Friends Life Holdings plc

Registered in England & Wales No. 06986155

Annual Report and Financial Statements 2016

Contents

Directors and Officers

Directors

D F S Rogers
T D Stoddard

Officer – Company Secretary

J C Baddeley

Independent Auditors

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London
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Registered Office

Pixham End
Dorking
Surrey
RH4 1QA

Company Number

Registered in England & Wales No. 06986155

Other Information

Friends Life Holdings plc is a member of the Aviva plc group of companies (the Aviva Group).

Strategic Report

The directors present their strategic report for the members of Friends Life Holdings plc (the Company) and its subsidiaries (the Group) for the year ended 31 December 2016.

Review of the Group's Business

The Company is a wholly-owned subsidiary of Aviva Group Holdings Limited (AGH). Its principal activity is to hold the three subordinated debt instruments listed on the London Stock Exchange.

Financial position and performance

The financial position of the Group as at 31 December 2016 is shown in the Consolidated Statement of Financial Position on page 26, with the results shown in the Consolidated Income Statement on page 23 and the Consolidated Statement of Cash Flows on page 27.

Future outlook

High level strategies of the Aviva Group are determined by the Board of Aviva plc and these are shown in the 2016 Aviva plc Annual Report and Accounts and Preliminary Announcement for the year ended 31 December 2016. The directors consider that the Group's principal activities will continue unchanged for the foreseeable future.

Principal risks and uncertainties

A description of the principal risks and uncertainties facing the Group and the Group's risk management policies to manage and mitigate these risks are set out in note 32 to the financial statements.

Risk factors beyond the Group's control that could cause actual results to differ materially from those estimated include:

Credit risk
The net asset value of the Group's financial resources is exposed to the potential default on its long term loans to Friends Life Limited (FLL), a subsidiary undertaking of Aviva plc, and which has an external insurer financial strength rating of A+, and as such the risk of counterparty default is considered remote.

Foreign exchange risk
The net asset value of the Group's financial resources is exposed to potential fluctuations in foreign exchange rates through its issuance of US$575 million (*2015: US$575 million*) reset perpetual subordinated note. The US$ cash flows for the coupons and principal up until the first reset date in 2018 have been fully hedged with cross currency derivative swaps.

Key performance indicators

The directors consider that the Group's key performance indicators (KPIs) that communicate the financial performance are as follows:

Measure	**2016** **£m**	2015 £m
Investment return	**171**	145
Finance costs	**(175)**	(110)

Investment return is higher in 2016 due to gain on the cross currency swap arising from weak USD:GBP foreign exchange rate, partly offset by the change in interest rate on the internal Step Up Tier 1 Insurance Capital Securities (STICS) with FLL from 6.302% to 4.39%.

Finance costs are higher in 2016 due to higher foreign exchange losses arising from weak USD:GBP foreign exchange rate.

On behalf of the Board on 8 March 2017

D F S Rogers
Director

Directors Report

The directors present their annual report and financial statements for Friends Life Holdings plc and its subsidiaries (the Group) for the year ended 31 December 2016. This Directors' Report also comprises the management report required under Disclosure and Transparency Rule 4.1.5R.

Directors

The names of the present directors of the Company appear on page 3.

The following directors were appointed on 12 August 2016:

S D Rich
D F S Rogers
T D Stoddard

J R Lister resigned as director on 12 August 2016.

Sir G M Williamson resigned as director on 31 August 2016

A D Briggs resigned as director on 9 September 2016.

S D Rich resigned as a director on 31 December 2016.

Future outlook

Likely future developments in the business of the Company and its subsidiaries are discussed in the strategic report on page 4.

Dividends and appropriations

Interim ordinary dividends of £210 million on the Company's ordinary shares were declared and paid during 2016 *(2015: £4,858 million)*. The directors do not recommend a final dividend on the Company's ordinary shares for the year ended 31 December 2016 *(2015: £nil)*. The total cost of dividends paid during the year, including interest on Step-up Tier One Insurance Capital Securities (STICS) of £Nil *(2015: £7 million)*, amounted to £210 million *(2015: £4,865 million)*.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the strategic report. The financial statements sections include notes on the management of its risks including market, credit and liquidity risk (note 32).

The Group and its ultimate parent, Aviva plc, have considerable financial resources and as a consequence, the directors believe that the Group is well placed to manage its business risks successfully despite the current uncertain macro-economic outlook. After making enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

Significant transactions

Liquidation of Syndicated loans
On 9 November 2015, the Company commenced a number of actions to support the disposal of the £160 million portfolio of syndicated loans managed by Ares Management Limited. Enhanced Loan Investment Strategy SICAV-SIF (ELIS), a SICAV based in Luxembourg, had been established to hold these assets and the Company owned the units in the SICAV. The wind down of the portfolio of syndicated loans was completed on 30 June 2016 and ELIS was placed into liquidation in 2016.

Capital reduction
On 7 December 2016, the Company undertook a capital reduction under the provisions of section 641(1) of the Companies Act 2006. Following this reduction, the ordinary share capital account has been reduced by £250 million. Distributable reserves have increased by a corresponding amount.

Financial instruments & financial risk management

The business of the Group includes the use of financial instruments. Details of the financial instruments are set out in note 13 to the financial statements.

Details of the Group's risk management objectives and policies and exposures to risk relating to financial instruments are set out in note 32 to the financial statements.

Directors Report continued

Employees

The Company has no employees. All staff are employed by fellow subsidiary undertakings of Aviva plc, Aviva Employment Services Limited and Aviva Investors Employment Services Limited, Friends Life Services Limited, Friends Life Management Services Limited and Sesame Services Limited. Disclosures relating to employees may be found in the Annual Report and Financial Statements of these companies respectively.

Disclosure of information to the auditors

Each person who was a director of the Company on the date that this report was approved confirms that:

(a) so far as the director is aware, there is no relevant audit information, being information needed by the auditors in connection with preparing their report, of which the auditors are unaware; and

(b) each director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Independent auditors

A resolution is to be proposed at the 2017 Annual General Meeting for the re-appointment of PricewaterhouseCoopers LLP as auditors of the Company under the deemed appointment rules of Section 487 of the Companies Act 2006.

A resolution will also be proposed authorising the directors to determine the auditors' remuneration.

Qualifying indemnity provisions

Aviva plc, the Company's ultimate parent, granted in 2004 an indemnity to the directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 1985 (which continue to apply in relation to any provision made before 1 October 2007). This indemnity is a 'qualifying third party indemnity' for the purposes of sections 309A to 309C of the Companies Act 1985. These qualifying third party indemnity provisions remain in force as at the date of approving the Directors' Report by virtue of paragraph 15, Schedule 3 of The Companies Act 2006 (Commencement No. 3, Consequential Amendments, Transitional Provisions and Savings) Order 2007.

Statement of directors' responsibilities

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

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

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

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

The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess a company's performance, business model and strategy.

Directors Report continued

Statement of directors' responsibilities continued

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

Corporate governance

The Group is a wholly-owned subsidiary of Aviva plc, a Group with a premium listing on the London Stock Exchange, and as such is subject to Aviva plc's system of risk management, internal control and financial reporting. Aviva plc is subject to the UK Corporate Governance Code. The Aviva plc Annual Report and Accounts set out details of how the Aviva Group has applied the principles and complied with the provisions of the UK Corporate Governance Code during 2016. Further information on the Code can be found on the Financial Reporting Council's website, www.frc.org.uk.

On behalf of the Board on 8 March 2017

D F S Rogers
Director

Independent Auditors' Report to the members of Friends Life Holdings plc

Independent auditors' report on the Financial Statements

Our opinion

In our opinion, Friends Life Holdings plc's group financial statements and company financial statements (the "financial statements"):

- give a true and fair view of the state of the group's and of the company's affairs as at 31 December 2016 and of the group's and the company's profit and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

What we have audited

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

- the Consolidated and Company Statement of Financial Position as at 31 December 2016;
- the Consolidated and Company Statement of Comprehensive income for the year then ended;
- the Consolidated Statement of Cash Flows for the year then ended;
- the Consolidated and Company Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

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

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

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the group, the company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

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

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

We have no exceptions to report arising from this responsibility.

Directors' remuneration

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

Independent Auditors' Report to the members of Friends Life Holdings plc continued

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors' Responsbilities set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

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

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

What an audit of financial statements involves

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

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

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

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

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.

Marcus Hine (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
8 March 2017

- The maintenance and integrity of the Aviva 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.
- Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Accounting policies

The Company is a public limited company incorporated and domiciled in England and Wales. The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

(A) Basis of preparation

The consolidated financial statements of the Group have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) and IFRS Interpretations Committee (IFRS IC) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU), and those parts of the Companies Act 2006 applicable to those reporting under IFRS. In addition to fulfilling their legal obligation to comply with IFRS as adopted by the EU, the Group has also complied with IFRS as issued by the IASB and applicable at 31 December 2016. The date of transition to IFRS was 1 January 2004.

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of land and buildings, investment property, available-for-sale financial assets, and financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The separate financial statements of the Company are on pages 57 to 70. In 2016, the Company has transitioned from Financial Reporting Standard 101, 'Reduced Disclosure Framework' (FRS 101) to IFRS as set out further on page 62.

The Group and its ultimate parent company, Aviva plc, have considerable financial resources and as a consequence, the directors believe that the Group is well placed to manage its business risks successfully despite the current uncertain macro-economic outlook. After making enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

The Company disposed of 100% of its interest in Friends Life FPG Limited (FPG), Friends Life Investments Limited (FLI) and Friends Life Funds Limited (FLFL), representing the main operating segments of the Company, related service companies and staff pension scheme on 13 April 2015. Following their disposal, the results of FPG and its subsidiary undertakings, FLI and FLFL were classified as results from discontinued operations in the Group's results for the 12 months ended 31 December 2015. The 2015 Consolidated Income Statement was restated to reflect the classification of the disposed businesses as discontinued operations.

The Group's financial statements are stated in sterling, which is the Group's functional and presentation currency. Unless otherwise noted, the amounts shown in these financial statements are in millions of pound sterling (£m).

New standards, interpretations and amendments to published standards that have been adopted by the Group.

The Group has adopted the following amendments to standards which became effective for the annual reporting period beginning on 1 January 2016.

(i) Amendments to IAS 16 and IAS 38 – Clarification of Acceptable Methods of Depreciation and Amortisation

These amendments provide additional guidance on how the depreciation or amortisation of property, plant and equipment and intangible assets should be calculated. The amendments to IAS 16 and IAS 38 prohibit the use of revenue-based depreciation for property, plant and equipment and significantly limit the use of revenue-based amortisation for intangible assets.

The adoption of these amendments has no impact for the Group's consolidated financial statements.

(ii) Amendments to IAS 27, Equity Method in Separate Financial Statements

The amendments to IAS 27 allow investments in subsidiaries to be accounted for using the equity method within the Company's financial statements. The Company has not elected to use the equity method in its separate financial statements.

(iii) Narrow scope amendments to IFRS10, IFRS 12 and IAS 28 – Applying the Consolidation Exception

These narrow scope amendments clarify the application of the requirements for investment entities to measure subsidiaries at fair value instead of consolidating them. There are no implications for the Group's consolidated financial statements as the Group does not meet the definition of an investment entity.

(iv) Amendments to IAS 1 – Disclosure Initiative

These amendments form part of the IASB's Disclosure Initiative and are intended to assist entities in applying judgement in considering presentation and disclosure requirements. The amendments clarify guidance in IAS *1 Presentation of Financial Statements* on materiality and aggregation, the presentation of subtotals, the order of the notes to financial statements and the disclosure of accounting policies. The adoption of these amendments has no impact on the Group's consolidated financial statements.

Accounting policies continued

(A) Basis of preparation continued

(v) Annual Improvements to IFRSs 2012-2014

These improvements consist of amendments to five IFRSs including IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*, IFRS 7 *Financial Instruments: Disclosures* and IAS 19 *Employee Benefits*. The amendments clarify existing guidance and there is no impact on the Group's consolidated financial statements.

Standards, interpretations and amendments to published standards that are not yet effective and have not been adopted early by the Group.

The following new standards, amendments to existing standards and interpretations have been issued, are not yet effective and have not been adopted early by the Group:

(i) Narrow scope amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses

The revisions to IAS 12 *Income Taxes* clarify the accounting for deferred tax assets on unrealised losses and state that deferred tax assets should be recognised when an asset is measured at fair value and that fair value is below the asset's tax base. It also provides further clarification on the estimation of probable future taxable profits that may support the recognition of deferred tax assets. The adoption of this amendment is not expected to have an impact on the consolidated financial statements as the clarifications are consistent with our existing interpretation. The amendment is effective from 1 January 2017 and has not yet been endorsed by EU.

(ii) Amendments to IAS 7 – Disclosure initiative

The amendments to IAS 7, *Statement of Cash Flows*, which form part of the IASB's Disclosure Initiative, require disclosure of the movements in liabilities arising from financing activities with cash and non-cash changes presented separately. The adoption of this amendment is not expected to have an impact on the consolidated financial statements as the Group already voluntarily discloses this information in note 25. The amendment is effective from 1 January 2017 and has not yet been endorsed by EU.

(iii) IFRS 15, Revenue from Contracts with Customers

IFRS 15 will replace IAS 18 *Revenue* and establishes a principle based five-step model to be also applied to all contracts with customers, except for insurance contracts, financial instruments and lease contracts. IFRS 15 also includes enhanced disclosure requirements. The adoption of this new standard will have no impact on the Group's consolidated financial statements. This standard applies to annual reporting periods beginning on or after 1 January 2018 and has not yet been endorsed by the EU.

(iv) Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions

In June 2016, the IASB issued amendments to IFRS 2 *Share-based Payment*. The amendments clarify that the fair value of a cash-settled share-based payment is determined on a basis that is consistent with that used for equity-settled share based payments. The amendments also clarify the classification of share-based payments settled net of withholding tax as well as the accounting consequences resulting from a modification of share-based payments from cash-settled to equity-settled. The adoption of these amendments will have no impact on the Group's consolidated financial statements. The amendments are effective from 1 January 2018 and have not yet been endorsed by the EU.

(v) IFRS 9, Financial Instruments (including amendments to IFRS 4, Insurance Contracts)

In July 2014, the IASB published IFRS 9 *Financial Instruments* which will replace IAS 39 *Financial Instruments: Recognition and Measurement*. The standard incorporates new classification and measurements requirements for financial assets, the introduction of an expected credit loss impairment model which will replace the incurred loss model of IAS 39, and new hedge accounting requirements. Under IFRS 9, all financial assets will be measured at either amortised cost or fair value. The basis of classification will depend on the business model and the contractual cash flow characteristics of the financial assets. The standard retains most of IAS 39's requirements for financial liabilities except for those designated at fair value through profit or loss whereby that part of the fair value changes attributable to own credit is to be recognised in other comprehensive income instead of the income statement. The hedge accounting requirements are more closely aligned with risk management practices and follow a more principle based approach.

In September 2016, the IASB published amendments to IFRS 4 *Insurance Contracts* that address the accounting consequences of the application of IFRS 9 to insurers prior to the publication of the forthcoming accounting standard for insurance contracts. The amendments introduce two options for insurers: the deferral approach and the overlay approach. The deferral approach provides an entity, if eligible, with a temporary exemption from applying IFRS 9 until the earlier of the effective date of a new insurance contract standard or 2021.The overlay approach allows an entity to remove from profit or loss the effects of some of the accounting mismatches that may occur before the new insurance contracts standard is applied.

The adoption of these amendments will have no impact on the Group's consolidated financial statements.

Accounting policies continued

(A) Basis of preparation continued

(vi) IFRS 16 Leases

In January 2016, the IASB published IFRS 16 *Leases* which will replace IAS 17 *Leases*. IFRS 16 introduces a definition of a lease with a single lessee accounting model eliminating the classification of either operating or finance leases. Lessees will be required to account for all leases in a similar manner to the current financial lease accounting recognising lease assets and liabilities on the statement of financial position. Lessor accounting remains similar to current practice. The impact of the adoption of this new standard will have no impact to the Group's consolidated financial statements. This standard applies to annual reporting periods beginning on or after 1 January 2019 and has not yet been endorsed by the EU.

