13 August 2013

Resolution Limited

Results for the half year ended 30 June 2013

Strong financial performance and improving cash generation

- Sustainable free surplus £147 million, up 23% (30 June 2012: £120 million)
- IFRS based operating profit before tax of £191 million (30 June 2012: £163 million)
- IFRS based operating earnings per share up 17% to 13.26 pence (30 June 2012: 11.32 pence)
- MCEV operating profit before tax of £214 million (30 June 2012: £235 million) reflects expected impact of long-term interest rate environment

Strong capital base underpins dividend

- Available shareholder cash £839 million (31 December 2012: £850 million)
- Group IGCA surplus(i) £2.1 billion, coverage ratio 222% (surplus at 31 December 2012: £2.2 billion, 221% coverage ratio)
- Economic capital surplus(ii) £3.7 billion, coverage ratio 192% (surplus at 31 December 2012: £3.5 billion, 194% coverage ratio)
- Interim dividend of 7.05 pence per share (30 June 2012: 7.05 pence per share)

Improving new business performance

- Strong growth in UK division; value of new business of £89 million, up 41% and at an IRR of 16.7%
- International division core value of new business £21 million (30 June 2012: £22 million) reflecting resilient performance in difficult markets
- Total Group VNB £97 million; Group new business IRR of 11.2%; Group margin increased to 2.8%

Operating highlights

- Successful recapture of an additional £7 billion of assets by in-house asset manager FLI
- Corporate Benefits performance exceeds expectations with 30% increase in VNB, strong pipeline of new schemes and auto-enrolling clients for the rest of the year
- £154 million of cost savings secured at 30 June 2013 (96% of 2015 target)
- Good progress made on delivering the International strategy with controlled exit from German manufacturing to be completed in third quarter 2013 and all other non-core exit actions completed

Andy Briggs, Group Chief Executive said:

"We continue to make excellent operational progress in line with the clear and consistent strategy and value agenda of the Group. The strong performance announced today reflects the attractive strategic outlook of the Group and has been led by the UK division where higher value of new business has been written at a lower cash cost. We have continued to deliver cash from our Heritage division and made good progress on International strategy implementation. This financial discipline underpins strong growth in cash generation and I remain confident about the future prospects of the Group."

Notes:

(i) Represents estimated Insurance Group Capital Adequacy (“IGCA”) at the Resolution holding company level
(ii) Economic capital surplus is estimated

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Media

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Forward-looking statements

This announcement includes statements that are, or may be deemed to be, "forward-looking statements" with respect to Resolution, its subsidiary undertakings and their outlook, plans and current goals. In some cases, these forward-looking statements can be identified by the use of forward-looking terminology, including the terms "targets", "believes", "estimates", "anticipates", "expects", "intends", "may", "will" or "should" or, in each case, their negative or other variations or comparable terminology. By their nature, forward-looking statements involve risks and uncertainties because they relate to events and depend upon circumstances that may or may not occur in the future. Forward-looking statements are not guarantees of future performance. Resolution's actual performance, results of operations, internal rate of return, financial condition, liquidity, distributions to shareholders and the development of its acquisition, financing and restructuring and consolidation strategies may differ materially from the impression created by the forward-looking statements contained in this announcement. Forward-looking statements in this announcement are current only as of the date of this announcement. Resolution undertakes no obligation to update the forward-looking statement it may make. Nothing in this announcement should be construed as a profit forecast.

Media

There will be a conference call today for wire services at 07.30 (BST). Dial in telephone number: UK Local call 0844 493 3800, UK Standard International +44 (0)1452 555 566 Passcode: 25283960.

Analysts/Investors

A presentation to analysts will take place at 09.30am (BST) at the London Stock Exchange, 10 Paternoster Square, London EC4M 7LS. Dial in telephone number: 0800 368 0649, UK standard International +44 (0)203 059 8125, *participant password: Resolution.

A webcast of the presentation and the presentation slides will be available on Resolution’s website, www.resolution.gg.

In accordance with the obligations for issuers of listed debt contained in the Disclosure and Transparency Rules, Friends Life Group plc will issue a separate half year results announcement later today.

Financial calendar

Third quarter 2013 interim management statement	12 November 2013
Full year 2013 results	18 March 2014
First quarter 2014 interim management statement	7 May 2014
Half year 2014 results	6 August 2014
Third quarter 2014 interim management statement	11 November 2014

2013 interim dividend

Dividend amount	7.05 pence per share
Ex-dividend date	4 September 2013
Record date	6 September 2013
Final date for DRIP elections	13 September 2013
Dividend payment date	4 October 2013

Website: www.resolution.gg

*Password must be quoted to operator to gain access to the conference.

Chairman's statement

Overview

The half year 2013 results, the first since I became Chairman of the simplified Group in May 2013, show strong performance in a number of areas. I am delighted with what we have achieved over the last six months while maintaining our focus on customers. The operating performance of the Group has been strong and shows the impact of the Group's continued delivery of value over volume.

The Heritage business, representing the majority of the existing books of business, continues to be the cash engine of the Group. The UK division, which comprises the Corporate Benefits, Protection and Retirement Income businesses, has made good progress towards financial targets reflecting ongoing operational improvements underpinned by improving efficiency of cash usage. We also continue to deliver the targeted cost savings.

I am pleased with the progress made on the operational turnaround of the International business, and a controlled exit will have been made from all non-core businesses by the end of the third quarter of 2013. Notwithstanding the moderate operating drag incurred while we complete this exercise, I am delighted to note the payment of internal interim dividends amounting to £10 million (Lombard £4 million and Friends Provident International ("FPI") £6 million) in July 2013.

The Chief Executive and Chief Financial Officer's statements that follow, together with the business review, contain a more comprehensive account of the first half of 2013.

Dividend

The Company's dividend policy remains unchanged and is an absolute amount determined by the Board, currently 21.14 pence per share per annum which is in line with dividends declared in respect of 2012. Consistent with the policy of dividends being paid one-third in respect of the interim dividend and two-thirds in respect of the final dividend, the Board has declared an interim dividend of 7.05 pence per share. The Company will consider moving to a progressive dividend when sustainable cash generation meets its £400 million per annum distributable cash target.

Capital

The Group maintains a strong capital position. The Board is confident that the Group remains well capitalised on both regulatory and economic bases.

Outlook

The Group is making good operating progress and this is supported by our focus on financial and operational discipline. The performance in the first half of 2013 further underpins the Board's confidence in the future performance of the Group.

Chief Executive's Review

We have continued to make excellent progress over the last six months, particularly in increasing sustainable free surplus ("SFS"), a key driver of cash generation, which was up by 23% to £147 million without compromising the strong capital base. The Heritage division continues to be the cash engine of the Group and our focus has moved from capital optimisation to generating incremental cash and value. Our core new business franchises have delivered strong value of new business ("VNB") growth as we continue to write profitable new business for future cash generation.

Despite continued macroeconomic uncertainty in the wider environment, the first half of 2013 saw signs of economic recovery and was marked by an improvement in asset prices with a strong rally in equity markets in particular, before falling back in June.

We are also starting to see the benefits of the International strategy announced in November 2012 with orderly exits from non-core businesses and the payment of dividends amounting to £10 million in July 2013.

The outlook for the Group remains very attractive and we are well-placed to take advantage of key demographic and regulatory trends in our chosen markets.

1. Strategy

The strategic aim of the Group is unchanged and remains focused on developing a sustainable business that meets the needs of customers and delivers cash and appropriate returns to shareholders. The UK has an ageing population, with reducing state support and a significant need to increase pension provision. The Group's products address these structural issues, as well as meeting customer needs for support for themselves and their families if they die or fall ill. The Group benefits from its existing book of business and the natural synergies that exist between its chosen business lines. In particular, the Heritage division and Corporate Benefits business provide a strong source of future new business for the Retirement Income business. At the same time the Group maintains a robust, low risk balance sheet, improving sustainable cash flow generation, and writing profitable new business to ensure future cash flow generation.

The goal across the UK and International divisions is to achieve higher returns on new business written and in this way to replenish the run-off of the existing book of business managed by the Heritage division. The focus of the Heritage division continues to be on disciplined management of the existing book to deliver cash and manage capital effectively. Turning embedded value into cash takes skilled management and we have a separate, dedicated management team, focused on managing the in-force book of business efficiently in order to deliver cash to the Group. In the UK division, the Group focuses on three core product areas (Corporate Benefits, Protection and Retirement Income) where we believe that we have competitive advantage and scale, and can thereby achieve attractive returns.

The International division is well placed to benefit from growth in global wealth, in line with the strategy we set out in late 2012. Friends Provident International ("FPI") serves expatriates globally and domestic affluent customers in selected markets (Hong Kong, Singapore and Dubai). Lombard continues its existing strategy focused on estate planning for high and ultra high net worth individuals through its private bank distribution in Europe and through targeted expansion in other regions.

2. Market environment

Long term interest rates across a number of countries have fluctuated throughout June and July 2013 but generally started to increase modestly suggesting that the markets are starting to price in economic recovery and the end of quantitative easing. However, in the medium-term a relatively low interest rate environment is expected to persist, as global central banks maintain their focus on loose monetary policy to stimulate economic growth. This continues to present a challenge to the Group as persistent lower interest rates impact the ability of the business to generate free surplus.

The first half of 2013 was characterised by a strong rally in UK equity markets underpinned by quantitative easing in the UK and the US, the avoidance of the US fiscal cliff, and dissipation of fears over the Eurozone. Nonetheless, the economic recovery in the UK remains fragile as evidenced by the equity falls in June and interest rates remaining very low by historical standards.

On 1 April 2013, the Financial Services Act came into force. The Act provides for dual supervision of UK insurance companies by two new regulators: the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA"). The regulatory environment continues to be robust for insurance companies and we maintain a healthy, open and constructive relationship with our regulators.

We remain well placed to benefit from the key market trends. The corporate benefits market is large and growing as a result of the structural shift from defined benefit pension schemes towards defined contribution and from the introduction of auto-enrolment which will improve the living standards of millions of people as they retire. Our Retirement Income business also benefits from these trends, and from the demographic forces that will bring an increasing number of people, and volume of funds, to retirement income over the next decade. The UK protection market is mature, concentrated and has remained relatively stable over the past few years.

Consistent with its strategy, the International division is focused on affluent domestic and expatriate clients in markets where there are strong external drivers for growth. In Lombard's core markets across Europe, despite an uncertain legal and tax environment, the longer term demand for individually structured Privatbancassurance solutions remains compelling. The core markets for FPI of North Asia, South-East Asia and the United Arab Emirates show strong medium term growth prospects.

3. Operational performance

Financial performance during the first half of 2013 continued to demonstrate execution of our strategy, driving strong progress in sustainable free surplus generation and higher returns on new business written in the UK division, as we manage a controlled exit from non-core International segments.

The Heritage division continues to be the main driver of sustainable free surplus generation, with substantial embedded value in products which are no longer actively marketed. We are constantly seeking new initiatives to generate incremental cash and value for the Group and the Heritage division is currently engaged in a significant range of initiatives to deliver cash from the existing book of business, including improving cost efficiencies, removing some of the inefficiencies in the capital structure and managing the Group's assets more effectively. A good example is the continued development and expansion of Friends Life Investments ("FLI"), which, whilst only launched in July 2012, now has £18 billion of fixed income assets under management, including £7 billion recaptured in the first half of 2013.

The focus of the division has moved to generating incremental cash from the Heritage book. One initiative is a potential deal to reallocate annuity reserves, currently within the with-profits funds, to the non-profits fund. We expect the reallocation of circa £2 billion of reserves to complete in the second half of 2013, subject to regulatory approval. The expectation is that this will deliver circa £10 million per annum sustainable free surplus benefit from 2014 at a cost of circa £(20) million of sustainable free surplus in the second half of 2013. We will continue to consider further de-risking proposals for the Heritage with-profits funds, balancing the needs of customers and shareholders and leveraging the skills of our dedicated divisional management team.

In Corporate Benefits, our assets under management have increased by nearly 11% to £20 billion and VNB has improved by 30% to £13 million. Second quarter performance exceeded our expectations and I am pleased to see that our pipeline of new schemes is nearly three times higher than at the same point in 2012.

In Retirement Income we have improved both our product proposition and the effectiveness of our customer engagement with a new dedicated retirement team, and as a result are well positioned to help a growing generation of retirees with their retirement plans. In the first half of 2012 we launched our own enhanced annuity to our internal vestings customers and expect to launch a version of this proposition to the open market in the fourth quarter of 2013. Margins remained very attractive in the first half of the year. Premium volumes increased by 73% to £324 million, and the value of new business is up 76% to £44 million. Sales have benefited from both improved retention rates of 32% and an initiative to redirect annuity business previously written in the with-profits funds to non-profit funds.

Group protection sales continue to deliver strong profitable growth, offset by lower sales of individual protection products where the gender neutral pricing directive drove higher volumes of business towards the end of 2012, depleting the pipeline of applications that carried on to 2013. I am extremely pleased that all of our business is now written on our target platforms which offer a better service for our customers at a lower cost of administration to the Group, however the competitive environment continues to be challenging. We are therefore continuing to generate distribution opportunities through existing and new partners including a new long-term protection partnership with Virgin Money starting from January 2014.

