total liabilities	8,439	21,899	19,364	202,905	252,607

1. For risk management purposes, bespoke consolidated CDOs are considered on a net basis. Accordingly, the table above presents derivative liabilities of £118m (2008: £388m) as a deduction to non profit non-unit linked investments and other liabilities.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL

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

Risk management objectives

The Group'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, aligned with the Group's risk appetite, is in place for material exposures.

Risk management approach

A significant part of the Group's business involves the acceptance and management of risk. The Group is exposed to insurance, market, credit, liquidity and operational risks and operates a formal risk management framework to ensure that all significant risks are identified and managed. The risk factors mentioned below should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties.

Insurance risk: the risk arising from higher claims being experienced than anticipated.

Market risk: the risk arising from fluctuations in interest rates, exchange rates, share prices and other relevant market prices.

Credit risk: the risk of loss if another party fails to perform its financial obligations to the Group.

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

Operational risk: the risk arising from inadequate or failed internal processes, people and systems, or from external events.

Contagion risk: the occurrence of a risk in one part of the Group may result in contagion elsewhere in the Group.

An explanation of the risk framework and the methods used to monitor and assess risk exposures can be found in pages 46 to 49.

Management of risks

The Group seeks to manage its exposures 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 in the following sections.

Insurance risk

Insurance risk is implicit in the Group'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. A detailed review of the Group's inherent residual risks associated with insurance products is included on pages 174 to 179. Insurance risk is managed using the following techniques:

Policies and delegated authorities for underwriting, pricing and reinsurance

The Group's insurance risk policy sets out the overall framework for the management of insurance risk. As part of the framework, a structure of delegated pricing and underwriting authorities is in place. Pricing is based on assumptions, such as mortality and persistency, which have regard to past experience and to trends. Insurance exposures are limited through reinsurance. Overall, the Group seeks to be conservative in its acceptance of insurance risks by establishing strict underwriting criteria and limits. The underwriting policy is clearly documented, setting out risks which are unacceptable and the terms applicable for non-standard risks.

Reinsurance is used to reduce potential loss to the Group from individual large risks and catastrophic events. It may also be used to manage capital or to provide access to specialist underwriting expertise. The Group makes extensive use of reinsurance for its UK individual protection business, placing a proportion of all risks meeting prescribed criteria.

The principal General insurance reinsurances are excess of loss catastrophe treaties, under which the cost of claims from a weather event, in excess of an agreed retention level, is recovered from insurers.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Reserving policy
All subsidiaries writing insurance business have a documented reserving policy setting out the basis on which liabilities are to be determined using statistical analysis and actuarial experience. Policies for each subsidiary are in line with locally established actuarial techniques, relevant regulation and legislation. Further details of the assumption setting process are included in Note 34.

Market risk
The Group 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 Group is exposed to these risks are:
- assets backing insurance and investment contracts other than unit linked 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 Group manages market risk using the following methods:

Asset liability matching
The Group manages its assets and liabilities in accordance with relevant regulatory requirements, reflecting the differing types of liabilities it has in each business.

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.

For businesses where a range of asset types, including equity and property, are held to meet liabilities, the Group uses stochastic models to assess the impact of a range of future return scenarios on investment values and associated liabilities. This allows the Group to devise an investment and with-profits policyholder bonus strategy which optimises returns to its policyholders over time, whilst limiting the capital requirements associated with these businesses. The Group uses this method extensively in connection with its UK with-profits business.

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

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

To mitigate the risk that guarantees and commitments are not met, the Group 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 or savings liabilities, the expected rate of return applicable on each class of asset and the capital available to meet the price fluctuations for each asset class, relative to the liabilities they support.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Additionally, fluctuations in interest rates will vary the repayments on variable rate debt issued by the Group (Note 35).

Asset liability matching significantly reduces the Group's exposure to interest rate risk. Sensitivity to interest rate changes is included in Table 2 of Note 46 and Tables 6 and 7 of Note 48.

Inflation risk
Inflation risk is the potential for loss as a result of relative or absolute changes in inflation rates. The Group is exposed to inflation risk in two specific areas.

- Certain non-linked contracts, such as annuities, may provide for future benefits to be paid taking account of changes in the level of inflation. Contracts in payment may also include an annual adjustment for movements in price indices, subject to an annual cap. The Group seeks to manage the risk of movements in price indices through an appropriate investment strategy including the use of inflation swaps.
- In writing long term business, the Group makes assumptions regarding the future costs of product servicing. The assumptions take account of changes in price indices and the costs of employment, with stress testing evaluating the effect of significant deviations on the Group's capital position.

Currency risk
The Group is potentially exposed to loss as a result of fluctuations in the value of, or income from, assets denominated in foreign currencies. The Group manages its currency risk exposure in the following way:

- In respect of long term business assets and liabilities denominated in non-sterling currencies, the Group protects its exposure to exchange rate fluctuations by backing obligations with investments in the same currency.
- Balance sheet foreign exchange currency translation exposure in respect of the Group's international subsidiaries is actively managed in accordance with a policy, agreed by the Group Board, which allows net foreign currency assets to be hedged through the use of derivatives.

As described in Note 47, the Group is not directly exposed to risks on unit linked contracts. Detailed risk disclosures have not been presented for unit linked assets and liabilities.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Table 1 – Currency risk

Table 1 summarises the Group's exposure to foreign currency exchange risk, in sterling. The functional currency represents the currency of the primary economic environment in which each of the Group's subsidiaries operates.

As at 31 December 2009 Shareholder	Sterling £m	Euro £m	US Dollar £m	Japanese Yen £m	Other £m	Functional currency £m	Carrying value £m
Assets							
Investment in associates	–	–	–	–	–	45	45
Plant and equipment	–	–	–	–	–	61	61
Investments	–	799	800	–	30	5,277	6,906
Purchased interests in long term business	–	–	–	–	–	146	146
Other operational assets	–	3	5	–	(5)	2,577	2,580
Total assets	–	802	805	–	25	8,106	9,738
Liabilities							
Subordinated borrowings	–	573	–	–	–	1,324	1,897
Participating contract liabilities	–	–	–	–	–	–	–
Non-participating contract liabilities	31	–	20	–	–	1,665	1,716
Senior borrowings	–	66	–	–	–	1,176	1,242
Other liabilities	–	10	242	–	–	2,273	2,525
Total liabilities	31	649	262	–	–	6,438	7,380
Non profit non-unit linked							
Assets							
Investment in associates	–	–	–	–	–	–	–
Plant and equipment	–	–	–	–	–	–	–
Investments[1]	–	76	7,455	–	19	15,812	23,362
Purchased interests in long term business	–	–	–	–	–	–	–
Other operational assets	–	–	–	–	–	2,468	2,468
Total assets	–	76	7,455	–	19	18,280	25,830
Liabilities							
Subordinated borrowings	–	–	–	–	–	–	–
Participating contract liabilities	–	–	–	–	–	34	34
Non-participating contract liabilities	–	–	–	–	–	22,465	22,465
Senior borrowings	–	–	9	–	–	–	9
Other liabilities[1]	–	92	7,239	–	–	(5,761)	1,570
Total liabilities	–	92	7,248	–	–	16,738	24,078

1. For risk management purposes, bespoke consolidated CDOs are considered on a net basis. Accordingly the table above presents derivative liabilities of £118m as a deduction to non profit non-unit linked investments and other liabilities.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

As at 31 December 2009 **With-profits**	Sterling £m	Euro £m	US Dollar £m	Japanese Yen £m	Other £m	Functional currency £m	Carrying value £m
Assets							
Investment in associates	–	–	–	–	–	–	–
Plant and equipment	–	–	–	–	–	–	–
Investments	–	721	645	406	681	17,122	19,575
Purchased interests in long term business	–	–	–	–	–	–	–
Other operational assets	–	–	1	–	–	259	260
Total assets	**–**	**721**	**646**	**406**	**681**	**17,381**	**19,835**
Liabilities							
Subordinated borrowings	–	–	–	–	–	–	–
Participating contract liabilities	–	–	–	–	–	17,218	17,218
Non-participating contract liabilities	–	–	–	–	–	1,953	1,953
Senior borrowings	–	–	–	–	–	40	40
Other liabilities	–	19	23	1	(1)	535	577
Total liabilities	**–**	**19**	**23**	**1**	**(1)**	**19,746**	**19,788**

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Table 1 – Currency risk (continued)

As at 31 December 2008 **Shareholder**	Sterling £m	Euro £m	US Dollar £m	Japanese Yen £m	Other £m	Functional currency £m	Carrying value £m
Assets							
Investment in associates	–	–	–	–	–	14	14
Plant and equipment	–	–	–	–	–	75	75
Investments	–	886	423	59	87	6,265	7,720
Purchased interests in long term business	–	–	–	–	–	118	118
Other operational assets	–	1	3	–	(2)	2,925	2,927
Total assets	–	887	426	59	85	9,397	10,854
Liabilities							
Subordinated borrowings	–	539	–	–	–	1,118	1,657
Participating contract liabilities	–	–	–	–	–	–	–
Non-participating contract liabilities	25	1	13	–	1	2,474	2,514
Senior borrowings	–	92	–	–	–	1,939	2,031
Other liabilities	–	272	848	–	–	1,117	2,237
Total liabilities	25	904	861	–	1	6,648	8,439
Non profit non-unit linked							
Assets							
Investment in associates	–	–	–	–	–	–	–
Plant and equipment	–	–	–	–	–	–	–
Investments[1]	–	1,576	4,435	–	–	14,578	20,589
Purchased interests in long term business	–	–	–	–	–	109	109
Other operational assets	–	–	3	–	–	2,402	2,405
Total assets	–	1,576	4,438	–	–	17,089	23,103
Liabilities							
Subordinated borrowings	–	–	–	–	–	–	–
Participating contract liabilities	–	–	–	–	–	39	39
Non-participating contract liabilities	–	–	–	–	–	19,070	19,070
Senior borrowings	–	–	–	–	–	29	29
Other liabilities[1]	–	1,545	4,423	–	–	(3,207)	2,761
Total liabilities	–	1,545	4,423	–	–	15,931	21,899

1. For risk management purposes, bespoke consolidated CDOs are considered on a net basis. Accordingly, the table above presents derivative liabilities of £388m as a deduction to non profit non-unit linked investments and other liabilities.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

As at 31 December 2008 **With-profits**	Sterling £m	Euro £m	US Dollar £m	Japanese Yen £m	Other £m	Functional currency £m	Carrying value £m
Assets							
Investment in associates	–	–	–	–	–	–	–
Plant and equipment	–	–	–	–	–	–	–
Investments	–	646	665	443	457	16,869	19,080
Purchased interests in long term business	–	–	–	–	–	–	–
Other operational assets	–	1	5	1	6	380	393
Total assets	–	647	670	444	463	17,249	19,473
Liabilities							
Subordinated borrowings	–	–	–	–	–	–	–
Participating contract liabilities	–	–	–	–	–	16,890	16,890
Non-participating contract liabilities	–	–	–	–	–	1,944	1,944
Senior borrowings	–	–	–	–	–	74	74
Other liabilities	–	264	302	–	–	(110)	456
Total liabilities	–	264	302	–	–	18,798	19,364

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

Table 2 – Currency sensitivity analysis

Currency sensitivity test	**Impact on pre-tax profit 2009 £m**	**Impact on equity 2009 £m**	Impact on pre-tax profit 2008 £m	Impact on equity 2008 £m
10% Euro appreciation	**14**	**10**	1	1
10% US Dollar appreciation	**75**	**54**	(42)	(29)

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 Group controls its exposure to geographic price risks by using internal country credit ratings. These ratings are based on macroeconomic data and key qualitative indicators. The latter take into account economic, social and political environments. Table 3 indicates the Group's exposure to different equity markets around the world. Unit linked equity investments are excluded from the table as the risk is retained by the policyholder.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Table 3 – Exposure to worldwide equity markets

	Shareholder 2009 £m	Non profit non-unit linked 2009 £m	With-profits 2009 £m	Total 2009 £m	Shareholder 2008 £m	Non profit non-unit linked 2008 £m	With-profits 2008 £m	Total 2008 £m
UK	439	–	2,029	2,468	697	69	1,968	2,734
North America	26	–	369	395	61	–	353	414
Europe	27	–	676	703	230	–	529	759
Japan	–	–	404	404	70	–	433	503
Asia Pacific	46	–	461	507	26	–	335	361
Other	3	–	57	60	58	–	8	66
Listed equities	541	–	3,996	4,537	1,142	69	3,626	4,837
Unlisted UK equities	85	–	16	101	9	–	66	75
Holdings in unit trusts	230	–	449	679	166	–	429	595
Total equities	856	–	4,461	5,317	1,317	69	4,121	5,507

The Group holds non-unit linked property investments totalling £139m (2008: £189m), of which £132m (2008: £182m) are located in the UK.

Credit risk

The Group's credit risk policy defines the overall framework for the management of credit risk. Significant areas where the Group is exposed to credit risk are:

- The Group holds corporate bonds 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 Group limits its exposure to insurance risk by ceding part of the risks it assumes to the reinsurance market. To limit the risk of reinsurer default the Group operates a credit rating policy when arranging cover. When selecting new reinsurance partners the Group considers only companies which have a minimum credit rating equivalent to A- from Standard & Poor's. Exposure limits for new and existing reinsurers are determined based on credit ratings and projected exposure.

Aggregate counterparty exposures are regularly monitored both at an individual subsidiary level and on a Groupwide basis.

The credit profile of the Group's assets exposed to credit risk is shown in Table 4. The credit rating bands are provided by independent rating agencies. For unrated assets, the Group maintains internal ratings which are used to manage exposure to these counterparties. Unit linked assets have not been included as shareholders are not directly exposed to risk.

The carrying amount of non-unit linked assets included in the balance sheet represents the maximum credit exposure.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Table 4 – Exposure to credit risk

As at 31 December 2009	Notes	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated bespoke CDOs £m	Unrated other £m	Total £m
Shareholder									
Government securities		832	25	5	1	–	–	–	863
Other fixed rate securities		297	185	920	631	74	–	39	2,146
Variable rate securities		510	108	149	52	14	–	55	888
Total debt securities	19i	1,639	318	1,074	684	88	–	94	3,897
Accrued interest	19i	14	3	15	12	2	–	1	47
Loans and receivables	19ii	–	16	23	–	–	–	91	130
Derivative assets	20	–	108	149	–	–	–	–	257
Cash and cash equivalents[1]	27	114	421	780	–	–	–	266	1,581
Financial assets		1,767	866	2,041	696	90	–	452	5,912
Reinsurers' share of contract liabilities	21	16	34	147	–	–	–	83	280
Other assets	26	80	57	80	13	–	–	222	452
		1,863	957	2,268	709	90	–	757	6,644

1. 'A' rated cash and cash equivalents include £246m (2008: £301m) holdings in commercial paper which are short term instruments which carry a short term rating of A1+/A1 from Standard & Poor's.

	Notes	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated bespoke CDOs £m	Unrated other £m	Total £m
Non profit non-unit linked									
Government securities		547	25	6	–	–	–	–	578
Other fixed rate securities		914	1,444	7,078	6,025	546	–	590	16,597
Variable rate securities[1]		1,148	492	1,065	238	32	1,104	158	4,237
Total debt securities	19i	2,609	1,961	8,149	6,263	578	1,104	748	21,412
Accrued interest	19i	21	30	156	134	14	–	9	364
Loans and receivables	19ii	–	1	–	–	–	–	–	1
Derivative assets	20	5	274	990	–	–	–	–	1,269
Cash and cash equivalents[1]	27	27	71	218	–	–	–	–	316
Financial assets		2,662	2,337	9,513	6,397	592	1,104	757	23,362
Reinsurers' share of contract liabilities	21	31	689	872	–	–	–	32	1,624
Other assets	26	–	1	–	–	–	–	118	119
		2,693	3,027	10,385	6,397	592	1,104	907	25,105

1. For risk management purposes, bespoke consolidated CDOs are considered net. For presentation in the balance sheet the components of the CDOs are shown within investments (£956m), cash equivalents (£266m) and derivative liabilities (£118m).