(vii) Annual Improvements to IFRSs 2014-2016

These improvements consist of amendments to three IFRSs including IFRS 1 *First-time Adoption of International Financial Reporting Standards*, IFRS 12 *Disclosure of Interests in Other Entities* and IAS28 *Investments in Associates*.The amendments clarify existing guidance. The adoption of these amendments is not expected to have an impact on the Group's consolidated financial statements. The amendments to IFRS 1 and IAS 28 are effective for annual reporting periods beginning on or after 1 January 2018; the amendment to IFRS 12 for annual reporting periods beginning on or after 1 January 2017. These amendments have not yet been endorsed by the EU.

(viii) Amendments to IAS 40 – Transfers of Investment Property

In December 2016, the IASB published amendments to IAS 40 *Investment Property* to clarify that transfers of property to, or from, investment property should only be made when there is evidence of a change in use of the property. The adoption of these amendments is not expected to have an impact on the Group's consolidated financial statements. The amendments are effective from 1 January 2018 and have not yet been endorsed by the EU.

(ix) IFRIC 22, Foreign Currency Transactions and Advance Consideration

In December 2016, the IASB published IFRIC 22 *Foreign Currency Transactions and Advance Consideration* to clarify the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency. For the purpose of determining the exchange rate, the date of the transaction is the date of initial recognition of the non-monetary prepayment asset or deferred income liability. The adoption of this standard is not expected to have a significant impact on the Group's consolidated financial statements. The standard is effective for annual reporting beginning on or after 1 January 2018 and has not yet been endorsed by the EU.

Segmental Information

The Company's interests in FPG, FLI and FLFL were disposed of in their entirety on 13 April 2015. These businesses represented all the main operating segments of the Group. As a result of this disposal, the Group no longer has any components that meet the definition of an operating segment and therefore no segmental information is provided.

(B) Critical accounting policies and the use of estimates

The preparation of financial statements requires the Group to select accounting policies and make estimates and assumptions that affect items reported in the Consolidated Income Statement, Consolidated Statement of Financial Position, other primary statements and notes to the financial statements.

All estimates are based on management's knowledge of current facts and circumstances, assumptions based on that knowledge and their predictions of future events and actions. Actual results can always differ from those estimates, possibly significantly.

The table below sets out those items we consider particularly susceptible to changes in estimates and assumptions, and the relevant accounting policy.

Item	Accounting policy
Consolidation principles	C
Fair value of financial investments	J & K
Impairment of financial investments	K
Income taxes	H
Provisions and contingent liabilities	CC
Fair value of derivative financial instruments	R

Accounting policies continued

(C) Consolidation principles

Subsidiaries
Subsidiaries are those entities over which the Group has control. The Group controls an investee if and only if the Group has all of the following:
- power over the investee,
- exposure, or rights, to variable returns from its involvement with the investee, and
- the ability to use its power over the investee to affect its returns.

The Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including: the purpose and design of an investee, relevant activities, substantive and protective rights, and voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Subsidiaries are consolidated from the date the Group obtains control and are excluded from consolidation from the date the Group loses control. All intercompany transactions, balances and unrealised surpluses and deficits on transactions between Group companies have been eliminated.

Associates and joint ventures
Associates are entities over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control. Generally, it is presumed that the Group has significant influence if it has between 20% and 50% of voting rights. Joint ventures are joint arrangements whereby the Group and other parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control. In a number of these, the Group's share of the underlying assets and liabilities may be greater or less than 50% but the terms of the relevant agreements make it clear that control is not exercised. Such jointly controlled entities are referred to as joint ventures in these financial statements.

Gains on transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's interest in the associates and joint ventures. Losses are also eliminated, unless the transaction provides evidence of an impairment of the asset transferred between entities.

(D) Net investment income

Investment income consists of dividends, interest receivable for the year, realised gains and losses, and unrealised gains and losses on fair value investments (as defined in policy K). Dividends on equity securities are recorded as revenue on the ex-dividend date. Dividends from investments in subsidiaries are recorded as revenue on the date dividends are declared. Interest income is recognised as it accrues, taking into account the effective yield on the investment and includes the amortisation of any discount or premium.

Rental income from investment properties under operating leases is recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease income.

A gain or loss on a financial investment is only realised on disposal or transfer, and is the difference between the proceeds received, net of transaction costs, and its original cost or amortised cost, as appropriate. Unrealised gains and losses, arising on investments which have not been derecognised as a result of disposal or transfer, represent the difference between the carrying value at the year end and the carrying value at the previous year end or purchase value during the year, less the reversal of previously recognised unrealised gains and losses in respect of disposals made during the year.

(E) Administrative and other expenses

Ongoing administrative and other expenses are recognised as incurred.

(F) Finance costs

All borrowing costs are expensed as they are incurred and are calculated using the effective interest rate method.

Accounting policies continued

(G) Foreign currency transactions

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions, and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in the Income Statement. Translation differences on debt securities and other monetary financial assets measured at fair value and designated as held at fair value through profit or loss (FVTPL) (see accounting policy K) are included in foreign exchange gains and losses in the Income Statement.

For monetary financial assets designated as Available for Sale (AFS), translation differences are calculated as if they were carried at amortised cost and so are recognised in the Income Statement, whilst foreign exchange differences arising from fair value gains and losses are recognised in other comprehensive income and included in the investment valuation reserve within equity.

Translation differences on non-monetary items, such as equities which are designated as FVTPL, are reported as part of the fair value gain or loss, whereas such differences on AFS equities are included in the investment valuation reserve.

(H) Income taxes

The current tax expense is based on the taxable profits for the year, after any adjustments in respect of prior years. Tax, including tax relief for losses if applicable, is allocated over profits before taxation and amounts charged or credited to components of other comprehensive income and equity, as appropriate.

A provision is made for deferred tax liabilities, or credit taken for deferred tax assets, using the liability method, on all material temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. The rates enacted or substantively enacted at the Statement of Financial Position date are used to determine the deferred tax assets or liabilities.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Where there is a history of tax losses, deferred tax assets are only recognised in excess of deferred tax liabilities if there is convincing evidence that future profits will be available.

Deferred tax is provided on temporary differences arising from investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future. Deferred tax is not provided on revaluations of investments in subsidiaries as under current tax legislation no tax is expected to arise on their disposal.

Current and deferred tax relating to items recognised in other comprehensive income and directly in equity are similarly recognised in other comprehensive income and directly in equity respectively. Deferred tax related to fair value re-measurement of available for sale investments and other amounts charged or credited directly to other comprehensive income is recognised in the Statement of Financial Position as a deferred tax asset or liability.

(I) Dividends

Interim dividends on ordinary shares are recognised in equity in the period in which they are paid. Final dividends on these shares are recognised when they have been approved by shareholders.

(J) Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. This presumes that the transaction takes place in the principal (or most advantageous) market under current market conditions. Fair value is a market-based measure and in the absence of observable market prices in an active market, it is measured using the assumptions that market participants would use when pricing the asset or liability.

The fair value of a non-financial asset is determined based on its highest and best use from a market participant's perspective. When using this approach, the Group takes into account the asset's use that is physically possible, legally permissible and financially feasible.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price i.e. the fair value of the consideration given or received. In certain circumstances, the fair value at initial recognition may differ from the transaction price. If the fair value is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging), or is based on a valuation technique whose variables include only data from observable markets, then the difference between the fair value at initial recognition and the transaction price is recognised as a gain or loss in the Income Statement. When unobservable market data has a significant impact on the valuation of financial instruments, the difference between the fair value at initial recognition and the transaction price is not recognised immediately in the Income Statement, but deferred and recognised in the Income Statement on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out or otherwise matured.

If an asset or a liability measured at fair value has a bid price and an ask price, the price within the bid-ask spread that is most representative of fair value in the circumstances is used to measure fair value.

Accounting policies continued

(K) Financial investments

The Group classifies its investments as either financial assets at fair value through profit or loss (FVTPL), financial assets available for sale (AFS) or as loans at amortised cost.

The classification depends on the purpose for which the investments were acquired, and is determined by local management at initial recognition. The FVTPL category has two subcategories – those that meet the definition as being held for trading and those the Group chooses to designate as FVTPL (referred to in this accounting policy as 'other than trading') upon initial recognition.

In general, the other than trading category is used as, in most cases, the Group's investment or risk management strategy is to manage its financial investments on a fair value basis. Debt securities and equity securities, which the Group buys with the intention to resell in the short term, are classified as trading, as are non-hedge derivatives (see accounting policy R below). The AFS category is used where the relevant long-term business liability (including shareholders' funds) is passively managed, as well as in certain fund management and non-insurance operations.

Purchases and sales of investments are recognised on the trade date, which is the date that the Group commits to purchase or sell the assets, at their fair values. Debt securities are initially recorded at their fair value, which is taken to be amortised cost, with amortisation credited or charged to the Income Statement. Investments classified as trading, other than trading and AFS are subsequently carried at fair value. Changes in the fair value of trading and other than trading investments are included in the Income Statement in the period in which they arise. Changes in the fair value of securities classified as AFS are recognised in other comprehensive income and recorded in a separate investment valuation reserve within equity.

Investments carried at fair value are measured using the methodology outlined in note 14, with values based on the quoted price within the bid-ask spread that is most representative of fair value or based on cash flow models using market observable inputs or unobservable inputs. When securities classified as AFS are sold or impaired, the accumulated fair value adjustments are transferred out of the investment valuation reserve to the Income Statement with a corresponding movement through other comprehensive income.

Loans are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans are measured on initial recognition at the fair value of the consideration given plus incremental costs that are incurred on the acquisition of the investment. Subsequent to initial recognition, loans are either measured at amortised cost less impairment losses or, if they meet the criteria for designation at fair value through profit or loss (such as the elimination of, or significant reduction in, accounting mismatches) and are so designated on initial recognition, they are measured at fair value.

The amortised cost is the present value of estimated future cash flows discounted at the effective interest rate at the date of acquisition or origination of the loan. Subsequent to initial recognition, any difference between cost and redemption value is amortised through the income statement over the life of the instrument. The carrying values of loans at amortised cost are reviewed for impairment in accordance with IAS 39 at each reporting date. If there is objective evidence of impairment, for example there is a default or delinquency in payment, the impairment loss is calculated and recognised.

The Group reviews the carrying value of its AFS investments on a regular basis. If the carrying value of an AFS investment is greater than the recoverable amount, the carrying value is reduced through a charge to the income statement in the period of impairment. The following policies are used to determine the level of any impairment, some of which involve considerable judgement:

An AFS equity security is considered impaired if there is objective evidence that the cost may not be recovered. In addition to qualitative impairment criteria, such evidence includes a significant or prolonged decline in fair value below cost. Unless there is evidence to the contrary, an equity security is considered impaired if the decline in fair value relative to cost has been either at least 20% for a continuous six-month period or more than 40% at the end of the reporting period, or been in an unrealised loss position for a continuous period of more than 12 months at the end of the reporting period. We also review our largest equity holdings for evidence of impairment, as well as individual equity holdings in industry sectors known to be in difficulty. Where there is objective evidence that impairment exists, the security is written down regardless of the size of the unrealised loss.

For securities identified as being impaired, the cumulative unrealised loss previously recognised within the investment valuation reserve is transferred to realised losses for the year with a corresponding movement through other comprehensive income. Any subsequent increase in fair value of these impaired securities is recognised in other comprehensive income and recorded in the investment valuation reserve. Reversals of impairments on any of these assets are only recognised where the decrease in the impairment can be objectively related to an event occurring after the write-down (such as an improvement in the debtor's credit rating), and are not recognised in respect of equity instruments.

Accounting policies continued

(L) Receivables and other financial assets

Receivables and other financial assets are recognised when due and measured on initial recognition at the fair value of the amount receivable plus incremental costs. Subsequent to initial recognition, these receivables are measured at amortised cost using the effective interest rate method.

(M) Statement of Cash Flows

Cash and cash equivalents

Cash and cash equivalents consist of cash at banks and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are those with less than three months' maturity from the date of acquisition, or which are redeemable on demand with only an insignificant change in their fair values.

For the purposes of the Statement of Cash Flows, cash and cash equivalents also include bank overdrafts, which are included in payables and other financial liabilities on the Statement of Financial Position.

(N) Share capital

Equity instruments

An equity instrument is a contract that evidences a residual interest in the assets of an entity after deducting all its liabilities. Accordingly, 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 terms that may be unfavourable; and
- the instrument is a non-derivative that contains no contractual obligation to deliver a variable number of shares, or is a derivative that will be settled only by the Group exchanging a fixed amount of cash or other assets for a fixed number of the Group's own equity instruments.

(O) Borrowings

The Group classifies its loans and borrowings as financial liabilities carried at amortised cost. Borrowings are recognised initially at fair value, which is generally the cash consideration received, net of transaction costs incurred, and subsequently measured at amortised cost. The amortised cost of a financial liability is the amount at which the financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest rate method of any difference between that initial amount and the maturity amount.

Any difference between the proceeds, net of transaction costs, and the redemption value is recognised in the income statement over the period of the borrowings, using the effective interest rate method. Interest accrued on loans and borrowings is recognised under insurance payables, other payables and deferred income and not included in the carrying value of interest-bearing loans and borrowings.

(P) Payables and other financial liabilities

Payables and other financial assets are recognised when due and are measured on initial recognition at the fair value of the consideration payable. Subsequent to initial recognition, derivative contract liabilities are carried at fair value and other payables are measured at amortised cost using the effective interest rate method.

Front-end fees charged at the inception of certain investment contracts are recognised as income over the expected term of the contract on a straight-line basis with the unrecognised amount at the end of the year presented as a liability.

(Q) Derecognition and offset of financial assets and financial liabilities

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- The rights to receive cash flows from the asset have expired;
- The Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- The Group has transferred its rights to receive cash flows from the asset and either transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Financial assets and liabilities are offset and the net amount reported in the Statement of Financial Position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Accounting policies continued

(R) Derivative financial instruments and hedging

Derivative financial instruments include foreign exchange contracts and currency swaps that derive their value mainly from underlying foreign exchange rates.

All derivatives are initially recognised in the Statement of Financial Position at their fair value, which usually represents their cost. They are subsequently remeasured at their fair value, with the method of recognising movements in this value depending on whether they are designated as hedging instruments and, if so, the nature of the item being hedged. Fair values are obtained from quoted market prices or, if these are not available, by using valuation techniques such as discounted cash flow models or option pricing models. All derivatives are carried as assets when the fair values are positive and as liabilities when the fair values are negative. Premiums paid for derivatives are recorded as an asset on the Statement of Financial Position at the date of purchase, representing their fair value at that date.

Derivative contracts may be traded on an exchange or over-the-counter (OTC). Exchange-traded derivatives are standardised and include certain futures and option contracts. OTC derivative contracts are individually negotiated between contracting parties and include forwards, swaps, caps and floors. Derivatives are subject to various risks including market, liquidity and credit risk, similar to those related to the underlying financial instruments. Many OTC transactions are contracted and documented under International Swaps and Derivatives Association (ISDA) master agreements or their equivalent, which are designed to provide legally enforceable set-off in the event of default, reducing the Group's exposure to credit risk.

The notional or contractual amounts associated with derivative financial instruments are not recorded as assets or liabilities on the Statement of Financial Position as they do not represent the fair value of these transactions.

The Group has collateral agreements in place with relevant counterparties. Accounting policy S below covers collateral, both received and pledged, in respect of these derivatives.

Currency swaps

Currency swaps, in their simplest form, are contractual agreements that involve the exchange of both periodic and final amounts in two different currencies. These contracts may include the net exchange of principal. Exposure to gain or loss on these contracts will increase or decrease over their respective lives as a function of maturity dates, foreign exchange rates, and the timing of payments.

Foreign exchange contracts

Foreign exchange contracts, which include spot and forward contracts, represent agreements to exchange the currency of one country for the currency of another country at an agreed price and settlement date. Foreign exchange option contracts are similar to interest rate option contracts, except that they are based on currencies, rather than interest rates. Exposure to gain or loss on these contracts will increase or decrease over their respective lives as currency exchange and interest rates fluctuate.

Derivative instruments for hedging

On the date a derivative contract is entered into, the Group designates certain derivatives as either:

(i) a hedge of the fair value of a recognised asset or liability (fair value hedge);
(ii) a hedge of a future cash flow attributable to a recognised asset or liability, a highly probable forecast transaction or a firm commitment (cash flow hedge); or
(iii) a hedge of a net investment in a foreign operation (net investment hedge).