The International division is starting to see the benefits of last year's strategic review with the completion of the sale of AmLife in January 2013 and a further focus on core markets. I am pleased to note that Lombard has contributed an interim dividend of £4 million and FPI a first ever dividend of £6 million, both paid to the Group in July.

The results of FPI are impacted by the timing of the strategic review in 2012. Changes to assumptions were reflected only in full year 2012 financial statements, and therefore half year results are not directly comparable. In FPI, we have managed an exit or are in a controlled withdrawal from all of the non-core markets which we had identified as being unprofitable or outside our acceptable risk parameters. In Germany, fpb AG (the Group's distribution business) has extended its distribution agreement with Cardea to replace FPI's regular pension products. The process of transitioning to Cardea's pension products is expected to complete in the third quarter of 2013. The core business, focused on the growth in global, and particularly Asian, wealth, has seen assets under management increase by 10% to £6.7 billion.

Lombard has performed well in a challenging market with flat value of new business on sales down 11% on a constant currency basis (8% in sterling) in a highly uncertain market environment. Assets under management for Lombard increased slightly to €23.5 billion.

4. Capital

The Group continues to maintain a robust low risk balance sheet and deliver improvements in sustainable free surplus generation, underpinned by an IGCA surplus of £2.1 billion, representing a 222% coverage ratio.

5. Progress on medium-term targets

As indicated previously, progress towards the distributable cash target ("DCT") and the target level of ROEV has been impacted adversely by the fall in interest rates since the targets were announced in 2010. The expectation of relatively low interest rates in the medium term continues to present a challenge to the Group by depressing the emergence of free surplus from the in-force book and reducing the returns available on shareholder assets.

Notwithstanding this challenging economic headwind, the Group continues to pursue achievement of the DCT and ROEV targets in the medium term with the balance of the business and the strategic aims of the divisions firmly aligned with the targets and the drivers of value.

In the first six months of the year, the increase in sustainable free surplus reflects a significant reduction in the investment in new business without compromising the profitability of the new business we write in our chosen markets. This has contributed to improving cash emergence and is a key requirement for improving ROEV.

The level of ROEV is an important driver of market value for life insurance companies. The key drivers of ROEV are the value of new business, investment market conditions and the absolute level of interest rates. Interest rates remain at historically low levels which inevitably cause a drag on ROEV. Over 2013 Resolution has further grown its new business contribution, extracted value from its back book and continues to see benefits from its new asset management strategy. The building blocks of growing our ROEV are fully embedded in our plans and are increasingly visible in our results.

6. Outlook

The Group's priorities in 2013 remain the execution of the Heritage, UK and International divisional strategies, the application of rigorous financial discipline to the management of in-force policies and the writing of profitable new business.

In this way the Group aims to deliver attractive returns for shareholders and positive customer outcomes.

Chief Financial Officer's review

1. Summary

The Group's strategy over the last 18 months has been clear, with a focus on delivering cash generation today, profitable new business and securing cash generation for the future. These principles continue to direct the Group's progress and I am pleased that many of our performance metrics reflect the delivery against these strategic objectives over the first half of 2013.

The focus throughout 2012 on the structure and implementation of the UK and Heritage divisions has delivered notable improvements across these strategic fronts. In particular, it is important to recognise the progress made on new business profitability over the last few periods, with the value of UK and Heritage new business at £81 million in the first half of 2013 over 2.8 times that achieved in the first half of 2011.

Underlying this growth the UK division has delivered VNB of £89 million in the first half of 2013, up 41% on the same period in 2012, and is well on course to reach the UK target of £155 million. Of course there remain some challenges, but notwithstanding this we believe that the focus on value rather than volume has been critical in the delivery of the improved performance of the Group and this focus will continue over the remainder of 2013 and beyond.

The other key area of our recent focus has been the reshaping of our International division, the strategy for which we set out in November 2012. To date, good progress has been made with its implementation, with many of the structural outcomes now in place. The benefits of these changes, as with those delivered in the UK over the last few years, will emerge over time. Our confidence of this is reflected in the payment of interim dividends amounting to £10 million in July 2013 (Lombard £4 million and FPI £6 million) in line with expectations.

In FPI, activities to rebase the business are progressing well, although the impact of these has made comparison to 2012 less meaningful. The withdrawal from non-core markets is apparent in the 2013 results, with new business volumes significantly down on the same period in 2012 following the decision to no longer accept new business from Japanese nationals, the closure to new corporate pensions business and the sale of AmLife. As expected, the 2013 results include a modest operating drag as the business undertakes the controlled withdrawal from writing pensions business in Germany. This withdrawal will be complete by the end of September 2013 and supports the Group's expectation that the operating drag from non-core businesses in 2013 will be short lived.

2. Operating results

£m (unless otherwise stated)	**2013 Half year**	2012 Half year	2012 Full year
IFRS based operating profit	**191**	163	274
IFRS based operating earnings per share	**13.26p**	11.32p	19.84p
Sustainable free surplus	**147**	120	300
MCEV operating profit	**214**	235	382
MCEV new business margin	**2.8%**	2.4%	2.4%

The Group operating performance continues to reflect the focus on cash delivery with improving efficiency of cash usage a key driver of the 2013 results. In the first half of 2013 IFRS based operating profit increased 17% to £191 million (30 June 2012: £163 million) and sustainable free surplus increased 23% to £147 million (30 June 2012: £120 million). These improvements reflect a strong period on period performance and are underpinned by the reduction in the cost of writing new business and the absence of one-off costs incurred in 2012.

The economic environment has continued to be challenging in the early part of 2013. Despite equity markets closing above 2012 year end levels, they remain volatile. In addition, the low interest rate environment persists with opening risk free returns lower than prior periods. The impact of this is particularly noticeable in the Group MCEV operating results where, as highlighted in the 2012 full year results, expected returns have been impacted by the reduction in start of year risk free rates from the 1.35% applied in 2012 to 0.67% in 2013. This reduction in rates is broadly mirrored across all asset types and the impact has more than offset the benefit from growing value of in-force in the second half of 2012.

IFRS based operating profit

In our UK and Heritage divisions, IFRS based operating profit of £129 million was £8 million lower than in the first half of 2012. Comparatively however, these results are of better underlying quality with the 2013 results up £20 million after the exclusion of principal reserving changes and one-off items in both periods. Key to this growth has been the focus on reducing the cost of new business. UK and Heritage IFRS new business strain has reduced significantly to £15 million (30 June 2012: £41 million) and includes a strong positive contribution from the Retirement Income business of £21 million as well as the benefits from the migration of new business to the target platforms and lower acquisition costs. Within in-force surplus, the higher equity markets over the first six months have resulted in higher annual management charges.

The International IFRS operating profit in the first six months amounted to £74 million, up £43 million on the same period in 2012. This has been driven by higher income levels as the in-force book grows and positive economic variances resulting in a reduction in guarantee provisions. Additionally, the result has benefitted from an uplift of £10 million in premium margin across certain non-core in-force products, expected to reduce going forwards, and the absence of one-off costs incurred in the comparative period principally relating to the strategic review.

The factors noted above have combined to improve the operating earnings per share by 17% to 13.26 pence.

Sustainable free surplus

The UK and Heritage divisions contributed £178 million to Group sustainable free surplus, up 11% on the same period in 2012. The principal driver, as in the IFRS result, has been the significant reduction in cost of writing new business, validating the Group's strategy in recent periods.

UK and Heritage in-force surplus generation is up in the period with the prevailing economic factors resulting in broadly offsetting impacts. The £263 million surplus generated from the in-force book is higher than the run-off expectation set out at the 2012 year end (annualised £500 million for 2013). However, £13 million of this relates to a spike in With Profits fund maturities.

As we set out in 2012, the expected cash flow contribution from the 2012 in-force book is set to decrease by circa £25 million between 2013 and 2014. This is a key area of focus for the Group with a number of initiatives underway to replenish this run-off. To date, these include the expected benefits from the with-profits annuity transfer (circa £10 million per annum) and an additional £5 million benefit delivered by FLI. The combination of these actions and surplus generated from new business is driving increased confidence in replenishing future run-off.

The contribution to sustainable free surplus from the International division is also up on the same period of 2012 by £14 million. Within the core businesses, an improvement of £3 million reflects growth of Lombard's book and the non-recurrence of one-off costs spent in 2012, partially offset by lower volumes of regular premium savings business written in FPI in 2012. The non-core sustainable free surplus has improved by £11 million principally reflecting the reduced volumes in these businesses. As highlighted below the contribution from non-core businesses includes some modest operating drag, amounting to £(16) million of investment in new business in the first half of 2013.

MCEV operating profit

The UK and Heritage divisions' MCEV operating profit of £241 million is marginally below the first half result in 2012 (30 June 2012: £249 million) and as expected reflects the ongoing challenge presented by reduced in-force returns in a low interest rate environment. In the first half of 2013, lower expected returns reduced the MCEV operating result by £(34) million although this has largely been offset by positive performances elsewhere. These include the continued growth in new business contribution from the UK division, up 41% to £89 million, and a £34 million benefit from recognition of reduced investment expenses as FLI manages more assets in-house.

In contrast, the International division MCEV operating result is down from £43 million to £21 million for the six months ended 30 June 2013. This reduction is largely a result of the impact on new business following the strategic review (highlighted below) as well as the effects of the challenging market and regulatory conditions in Europe. Despite these factors the core International business is now working to a narrower focus and Lombard remains well positioned in its high and ultra high net worth target markets.

The Group new business margin has improved to 2.8% predominately due to substantial improvement in the UK new business margin which has increased from 3.1% to 4.9% with improvement across all UK business units.

3. International non-core business impacts

£m	2013 Half year	2012 Half year	2012 Full year
VNB	**(5)**	8	(12)
Investment in new business	**(16)**	(22)	(62)
APE	**9**	30	56

As previously reported, the strategic actions in 2012 to refocus the International business remain a factor within the 2013 results. Implementation progress remains on track with swift action taken to close certain product lines at the end of 2012. The Group has also made good progress on the controlled withdrawal from manufacturing for the German market, although this has resulted in an element of ongoing operating drag from this business. This withdrawal is due to complete by the end of the third quarter of 2013 at which point the operating drag is expected to fall away. Excluding the non-core elements, the International businesses are now well positioned to deliver ongoing growth in their core markets.

4. Cost savings

One of the Group's key targets over the last few years has been the delivery of UK and Heritage cost savings. In the first half of 2013, the Group has delivered run-rate cost savings of £119 million, 94% of the 2013 target. A further £35 million cost savings have been contractualised in outsourcing agreements, taking our total secured savings to 96% of our 2015 £160 million target.

Activities to separate our infrastructure from that of AXA UK have supported the delivery of our cost savings. In the six months to 30 June 2013, the Group successfully completed the single largest remaining element of this programme. This challenging piece of the programme was more complex than originally expected, but it has been completed within the revised expectations set out in November 2012. Both the separation and integration programme and the Diligenta outsourcing remain on track and within the guidance previously provided.

5. Balance sheet

The Group has maintained a strong capital position over the period with an estimated IGCA surplus of £2.1 billion at 30 June 2013, representing a coverage ratio of 222% (31 December 2012: £2.2 billion, coverage ratio 221%). The reduction since the end of 2012 principally reflects the payment of the 2012 final dividend in May 2013 which amounted to £200 million. Our economic capital position also remains strong with estimated surplus capital of £3.7 billion representing a coverage ratio of 192%.

The Group continues to manage a highly rated portfolio of corporate bonds and has as an immaterial exposure to peripheral European sovereign debts. The Group holds a shareholder's share of credit default reserve of £0.5 billion to cover the risk of defaults in the corporate bonds backing the Group's annuity portfolios. No defaults have been experienced in the first half of 2013.

Available shareholder cash of £839 million (31 December 2012: £850 million) decreased by £11 million as the contribution from the life companies and increase in cash set aside at holding company level was more than offset by dividends paid to shareholders.

6. Outlook: target delivery

In summary, the Group's performance in the first half of 2013 is pleasing, with the strategic execution delivering results. As expected, economic conditions continue to have some impact on our results, particularly embedded value returns, although this has to a large extent been mitigated by positive actions and strong operational delivery.

The delivery of profitable new business at lower cost validates the important decisions taken in the UK and Heritage divisions over the last 18 months and more recently in the International division.

In our International division we can see the results of the revised strategy taking effect. Actions to exit non-core markets have been swift and will be completed by the end of the third quarter of 2013, leaving the focus of the core business narrowed and results rebased.

Looking forwards, the Group will continue to focus on what it has done best over recent periods and whilst there remain a number of challenges including increased competitive pressure in the individual protection marketplace, we are confident of achieving the vast majority of the financial performance targets set for the end of the year.