	Notes	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated bespoke CDOs £m	Unrated other £m	Total £m
With-profits									
Government securities		2,093	51	56	19	–	–	1	2,220
Other fixed rate securities		3,905	854	2,645	1,365	126	–	513	9,408
Variable rate securities		117	33	51	4	–	–	5	210
Total debt securities	19i	6,115	938	2,752	1,388	126	–	519	11,838
Accrued interest	19i	102	22	66	43	3	–	11	247
Loans and receivables	19ii	–	148	147	–	–	–	1	296
Derivative assets	20	–	1	58	–	–	–	4	63
Cash and cash equivalents	27	145	126	1,062	–	–	–	–	1,333
Financial assets		6,362	1,235	4,085	1,431	129	–	535	13,777
Reinsurers' share of contract liabilities	21	–	–	1	–	–	–	2	3
Other assets	26	–	–	–	–	–	–	101	101
		6,362	1,235	4,086	1,431	129	–	638	13,881

At the year end, the Group held £793m (2008: £1,023m) of collateral in respect of non-unit linked derivative assets.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Table 4 – Exposure to credit risk (continued)

As at 31 December 2008	Notes	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated bespoke CDOs £m	Unrated other £m	Total £m
Shareholder									
Government securities		805	25	2	–	–	–	–	832
Other fixed rate securities		454	158	881	528	13	–	42	2,076
Variable rate securities		541	127	132	66	2	–	51	919
Total debt securities	19i	1,800	310	1,015	594	15	–	93	3,827
Accrued interest	19i	21	5	17	12	–	–	1	56
Loans and receivables	19ii	–	4	6	–	–	–	88	98
Derivative assets	20	–	135	170	–	–	–	–	305
Cash and cash equivalents	27	166	549	1,191	–	–	–	23	1,929
Financial assets		1,987	1,003	2,399	606	15	–	205	6,215
Reinsurers' share of contract liabilities	21	8	158	31	1	11	–	103	312
Other assets	26	–	36	87	16	–	–	347	486
		1,995	1,197	2,517	623	26	–	655	7,013
Non profit non-unit linked									
Government securities		663	12	–	–	–	–	–	675
Other fixed rate securities		1,126	1,522	6,022	3,437	161	–	623	12,891
Variable rate securities[1]		977	473	963	252	–	878	94	3,637
Total debt securities	19i	2,766	2,007	6,985	3,689	161	878	717	17,203
Accrued interest	19i	31	37	161	90	7	–	9	335
Loans and receivables	19ii	–	–	–	–	–	–	–	–
Derivative assets	20	11	654	1,326	3	–	–	–	1,994
Cash and cash equivalents	27	362	148	478	–	–	–	–	988
Financial assets		3,170	2,846	8,950	3,782	168	878	726	20,520
Reinsurers' share of contract liabilities	21	4	1,072	419	–	–	–	42	1,537
Other assets	26	–	1	–	–	–	–	120	121
		3,174	3,919	9,369	3,782	168	878	888	22,178

1. For risk management purposes, bespoke consolidated CDOs are considered net. For presentation in the balance sheet the components of the CDOs are shown within variable rate securities (£1,266m) and derivative liabilities (£388m).

With-profits									
Government securities		1,991	6	–	–	–	–	–	1,997
Other fixed rate securities		3,455	957	2,767	1,123	44	–	587	8,933
Variable rate securities		158	37	62	3	–	–	5	265
Total debt securities	19i	5,604	1,000	2,829	1,126	44	–	592	11,195
Accrued interest	19i	95	26	77	35	3	–	15	251
Loans and receivables	19ii	–	70	25	–	–	–	187	282
Derivative assets	20	–	7	59	–	–	–	–	66
Cash and cash equivalents	27	114	91	1,326	–	–	–	3	1,534
Financial assets		5,813	1,194	4,316	1,161	47	–	797	13,328
Reinsurers' share of contract liabilities	21	–	1	–	–	–	–	13	14
Other assets	26	–	–	–	–	–	–	163	163
		5,813	1,195	4,316	1,161	47	–	973	13,505

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Table 5 provides information regarding the carrying value of financial assets which have been impaired and the ageing analysis of financial assets which are past due but not impaired. Unit linked assets have not been included as shareholders are not exposed to the risks from unit linked policies.

Table 5 – Ageing of financial assets that are past due but not impaired

As at 31 December 2009	Notes	Neither past due nor impaired £m	Financial assets that are past due but not impaired 0-3 months £m	3-6 months £m	6 months-1 year £m	Over 1 year £m	Financial assets that have been impaired £m	Carrying value £m
Shareholder								
Government securities		**863**	**–**	**–**	**–**	**–**	**–**	**863**
Other fixed rate securities		**2,146**	**–**	**–**	**–**	**–**	**–**	**2,146**
Variable rate securities		**883**	**–**	**–**	**–**	**5**	**–**	**888**
Total debt securities	19i	**3,892**	**–**	**–**	**–**	**5**	**–**	**3,897**
Accrued interest	19i	**47**	**–**	**–**	**–**	**–**	**–**	**47**
Loans and receivables	19ii	**130**	**–**	**–**	**–**	**–**	**–**	**130**
Derivative assets	20	**257**	**–**	**–**	**–**	**–**	**–**	**257**
Cash equivalents	27	**1,372**	**10**	**–**	**–**	**–**	**–**	**1,382**
Financial assets		**5,698**	**10**	**–**	**–**	**5**	**–**	**5,713**
Reinsurers' share of contract liabilities	21	**280**	**–**	**–**	**–**	**–**	**–**	**280**
Other assets	26	**429**	**19**	**1**	**–**	**3**	**–**	**452**
		6,407	**29**	**1**	**–**	**8**	**–**	**6,445**
Non profit non–unit linked								
Government securities		**578**	**–**	**–**	**–**	**–**	**–**	**578**
Other fixed rate securities		**16,597**	**–**	**–**	**–**	**–**	**–**	**16,597**
Variable rate securities[1]		**4,237**	**–**	**–**	**–**	**–**	**–**	**4,237**
Total debt securities	19i	**21,412**	**–**	**–**	**–**	**–**	**–**	**21,412**
Accrued interest	19i	**364**	**–**	**–**	**–**	**–**	**–**	**364**
Loans and receivables	19ii	**1**	**–**	**–**	**–**	**–**	**–**	**1**
Derivative assets	20	**1,269**	**–**	**–**	**–**	**–**	**–**	**1,269**
Cash equivalents	27	**218**	**–**	**–**	**–**	**–**	**–**	**218**
Financial assets		**23,264**	**–**	**–**	**–**	**–**	**–**	**23,264**
Reinsurers' share of contract liabilities	21	**1,624**	**–**	**–**	**–**	**–**	**–**	**1,624**
Other assets	26	**17**	**97**	**2**	**1**	**2**	**–**	**119**
		24,905	**97**	**2**	**1**	**2**	**–**	**25,007**

1. For risk management purposes, bespoke consolidated CDOs are considered net. For presentation in the balance sheet the components of the CDOs are shown within investments (£956m), cash equivalents (£266m) and derivative liabilities (£118m).

With profits								
Government securities		**2,220**	**–**	**–**	**–**	**–**	**–**	**2,220**
Other fixed rate securities		**9,408**	**–**	**–**	**–**	**–**	**–**	**9,408**
Variable rate securities		**210**	**–**	**–**	**–**	**–**	**–**	**210**
Total debt securities	19i	**11,838**	**–**	**–**	**–**	**–**	**–**	**11,838**
Accrued interest	19i	**247**	**–**	**–**	**–**	**–**	**–**	**247**
Loans and receivables	19ii	**296**	**–**	**–**	**–**	**–**	**–**	**296**
Derivative assets	20	**63**	**–**	**–**	**–**	**–**	**–**	**63**
Cash equivalents	27	**1,271**	**–**	**–**	**–**	**–**	**–**	**1,271**
Financial assets		**13,715**	**–**	**–**	**–**	**–**	**–**	**13,715**
Reinsurers' share of contract liabilities	21	**3**	**–**	**–**	**–**	**–**	**–**	**3**
Other assets	26	**72**	**25**	**–**	**1**	**3**	**–**	**101**
		13,790	**25**	**–**	**1**	**3**	**–**	**13,819**

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Table 5 – Ageing of financial assets that are past due but not impaired (continued)

As at 31 December 2008	Notes	Neither past due nor impaired £m	Financial assets that are past due but not impaired 0-3 months £m	3-6 months £m	6 months-1 year £m	Over 1 year £m	Financial assets that have been impaired £m	Carrying value £m
Shareholder								
Government securities		832	–	–	–	–	–	832
Other fixed rate securities[1]		2,076	–	–	–	–	23	2,076
Variable rate securities		915	–	–	–	4	–	919
Total debt securities	19i	3,823	–	–	–	4	23	3,827
Accrued interest	19i	56	–	–	–	–	–	56
Loans and receivables	19ii	98	–	–	–	–	–	98
Derivative assets	20	305	–	–	–	–	–	305
Cash equivalents	27	1,692	–	–	–	–	–	1,692
Financial assets		5,974	–	–	–	4	23	5,978
Reinsurers' share of contract liabilities	21	312	–	–	–	–	–	312
Other assets	26	453	25	3	3	2	4	486
		6,739	25	3	3	6	27	6,776

1. The £23m of debt securities that have been impaired include Other fixed rate securities in the US, primarily Lehman Brothers (£15m) and Harrah's (£4m).

Non profit non–unit linked								
Government securities		675	–	–	–	–	–	675
Other fixed rate securities		12,891	–	–	–	–	–	12,891
Variable rate securities[1]		3,637	–	–	–	–	–	3,637
Total debt securities	19i	17,203	–	–	–	–	–	17,203
Accrued interest	19i	335	–	–	–	–	–	335
Loans and receivables	19ii	–	–	–	–	–	–	–
Derivative assets	20	1,994	–	–	–	–	–	1,994
Cash equivalents	27	856	–	–	–	–	–	856
Financial assets		20,388	–	–	–	–	–	20,388
Reinsurers' share of contract liabilities	21	1,537	–	–	–	–	–	1,537
Other assets	26	22	74	9	9	7	10	121
		21,947	74	9	9	7	10	22,046

1. For risk management purposes, bespoke consolidated CDOs are considered net. For presentation in the balance sheet the components of the CDOs are shown within variable rate securities (£1,266m) and derivative liabilities (£388m).

With profits								
Government securities		1,997	–	–	–	–	–	1,997
Other fixed rate securities		8,933	–	–	–	–	–	8,933
Variable rate securities		265	–	–	–	–	–	265
Total debt securities	19i	11,195	–	–	–	–	–	11,195
Accrued interest	19i	251	–	–	–	–	–	251
Loans and receivables	19ii	282	–	–	–	–	–	282
Derivative assets	20	66	–	–	–	–	–	66
Cash equivalents	27	1,434	–	–	–	–	–	1,434
Financial assets		13,228	–	–	–	–	–	13,228
Reinsurers' share of contract liabilities	21	14	–	–	–	–	–	14
Other assets	26	138	21	1	1	2	2	163
		13,380	21	1	1	2	2	13,405

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Liquidity risk
The Group's liquidity risk policy defines the overall framework for the management of liquidity risk. The Group 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 Legal & General's insurance businesses may be exposed primarily stem from low probability events that if not adequately planned for may result in unanticipated liquidity requirements. Such events may include a flu pandemic or natural disaster leading to significantly higher levels of claims than would normally be expected and extreme market conditions impacting the timing of cash flows or the ability to realise investments at a given value within a specified timeframe. Collateral requirements for derivative/futures transactions and other types of financial instrument can also give rise to liquidity risk if sufficient cash or suitable alternative assets are not available to meet collateral calls when due. At a Group level, liquidity risk may arise in extreme market conditions, should the Group be unable to issue short term debt or commercial paper.

A limited level of contingent liquidity risk is an accepted element of writing contracts of insurance. However, the Group's insurance businesses seek 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 benchmarks. The level of insurance funds held in cash and other readily realisable assets at 31 December 2009 was £2.2bn.

In addition to each insurance fund maintaining a pool of liquid assets, the Group's Treasury function provides formal facilities to the Group's operating subsidiaries to cover contingent liquidity requirements arising from more extreme events and where investment assets may not be readily realisable. The facility available to each subsidiary is determined through analysis of potential shock events and the potential timing differences that may arise in cash flows.

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

Annuities: Potential for liquidity risk arises within two specific aspects of the Group's annuity businesses – (i) future pension commitments and (ii) risk hedging strategies.

(i) Future pension commitments - Once business has been written, cash outflows for pensions in payment are generally predictable, enabling the Group 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 cash outflows over the long term, trends are gradual, providing opportunity to respond with appropriate risk mitigation strategies.

(ii) Risk hedging strategies - As part of the investment asset management strategy for the Group's UK annuities 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. Financial instruments are also used to mitigate the impact of rating downgrades and defaults within corporate bond portfolios. The use of such financial instruments can require the posting of collateral with counterparties, and as such an appropriate pool of the asset types specified by counterparties must either be held or readily available. In this context, the Group's annuities business held a coverage ratio of 3.5 times its required collateral as at 31 December 2009. Liquidity requirements in excess of the surplus assets would be met by funds held by the Group's Treasury function.

Typically within the overall fund of investment assets held to meet the long term liabilities arising from annuity business, £550m is held in cash and other highly liquid investment types for general liquidity purposes.

Protection: Potential for liquidity risk within the Group's protection businesses may arise should the rate of claims diverge significantly from that anticipated, typically as a consequence of an extreme event.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

The risk of being unable to settle claims as they fall due is actively managed with provision being made and cash pools maintained within investment portfolios for a prudent estimate of the potential claims that may arise from in-force business, taking account of extreme events. Such provisions are validated using stress tests. The use of reassurance also acts to mitigate liquidity; the effect of the treaties being to limit the Group's liability for the overall sums assured, with a recovery being made from the reinsurance counterparty for that element of the claim covered by the treaty. Whilst timing differences can arise between the payment of claims and reimbursement by reinsurance counterparties, the Group seeks to ensure that these are accommodated from cash pools and intra-group facilities.

With-profits: Exposure to liquidity risk may arise if the profile of investment assets held to meet obligations to with-profits policyholders is not aligned with the maturity profile of policies, or the profile does not adequately take account of the rights of policyholders to exercise options or guarantees to specified early surrender terms or minimum rates of return.

Liquidity risk associated with with-profits business is managed through the analysis of the maturity profile of the fund taking account of projected future levels of bonus, policyholders reasonable expectations and projected early withdrawals, and ensuring that an appropriate proportion of the fund is held in cash or other readily realisable assets to meet each tranche of maturities and anticipated early withdrawals as they fall due. Where policyholders have discretion to require early payment of policy proceeds (for example by requesting a surrender value), appropriate contractual safeguards are in place to ensure that the fund and remaining policyholders are not disadvantaged should a material number of policyholders exercise this discretion.

Unit linked business: Investment risks associated with unit linked business, including those associated with liquidity, are generally borne by the holders of units in these funds. Liquidity risk specifically arises for unit holders in that certain asset classes in which the funds invest such as property in certain market conditions may not be readily realisable or only realisable in a specified timeframe at a diminution of value. Liquidity risks associated with these asset classes are documented and communicated to customers in point of sale product literature. Product terms & conditions also highlight that for certain product types that include asset classes that may be illiquid, the Group retains the right to defer the processing of fund withdrawal requests for up to six months, should underlying assets need to be realised to meet payment requests. To minimise the need to invoke these terms, the funds seek to maintain sufficient holdings in cash assets to meet foreseeable withdrawal activity.

The Group's treasury function manages the Group's banking relationships, capital raising activities, overall cash and liquidity position and the payment of dividends. 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. The Group has in place a £960m syndicated borrowing facility, expiring in 2012, which provides flexibility in the management of the Group's liquidity.

Other risks

Operational risk

All business managers are required to confirm regularly the adequacy of controls over operational risks to business unit Risk and Compliance Committees (RCCs), the Group Risk Committee and the Group Audit Committee. Significant control issues which business areas identify are escalated to business unit RCCs, which oversee their resolution. There are a number of categories under which operational risk and its management across the Group can be considered, and these are outlined in the following paragraphs.

Internal process failure

The Group is potentially exposed to the risk of loss from failure of the internal processes with which it transacts its business. Each subsidiary is responsible for ensuring the adequacy of the controls over its processes and regular reviews are undertaken of their appropriateness and effectiveness.

People

The Group is potentially exposed to the risk of loss from inappropriate actions by its staff. The risk is actively managed by business management and human resource (HR) functions. Recruitment is managed centrally by HR functions, and all new recruits undergo a formal induction programme. All employees have job descriptions setting out their accountabilities and reporting lines, and are appraised annually in accordance with agreed performance management frameworks. Employees in regulated subsidiaries 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Outsourcing
The Group 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 key 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 Legal Risk framework, which defines minimum standards of control to be applied to minimise the risk of loss.

Compliance
Compliance risk within the Group 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. A Group compliance function has oversight of the Group's compliance with conduct of business requirements and standards, providing policy advice and guidance and oversight of compliance arrangements and responsibilities.

Event
Event risk relates to the potential for loss arising from significant external events such as terrorism, financial crisis, major changes in fiscal systems or disaster. Typically, such events have a low likelihood of occurrence, a material impact and can be difficult to prevent. The Group'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 Group 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 fully validate claims and ensure that only bona fide claims are settled. Anti-fraud techniques are regularly updated to mitigate risks and emerging threats. The Group'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 Group has contact. A formal code of ethics sets out the Group's expectations in this respect. Effective and honest communication is essential if malpractice is to be effectively dealt with. The Group has defined whistle blowing procedures to enable all employees and those who work with Legal & General to raise matters of concern relating to Legal & General in confidence. Personnel independent of the business reporting line act as designated whistle blowing contacts and include the heads of Internal Audit and Group Compliance. The Group also operates a hotline facility to report concerns, either in confidence or anonymously.

Technology
The Group places a high degree of reliance on IT in its business activities. The failure of IT systems could potentially expose the Group to significant business disruption and loss. To mitigate this risk, standards and methodologies for developing, testing and operating IT systems are maintained. There is a centralised management for development activity and production systems to ensure consistency and adherence to standards. 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. All records are remotely backed up and computer suites are equipped with alternative power sources.

Contagion risk
The potential for contagion risk arises as a consequence of:
- the use of a common brand across the majority of the Group;
- the provision of intra-group loans and indemnities.

The Group has defined policies and procedures for managing matters that may have reputational implications, to ensure that Legal & General's position is correctly understood. The Group also has defined policies for the provision of guarantees, indemnities and letters of comfort.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Concentration of risk

As part of the ongoing risk assessment processes the Group considers the concentration of risk. The Group seeks to manage concentrations by setting limits around the maximum exposure to loss that it can tolerate from a series of related events. Limits set include maximum exposures to single lives, geographic locations, financial instruments and reinsurance balances.

Long term insurance risks

UK long term insurance products are structured as either participating or non-participating. The level of shareholders' interest in the value of policies and their share of the related profit or loss varies depending upon the contract structure.