Hedge accounting is used for derivatives designated in this way, provided certain criteria are met. At the inception of the transaction, the Group documents the relationship between the hedging instrument and the hedged item, as well as the risk management objective and the strategy for undertaking the hedge transaction. The Group also documents its assessment of whether the hedge is expected to be, and has been, highly effective in offsetting the risk in the hedged item, both at inception and on an ongoing basis.

Changes in the fair value of derivatives that are designated and qualify as net investment or cash flow hedges, and that prove to be highly effective in relation to the hedged risk, are recognised in other comprehensive income and a separate reserve within equity. Gains and losses accumulated in this reserve are included in the income statement on disposal of the relevant investment or occurrence of the cash flow as appropriate.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recognised in the Income Statement. The gain or loss on the hedged item that is attributable to the hedged risk is recognised in the Income Statement. This applies even if the hedged item is an available for sale financial asset or is measured at amortised cost. If a hedging relationship no longer meets the criteria for hedge accounting, the cumulative adjustment made to the carrying amount of the hedged item is amortised to the Income Statement, based on a recalculated effective interest rate over the residual period to maturity. In cases where the hedged item has been derecognised, the cumulative adjustment is released to the Income Statement immediately.

For a variety of reasons, certain derivative transactions, while providing effective economic hedges under the Group's risk management positions, do not qualify for hedge accounting under the specific IFRS rules and are therefore treated as derivatives held for trading. Their fair value gains and losses are recognised immediately in net investment income.

Accounting policies continued

(S) Collateral

The Group receives and pledges collateral in the form of cash or non-cash assets in respect of stock lending transactions, certain derivative contracts, in order to reduce the credit risk of these transactions. Collateral is also pledged as security for bank letters of credit. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty.

Collateral received in the form of cash, which is not legally segregated from the Group, is recognised as an asset in the Statement of Financial Position with a corresponding liability for the repayment in financial liabilities. However, where the Group has a currently enforceable legal right of set-off, the collateral liability and associated derivative balances are shown net, in line with market practice. Non-cash collateral received is not recognised in the Statement of Financial Position unless the Group either (a) sells or repledges these assets in the absence of default, at which point the obligation to return this collateral is recognised as a liability; or (b) the counterparty to the arrangement defaults, at which point the collateral is seized and recognised as an asset.

Collateral pledged in the form of cash, which is legally segregated from the Group, is derecognised from the Statement of Financial Position with a corresponding receivable recognised for its return. Non-cash collateral pledged is not derecognised from the Statement of Financial Position unless the Group defaults on its obligations under the relevant agreement, and therefore continues to be recognised in the Statement of Financial Position within the appropriate asset classification.

(T) Goodwill, AVIF and intangible assets

Goodwill
Goodwill arising on business combinations is the future economic benefit arising from assets that are not capable of being individually identified and separately recognised. After initial recognition, goodwill is stated at cost less any accumulated impairment losses, with the carrying value being reviewed for impairment at least annually and whenever events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill is allocated to the related cash generating units (CGUs). Where the recoverable amount of the CGU is less than its carrying amount, including the related goodwill, an impairment loss is recognised in the income statement.

In a business combination, where the purchase consideration is lower than the fair value of the net assets acquired, a gain on acquisition arises, sometimes referred to as negative goodwill. Such a gain on acquisition is recognised in the income statement in the period in which it arises.

AVIF
On acquisition of a portfolio of insurance contracts and/or investment contracts, either directly or through the acquisition of a subsidiary undertaking, the net present value of the Group’s interest in the expected pre-tax cash flows of the in-force business is capitalised in the statement of financial position, using a MCEV methodology.

AVIF is amortised over the anticipated lives of the related contracts which typically vary between five years and 35 years, with the amortisation profile being in accordance with expected profit emergence from the contracts. Any changes in estimated useful lives are accounted for prospectively with the effect of the change being recognised in the current and future periods, if relevant.

Other intangible assets
Customer relationships, distribution relationships and brands acquired are capitalised at cost, being the fair value of the consideration paid. Software is capitalised on the basis of the costs incurred to acquire and bring it into use.

These intangible assets have finite useful lives and are consequently carried at cost less accumulated amortisation and impairment. Any changes in estimated useful lives are accounted for prospectively with the effect of the change being recognised in the current and future periods, if relevant. Amortisation is calculated using the straight-line method to allocate the cost over the estimated useful lives of the intangible assets with ranges as shown below:

	Years
Customer relationships	8 – 12
Distribution relationships	5 – 10
Brands	10 – 15
Computer software	3 – 4

Intangible assets relating to customer relationships and distribution channels have been valued using an income approach method, specifically the Multi-period Excess Earnings Method (“MEEM”). The principle behind the MEEM is that the value of an intangible asset is equal to the present value of the after tax cash flows attributable only to that intangible asset. Other intangibles include in-house developed IT systems and databases which have been valued using a replacement cost approach which assesses the cost of reproducing the equivalent technology in its current form.

Subsequent expenditure on other intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Accounting policies continued

(T) Goodwill, AVIF and intangible assets continued

Impairment testing
All identifiable intangible assets are reviewed at each reporting date, or where impairment indicators are present, to assess whether there are any circumstances that might indicate that they are impaired. If such circumstances exist, impairment testing is performed and any resulting impairment losses are charged to the consolidated income statement.

For the purpose of impairment testing, goodwill and AVIF are allocated to the CGU, which represents the lowest level within the Group at which the intangible assets are monitored for internal management purposes.

AVIF is tested for impairment by comparing the carrying amount with its recoverable amount. The calculation of the recoverable amount is consistent with the measurement methodology for AVIF at initial recognition and is based on the current MCEV VIF balance for pre-acquisition business only, adjusted for differences between the IFRS and MCEV measurement basis for other net assets.

(U) Property, plant & equipment

Owned assets
Land and buildings are initially recognised at cost and subsequently measured at fair value. Revaluations are performed annually by independent valuers, who hold a recognised and relevant professional qualification and have recent experience in the location and category of properties being valued. Valuations are performed with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the balance sheet date. The fair value is the amount for which a property could be exchanged between knowledgeable and willing parties in an arm’s length transaction.

Properties occupied by the Group are held at fair value, based on highest and best use, measured at the date of revaluation. Revaluation surpluses, and their reversal, are recognised in the statement of other comprehensive income. Revaluation losses, and their reversal, are recognised in the income statement.

Equipment is recognised at cost less accumulated depreciation and impairment losses.

Depreciation
Depreciation is charged so as to write off the cost of certain assets net of the estimated residual value, using the straight-line method, over the estimated useful life of the asset, as follows:

	Years
Computer hardware and related software	1 – 4
Fixtures, fittings and office equipment	3 – 10

Residual values and useful lives are reviewed at each financial year end and adjusted if appropriate. Any changes in estimated useful lives are accounted for prospectively with the effect of the change being recognised in the current and future periods, if relevant.

Disposal and derecognition
An item of property and equipment is derecognised upon disposal or when no further future economic benefits are expected from its use. Any gain or loss arising on derecognition of the asset is included in the income statement in the year the asset is derecognised.

Any revaluation reserve relating to the particular asset being disposed of or no longer in use is transferred to retained earnings.

(V) Investment properties

Investment properties comprise land and/or buildings that are not occupied by the Group and are held either to earn rental income or for capital appreciation, or for both.

Investment properties are initially included in the balance sheet at cost and subsequently measured at fair value, at least annually at the reporting date. Fair values, based on highest and best use, are measured by external independent valuers, who hold a recognised and relevant professional qualification and have recent experience in the location and category of the investment property being valued.

Movements in the fair value of investment properties are taken to the income statement in the period in which they arise.

In accordance with IAS 17: *Leases* properties held by the Group under operating leases are classified as investment properties when the properties otherwise meet the definition of investment properties.

Accounting policies continued

(W) Deferred acquisition costs

Insurance and investment contracts with Discretionary Participating Features (DPF)
Acquisition costs comprise all direct and indirect costs arising from writing the contracts, which are incurred during a financial period. Acquisition costs are deferred and amortised over the life of the contracts where their recovery has not been reflected in the valuation of policyholder liabilities but only to the extent that they are recoverable from future margins. The rate of amortisation of acquisition costs on such contracts is proportional to the future margins expected to emerge in respect of the related policies, over the life of those policies.

Investment contracts without DPF
Acquisition costs comprise all incremental costs that are directly related to the writing of the contract, which are incurred during a financial period, and are amortised on a straight-line basis over the lifetime of the contract if they are recoverable out of future margins.

(X) Reinsurance assets

The benefits to which the Group is entitled under its reinsurance contracts are recognised as reinsurance assets. Amounts recoverable from reinsurers are measured consistently with the amounts associated with the underlying insurance contracts that are being reinsured and in accordance with the terms of each reinsurance contract.

Contracts that do not give rise to a significant transfer of insurance risk to the reinsurer are considered financial reinsurance and are accounted for and disclosed in a manner consistent with financial instruments (see note 16 for further details).

(Y) Insurance contracts

Contracts under which the Group accepts significant insurance risk from another party (the policyholder), by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder, are classified as insurance contracts. Under IFRS 4: *Insurance contracts* insurance risk is risk other than financial risk. Financial risk is the risk of a possible future change in one or more of: a specified interest rate, security price, commodity price, foreign exchange rate, index of price or rates, a credit rating or credit index or other variable. Insurance contracts may also transfer some financial risk.

Once a policyholder contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period. As a general guideline, the Group defines as significant insurance risk the possibility of having to pay benefits on the occurrence of an insured event that are more than 5% greater than the benefits payable if the insured event did not occur.

For operations conducted in the UK, insurance contract liabilities are calculated based on the relevant PRA rules contained in the Prudential Sourcebook for Insurers. For overseas operations, insurance contract liabilities are calculated on recognised actuarial principles, based on local regulatory requirements.

For conventional with-profits policies, the liabilities to policyholders include both declared and constructive obligations for future bonuses not yet declared (excluding the shareholders' share of future bonuses) and include the cost of options and guarantees measured on a market consistent basis. The basis of calculation does not recognise deferred acquisition costs, but allows for future profits of non-profit and unit-linked business written in the with-profits fund to be recognised.

The calculation of liabilities to policyholders for non-profit contracts includes explicit allowance for future expenses and allows for lapses where appropriate.

The value of unit-linked insurance contract liabilities includes provision for tax losses in the unit-linked funds whose benefit will ultimately accrue to policyholders.

The Group applies shadow accounting in relation to certain insurance contract liabilities, which are supported by owner-occupied properties and overseas subsidiaries, on which unrealised gains and losses are recognised in the statement of other comprehensive income. Adjustments are made to the insurance contract provisions to reflect the movements that would have arisen if the unrealised gains and losses had been recognised in the income statement. The corresponding change in the value of these insurance contract liabilities is recognised in the consolidated statement of comprehensive income.

The Group carries out an annual liability adequacy test on its insurance contract liabilities less related deferred acquisition costs and other related intangible assets to ensure that the carrying amount of its liabilities is sufficient in light of estimated future cash flows. Where a shortfall is identified, an additional provision is made.

Accounting policies continued

(Z) Unallocated surplus

The unallocated surplus in the with-profits funds is presented as a liability and comprises all amounts available for allocation, either to policyholders or to shareholders, the allocation of which has not been determined at the balance sheet date.

Insurance and investment contract liabilities within with-profits funds are measured on a realistic basis and therefore include amounts attributable in respect of future bonuses. Such amounts are estimated in accordance with the published Principles and Practices of Financial Management (PPFM) and represent a constructive obligation. The realistic liabilities include an estimate of the fair value of policyholder options and guarantees. The unallocated surplus within the with-profits funds represents the excess of assets of the fund relative to the realistic liabilities and other current liabilities not included within the realistic liability measurement. The unallocated surplus can be considered to represent the working capital of the funds and includes a part which represents the value of future transfers to shareholders from the with-profits funds.

(AA) Investment contracts

Policyholder contracts not considered insurance contracts under IFRS 4 are classified as investment contracts. Contracts classified as investment contracts are either unit-linked or contracts with Discretionary Participating Features (DPF) with no significant insurance risk. The latter are mainly unitised with-profits contracts.
An investment contract is a financial liability designated on initial recognition at fair value through profit or loss, when one of the following criteria is satisfied:

- it eliminates or significantly reduces an accounting mismatch with corresponding assets which are managed on a fair value basis.
- it contains or may contain an embedded derivative.

A unit-linked contract is recognised at fair value through profit or loss and is calculated as the number of units allocated to policyholders in each of the unit-linked funds multiplied by the bid price of the units which reflects the fair value of the assets in the fund at the balance sheet date. In addition, the fair value of the investment contract liability includes provision for tax losses in the unit-linked funds whose benefit will ultimately accrue to the policyholders and provision for renewal commissions where intermediaries are not required to perform any service once the policy is incepted. Non-unit reserves, relating primarily to deferral of front end fees in the form of unfunded units, are also included as an investment contract liability and recognised as income on a straight-line basis over the period in which services are rendered.

Investment contracts with DPF held within the with-profits funds (which are mainly unitised with-profits contracts) are measured on a basis that is consistent with a measurement basis for insurance contracts held within these funds.

(BB) Net asset value attributable to unit-holders

OEICs and unit trusts where the Group has a controlling interest and the units are not owned by the Group are treated as a liability, as there is a contractual obligation to deliver cash, and are presented as “net asset value attributable to unit-holders”.

(CC) Provisions and contingent liabilities

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. The amount recorded as a provision is the best estimate of the expenditure required to settle the present obligation at the balance sheet date. Where the effect of the time value of money is material, the provision is the present value of the expected expenditure. Provisions are not recognised for future operating losses.

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.

Contingent liabilities are disclosed if there is a possible future obligation as a result of a past event, or if there is a present obligation as a result of a past event but either a payment is not probable or the amount cannot be reliably estimated.

Accounting policies continued

(DD) Share based payments

The Group offers share-based payment plans to certain key employees. The expense charged to the income statement is based on the fair value of the options granted, the vesting period and the vesting conditions. Fair values are determined using stochastic and scenario-based modelling techniques where appropriate.

For equity-settled schemes, the fair value is determined at grant date and expensed on a straight-line basis over the vesting period in the income statement. A corresponding amount is credited to equity. At each reporting date the Group revises its estimates of the number of shares that are expected to be issued for the achievement of non-market related performance conditions: the impact of any revisions are recognised in the income statement, with a corresponding adjustment to equity over the remaining vesting period. Where a leaver is entitled to their scheme benefits, this is treated as an acceleration of vesting and hence a shortening of the period over which the expense is charged.

For cash-settled schemes, the fair value is expensed on a straight-line basis over the vesting period in the income statement and the cumulative provision for obligations under cash-settled schemes is recognised as a liability in the statement of financial position. The fair value is remeasured at each reporting date, with any changes in fair value recognised in the income statement for the period.

Consolidated Income Statement
For the year ended 31 December 2016

	Note	**2016 £m**	2015 £m
Income			
Net investment income	D & 4	**171**	145
		171	145
Expenses			
Other expenses	E & 5	**(5)**	(20)
Finance costs	F & 7	**(175)**	(110)
		(180)	(130)
(Loss)/profit for the year before tax from continuing operations		**(9)**	15
Tax charge from continuing operations	H & 8	**(3)**	(1)
(Loss)/profit for the year after tax from continuing operations		**(12)**	14
Profit for the year after tax from discontinued operations		**-**	4
(Loss)/profit for the year		**(12)**	18
Attributable to:			
Equity holders of Friends Life Holdings plc			
– from continued operations		**(12)**	(6)
– from discontinued operations		**-**	4
Non controlling interests		**-**	20
(Loss)/profit for the year		**(12)**	18

For 2015 the Consolidated Income Statement includes the results of business classified as discontinued operations. A single amount is shown on the face of the Income Statement representing the operation's post-tax result.

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 28 to 70 are an integral part of these financial statements.