Business review

1 Key performance indicators

The Group uses the following key performance indicators:

£m (unless otherwise stated)	**Half year 2013**	Half year 2012	Full year 2012
IFRS based operating profit before tax	**191**	163	274
IFRS profit/(loss) after tax	**61**	(58)	(41)
Sustainable free surplus	**147**	120	300
MCEV(i) operating profit before tax	**214**	235	382
MCEV profit after tax	**321**	296	268
Group embedded value on an MCEV basis	**5,980**	5,939	5,831
FLG operating ROEV(ii)	**6.1%**	6.4%	5.1%
Group available shareholder cash	**839**	619	850
IGCA(iii) surplus capital (£bn)	**2.1**	1.6	2.2
Asset quality(iv) for shareholder related assets	**98%**	97%	97%

- IFRS based operating profit before tax of £191 million is £28 million higher than the £163 million reported in 2012 principally reflecting the reduction in the cost of writing new business, positive economic factors and higher levels of income, and the non-recurrence of one-off costs in the International division. These benefits are partially offset by a lower contribution from principal reserving changes and one-off items.
- IFRS profit after tax of £61 million (30 June 2012: £(58) million) principally reflects favourable investment return variances from narrowing credit spreads and the release of credit default allowances, a lower level of non-recurring costs as the Group nears the completion of the separation and integration projects, the gain on the sale of the Group's 30% stake in AmLife as well as the amortisation of the acquired intangible assets.
- Sustainable free surplus increased by £27 million to £147 million principally reflecting the reduction in the cost of writing new business, reduced volumes in the non-core business and the non-recurrence of one-off costs.
- MCEV operating profit before tax of £214 million (30 June 2012: £235 million) reflects lower expected returns in the ongoing low interest rate environment. These are partially offset by positive assumption changes reflecting the benefits of asset recapture in FLI.
- MCEV profit after tax of £321 million is higher than the £296 million reported in the first half of 2012 principally reflecting lower non-recurring costs.
- Group embedded value on an MCEV basis of £5,980 million (31 December 2012: £5,831 million) is up by £149 million with both the operating performance and positive economic variances partially offset by dividend payments in respect of 2012.
- FLG operating ROEV of 6.1% (30 June 2012: 6.4%) reflects lower expected returns in the low interest rate environment.
- Group available shareholder cash of £839 million (31 December 2012: £850 million) is at a similar level to end 2012, and reflects dividends paid to shareholders and the contribution from life companies in the first six months.
- IGCA surplus capital of £2.1 billion (31 December 2012: £2.2 billion) represents a coverage ratio of 222% (31 December 2012: 221%).

- The Group has maintained high asset quality, with 98% of shareholder-related corporate debt and asset backed securities at investment grade or above (31 December 2012: 97%). The Group has no significant shareholder exposure to sovereign debt or corporate bonds of higher risk European economies. No defaults were recorded in the period and the shareholder's share of default provisions amounted to £0.5 billion.

(i) The MCEV basis is in compliance with the European Insurance CFO Forum MCEV Principles ("MCEV Principles") (Copyright© Stichting CFO Forum Foundation 2008), issued in June 2008, and re-issued in amended form in October 2009.

(ii) Friends Life Group ("FLG") operating ROEV is calculated on an annualised basis as the MCEV operating return, after tax and financing, divided by the start of period net embedded value, and is adjusted to allow for the timing of significant capital movements such as dividends and acquisitions.

(iii) IGCA is presented at Resolution Holding company level.

(iv) Corporate debt and asset-backed securities at investment grade.

2 Group results

2.1 Group IFRS results

The Group's IFRS results are set out below, including a reconciliation from IFRS based operating profit to the IFRS result after tax. The Group uses the operating profit measure as its key IFRS metric as the Board considers that this better represents the underlying performance of the business and the way in which it is managed.

£m	**UK & Heritage**	**International**	**Corporate**	**2013 Half year**	2012 Half year	2012 Full year
New business strain	**(15)**	**(40)**	**-**	**(55)**	(83)	(142)
In-force surplus	**203**	**116**	**-**	**319**	275	550
Long-term investment return	**(32)**	**-**	**1**	**(31)**	(17)	(23)
Principal reserving changes and one-off items	**(1)**	**3**	**-**	**2**	27	(23)
Development costs	**(21)**	**(5)**	**-**	**(26)**	(22)	(50)
Other income and charges	**(5)**	**-**	**(13)**	**(18)**	(17)	(38)
IFRS based operating profit before tax	**129**	**74**	**(12)**	**191**	163	274
Short-term fluctuations in investment return				**133**	18	275
Gain on sale of associates (AmLife)				**20**	-	-
Other non-recurring items				**(57)**	(118)	(258)
STICS interest adjustment to reflect IFRS accounting for STICS as equity				**16**	16	31
IFRS profit before acquisition accounting adjustments and shareholder tax				**303**	79	322
Amortisation and impairment of acquired in-force business				**(192)**	(204)	(417)
Amortisation and impairment of other intangible assets				**(41)**	(42)	(97)
IFRS profit/(loss) before shareholder tax				**70**	(167)	(192)
Shareholder tax				**(9)**	109	151
IFRS profit/(loss) after tax				**61**	(58)	(41)
Total net assets				**5,562**	5,783	5,698

Operating profit

The Group IFRS based operating profit in the period to 30 June 2013 totalled £191 million compared to £163 million in the same period of 2012. This improvement principally reflects the reduction in the cost of writing new business, positive economic factors and higher levels of income, in addition to the non-recurrence of one-off costs in the International division. These benefits are partially offset by the lower contribution from principal reserving changes and one-off items.

A summary of the Group's operating performance is provided in the Chief Financial Officer's review. Further details of the operating performance of the Group's divisions are included in the relevant operating reviews below.

Non-operating items

Short-term fluctuations in investment returns, on assets backing the shareholder and non-profit funds, were a favourable £133 million in the period to 30 June 2013. This benefit mainly reflects the narrowing of credit spreads and the release of credit default allowances.

Gain on sale of associates of £20 million reflects the profit on the sale of the Group's 30% stake in AmLife (AmLife Insurance Berhad and AmFamily Takaful Berhad), which was completed on 4 January 2013.

Other non-recurring items of £(57) million include:

- separation and integration programme costs, net of provision releases, of £(10) million;
    - the cumulative spend on the separation and integration projects amounted to £(267) million (31 December 2012: £(257) million).
- outsourcing implementation costs of £(30) million;
    - costs incurred to date in respect of Diligenta outsourcing implementation total £(155) million with total implementation costs expected to be in the region of £(280) million.
- finance transformation costs of £(10) million largely relating to Solvency II; and
- costs of the capital optimisation programme of £(7) million.

A shareholder tax charge of £(9) million is recognised for the period and includes £50 million tax credit in relation to the amortisation and impairment of AVIF and other intangibles in the period.

At 30 June 2013, IFRS total equity was £5,562 million (31 December 2012: £5,698 million), with equity attributable to equity holders of the parent of £5,233 million (31 December 2012: £5,377 million). IFRS net assets per share attributable to shareholders were £3.69 (31 December 2012: £3.79) based on shares in issue at the balance sheet date.

2.2 Group free surplus generation

The generation of free surplus, net of movements in required capital, underpins the declaration of future dividends. The table below analyses the free surplus result after tax for the period.

£m	UK & Heritage	International	Corporate	2013 Half year	2012 Half year	2012 Full year
Expected return from in-force business	**272**	**79**	**-**	**351**	348	668
Investment in new business	**(58)**	**(52)**	**-**	**(110)**	(157)	(285)
Underlying free surplus generation	**214**	**27**	**-**	**241**	191	383
Development costs	**(15)**	**(5)**	**-**	**(20)**	(20)	(38)
Coupon on external debt	**-**	**-**	**(45)**	**(45)**	(35)	(73)
Coupon on internal debt	**-**	**-**	**-**	**-**	(7)	(12)
	199	**22**	**(45)**	**176**	129	260
Operating experience variances	**(15)**	**(2)**	**-**	**(17)**	(23)	(31)
Other operating variances	**-**	**(2)**	**-**	**(2)**	16	86
Other income and charges	**(6)**	**-**	**(4)**	**(10)**	(2)	(15)
Sustainable free surplus generation	**178**	**18**	**(49)**	**147**	120	300
Operating assumption changes	**-**	**(11)**	**-**	**(11)**	-	(68)
Operating free surplus generation	**178**	**7**	**(49)**	**136**	120	232
Economic variances				**62**	6	120
Capital optimisation programme				**-**	-	101
Other non-operating items				**(114)**	(82)	(208)
FLG free surplus generated				**84**	44	245
RSL income and charges				**(10)**	(15)	(30)
Total free surplus generated				**74**	29	215

Sustainable free surplus

Sustainable free surplus generated in the period was £147 million, up 23% on the £120 million generated in the prior period. The increase reflects a reduction in the cost of writing new business in the UK and Heritage divisions, reduced volumes in the non-core FPI business and the non-recurrence of one-off costs in the International division.

A summary of the Group's operating performance is provided in the Chief Financial Officer's review. Further details of the operating performance of the Group's divisions are included in the relevant operating reviews below.

Other free surplus movements

In the period to 30 June 2013, operating assumption changes within International, primarily in respect of changes to the capital requirements, reduced free surplus by £11 million.

Positive economic variances of £62 million increased free surplus, principally driven by the impact of narrowing credit spreads on assets backing the annuity business. Other non-operating items include £(89) million in respect of a provision made to meet the deficit reduction plan for the Group's defined benefit pension scheme, bringing the total provision to £(108) million, equivalent to 5 years of the 10 year funding plan; and £(25) million in respect of non-recurring costs.

Available shareholder cash

£m	**2013 Half year**	2012 Half year	2012 Full year
Opening available shareholder cash	**850**	853	853
Dividends from life companies declared in the period	**110**	100	354
Dividends to shareholders	**(200)**	(150)	(193)
DCN repayment and interest	**-**	(88)	(423)
Corporate costs and other	**79**	(96)	(89)
Issue of UT2 reset perpetual debt (net of costs)	**-**	-	348
Closing available shareholder cash	**839**	619	850

Available shareholder cash ("ASC") represents cash available to cover corporate costs, to service debt issued by holding companies and, subject to shareholder approval, to pay dividends. ASC provides a buffer, firstly to ensure that sufficient cash is available to meet the next 12 months dividend commitments and secondly to enable the Group to continue to grow its sustainable free surplus in line with its medium term business plan in volatile investment markets.

Dividends declared by Friends Life Limited ("FLL"), and due for payment to FLG later in 2013 totalled £110 million, and this gives the contribution to the distributable cash target ("DCT") for the period. This dividend includes dividends declared by the International subsidiaries (FPIL and Lombard) totalling £10 million in the period. Free surplus generated within the long term funds of the life companies does not contribute to ASC until the year end actuarial valuation has been completed and any transfers agreed.

Other movements in ASC comprise corporate cash flows, including external interest payments net of interest received from life companies, and changes in the amount of cash set aside at holding company level to fund working capital requirements. In 2012, this included the provision in working capital for deficit reduction contributions for the Group's pension scheme. This has been released in the period as the deficit reduction contributions have now been provided for in the life companies (reducing free surplus).

Dividends

The Company's dividend policy can be summarised as being an absolute amount determined by the Board, currently 21.14 pence per share per annum, with the expectation that a progressive dividend would be considered once sustainable cash generation reaches the £400 million per annum distributable cash target. The Company expects to pay one-third of the total annual dividend as an interim dividend and two-thirds of the total annual dividend as the final dividend.

The interim dividend in respect of the period to 30 June 2013 will be 7.05 pence per share.

2.3 Group MCEV results

MCEV is an alternative accounting basis to IFRS for life assurance companies. MCEV reporting is designed to recognise profit as it is earned over the lifetime of each policy and reflects the future cash flows that are expected to arise from sales in the period, together with the effect of updating the previous period's assumptions on existing business for the actual experience. The total profit recognised under both MCEV and IFRS will be the same over the life of each policy, it is the timing of the recognition of that profit which differs.

The results and financial position of the Group's life and pensions business ("covered business") are presented on the MCEV basis with all other businesses included on an IFRS basis.

£m	**UK & Heritage**	**International**	**Corporate**	**2013 Half year**	2012 Half year	2012 Full year
Value of new business	**81**	**16**	**-**	**97**	97	194
Expected existing business contribution	**136**	**27**	**(37)**	**126**	165	325
Operating experience variances	**(14)**	**(17)**	**-**	**(31)**	(15)	(56)
Operating assumption changes	**34**	**-**	**-**	**34**	14	(9)
Other operating variances	**30**	**-**	**-**	**30**	19	27
Development costs	**(21)**	**(5)**	**-**	**(26)**	(22)	(50)
Other income and charges	**(5)**	**-**	**(11)**	**(16)**	(23)	(49)
MCEV operating profit/(loss) before tax	**241**	**21**	**(48)**	**214**	235	382
Economic variances				**228**	242	154
Amortisation and impairment of non-covered business intangible assets				**-**	(1)	(15)
Non-recurring costs				**(70)**	(115)	(255)
Other non-recurring items and non-operating variances				**37**	24	128
MCEV profit from continuing operations before tax				**409**	385	394
Tax				**(88)**	(89)	(126)
MCEV profit from continuing operations after tax				**321**	296	268
Net Group MCEV				**5,980**	5,939	5,831
FLG operating ROEV (%)				**6.1**	6.4	5.1

Operating profit

The Group MCEV operating profit in the period to 30 June 2013 was £214 million, £21 million lower than the prior year of £235 million. The results reflect stable performance in the UK and Heritage divisions, where the impact of the reduction in expected returns from the low interest rate environment has largely been offset by continued growth in new business. This was offset by a lower contribution from the International division, primarily driven by the strategic market exits as well as the effects of the challenging economic conditions in Europe.