Non-participating contracts

Non-participating business is written mainly in the non profit part of the Society LTF. Profits accrue solely to shareholders. In addition, there is some non-participating business in the with-profits part of the Society LTF where the profits are shared between participating policyholders and shareholders.

Protection business (individual and group)

The Group offers protection products which provide mortality or morbidity benefits. They may include health, disability, critical illness and accident benefits; these additional benefits are commonly provided as supplements to main life policies but can also be sold separately. The benefit amounts would usually be specified in the policy terms. Some sickness benefits cover the policyholder's mortgage repayments and are linked to the prevailing mortgage interest rates. In addition to these benefits, some contracts may guarantee premium rates, provide guaranteed insurability benefits and offer policyholders conversion options.

Life savings business

A range of contracts are offered in a variety of different forms to meet customers' long term savings objectives. Policyholders may choose to include a number of protection benefits within their savings contracts. Typically, any guarantees under the contract would only apply on maturity or earlier death. On certain older contracts there may be provisions guaranteeing surrender benefits. Savings contracts may or may not guarantee policyholders an investment return. Where the return is guaranteed, the Group may be exposed to interest rate risk with respect to the backing assets.

Pensions (individual and corporate)

These are long term savings contracts through which policyholders accumulate pension benefits. Some older contracts contain a basic guaranteed benefit expressed as an amount of pension payable or a guaranteed annuity option, which exposes the Group to interest rate and longevity risk. These guarantees become more costly during periods when interest rates are low or when annuitant mortality improves faster than expected. The ultimate cost will also depend on the take-up rate of any option and the final form of annuity selected by the policyholder.

Other options provided by these contracts include an open market option on maturity, early retirement and late retirement. The Group would generally have discretion over the terms on which these options are offered.

Annuities

Deferred and immediate annuity contracts are offered. Immediate annuities provide a regular income stream to the policyholder, purchased with a lump sum investment, where the income stream starts immediately after the purchase. The income stream from a deferred annuity is delayed until a specified future date. Bulk annuities are also offered, where the Group accepts the assets and liabilities of a company pension scheme or a life fund.

Non-participating deferred annuities written by the Group do not contain guaranteed cash options.

Annuity products provide guaranteed income for a specified time, usually the life of the policyholder, in exchange for a lump sum capital payment. No surrender value is available under any of these products. The primary risks to the Group from annuity products are therefore mortality improvements and investment performance.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

There is a block of immediate and deferred annuities within the UK non profit business with benefits linked to changes in the RPI, but with contractual maximum or minimum increases. In particular, most of these annuities have a provision that the annuity will not reduce if RPI becomes negative. The total of such annuities in payment at 31 December 2009 was £242m (2008: £226m). Thus, 1% negative inflation, which was reversed in the following year would result in a guarantee cost of approximately £2m (2008: £2m). Negative inflation sustained over a longer period would give rise to significantly greater guarantee costs. Some of these guarantee costs have been partially matched through the purchase of negative inflation hedges and limited price indexation swaps.

Key risk factors
(a) Insurance risk
(i) Mortality
For contracts providing death benefits, higher mortality rates would lead to an increase in claims costs. For annuity contracts, the Group is exposed to the risk that mortality experience is lower than assumed; lower than expected mortality would require payments to be made for longer and increase the cost of benefits provided. The Group regularly reviews its mortality experience and industry projections of longevity and adjusts the valuation and pricing assumptions accordingly.

The Group is exposed to mortality risk on protection and annuity business. For protection products, the Group has entered into reinsurance arrangements to mitigate this risk and provide financing.

(ii) Persistency
In the early years of a policy, lapses and surrenders are likely to result in a loss to the Group, as the acquisition costs associated with the contract would not have been recovered from product margins. Some contracts include surrender deductions to mitigate this risk.

In later periods, once the acquisition costs have been recouped, the effect of lapses and surrenders depends upon the relationship between the exit benefit, if any, and the liability for that contract. Exit benefits are not generally guaranteed and the Group has some discretion in determining the amount of the payment. As a result, the effect on profit at later duration is expected to be broadly neutral.

Following the adoption of PS06/14 in 2006 the persistency assumption for non-participating protection business allows for the expected pattern of persistency, adjusted to incorporate a margin for adverse deviation.

There is no persistency risk exposure for annuities in payment, and these contracts do not provide a lapse or surrender option.

(iii) Morbidity rates
The cost of health related claims depends on both the incidence of policyholders becoming ill and the duration over which they remain ill. Higher than expected incidence or duration would increase costs over the level currently assumed in the calculation of liabilities.

(iv) Expense variances
Higher expenses and/or expense inflation will tend to increase the amount of the reserves required. The Group is exposed to the risk that its liabilities are not sufficient to cover future expenses.

(v) Geographic concentrations of risk
Insurance risk may be concentrated in geographic regions, altering the risk profile of the Group. The most significant exposure of this type arises for the group protection business, where a single event could result in a large number of related claims. To reduce the overall exposure, current contracts include an 'event limit' which caps the total liability. Additionally, excess of loss reinsurance arrangements further mitigate the exposure.

(vi) Epidemics
The spread of an epidemic could cause large aggregate claims across the Group's portfolio. Quota share reinsurance contracts are used to manage this risk. The management of associated counterparty risks from the use of reinsurance is set out on page 166. Depending on the nature of an epidemic, mortality experience may lead to a reduction in the cost of claims for annuity business.

(vii) Accumulation of risks
There is limited potential for single incidents to give rise to a large number of claims across the different contract types written by the Group. In particular, there is little significant overlap between the long term and short term insurance business written by the Group. However, there are potentially material correlations of insurance risk with other types of risk exposure. These correlations are difficult to estimate though they would tend to be more acute as the underlying risk scenarios became more extreme. An example of the accumulation of risk is the correlation between reinsurer credit risk with mortality and morbidity exposures.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

(b) Market risk

Investment of the assets backing the Group liabilities reflects the nature of the liabilities being supported. For non-participating business, the strategy is to invest in fixed income securities of appropriate maturity dates. The risk of default on fixed interest securities is managed through diversified portfolios with exposure limits for individual economies, sectors and counterparties.

Interest rate risk is reduced by managing the duration and maturity structure of each investment portfolio in relation to the estimated cash flows of the liabilities it supports. A number of derivatives are held to enable the closer matching of assets and liabilities and to mitigate further exposure to interest rate movements, in particular, to limit the exposure to any options and guarantees in contracts.

In addition, the exposure to these risks is allowed for in the actuarial valuation of liabilities under these contracts.

Participating contracts

Participating contracts are supported by the with-profits part of the Society LTF. They offer policyholders the possibility of the payment of benefits in addition to those guaranteed by the contract. The amount and timing of the additional benefits (usually called bonuses) are contractually at the discretion of the Group.

Discretionary increases to benefits on participating contracts are allowed in one or both of annual and final bonus form. These bonuses are determined in accordance with the principles outlined in the Group's PPFM for the management of the with-profits part of the Society LTF. The principles include:

- The with-profits part of the Society LTF will be managed with the objective of ensuring that its assets are sufficient to meet its liabilities without the need for additional capital.
- With-profits policies have no expectation of any distribution from the with-profits part of the Society LTF's inherited estate. The inherited estate is the excess of assets held within the Society LTF over and above the amount required to meet liabilities, including those which arise from the regulatory duty to treat customers fairly in settling discretionary benefits.
- Bonus rates will be smoothed so that some of the short term fluctuations in the value of the investments of the with-profits part of the Society LTF and the business results achieved in the with-profits part of the UK LTF are not immediately reflected in payments under with-profits policies.

At 30 June 2005 an assessment was made of the expected cost of guarantees and options to be paid in the future, and funds with the same value to meet these costs were allocated from the capital in the with-profits sub-fund. The value of the funds is regularly assessed and is reduced by the cost of guarantees and options paid since 1 July 2005. At each assessment point, if the value of the funds is lower than the expected cost of guarantees and options, it is possible to make deductions from asset shares to cover the difference. It is intended to limit deductions to no more than 0.75% each year, up to a maximum of 5% per policy.

Following the movement in the expected cost and the value of the associated funds up to 31 December 2009, and in accordance with the Group's PPFM, a refund of 0.4% was made to the asset shares. This followed a deduction of 0.75% made in respect of the year to 31 December 2008. In the technical provisions, allowance has also been made for future deductions in respect of the expected costs of meeting future guarantees and options not covered by the current year deduction. For policyholders who decide to surrender a charge will generally be made in respect of the expected cost of guarantees and options not covered by the charge already taken.

Some older participating contracts include a guaranteed minimum rate of roll up of the policyholder's fund up to the date of retirement or maturity.

The nature of the participating contracts written in the with-profits part of the Society LTF is that more emphasis can be placed on investing to maximise future investment returns. This results in a broader range of investments being held within the fund.

With-profits bonds

These contracts provide an investment return to the policyholder which is determined by the attribution of regular and final bonuses over the duration of the contract. In addition, the contracts provide a death benefit, typically of 101% of the value of the units allocated to the policyholder.

Pension contracts

The Group has sold pension contracts containing guaranteed annuity options which expose the Group to both interest rate and longevity risk. The market consistent value of these guarantees carried in the balance sheet is £31m (2008: £48m).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Deferred annuity contracts

The Group has written some deferred annuity contracts which guaranteed minimum pensions. These options expose the Group to interest rate and longevity risk as the cost would be expected to increase with decreasing interest rates and improved longevity. The market consistent value of these guarantees carried in the balance sheet is £111m (2008: £133m).

Endowment contracts

These contracts provide a lump sum on maturity determined by the addition of annual and final bonuses over the duration of the contract. In addition, the contracts provide a minimum sum assured death benefit.

Key risk factors

The insurance and market risk exposures for participating business are largely the same as those discussed for non-participating contracts. The main differences in the operation of these contracts are discussed below.

(a) Insurance risk - Persistency

At early durations, the nature of the persistency risks on with-profits business is largely the same as for non-participating business and is influenced mainly by the ability to recover acquisition costs from product margins. At later durations, there is less scope for withdrawal to result in a loss for the Group as these contracts typically provide explicit allowances for market conditions. Allowance for future withdrawals is made in the assessment of participating contract liabilities. The Group is generally exposed to the risk that future withdrawals are lower than assumed, resulting in higher future guarantee costs.

(b) Market risk

The financial risk exposure for participating contracts is different from that for non-participating business. Greater emphasis is placed on investing to maximise future investment returns rather than matching assets to liabilities. This results in holding significant equity and property investments. Lower investment returns increase the costs associated with maturity and investment guarantees provided on these contracts.

These risks are managed by maintaining capital sufficient to cover the consequences of mismatch under a number of adverse scenarios. In addition, different investment strategies are followed for assets backing policyholder asset shares and assets backing other participating liabilities and surplus. The former include significant equity and property holdings, whilst the latter are invested largely in fixed interest securities. The assets held are managed so as to provide a partial hedge to movements in fixed interest yields and equity markets.

The methodology used to calculate the liabilities for participating contracts makes allowance for the possibility of adverse changes in investment markets on a basis consistent with the market cost of hedging the guarantees provided. The methodology also makes allowance for the cost of future discretionary benefits, guarantees and options.

The value of future discretionary benefits depends on the return achieved on assets backing these contracts. The asset mix varies with investment conditions reflecting the Group’s investment policy, which aims to optimise returns to policyholders over time whilst limiting capital requirements for this business.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

The distribution of surplus to shareholders depends upon the bonuses declared for the period. Typically, bonus rates are set having regard to investment returns, although the Group has some discretion setting rates and would normally smooth bonuses over time. The volatility of investment returns could impact the fund's capital position and its ability to pay bonuses. If future investment conditions were less favourable than anticipated, the lower bonus levels resulting would also reduce future distributions to shareholders.

However, business which is written in the with-profits part of the Society LTF is managed to be self-supporting. The unallocated divisible surplus in the fund would normally be expected to absorb the impact of these investment risks. Only in extreme scenarios, where shareholders were required to provide capital support to the with-profits part of the Society LTF, would these risks affect equity.

As part of the 2007 Society LTF restructure, the 1996 Sub-fund (£321m) was merged into the Shareholder Retained Capital (SRC). As a result, Society's Board of Directors undertook to initially maintain £500m of assets within Society to support the with-profits business. The amount of the commitment will reduce to £400m in 2010 and then gradually reduce to zero over a period not exceeding eight years.

The Group's approach to setting bonus rates is designed to treat customers fairly. The approach is set out in the Society's PPFM for the with-profits part of the Society LTF. In addition, bonus declarations are also affected by FSA regulations relating to Treating Customers Fairly (TCF), which limit the discretion available when setting bonus rates. The Group's approach to setting bonuses and meeting the FSA's TCF regulations may increase the Group's exposure to market risk should the ability to cut bonuses, during periods when investment returns are poor, be reduced.

Unit linked contracts

The Group's primary exposure to financial risk from these contracts is the risk of volatility in asset management fees due to the impact of interest rate and market price movements on the fair value of the assets held in the linked funds, on which investment management fees are based. The Group is also exposed to the risk of an expense overrun should the market depress the level of charges which could be imposed, although for some contracts the Group has discretion over the level of management charges levied.

Sensitivity analysis

Table 6 shows the impact on pre-tax profit and equity, net of reinsurance, under each sensitivity scenario for the non-participating business written in the non profit part of the UK LTF.

Table 6 – UK long term business IFRS sensitivity analysis

	Impact on pre-tax profit net of reinsurance 2009 £m	Impact on equity net of reinsurance 2009 £m
Sensitivity test		
1% increase in interest rates	(92)	(66)
1% decrease in interest rates	71	51
Credit spread widens by 100bps with no change in expected defaults	(141)	(101)
1% increase in inflation	(3)	(2)
Default of largest reinsurer	(589)	(424)
5% decrease in annuitant mortality	(281)	(202)

- In calculating the alternative values, all other assumptions are left unchanged. In practice, items of the Group's experience may be correlated.
- The Group 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 Group asset and liability position and any second order tax effects.
- 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 100bps change in the gross redemption yield on fixed interest securities together with a 100bps 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 FSA regulations.
- In the sensitivity for credit spreads corporate bond yields have increased by 100bps, gilt and approved security yields unchanged, and there has been no adjustment to the default assumptions.
- The inflation stress adopted is a 1% pa increase in inflation resulting in a 1% pa reduction in real yield and no change to the nominal yield. In addition the expense inflation rate has increased by 1% pa.
- The reinsurer stress shown is equal to the technical provisions ceded to that insurer.
- The annuitant mortality stress is a 5% 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 76% of that standard table).

Details of IGD sensitivity analysis can be found in Table 2 of Note 46.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

International

Legal & General America (LGA)

The principal products written by LGA are individual term assurance, universal life insurance and smaller blocks of deferred and immediate annuities.

The individual term assurances provide death benefits over the medium to long term. The contracts have level premiums for an initial period with premiums increasing annually thereafter. During the initial period, there is generally an option to convert the contract to a universal life contract. After the initial period, the premium rates are not guaranteed, but cannot exceed the age related guaranteed premium.

Reinsurance is used to reduce the insurance risk on this portfolio and manage liquidity risks, through the reinsurance commission received under quota share arrangements. Reinsurance and securitisation are used to provide regulatory solvency relief (including relief from regulation Triple X). These practices led to the establishment of reinsurance assets on the Group's balance sheet.

The universal life insurance and deferred annuities provide a savings component. In addition, the universal life contract provides substantial death benefits over the medium to long term. The savings element has a guaranteed minimum growth rate. LGA has exposure to loss in the event that interest rates decrease and it is unable to earn enough on the underlying assets to cover the guaranteed rate. LGA is also exposed to loss should interest rates increase, as the underlying market value of assets will generally fall without a change in the surrender value. The reserves for universal life and deferred annuities totalled $723m and $221m respectively at 31 December 2009 (31 December 2008: $753m and $230m respectively). The guaranteed interest rates associated with those reserves ranged from 0.0% to 5.5%, with the majority of the policies having a 4% guaranteed rate (2008: 4%).

The deferred annuity contracts also contain a provision that, at maturity, a policyholder may move the account value into an immediate annuity, at rates which are either those currently in effect, or rates guaranteed in the contract. The other annuity contracts have similar risks to those in the UK.

Legal & General Netherlands (LGN)

LGN principally writes non-participating individual unit linked savings, individual term assurance and annuity business.

The unit linked savings business generally includes an element of exposure to mortality risk. The individual term assurances provide death benefits over the medium to long term. Reinsurance is used to reduce the share of insurance risk. The annuity contracts have similar risks to those in the UK; however, the majority of annuity business has a term of three years or less.

Legal & General France (LGF)

LGF writes a range of long term insurance and investment business through its subsidiaries. The principal products written are group protection, annuities, savings and open ended investment vehicles.

The group protection business consists of group term assurance, renewable on an annual basis, sickness and disability, and medical expenses assurance. The group sickness and disability and medical expenses policies integrate with social security benefits providing a level of top-up to those benefits. Reinsurance is used to manage exposure to large individual and group claims.

The annuity contracts have similar risks to those in the UK.

Savings products include contracts that provide minimum guaranteed rates of return. The guarantee is aligned with current and projected rates of return from government securities. Investment risks associated with open ended investment vehicles are borne by unit holders of these funds.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

48 RISK MANAGEMENT AND CONTROL (CONTINUED)

Sensitivity analysis

Table 7 below shows the effect of alternative assumptions on the long term embedded value, prepared in accordance with the guidance issued by the European Insurance CFO Forum in October 2005. These sensitivities correspond to those contained within the Supplementary Financial Statements on page 201 of the Annual Report & Accounts.