Consolidated Statement of Comprehensive Income
For the year ended 31 December 2016

	2016 £m	2015 £m
(Loss)/profit for the year from continuing operations	**(12)**	14
Profit for the year from discontinued operations	**-**	4
Total (loss)/profit for the year	**(12)**	18
Items that may be reclassified subsequently to income statement		
Investment classified as available for sale		
Fair value gains/(losses)	**3**	(35)
Aggregate tax effect	**(1)**	6
Other comprehensive income/(loss), net of tax from continuing operations	**2**	(29)
Other comprehensive loss, net of tax from discontinued operations	**-**	(17)
Total other comprehensive income/(loss) for the year	**2**	(46)
Total comprehensive loss, net of tax from continuing operations	**(10)**	(15)
Total comprehensive loss, net of tax from discontinued operations	**-**	(13)
Total comprehensive loss for the year	**(10)**	(28)
Attributable to:		
Equity holders of Friends Life Holdings plc		
- from continued operations	**(10)**	(35)
- from discontinued operations	**-**	(13)
Non controlling interests	**-**	20
Total comprehensive loss for the year	**(10)**	(28)

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 28 to 70 are an integral part of these financial statements.

Consolidated Statement of Changes in Equity
For the year ended 31 December 2016

		Equity attributable to shareholders of Friends Life Holdings plc						
	Note	Ordinary share capital £m	Other reserves £m	Retained earnings £m	Total £m	STICS £m	Non controlling interests £m	Total equity £m
Balance at 1 January 2016		**515**	**(35)**	**81**	**561**	**-**	**-**	**561**
Loss for the year		**-**	**-**	**(12)**	**(12)**	**-**	**-**	**(12)**
Other comprehensive income		**-**	**3**	**(1)**	**2**	**-**	**-**	**2**
Total comprehensive loss		**-**	**3**	**(13)**	**(10)**	**-**	**-**	**(10)**
Dividends and appropriations	I & 9	**-**	**-**	**(210)**	**(210)**	**-**	**-**	**(210)**
Transfer between capital and reserves	20 & 22	**(250)**	**-**	**250**	**-**	**-**	**-**	**-**
Balance at 31 December 2016		**265**	**(32)**	**108**	**341**	**-**	**-**	**341**

		Equity attributable to shareholders of Friends Life Holdings plc						
	Note	Ordinary share capital £m	Other reserves £m	Retained earnings £m	Total £m	STICS £m	Non controlling interests £m	Total equity £m
Balance at 1 January 2015		515	414	3,446	4,375	318	1	4,693
(Loss)/profit for the year		-	-	(2)	(2)	20	-	18
Other comprehensive loss		-	(35)	(11)	(46)	-	-	(46)
Total comprehensive loss		-	(35)	(13)	(48)	20	-	(28)
Dividends and appropriations	I & 9	-	(435)	(4,423)	(4,858)	(7)	-	(4,865)
Capital contribution	1	-	21	1,208	1,229	-	-	1,229
Reclassification of STICS as a financial liability	31	-	-	(93)	(93)	(192)	-	(285)
Transfer of 2003 STICS to Aviva plc	31	-	-	(85)	(85)	(139)	-	(224)
Share-based payments, net of settlements	33	-	-	(3)	(3)	-	-	(3)
Funding of Employee Benefit Trust	33	-	-	8	8	-	-	8
Aggregate tax effect				36	36	-	-	36
Attributable to non-controlling interests		-	-	-	-	-	(1)	-
Balance at 31 December 2015		515	(35)	81	561	-	-	561

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 28 to 70 are an integral part of these financial statements.

Consolidated Statement of Financial Position
As at 31 December 2016

	Note	2016 £m	2015 £m
Assets			
Non current assets			
Financial investments	K & 13	**1,459**	1,538
Tax assets	H & 17	**-**	14
Deferred tax assets	H & 17	**8**	9
Current assets			
Financial investments	K & 13	**-**	1
Receivables and other financial assets	L & 18	**44**	65
Cash and cash equivalents	M & 19	**143**	95
Total assets		**1,654**	1,722
Equity			
Ordinary share capital	N & 20	**265**	515
Other reserves	21	**(32)**	(35)
Retained earnings	22	**108**	81
Total equity		**341**	561
Liabilities			
Non current liabilities			
Borrowings	O & 25	**1,132**	1,052
Tax liabilities	H & 17	**4**	-
Current liabilities			
Borrowings	O & 25	**2**	2
Payables and other financial liabilities	P & 29	**129**	62
Other liabilities	Q & 30	**46**	45
Total liabilities		**1,313**	1,161
Total equity and liabilites		**1,654**	1,722

The financial statements on pages 23 to 56 were approved by the Board of Directors on 8 March 2017 and signed on its behalf by

T Stoddard
Director

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 28 to 70 are an integral part of these financial statements.

Consolidated Statement of Cash Flows
For the year ended 31 December 2016

	Note	2016 £m	2015 £m
Cash flows from investing activities			
Interest received		**89**	77
Collateral received		**86**	34
Net disposal of financial investments		**176**	23
Disposal of held for sale assets, net of cash transferred		**-**	(6,954)
Net cash from/(used in) investing activities		**351**	(6,820)
Cash flows from financing activities			
Repayment of loan to parent		**-**	145
Repayment of the 2005 STICS		**-**	(285)
Net funding of Employee Benefit Trust		**-**	8
Finance costs		**(95)**	(88)
STICS interest		**-**	(7)
Net movement in other borrowings, net of expenses		**-**	(13)
Ordinary dividends paid		**(210)**	(376)
Amounts repaid to fellow Group companies		**(18)**	-
Amounts repaid from fellow Group companies		**21**	25
Net cash used in financing activities		**(302)**	(591)
Total net increase/(decrease) in cash and cash equivalents		**49**	(7,411)
Cash and cash equivalents at 1 January		**95**	7,503
Effect of exchange rate changes on cash and cash equivalents		**(10)**	3
Cash and cash equivalents at 31 December	M & 19	**134**	95

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 28 to 70 are an integral part of these financial statements.

Notes to the Consolidated Financial Statements

1. Business disposals

(a) Disposal of discontinued operations

On 13 April 2015 the former Friends Life Group (FL Group) companies were restructured within the Aviva Group. As part of this restructuring the Company disposed of its interests in Friends Life FPG Limited (FPG), Friends Life Investments Limited (FLI) and Friends Life Funds Limited (FLFL). The Company's shareholdings in FLI and FLFL, plus 68% of the Company's interest in FPG were transferred to the Group's then parent undertaking, Friends Life Group Holdings Limited (FLGH), by way of a dividend in specie of £3,297 million. The Company's remaining 32% shareholding in FPG was transferred to Aviva Group Holdings Limited (AGH) in exchange for consideration of £1,544 million in the form of a loan payable by AGH. The loan was fully settled as at 31 December 2015.

The Company retained its interest in £500 million of internal STICS with Friends Life Limited (FLL), an insurance undertaking of the disposal Group (see note 13 for details).

The profit on the restructure was recognised as a capital contribution:

	13 April 2015 £m
Disposal group equity attributable to shareholders of Friends Life Holdings plc	(3,612)
Dividend in specie	3,297
Residual equity attributable to shareholders of Friends Life Holdings plc	(315)
Loan consideration	1,544
Capital contribution	1,229

The results of FPG, FLI and FLFL and their subsidiary undertakings were classified as results from discontinued operations in the Group's results for 2015.

Notes to the Consolidated Financial Statements continued

1. Business disposals continued

(b) Results of discontinued operations

	Period to 13 April 2015 £m
Revenue	
Gross earned premiums	380
Premiums ceded to reinsurers	(170)
Net earned premiums	210
Fee and commission income and income from service activities	164
Investment return	6,109
Total revenue	6,483
Claims, benefits and expenses	
Gross claims and benefits paid	(998)
Amounts receivable from reinsurers	168
Net claims and benefits paid	(830)
Change in insurance contract liabilities	(352)
Change in investment contract liabilities	(4,526)
Movement in net asset value attributable to unit-holders	(36)
Movement in policyholder liabilities	(4,914)
Acquisition expenses	(129)
Administrative and other expenses	(299)
Finance costs	(15)
Total claims, benefits and expenses	(6,187)
Profit before tax from discontinued operations	296
Policyholder tax	(279)
Profit before shareholder tax from discontinued operations	17
Shareholder tax	(13)
Profit after tax from discontinued operations	4
Other comprehensive loss, net of tax	(17)
Total comprehensive loss, net of tax	(13)

(c) Cash flows of discontinued operations

	Period to 13 April 2015 £m
Operating cash flows	(45)
Financing cash flows	(295)
Total cash flows	(340)

Notes to the Consolidated Financial Statements continued

1. Business disposals continued

(d) Major classes of assets and liabilities at disposal date (FPG, FLI and FLFL in aggregate)

	Notes	13 April 2015 £m
Intangible assets	T & 10	3,026
Property, plant and equipment	U & 11	42
Investment properties	V & 12	2,685
Investment in associates		4
Financial investments	K	97,359
Deferred acquisition costs	W & 15	849
Reinsurance assets	X & 16	1,269
Insurance and other receivables		1,653
Cash and cash equivalents	M	6,954
Assets		113,841
Insurance contracts	Y	36,081
Unallocated surplus	Z	693
Financial liabilities		
– Investment contracts		68,789
– Loans and borrowings	O	868
Net asset value attributable to unit-holders	26	212
Provisions	CC & 27	135
Pension deficits	28	26
Deferred tax liabilities	H	1,125
Current tax liabilities	H	51
Insurance payables, other payables and deferred income		1,724
Liabilities		109,704
Equity attributable to shareholders of Friends Life Holdings plc		3,612
Non controlling interests		525
Total equity		4,137
Total equity and liabilities		113,841

2. Directors

The directors were all remunerated by Aviva Employment Services Limited, a fellow subsidiary of Aviva plc for their services to the Aviva Group as a whole. They were not remunerated for their services as directors of the Company and the amount of time spent performing their duties is incidental to their roles across the Aviva Group. This is consistent with prior years.

Messrs Briggs and Stoddard were directors of Aviva plc during the year and their emoluments are disclosed in that company's annual report and accounts.

Sir G M Williamson was remunerated as senior independent non-executive director of Aviva plc and details of his remuneration is included in the annual report and financial statements of Aviva plc.

Messrs D F S Rogers, Rich and Lister are remunerated for their role as employees across the Group. They are not remunerated directly for their services as directors for the Company and the amount of time spent performing their duties is incidental to their role across the Aviva Group.

Notes to the Consolidated Financial Statements continued

3. Employees

The Company has no employees. All staff are employed by fellow subsidiary undertakings of Aviva plc, Aviva Employment Services Limited and Aviva Investors Employment Services Limited; Friends Life Services Limited, Friends Life Management Services Limited and Sesame Services Limited. Disclosures relating to employees may be found in the Annual Report and Financial Statements of these companies respectively.

4. Details of income

Income comprises:

	Note	**2016** **£m**	2015 £m
Interest and other similar income			
Bank interest		**1**	1
Interest income due from loans to fellow subsidiaries [(i)]	37	**69**	80
Interest income due from syndicated loan portfolio		**1**	10
Interest income due from cross currency swap		**5**	-
Interest income due from AFS investments	37	**22**	32
		98	123
Other income from investments designated as trading			
Realised losses		**-**	(2)
Gains arising in the year		**82**	22
Unrealised gains		**82**	22
	13	**82**	20
Other income from investments designated as other than trading			
Realised gains		**2**	4
Losses arising in the year		**-**	(2)
Gains recognised in prior years and now realised		**(1)**	-
Unrealised losses		**(1)**	(2)
	13	**1**	2
Realised foreign exchange losses		**(10)**	-
Total income		**171**	145

(i) Interest on the internal STICS debt instrument is paid annually in arrears on 30 June. The STICS have no maturity but are redeemable in the whole or part at the option of FLL on 1 July 2015 and thereafter on every fifth anniversary date. The option to redeem was not taken on 1 July 2015 and the interest rate was reset to 4.39% from 6.302%.

5. Administrative and other expenses

	2016 **£m**	2015 £m
Other administrative expenses	**(5)**	(20)
	(5)	(20)

Notes to the Consolidated Financial Statements continued

6. Auditors' remuneration

The total remuneration payable by the Company, excluding VAT, to its auditors, PricewaterhouseCoopers LLP is shown below.

	2016	2015
	£'000	£'000
Fees payable to the Company's auditors for the audit of financial statements	**23**	41
	23	41

There were no non-audit fees paid to the Company's auditors during the year *(2015: £Nil)*. All fees have been borne by Aviva plc (Refer note 37(a)(ii)).

7. Finance costs

	2016	2015
	£m	£m
Interest on subordinated debt	**(101)**	(87)
Retranslation of foreign currency borrowings	**(74)**	(21)
Interest due on loans from fellow subsidiaries	**-**	(2)
	(175)	(110)

8. Tax charge

(a) Tax charged to the consolidated Income Statement

The total tax charge comprises:

		2016	2015
	Note	**£m**	£m
Current tax			
For the year		**-**	-
Adjustment in respect of prior years		**(3)**	(1)
Total tax charged to the consolidated Income Statement	8(c)	**(3)**	(1)

(b) Tax (charged)/credited to the consolidated Statement of Comprehensive Income

The tax (charged)/credited to other comprehensive income comprises:

	2016	2015
	£m	£m
Deferred tax		
Origination and reversal of temporary differences	**(1)**	6
Total tax (charged)/credited to consolidated other comprehensive income	**(1)**	6

Notes to the Consolidated Financial Statements continued

(8) Tax charge continued

(c) Tax reconciliation

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the tax rate of the United Kingdom as follows:

	2016 £m	2015 £m
(Loss)/profit for the year before tax	**(9)**	15
Tax calculated at standard UK corporation tax rate of 20% (*2015: 20.25%*)	**2**	(3)
Adjustment in respect of prior years	**(3)**	(1)
Non taxable income	**(2)**	3
Tax charge	**(3)**	(1)

9. Dividends and appropriations

	2016 £m	2015 £m
Ordinary dividends declared and charged to equity in the year:		
Interim 2016 – 79.25 pence per share, paid on 22 December 2016	**210**	-
Interim 2015 – 9.71 pence per share, paid on 22 December 2015	**-**	50
Interim 2015 – 14.76 pence per share, paid on 4 September 2015	**-**	76
Interim 2015 – In specie dividend, paid on 13 April 2015	**-**	4,482
Interim 2014 – 48.54 pence per share, paid on 30 March 2015	**-**	250
	210	4,858
Coupon payments on 2003 STICS [(i)]	**-**	7
	210	4,865

(i) Interest on 2003 STICS is treated as an appropriation of retained profits and, accordingly was accounted for when paid in 2015. Tax relief was obtained at a rate of 20.25%.The 2003 STICS were transferred to Aviva plc on 2 October 2015.

10. Intangible assets

The Company had no intangible assets at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

	AVIF £m	Other £m	Total £m
Cost			
At 1 January 2015	4,921	402	5,323
Disposals (note 1)	(4,921)	(402)	(5,323)
At 31 December 2015	-	-	-
Accumulated amortisation and impairment			
At 1 January 2015	1,935	278	2,213
Amortisation charge for the year[(i)]	73	11	84
Disposals (note 1)	(2,008)	(289)	(2,297)
At 31 December 2015	-	-	-
Carrying amount at 31 December 2015	-	-	-

(i) Amortisation and impairment charges are included within discontinued operations in the Consolidated Income Statement.

Notes to the Consolidated Financial Statements continued

11. Property, plant and equipment

The Group has no property, plant and equipment at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

	Owner occupied properties £m	Computer equipment £m	Fixtures, fittings and office equipment £m	Total £m
Cost				
At 1 January 2015	35	9	16	60
Disposals (note 1)	(35)	(9)	(16)	(60)
At 31 December 2015	-	-	-	-
Depreciation				
At 1 January 2015	-	8	8	16
Depreciation charge for the year(i)	-	-	2	2
Disposals (note 1)	-	(8)	(10)	(18)
At 31 December 2015	-	-	-	-
Carrying amount at 31 December 2015	-	-	-	-

(i) Depreciation charges are included within discontinued operations in the Consolidated Income Statement.

12. Investment properties

The Group has no investment properties at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

	2015 £m
At 1 January	2,690
Purchases	5
Fair value adjustments	28
Foreign exchange adjustments	1
Disposals(i)	(2,724)
At 31 December	-

(i) Disposals include £2,685 million relating to discontinued operations as discussed in note 1.