The FLG operating ROEV, after tax, for the period to 30 June 2013 was 6.1% (31 December 2012: 5.1%) and continues to reflect the low expected returns achievable in the current economic environment. The Group continues to focus on this performance measure and remains committed to the targeted ROEV of 10% in the medium term.

A summary of the Group's operating performance is provided in the Chief Financial Officer's review. Further details of the operating performance of the Group's divisions are included in the relevant operating reviews below.

Non-operating items

Economic variances combine the impact of changes to economic assumptions with the investment return variances over the period. Total economic variances in the first half of 2013 had a £228 million positive impact on MCEV profit before tax. The key positive variances arose from the narrowing of corporate bond spreads and higher than expected movement in the equity markets. Corporate bond spreads narrowed by around 35bps over the period which resulted in an increase in MCEV profit of £189 million, primarily in respect of annuity business in the Heritage division. The equity market movements increased the value of future annual management charges on unit-linked business, resulting in an increase of £164 million. These positive movements were offset by a £(110) million charge from an increase in long term interest rates from low opening levels.

Non-recurring costs in the first half of 2013 total £(70) million and include costs of £(57) million, consistent with those reported within the IFRS result, in addition to net costs of £(13) million specific to MCEV. The £(13) million includes a £(28) million difference between the actual tax relief expected and the notional tax gross up applied to all non-recurring costs under MCEV. The application of these different tax rates results in a higher cost, gross of notional tax, under MCEV than under IFRS. This is partially offset by the release of £15 million of provisions for the Diligenta outsourcing, the AXA separation project and Solvency II under MCEV.

The balance of non-recurring and non-operating variances represent the impact of the additional 1% reduction in the rate of Corporation Tax from 1 April 2015 announced on 20 March 2013.

At 30 June 2013, net Group MCEV was £5,980 million (31 December 2012: £5,831 million) giving MCEV per share of £4.22 (31 December 2012: £4.11).

3 UK and Heritage divisions

Structure

The Heritage division forms the bulk of the UK based business by assets and in-force value and as a result is the principal driver of the Group's surplus generation. The division is focused on the management of products that are no longer actively marketed and is therefore distinct from the activities undertaken by the UK division.

The UK division combines the Corporate Benefits, Protection and Retirement Income business units. These business units are focused on scale markets where good margins are generally available and where the Group has strong market positions enabling access to those margins.

The UK division's results also include intermediary business Sesame Bankhall Group ("SBG"). In February, SBG confirmed that it had appointed advisors to carry out a strategic review.

The operational reviews of these standalone divisions are set out in the sections that follow. The financial metrics for the combined UK and Heritage divisions are shown below.

Half year 2013 operational highlights

- **UK and Heritage IFRS based operating result was £129 million** (30 June 2012: £137 million) with the benefit from lower new business strain being offset by reduced positive one-off items in 2013 compared to 2012.
- **UK and Heritage MCEV operating profit was £241 million** (30 June 2012: £249 million) with continued strong VNB growth offset by materially lower expected returns in the current low interest rate environment.
- **UK and Heritage sustainable free surplus generation up to £178 million** (30 June 2012: £160 million) reflecting reduced levels of free surplus invested in new business.
- **At mid-year 2013, the UK and Heritage divisions have delivered run-rate savings of £119 million** (31 December 2012: £86 million) with a further £35 million secured through contractual arrangements with outsource providers.

£m (unless otherwise stated)	UK	Heritage	2013 Half year	2012 Half year	2012 Full year
IFRS based operating profit before tax	**26**	**103**	**129**	137	300
MCEV operating profit before tax	**95**	**146**	**241**	249	502
Sustainable free surplus (i)	**(4)**	**182**	**178**	160	423
Regular dividends paid to Group(ii)	**n/a**	**n/a**	**250**	250	350
Value of new business	**89**	**(8)**	**81**	67	144
Investment in new business	**(38)**	**(20)**	**(58)**	(98)	(161)
Funds under management (£bn)	**21.6**	**70.9**	**92.5**	86.4	88.4

(i) UK result includes £(5) million of a £(6) million FCA fine in Sesame Limited (£(1) million was included in 2012 results)
(ii) This represents dividends from FLL to Group.

3.1 UK and Heritage divisions, financial performance

UK and Heritage divisions IFRS based operating profit

£m	UK	Heritage	2013 Half year	2012 Half year	2012 Full year
New business strain	**(7)**	**(8)**	**(15)**	(41)	(59)
In-force surplus	**50**	**153**	**203**	196	395
Long-term investment return	**5**	**(37)**	**(32)**	(26)	(40)
Principal reserving changes and one-off items	**2**	**(3)**	**(1)**	27	47
Development costs	**(19)**	**(2)**	**(21)**	(18)	(42)
Other income and charges	**(5)**	**-**	**(5)**	(1)	(1)
IFRS based operating profit before tax	**26**	**103**	**129**	137	300

The 2013 half year UK and Heritage IFRS based operating profit of £129 million is £(8) million lower than in 2012, with the improvement in IFRS new business strain, following the continued focus on target new business platforms and lower costs, being offset by reduced principal reserving changes and one-off items compared to 2012. New business strain is incurred evenly across the divisions despite the majority of new business being written in the UK division. This reflects the £21 million positive contribution from annuity business which is largely written in the UK division.

In-force surplus has improved primarily as a result of the higher management charges received on unit-linked business reflecting the improved equity markets in 2013. However, the change in the long-term investment return has offset this due to lower interest rates on shareholder assets and higher internal debt costs paid to the Corporate segment, following the $575 million UT2 debt issued in November 2012. The Heritage division meets all of these internal debt costs.

Other income and charges includes £(5) million of a £(6) million FCA fine on Sesame Limited (of which £1 million was provided in the 2012 full year results).

Operating expenses

In November 2012, the Group announced an increase in the cost savings run-rate target to £160 million by the end of 2015 with savings to be achieved by the end of 2013 also increased to a run-rate of £126 million.

At 30 June 2013, the UK and Heritage divisions have delivered run-rate savings of £119 million (31 December 2012: £86 million) with a further £35 million secured through contractual arrangements with outsource providers. In total, savings equate to 96% of the £160 million 2015 target. The increase in realised synergies is due primarily to the successful implementation of the IT infrastructure separation programme from AXA, enabling reduced IT service costs.

The Group expects to deliver its 2013 target of £126 million through the completion of in-flight savings initiatives and maintaining controls over operational costs. In 2014 and 2015, the delivery of the £160 million target remains aligned to the realisation of contractualised savings already secured.

£m	2013 Half year	2012 Half year	2012 Full year	2010 Full year baseline[i]
Acquisition	**67**	77	150	220
Maintenance	**134**	141	293	256
	201	218	443	476
Development	**21**	18	42	23
Total	**222**	236	485	499

(i) 2010 full year baseline includes an estimate of 12 months operating expenses for AXA UK Life Business, BHA and the acquired WLUK business.

Development costs continue to be incurred on building propositional changes to the UK and Heritage businesses with the level of development spend this year focusing on developing the Group's annuities capability, new product launches and some continued spend on auto-enrolment across UK and Heritage.

UK and Heritage divisions MCEV operating profit

£m	UK	Heritage	2013 Half year	2012 Half year	2012 Full year
Value of new business	**89**	**(8)**	**81**	67	144
Expected existing business contribution	**30**	**106**	**136**	170	342
Operating experience variances	**-**	**(14)**	**(14)**	3	(21)
Operating assumption changes	**-**	**34**	**34**	9	62
Other operating variances	**-**	**30**	**30**	19	19
Development costs	**(19)**	**(2)**	**(21)**	(18)	(42)
Life and pensions covered business operating profit before tax	**100**	**146**	**246**	250	504
Other income and charges	**(5)**	**-**	**(5)**	(1)	(2)
MCEV operating profit before tax	**95**	**146**	**241**	249	502

The UK and Heritage MCEV operating profit of £241 million is £(8) million lower than the £249 million reported in 2012, with an increase in value of new business and favourable operating assumption changes being offset by the expected material reduction in expected existing business contribution.

The contribution from new business has improved with the £81 million reported in 2013 representing a 21% improvement on the same period last year. The improvement in new business profitability has been driven by lower costs due to a higher proportion of new business now being written on target platforms and continued focus on value over volume.

MCEV operating profit includes an expected existing business contribution which is calculated with reference to risk free interest rates. As advised previously, expected existing business contribution has reduced significantly compared to the same period in 2012 to £136 million (30 June 2012: £170 million), due to material reductions in the level of expected rates of return on all asset classes in line with the rates reported at year end 2012. The rates applied to the opening balance sheet are shown below with the cash and gilt rate halving to 0.67%.

	Rates used for expected return contribution	
%	**2013**	2012
Reference rate (non annuity business)	**0.67**	1.35
Reference rate (annuity business)	**1.42**	2.25
Best estimate returns:		
Corporate bonds(i)	**2.25**	3.30
Cash/Government Bonds	**0.67**	1.35
Equity	**4.90**	5.40
Property	**3.90**	4.40

(i) Returns on corporate bonds vary by portfolio with the rates shown being a weighted average.

The £(14) million operating experience variances mainly reflect a strengthening of provisions in respect of a number of operational items. In addition, both the UK and Heritage divisions have experienced persistency impacts as a result of the RDR changes introduced at the start of 2013, with the remaining £(33) million provision set up to cover these expected impacts being fully utilised and materially covering the losses experienced.

A benefit of £34 million has been recognised during the period reflecting revised assumption changes in respect of future investment expenses. This has been enabled by the recapture of certain asset portfolios with these being managed by FLI.

Favourable other operating variances of £30 million principally relate to modelling adjustments, including a £15 million benefit from an increase in deferred tax assets on pension business following a review of methodology.

UK and Heritage divisions sustainable free surplus generation

£m	UK	Heritage	2013 Half year	2012 Half year	2012 Full year
Expected return from in-force business					
Free surplus emergence	**47**	**216**	**263**	249	505
Return on shareholder assets	**2**	**7**	**9**	20	34
Investment in new business	**(38)**	**(20)**	**(58)**	(98)	(161)
Underlying free surplus generation	**11**	**203**	**214**	171	378
Development costs	**(14)**	**(1)**	**(15)**	(17)	(32)
Operating experience variances	**3**	**(18)**	**(15)**	(10)	(6)
Other operating variances	**2**	**(2)**	**-**	16	88
Sustainable free surplus before Sesame	**2**	**182**	**184**	160	428
Sesame	**(6)**	**-**	**(6)**	-	(5)
Sustainable free surplus generation	**(4)**	**182**	**178**	160	423

The UK and Heritage sustainable free surplus generation of £178 million is up 11% on the first half of 2012. Consistent with the IFRS based operating result, this is largely due to an improvement in the investment in new business, reflecting the migration on to the target new business platforms and lower costs.

Expected return from in-force business at £272 million is broadly consistent with that in 2012 despite an £(11) million impact from reduced returns on shareholder assets from lower interest rates. This is offset by higher returns following a spike in with profits maturities.

Operating experience of £(15) million mainly reflects the strengthening of provisions in respect of a number of small operational items, whilst the Sesame result of £(6) million largely relates to the FCA fine.

3.2 Heritage division

Half year 2013 operational highlights

- **Service improvement programme progressing well**, including the transfer of IT services in March to Diligenta.
- **A further £7 billion of assets recaptured into FLI**: £18 billion managed by FLI at 30 June 2013.
- **Further internal company structure rationalisation expected to complete this year**, delivering material operational simplification and leaving only two life companies within the UK and Heritage divisions.
- **Agreement, subject to regulatory approval, to reallocate circa £2 billion of annuities from the FLAS and FLC with profits funds into the shareholder owned FLL non-profit fund**, expected to be effective and completed in the second half of the year.

Market environment

The end of 2012 brought significant regulatory change for the UK Life and Pensions market, with the Heritage division's broad range of products being impacted by the Retail Distribution Review ("RDR"), gender neutral pricing and auto-enrolment of occupational pensions. The impact of the RDR on the 2013 results has been materially within the amounts previously provided for although the business remains focussed on further potential impacts as schemes begin to select providers for auto-enrolment staging. Financial conditions have seen a narrowing of credit spreads and improvement in stock markets (that partially reversed in June).

Strategy

The Heritage division serves circa four million customers. It manages a significant proportion of the value of in-force of the Group, relating to a large suite of products that are no longer actively marketed and are administered on complex legacy systems. A dedicated management team focused on the Heritage business is in place, with the aim to be the United Kingdom's leading legacy business manager with the knowledge and expertise to maximise the value created from legacy books.

The value drivers for the Heritage division are:

- operational excellence – focused customer service within an efficient cost base in line with business scale;
- capital efficiency – minimisation of capital required for the business;
- strong product management – maximisation of value generated and retention of business;
- robust financial risk and balance sheet volatility management; and
- in-house asset management – utilising the recently created internal asset management capability to maximise returns and lower costs.

In the context of this strategy, the Heritage division is making good progress towards achieving its strategic outcomes.