Table 7 – Effect on embedded value

As at 31 December 2009	**As published £m**	**1% lower risk discount rate £m**	**1% higher risk discount rate £m**	**1% lower interest rate £m**	**1% higher interest rate £m**	**1% higher equity/ property yields £m**
UK	**6,267**	**376**	**(328)**	**28**	**(51)**	**106**
International	**1,446**	**107**	**(97)**	**11**	**(25)**	**3**
	7,713	**483**	**(425)**	**39**	**(76)**	**109**

As at 31 December 2009	**As published £m**	**10% lower equity/ property values £m**	**10% lower maintenance expenses £m**	**10% lower lapse rates £m**	**5% lower mortality (UK annuities) £m**	**5% lower mortality (other business) £m**
UK	**6,267**	**(149)**	**77**	**75**	**(157)**	**59**
International	**1,446**	**(6)**	**13**	**54**	**n/a**	**89**
	7,713	**(155)**	**90**	**129**	**(157)**	**148**

As at 31 December 2008	As published £m	1% lower risk discount rate £m	1% higher risk discount rate £m	1% lower interest rate £m	1% higher interest rate £m	1% higher equity/ property yields £m
UK	6,146	384	(336)	(73)	5	110
International	1,463	126	(109)	17	(23)	3
	7,609	510	(445)	(56)	(18)	113

As at 31 December 2008	As published £m	10% lower equity/ property values £m	10% lower maintenance expenses £m	10% lower lapse rates £m	5% lower mortality (UK annuities) £m	5% lower mortality (other businesses) £m
UK	6,146	(248)	68	66	(111)	40
International	1,463	(6)	12	59	n/a	95
	7,609	(254)	80	125	(111)	135

Opposite sensitivities are broadly symmetrical.

The Group also uses embedded value (EV) financial information in addition to IFRS to manage and monitor performance, and to manage interdependences between different aspects of financial risks, for example for market risk. This provides information about the value which is being created on the Group's long term insurance contracts.

EV information is calculated for the Group's life and pensions business (covered business). All other businesses are accounted for on the IFRS basis adopted in the primary financial statements.

The EV methodology requires assets of an insurance company, as reported in the primary financial statements, to be attributed between those supporting the covered business and the remainder. The method accounts for assets in the covered business on an EV basis and the remainder of the Group's assets on the IFRS basis adopted in the primary financial statements. Sensitivities have been presented for covered business only. In this context the non-covered business is considered not to be material. Whilst EV sensitivities do not directly reflect the short term movements under IFRS, they more closely reflect the long term economic out turn.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Cash flow projections are determined using realistic assumptions for each component of cash flow and for each policy group. Future economic and investment return assumptions are based on conditions at the end of the financial year. Future investment returns are projected by one of two methods. The first method is based on an assumed investment return attributed to assets at their market value. The second, which is used in the US, where the investments of that subsidiary are substantially all fixed interest, projects the cash flows from the current portfolio of assets and assumes an investment return on reinvestment of surplus cash flows. The assumed discount and inflation rates are consistent with the investment return assumptions. The main assumptions are provided on page 202 in the Supplementary Financial Statements.

UK general insurance

The principal products are:

- Household. These contracts provide cover in respect of policyholders' homes, investment properties, contents, personal belongings and incidental liabilities which they may incur as a property owner, occupier and individual. Exposure is normally limited to the rebuilding cost of the home, the replacement cost of belongings and a policy limit in respect of liability claims. LGI uses reinsurance to manage the exposure to an accumulation of claims arising from any one incident, usually severe weather. The catastrophe cover runs from 1 July to 30 June and reinsures LGI for losses between £30m and £250m (2008/2009: £30m and £270m) for a single weather event.
- Accident, sickness and unemployment (ASU). These contracts provide cover in respect of continuing payment liabilities incurred by customers when they are unable to work as a result of accident, sickness or unemployment. They protect predominantly mortgage payments. Exposure is limited to the monthly payment level selected by the customer sufficient to cover the payment and associated costs, up to the duration limit specified in the policy, usually 12 months.
- Motor insurance (in run-off). These contracts provide cover in respect of customers' private cars and their liability to third parties in respect of damage to property and injury. Exposure is normally limited to the replacement value of the vehicle, and a policy limit in respect of third party property damage. Exposure to third party bodily injury is unlimited in accordance with statutory requirements. The motor book continues in run-off, the final policy having expired in August 2007, but this is expected to take several years.
- Healthcare (in run-off). These contracts are primarily private medical insurance, which compensate customers for the costs of eligible medical consultations, diagnostic tests, in-patient, day care and outpatient treatment up to the limits specified in the policy. They are mainly exposed to the underlying incidence of morbidity, medical claims inflation and advances in medical treatments. The healthcare business is in run-off with the final policies having expired in July 2008. By 2009, the run-off was substantially complete and the residual claims were minimal.
- Domestic mortgage indemnity (DMI). These contracts (primarily in run-off) protect a mortgage lender should an insured property be repossessed and subsequently sold at a loss. Since 1993, the contract has included a maximum period of cover of 10 years, and a cap on the maximum claim. For business accepted prior to 1993, cover is unlimited and lasts until the insured property is remortgaged or redeemed.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Key risk factors

Weather events

Significant weather events such as windstorms, and coastal and river floods can lead to significant claims.

Concentration

The insurance of properties which are concentrated in high risk areas, or an above average market share in a particular region, can give rise to a concentration of insurance risk. This risk is managed by ensuring that the risk acceptance policy, terms and premiums both reflect the expected claim cost associated with the location and avoid adverse selection. Additionally, exposure and competitor activity is monitored by location to ensure that there is a geographic spread of business. Catastrophe reinsurance cover reduces the Group's exposure to concentrations of risk. The catastrophe reinsurance is designed to protect against a modelled windstorm and coastal flood event with a return probability of 1 in 200 years.

Subsidence

The incidence of subsidence can have a significant impact on the level of claims on household policies. The Group's underwriting and reinsurance strategy mitigates the exposure to concentrations of risk arising from geographic location or adverse selection.

Economic downturn

Periods of rapid and prolonged national economic downturn can create significant variation in the frequency and severity of ASU claims experience.

This risk is managed through the monitoring of economic trends and the underwriting of policies to ensure that the customer completing a mortgage loan transaction achieves credit scoring approval.

Unlimited motor claims

A single motor policy can result in major multiple liability claims in extreme scenarios. To mitigate this risk, accident excess of loss reinsurance is in place for claims in excess of £1m (2008: £1m).

Sensitivity analysis

Table 8 shows material sensitivities for the General insurance business on pre-tax profit and equity, net of reinsurance.

Table 8 – General insurance sensitivity analysis

	Impact on pre-tax profit net of reinsurance 2009 £m	**Impact on equity net of reinsurance 2009 £m**	Impact on pre-tax profit net of reinsurance 2008 £m	Impact on equity net of reinsurance 2008 £m
Sensitivity test				
Single storm event with 1 in 200 year probability	**(50)**	**(36)**	(50)	(36)
Subsidence event – worst claim ratio in last 30 years	**(41)**	**(29)**	(46)	(33)
Economic downturn	**(39)**	**(28)**	(39)	(28)
5% decrease in overall claims ratio	**8**	**6**	10	7
5% surplus over claims liabilities	**5**	**4**	6	4

For any single event with claims in excess of £30m but less than £250m, the ultimate cost to the Group would be £30m. The impact of a 1 in 500 year modelled windstorm and coastal flood event would exceed the catastrophe cover by approximately £120m.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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EUROPEAN EMBEDDED VALUE BASIS

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2009	Notes	2009 £m	2008 Restated[1] £m
From continuing operations			
Risk	2	**913**	439
Savings	2	**82**	50
Investment management	5	**139**	130
International	6	**170**	100
Group capital and financing	7	**47**	156
Investment projects		**(32)**	–
Operating profit		**1,319**	875
Variation from longer term investment return	8	**(413)**	(1,584)
Effect of economic assumption changes	9	**(335)**	(609)
Property losses attributable to minority interests		**(19)**	(63)
Profit/(loss) from continuing operations before tax attributable to equity holders of the Company		**552**	(1,381)
Tax (expense)/credit on profit/(loss) from ordinary activities	11	**(114)**	327
Tax impact of corporate restructure		**59**	81
Profit/(loss) for the year		**497**	(973)
Loss attributable to minority interests		**19**	63
Profit/(loss) attributable to equity holders of the Company		**516**	(910)

		p	p
Earnings per share	12		
Based on operating profit from continuing operations after tax attributable to equity holders of the Company		**16.28**	10.72
Based on profit/(loss) attributable to equity holders of the Company		**8.86**	(15.25)
Diluted earnings per share	12		
Based on operating profit from continuing operations after tax attributable to equity holders of the Company		**16.19**	10.68
Based on profit/(loss) attributable to equity holders of the Company		**8.81**	(15.25)

1. The EEV comparatives have been restated to reflect the impact of the change in definition of IFRS operating profit on non covered business. The change has increased 2008 EEV operating profit by £5m and reduced variation from longer term investment return by £5m. There is no impact on profit after tax or shareholders' equity.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2009	2009 £m	2008 £m
Profit/(loss) for the year	**497**	(973)
Other comprehensive income after tax		
Exchange differences on translation of overseas operations	**(88)**	196
Actuarial (losses)/gains on defined benefit pension schemes	**(90)**	12
Actuarial losses/(gains) on defined benefit pension schemes transferred to unallocated divisible surplus	**62**	(8)
Total comprehensive income/(expense) for the year	**381**	(773)
Total comprehensive income/(expense) attributable to:		
Minority interests	**(19)**	(63)
Equity holders of the Company	**400**	(710)

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

CONSOLIDATED BALANCE SHEET

As at 31 December 2009	Notes	2009 £m	2008 £m
Assets			
Investments		**290,550**	249,185
Long term in-force business asset		**2,645**	3,160
Other assets		**6,348**	7,315
Total assets		**299,543**	259,660
Equity			
Shareholders' equity	14/15	**6,695**	6,521
Minority interests		**2**	144
Total equity		**6,697**	6,665
Liabilities			
Subordinated borrowings		**1,870**	1,657
Unallocated divisible surplus		**1,284**	913
Participating contract liabilities		**16,176**	16,205
Non-participating contract liabilities		**263,085**	222,539
Senior borrowings		**1,407**	2,314
Other liabilities and provisions		**9,024**	9,367
Total liabilities		**292,846**	252,995
Total equity and liabilities		**299,543**	259,660

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS

1 BASIS OF PREPARATION

The supplementary financial statements have been prepared in accordance with the European Embedded Value (EEV) Principles issued in May 2004 by the European Insurance CFO Forum.

These supplementary financial statements have been audited by PricewaterhouseCoopers LLP and prepared in conjunction with our consulting actuaries – Towers Watson and, in the US, Milliman USA.

Covered business

The Group uses EEV methodology to value individual and group life assurance, pensions and annuity business written in the UK, Continental Europe and the US. The UK covered business also includes non-insured self invested personal pension (SIPP) business.

The managed pension funds business has been excluded from covered business and is reported on an IFRS basis, as management believe IFRS to be the most appropriate reporting basis for the investment management business.

All other businesses are accounted for on the IFRS basis adopted in the primary financial statements.

There is no distinction made between insurance and investment contracts in our covered business as there is under IFRS.

Description of methodology

The objective of EEV is to provide shareholders with realistic information on the financial position and current performance of the Group.

The methodology requires assets of an insurance company, as reported in the primary financial statements, to be attributed between those supporting the covered business and the remainder. The method accounts for assets in the covered business on an EEV basis and the remainder of the Group's assets on the IFRS basis adopted in the primary financial statements.

The EEV methodology recognises profit from the covered business as the total of:

i. cash transfers during the relevant period from the covered business to the remainder of the Group's assets; and
ii. the movement in the present value of future distributable profits to shareholders arising from the covered business over the relevant reporting period.

Embedded value

Shareholders' equity on the EEV basis comprises the embedded value of the covered business plus the shareholders' equity of other businesses, less the value included for purchased interests in long term business.

The embedded value is the sum of the shareholder net worth (SNW) and the value of the in-force business (VIF). SNW is defined as those amounts, within covered business (both within the long term fund and held outside the long term fund but used to support long term business), which are regarded either as required capital or which represent free surplus.

The VIF is the present value of future shareholder profits arising from the covered business, projected using best estimate assumptions, less an appropriate deduction for the cost of holding the required level of capital and the time value of financial options and guarantees (FOGs).

Service companies

All services relating to the UK covered business are charged on a cost recovery basis, with the exception of investment management services provided to Legal & General Pensions Limited (LGPL), which have been charged at market referenced rates since 1 January 2007, and to Legal & General Assurance Society Limited (Society), which have been charged at market referenced rates since 1 July 2007. Profits arising on the provision of these services are valued on a look through basis.

As the EEV methodology incorporates the future capitalised cost of these internal investment management services, the equivalent IFRS profits have been removed from the Investment management segment and are instead included in the results of the Risk and Savings segments on an EEV basis.

The capitalised value of future profits emerging from internal investment management services are therefore included in the embedded value and new business contribution calculations for the Risk and Savings segments. However, the historical profits which have emerged continue to be reported in the shareholders' equity of the Investment management segment on an IFRS basis. Since the look through into service companies includes only future profits and losses, current intra-group profits or losses must be eliminated from the closing embedded value and in order to reconcile the profits arising in the financial period within each segment with the net assets on the opening and closing balance sheet, a transfer of IFRS profits for the period from the UK SNW is deemed to occur.

New business

New business premiums reflect income arising from the sale of new contracts during the reporting period and any changes to existing contracts, which were not anticipated at the outset of the contract.

In-force business comprises previously written single premium, regular premium and recurrent single premium contracts.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

Department of Work and Pensions rebates have not been treated as recurring and are included in single premium new business when received.

New business contribution arising from the new business premiums written during the reporting period has been calculated on the same economic and operating assumptions used in the embedded value at the end of the financial period. This has then been rolled forward to the end of the financial period using the risk discount rate applicable at the end of the reporting period.

The present value of new business premiums (PVNBP) has been calculated and expressed at the point of sale. The PVNBP is equivalent to the total single premiums plus the discounted value of regular premiums expected to be received over the term of the contracts using the same economic and operating assumptions used for the embedded value at the end of the financial period. The new business margin is defined as new business contribution at the end of the reporting period divided by the PVNBP. The premium volumes and projection assumptions used to calculate the PVNBP are the same as those used to calculate new business contribution.

Projection assumptions

Cash flow projections are determined using best estimate assumptions for each component of cash flow and for each policy group. Future economic and investment return assumptions are based on conditions at the end of the financial period. Future investment returns are projected by one of two methods. The first method is based on an assumed investment return attributed to assets at their market value. The second, which is used in the US, where the investments of that subsidiary are substantially all fixed interest, projects the cash flows from the current portfolio of assets and assumes an investment return on reinvestment of surplus cash flows. The assumed discount and inflation rates are consistent with the investment return assumptions.

Detailed projection assumptions including mortality, morbidity, persistency, and expenses reflect recent operating experience and are normally reviewed annually. Allowance is made for future improvements in annuitant mortality based on experience and externally published data. Favourable changes in operating experience are not anticipated until the improvement in experience has been observed.

All costs relating to the covered business, whether incurred in the covered business or elsewhere in the Group, are allocated to that business. The expense assumptions used for the cash flow projections therefore include the full cost of servicing this business.

Tax

The projections take into account all tax which is expected to be paid, based on best estimate assumptions, applying current legislation and practice together with known or expected future changes.

Allowance for risk

Aggregate risks within the covered business are allowed for through the following principal mechanisms:

i. setting required capital levels with reference to both the Group's internal risk based capital models, and an assessment of the strength of regulatory reserves in the covered business;
ii. allowing explicitly for the time value of financial options and guarantees within the Group's products; and
iii. setting risk discount rates by deriving a Group level risk margin to be applied consistently to local risk free rates.

Required capital and free surplus

Regulatory capital for the Risk and Savings businesses is provided by assets backing the with-profits business or by the SNW. The SNW comprises all shareholders' capital within Society, including those funds retained within the long term fund and the excess assets in LGPL (collectively Society shareholder capital).

Society shareholder capital is either required to cover EU solvency margin or is free surplus as its distribution to shareholders is not restricted.

For UK with-profits business, the required capital is covered by the surplus within the with-profits part of the fund and no effect is attributed to shareholders except for the burn-through cost, which is described later. This treatment is consistent with the Principles and Practices of Financial Management for this part of the fund.

For UK non profit business, the required capital will be maintained at no less than the level of the EU minimum solvency requirement. This level, together with the margins for adverse deviation in the regulatory reserves, is, in aggregate, in excess of internal capital targets assessed in conjunction with the Individual Capital Assessment (ICA) and the with-profits support account.

The initial strains relating to new non profit business, together with the related EU solvency margin, are supported by releases from existing non profit business and the Society shareholder capital. As a consequence, the writing of new business defers the release of capital to free surplus. The cost of holding required capital is defined as the difference between the value of the required capital and the present value of future releases of that capital. For new business, the cost of capital is taken as the difference in the value of that capital assuming it was available for release immediately and the present value of the future releases of that capital. As the investment return, net of tax, on that capital is less than the risk discount rate, there is a resulting cost of capital which is reflected in the value of new business.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

For Legal & General America, the Company Action Level (CAL) of capital has been treated as required capital for modelling purposes. The CAL is the regulatory capital level at which the Company would have to take prescribed action, such as submission of plans to the State insurance regulator, but would be able to continue operating on the existing basis. The CAL is currently twice the level of capital at which the regulator is permitted to take control of the business.