Notes to the Consolidated Financial Statements continued

13. Financial investments

a) Carrying amount

Financial investments comprise:

	At fair value through profit or loss				**2016**
	Trading	**Other than trading**	**Available for sale**	**Amortised cost**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Available for sale					
Internal STICS	**-**	**-**	**489**	**-**	**489**
Other investments					
Derivative financial instruments	**114**	**-**	**-**	**-**	**114**
Loans at amortised cost	**-**	**-**	**-**	**856**	**856**
Total financial investments	**114**	**-**	**489**	**856**	**1,459**

	At fair value through profit or loss				2015
	Trading	Other than trading	Available for sale	Amortised cost	Total
	£m	£m	£m	£m	£m
Fixed maturity securities					
Debt securities					
Other corporate	-	160	-	-	160
Available for sale					
Internal STICS	-	-	486	-	486
Other investments					
Derivative financial instruments	37	-	-	-	37
Loans at amortised cost	-	-	-	856	856
Total financial investments	37	160	486	856	1,539

Of the above total, £1,459 million (*2015: £1,538 million*) is expected to be recovered more than one year after the Statement of Financial Position date.

Notes to the Consolidated Financial Statements continued

14. Fair value methodology

(a) Basis for determining fair value hierarchy of financial instruments

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the ‘fair value hierarchy’ described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1

Inputs to Level 1 fair values are quoted prices (unadjusted) in active markets for identical assets and liabilities that the entity can access at the measurement date.

Level 2

Inputs to Level 2 fair values are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the instrument. Level 2 inputs include the following:

- Quoted prices for similar assets and liabilities in active markets.
- Quoted prices for identical or similar assets and liabilities in markets that are not active, the prices are not current, or price quotations vary substantially either over time or among market makers, or in which little information is released publicly.
- Inputs other than quoted prices that are observable for the asset or liability (for example, interest rates and yield curves observable at commonly quoted intervals, implied volatilities, and credit spreads).
- Market-corroborated inputs.

Where the Group uses broker quotes and no information as to the observability of inputs is provided by the broker, the investments are classified as follows:

- Where the broker price is validated by using internal models with market observable inputs and the values are similar, the Group classifies the investment as Level 2.
- In circumstances where internal models are not used to validate broker prices, or the observability of inputs used by brokers is unavailable, the investment is classified as Level 3.

Level 3

Inputs to Level 3 fair values are unobservable inputs for the asset or liability. Unobservable inputs may have been used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. However, the fair value measurement objective remains the same, i.e. an exit price at the measurement date from the perspective of a market participant that holds the asset or owes the liability. Therefore, unobservable inputs reflect the assumptions the business unit considers that market participants would use in pricing the asset or liability. Examples are investment properties, certain private equity investments and private placements.

Third-party valuations using significant unobservable inputs validated against Level 2 internally modelled valuations are classified as Level 3, where there is a significant difference between the third-party price and the internally modelled value. Where the difference is insignificant, the instrument would be classified as Level 2.

(b) Changes to valuation techniques

There were no changes in the valuation techniques during the year compared to those described in the 2015 annual report and financial statements.

Notes to the Consolidated Financial Statements continued

14. Fair value methodology continued

(c) Comparison of the carrying amount and fair values of financial instruments

Set out below is a comparison of the carrying amounts and fair values of financial assets and liabilities. These amounts may differ where the asset or liability is carried on a measurement basis other than fair value, e.g. amortised cost.

	Note	**2016 Fair value £m**	**2016 Carrying amount £m**	2015 Fair value £m	2015 Carrying amount £m
Financial investments					
Fixed maturity securities	13	**-**	**-**	160	160
Available for sale	13	**489**	**489**	486	486
Other investments	13	**114**	**114**	37	37
Loans at amortised cost	13	**1,131**	**856**	1,042	856
Total financial investments		**1,734**	**1,459**	1,725	1,539
Financial liabilities					
Borrowings	25	**(1,354)**	**(1,134)**	(1,264)	(1,054)
Derivative liabilities	29	**-**	**-**	(5)	(5)
Total financial liabilities		**(1,354)**	**(1,134)**	(1,269)	(1,059)

Fair value of the following assets and liabilities approximate to their carrying amounts:

- Receivables
- Cash and cash equivalents
- Payables and other financial liabilities

(d) Fair value hierarchy

An analysis of assets and liabilities measured at amortised cost and fair value categorised by fair value hierarchy is given below.

(i) Recurring fair value measurements

	Fair value hierarchy Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Amortised cost £m**	**2016 Statement of Financial Position £m**
Financial investments					
Available for sale	**-**	**489**	**-**	**-**	**489**
Other investments	**-**	**114**	**-**	**-**	**114**
Loans at amortised cost	**-**	**-**	**-**	**856**	**856**
Total financial investments	**-**	**603**	**-**	**856**	**1,459**
Financial liabilities					
Borrowings	**-**	**-**	**-**	**(1,134)**	**(1,134)**
Total financial liabilities	**-**	**-**	**-**	**(1,134)**	**(1,134)**

Notes to the Consolidated Financial Statements continued

14. Fair value methodology continued

(d) Fair value hierarchy continued

(i) Recurring fair value measurements continued

	Fair value hierarchy Level 1 £m	Level 2 £m	Level 3 £m	Amortised cost £m	2015 Statement of Financial Position £m
Financial investments					
Fixed maturity securities	-	160	-	-	160
Available for sale	-	486	-	-	486
Other investments	-	37	-	-	37
Loans at amortised cost	-	-	-	856	856
Total financial investments	-	683	-	856	1,539
Financial liabilities					
Borrowings	-	-	-	(1,054)	(1,054)
Derivative liabilities	-	(5)	-	-	(5)
Total financial liabilities	-	(5)	-	(1,054)	(1,059)

(ii) Non-recurring fair value measurements

There are no non-recurring fair value measurements at 31 December 2016 or 31 December 2015.

(e) Assets and liabilities not carried at fair value for which fair value is disclosed

The table below shows the fair value and fair value hierarchy and liabilities not carried at fair value.

	Fair value hierarchy Level 1 £m	**Level 2 £m**	**Level 3 £m**	**2016 Total Fair value £m**
Assets and liabilities not carried at fair value				
Loans	**1,131**	**-**	**-**	**1,131**

	Fair value hierarchy Level 1 £m	Level 2 £m	Level 3 £m	2015 Total Fair value £m
Assets and liabilities not carried at fair value				
Loans	1,042	-	-	1,042

(f) Transfers between levels of the fair value hierarchy

For financial instruments that are recognised at fair value on a recurring basis, the Group determines whether transfers have occurred between levels of the fair value hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of the reporting year.

As at 31 December 2016, for financial instruments recognised at fair value on a recurring basis £Nil (*2015: £60 million*) of corporate bonds, shares and other variable yield securities were transferred from level 3 to level 1.

Notes to the Consolidated Financial Statements continued

14. Fair value methodology continued

(g) Further information on Level 3 assets and liabilities

The Group has no level 3 assets and liabilities measured at fair value at 31 December 2016 or 31 December 2015.

The table below shows movement in the Level 3 assets and liabilities measured at fair value in 2015.

					2015
	Investment property	Owner-occupied properties	Shares and other variable yield securities	Corporate bonds and loans at fair value (including ABS)	Total
	£m	£m	£m	£m	£m
At 1 January	2,690	35	1,317	1,972	6,014
Total gains/(losses) in consolidated income statement[(i)]	83	-	(64)	22	41
Purchases	1	-	1	16	18
Sales	(64)	-	(262)	(44)	(370)
Net transfer to level 1 and level 2[(ii)]	-	-	-	(60)	(60)
Business disposal	(2,710)	(35)	(992)	(1,906)	(5,643)
At 31 December	-	-	-	-	-

(i) Gains and their reversal on owner-occupied properties were recognised in the consolidated statement of comprehensive income, losses and their reversal were recognised in the income statement within discontinued operations. All other gains and losses on assets held at fair value were recognised in the income statement within discontinued operations.
(ii) Amounts were transferred to level 1 and level 2 because observable market data became available for the securities.

15. Deferred acquisition costs

The Group has no deferred acquisition costs at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

	Insurance contracts	Investment contracts	Total
	£m	£m	£m
At 1 January 2015	100	753	853
Incurred and deferred in the period	4	23	27
Amortisation and impairment	(11)	(20)	(31)
Disposals (note 1)	(93)	(756)	(849)
At 31 December 2015	-	-	-

16. Reinsurance assets

The Group has no reinsurance assets as at 31 December 2016 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

	2015
	£m
At 1 January	1,231
Premiums	170
Claims	(168)
Other movements[(i)]	36
Disposals (note 1)	(1,269)
At 31 December	-

(i) Other movements include changes in economic and non-economic assumptions.

Notes to the Consolidated Financial Statements continued

17. Tax assets and liabilities

(a) Tax (liability) / asset

	2016 £m	2015 £m
Tax (liability)/asset		
Expected to be (paid)/received in more than one year	**(4)**	14
Tax (liability)/asset recognised in Statement of Financial Position	**(4)**	14

The 2015 tax asset of £14 million has been settled by amounts paid from fellow Group companies (note 37 (a)(ii)).

(b) Deferred tax

(i) The balances at 31 December comprise:

	2016 £m	2015 £m
Deferred tax asset	**8**	9

(ii) The deferred tax balance arises on the following items:

	2016 £m	2015 £m
Deferred tax on unrealised gains on investments	**8**	9

The deferred tax asset is recognised against future profits against which the asset will be utilised.

(iii) The movement in the deferred tax balance was as follows:

	2016 £m	2015 £m
At 1 January	**9**	(961)
Amounts charged to income statement	**-**	(193)
Amounts (charged)/credited to other comprehensive income	**(1)**	6
Disposal of STICS	**-**	32
Disposals (note 1)	**-**	1,125
At 31 December	**8**	9

Deferred 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. The Group has unrecognised deferred tax assets of £3 million (*2015: £Nil*).

UK legislation was substantively enacted in September 2016 to further reduce the corporation tax rate from 1 April 2020 to 17%. Under IFRS, deferred tax is calculated using rates substantively enacted by the reporting date and as such the 17% rate has been taken into account in deferred tax balances.

Notes to the Consolidated Financial Statements continued

18. Receivables and other financial assets

	Note	2016 £m	2015 £m
Accrued income		**42**	33
Amounts receivable from investment sales		**-**	12
Amounts receivable from fellow Aviva Group companies	37(a)(ii)	**-**	11
Investment income receivables			2
Other receivables		**2**	7
Total at 31 December		**44**	65

All receivables and other financial assets are expected to be recovered in less than one year.

19. Cash and cash equivalents

Cash and cash equivalents in the Statement of Cash Flows at 31 December comprise:

	Note	2016 £m	2015 £m
Cash at bank and in hand		**-**	27
Cash equivalents		**143**	68
		143	**95**
Bank overdraft	29	**(9)**	**-**
Total as 31 December		**134**	95

20. Ordinary share capital

(a) Details of the Company's ordinary share capital are as follows:

	2016 £m	2015 £m
Allotted, called and fully paid		
265 million (*2015: 515 million*) ordinary shares of £1 each	**265**	515

The Companies Act 2006 abolished the requirement for a company to have an authorised share capital with effect from 1 October 2009. Whilst there is no longer any limitation on the number of shares that the Company may issue, the directors will still be limited as to the number of shares they can allot because authority to allot continues to be required under the Companies Act 2006.

Ordinary shares in issue in the Company rank pari passu. All the ordinary shares in issue carry the same right to receive all dividends and other distributions declared, made or paid by the Company.

(b) Movements in the year comprise:

	Number of shares	Share capital £m
At 1January 2015 and 31 December 2015	**515,000,000**	**515**
Transfer between capital and reserves	**(250,000,000)**	**(250)**
At 31 December 2016	**265,000,000**	**265**

On 7 December 2016, the Company undertook a capital reduction under the provisions of section 641(1) of the Companies Act 2006. Following this reduction, the ordinary share capital account has been reduced by £250 million. Distributable reserves have increased by a corresponding amount.

Notes to the Consolidated Financial Statements continued

21. Other reserves

Details of the other reserves forming part of the Group's consolidated equity and movements during the year net of non-controlling interests are as follows:

	Merger reserve £m	Capital contribution reserve £m	Investment valuation reserve £m	2016 Total other reserves £m
Balance at 1 January 2016	**-**		**(35)**	**(35)**
Arising in the year through other comprehensive income				**-**
Fair value losses	**-**		**3**	**3**
Balance at 31 December 2016	**-**		**(32)**	**(32)**

	Note	Merger reserve £m	Capital contribution reserve £m	Investment valuation reserve £m	2015 Total other reserves £m
Balance at 1 January 2015		102	312	-	414
Arising in the year through other comprehensive income					
Fair value losses		-	-	(35)	(35)
Capital contribution	1	-	21	-	21
Dividends and appropriations		(102)	(333)	-	(435)
Balance at 31 December 2015		-	-	(35)	(35)

22. Retained earnings

	Note	2016 £m	2015 £m
At 1 January		**81**	3,446
Loss for the year attributable to equity shareholders		**(12)**	(2)
Transfer between capital and reserves	20	**250**	-
Capital contribution	1	**-**	1,208
Dividends and appropriations	9	**(210)**	(4,423)
Realised loss on the reclassification of STICS as a financial liability	31	**-**	(93)
Realised loss on the transfer of 2003 STICS to Aviva plc	31	**-**	(85)
Share-based payments, net of settlements	33(a) & 33(b)	**-**	(3)
Funding of Employee Benefit Trust	33(c)	**-**	8
Other comprehensive loss, net of tax from discontinued operations		**-**	(11)
Aggregate tax effect		**(1)**	36
At 31 December		**108**	81

Notes to the Consolidated Financial Statements continued

23. Insurance contracts

The Group has no insurance contracts at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1

Movement in insurance contracts liabilities are shown in the table below.

	2015 £m
At 1 January	35,750
Increase in liability from premiums	280
Release of liability due to recorded claims	(924)
Unwinding of discount	106
Change in economic assumptions	338
Other movements including net investment return	531
Disposals (note 1)	(36,081)
At 31 December	-

24. Investment contracts

The Group has no investment contracts at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

Movement in investment contracts liabilities are shown in the table below.

	2015 £m
At 1 January	64,087
Premiums	935
Claims	(1,235)
Investment return, annual management charges and other expenses(i)	5,002
Disposals (note 1)	(68,789)
At 31 December	-

(i) Investment return of £Nil (*2015: £5,525 million*) is included within discontinued operations in the Consolidated Income Statement arising from movements in investment contract liabilities.

25. Loans and borrowings

(a) Carrying amount of the Group's loans and borrowings stated at amortised cost is as follows.

	2016 £m	2015 £m
7.875% $575 million undated subordinated notes	**461**	382
12.00% £162 million subordinated notes 2021	**175**	174
8.25% £500 million subordinated notes 2022	**498**	498
Total at 31 December	**1,134**	1,054

Subordinated notes issued by the Company rank below its senior obligations and ahead of its ordinary share capital. The dated subordinated notes rank ahead of the undated subordinated notes. The fair value of notes at 31 December 2016 was £1,354 million (*2015: £1,264 million*), calculated with reference to quoted prices.

Notes to the Consolidated Financial Statements continued

25. Loans and borrowings continued

The 7.875% $575 million undated subordinated notes are irrevocably guaranteed on a subordinated basis by FLL. The debt does not have a fixed repayment date but has an initial call date in November 2018 and is callable on every subsequent interest payment date from the initial call date. With effect from the initial call date, and for so long as the debt is outstanding, the interest coupon will be reset every six years at a rate equal to the six year US dollar mid swap rate plus a margin of 6.828%. The Group holds a derivative instrument to manage the risks associated with fluctuations in exchange rates on the issue of this debt.

The 12% £162 million subordinated notes 2021 are irrevocably guaranteed on a subordinated basis by FLL. This debt is carried at amortised cost based on the fair value at the date of acquisition of Friends Provident by the Company.

The 8.25% £500 million subordinated notes 2022 are irrevocably guaranteed on a subordinated basis by FLL. This debt is carried at amortised cost being £500 million principal less capitalised issue costs of £2 million (*2015: £2 million*).