The Group's outsourced suppliers continue to provide good service to Friends Life's customers. In March, Friends Life successfully moved a number of IT services (helpdesk, networks, telephony) from an existing supplier to one of the Group's strategic partners, Diligenta (and their parent company TCS). In the second half of 2013, the Group is planning the first major migration from two legacy administration systems onto the Diligenta BaNCS IT platform, representing a key milestone in the deliveries of Friends Life's customer strategy.

The 2013 capital optimisation programme has received initial High Court direction to notify all impacted customers of the proposals to transfer the remaining acquired AXA UK Life Businesses to the separate UK and Heritage companies. Subject to final Court sanctioning of the transfer, this will leave two active life companies within the UK and Heritage group, with all six with-profits funds managed under a single Heritage life company Friends Life Limited ("FLL"). Whilst no material capital release is expected from this initiative, the capital efficiency gains are expected to cover the programme's costs, with the principal benefits achieved through material operational simplification of the Group.

In addition, a multi-year programme to implement a uniform capital management framework for the six with-profits funds is ongoing. As part of that development and the Heritage division's ongoing objective to ensure that with-profit funds remain appropriately invested, a proposal for an initial annuity book reallocation has been agreed between the With-Profits Committee and the Board of FLL. These proposals have also been submitted to the regulators for review before expected reallocation later in 2013. Further de-risking proposals are being developed as part of this programme as well as seeking other value generation opportunities in the Heritage business.

Having been launched in July 2012, FLI now manages £18 billion of fixed interest assets, including a further £7 billion of recaptures in 2013. This has delivered more internal control over the investment performance, together with a material reduction in investment costs, benefitting MCEV operating profit in 2012 by £11 million and in the first half of 2013 by a further £34 million. Work continues to assess further potential recaptures.

Financial performance

Value of in-force business

The Heritage business represents a significant proportion of the Group's in-force value and regulatory capital. There has been no change in the overall value of in-force business. The breakdown by product is shown below.

£bn	**30 June 2013**	31 December 2012
Pensions	**0.4**	0.5
Investments	**0.7**	0.6
Annuities	**0.3**	0.2
Protection	**0.4**	0.5
With-profits	**0.5**	0.5
Total Heritage VIF	**2.3**	2.3

Heritage unit-linked funds under management

The operating performance during 2013 indicates that the lapse experience of the book is performing broadly in line with the business's assumptions other than for unit-linked group pensions, where lapse experience has been worse than expected in the short term due to increased scheme re-broking activity as part of RDR and the new auto-enrolment requirements in 2012-14. This worsened experience is covered by the RDR provision that has been released at the half year in line with previous expectations.

Heritage unit-linked funds under management were up 6% primarily driven by market growth in the period. Net flows however, continue to reflect the maturity of products and are in line with expectations of the Heritage division's run-off strategy.

£bn	Pensions	Investments	Total
1 January 2013	**18.3**	**15.4**	**33.7**
Inflows	0.4	0.1	0.5
Outflows	(1.4)	(0.9)	(2.3)
Net investment return	2.2	1.5	3.7
30 June 2013	**19.5**	**16.1**	**35.6**

New business

£m (unless otherwise stated)	**2013 Half year**	2012 Half year	2012 Full year
Value of new business	**(8)**	4	2
Investment in new business	**(20)**	(30)	(55)
IRR	**(0.9)%**	4.2%	4.6%
APE	**27**	60	102

The Heritage division specifically focuses on those products no longer actively marketed. Despite not actively seeking new business, the Heritage book delivers ongoing incremental business written across all product types. This incremental new business is largely required to retain the existing business, but requires a relatively fixed cost base to support it.

The fall in investment in new business reflects the lower sales volumes and corresponding reduction in Heritage capital costs, with the balance reflecting the relatively fixed cost base of the division.

The contribution from Heritage new business in 2013 was a loss of £(8) million compared to a profit of £4 million in 2012. This reduction reflects 2012 being the final year of Department of Work and Pensions ("DWP") rebate new business, following regulatory changes. The 2012 full year VNB for DWP business was £13 million with £8 million in the first half of 2012.

Outlook

During the second half of 2013, planned actions include the first major migration from two legacy administration systems onto the Diligenta platform, and completing the final stage of the Part VII initiatives to leave only two active UK territory life companies.

The Group also expects, subject to regulatory approval, to conclude on the reallocation of a circa £2 billion annuity book to a shareholder backed fund. The financial impact will depend on achievement of asset allocation changes over coming months and market conditions at year end. However, within sustainable free surplus where the impact allows for the target investment mix, a reduction of circa £(20) million in the second half of 2013 is anticipated followed by an increase of circa £10 million per annum from 2014 onwards.

3.3 UK division

Half year 2013 operational highlights

- **Value of new business up 41% to £89 million** driven by a focus on the most profitable lines, commission restructuring and a continued focus on cost control.
- **Cost of investment in new business down 44% to £38 million** with continued strong performance by the Protection and Retirement Income businesses and solid progress made re-structuring the commission arrangements on individual schemes within Corporate Benefits.
- **Sales APE of £324 million down from £354 million** in the first half of 2012. The Retirement Income business has shown strong growth, whilst volumes for Corporate Benefits are lower as a result of a deliberate shift in strategy away from high volume low margin business. Protection sales are broadly flat with lower, post-gender neutral volumes of individual protection business offset by higher volumes of group protection.
- **Corporate Benefits assets under administration up to £19.7 billion (31 December 2012: £17.8 billion)** with new scheme sales pipeline at nearly three times the level at the equivalent time last year. 40 schemes have staged for auto-enrolment in the first half of 2013 with over 150 confirmed as staging in the second half.
- **New long-term protection partnership with Virgin Money starting from January 2014** including the distribution of a suite of high-quality simple protection products in-store, over the phone and online.

Structure

The UK division comprises three business lines:

- Corporate Benefits is a Workplace Savings business specialising in Trust and Contract based pensions and workplace ISAs;
- Protection specialises in individual and group, Critical Illness, Income Protection and Life Cover products; and
- Retirement Income specialises in Retirement Annuity and other retirement products.

The division brings together the UK-based, market-facing businesses and enables better operational efficiencies and management of costs and capital between these business lines as Friends Life rationalises and optimises pricing, capital and channel management functions. Additionally, the UK Division expects to take advantage of the natural synergies between Corporate Benefits and Retirement Income in the savings and retirement life-cycle and between Protection and Corporate Benefits in the management of the Group's corporate customers.

Market environment

The UK businesses operate in markets with distinct features and different recent regulatory and economic impacts. 2013 has seen the introduction of RDR and auto-enrolment (principally affecting Corporate Benefits), and the effects of gender neutral pricing implemented at the end of last year (affecting Protection and Annuity business); all against a backdrop of continued economic pressure.

Corporate Benefits operates in a large, fast-growing but low-margin market with strong price competition. Expectations are that this market will grow from £0.4 trillion to £1.2 trillion by 2020. Currently, market activity continues to focus on auto-enrolment which was introduced in the UK in the latter part of 2012. The business has yet to see significant changes to the distribution landscape following the introduction of RDR with a period of uncertainty anticipated following the pension minister's stated plan to ban consultancy charging. Friends Life does not promote consultancy charging.

The UK protection market is mature, and has remained relatively stable over the last few years despite the turbulent macro-economic climate. Implementation of gender neutral pricing and life tax reforms around the turn of the year have generally resulted in a rise in average market prices although impacts have varied by product. Further, these changes drove significant volumes of peaks and troughs in late 2012 and early 2013. For Friends Life, this drove high volumes of business towards the end of 2012, depleting the pipeline of applications carried into 2013, though over the fourth quarter of 2012 and the first quarter of 2013 the Group's market share was similar to the first three quarters of 2012.

The annuity market experienced significant growth in 2012 and is expected to continue to grow, from £14 billion in 2012 to £40 billion in 2020, driven by demographic trends, including the retirement of the baby boomer generation. Sales in the open market continue to show a strong trend towards enhanced annuities which account for approximately half of total open market sales.

Strategy

Friends Life presented the UK division's strategic agenda at an investor briefing in November 2011 and excellent progress has been made across the division in progressing this agenda.

Friends Life is ready for the opportunities now being presented by the regulatory and market changes. The division has developed auto-enrolment technology which, through automatically assessing employee eligibility and linking employer payroll systems to Friends Life product platforms, eases the legislative and administrative burden on employers, and has been launched with encouraging take up. The division has also completed the range of its innovative Simple Protection propositions in the first quarter of 2013 and will look to strengthen its position through further developments largely aimed at customers who choose to self serve or purchase without advice.

Investment in proposition enhancements continues:

- a new range of default funds launched for auto-enrolling schemes: the 'My Future' solution has attracted interest from a large number of auto-enrolling clients with many already using it;
- the Group has recently announced a partnership with Key Retirement Solutions to provide a 'shopping around' service which will support customers close to or at retirement with options around provider and product type which will be piloted in the second half of 2013;
- planned enhancements to the highly regarded Protect+ range of products are expected to deliver further growth in the value of new business in the second half of the year; and
- retirement income capabilities, including market testing, for an open market offering are well advanced and are planned to launch in the last quarter of 2013.

More than 80% of new group scheme business and all of protection new business is now written on target platforms, while the business continues to focus on profitable growth driven by the provision of market leading products in both individual and group protection – in particular critical illness and income protection; and to selectively write profitable new business within its target range of mid to large group pension schemes.

Financial performance

The UK division delivered improved value of new business up 41% on the first half of 2012, on lower volumes and with reduced Investment in New Business.

£m (unless otherwise stated)	2013 Full year target	**2013 Half year**	2012 Half year	2012 Full year
VNB				
Corporate Benefits	25	**13**	10	21
Protection	80	**32**	28	62
Retirement Income	50	**44**	25	59
Total VNB	155	**89**	63	142
Investment in new business				
Corporate Benefits	n/a	**(20)**		
Protection	n/a	**(21)**		
Retirement Income	n/a	**3**		
Total investment in new business	n/a	**(38)**	(68)	(106)
IRR				
Corporate Benefits	10%+	**7.6%**	6.8%	7.2%
Protection	20%	**15.0%**	9.8%	13.8%
Retirement Income	15%+	**25%+**	25%+	25%+
Total IRR	n/a	**16.7%**	11.2%	13.3%
APE				
Corporate Benefits	n/a	**253**	291	535
Protection	n/a	**39**	44	90
Retirement Income	n/a	**32**	19	44
Total APE	n/a	**324**	354	669

Corporate Benefits: £13 million VNB, 30% increase on prior period

VNB for Corporate Benefits is up 30% despite lower sales volumes and with the VNB for the second quarter being 333% of the first quarter. This momentum is expected to continue driven by the pipeline of new scheme wins and auto-enrolling schemes highlighted below.

Corporate Benefits continues to follow a value based strategy, targeting mid to large sized employers, and shifting focus towards the My Money corporate wrap proposition and away from less profitable lines which drove high volume but low value in the first half of 2012. This strategy is delivering improvements in cash generation, with the business now cash positive when comparing fee income to fully loaded costs.

The first half of 2013 has seen positive experience of auto-enrolment participation despite the slower than anticipated development of this business as more employers exercised their right to defer commencement. Some 40 schemes have staged with Friends Life in the first half of the year with more than 150 further schemes confirmed as staging in the second half, the majority of which are expected to make use of the auto-enrolment hub.

New sales APE on the My Money platform are up 135% against prior period. This growth is set to accelerate in the second half of 2013, with a pipeline of all scheme wins expected to result in premiums in the second half of 2013 at three times the level of new sales in the same period of last year.

Corporate Benefits funds under management

£bn	
1 January 2013	**17.8**
Inflows	1.1
Outflows	(1.1)
Net investment return	1.9
30 June 2013	**19.7**

Fund inflows of £1.1 billion in the first half of 2013 and healthy investment returns have resulted in a strong increase in total assets under administration. Outflows are temporarily high, as expected, with approximately half of the £1.1 billion outflow in the first half in respect of closed lines of business or schemes paying initial commission. Inflows have also been depressed by the low number of new schemes commencing in the first half of the year, but, as above, this is expected to materially improve in the second half of the year.

A provision was made in MCEV at the end of 2011 to allow for an expected peak of adverse persistency experience driven by corporate pensions business being re-broked prior to the implementation of RDR on 1 January 2013. Experience of scheme losses to commission-paying providers in 2012 and the first half of 2013 is broadly in line with the expectations underpinning this provision though there is a small proportion of schemes which may still be affected by the impact of reviews in the run up to RDR. These, combined with the continuing unfavourable economic environment, may lead to some further modest movement in the second half of 2013.

Protection: £32 million VNB, 14% increase on prior period

Following the successful migration to low cost target platforms at the end of last year, all new business is now written on target platforms, delivering significant cost savings and increasing the value of new business.

Group protection volumes continue to deliver strong growth, up 5% on the same period in 2012. Focus on more profitable lines and promotion of flexible benefits continues to deliver positive results with group protection VNB up 58%.

The trajectory for volumes of individual protection is gathering pace with volumes in the second quarter of 2013 up 46% on the first, and value up over 400% over the same period as a result of continuing strong relationships with key partners and distributors.

Retirement Income: VNB of £44 million up 76% on prior period

The Retirement Income business has delivered £44 million of VNB, up 76% on the same period in 2012, with a new business surplus of £3 million.