For Legal & General Netherlands, required capital has been set at 100% of EU minimum solvency margin for all products without FOGs. For those products with FOGs, capital of between 100% and 175% of the EU minimum solvency margin has been used. The level of capital has been determined using risk based capital techniques.

For Legal & General France, 100% of EU minimum solvency margin has been used for EV modelling purposes for all products both with and without FOGs. The level of capital has been determined using risk based capital techniques.

The contribution from new business for our International businesses reflects an appropriate allowance for the cost of holding the required capital.

Financial options and guarantees

In the UK, all financial options and guarantees (FOGs) are within the UK covered business.

Under the EEV Principles an allowance for time value of FOGs is required where a financial option exists which is exercisable at the discretion of the policyholder. These types of options principally arise within the with-profits part of the fund and their time value is recognised within the with-profits burn-through cost described below. Additional financial options for non profit business exist only for a small amount of deferred annuity business where guaranteed early retirement and cash commutation terms apply when the policyholders choose their actual retirement date.

Further financial guarantees exist for non profit business, in relation to index-linked annuities where capped or collared restrictions apply. Due to the nature of these restrictions and the manner in which they vary depending on the prevailing inflation conditions, they are also treated as FOGs and a time value cost recognised accordingly.

The time value of FOGs has been calculated stochastically using a large number of real world economic scenarios derived from assumptions consistent with the deterministic EEV assumptions and allowing for appropriate management actions where applicable. The management action primarily relates to the setting of bonus rates. Future regular and terminal bonuses on participating business within the projections are set in a manner consistent with expected future returns available on assets deemed to back the policies within the stochastic scenarios.

In recognising the residual value of any projected surplus assets within the with-profits part of the fund in the deterministic projection, it is assumed that terminal bonuses are increased to exhaust all of the assets in the part of the fund over the future lifetime of the in-force with-profits policies. However, under stochastic modelling, there may be some extreme economic scenarios when the total projected assets within the with-profits part of the fund are insufficient to pay all projected policyholder claims and associated costs. The average additional shareholder cost arising from this shortfall has been included in the time value cost of options and guarantees and is referred to as the with-profits burn-through cost.

Economic scenarios have been used to assess the time value of the financial guarantees for non profit business by using the inflation rate generated in each scenario. The inflation rate used to project index-linked annuities will be constrained in certain real world scenarios, for example, where negative inflation occurs but the annuity payments do not reduce below pre-existing levels. The time value cost of FOGs allows for the projected average cost of these constrained payments for the index-linked annuities. It also allows for the small additional cost of the guaranteed early retirement and cash commutation terms for the minority of deferred annuity business where such guarantees have been written.

In the US, FOGs relate to guaranteed minimum crediting rates and surrender values on a range of contracts. The guaranteed surrender value of the contract is based on the accumulated value of the contract including accrued interest. The crediting rates are discretionary but related to the accounting income for the amortising bond portfolio. The majority of the guaranteed minimum crediting rates are between 4% and 5%. The assets backing these contracts are invested in US Dollar denominated fixed interest securities.

In the Netherlands, there are two types of guarantees which have been separately provided for: interest rate guarantees and maturity guarantees. Certain contracts provide an interest rate guarantee where there is a minimum crediting rate based on the higher of 1-year Euribor and the policy guarantee rate. This guarantee applies on a monthly basis. Certain unit linked contracts provide a guaranteed minimum value at maturity where the maturity amount is the higher of the fund value and a guarantee amount. The fund values for both these contracts are invested in Euro denominated fixed interest securities.

In France, FOGs which have been separately provided for relate to guaranteed minimum crediting rates and surrender values on a range of contracts. The guaranteed surrender value of the contract is the accumulated value of the contract including accrued bonuses. The bonuses are based on the accounting income for the amortising bond portfolios plus income and releases from realised gains on any equity type investments. Policy liabilities equal guaranteed surrender values. Local statutory accounting rules require the establishment of a specific

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

liability when the accounting income for a company is less than 125% of the guaranteed minimum credited returns, although this has never been required. In general, the guaranteed annual bonus rates are between 0% and 4.5%.

Risk discount rate

The risk discount rate (RDR) is a combination of the risk free rate and a risk margin, which reflects the residual risks inherent in the Group's covered businesses, after taking account of prudential margins in the statutory provisions, the required capital and the specific allowance for FOGs.

The risk margin has been determined based on an assessment of the Group's weighted average cost of capital (WACC). This assessment incorporates a beta for the Group, which measures the correlation of movements in the Group's share price to movements in a relevant index. Beta values therefore allow for the market's assessment of the risks inherent in the business relative to other companies in the chosen index.

The WACC is derived from the Group's cost of equity and debt, and the proportion of equity to debt in the Group's capital structure measured using market values. Each of these three parameters are forward looking, although informed by historic information. The cost of equity is calculated as the risk free rate plus the equity risk premium for the chosen index multiplied by the Company's beta. Forward-looking or adjusted betas make allowance for the observed tendency for betas to revert to 1 and therefore a weighted average of the historic beta and 1 tends to be a better estimate of the Company's beta for the future period. We have computed the WACC using an arithmetical average of forward-looking betas against the FTSE 100 index.

The cost of debt used in the WACC calculations takes account of the actual locked-in rates for our senior and subordinated long term debt. All debt interest attracts tax relief at a rate of 28%.

Whilst the WACC approach is a relatively simple and transparent calculation to apply, subjectivity remains within a number of the assumptions. Management believes that the chosen margin, together with the levels of required capital, the inherent strength of the Group's regulatory reserves and the explicit deduction for the cost of options and guarantees, is appropriate to reflect the risks within the covered business.

For the 2009 results the risk margin was decreased to 3.5% (31.12.2008: 4.5%). The decrease reflects the reduction in the market perceived company specific risks that were apparent in the dislocated market conditions at the 2008 year end.

Analysis of profit

Operating profit is identified at a level which reflects an assumed longer term level of investment return.

The contribution to operating profit in a period is attributed to four sources:

i. new business;
ii. the management of in-force business;
iii. development costs; and
iv. return on shareholder net worth.

Further profit contributions arise from actual investment returns differing from the assumed long term investment returns (investment return variances), and from the effect of economic assumption changes.

The contribution from new business represents the value recognised at the end of each period from new business written in that period, after allowing for the actual cost of acquiring the business and of establishing the required technical provisions and reserves and after making allowance for the cost of capital. New business contributions are calculated using closing assumptions.

The contribution from in-force business is calculated using opening assumptions and comprises:

i. expected return - the discount earned from the value of business in-force at the start of the year;
ii. experience variances - the variance in the actual experience over the reporting period from that assumed in the value of business in-force as at the start of the year; and
iii. operating assumption changes - the effects of changes in future assumptions, other than changes in economic assumptions from those used in valuing the business at the start of the year. These changes are made prospectively from the end of the year.

Development costs relate to investment in strategic systems and development capability.

The contribution from shareholder net worth comprises the increase in embedded value based on assumptions at the start of the year in respect of the expected investment return on the Society shareholder capital.

Further profit contributions arise from investment return variances and the effect of economic assumption changes.

Investment return variances represent the effect of actual investment performance and changes to investment policy on shareholder net worth and the value of in-force business from that assumed at the beginning of the period.

Economic assumption changes comprise the effect of changes in economic variables on shareholder net worth and the value of in-force business from that assumed at the beginning of the period, which are beyond the control of management, including associated changes to valuation bases to the extent that they are reflected in revised assumptions.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

2 PROFIT/(LOSS) FOR THE YEAR

For the year ended 31 December 2009	Notes	Risk and Savings £m	Investment management £m	International £m	Group capital and financing £m	Total £m
Business reported on an EEV basis:						
Contribution from new business after cost of capital	3	305		23		328
Contribution from in-force business:						
– expected return[1]		496		118		614
– experience variances	4	46		17		63
– operating assumption changes	4	156		1		157
Development costs		(30)		–		(30)
Contribution from shareholder net worth[2]				16	125	141
Operating profit on covered business		973	–	175	125	1,273
Business reported on an IFRS basis:						
General insurance		17				17
Core retail investments		9				9
Investment management[3]	5		139			139
Group capital and financing	7				(78)	(78)
Investment projects[4]					(32)	(32)
Other[5]		(4)		(5)		(9)
Total operating profit		995	139	170	15	1,319
Variation from longer term investment return	8	(501)	(4)	62	30	(413)
Effect of economic assumption changes	9	(249)	–	(97)	11	(335)
Property losses attributable to minority interests		–	–	–	(19)	(19)
Profit from continuing operations before tax		245	135	135	37	552
Tax (expenses)/credit on profit from ordinary activities		(68)	(36)	(43)	33	(114)
Tax impact of corporate restructure[6]		–	–	–	59	59
Profit for the year		177	99	92	129	497
Operating profit attributable to:						
Risk		913				
Savings		82				

1. The expected return on in-force is based on the unwind of the risk discount rate on the opening, adjusted base value of in-force (VIF). The opening base VIF of the Risk and Savings business was £4,268m in 2009. This is adjusted for the effects of opening model changes of £31m to give an adjusted opening base VIF of £4,299m. This is then multiplied by the opening risk discount rate of 8.3% and the result grossed up at the notional attributed tax rate of 28% to give a return of £496m.
2. The 2009 Group capital and financing contribution from shareholder net worth (SNW) of £125m comprises the average return of 7% on the average balance of invested assets of £2.1bn (£138m); offset by an adjustment for opening tax and other modelling changes of £(2)m and pre-tax corporate expenses charged to shareholders' funds of £(11)m.
3. Investment management operating profit excludes £28m (2008: £35m) of profits arising from the provision of investment management services at market referenced rates to the covered business. These are reported on a look through basis and as a consequence are included in the Risk, Savings and Group capital and financing covered business on an EEV basis.
4. Investment projects comprises Solvency II and other strategic investments.
5. On an EEV basis, Suffolk Life, operations in Ireland and business unit costs allocated to the Risk and Savings business are included in the covered business operating profit. These are included within Other Risk and Other Savings within IFRS operating profit.
6. In 2009, in addition to current year investment return, £469m was released from the Shareholder Retained Capital and declared as surplus for tax purposes. As a result of the 2007 corporate restructure, this release along with current year movements did not give rise to any incremental tax and therefore resulted in a £59m benefit to embedded value.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

2 PROFIT/(LOSS) FOR THE YEAR (CONTINUED)

For the year ended 31 December 2008	Notes	Risk and Savings £m	Investment management £m	International £m	Group capital and financing Restated £m	Total Restated £m
Business reported on an EEV basis:						
Contribution from new business after cost of capital	3	265		32		297
Contribution from in-force business:						
– expected return		370		100		470
– experience variances	4	12		(34)		(22)
– operating assumption changes	4	(100)		(15)		(115)
Development costs		(51)		–		(51)
Contribution from shareholder net worth				17	256	273
Operating profit on covered business		496	–	100	256	852
Business reported on an IFRS basis:						
General insurance		(2)				(2)
Core retail investments		–				–
Investment management[1]	5		130			130
Group capital and financing	7				(100)	(100)
Other[2]		(5)		–		(5)
Total operating profit		489	130	100	156	875
Variation from longer term investment return	8	(175)	7	(110)	(1,306)	(1,584)
Effect of economic assumption changes	9	(505)	–	(110)	6	(609)
Property losses attributable to minority interests		–	–	–	(63)	(63)
(Loss)/profit from continuing operations before tax		(191)	137	(120)	(1,207)	(1,381)
Tax credit/(expense) on (loss)/profit from ordinary activities		54	(42)	37	278	327
Tax impact of corporate restructure[3]		53	–	–	28	81
(Loss)/profit for the year		(84)	95	(83)	(901)	(973)
Operating profit attributable to:						
Risk		439				
Savings		50				

1. 2008 Investment management operating profit excludes £35m of profits arising from the provision of investment management services at market referenced rates to the covered business. These are reported on a look through basis and as a consequence are included in the Risk, Savings and Group capital and financing covered business on an EEV basis.
2. On an EEV basis, Suffolk Life, operations in Ireland and business unit costs allocated to the Risk and Savings business are included in the covered business operating profit. These are included within Other Risk and Other Savings within IFRS operating profit.
3. In 2008 £0.9bn was transferred from Shareholder Retained Capital to shareholder capital held outside the long term fund. This transfer did not give rise to any incremental tax and therefore resulted in an £81m benefit to embedded value.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

3 NEW BUSINESS[1]

For the year ended 31 December 2009	Annual premiums £m	Present value of annual premiums £m	Capitalisation factor	Single premiums £m	PVNBP £m	Contribution from new business £m	New business margin %
Risk	180	866	4.8	1,862	2,728	285	10.4
Savings	247	831	3.4	2,845	3,676	20	0.5
International	71	497	7.0	379	876	23	2.6
	498	2,194	4.4	5,086	7,280	328	4.5

For the year ended 31 December 2008	Annual premiums £m	Present value of annual premiums £m	Capitalisation factor	Single premiums £m	PVNBP £m	Contribution from new business £m	New business margin %
Risk	207	1,005	4.9	2,806	3,811	271	7.1
Savings	289	1,110	3.8	3,612	4,722	(6)	(0.1)
International	81	575	7.1	321	896	32	3.6
	577	2,690	4.7	6,739	9,429	297	3.1

1. Excludes core retail investments.

4 ANALYSIS OF EXPERIENCE VARIANCES AND OPERATING ASSUMPTION CHANGES

	Risk and Savings			International		
For the year ended 31 December 2009	Experience variances £m	Operating assumption changes £m	Total £m	Experience variances £m	Operating assumption changes £m	Total £m
Persistency	(5)	(42)	(47)	(2)	(13)	(15)
Mortality/morbidity	(6)	114	108	13	26	39
Expenses	(19)	60	41	(7)	(12)	(19)
Other	76	24	100	13	–	13
	46	156	202	17	1	18

Risk and Savings persistency operating assumption changes relate to the strengthening of lapse assumptions for individual protection and unit linked bond policies; partially offset by improved persistency for with-profits products.

Risk and Savings mortality assumption changes relates to favourable annuitant mortality experience in 2009 which has been reflected in the latest three year average experience, and favourable individual protection mortality.

Risk and Savings expense assumption changes primarily reflects the £76m impact of the cost reductions delivered in 2009; partially offset by the impact of assumed higher future investment expenses of £(29)m. Other smaller items have a net positive impact of £13m. Expense experience variances include the impact of redundancy costs as a result of the cost reduction programme of £(17)m and exceptional project expenses and other items of £(8)m; partially offset by the impact of lower maintenance expenses than assumed of £6m.

Risk and Savings other experience variances includes £44m reflecting a reassessment of future reserve releases as data is loaded onto the BPA system and £43m relating to one-off modelling improvements.

International mortality operating assumption changes primarily reflects improved claims ratios on group protection business in France, following positive experience in 2009.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

4 ANALYSIS OF EXPERIENCE VARIANCES AND OPERATING ASSUMPTION CHANGES (CONTINUED)

	Risk and Savings			International		
For the year ended 31 December 2008	Experience variances £m	Operating assumption changes £m	Total £m	Experience variances £m	Operating assumption changes £m	Total £m
Persistency	(12)	(114)	(126)	(5)	(2)	(7)
Mortality/morbidity	27	(49)	(22)	(12)	8	(4)
Expenses	(9)	35	26	1	(9)	(8)
Other	6	28	34	(18)	(12)	(30)
	12	(100)	(88)	(34)	(15)	(49)

2008 Risk and Savings persistency operating assumption changes of £(114)m relate primarily to the strengthening of lapse assumptions for unit linked bond policies.

2008 Risk and Savings mortality assumption changes relate primarily to annuitant mortality where the assumption has been updated to reflect the latest three year average experience where lighter 2008 experience replaced heavier 2005 experience in the calculation.

5 INVESTMENT MANAGEMENT OPERATING PROFIT

	2009 £m	2008 £m
Managed pension funds[1]	**128**	117
Private equity	**(1)**	(1)
Property	**4**	4
Other income[2]	**13**	17
Legal & General Investment Management	**144**	137
Institutional unit trusts[3]	**(5)**	(7)
Total Investment management operating profit	**139**	130

1. The managed pension funds business within Investment management has been reported on an IFRS basis as management believe IFRS to be the most appropriate reporting basis for the Investment management business.
2. Other income excludes £28m (2008: £35m) of profits arising from the provision of investment management services at market referenced rates to the covered business. These are reported on a look through basis within the Risk, Savings and Group capital and financing covered business on an EEV basis.
3. Investment management operating profit excludes core retail investments, of £9m (2008: £nil), which has been disclosed as part of Savings.

6 INTERNATIONAL OPERATING PROFIT

	2009 £m	2008 £m
USA	**109**	70
Netherlands	**29**	8
France	**37**	22
Other[1]	**(5)**	–
Total International operating profit	**170**	100

1. Other includes our joint venture operations in Egypt, the Gulf and India.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

7 GROUP CAPITAL AND FINANCING OPERATING PROFIT[1]

	2009 £m	2008 Restated £m
Business reported on an EEV basis	**125**	256
Business reported on an IFRS basis:		
Investment return	**53**	47
Interest expense[2]	**(127)**	(138)
Unallocated corporate expenses	**(4)**	(9)
	(78)	(100)
Total Group capital and financing operating profit	**47**	156

1. Group capital and financing represents operating profit on the shareholder assets held within the covered business, reported on an embedded value basis, and operating profit on the shareholder assets held outside the covered business reported on an IFRS basis.
2. Interest expense excludes non recourse financing.