(b) The contractual maturity dates of undiscounted cash flows for these borrowings are:

			2016			2015
	Principal	**Interest**	**Total**	Principal	Interest	Total
	£m	**£m**	**£m**	£m	£m	£m
Within one year	**-**	**97**	**97**	-	91	91
1 to 5 years	**162**	**378**	**540**	162	365	527
5 to 10 years	**500**	**197**	**697**	500	217	717
10 to 15 years	**465**	**177**	**642**	390	154	544
Total at 31 December	**1,127**	**849**	**1,976**	1,052	827	1,879

In addition to above, annual principal repayments include £2 million per annum amortisation of fair value adjustments and issue costs.

Total interest expense for financial liabilities not measured at fair value through profit or loss, which arises solely from interest-bearing loans and borrowings, is £101 million (*2015: £89 million*).

Notes to the Consolidated Financial Statements continued

26. Net asset value attributable to unit-holders

The Group has no net asset value attributable to unit-holders at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

The movements in the value of third party interests in OEICS and unit trusts that are consolidated by the Group are as follows:

	2015 £m
At 1 January	589
Share of total return in the year	36
Share of distributions in the year	(1)
Amount paid on issue of shares	(5)
Amount received on cancellation of shares	(8)
Disposals(i)	(611)
At 31 December	-

(i) Disposals include £212 million are relating to discontinued operations as set out in note 1.

27. Provisions

The Group has no provisions at either 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

Movement in provisions are shown in the table below.

						2015
	At 1 January £m	Charged in the period £m	Released in the period £m	Utlised in the period £m	Disposals (note 1) £m	At 31 December £m
Customer redress	117	6	(26)	(13)	(84)	-
Separation and integration	1	-	-	(1)	-	-
Outsourcing	2	-	-	(2)	-	-
ROL separation costs	1	-	-	-	(1)	-
Sesame lapses	13	2	-	(3)	(12)	-
Vacant property	8	-	-	(2)	(6)	-
Other	34	16	(6)	(12)	(32)	-
Total at 31 December	176	24	(32)	(33)	(135)	-

Notes to the Consolidated Financial Statements continued

28. Staff pension scheme

On 1 January 2013, the FL Group set up a defined contribution arrangement for UK employees as part of the “My Money” savings and investments platform, called the Flexible Retirement Account (FRA). Employer contributions are typically in the range of 6.3% to 13% depending on contribution levels selected by members and the arrangement has a minimum employer plus member contribution level of 9.3% of pensionable salary (basic annual salary up to a defined earnings cap). The FRA has been used for auto-enrolment from the Group’s UK staging date of July 2013 and each member has their own personal pension.

The FL Group had one closed defined benefit scheme: the Friends Provident Pension Scheme (FPPS), which closed to active membership on 31 December 2012. The Group has no staff pension schemes at 31 December 2016 or 31 December 2015 following the disposal of its interests in FPG, FLI and FLFL as set out in note 1.

Full details of the Aviva Group’s pension arrangements are given in note 48 of the Aviva plc annual report and accounts.

(a) An analysis of the amounts recognised in the 2015 consolidated financial statements in respect of the FPPS pension surplus is set out below.

	Note	2015 £m
At 1 January		59
Net interest on defined benefit asset		1
Remeasurement gains		9
Administration costs[(i)]		(1)
Pension surplus		68
Authorised payments surplus charge (penal tax) at 35% of available surplus following deficit reduction contribution, discounted to present value	28(b)	(57)
Remeasurement assumption changes	28(c)	(37)
Disposals (note 1)		26
At 31 December		-

(i) Administration costs are recognised within discontinued operations in the Consolidated Income Statement.

(b) Authorised payments surplus charge (penal tax)

Under IFRIC 14, deficit reduction contributions are considered to be a minimum funding requirement and, to the extent that the contributions payable will not be available after they are paid into the scheme, a liability is recognised when the obligation arises. In accordance with s207(4) Finance Act 2004, an additional liability of £66 million had been recognised at 31 December 2015, reflecting the 35% tax that would arise on any notional refund in respect of the resultant IAS 19 surplus of £190 million (£151 million of deficit reduction contributions at a present value of £131 million plus the surplus of £59 million). A deferred tax asset of £30 million had also been recognised to reflect tax relief at a rate of 20% that was expected to be available on the deficit reduction contributions in future periods.

As part of the acquisition of the FL Group by Aviva plc, the recognition and measurements principles of the authorised payments surplus charge was aligned to the Aviva plc treatment to consider this charge as tax under IAS 12 – *Income Taxes*, rather than a restriction to the IAS 19 pension asset. This resulted in an uplift to the pension asset disclosed within Aviva plc on acquisition of £57 million.

(c) Remeasurement assumption changes

A further additional £37 million remeasurements arising from updated assumptions were reflected in the pension asset disclosed within Aviva plc on acquisition. Full details of assumptions used in the valuation of the pension surplus are disclosed within in note 48 of the Aviva plc annual report and accounts.

Notes to the Consolidated Financial Statements continued

29. Payables and other financial liabilities

	Note	**2016 £m**	2015 £m
Derivative liabilties	34	**-**	5
Obligations for repayments of cash collateral received	35	**120**	34
Amounts payable to fellow Aviva Group companies	37(a)(ii)	**-**	22
Bank Overdraft		**9**	-
Amounts due for investment purchases		**-**	1
Total at 31 December		**129**	62

All payables and other financial liabilities are carried at cost, which approximates to fair value, except for derivative liabilities, which are carried at their fair values. The total is expected to be paid in less than one year.

30. Other liabilities

	2016 £m	2015 £m
Accruals	**46**	45
Total at 31 December	**46**	45

All other liabilities are expected to be paid in less than one year.

31. Step-up Tier One Insurance Capital Securities (STICS)

The non controlling interests of the Group comprised Step-up Tier One Insurance Capital Securities (STICS) which were classified as equity instruments as there was no requirement to settle the obligation in cash or another financial asset. Consistent with this equity classification, interest on these instruments was not treated as an expense but as an appropriation of profit.

The Group has no external STICS at 31 December 2016 or 31 December 2015.

Movement in external STICS are shown in the table below.

	Note	2003 STICS £m	2005 STICS £m	Total £m
At 1 January 2015		135	183	318
Interest payable in the period		11	9	20
Interest paid in the period	9	(7)	-	(7)
Revaluation of STICS to fair value	22	85	93	178
Reclassification of 2005 STICS as a financial liability		-	(285)	(285)
Transfer of 2003 STICS to Aviva plc		(224)	-	(224)
At 31 December 2015		-	-	-

The Company's external STICS had been recognised at fair value at the acquisition date of Friends Provident. The STICS were described as the 2003 STICS and the 2005 STICS, respectively, reflecting the year in which they were originally issued by Friends Provident.

Notes to the Consolidated Financial Statements continued

31. Step-up Tier One Insurance Capital Securities (STICS) continued

2005 STICS
On 29 May 2015 the Company issued notification to holders of the 2005 STICS that the notes would be redeemed on 1 July 2015. Consequently the 2005 STICS were classified as a liability from 29 May 2015, initially recognised at a fair value of £268 million, with associated accrued interest of £17 million. A fair value revaluation of £93 million and related reversal of deferred tax of £17 million was recognised directly in equity on reclassification. The liability was fully settled in cash on 1 July 2015.

2003 STICS
On 2 October 2015, the 2003 STICS were transferred to the Group's ultimate parent, Aviva plc, at fair value of £224 million via novation of the intercompany loan with AGH. A fair value revaluation of £85 million and related reversal of deferred tax of £15 million was recognised directly in equity on transfer.

32. Risk management

(a) The Company's approach to risk and capital management

Risk management framework

The Company's risk management framework is aligned with that of the Aviva plc Group and forms an integral part of the management and Board processes and decision-making framework.

The Company's risk management approach is proportionate to its activities as a non-trading issuer of three subordinated debt instruments listed on the London Stock Exchange. At least annually the Company's management review the key risks specific to the Company.

To promote a consistent and rigorous approach to risk management, the Aviva plc Group has set out formal risk management policies and business standards which set out the risk strategy, framework and minimum requirements for the Group's worldwide operations, including the Company.

The directors recognise the critical importance of having efficient and effective risk management systems in place and acknowledge that they are responsible for the Company's framework of internal control and of reviewing its effectiveness. The framework is designed to manage rather than eliminate the risk of failure to achieve the Company's objectives, and can only provide reasonable assurance against misstatement or loss. The directors of the Company are satisfied that their adherence to this Group framework provides an adequate means of managing risk in the Company.

Sections (b) to (f) below are limited to the specific risks of the Company.

(b) Credit risk

Credit risk is the risk of financial loss as a result of the default or failure of third parties to meet their payment obligations to the Company, or variations in market values as a result of changes in expectation related to these risks.

The Group and Company's approach to managing credit risk recognises that there is a risk of adverse financial impact resulting from fluctuations in credit quality of third parties including default, rating transition and credit spread movements.

The credit risks of the Group and Company arise directly through exposures to loans to third parties and fellow Aviva Group counterparties, cash deposits, derivative counterparties and receivables. The Group and Company's maximum exposure to credit risk of financial assets, without taking collateral into account, is represented by the carrying amount of assets included in the Statement of Financial Position.

The Group and Company have significant financial exposure to amounts due from fellow Aviva Group companies. The credit risk arising from Aviva Group counterparties failing to meet all or part of their obligations is considered remote. Due to the nature of the intra-group loans, and the fact that these loans are not traded, the Company does not allow for fluctuations in market value caused by changing perceptions of the credit worthiness of such counterparties.

Financial assets, other than equities, are graded according to current external credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. Financial investments which fall outside this range are classified as sub-investment grade.

The following table provides information regarding the aggregated credit risk exposure of the Group for financial assets with external credit ratings. 'Not rated' assets capture assets not rated by external ratings agencies.

Notes to the Consolidated Financial Statements continued

32. Risk management continued

(b) Credit risk continued

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Not rated £m	2016 Carrying value £m
Available for sale	**-**	**-**	**100%**	**-**	**-**	**-**	**-**	**489**
Other investments	**-**	**-**	**-**	**-**	**-**	**-**	**100%**	**114**
Loans at amortised cost	**-**	**-**	**100%**	**-**	**-**	**-**	**-**	**856**

	AAA £m	AA £m	A £m	BBB £m	BB £m	B and below £m	Not rated £m	2015 Carrying value £m
Available for sale	-	-	100%	-	-	-	-	486
Fixed maturity securities	-	-	-	3%	29%	69%	-	160
Other investments	-	-	-	-	-	-	100%	37
Loans at amortised cost	-	-	100%	-	-	-	-	856

The Group and Company's principal counterparty exposure, amounting to £856 million (*2015: £856 million*), is to fellow Aviva plc group company, FLL, which has an external insurer financial strength rating of A+, and as such the risk of counterparty default is considered remote. Due to the nature of the loans to FLL, and the fact that these loans are recognised at amortised cost are settled, and not traded, the Group and Company is not exposed to the risk of changes to their market value caused by changing perceptions of the credit worthiness of such counterparties.

Although there is no contractual obligation for FLL to make interest payments or redeem the principal of the internal STICS, the Group and Company has an expectation and is confident that interest will be paid for the reasons set out above as well as the consequential restrictions on the ability of FLL to make dividend payments and redeem capital under the terms of the internal STICS, if it defers any interest payment. The Company's exposure to the internal STICS, which is classified as available for sale, at 31 December 2016 amounted to £489 million (*2015: £486 million*). The price of the internal STICS is sensitive to changes in the inputs used to determine its fair value, principally being market observable yields, as described in note 14, and as such the Company is exposed to changes in market perception as to the credit worthiness of the issuers of the instruments on which the market observable yields are based, being considered a suitable proxy for the internal STICS. The impact of a 100bps increase / decrease in the market observable yields used to calculate the fair value of the internal STICS would be a £15 million decrease / £16 million increase (*2015: £19 million decrease / £20 million increase*) in profit before tax and ordinary shareholders' net equity.

Although derivative instruments are not rated individually, the counterparties to these contracts all have investment grade issuer credit ratings, and the credit exposures are fully collaterised at 31 December 2016. Further information on collateral held in respect of derivatives is provided in Note 34(c).

The credit quality of receivables and other financial assets is monitored by the Group and Company, and provisions for impairment are made for irrecoverable amounts. There were no financial assets past due or impaired in either 2016 or 2015.

(c) Market risk

Market risk is the risk of adverse financial impact resulting, directly or indirectly from fluctuations in interest rates, equity prices, foreign currency exchange rates, and property prices. Market risk arises due to fluctuations in both the value of liabilities and the value of investments held.

The management of market risk is undertaken at business unit and at Aviva Group level. Businesses manage market risks locally using the Group market risk framework and within local regulatory constraints. Group Capital is responsible for monitoring and managing market risk at Group level and has established criteria for matching assets and liabilities to limit the impact of mismatches due to market movements.

For each of the major components of market risk, described in more detail below, additional policies and business standards are in place to set out how each risk should be managed and monitored, and the approach to setting an appropriate risk appetite.

Notes to the Consolidated Financial Statements continued

32. Risk management continued

(c) Market risk continued

Interest rate risk	Interest on the Group and Company's external borrowings and STICS and loans to Friends Life Limited are fixed, and therefore the Company is not exposed to interest rate risk through these instruments. Key terms and conditions are disclosed in notes 13 and 25.
Currency risk	The Group and Company is also exposed to foreign exchange risk through its issuance of US$575 million reset perpetual subordinated note. The USD cash flows for the coupons and principal up until the first reset date in 2018 have been fully hedged with cross currency derivative swaps.
Derivatives risk	Derivatives are used within policy guidelines agreed by the Group Asset and Liability Committee. Derivatives are only used for efficient investment management, asset and liability management or risk hedging purposes.

(d) Liquidity risk

Liquidity risk is the risk of the Group and Company not being able to make payments as they become due because there are insufficient assets in cash form.

The Group and Company has set its investment strategy to ensure it has sufficient liquid funds to meet its expected obligations as they fall due. In extreme circumstances, the Group and Company would approach the Company's parent, Aviva plc, for additional short-term borrowing whilst the Group and Company liquidated other assets. Aviva plc maintains significant undrawn committed borrowing facilities (£1,650 million) from a range of highly-rated banks to mitigate this risk further. In addition, the Company's long term subordinated debt and subordinated perpetual debt is irrevocably guaranteed by Friends Life Limited (see note 25). Aviva plc has an external issuer credit rating of A- and Friends Life Limited has an external insurer financial strength rating of A+, and therefore the likelihood of Aviva plc being unable to provide liquid funds to the Group and Company or FLL failing to honour its guarantee is considered remote.

The following table provides an analysis, by maturity date of the principal, of the carrying value of financial assets which are available to fund the repayment of liabilities as they crystallise:

						2016
	Note	**On demand or within 1 year £m**	**1-5 years £m**	**Greater than 5 years £m**	**No fixed term (perpetual) £m**	**Total £m**
Available for sale	13	**-**	**-**	**-**	**489**	**489**
Other investments	13	**-**	**114**	**-**	**-**	**114**
Loans at amortised cost	13	**-**	**356**	**500**	**-**	**856**
Receivables and other financial assets	18	**44**	**-**	**-**	**-**	**44**
Cash and cash equivalents	19	**143**	**-**	**-**	**-**	**143**
		187	**470**	**500**	**489**	**1,646**

						2015
	Note	On demand or within 1 year £m	1-5 years £m	Greater than 5 years £m	No fixed term (perpetual) £m	Carrying value £m
Available for sale	13	-	-	-	486	486
Fixed maturity securities	13	1	65	94	-	160
Other investments	13	-	37	-	-	37
Loans at amortised cost	13	-	356	500	-	856
Receivables and other financial assets	18	65	-	-	-	65
Cash and cash equivalents	19	95	-	-	-	95
		161	458	594	486	1,699

Notes to the Consolidated Financial Statements continued

32. Risk management continued

The derivative financial instruments above with a positive carrying value of £114 million (*2015: £37 million*) are comprised of cross currency swaps. An increase in the USD:GBP exchange rate could result in these derivatives having a negative carrying value, requiring cash resources to fund collateral and other contractual payments.