In conjunction with the Heritage division and reflecting a desire to de-risk the with-profits fund, annuity business previously written in the former AXA with-profit funds has been redirected to non-profit funds. This has made a significant contribution to the increased APE which is up 68% to £32 million in the period. Sales have also benefitted from the launch of the enhanced annuity proposition which was only launched towards the end of the first half of 2012. Retention rates of 32% have been achieved, peaking at over 50% for customers engaging with the enhanced proposition. System enhancements to enable more sophisticated pricing have been implemented facilitating progressive improvements in competitiveness through the first half.

In line with the change implemented at the end of 2012, new business results now include the premium in respect of the cost of the guarantee for policies with guaranteed annuity options accounting for further improvement against the first half of 2012.

Outlook

Relationships with Employee Benefits Consultants continue to be strong and the client relationship managers are focusing on the full engagement of key auto-enrolling clients and clients transitioning from the Embassy platform to ensure high levels of retention. Focus is also being given to corporate actions in the market (Defined Benefit scheme closures and acquisitions, for example) where growth opportunities are anticipated.

Friends Life continues to secure protection scale across a strong, diverse distribution footprint, including through intermediary panels, banks, estate agencies and brands for individual protection and Employee Benefit Consultants for group protection. New distribution opportunities involve both developing new channels with existing partners and the growth of new partners including the long-term partnership with Virgin Money starting in January 2014. The company is also continually enhancing its proposition portfolio to ensure that it remains a market leader in terms of product quality.

Retirement Income volumes are expected to grow in the second half of 2013 as the division continues to roll out improvements to its annuity proposition and the more sophisticated pricing flexibility supports an improvement in retention rates.

The division remains focused on achieving its 2013 full year targets as outlined in the table above although competitive pressures in the individual protection marketplace are increasing.

4 International division

Half year 2013 operational highlights

- International division results are encouraging as a result of the actions taken to reshape the business.
- Dividend payments totalling £10 million were made in July from International businesses (£6 million from FPI and £4 million from Lombard) and the division's dividend target for this year is reiterated.
- In line with the strategic development plan launched in 2012, the re-engineering of Lombard's head office is progressing well.
- The exit from manufacturing new pensions business in Germany has been announced and the closure to new business will be completed by the end of September 2013.

New business

- International VNB at £16 million (30 June 2012: £30 million). The core business of FPI and Lombard generated a VNB of £21 million and an IRR of 12.5% (30 June 2012: £22 million VNB and 11.8% IRR).
- Lombard VNB was in line with the same period last year at £12 million. Sales have a heavy annual seasonality towards the fourth quarter.
- FPI core VNB was £9 million (30 June 2012: £10 million). Distribution has focused on growing lower strain single premium business to offset the fall in the Asian unit-linked markets. The IRR of the core business increased from 10.7% to 11.4%.
- FPI non-core VNB fell to £(5) million (30 June 2012: £8 million; 31 December 2012: £(12) million) largely reflecting the change in the assumptions at the end of 2012 on regular premium pensions business in Germany.

Financial performance

- International IFRS based operating profit of £74 million (30 June 2012: £31 million) largely reflects the non-recurrence of one-off costs in 2012, favourable economic experience on the return of premium guarantee on German business and income from the larger in-force book in FPI.
- International MCEV operating profit of £21 million (30 June 2012: £43 million; 31 December 2012: £1 million) was impacted by a reduction in International VNB, the impacts of the German strategic review undertaken in the fourth quarter of 2012, and worsening lapse experience in Lombard, partially offset by some favourable experience variances compared to prior period.
- International sustainable free surplus of £18 million (30 June 2012: £4 million) largely reflects the non-recurrence of one-off costs in 2012 combined with lower investment in new business and better 2013 experience variances in FPI.

Structure

The International division comprises two business units, Lombard and FPI.

Lombard is the leading pan-European specialist in estate and succession planning solutions for high and ultra-high net worth individuals ("HNWIs") using life assurance. Based in Luxembourg, the business offers innovative solutions and superior service through a well-established distribution network of private banks and independent financial advisers to HNWIs across Europe and selected markets in Latin America and Asia. Solutions offered by Lombard are typically based on single premium, whole of life, unit-linked life assurance structures with limited levels of reinsured life cover. The business is well placed to benefit from increasing demand for fully compliant structured solutions for HNWIs that are both robust and portable.

FPI sells unit-linked savings, single premium bonds and protection products with a strategic focus on affluent domestic customers and expatriates in its core markets via branches in Hong Kong, Singapore and Dubai, as well as serving UK customers with offshore products. FPI is in the course of completing its previously announced withdrawal from non-core markets with the sale of its 30% stake in AmLife on 4 January 2013 and the closure to new business with Japanese residents in 2012. The closure to manufacturing of new pensions business from Germany is scheduled for completion by the end of the third quarter of 2013.

Market environment

The legal and tax environment in most of Lombard's core markets across Europe remains uncertain. This leads to a continued lack of momentum in the market with clients and partners more reluctant to take long-term investment decisions. Whilst Lombard is seeing this trend across most of its European markets, it has been particularly evident in Belgium in the first half of 2013, where significant tax and legal uncertainties have resulted in increased lapses and substantial reductions in new business.

Notwithstanding the challenging short-term market conditions, the longer term drivers of the demand for individually structured Privatbancassurance solutions remain compelling. Lombard's position as a leading player in this market means it is well placed to benefit from opportunities arising from the changes in the market.

FPI's main markets are in Hong Kong, Singapore and the United Arab Emirates. The life markets in Hong Kong and Singapore are attractive and growing strongly. However, as a result of uncertainty from more demanding regulatory requirements, the unit linked segments have declined in the first quarter of 2013 compared with the same period last year by 11% and 13% in Hong Kong and Singapore respectively. In the Middle East, the Emirates life insurance market has experienced growth of 19% per annum since 2008 and includes an increasing non-resident Indian population as well as professionals as the local economy benefits from relative stability compared to the wider region.

International strategy

The International strategy was presented to the market in November 2012 and is unchanged. It will enhance value creation through a sustainable portfolio of international businesses in regions with sound regulatory frameworks, focusing on profitable growth and cash generation. The priorities of the division are to:

- selectively grow the business and generate an IRR of new business of 20% for the division as a whole;
- improve the efficiency of the back-office and deploy more resources to Asia; and
- increase the dividends to Group to £50 million per annum from 2015 onwards (target of £33 million for 2013).

Financial performance

The consolidated results of the International division are set out below. The results of the Lombard and FPI businesses are set out in the following sections, including a split of the core and non-core elements in FPI.

£m	**2013 Half year**	2012 Half year	2012 Full year
IFRS			
Lombard	**20**	10	28
FPI – core	**41**	30	58
Core International IFRS based operating profit before tax	**61**	40	86
FPI – non-core	**13**	(9)	(95)
Total International IFRS based operating result before tax	**74**	31	(9)
MCEV			
Lombard	**11**	25	104
FPI – core	**15**	14	(2)
Core International MCEV operating profit before tax	**26**	39	102
FPI – non-core	**(5)**	4	(101)
Total International MCEV operating profit before tax	**21**	43	1
SFS			
Lombard	**5**	(3)	(4)
FPI – core	**14**	19	30
Core International sustainable free surplus generation	**19**	16	26
FPI – non-core	**(1)**	(12)	(54)
Total International sustainable free surplus generation	**18**	4	(28)

The International division results include good progress on IFRS and cash generation, but a reduction in MCEV operating profit.

The International division's IFRS based operating profit was £74 million, up 139% on 2012. This largely reflects positive economics on the return of premium guarantee in Germany, income from the larger in-force book in FPI together with the non-recurrence of Lombard's one-off costs incurred in 2012.

International MCEV operating profit of £21 million was lower than in the first half of 2012, principally reflecting the effects of the revised strategy announced in November 2012 and the subsequent year end assumption change on the FPI business. Whilst these changes make comparisons between periods less meaningful, the results do reflect the impact of reduced sales in the non-core business as well as the negative lapse experience in Lombard.

Sustainable free surplus of £18 million for the International business increased by £14 million above 2012 and reflects the strategic decisions taken to exit FPI's non-core businesses, better experience variance in FPI than in 2012 and the non-recurrence of one-off costs in Lombard.

Outlook

The Group remains confident that the International division will make an increasing contribution towards generating shareholder cash, as evidenced by the £10 million of dividends paid in July 2013.

4.1 Lombard operating review

£m (unless otherwise stated)	**2013 Half year**	2012 Half year	2012 Full year
IFRS based operating profit	**20**	10	28
MCEV operating profit	**11**	25	104
Sustainable free surplus	**5**	(3)	(4)
Funds under management (£bn)	**20.1**	17.8	18.9
Dividends paid to Group (July 2013/November 2012)	**4**	-	4

The persisting significant macroeconomic uncertainty combined with important changes in the tax and legal framework of several key markets in which Lombard operates, adversely impacted the sales volumes and MCEV operating profits. Notwithstanding this, funds under management continue to grow supported by market returns and now total £20.1 billion (€23.5 billion) at 30 June 2013. Lombard paid the second dividend in its history following the £4 million dividend paid in November 2012 with an interim dividend of £4 million paid in July 2013.

New business profitability

£m (unless otherwise stated)	**2013 Half year**	2012 Half year	2012 Full year
VNB	**12**	12	45
Investment in new business	**(12)**	(12)	(23)
IRR[(i)]	**13.8%**	14.1%	22.5%
APE	**87**	95	238
APE in constant currency	**85**	95	n/a

(i) Lombard IRR takes into account the Luxembourg regulatory regime in which DAC is an allowable asset.

Lombard's value of new business amounted to £12 million, the same level as in the first half of 2012. The impact of lower volumes (8% down on the same period last year) is offset by overall margin improvement as a result of a lower proportion of large cases and the benefits of expense reduction initiatives last year. IRR and investment in new business are in line with the first half of 2012. Results to date reflect Lombard's sales profile, which remains materially weighted towards the latter part of the year, whilst the acquisition cost base is largely fixed. As such, extrapolation of the current period's results will not be indicative of the full year's results.

Some regions have performed well compared to the prior period, notably UK, Southern European and Scandinavian markets. However, in Northern Europe, there was a significant reduction in sales in Belgium.

In line with Lombard's long-term strategy, the mix of new business sales increasingly originates through private banks (49% in the first half of 2013 compared with 46% in the same period in 2012) rather than IFAs.

APE performance by region is as follows:

APE by region (actual exchange rates, £m)	**2013 Half year**	2012 Half year
UK and Nordic	**34**	30
Northern Europe	**1**	14
Southern Europe	**48**	41
Rest of world	**4**	10
Total including large cases	**87**	95
Of which: large cases (greater than €10 million)	**24**	33
Total excluding large cases	**63**	62

IFRS based operating profit

£m	**2013 Half year**	2012 Half year	2012 Full year
New business strain	**(16)**	(18)	(30)
In-force surplus	**37**	28	60
Development costs	**(1)**	-	(2)
IFRS based operating profit before tax	**20**	10	28

Lombard generated an IFRS based operating profit before tax of £20 million in the first half of 2013, £10 million up on the same period in 2012. The period on period increase principally reflects the non-recurrence of one-off expenses totalling £(9) million incurred in 2012. Excluding these costs, IFRS based operating profit was 5% above 2012.

IFRS new business strain is 11% lower than in the first half of 2012 (6% in constant currency), benefitting from lower acquisition expenses.

Funds under management

FUM continued to increase in 2013. Positive investment return and weakening of the Euro against sterling in 2013, while net trading volumes were neutral, drove FUM from £18.9 billion (€23.3 billion) at the end of 2012 to £20.1 billion (€23.5 billion) at 30 June 2013. Over the 12-month period from 30 June 2012, FUM has grown 7% in Euro terms.

	€bn	£bn
1 January 2013	**23.3**	**18.9**
Inflows	1.0	0.9
Outflows	(1.0)	(0.9)
Net investment return	0.2	0.2
Foreign exchange	-	1.0
30 June 2013	**23.5**	**20.1**

Operating expenses

£m	**2013 Half year**	2012 Half year	2012 Full year
Acquisition	**19**	20	41
Maintenance	**12**	21	34
	31	41	75
Development	**1**	-	2
Total	**32**	41	77

Operating expenses, which exclude commission payments, were 22% below those in the first half of 2012; although comparative maintenance costs included one-off and restructuring costs totalling £(9) million, while 2013 includes restructuring costs of £(1) million. Excluding one-off costs, operating expenses are stable on 2012. Lombard has retained tight control of recurring expense levels which, despite an increase in average funds under management, have remained in line with 2012 levels.

MCEV operating profit

£m	2013 Half year	2012 Half year	2012 Full year
Value of new business	**12**	12	45
Expected existing business contribution	**18**	18	35
Operating experience variances	**(18)**	(10)	(23)
Operating assumption changes	**-**	5	36
Other operating variances	**-**	-	13
Development costs	**(1)**	-	(2)
Life and pensions covered business operating profit before tax	**11**	25	104

MCEV operating profit was down 56% on the first half of 2012 primarily due to negative lapse experience. This arose across a number of European territories with the single largest impact arising in Belgium.