8 VARIATION FROM LONGER TERM INVESTMENT RETURN

	2009 £m	2008 Restated £m
Business reported on an EEV basis:		
Risk and Savings[1]	**(513)**	(146)
International	**62**	(110)
Group capital and financing	**(8)**	(1,176)
	(459)	(1,432)
Business reported on an IFRS basis:		
Risk and Savings	**12**	(29)
Investment management	**(4)**	7
Group capital and financing	**38**	(130)
	(413)	(1,584)

1. The 2009 Risk and Savings covered business variation from longer term investment return improved significantly during the second half of 2009 as a result of the investment actions taken within the non profit annuity credit portfolios and the general improvements in all investment markets. The reported adverse variance of £(513)m is primarily due to the £(335)m EEV impact of swap transactions undertaken in the first half of 2009 to improve the IFRS matching of annuity business which reduced the assumed future yield on the annuity assets for EEV purposes, £(77)m is due to an increased cost of capital arising from de-risking activity to reduce the equity ratio for assets backing solvency capital and £(50)m is the EEV impact of holding additional cash balances, largely to back the short term default provision. These effects were all reported in the half-year 2009 results.

9 EFFECT OF ECONOMIC ASSUMPTION CHANGES

	2009 £m	2008 £m
Business reported on an EEV basis:		
Risk and Savings[1]	**(249)**	(505)
International[2]	**(97)**	(110)
Group capital and financing	**11**	6
	(335)	(609)

1. 2009 Risk and Savings economic assumption changes include £125m relating to the decrease in the UK risk discount rate in 2009 from 8.3% to 8.0%, and £(250)m as a result of higher assumed future inflation and higher cost of capital on increased annuity reserves. In addition, increases in the realistic and statutory long term default provisions for the assets backing annuity business had an EEV impact of £(124m).
2. 2009 International economic assumption changes primarily reflect the increase in the US risk discount rate in 2009 from 6.8% to 7.4%.

10 TIME VALUE OF OPTIONS AND GUARANTEES

	2009 £m	2008 £m
Risk and Savings[1]	**13**	46
International	**19**	13
	32	59

1. Includes £9m (2008: £21m) relating to UK with-profits business, reflecting the impact of rising investment markets, and £4m (2008: £25m) relating to UK non profit business, due to a higher inflation environment than 2008 and its impact on the allowance for negative inflation within the annuity business.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

11 TAX

	Profit/(loss) before tax 2009 £m	Tax (expense)/ credit 2009 £m	Profit/(loss) before tax 2008 Restated £m	Tax (expense)/ credit 2008 Restated £m
From continuing operations				
Risk	**913**	**(254)**	439	(125)
Savings	**82**	**(24)**	50	(11)
Investment management	**139**	**(37)**	130	(40)
International	**170**	**(57)**	100	(35)
Group capital and financing	**47**	**(8)**	156	(24)
Investment projects	**(32)**	**9**	–	–
Operating profit	**1,319**	**(371)**	875	(235)
Variation from longer term investment return	**(413)**	**158**	(1,584)	386
Effect of economic assumption changes	**(335)**	**99**	(609)	176
Property losses attributable to minority interests	**(19)**	**–**	(63)	–
Profit/(loss) from continuing operations before tax/Tax	**552**	**(114)**	(1,381)	327

12 EARNINGS PER SHARE

(a) Earnings per share

	Profit/(loss) before tax 2009 £m	Tax (expense)/ credit 2009 £m	Profit/(loss) after tax 2009 £m	Per share 2009 p	Profit/(loss) before tax 2008 Restated £m	Tax (expense)/ credit 2008 Restated £m	Profit/(loss) after tax 2008 Restated £m	Per share 2008 Restated p
Operating profit from continuing operations	**1,319**	**(371)**	**948**	**16.28**	875	(235)	640	10.72
Variation from longer term investment return	**(413)**	**158**	**(255)**	**(4.38)**	(1,584)	386	(1,198)	(20.07)
Effect of economic assumption changes	**(335)**	**99**	**(236)**	**(4.05)**	(609)	176	(433)	(7.26)
Tax impact of corporate restructure	**–**	**59**	**59**	**1.01**	–	81	81	1.36
Earnings per share based on profit/ (loss) attributable to equity holders	**571**	**(55)**	**516**	**8.86**	(1,318)	408	(910)	(15.25)

(b) Diluted earnings per share

(i) Based on operating profit from continuing operations after tax

	Profit after tax 2009 £m	Number of shares[1] 2009 m	Per share 2009 p	Profit after tax 2008 Restated £m	Number of shares[1] 2008 m	Per share 2008 Restated p
Operating profit from continuing operations after tax	**948**	**5,824**	**16.28**	640	5,968	10.72
Net shares under options allocable for no further consideration	**–**	**33**	**(0.09)**	–	22	(0.04)
Diluted earnings per share	**948**	**5,857**	**16.19**	640	5,990	10.68

(ii) Based on profit/(loss) attributable to equity holders of the Company

	Profit after tax 2009 £m	Number of shares[1] 2009 m	Per share 2009 p	Loss after tax 2008 £m	Number of shares[1] 2008 m	Per share 2008 p
Profit/(loss) attributable to equity holders of the Company	**516**	**5,824**	**8.86**	(910)	5,968	(15.25)
Net shares under options allocable for no further consideration[2]	**–**	**33**	**(0.05)**	–	22	–
Diluted earnings per share	**516**	**5,857**	**8.81**	(910)	5,990	(15.25)

1. Weighted average number of shares.
2. At 31 December 2008, net shares under options allocable for no further consideration were anti-dilutive and were therefore excluded from the diluted earnings per share calculation.

The number of shares in issue at 31 December 2009 was 5,862,216,780 (31 December 2008: 5,861,627,994).

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

13 GROUP EMBEDDED VALUE RECONCILIATION

	Covered business						
For the year ended 31 December 2009	**UK free surplus £m**	**UK required capital £m**	**UK value of in-force £m**	**Total UK £m**	**International £m**	**Non-covered business £m**	**Total £m**
At 1 January							
Value of in-force business (VIF)	–	–	4,268	4,268	1,059	–	5,327
Shareholder net worth (SNW)	509	1,369	–	1,878	404	(1,088)	1,194
	509	1,369	4,268	6,146	1,463	(1,088)	6,521
Exchange rate movements	–	–	–	–	(153)	65	(88)
	509	1,369	4,268	6,146	1,310	(1,023)	6,433
Operating profit/(loss) for the year:							
– New business contribution[1]	(189)	155	253	219			
– Expected return on VIF	–	–	358	358			
– Expected transfer from Non profit VIF to SNW[2]	648	(147)	(501)	–			
– With-profits transfer	46	–	(46)	–			
– Experience variances	30	29	(31)	28			
– Operating assumption changes	285	(23)	(152)	110			
– Development costs	(21)	–	–	(21)			
– Expected return on SNW	34	61	–	95			
Operating profit/(loss)	833	75	(119)	789	117	42	948
Non-operating (loss)/profit for the year:							
– Investment variances	(66)	2	(276)	(340)			
– Economic assumption changes	(66)	75	(180)	(171)			
– Tax impact of corporate restructure	59	–	–	59			
Non-operating (loss)/profit	(73)	77	(456)	(452)	(21)	22	(451)
Profit/(loss) for the year	760	152	(575)	337	96	64	497
Capital movements	–	–	–	–	50	(50)	–
Intra-group distributions	(154)	–	–	(154)	(10)	164	–
Dividends to equity holders of the Company	–	–	–	–	–	(185)	(185)
Net movements in employee share schemes	–	–	–	–	–	19	19
Loss attributable to minority interests	–	–	–	–	–	19	19
Transfer to non-covered business[3]	(20)	–	–	(20)	–	20	–
Other reserve movements including pension deficit	(28)	–	(14)	(42)	–	(46)	(88)
Embedded value	1,067	1,521	3,679	6,267	1,446	(1,018)	6,695
Represented by:							
– Non profit			3,213				
– With-profits			466				
Value of in-force business	–	–	3,679	3,679	928	–	4,607
Shareholder net worth	1,067	1,521	–	2,588	518	(1,018)	2,088

1. The free surplus reduction of £189m to finance new business includes £27m IFRS new business strain and £155m additional required capital. Other items have a net negative impact of £7m.
2. The increase in free surplus of £648m from the expected transfer from the in-force non profit business includes £496m of IFRS operational cash generation and a £147m reduction in required capital. Other items have a net positive impact of £5m.
3. The transfer to non-covered business represents the IFRS profits arising in the period from the provision of investment management services by Legal & General Investment Management to the UK covered business, which have been included in the operating profit of the covered business on the look through basis.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

13 GROUP EMBEDDED VALUE RECONCILIATION (CONTINUED)

For the year ended 31 December 2008	Covered business UK free surplus £m	UK required capital £m	UK value of in-force £m	Total UK £m	International £m	Non-covered business Restated £m	Total Restated £m
At 1 January							
Value of in-force business (VIF)	–	–	3,460	3,460	782	–	4,242
Shareholder net worth (SNW)	2,639	1,198	–	3,837	324	(275)	3,886
	2,639	1,198	3,460	7,297	1,106	(275)	8,128
Exchange rate movements	–	–	–	–	386	(190)	196
Opening adjustment	27	–	(27)	–	–	–	–
	2,666	1,198	3,433	7,297	1,492	(465)	8,324
Operating profit for the year:							
– New business contribution[1]	(661)	232	620	191			
– Expected return on VIF	–	–	267	267			
– Expected transfer from Non profit VIF to SNW	565	(115)	(450)	–			
– With-profits transfer	77	–	(77)	–			
– Experience variances	39	3	(38)	4			
– Operating assumption changes	(31)	1	(38)	(68)			
– Development costs	(37)	–	–	(37)			
– Expected return on SNW	140	51	–	191			
Operating profit/(loss)	92	172	284	548	65	27	640
Non-operating (loss)/profit for the year:							
– Investment variances	(1,092)	(83)	189	(986)			
– Economic assumption changes	(531)	(3)	175	(359)			
– Tax impact of corporate restructure	28	–	53	81			
Non-operating (loss)/profit	(1,595)	(86)	417	(1,264)	(148)	(201)	(1,613)
(Loss)/profit for the year[2]	(1,503)	86	701	(716)	(83)	(174)	(973)
Capital movements[3]	(260)	–	–	(260)	60	(115)	(315)
Embedded value of business acquired	71	85	143	299	–	–	299
Intra-group distributions	(405)	–	–	(405)	(6)	411	–
Dividends to equity holders of the Company	–	–	–	–	–	(367)	(367)
Issue of share capital	–	–	–	–	–	10	10
Share buyback	–	–	–	–	–	(523)	(523)
Net movements in employee share schemes	–	–	–	–	–	(4)	(4)
Loss attributable to minority interests	–	–	–	–	–	63	63
Transfer to non-covered business[4]	(25)	–	–	(25)	–	25	–
Other reserve movements including pension deficit	(35)	–	(9)	(44)	–	51	7
Embedded value	509	1,369	4,268	6,146	1,463	(1,088)	6,521
Represented by:							
– Non profit			3,845				
– With-profits			423				
Value of in-force business	–	–	4,268	4,268	1,059	–	5,327
Shareholder net worth	509	1,369	–	1,878	404	(1,088)	1,194

1. The free surplus reduction of £661m to finance new business includes £101m of the short term default allowance, as well as £334m IFRS new business strain and £232m additional required capital. Other items have a net positive impact of £6m.
2. Included in the loss for the period is a non profit inter-fund transfer from free surplus to VIF of £710m.
3. Capital movements within the UK comprise the £252m cost of acquiring Nationwide Life and £8m (€10m) of capital injected from Society into France. The acquisition of Suffolk Life (£63m) was funded from the non-covered business element of Group capital and financing. The International capital movements comprise £52m ($96m) of capital injected into the USA and the £8m (€10m) of capital injected into France.
4. The transfer to non-covered business represents the IFRS profits arising in the period from the provision of investment management services by Legal & General Investment Management to the UK covered business, which have been included in the operating profit of the covered business on the look through basis.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS

14 ANALYSIS OF SHAREHOLDERS' EQUITY

As at 31 December 2009	Risk and Savings £m	Investment manage-ment £m	International £m	Group capital and financing £m	Total £m
Analysed as:					
IFRS basis shareholders' equity[1]	199	339	1,372	2,286	4,196
Additional retained profit/(loss) on an EEV basis	3,679	–	108	(1,288)	2,499
Shareholders' equity on an EEV basis	3,878	339	1,480	998	6,695
Comprising:					
Business reported on an IFRS basis	199	339	34	(1,590)	(1,018)
Business reported on an EEV basis:					
Shareholder net worth					
– Free surplus[2]			263	1,067	1,330
– Required capital to cover solvency margin			255	1,521	1,776
Value of in-force					
– Value of in-force business	3,987		1,012		4,999
– Cost of capital	(308)		(84)		(392)

As at 31 December 2008	Risk and Savings £m	Investment manage-ment £m	International £m	Group capital and financing £m	Total £m
Analysed as:					
IFRS basis shareholders' equity[1]	174	322	1,272	1,820	3,588
Additional retained profit/(loss) on an EEV basis	4,268	–	203	(1,538)	2,933
Shareholders' equity on an EEV basis	4,442	322	1,475	282	6,521
Comprising:					
Business reported on an IFRS basis	174	322	12	(1,596)	(1,088)
Business reported on an EEV basis:					
Shareholder net worth					
– Free surplus[2]			144	509	653
– Required capital to cover solvency margin			260	1,369	1,629
Value of in-force					
– Value of in-force business	4,576		1,156		5,732
– Cost of capital	(308)		(97)		(405)

1. Shareholders' equity supporting the non profit Risk and Savings businesses is held within Legal & General Assurance Society Limited and Legal & General Pensions Limited and is managed on a groupwide basis within the Group capital and financing segment.
2. Free surplus is the value of any capital and surplus allocated to, but not required to support, the in-force covered business at the valuation date.

Further analysis of shareholders' equity is included in Note 15.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

15 SEGMENTAL ANALYSIS OF SHAREHOLDERS' EQUITY

	Covered business EEV basis 2009 £m	Other business IFRS basis 2009 £m	Total 2009 £m	Covered business EEV basis 2008 £m	Other business IFRS basis 2008 £m	Total 2008 £m
Risk						
– Risk reported on an EEV basis	2,530	–	2,530	3,138	–	3,138
– General insurance	–	120	120	–	99	99
– Other	–	–	–	–	2	2
Total Risk	2,530	120	2,650	3,138	101	3,239
Savings						
– Savings reported on an EEV basis	1,149	–	1,149	1,130	–	1,130
– Core retail investments	–	66	66	–	59	59
– Other	–	13	13	–	14	14
Total Savings	1,149	79	1,228	1,130	73	1,203
Investment management	–	339	339	–	322	322
International						
– USA	904	–	904	937	–	937
– Netherlands	316	–	316	305	–	305
– France	226	–	226	221	–	221
– Emerging markets	–	34	34	–	12	12
Total International	1,446	34	1,480	1,463	12	1,475
Group capital and financing	2,588	(1,590)	998	1,878	(1,596)	282
	7,713	(1,018)	6,695	7,609	(1,088)	6,521

16 RECONCILIATION OF SHAREHOLDER NET WORTH

	UK covered business 2009 £m	Total 2009 £m	UK covered business 2008 £m	Total 2008 £m
SNW of long term operations (IFRS basis)	3,876	5,214	3,415	4,676
Other liabilities (IFRS basis)	–	(1,018)	–	(1,088)
Shareholders' equity on the IFRS basis	3,876	4,196	3,415	3,588
Purchased interest in long term business	(114)	(126)	(171)	(202)
Deferred acquisition costs/deferred income liabilities	(250)	(1,132)	(233)	(1,160)
Contingent loan[1]	(421)	(421)	(786)	(786)
Deferred tax[2]	(324)	(33)	(354)	(51)
Other[3]	(179)	(396)	7	(195)
Shareholder net worth on the EEV basis	2,588	2,088	1,878	1,194

1. On an EEV basis the contingent loan (between Society and LGPL) is modelled within the VIF. On an IFRS basis the contingent loan asset is included within the Group capital and financing net assets.
2. Deferred tax represents all tax which is expected to be paid under current legislation.
3. Other in the UK covered business relates primarily to the different treatment of sterling reserves, other long term reserves and the non profit result of LGPL under EEV compared with IFRS. Total business also includes the different treatment of the US Triple X securitisation on an EEV and IFRS basis.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

17 SENSITIVITIES

In accordance with the guidance issued by the European Insurance CFO Forum in October 2005 the table below shows the effect of alternative assumptions on the long term embedded value and new business contribution.

Effect on embedded value as at 31 December 2009

	As published £m	1% lower risk discount rate £m	1% higher risk discount rate £m	1% lower interest rate £m	1% higher interest rate £m	1% higher equity/property yields £m
UK	6,267	376	(328)	28	(51)	106
International	1,446	107	(97)	11	(25)	3
Total covered business	7,713	483	(425)	39	(76)	109

	As published £m	10% lower equity/property values £m	10% lower maintenance expenses £m	10% lower lapse rates £m	5% lower mortality (UK annuities) £m	5% lower mortality (other business) £m
UK	6,267	(149)	77	75	(157)	59
International	1,446	(6)	13	54	n/a	89
Total covered business	7,713	(155)	90	129	(157)	148

Effect on new business contribution for the year

	As published £m	1% lower risk discount rate £m	1% higher risk discount rate £m	1% lower interest rate £m	1% higher interest rate £m	1% higher equity/property yields £m
UK	305	45	(39)	7	(12)	16
International	23	17	(14)	–	(2)	–
Total covered business	328	62	(53)	7	(14)	16

	As published £m	10% lower equity/property values £m	10% lower maintenance expenses £m	10% lower lapse rates £m	5% lower mortality (UK annuities) £m	5% lower mortality (other business) £m
UK	305	(19)	11	14	(12)	6
International	23	–	1	10	n/a	12
Total covered business	328	(19)	12	24	(12)	18

Opposite sensitivities are broadly symmetrical.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

18 ASSUMPTIONS

UK assumptions

The assumed future pre-tax returns on fixed interest and RPI linked securities are set by reference to the portfolio yield on the relevant backing assets held at market value at the end of the reporting period. The calculated return takes account of derivatives and other credit instruments in the investment portfolio. Indicative yields on the total portfolios, after allowance for long term default risk, are shown below.