(d) Liquidity risk continued

The following table shows the Company's financial liabilities analysed by duration:

	Note	On demand or within 1 year £m	1-5 years £m	Greater than 5 years £m	No fixed term (perpetual) £m	2016 Total £m
Loans and borrowings	25	**2**	**636**	**496**	**-**	**1,134**
Payables and other financial liabilities	29	**129**	**-**	**-**	**-**	**129**
Other liabilities	30	**46**	**-**	**-**	**-**	**46**
		177	**636**	**496**	**-**	**1,309**

	Note	On demand or within 1 year £m	1-5 years £m	Greater than 5 years £m	No fixed term (perpetual) £m	2015 Carrying value £m
Loans and borrowings	25	2	382	670	-	1,054
Payables and other financial liabilities	29	62	-	-	-	62
Other liabilities	30	45	-	-	-	45
		109	382	670	-	1,161

(e) Operational risk

Operational risk is the risk of direct or indirect loss, arising from inadequate or failed internal processes, people and systems, or external events including changes in the regulatory environment.

Given its limited activities, the key operational risks to the Company are inadequate governance and lack of sufficiently robust financial controls. The risks are mitigated by the Board’s adoption and implementation of the Group’s risk management policies and framework and compliance with the Group’s financial reporting and controls framework.

(f) Capital management

The Group and Company’s capital risk is determined with reference to the requirements of the Group and Company’s stakeholders. In managing capital, the Group and Company seeks to maintain sufficient, but not excessive, financial strength to support the payment of interest due on loans and the requirements of other stakeholders. The sources of capital used by the Group and Company are equity shareholders’ funds. At 31 December 2016 the Company had £341 million (*2015: £561 million*) of total capital employed.

Notes to the Consolidated Financial Statements continued

33. Share based payments

Friends Life Group operated a number of share-based payment schemes which vested/crystallised on the acquisition of the Group by Aviva plc on 13 April 2015.

No share based payments expense is recognised in the Group Consolidated Income Statement or equity in in the Consolidated Statement of Financial Position for 2016. The disclosures below relate to the 2015 consolidated financial statements.

(a) Friends Life Group plc Long Term Incentive Plan (FLG LTIP)

The scheme was introduced in 2010 as a cash-settled share-based payment scheme, and was modified in May 2013 in order to continue to properly incentivise the Group's senior executives following a change in the Group's strategy. The LTIP terms were amended so that the implicit need for an exit event was replaced with a market value based calculation to measure performance, without altering the required internal rate of return. The change to the scheme was accounted for as a modification under IFRS 2: *Share-based payment*s. The modified scheme was an equity-settled scheme, to be settled in three tranches of shares in Friends Life Group Limited (FLG) over 2014 to 2016 (Tranches A, B and C).

The amount to be paid to participants was determined by a formula set out in the scheme rules. The LTIP created a profit pool equal to 2% of the growth in the value of Friends Life, as assessed under the LTIP rules. The calculation of the value of the profit pool on acquisition of the Friends Life Group by Aviva plc (refer note 1) was partly based on the value of Aviva shares over the 40 day period immediately prior to the date of the first announcement of the proposed acquisition and also involved an assessment of the market value of Friends Life using the consideration paid to Friends Life shareholders and to RCAP under the value share arrangement.

The expense recognised in the Group in 2015 comprised £23 million charge reflected in administrative expenses in the Consolidated Income Statement and £4 million decrease in equity included in the Consolidated Statement of Financial Position representing the cumulative charge of the equity settled awards reclassified to cash-settled. The expense was recognised in Friends Life Management Services Limited (FLMS) (the employing company) and then recharged to the Group.

(b) Contractual share awards

Certain directors were entitled to cash and shares in FLG to compensate them for awards they forfeited from their previous employer as a result of joining Friends Life. The share elements of these awards were treated as equity-settled schemes. The final award vested in June 2015. The vesting of this award occurred on acquisition. A fair value charge of £1 million had been recognised in 2015 in discontinued operations in the Consolidated Income Statement with corresponding increase in equity included in the Consolidated Statement of Financial Position.

(c) Employee Benefit Trust (EBT)

During 2015 the Group provided funding of £13 million to an EBT which purchased and held shares of FLG for delivery to employees under various share-based payment schemes. In April 2015, the EBT repaid cash of £8 million to the Group.

34. Derivative financial instruments and hedging

The Group uses cross-currency swap derivative contracts to manage the risks associated with fluctuations in the US Dollar/GBP exchange rate, linked to its US Dollar denominated subordinated debt instrument, see note 25.

Both the notional amounts and fair values of these instruments are given below. The notional amounts reflect the aggregate of individual derivative positions on a gross basis and so give an indication of the overall scale of the derivative transaction. They do not reflect current market values of the open positions. The fair values represent the gross carrying values at the year-end for each class of derivative contract held (or issued) by the Company.

The fair values do not provide an indication of credit risk, as many over-the-counter transactions are contracted and documented under ISDA (International Swaps and Derivatives Association Inc) master agreements or their equivalent. Such agreements are designed to provide a legally enforceable set-off in the event of default, which reduces credit exposure.

(a) Instruments qualifying for hedge accounting

The Company has no instruments qualifying for hedge accounting in accordance with IAS 39, Financial Instruments: Recognition and Measurement.

Notes to the Consolidated Financial Statements continued

34. Derivative financial instruments and hedging continued

(b) Instruments not qualifying for hedge accounting

Certain derivatives either do not qualify for hedge accounting under IAS 39 or the option to hedge account has not been taken. These are referred to below as non-hedge derivatives.

The Company's non-hedge derivative activity at 31 December 2016 was as follows:

			2016
	Contract/ notional amount	**Fair value asset**	**Fair value liability**
	£m	**£m**	**£m**
Foreign exchange contracts			
OTC			
Swaps	**356**	**114**	**-**
Total at 31 December	**356**	**114**	**-**

			2015
	Contract/ notional amount	Fair value asset	Fair value liability
	£m	£m	£m
Foreign exchange contracts			
OTC			
Forwards	(5)	-	(5)
Swaps	356	37	-
Total at 31 December	351	37	(5)

Fair value assets are recognised as ‘Derivative financial instruments’ in note 13. Fair value liabilities are recognised as ‘Derivative liabilities’ in note 29.

The Company’s derivative risk management policies are outlined in note 32.

(c) Collateral

Certain derivative contracts, primarily interest rate and currency swaps, involve the receipt or pledging of cash and non-cash collateral. The amount of collateral payable is included in note 29.

35. Financial assets and liabilities subject to offsetting, enforceable master netting arrangements and similar agreements

Financial assets and liabilities are offset in the Statement of Financial Position when the Company has a legally enforceable right to offset and has the intention to settle the asset and liability on a net basis, or to realise the asset and settle the liability simultaneously.

The Company mitigates credit risk in derivative contracts by entering into collateral agreements, where practical, and in ISDA master netting agreements for each of the legal entities to facilitate Aviva’s right to offset credit risk exposure. The credit support agreement will normally dictate the threshold over which collateral needs to be pledged by Aviva or its counterparty.

Transactions requiring the Company or its counterparty to post collateral are typically the result of over-the-counter derivative trades, comprised mostly of interest rate swaps, currency swaps and credit default swaps. These transactions are conducted under terms that are usual and customary to standard long-term borrowing, derivative, securities lending and securities borrowing activities.

Notes to the Consolidated Financial Statements continued

35. Financial assets and liabilities subject to offsetting, enforceable master netting arrangements and similar agreements continued

The derivative assets and liabilities in the table below are made up of the contracts described in detail in note 34.

	Note	**2016** £m	2015 £m
Derivative assets			
Gross amounts recognised in the Statement of Financial Position			
Gross amounts of recognised financial liabilities set off in the Statement of Financial Position	13	**114**	37
Net amounts of financial assets presented in the Statement of Financial Position		**114**	37
Related amounts not set off in the Statement of Financial Position:			
Collateral received	29	**(120)**	(34)
Net amount		**(6)**	3
Derivative liabilities			
Gross amounts recognised in the Statement of Financial Position			
Gross amounts of recognised financial assets set off in the Statement of Financial Position	29	**-**	(5)
Net amounts of financial liabilities presented in the Statement of Financial Position		**-**	(5)
Related amounts not set off in the Statement of Financial Position:			
Collateral pledged	18	**-**	-
Net amount		**-**	(5)

36. Related Undertakings

(a) The related undertakings which are included within the consolidated financial statements as at 31 December 2016 are listed below.

Name of undertaking	**Registered office**	**Share class**	**% held by Group companies**	**Aggregate capital and reserves £m**	**2016 Profit for the year £m**
Enhanced Loan Investment Strategy	49 Avenue J.F. Kennedy L-1855 Luxembourg, Grand Duchy of Luxembourg	Ordinary shares	100%	-	2
Enhanced Loan Investment Strategy Direct Holdings S.a.r.l	49 Avenue J.F. Kennedy L-1855 Luxembourg, Grand Duchy of Luxembourg	Ordinary shares	100%	-	-

Name of undertaking	Registered office	Share class	% held by Group companies	Aggregate capital and reserves £m	2015 Profit for the year £m
Enhanced Loan Investment Strategy	49 Avenue J.F. Kennedy L-1855 Luxembourg, Grand Duchy of Luxembourg	Ordinary shares	100%	188	4
Enhanced Loan Investment Strategy Direct Holdings S.a.r.l	49 Avenue J.F. Kennedy L-1855 Luxembourg, Grand Duchy of Luxembourg	Ordinary shares	100%	1	-

Notes to the Consolidated Financial Statements continued

37. Related party transactions

(a) The Group had the following related party transactions

(i) Loans receivable

On 8 November 2012 the Company provided an unsecured loan of £356 million to its subsidiary, FLL. The loan accrues interest at a rate of 7.92% per annum with settlement expected to be received at maturity in 8 November 2018. As at the Statement of Financial Position date, the total loan balance outstanding was £356 million (*2015: £356 million*).

On 21 April 2011 the Company provided an unsecured loan of £500 million to its subsidiary, FLL. The loan accrues interest at a rate of 8.25% per annum with settlement expected to be received at maturity in 21 April 2022. As at the Statement of Financial Position date, the total loan balance outstanding was £500 million (*2015: £500 million*).

The maturity analysis of the related party loans receivable is as follows:

	2016	2015
	£m	£m
1-5 years	**356**	356
Greater than 5 years	**500**	500
Total at 31 December	**856**	856

The interest received on these loans shown in the Income Statement is £69 million (*2015: £80 million*). The 2015 interest received includes £11 million of interest from loan with AGH which was repaid in 2015. Refer note 4.

(ii) Other transactions

Services provided to related parties

	2016		2015	
	Income earned in the year	**Receivable at year end**	Income earned in the year	Receivable at year end
	£m	**£m**	£m	£m
Fellow Group companies	**-**	**-**	111	7

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms.

Services provided by related parties

	2016		2015	
	Expenses paid in the year	**Payable at year end**	Expenses incurred in the year	Payable at year end
	£m	**£m**	£m	£m
Fellow Group companies	**-**	**-**	18	22

Expenses incurred relate to share scheme charges and corporate costs of £Nil *(2015: £18 million)*.

The related parties' payables are not secured and no guarantees were received in respect thereof. The payables will be settled in accordance with normal credit terms.

There were no non-audit fees paid to the Company's auditors during the year *(2015: £Nil)*. Audit fees as decribed in note 6 are borne by the Company's ultimate parent, Aviva plc.

Notes to the Consolidated Financial Statements continued

37. Related party transactions continued

a) The Company had the following related party transactions continued

(ii) Other transactions continued

Group relief

Transactions with Group companies for settlement of corporation tax assets and liabilities by group relief are described in note 17.

Dividends paid

Dividends paid relates to an intercompany transaction of £210 million *(2015: £4,865 million)* with the Company's parent, AGH.

(b) Key management compensation

Key management, which comprises the directors of the Company, are not remunerated directly for their services as directors for the Company and the amount of time spent performing their duties are incidental to their role across the Aviva Group. The majority of such costs are borne by Aviva plc and are not recharged to the Company. Refer to note 2 for details of director's remuneration.

(c) Ultimate parent entity

The immediate parent entity is Aviva Group Holdings Limited, a private limited Group incorporated and domiciled in England and Wales. The ultimate parent entity and controlling party is Aviva plc, a public limited Group incorporated and domiciled in England and Wales. This is the parent undertaking of the smallest and largest Group to consolidate these financial statements. Copies of Aviva plc consolidated financial statements are available on application to the Group Secretary, Aviva plc, St Helen's, 1 Undershaft, London EC3P 3DQ, and on the Aviva plc website at www.aviva.com.

Company Income Statement
For the year ended 31 December 2016

	Note	**2016 £m**	2015 £m
Income			
Net investment income	C	**173**	753
		173	753
Expenses			
Other expenses		**(5)**	(19)
Finance costs	7	**(175)**	(110)
Impairment of investment in subsidiaries	E	**-**	(20)
		(180)	(149)
(Loss)/profit for the year before tax		**(7)**	604
Tax charge	D	**(3)**	-
(Loss)/profit for the year		**(10)**	604
Attributable to:			
Equity holders of Friends Life Holdings plc		**(10)**	584
Non controlling interests		**-**	20
(Loss)/profit for the year		**(10)**	604

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 62 to 70 are an integral part of these financial statements.

Company Statement of Comprehensive Income
For the year ended 31 December 2016

	2016	2015
	£m	£m
(Loss)/profit for the year	**(10)**	604
Items that may be reclassified subsequently to income statement		
Investment classified as available for sale		
Fair value gains/(losses)	**3**	(35)
Aggregate tax effect	**(1)**	6
Other comprehensive income/(loss), net of tax	**2**	(29)
Total other comprehensive (loss)/income for the year	**(8)**	575
Attributable to:		
Equity holders of Friends Life Holdings plc	**(8)**	555
Non controlling interests	**-**	20
Total other comprehensive (loss)/income for the year	**(8)**	575

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 62 to 70 are an integral part of these financial statements.

Company Statement of Changes in Equity
For the year ended 31 December 2016

		Equity attributable to shareholders of Friends Life Holdings plc					
	Note	Ordinary share capital £m	Other reserves £m	Retained earnings £m	Total £m	STICS £m	Total equity £m
Balance at 1 January 2016		**515**	**(35)**	**71**	**551**	**-**	**551**
Loss for the year		**-**	**-**	**(10)**	**(10)**	**-**	**(10)**
Other comprehensive income		**-**	**3**	**(1)**	**2**	**-**	**2**
Total comprehensive loss		**-**	**3**	**(11)**	**(8)**	**-**	**(8)**
Dividends and appropriations	9	**-**	**-**	**(210)**	**(210)**	**-**	**(210)**
Transfer between capital and reserves	20 & L	**(250)**	**-**	**250**	**-**	**-**	**-**
Balance at 31 December 2016		**265**	**(32)**	**100**	**333**	**-**	**333**

		Equity attributable to shareholders of Friends Life Holdings plc					
	Note	Ordinary share capital £m	Other reserves £m	Retained earnings £m	Total £m	STICS £m	Total equity £m
Balance at 1 January 2015		515	414	3,900	4,829	488	5,317
Profit for the year		-	-	584	584	20	604
Other comprehensive loss		-	(35)	6	(29)	-	(29)
Total comprehensive income		-	(35)	590	555	20	575
Dividends and appropriations	9	-	(435)	(4,423)	(4,858)	(7)	(4,865)
Capital contribution		-	21	-	21	-	21
Reclassification of STICS as a financial liability	P	-	-		-	(285)	(285)
Transfer of 2003 STICS to Aviva plc	P	-	-	(8)	(8)	(216)	(224)
Funding of Employee Benefit Trust	33	-	-	8	8	-	8
Aggregate tax effect				4	4	-	4
Balance at 31 December 2015		515	(35)	71	551	-	551

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 62 to 70 are an integral part of these financial statements.