Expected existing business contribution

Expected existing business contribution is in line with 2012, as a result of the higher opening value of the in-force book being broadly offset by reduced economic assumptions.

	Rates used for expected return contribution	
%	**2013**	2012
Reference rate	**2.13**	1.61
Best estimate returns:		
Corporate bonds	**3.13**	3.55
Equity	**5.13**	5.55

Operating experience variances

Adverse operating experience variances of £(18) million primarily consist of persistency experience relating to surrenders, particularly in Belgium, where new tax reforms including the launch of new rules around asset regularisation have been implemented in 2013. This new landscape has materially affected the wider Luxembourg life assurance market in respect of Belgium.

Sustainable free surplus generation

£m	2013 Half year	2012 Half year	2012 Full year
Expected return from in-force business	**22**	14	36
Investment in new business	**(12)**	(12)	(23)
Underlying free surplus generation	**10**	2	13
Development costs	**(1)**	-	(1)
Operating experience variances	**(3)**	(5)	(16)
Other operating variances	**(1)**	-	-
Sustainable free surplus generation	**5**	(3)	(4)

Sustainable free surplus of £5 million is up £8 million on the first half of 2012 and reflects both the higher operating funds under management as well as the non-recurrence of £(7) million of one-off expenses incurred in 2012.

4.2 FPI operating review

£m (unless otherwise stated)	**2013 Half year**	2012 Half year	2012 Full year
IFRS based operating result	**54**	21	(37)
MCEV operating result	**10**	18	(103)
Sustainable free surplus	**13**	7	(24)
Dividends paid to Group (July 2013)	**6**	-	-
Funds under management (£bn)	**7.3**	6.2	6.7

The results of the FPI business in 2013 are encouraging. The results in the first half of 2012 did not reflect the impact of one-off charges relating to market exits and assumption changes allowed for in the 2012 full year, principally in the non-core businesses, which dominated the full year 2012 results.

The FPI results are shown in the sections below analysed between the core and non-core business. Additional detail is shown at the end of this section including the Lombard business. The core business excludes AmLife, OLAB (mainly Germany) and new business written in Japan in 2012 (prior to market exit).

New business profitability

£m (unless otherwise stated)	**2013 Half year**			2012 Half year			2012 Full year		
	Core	**Non-core**	**Total**	Core	Non-core	Total	Core	Non-core	Total
VNB	**9**	**(5)**	**4**	10	8	18	17	(12)	5
Investment in new business	**(24)**	**(16)**	**(40)**	(25)	(22)	(47)	(39)	(62)	(101)
IRR	**11.4%**	**(0.1)%**	**5.0%**	10.7%	10.1%	10.5%	11.0%	2.0%	5.4%
APE	**70**	**9**	**79**	74	30	104	146	56	202

Total FPI sales volumes were 24% lower than in 2012, reflecting the good progress made in reducing non-core regular premium business in particular new business with Japanese nationals, the sale of AmLife and a controlled exit from writing new business in Germany.

Whilst the unit-linked markets in Hong Kong and Singapore fell by 11% and 13% from first quarter 2012 to first quarter 2013 respectively, core business APE fell by just 5%. Despite the challenging environment in Asia, sales of single premium bonds increased. Core FPI IRR improved to 11.4%, benefiting from this favourable mix of business combined with a favourable impact of mortality assumption changes on protection business. The ratio of investment in new business to APE has been maintained. VNB in the core business is lower at £9 million as the benefits of assumption changes and lower expenses are offset by the lower volumes.

Non-core value of new business of £(5) million was significantly lower than 30 June 2012 reflecting the planned reduction in volumes and assumption changes relating to German business allowed for in the 2012 full year results. In addition, the impact of modelling improvements already accounted for in the final quarter of 2012 increased the cost of embedded German guarantees. IRR and investment in new business relative to sales volumes were similarly impacted.

IFRS based operating result

£m	Core	Non-core	**2013** Half year	2012 Half year	2012 Full year
New business strain	**(11)**	**(13)**	**(24)**	(24)	(53)
In-force surplus	**55**	**24**	**79**	51	95
Principal reserving changes and one-off items	**-**	**3**	**3**	-	(70)
Development costs	**(3)**	**(1)**	**(4)**	(4)	(6)
Other income and charges	**-**	**-**	**-**	(2)	(3)
IFRS based operating profit/(loss) before tax	**41**	**13**	**54**	21	(37)

FPI IFRS based operating result increased to £54 million from £21 million in the same period of 2012. This reflects an increase in IFRS in-force surplus of £28 million due to a larger book of in-force business together with the impact of improved economic conditions largely relating to the return of premium guarantee business in Germany. Additionally, the results have benefited from an uplift of £10 million in premium margin across certain non-core in-force products which is expected to reduce going forwards. IFRS new business strain is in line with prior period at £(24) million. Core new business strain benefits from lower expenses and assumption changes on protection business. This is offset by increases in non-core new business strain due to assumption changes and higher guarantee costs partially offset by lower sales volumes.

Principal reserving changes of £3 million relate to improvements in the modelling of the costs of the guarantees on German business.

Funds under management

£bn	**1 January 2013**	**Inflows**	**Outflows**	**Market and other movements**	**Sale of AmLife**	**30 June 2013**
FPIL	**6.1**	0.6	(0.4)	0.4	-	**6.7**
OLAB	**0.5**	0.1	-	-	-	**0.6**
AmLife	**0.1**	-	-	-	(0.1)	**-**
FPI total	**6.7**	0.7	(0.4)	0.4	(0.1)	**7.3**

Funds under management as at 30 June 2013 increased to £7.3 billion. The business generated net inflows of £0.3 billion and market growth accounted for a further £0.4 billion.

Operating expenses

£m	**2013** Half year	2012 Half year	2012 Full year
Acquisition	**13**	17	33
Maintenance	**17**	17	34
	30	34	67
Development	**4**	4	6
Total	**34**	38	73

Operating expenses, which exclude commission payments and non-recurring costs, decreased to £34 million from £38 million in the first half of 2012. Acquisition costs decreased largely as a result of the lower new business volumes following the strategic market exits. Maintenance expenses are in line with 2012. Development expenses amounting to £(4) million principally reflect the International transformation programme focusing on system and process improvements. Work on core Personal Portfolio Bond systems and the development of the digital portal strategy will drive efficiencies including the online submission of new business and dealing. In addition, a service improvement programme will deliver staffing efficiencies in the back office by June 2014.

MCEV operating result

£m	Core	Non-core	2013 Half year	2012 Half year	2012 Full year
Value of new business	**9**	**(5)**	**4**	18	5
Expected existing business contribution	**8**	**1**	**9**	12	23
Operating experience variances	**2**	**(1)**	**1**	(8)	(12)
Operating assumption changes	**-**	**-**	**-**	-	(107)
Other operating variances	**(1)**	**1**	**-**	-	(5)
Development costs	**(3)**	**(1)**	**(4)**	(4)	(6)
Life and pensions covered business operating profit/(loss) before tax	**15**	**(5)**	**10**	18	(102)
Other income and charges	**-**	**-**	**-**	-	(1)
MCEV operating profit/(loss) before tax	**15**	**(5)**	**10**	18	(103)

FPI MCEV operating profits of £10 million (30 June 2012: £18 million) reflects a £9 million improvement in operating experience variances including favourable persistency, expenses and fund rebate income experience compared to the prior period. Strategic reductions in volume, changes in assumptions, mostly in the German business, and the more onerous cost of embedded German guarantees driven by interest rate movements at the end of 2012 resulted in a lower VNB.

MCEV operating profits on core business at £15 million remain consistent with the same period last year (30 June 2012: £14 million). Non-core MCEV operating result of £(5) million has been adversely impacted by assumption changes made in the 2012 full year results.

Expected existing business contribution

The expected existing business contribution has reduced from £12 million to £9 million reflecting the lower opening in-force book resulting from the assumption changes arising from the strategic review combined with lower rates of expected return on all assets.

	Rates used for expected return contribution	
%	**2013**	2012
Reference rate	**0.67**	1.35
Best estimate returns:		
Corporate bonds	**2.40**	2.98
Equity	**4.90**	5.40
Property	**3.90**	4.40

Operating experience variances

A small favourable operating experience variance of £1 million represents a number of small offsetting items particularly in respect of mortality, persistency and expenses.

Operating assumption changes

There are no operating assumption changes impacting MCEV during the period. The 2012 full year results reflected the assumption changes for persistency and expenses as a result of the strategic review.

Sustainable free surplus generation

£m	Core	Non-core	2013 Half year	2012 Half year	2012 Full year
Expected return from in-force business	**44**	**13**	**57**	65	93
Investment in new business	**(24)**	**(16)**	**(40)**	(47)	(101)
Underlying free surplus generation	**20**	**(3)**	**17**	18	(8)
Development costs	**(3)**	**(1)**	**(4)**	(3)	(5)
Operating experience variances	**-**	**1**	**1**	(8)	(9)
Other operating variances	**(3)**	**2**	**(1)**	-	(2)
Sustainable free surplus generation	**14**	**(1)**	**13**	7	(24)

FPI sustainable free surplus increased to £13 million (30 June 2012: £7 million) arising from better experience variances than in the first half of 2012, particularly from expenses and higher rebates.

The core business sustainable free surplus has reduced compared with 30 June 2012 as a result of the lower in-force surplus from lower volumes of regular premium savings business written in 2012 compared with 2011. The surplus emergence on the regular premium savings business is weighted towards the early years of the contract, hence the recent volumes of new business and the phasing over the year will impact expected returns in subsequent reporting periods. The non-core sustainable free surplus has improved significantly as the volumes of regular premium German pensions business, and hence the investment in new business, is reduced.

International division additional information

IFRS based operating profit

	Core			Non-core	Total
Half year ended 30 June 2013					
£m	FPI	Lombard	**International**	FPI	**International**
New business strain	(11)	(16)	**(27)**	(13)	**(40)**
In-force surplus	55	37	**92**	24	**116**
Principal reserving changes and one-off items	-	-	**-**	3	**3**
Development costs	(3)	(1)	**(4)**	(1)	**(5)**
IFRS based operating profit before tax	41	20	**61**	13	**74**

MCEV operating profit

	Core			**Non-core**	**Total**
Half year ended 30 June 2013					
£m	FPI	Lombard	**International**	FPI	**International**
Value of new business	9	12	**21**	(5)	**16**
Expected existing business contribution	8	18	**26**	1	**27**
Operating experience variance	2	(18)	**(16)**	(1)	**(17)**
Other operating variances	(1)	-	**(1)**	1	**-**
Development costs	(3)	(1)	**(4)**	(1)	**(5)**
MCEV operating profit before tax	15	11	**26**	(5)	**21**

Sustainable free surplus

	Core			Non-core	Total
Half year ended 30 June 2013					
£m	FPI	Lombard	**International**	FPI	**International**
Expected return from in-force business	44	22	**66**	13	**79**
Investment in new business	(24)	(12)	**(36)**	(16)	**(52)**
Development costs	(3)	(1)	**(4)**	(1)	**(5)**
Operating experience	-	(3)	**(3)**	1	**(2)**
Other operating variances	(3)	(1)	**(4)**	2	**(2)**
Sustainable free surplus generation	14	5	**19**	(1)	**18**

5 Corporate review

The Corporate segment includes the corporate holding and service companies of the Group.

Corporate IFRS based operating result

£m	**2013 Half year**	2012 Half year	2012 Full year
Investment return and other items excluding external debt	**61**	58	118
External finance costs(i)	**(60)**	(53)	(108)
Other corporate net costs	**(13)**	(10)	(27)
IFRS based operating loss before tax	**(12)**	(5)	(17)

(i) 2012 half year and full year external finance costs include net finance costs within the Resolution holding companies of £(4) million and £(7) million respectively and reflect the receipt of interest from FLG and payment of DCN interest.

The Corporate IFRS operating result is principally driven by external finance costs and corporate costs, offset by interest on internal debt. The period on period increase in external finance costs reflects the UT2 subordinated debt issue in November 2012 together with a refinement to the finance cost methodology.

Other corporate net costs of £(13) million principally relate to overhead costs associated with management of the Resolution holding companies with the increase primarily reflecting an increase in provisions for long term incentive plan costs.

Corporate MCEV operating results

The Corporate segment consists of both non-covered and covered business. The non-covered element relates to the net assets of the corporate holding and service companies whilst the covered element principally represents the net debt liabilities held at the Group level.

£m	**2013 Half year**	2012 Half year	2012 Full year
Expected existing business contribution on debt	**(37)**	(35)	(75)
Life and pensions covered business operating loss before tax	**(37)**	(35)	(75)
Other income and charges	**(11)**	(22)	(46)
Operating loss before tax	**(48)**	(57)	(121)

The expected existing business contribution on debt has increased to £(37) million in the first half of 2013 reflective of the additional UT2 debt and higher market value of debt. These factors have largely been offset by a reduction in the expected rates of return applied in calculation of the debt contribution.