For annuities, separate returns are calculated for new and existing business.

Where cash balances are held at the reporting date in excess of or below strategic investment guidelines, then it is assumed that these cash balances are immediately invested, or disinvested at current yields.

Where interest rate swaps are used to reduce risk, it is assumed that these swaps will be sold before expiry and the proceeds reinvested in corporate bonds with a redemption yield 0.70% p.a. (0.70% p.a. at 31 December 2008) greater than the swap rate at that time (i.e. the long term credit rate).

Additionally where reinvestment or disinvestment is necessary to rebalance the asset portfolio in line with projected outgo, this is also assumed to take place at the long term credit rate above the swap rate at that time.

The returns on fixed and index-linked securities are calculated net of an allowance for default risk which takes account of the credit rating, outstanding term of the securities and increase in credit defaults over the short term. The allowance expressed as a level rate deduction from the expected returns was 40bps at 31 December 2009 (32bps at 31 December 2008).

Economic assumptions

	31.12.2009 % p.a.	31.12.2008 % p.a.
Equity risk premium	**3.5**	3.5
Property risk premium	**2.0**	2.0
Investment return		
– Gilts:		
– Fixed interest	**4.0**	3.8
– RPI linked	**4.5**	3.7
– Non gilts:		
– Fixed interest	**4.4 – 6.2**	4.2 – 8.2
– RPI linked	**5.1 – 6.1**	4.7 – 5.9
– Equities	**8.0**	7.3
– Property	**6.5**	5.8
Risk free rate[1]	**4.5**	3.8
Risk margin	**3.5**	4.5
Risk discount rate (net of tax)	**8.0**	8.3
Inflation		
– Expenses/earnings	**4.6**	3.6
– Indexation	**3.6**	2.6

1. The risk free rate is the gross redemption yield on the 20 year gilt index.

UK covered business

i. Assets are valued at market value.
ii. Future bonus rates have been set at levels which would fully utilise the assets supporting the policyholders' portion of the with-profits business. The proportion of profits derived from with-profits business allocated to shareholders has been assumed to be 10% throughout.
iii. The value of in-force business reflects the cost, including administration expenses, of providing for benefit enhancement or compensation in relation to certain products.
iv. Other actuarial assumptions have been set at levels commensurate with recent operating experience, including those for mortality, morbidity, persistency and maintenance expenses (excluding the development costs referred to below). These are normally reviewed annually.

    An allowance is made for future improvements in annuitant mortality based on experience and externally published data. Male annuitant mortality is assumed to improve in accordance with CMI Working Paper 30, projection MC, with a minimum annual improvement of 1.5% for future experience, and 2.0% for statutory reserving. Female annuitant mortality is assumed to improve in accordance with 75% of projection MC, with a minimum annual improvement of 1.0% for future experience and 1.5% for statutory reserving. In each case, the annual improvement is assumed to reduce linearly after age 89 to zero at age 120.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

NOTES TO THE SUPPLEMENTARY FINANCIAL STATEMENTS (CONTINUED)

On this basis, the best estimate of the expectation of life for a new 65 year old Male CPA annuitant is 24.5 years (31.12.2008: 25.2 years). The expectation of life on the regulatory reserving basis is 25.7 years (31.12.2008: 26.4 years).

v. Development costs relate to investment in strategic systems and development capability that are charged to the covered business. Projects charged to the non-covered business are included within Investment projects in Group capital and financing.

International

vi. Key assumptions:

	31.12.2009 % p.a.	31.12.2008 % p.a.
USA		
Reinvestment rate	**5.1**	5.4
Risk margin	**3.5**	4.5
Risk discount rate (net of tax)	**7.4**	6.8
Europe		
Government bond return	**3.6**	3.5
Risk margin	**3.5**	4.5
Risk discount rate (net of tax)	**7.1**	8.0

vii. Other actuarial assumptions have been set at levels commensurate with recent operating experience, including those for mortality, morbidity, persistency and maintenance expenses.

Tax

viii. The profits on the covered business, except for the profits on the Society shareholder capital held outside the long term fund, are calculated on an after tax basis and are grossed up by the notional attributed tax rate for presentation in the income statement. The tax rate used for grossing up is the corporate tax rate in the territory concerned, which for the UK was 28% (31.12.2008: 28%). The profits on the Society shareholder capital held outside the long term fund are calculated before tax and therefore tax is calculated on an actual basis.

EUROPEAN EMBEDDED VALUE BASIS (CONTINUED)

INDEPENDENT AUDITORS' REPORT

To the Directors of Legal & General Group Plc ("the Company") on the Supplementary Financial Statements – European Embedded Value Basis

We have audited the Supplementary Financial Statements – European Embedded Value Basis of Legal & General Group Plc for the year ended 31 December 2009 which comprise the Consolidated Income Statement – European Embedded Value Basis, Consolidated Statement of Comprehensive Income – European Embedded Value Basis, Consolidated Balance Sheet – European Embedded Value Basis and the relevant notes ("the supplementary financial statements") which have been prepared in accordance with the European Embedded Value ("EEV") basis set out in Note 1 – Basis of Preparation and which should be read in conjunction with the Group's financial statements.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the supplementary financial statements in accordance with the EEV basis set out in Note 1 – Basis of Preparation. Our responsibility, as set out in our letter of engagement agreed with you dated 27 January 2010 is to audit the supplementary financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors. This report, including the opinion, has been prepared for and only for the Company's directors as a body in accordance with our letter of engagement dated 27 January 2010 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the supplementary financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

Opinion on the supplementary financial statements

In our opinion, the supplementary financial statements for the year ended 31 December 2009 have been properly prepared in all material respects in accordance with the European Embedded Value Basis set out in Note 1 – Basis of Preparation.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants
London
22 March 2010

Notes:
(a) The supplementary financial statements are published on the website of Legal & General Group Plc, www.legalandgeneralgroup.com. The maintenance and integrity of the Legal & General Group Plc website is the responsibility of the directors; the audit work does not involve consideration of these matters and, accordingly, we accept no responsibility for any changes that may have occurred to the supplementary financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of supplementary financial statements may differ from legislation in other jurisdictions.

INDEPENDENT AUDITORS' REPORT

To the Members of Legal & General Group Plc

We have audited the parent company financial statements of Legal & General Group Plc for the year ended 31 December 2009 which comprise the Company Balance Sheet, the Company Statement of Total Recognised Gains and Losses, Company Reconciliation of Movements in Total Equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion the parent company financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2009;
- have been properly prepared in accordance with the United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the parent company financial statements are prepared is consistent with the parent company financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matter

We have reported separately on the group financial statements of Legal & General Group Plc for the year ended 31 December 2009.

Richard Keers (Senior Statutory Auditor)
For and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
22 March 2010

Notes:
(a) The financial statements are published on the website of Legal & General Group Plc, www.legalandgeneralgroup.com. The maintenance and integrity of the Legal & General Group Plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

COMPANY BALANCE SHEET

As at 31 December 2009	Notes	2009 £m	2008 £m
Fixed assets			
Investments	8	**5,699**	5,075
Current assets			
Amounts owed by Group undertakings		**848**	747
Tax		**26**	30
Derivative assets	9	**236**	280
Other debtors		**15**	9
Creditors: amounts falling due within one year			
Amounts owed to Group undertakings		**(12)**	(9)
Other creditors	10	**(77)**	(116)
Net current assets		**1,036**	941
Total assets less current liabilities		**6,735**	6,016
Creditors: amounts falling due after more than one year			
Subordinated borrowings	11	**(1,897)**	(1,657)
Senior borrowings	11	**–**	(146)
Amounts owed to Group undertakings		**(621)**	(621)
Net assets		**4,217**	3,592
Capital and reserves			
Called up share capital	12	**147**	147
Share premium account	12	**936**	936
Capital redemption and other reserves	13	**57**	54
Revaluation reserve	13	**1,969**	1,351
Profit and loss account	13	**1,108**	1,104
Total shareholders' funds		**4,217**	3,592

The notes on pages 208 to 213 form an integral part of these financial statements.

The financial statements on pages 206 to 213 were approved by the directors on 22 March 2010 and were signed on their behalf by:

John Stewart
Chairman

Tim Breedon
Group Chief Executive

Nigel Wilson
Group Chief Financial Officer

COMPANY STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

For the year ended 31 December 2009	Notes	2009 £m	2008 £m
Profit for the financial year		**182**	445
Gains/(losses) on revaluation of investments in subsidiary undertakings	8	**618**	(1,423)
Total recognised gains and losses relating to the year		**800**	(978)

COMPANY RECONCILIATION OF MOVEMENTS IN TOTAL SHAREHOLDERS' FUNDS

For the year ended 31 December 2009	Notes	2009 £m	2008 £m
As at 1 January		**3,592**	5,442
Total recognised gains and losses		**800**	(978)
Net movements in employee scheme shares		**2**	4
Dividend distributions to equity holders of the Company during the year	3	**(185)**	(367)
Issue of share capital		**–**	10
Cancellation of shares under the share buyback programme		**–**	(523)
Transfer from share-based payments reserve		**8**	4
As at 31 December		**4,217**	3,592

NOTES TO THE COMPANY FINANCIAL STATEMENTS

1 ACCOUNTING POLICIES

Basis of preparation

The Company's financial statements have been prepared under the historical cost convention, modified by the revaluation of certain assets, as required by the Companies Act 2006, and in accordance with applicable UK accounting standards.

The Company's financial statements have been prepared in compliance with Section 394 and 396 of, the Companies Act 2006 adopting the exemption of omitting the profit and loss account conferred by Section 408 of that Act.

Investment income

Investment income includes dividends and interest. Dividends receivable from Group companies are recognised in the period in which the dividends are declared and approved at the general meeting or paid. Interest income is recognised using the effective interest method.

Distributions

Dividend distribution to the Company's shareholders is recognised as a liability in the period in which the dividends are authorised and are no longer at the discretion of the Company. Final dividends are accrued when approved by the Company's shareholders at a general meeting and interim dividends are recognised when paid.

Interest expense

Interest expense reflects the underlying cost of borrowing, based on the effective interest method, and includes payments and receipts made under derivative instruments which are amortised over the interest period to which they relate.

Investment in subsidiary undertakings

Shares in subsidiary undertakings are stated at current value. Unrealised gains or losses arising on investments in subsidiary undertakings are taken to the revaluation reserve.

Loans and receivables

Loans and receivables are held at amortised cost using the effective interest method.

Derivative financial instruments and hedge accounting

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 and interest rate swap contracts to hedge these exposures. The Company uses hedge accounting, provided the prescribed criteria are met, to recognise the offsetting effects of changes in the fair value or cash flow of the derivative instrument and the hedged item. The Company's principal use of hedge accounting is to hedge the fair value movements in loans due to interest rate and exchange rate fluctuations. Any gain or loss from remeasuring the hedging instrument at fair value is recognised immediately in the profit and loss account. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the profit and loss account.

The relationship between the hedging instrument and the hedged item, together with the risk management objective and strategy for undertaking the hedge transaction, are documented at the inception of the transaction. The effectiveness of the hedge is documented and monitored on an ongoing basis. Hedge accounting is only applied for highly effective hedges (between 80% and 125% effectiveness) with any ineffective portion of the gain or loss recognised in the profit and loss account in the current period.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instruments which do not qualify for hedge accounting are recognised immediately in the profit and loss account.

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 profit and loss account over the borrowing period using the effective interest method.

Deferred tax

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Deferred tax is measured using tax rates expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled, based on tax rates and law which have been enacted or substantively enacted at the balance sheet date. Deferred income tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised. Deferred tax assets and liabilities are not discounted.

Foreign currencies

Transactions denominated in foreign currencies are translated into Sterling at the rates of exchange prevailing at the time of the transactions. Assets and liabilities denominated in foreign currencies are translated into Sterling at the rates of exchange prevailing at the balance sheet date with the exception of non-monetary items which are maintained at historic rates. Exchange gains or losses are recognised in the profit and loss account, except those arising upon the revaluation of fixed assets, which are included in the revaluation reserve.

Pension costs

The Company participates in multi-employer defined benefit schemes, within the meaning of FRS 17, 'Retirement Benefits', which, as its share of the underlying assets and liabilities cannot be identified, have been treated for reporting purposes as defined contribution schemes. In addition to these schemes the Company also contributes to defined contribution schemes. The Company charges the costs of its pension schemes against profit as incurred. Any difference between the cumulative amounts charged against profits and contribution amounts paid is included as a provision or prepayment in the balance sheet.

NOTES TO THE COMPANY FINANCIAL STATEMENTS (CONTINUED)

The assets of the defined benefit schemes are held in separate trustee administered funds, which have been subject to regular valuation every three years and updated by formal reviews at reporting dates by qualified actuaries who were employees of the Group.

Share-based payments

The Company operates a number of share-based payment plans on behalf of its subsidiaries. The fair value of the equity instruments granted is spread over the vesting period of the instrument and treated as a capital contribution to the respective subsidiary. The total capital contribution is determined by reference to the fair value of the awards, excluding the impact of any non-market vesting conditions.

At each balance sheet date, the Company revises its estimate of the number of equity instruments which are expected to become exercisable. It recognises the impact of the revision of original estimate, if any, in the cost of the investment in the subsidiary and a corresponding adjustment is made to equity over the remaining vesting period. On vesting or exercise, the difference between the accumulated capital contribution and the actual cost to the Company is transferred to retained earnings. Where new shares are issued, the proceeds received are credited to share capital and share premium. Any capital contribution is subsequently recharged to the respective subsidiary as incurred and the corresponding cost of investment is reduced.

Share buyback

Where shares are cancelled under the share buyback programme, the consideration paid, including any directly attributable incremental costs, is deducted from equity attributable to shareholders. As required by the Companies Act 2006, the equivalent of the nominal value of shares cancelled is transferred to a capital redemption reserve.

2 RISK MANAGEMENT AND CONTROL

Management of risk

The Company, in course of its business activities, is exposed to market, credit and liquidity risk. Overall responsibility for the management of these risks is vested in the Board. To support it in this role, a risk framework is in place comprising a structure of formal committees, risk assessment and reporting processes and risk review functions. The framework provides assurance that risks are being appropriately identified and managed and that an independent assessment of risks is being performed.

Risk assessment processes

A continuous process is in place formally identifying, evaluating and managing the significant risks to the achievement of the Company's objectives. A standard approach is used to assess risks.

Senior management and the risk review functions (see below) review the output of the assessments.

Risk review functions

Risk review functions provide oversight of the risk management processes within the Company. Responsibilities include the evaluation of changes in the business operating environment and business processes, the assessment of these changes on risks to business and the monitoring of the mitigating actions. They also ensure that risk committees are provided with meaningful risk reports and that there is appropriate information to assess risk issues.

Details of the categories of risk to the Company and high level management processes are set out below. Defined policies for the management of its key risks are in place, the operation of which are supported by risk review functions and are independently confirmed by Group internal audit.

Market risk

Market risk is the risk arising from fluctuations in interest and exchange rates and market valuations.

Credit risk

Credit risk is the risk that the Company is exposed to loss if another party fails to perform its financial obligations to the Company.

Credit risk is managed through the setting and regular review of detailed counterparty credit and concentration limits. Compliance with these limits for investment and treasury transactions is monitored daily. The Counterparty Credit Committee oversees these processes. Counterparties used for the provision of hedging derivatives have a minimum credit rating of A- from Standard & Poor's. The Company's maximum exposure to credit risk on its financial assets at the balance sheet date is equal to the value of the derivative assets.

Liquidity risk

Liquidity risk is 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 costs.

A degree of liquidity risk is implicit in the Company. Liquidity risk arises as a consequence of the uncertainty surrounding the value and timing of cash flows. The Company's treasury function manages liquidity to ensure that it maintains sufficient liquid assets and standby facilities to meet a prudent estimate of its net cash outflows.

NOTES TO THE COMPANY FINANCIAL STATEMENTS (CONTINUED)

3 DIVIDENDS AND OTHER DISTRIBUTIONS

	Per share 2009 p	Total 2009 £m	Per share 2008 p	Total 2008 £m
Ordinary share dividends paid in the year				
– Prior year final dividend	**2.05**	**120**	4.10	248
– Current year interim dividend	**1.11**	**65**	2.01	119
	3.16	**185**	6.11	367
Ordinary share dividend proposed[1]	**2.73**	**160**	2.05	120

1. The dividend proposed has not been included as a liability in the balance sheet.

4 DIRECTORS' EMOLUMENTS AND OTHER EMPLOYEE INFORMATION

Full disclosures of Legal & General Group Plc directors' emoluments are contained within those parts of the Directors' Report on Remuneration which are described as having been audited. At 31 December 2009 there were no loans outstanding with directors of the Company (2008: £nil). The Company has no other employees (2008: £nil).