Company Statement of Financial Position
As at 31 December 2016

	Note	**2016** £m	2015 £m	1 January 2015 £m
Assets				
Non current assets				
Investment in subsidiaries	E	**-**	-	4,846
Financial investments	F	**1,459**	1,342	1,356
Tax assets	H	**-**	14	36
Deferred tax assets	H	**5**	6	-
Current assets				
Financial investments	F	**-**	226	215
Receivables and other financial assets	I	**44**	72	64
Cash and cash equivalents	J	**143**	53	193
Total assets		**1,651**	1,713	6,710
Equity				
Ordinary share capital	20	**265**	515	515
Other reserves	K	**(32)**	(35)	414
Retained earnings	L	**100**	71	3,900
Step-up Tier One Insurance Capital Securities (STICS)	P	**-**	-	488
Total equity		**333**	551	5,317
Liabilities				
Non current liabilities				
Borrowings	M	**1,137**	1,059	1,040
Tax liabilities	H	**4**	-	-
Current liabilities				
Borrowings	M	**2**	2	262
Payables and other financial liabilities	N	**129**	56	46
Other liabilities	30	**46**	45	45
Total liabilities		**1,318**	1,162	1,393
Total equity and liabilites		**1,651**	1,713	6,710

The financial statements on pages 57 to 70 were approved by the Board of Directors on 8 March 2017 and signed on its behalf by

T Stoddard
Director

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 62 to 70 are an integral part of these financial statements.

Company Statement of Cash Flows

	Note	**2016 £m**	2015 £m
Cash flows from investing activities			
Interest received		**87**	101
Collateral received		**86**	34
Net disposal of financial investments		**210**	-
Dividends income		**-**	610
Net purchase of financial investments		**-**	(9)
Net cash from investing activities		**383**	736
Cash flows from financing activities			
Repayment of loan to parent		**-**	145
Repayment of the 2005 STICS		**-**	(285)
Finance costs		**(95)**	(91)
Net funding of Employee Benefit Trust		**-**	8
STICS interest		**-**	(7)
Repayment of Loan to FLP		**-**	(260)
Ordinary dividends paid		**(210)**	(376)
Amounts repaid to fellow Group companies		**(18)**	(35)
Amounts repaid from fellow Group companies		**21**	25
Net cash used in financing activities		**(302)**	(876)
Total net cash increase/(decrease) in cash and cash equivalents		**81**	(140)
Cash and cash equivalents at 1 January		**53**	193
Cash and cash equivalents at 31 December	J	**134**	53

The accounting policies (identified alphabetically) on pages 10 to 22 and notes (identified numerically) on pages 62 to 70 are an integral part of these financial statements.

Notes to the Company's Financial Statements

A Basis of preparation

The Company is a public limited Company incorporated and domiciled in the England and Wales.

The financial statements of the Company have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) and IFRS Interpretations Committee (IFRS IC) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU), and those parts of the Companies Act 2006 applicable to those reporting under IFRS. In addition to fulfilling their legal obligation to comply with IFRS as adopted by the EU, the Company has also complied with IFRS as issued by the IASB and applicable at 31 December 2016.

For all periods up to and including the year ended 31 December 2015, the Group prepared its financial statements in accordance with Financial Reporting Standard 101, 'Reduced Disclosure Framework' (FRS 101). These financial statements for the year ended 31 December 2016 are the first the Company has prepared in accordance with IFRS. Refer to Note B for information on how the Company adopted IFRS.

The Directors have adopted the going concern basis in preparing the Company's financial statements (see basis of preparation in policy A of the Group's consolidated financial statements).

The Company has followed the same accounting policies as those shown in the Group's consolidated financial statements. There were no significant judgements applied in selecting these accounting policies.

B First-time adoption of IFRS

These financial statements, for the year ended 31 December 2016, are the first the Company has prepared in accordance with IFRS.

For periods up to and including the year ended 31 December 2015, the Company prepared its financial statements in accordance with Financial Reporting Standard 101, 'Reduced Disclosure Framework' (FRS 101).

Accordingly, the Company has prepared financial statements that comply with IFRS applicable as at 31 December 2016, together with the comparative period data for the year ended 31 December 2015, as described in the summary of significant accounting policies.

In preparing the financial statements, the Company's opening Statement of Financial Position was prepared as at 1 January 2015, the Company's date of transition to IFRS.

No adjustments have arisen from the transition made by the Company in restating its FRS101 financial statements, including the Statement of Financial Position as at 1 January 2015 and the financial statements for the year ended 31 December 2015.

Notes to the Company's Financial Statements continued

C Details of income

	2016 £m	2015 £m
Dividend income from subsidiaries	**-**	610
Interest and other similar income		
Bank interest	**1**	1
Interest income due from loans to fellow subsidiaries	**69**	80
Interest income due from cross currency swap	**5**	-
Interest income due from AFS investments	**22**	32
	97	113
Other income from investments designated as trading		
Gains arising in the year	**77**	27
Unrealised gains	**77**	27
Other income from investments designated as other than trading		
Gains arising in the year	**-**	3
Gains recognised in prior years and now realised	**(1)**	-
Unrealised (losses)/gains	**(1)**	3
	(1)	3
Total income	**173**	**753**

Interest on the internal STICS debt instrument is paid annually in arrears on 30 June. The STICS have no maturity but are redeemable in the whole or part at the option of FLL on 1 July 2015 and thereafter on every fifth anniversary date. The option to redeem was not taken on 1 July 2015 and the interest rate was reset to 4.39% from 6.302%.

D Tax charge

(a) Tax charged to the Income Statement

The total tax charge comprises:

	Note	2016 £m	2015 £m
Current tax			
For the year		**-**	1
Adjustment in respect of prior years		**(3)**	(1)
Total tax charged to the Income Statement	8(c)	**(3)**	-

(b) Tax credited to Statement of Comprehensive Income

The tax credited to other comprehensive income comprises:

	2016 £m	2015 £m
Deferred tax		
Origination and reversal of temporary differences	**(1)**	6
Total tax (charged)/credited to other comprehensive income	**(1)**	6

Notes to the Company's financial statements continued

D Tax charge continued

(c) Tax reconciliation

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the tax rate of the United Kingdom as follows:

	2016 **£m**	2015 £m
(Loss)/profit for the year before tax	**(7)**	604
Tax calculated at standard UK corporation tax rate of 20% (*2015: 20.25%*)	**1**	(122)
Adjustment in respect of prior years	**(3)**	(1)
Non taxable income	**(1)**	127
Impairment of investment in subsidiaries	**-**	(4)
Tax charge	**(3)**	-

E Investment in subsidiaries

	2016 **£m**	2015 £m
At 1 January	**-**	4,846
Additions (i)	**-**	22
Impairment of subsidiaries (ii)	**-**	(20)
Disposals (iii)(iv)	**-**	(4,848)
At 31 December	**-**	-

(i) The impairment of a debtor related to the acquisition of Friends ASLH Limited (FASLH) was accounted for as an increase in the cost of investment of £22 million.
(ii) Impairment of subsidiaries relates to the write-down of the net asset value of Friends ASLH.
(iii) On 13 April 2015 the former FL Group companies were restructured within the Aviva Group. A key part of this restructuring involved the Company's interests in its principal subsidiaries being transferred to other Aviva Group companies. The Company disposed of 100% of its interest in FPG, FLI and FLFL, representing the main operating segments of the Group, related service companies and staff pension scheme. Refer to note 1(a) of the Group's Consolidated Financial Statements for further details.
(iv) On 30 June 2015 the Company transferred 100% of its holding in Friends ASLH Limited to another Aviva Group company for consideration of £7 million.

Notes to the Company's financial statements continued

F Financial investments

a) Carrying amount

Financial investments comprise:

	At fair value through profit or loss				**2016**
	Trading	**Other than trading**	**Available for sale**	**Amortised cost**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Available for sale					
Internal STICS	**-**	**-**	**489**	**-**	**489**
Other investments					
Derivative financial instruments	**114**	**-**	**-**	**-**	**114**
Loans at amortised cost	**-**	**-**	**-**	**856**	**856**
Total financial investments	**114**	**-**	**489**	**856**	**1,459**

	At fair value through profit or loss				2015
	Trading	Other than trading	Available for sale	Amortised cost	Total
	£m	£m	£m	£m	£m
Available for sale					
Internal STICS	-	-	486	-	486
Fixed maturity securities					
Debt securities					
Other corporate	-	189	-	-	189
Other investments					
Derivative financial instruments	37	-	-	-	37
Loans at amortised cost	-	-	-	856	856
Total financial investments	37	189	486	856	1,568

Of the above total, £1,459 million (*2015: £1,342 million*) is expected to be recovered more than one year after the Statement of Financial Position date.

The Company uses cross-currency swap derivative contracts to manage the risks associated with fluctuations in the US Dollar/GBP exchange rate, linked to its US Dollar denominated subordinated debt instrument, see note M. The derivative instruments are measured at fair value through profit or loss and as at 31 December 2016 the Company has received collateral of £120 million in respect of the swaps (*2015: £34 million)*. The obligations for repayment of cash collateral received are reflected in the Company Statement of Financial Position.

Notes to the Company's financial statements continued

G Fair value methodology

Refer to note 14 to the Group's consolidated financial statements for further details on the fair value methodology.

An analysis of assets and liabilities measured at amortised cost and fair value categorised by fair value hierarchy is given below.

	Fair value hierarchy				2016
	Level 1	Level 2	Level 3	Amortised cost	Statement of Financial Position
	£m	£m	£m	£m	£m
Financial investments					
Available for sale	**-**	**489**	**-**	**-**	**489**
Other investments	**-**	**114**	**-**	**-**	**114**
Loans at amortised cost	**-**	**-**	**-**	**856**	**856**
Total financial investments	**-**	**603**	**-**	**856**	**1,459**
Financial liabilities					
Borrowings	**-**	**-**	**-**	**1,139**	**1,139**
Total financial liabilities	**-**	**-**	**-**	**1,139**	**1,139**

	Fair value hierarchy				2015
	Level 1	Level 2	Level 3	Amortised cost	Statement of Financial Position
	£m	£m	£m	£m	£m
Financial investments					
Available for sale	-	486	-	-	486
Fixed maturity securities	-	189	-	-	189
Other investments	-	37	-	-	37
Loans at amortised cost	-	-	-	856	856
Total financial investments	-	712	-	856	1,568
Financial liabilities					
Borrowings	-	-	-	1,061	1,061
Total financial liabilities	-	-	-	1,061	1,061

Notes to the Company's financial statements continued

H Tax assets and liabilities

(a) Tax (liability) / asset

	2016 £m	2015 £m
Tax (liability) / asset		
Expected to be (paid) / received in more than one year	**(4)**	14
Tax (liability) / asset recognised in Statement of Financial Position	**(4)**	14

(b) Deferred tax

(i) The balances at 31 December comprise:

	2016 £m	2015 £m
Deferred tax asset	**5**	6

(ii) The deferred tax balance arises on the following items:

	2016 £m	2015 £m
Unrealised gains on investments	**5**	6

The deferred tax asset is recognised against future profits against which the asset will be utilised.

(iii) The movement in the deferred tax balance was as follows:

	2016 £m	2015 £m
At 1 January	**6**	-
Amounts charged to other comprehensive income	**(1)**	6
At 31 December	**5**	6

Deferred 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. The Company has unrecognised deferred tax assets of £3 million *(2015: £Nil).*

UK legislation was substantively enacted in September 2016 to further reduce the corporation tax rate from 1 April 2020 to 17%. Under IFRS, deferred tax is calculated using rates substantively enacted by the reporting date and as such the 17% rate has been taken into account in deferred tax balances.

Notes to the Company's financial statements continued

I Receivables and other financial assets

	Note	2016 £m	2015 £m
Accrued income		**42**	33
Amounts receivable from investment sales		**-**	20
Amounts receivable from fellow Aviva Group companies	37(a)(ii)	**-**	11
Other receivables		**2**	8
Total at 31 December		**44**	72

All receivables and other financial assets are expected to be received in less than one year.

J Cash and cash equivalents

Cash and cash equivalents in the Statement of Cash Flows at 31 December comprise:

	Note	2016 £m	2015 £m
Cash at bank and in hand		**-**	6
Cash equivalents		**143**	47
		143	53
Bank overdraft	N	**(9)**	-
Total as 31 December		**134**	53

K Other reserves

Details of the other reserves forming part of the Company's equity and movements during the year net of non-controlling interests are as follows:

	Merger reserve £m	Capital contribution reserve £m	Investment valuation reserve £m	2016 Total other reserves £m
Balance at 1 January	**-**	**-**	**(35)**	**(35)**
Arising in the year through other comprehensive income				**-**
Fair value gains	**-**	**-**	**3**	**3**
Balance at 31 December	**-**	**-**	**(32)**	**(32)**

Notes to the Company's financial statements continued

K Other reserves continued

	Merger reserve £m	Capital contribution reserve £m	Investment valuation reserve £m	2015 Total other reserves £m
Balance at 1 January	102	312	-	414
Arising in the year through other comprehensive income				-
Fair value losses	-	-	(35)	(35)
Capital contribution(i)		21	-	21
Dividends and appropriations	(102)	(333)	-	(435)
Balance at 31 December	-	-	(35)	(35)

(i) The capital contribution reflects the impact of disposal of FPG on the carrying value of Company's equity investments in FLL. These were revalued from historic cost to market value at the date of disposal with the £21 million net asset impact being shown as a capital contribution reflecting the IAS 1 requirement that transactions with owners in their capacity as owners are reflected in the statement of changes in equity as notional capital contributions or distributions.

L Retained earnings

	Note	**2016 £m**	2015 £m
At 1 January		**71**	3,900
Total (loss)/profit for the year attributable to equity shareholders		**(10)**	584
Transfer between capital and reserves	20	**250**	-
Dividends and appropriations		**(210)**	(4,423)
Realised loss on the transfer of 2003 STICS to Aviva plc		**-**	(8)
Funding of Employee Benefit Trust		**-**	8
Aggregate tax effect		**(1)**	10
At 31 December		**100**	71

M Loans and borrowings

(a) Carrying amount of the Company's loans and borrowings stated at amortised cost is as follows.

	2016 £m	2015 £m
7.875% $575 million undated subordinated notes	**461**	382
12.00% £162 million subordinated notes 2021	**180**	181
8.25% £500 million subordinated notes 2022	**498**	498
Total at 31 December	**1,139**	1,061
Expected to be paid in less than one year	**2**	2
Expected to be paid in more than one year	**1,137**	1,059
Total at 31 December	**1,139**	1,061

Further details of the Company's borrowings are set out in note 25 of the Group's consolidated financial statements.

Notes to the Company's financial statements continued

N Payables and other financial liabilities

	Note	2016 £m	2015 £m
Obligations for repayments of cash collateral received		**120**	34
Bank overdraft		**9**	-
Amounts payable to fellow Aviva Group companies	37(a)(ii)	**-**	22
Total at 31 December		**129**	56

All payables and other financial liabilities are carried at cost, which approximates to fair value, except for derivative liabilities, which are carried at their fair values. The total is expected to be paid in less than one year.

O Risk management

Details of the objectives, policies and processes for mitigating credit risk, market risk and liquidity risk are set out in note 32 to the Group's consolidated financial statements. None of the financial assets are deemed to be past due or impaired.

P STICS

The non controlling interests of the Company comprised STICS which were classified as equity instruments as there was no requirement to settle the obligation in cash or another financial asset. Consistent with this equity classification, interest on these instruments was not treated as an expense but as an appropriation of profit.

The Company has no external STICS at 31 December 2016 or 31 December 2015.

Movement in external STICS are shown in the table below.

	Note	2003 STICS £m	2005 STICS £m	Total £m
At 1 January 2015		212	276	488
Interest payable in the year		11	9	20
Interest paid in the year	9	(7)	-	(7)
Revaluation of STICS to fair value	L	8	-	8
Reclassification of 2005 STICS as a financial liability		-	(285)	(285)
Transfer of 2003 STICS to Aviva plc		(224)	-	(224)
At 31 December 2015		-	-	-

2005 STICS
On 29 May 2015 the Company issued notification to holders of the 2005 STICS that the notes would be redeemed on 1 July 2015. Consequently the 2005 STICS were classified as a liability from 29 May 2015, initially recognised at a fair value of £276 million, with associated accrued interest of £17 million. A related reversal of deferred tax of £17 million was recognised directly in equity on reclassification. The liability was fully settled in cash on 1 July 2015.

2003 STICS
On 2 October 2015, the 2003 STICS were transferred to the Group's ultimate parent, Aviva plc, at fair value of £224 million via novation of the intercompany loan with AGH. A fair value revaluation of £8 million was recognised directly in equity on transfer.

Q Related party transactions

Details of the Company's related party transactions are set out in note 37 to the Group's consolidated financial statements.

R Post balance sheet events

There are no post balance sheet events to report.