5 PENSIONS

The Company operates the following pension schemes in the UK. There were no contributions prepaid or outstanding at either 31 December 2009 or 31 December 2008 in respect of these schemes and the Company has no liability for retirement benefits.

- Legal & General Group UK Pension and Assurance Fund (the Fund). The Fund is a defined benefit scheme which was closed to new members from January 1995; last full actuarial valuation as at 31 December 2006.
- Legal & General Group UK Senior Pension Scheme (the Scheme). The Scheme is a defined benefit scheme which, with a few exceptions (principally transfers from the Fund), was closed to new members from August 2000 and finally closed to new members from April 2007; last full actuarial valuation as at 31 December 2006.
- Legal & General Group Personal Pension Plan (UK) – a defined contribution scheme.
- Legal & General Staff Stakeholder Pension Scheme (UK) – a defined contribution scheme.

As the Fund and the Scheme are effectively closed to new members, under the projected unit method of valuation, the current service costs will increase as the age profile of active members rises.

In the UK, the Fund and the Scheme are multi-employer defined benefit schemes, which, as the Company's share of the underlying assets and liabilities cannot be identified, have been treated for reporting purposes as defined contribution schemes. There was a deficit in respect of these schemes for the year ended 31 December 2009 of £203m (2008: £101m) and the contributions in respect of them for the year were £59m (2008: £54m). Further information is given in Note 36 of the Group's consolidated financial statements.

6 SHARE-BASED PAYMENTS

Legal & General Group Plc grants share-based payments to employees within the Legal & General Group. The Group recognises an expense for these payments measured indirectly by reference to the fair value of the equity instruments granted. The expense is recognised over the vesting period as the services are received. The relevant company is recharged its share of this expense with reference to the benefits it receives from the employees. The full disclosures required by FRS 20 are provided in the Group's consolidated financial statements.

The total expense recharged to the Company in relation to share-based payments was £nil (2008: £nil).

7 AUDITORS' REMUNERATION

Remuneration receivable by the Company's auditor for the audit of the Company's financial statements is not presented. The Group's consolidated IFRS financial statements disclose the aggregate remuneration receivable by the Company's auditor for the audit of the Group's annual accounts, which include the Company's financial statements.

The disclosure of fees payable to the auditor and its associates for other (non-audit) services has not been made because the Group's consolidated financial statements are required to disclose such fees on a consolidated basis.

NOTES TO THE COMPANY FINANCIAL STATEMENTS (CONTINUED)

8 INVESTMENTS

	Shares in Group companies 2009 £m	Loans to Group companies 2009 £m	Total 2009 £m	Shares in Group companies 2008 £m	Loans to Group companies 2008 £m	Total 2008 £m
At valuation, 1 January	**4,237**	**838**	**5,075**	5,446	669	6,115
Additions	**74**	**–**	**74**	214	97	311
Repayment	**–**	**–**	**–**	–	(97)	(97)
Revaluation	**618**	**(68)**	**550**	(1,423)	169	(1,254)
At valuation, 31 December	**4,929**	**770**	**5,699**	4,237	838	5,075
At cost, 31 December	**2,994**	**746**	**3,740**	2,920	746	3,666

Additions represent capital injections into Group undertakings.

9 DERIVATIVE ASSETS AND LIABILITIES

	Contract/ notional amount 2009 £m	Fair values Assets 2009 £m	Fair values Liabilities[1] 2009 £m
Interest rate contracts – held for trading	**1,531**	**22**	**74**
Interest rate contracts – fair value hedges	**600**	**68**	**–**
Forward foreign exchange contracts – net investment hedges	**733**	**10**	**–**
Forward foreign exchange contracts – held for trading	**531**	**136**	**–**
Derivative assets and liabilities		**236**	**74**

	Contract/ notional amount 2008 £m	Fair values Assets 2008 £m	Fair values Liabilities[1] 2008 £m
Interest rate contracts – held for trading	1,583	5	94
Interest rate contracts – fair value hedges	600	84	–
Forward foreign exchange contracts – net investment hedges	679	–	19
Forward foreign exchange contracts – held for trading	583	191	–
Derivative assets and liabilities		280	113

1. Derivative liabilities are reported in the balance sheet within Other creditors.

The descriptions of each type of derivative are given in Notes 20 and 48 of the Group's consolidated financial statements.

10 OTHER CREDITORS

	2009 £m	2008 £m
Derivative liabilities (Note 9)	**74**	113
Other creditors	**3**	3
Other creditors	**77**	116

Other creditors are expected to be settled within five years.

NOTES TO THE COMPANY FINANCIAL STATEMENTS (CONTINUED)

11 BORROWINGS
Analysis by nature

	Carrying amount 2009 £m	Coupon rate 2009 %	Fair value 2009 £m	Carring amount 2008 £m	Coupon rate 2008 %	Fair value 2008 £m
Subordinated borrowings						
6.385% Sterling perpetual capital securities (Tier 1)	**666**	**6.39**	**473**	692	6.39	414
5.875% Sterling undated subordinated notes (Tier 2)	**425**	**5.88**	**326**	426	5.88	287
4.0% Euro subordinated notes 2025 (Tier 2)	**498**	**4.00**	**455**	539	4.00	283
10% Sterling subordinated notes 2041 (Tier 2)	**308**	**10.00**	**364**	–	–	–
Total subordinated borrowings	**1,897**		**1,618**	1,657		984
Senior borrowings						
Bank loans 2009	**–**	**–**	**–**	146	6.43	146
Total senior borrowings	**–**	**–**	**–**	146		146
Total borrowings	**1,897**		**1,618**	1,803		1,130

As at 31 December 2009, the Company had in place a £960m syndicated committed revolving credit facility provided by a number of its key relationship banks, maturing in December 2012.

£87m of interest expense was incurred during the year (2008: £86m).

6.385% Sterling perpetual capital securities
In 2007, Legal & General Group Plc issued £600m of 6.385% Sterling perpetual capital securities. Simultaneous with the issuance, the fixed coupon was swapped into six month LIBOR plus 0.94% pa. These securities are callable at par on 2 May 2017 and every three months thereafter. If not called, the coupon from 2 May 2017 will be reset to three month LIBOR plus 1.93% pa. For regulatory purposes these securities are treated as innovative tier 1 capital. These securities have been classified as liabilities as the interest payments become mandatory in certain circumstances.

5.875% Sterling undated subordinated notes
In 2004, Legal & General Group Plc issued £400m of 5.875% Sterling undated subordinated notes. These notes are callable at par on 1 April 2019 and every five years thereafter. If not called, the coupon from 1 April 2019 will be reset to the prevailing five year benchmark gilt yield plus 2.33% pa. These notes are treated as upper tier 2 capital for regulatory purposes. These securities have been classified as liabilities as the interest payments become mandatory in certain circumstances.

4.0% Euro subordinated notes 2025
In 2005, Legal & General Group Plc issued €600m of 4.0% Euro dated subordinated notes. The proceeds were swapped into sterling. The notes are callable at par on 8 June 2015 and each year thereafter. If not called, the coupon from 8 June 2015 will reset to a floating rate of interest based on prevailing three month Euribor plus 1.7% pa. These notes mature on 8 June 2025 and are treated as lower tier 2 capital for regulatory purposes.

10% Sterling subordinated notes 2041
On 16 July 2009, Legal & General Group Plc issued £300m of 10% dated subordinated notes. The notes are callable at par on 23 July 2021 and every five years thereafter. If not called, the coupon from 23 July 2021 will be reset to the prevailing five year benchmark gilt yield plus 9.325% pa. These notes mature on 23 July 2041 and are treated as lower tier 2 capital for regulatory purposes.

NOTES TO THE COMPANY FINANCIAL STATEMENTS (CONTINUED)

12 SHARE CAPITAL AND SHARE PREMIUM ACCOUNT

Authorised share capital	2009 Number of shares	2009 £m	2008 £m
At 31 December: ordinary shares of 2.5p each	**9,200,000,000**	**230**	230

Issued share capital, fully paid	Number of shares	Called up share capital £m	Share premium account £m
As at 1 January 2009	**5,861,627,994**	**147**	**936**
Cancellation of shares under the share buyback programme[1]	–	–	–
Options exercised under share option schemes			
– Executive share option scheme	**20,000**	–	
– Savings related share option scheme	**568,786**	–	–
As at 31 December 2009	**5,862,216,780**	**147**	**936**

Issued share capital, fully paid	Number of shares	Called up share capital £m	Share premium account £m
As at 1 January 2008	6,296,321,160	157	927
Cancellation of shares under the share buyback programme[1]	(449,891,914)	(11)	–
Options exercised under share option schemes			
– Executive share option scheme	640,846	–	1
– Savings related share option scheme	14,557,902	1	8
As at 31 December 2008	5,861,627,994	147	936

1. During 2008, 449,891,914 shares were repurchased and cancelled under the share buyback programme representing 7.1% of opening issued share capital, at a cost of £523m including expenses.

Options over the ordinary share capital of the Company are disclosed in Note 15 of the Group's consolidated financial statements.

13 MOVEMENTS IN RESERVES

	Capital redemption reserve £m	Hedging reserve £m	Share-based payment reserve £m	Revaluation reserve £m	Profit and loss account £m	Total £m
As at 1 January 2009	**17**	**(1)**	**38**	**1,351**	**1,104**	**2,509**
Retained profit after tax and dividends	–	–	–	–	**(4)**	**(4)**
Increase in the net assets of subsidiaries	–	–	–	**618**	–	**618**
Value of employee services	–	–	**21**	–	–	**21**
Shares vested and transfer from share-based payments reserve	–	–	**(18)**	–	**8**	**(10)**
Balance at 31 December 2009	**17**	**(1)**	**41**	**1,969**	**1,108**	**3,134**

	Capital redemption reserve £m	Hedging reserve £m	Share-based payment reserve £m	Revaluation reserve £m	Profit and loss account £m	Total £m
As at 1 January 2008	6	(1)	34	2,774	1,545	4,358
Retained profit after tax and dividends	–	–	–	–	78	78
Decrease in the net assets of subsidiaries	–	–	–	(1,423)	–	(1,423)
Value of employee services	–	–	22	–	–	22
Shares vested and transfer from share-based payments reserve	–	–	(18)	–	4	(14)
Cancellation of shares under the share buyback programme	11	–	–	–	(523)	(512)
Balance at 31 December 2008	17	(1)	38	1,351	1,104	2,509

14 SUBSIDIARY UNDERTAKINGS

Full disclosure of the Company's investments in subsidiary undertakings is contained in Note 43 of the Group's consolidated financial statements.

SHAREHOLDER INFORMATION

Annual General Meeting

The 2010 Annual General Meeting (AGM) will be held on Wednesday, 26 May 2010 at 11.30am at The Institution of Engineering and Technology, Savoy Place, London WC2R 0BL. The AGM provides Legal & General with the opportunity to meet its shareholders. The Board regards the AGM as an important opportunity to communicate directly with private investors. The Notice of Meeting and all other details for the AGM are available at www.legalandgeneralgroup.com (Website).

Dividend information

Dividend per share

This year the directors are recommending the payment of a final dividend of 2.73p per share. If you add this to your interim dividend of 1.11p per share, the total dividend recommended for 2009 will be 3.84p per share (2008: 4.06p per share). The key dates for the payment of dividends this year are:

Final dividend 2009	
Ex-dividend date	14 April 2010
Record date	16 April 2010
Payable	1 June 2010

Interim dividend 2010	
Ex-dividend date	1 September 2010
Record date	3 September 2010
Payable	1 October 2010

Dividend payments

Legal & General is keen to encourage all its shareholders to have their dividends paid directly into a Bank or Building Society Account. If you would like more details or a dividend mandate form, please contact our Registrars, Equiniti Limited. Details of how to contact the Registrars can be found on the opposite page.

Dividend reinvestment plan

The Legal & General Dividend Reinvestment Plan (DRIP) enables shareholders to use their cash dividends to purchase Legal & General Group Plc shares.

If you would like more details, please contact our Registrars. Alternatively, the DRIP booklet and mandate form can be found in the Investors Section of the Website.

Communications

Internet

Information about the Company including details of the current share price is available in the Investors Section of the Website.

Investor relations

Private investors should contact the Registrars.

Institutional investors can contact the Investor Relations Team on telephone: 020 3124 2345 or email: investor.relations@group.landg.com.

Over the last year many companies have become aware that their shareholders have received unsolicited phone calls or correspondence concerning investment matters which imply a connection to the company concerned. These are typically from overseas based 'brokers' who target UK shareholders offering to sell them what often turn out to be worthless or high risk shares in US or UK investments.

They can be very persistent and extremely persuasive and a 2006 survey by the Financial Services Authority (FSA) has reported that the average amount lost by investors is around £20,000. It is not just the novice investor that has been duped in this way; many of the victims had been successfully investing for several years. Shareholders are advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers of free reports into the company.

If you receive any unsolicited investment advice, make sure you get the correct name of the person and organisation and make a record of any other information they give you, e.g. telephone number, address etc.

Check that they are properly authorised by the FSA before getting involved. You can check at www.fsa.gov.uk/register/.

The FSA also maintains on its website a list of unauthorised overseas firms who are targeting, or have targeted, UK investors and any approach from such organisations should be reported to the FSA so that this list can be kept up to date and any other appropriate action can be considered. If you deal with an unauthorised firm, you would not be eligible to receive payment under the Financial Services Compensation Scheme. The FSA can be contacted by completing an online form at http://www.fsa.gov.uk/pages/doing/regulated/law/alerts/overseas.html or, if you do not have access to the internet, on 0845 606 1234.

Inform our Registrars, Equiniti Limited, on 0871 384 2118. They are not able to investigate such incidents themselves but will record the details and pass them onto us and liaise with the FSA.

Details of any sharedealing facilities that the company endorses will be included in company mailings.

More detailed information on this or similar activity can be found on the FSA website http://www.fsa.gov.uk/consumer/.

SHAREHOLDER INFORMATION (CONTINUED)

Financial reports
Legal & General publishes an Annual Report and Accounts and, for investors not needing the full details of an Annual Report, Summary Financial Statements. These are available on the Website.

The Annual Report and Accounts and Summary Financial Statements are sent to those shareholders who have elected to receive paper copies. Alternatively, shareholders may elect to receive notification by email by registering on www.shareview.com

Copies of previous financial reports are available on the Website. Printed copies can be obtained on request to the Company. If you receive more than one copy of our communications, it could be because you have more than one record on the share register. To avoid duplication mailings, please contact the Registrars, who can arrange for your accounts to be amalgamated.

Registrars
You can contact our Registrars, Equiniti Limited:
By post: Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA.
By telephone: Shareholder Helpline: 0871 384 2118*.

* Calls to this number are charged at 8p per minute from a BT landline. Other telephone provider costs may vary.

All shareholder enquiries should be addressed to Equiniti.

The Registrars also provide the following services:

Electronic share service
The electronic share service allows you to hold shares in Legal & General without the need for a share certificate and enables you to benefit from shorter market settlement periods. Individual shareholders hold their Legal & General shares in a nominee holding registered in the name of Equiniti Corporate Nominees Limited.

To join, or obtain further information, contact the Registrars. They will send you a booklet, outlining the terms and conditions under which your shares will be held, together with the appropriate share transfer form. The booklet and the share transfer form are also available in the Investors Section of the Website.

Shareview
Shareview allows you to view your Legal & General shareholding on the internet. Registering is easy; simply log on to www.shareview.co.uk and follow the instructions. You will need your shareholder reference number, which can be found on your latest dividend counterfoil. If you have any queries, please call the Shareholder Helpline.

Individual Savings Account (ISA)
Equiniti Financial Services Limited provide a Single Company ISA for Legal & General Group Plc shares. If you would like more information, please call 0871 384 2244*.

* Calls to this number are charged at 8p per minute from a BT landline. Other telephone provider costs may vary.

Share dealing service
Shareholders may buy or sell shares using the internet or telephone through a number of nominated providers. Details can be found on the Website.

General information
Capital gains tax: For the purpose of calculating UK capital gains tax, the market value on 31 March 1982 of each share was 7.996p, after adjusting for the 1986 capitalisation issue and the 1996 and 1999 sub-divisions, but not reflecting any rights taken up under the 2002 rights issue.

Close company provisions: The Company is not a close company within the terms of the Income and Corporation Taxes Act 1988.

Registered office: One Coleman Street, London EC2R 5AA. Registered in England and Wales, No. 1417162.

Shareholder offer line: For details of shareholder offers on Legal & General products call 0500 65 5555.

IMPORTANT DATES

23 March 2010	Publication of Preliminary Results 2009
14 April 2010	Ex-dividend date
17 May 2010	Last day for DRIP elections
26 May 2010	Annual General Meeting
1 June 2010	Payment of Final Dividend for 2009 (to members registered on 16 April 2010)
4 August 2010	Publication of Interim Results for 2010 and Declaration of Interim Dividend
1 September 2010	Ex-dividend date
17 September 2010	Last day for DRIP elections
1 October 2010	Payment of Interim Dividend for 2010 (to members registered on 3 September 2010)

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www.legalandgeneralgroup.com

Designed and produced by Addison www.addison.co.uk

Printed on 9lives 55 Silk paper and 9lives Offset paper. These papers have been independently certified according to the rules of the Forest Stewardship Council (FSC). The inks used are all vegetable oil based.

Printed at St Ives Westerham Press Ltd, ISO14001, FSC certified and CarbonNeutral®

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Product group from well-managed forests, controlled sources and recycled wood or fiber
Cert no. SGS-COC-1732
www.fsc.org
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