Corporate sustainable free surplus generation

£m	**2013 Half year**	2012 Half year	2012 Full year
Coupon on external debt	**(45)**	(35)	(73)
Coupon on internal debt	**-**	(7)	(12)
Other income and charges	**(4)**	(2)	(10)
Sustainable free surplus generation	**(49)**	(44)	(95)

The sustainable free surplus contribution from Corporate principally reflects the debt costs (net of tax) incurred by the Group. Following the repayment of the £363 million deferred consideration notes in 2012 and the raising of the UT2 reset perpetual subordinated debt, all of the Group’s finance costs are now reflected within sustainable free surplus.

Sustainable free surplus continues to exclude corporate costs relating to the Resolution holding companies.

Financing and interest costs

The Group has a number of debt instruments and the operating costs of financing these for the period ended 30 June 2013 are presented below.

£m	Principal	Clean market value of debt[i]	Finance costs[iii] IFRS	Finance costs[iii] MCEV
LT2 subordinated debt 2021	162	204	(10)	(5)
LT2 subordinated debt 2022	500	525	(21)	(13)
UT2 reset perpetual subordinated debt[ii]	379	396	(14)	(9)
STICS 2003	210	198	(7)	(4)
STICS 2005	268	252	(8)	(6)
Total 30 June 2013	**1,519**	**1,575**	**(60)**	**(37)**
Total 30 June 2012	1,140	916	(53)	(35)

(i) Market value is based on listed ask price, at 30 June 2013, excluding accrued interest.

(ii) The UT2 reset perpetual subordinated debt is a $575 million US Dollar denominated instrument. The principal and clean market values represent sterling equivalent values as at 30 June 2013. The finance cost of £14 million is based on the hedged sterling equivalent principal on the day of issue of £356 million.

(iii) Finance costs within sustainable free surplus amount to £(45) million, being the IFRS amount of £(60) million net of tax.

The finance cost included within IFRS based operating profit reflects the actual coupon paid. This represents a refinement in estimation to reflect a more accurate view of the longer term cost of the Group's external debt. In previous periods operating finance costs were based on the market value of the debt instruments. The change has not had a material impact on the results of the Group. Finance costs within the MCEV result continue to reflect the expected rate of return.

Gearing and liquidity

IFRS gearing (£m)	**30 June 2013**	31 December 2012
Equity attributable to equity holders of the parent	**5,233**	5,377
Loans and borrowings	**1,112**	1,099
	17.5%	17.0%

(i) IFRS debt gearing excludes the 2003 and 2005 STICS, as these securities are classified as equity in IFRS.

MCEV gearing (£m)	**30 June 2013**	31 December 2012
Group MCEV, gross of debt	**7,532**	7,427
Debt	**1,552**	1,596
	20.6%	21.5%

At 30 June 2013, the ratio of debt to IFRS equity attributable to equity holders of the parent, gross of debt, was 17.5% (31 December 2012: 17.0%), with the change in equity principally reflecting the payment of dividends in the period.

The MCEV gearing of 20.6% (31 December 2012: 21.5%) is marginally down over the period reflecting the increase in gross Group MCEV.

The liquidity of the Group remains strong and is complimented with an undrawn £250 million funding facility with a consortium of banks. This facility was renegotiated in May 2013 with a five year term and replaces the previous £500 million facility which had never been drawn.

6 Cash and capital

Introduction

The Group remains committed to the optimisation of capital within the business. The Group has established cash and capital frameworks which are used to evaluate and monitor excess cash and capital, driven by strong governance and subject to regulatory approval. The cash and capital position of the Group at 30 June 2013 remains strong with available shareholder cash ("ASC") of £839 million and an estimated IGCA surplus of £2.1 billion resulting in a coverage ratio, excluding with-profits insurance capital component ("WPICC")[(i)], of 222%. At 30 June 2013 the estimated economic capital surplus[(ii)] at Group level was £3.7 billion corresponding to a coverage ratio of 192%.

(i) WPICC represents the difference between the surplus capital calculated on a regulatory basis and that on a realistic basis, in accordance with regulations, and is excluded from both capital resources and capital resources requirements under the Group's capital management policies ("CMPs").

(ii) The economic capital position at 30 June 2013 of the Group and its subsidiaries (including FLL on an economic capital basis, see (iii) below) is estimated and unaudited.

(iii) Economic capital is based on the individual Pillar 2 capital assessments for the UK life companies. FLL's economic capital is derived from consolidating the individual life companies' Pillar 2 capital requirements including making appropriate allowance for the diversification of risk between the companies. Pillar 2 strictly only applies at individual life company level and is the Individual Capital Assessment ("ICA") determined by management including any amounts set by the PRA as ICG.

6.1 Capital management policies and monitoring buffers

The Group's CMPs that apply at a life company level and at the Group level were set out in the 2012 full year results. These policies remain unchanged and are summarised below.

Life companies CMP:

The CMP of FLL, the principal UK life company, is to meet the higher of:

- 150% of Pillar 1 requirements, excluding WPICC, FPIL and Lombard; and
- 125% of Pillar 2 requirements, including any Individual Capital Guidance ("ICG") and specifically excluding FPIL and Lombard.

In addition to the above, capital within FLL is held to cover at least one year of the FLL debt servicing costs (currently £115 million per annum) and any debt repayment requirements in the following year.

Group CMP:

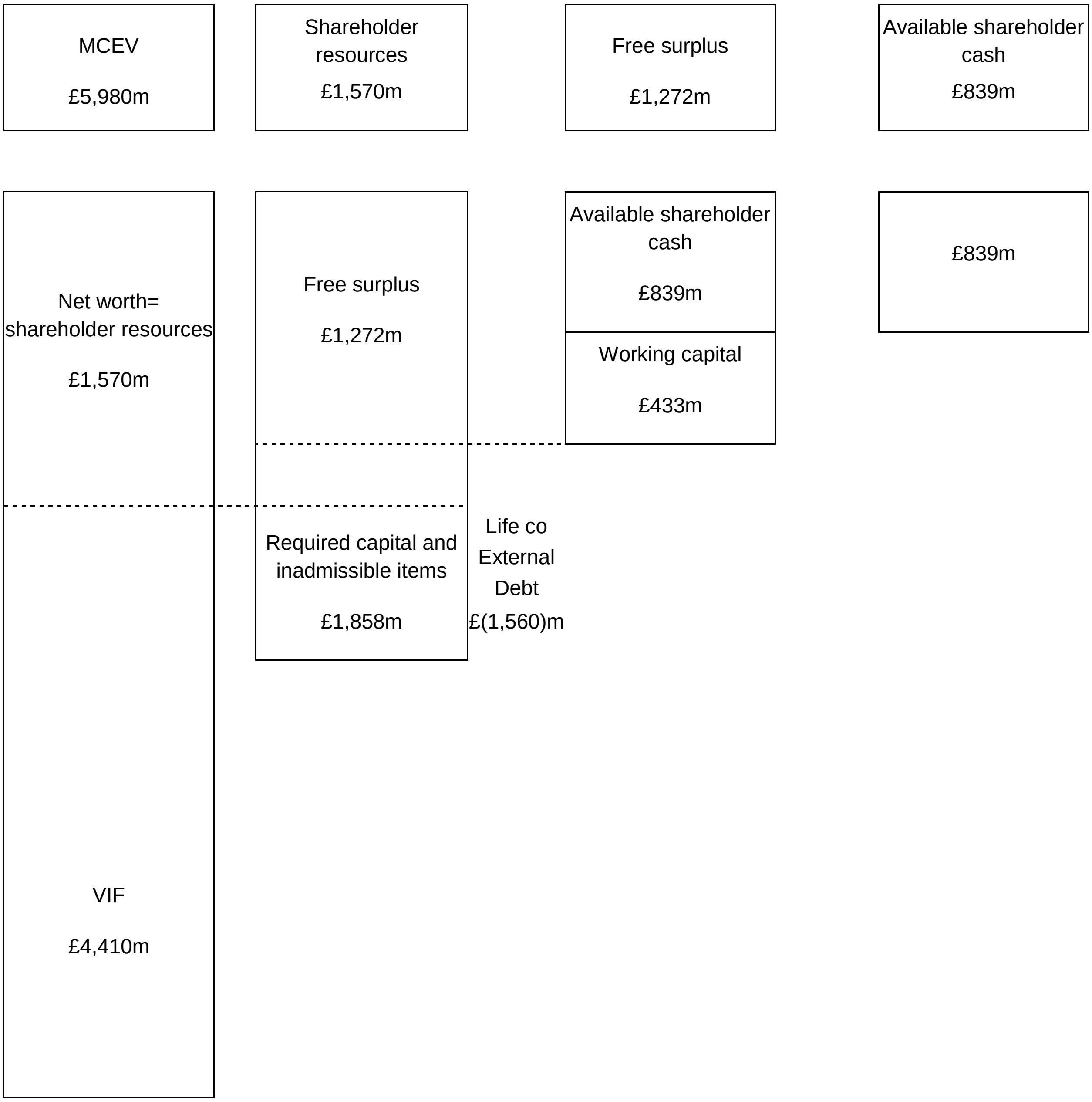
The CMP at Group level is to meet 150% of IGCA requirements, excluding WPICC. In order to protect the CMP in the highly remote event that payment of debt costs would lead to a breach of the policy, the Group has an additional requirement in respect of debt servicing costs. This requirement is to hold excess capital, over 150%, in the form of cash or cash equivalents at holding company level sufficient to pay at least the next year's gross annual interest cost (currently £120 million per annum) and any repayments of principal that fall due on debt in the next year.

Capital monitoring buffers:

The Group has a robust monitoring system and in addition to the amounts held to meet its CMPs, it holds a prudence buffer in the holding companies together with amounts for working capital in both the holding companies and the life companies. The monitoring buffers remain unchanged from those reported in the 2012 full year results.

6.2 Cash and capital management framework

The Group's cash and capital management framework is based on the movement in MCEV, reflecting the basis of MCEV as the discounted value of expected future cash flows on a market consistent basis. The chart below shows how the core components of MCEV and their respective values as at 30 June 2013, reconcile to ASC.



The total MCEV is split between the net worth, or shareholder resources, and the VIF. Shareholder resources comprise the free surplus, required capital and inadmissible assets of the business. Required capital is based on the most onerous CMP for the Group, currently the IGCA. For Resolution and Friends Life holding companies and other non-regulated businesses, free surplus is defined as IFRS net assets less required capital and inadmissible assets on an IGCA basis (for MCEV, where these assets relate to non-covered business, they are all included within free surplus). VIF comprises the value of the future cash flows arising from the policies currently in-force.

External debt issued by FLG is offset against required capital in the life businesses as this debt has been guaranteed by life operating companies and has been used to support their activities.

Working capital represents assets set aside to cover known future requirements and amounts necessary to maintain sufficient flexibility to facilitate compliance with the Group capital policy and additional regulatory requirements. In addition, any assets subject to restriction in their availability to shareholders will be designated as working capital.

ASC consists of cash held by the Friends Life and Resolution holding companies, together with any dividends declared and approved by the operating companies that are yet to be remitted. As such, ASC is stated after the deduction of working capital from free surplus. ASC represents cash available to cover Resolution's corporate costs, to service debt issued by holding companies and, subject to shareholder approval, to pay dividends or return to shareholders. The generation of ASC therefore represents a key performance metric of the Group.

The following table outlines the key movements in each of the components of total MCEV during the period:

		Shareholder resources		
£m (net of tax)	Value in-force	Required capital	Free surplus	Total MCEV
Opening MCEV at 1 January 2013	4,242	269	1,320	5,831
Sale of AmLife	(15)	(25)	47	7
Free surplus generated in the period	154	93	74	321
Dividend payment	-	-	(200)	(200)
Other reserve movements	29	(39)	31	21
Closing MCEV at 30 June 2013[(i)]	**4,410**	**298**	**1,272**	**5,980**

(i) Required capital at 30 June 2013 includes £236 million in respect of non-covered business required capital and inadmissible assets which are classified as free surplus in MCEV.

The free surplus generated in the six month period of £74 million is explained in section 2.2.

Other reserve movements include the impact of foreign exchange movements and actuarial losses on the Group's defined benefit pension scheme.

Working capital and other assets and liabilities

The working capital at 30 June 2013 of £433 million has reduced from £470 million at 31 December 2012, but includes a contribution to the 2013 final dividend in the first half of the year. This contribution will only be released to ASC once the year end actuarial valuations have been completed.

The remaining working capital comprises:

- amounts required to meet current estimates of future non-recurring costs, offset by related benefits that are expected in the short term;
- an appropriate monitoring buffer to facilitate ongoing compliance with the Group's Capital Management Policies;
- amounts to cover the necessary funding to protect against any temporary shortfall in delivery of cash generation relative to Group targets; and
- restricted assets (e.g. illiquid or intangible assets) included within free surplus.

The largest components are the monitoring buffer (£171 million) and amounts set aside to meet non-recurring costs (£109 million).

Working capital is held in both the life companies and the holding companies. The working capital in the life companies has reduced reflecting the utilisation of the working capital to fund non recurring spend, offset by the contribution to the 2013 final dividend. The working capital in the holding companies has reduced to reflect the utilisation of the working capital to fund the provision set up for the deficit reduction contributions in the Group's pension scheme.

Available shareholder cash

The ASC of £839 million comprises £661 million of shareholder cash at Friends Life holding company level (including the £110 million interim dividend proposed by FLL, net of service company capitalisation), together with £178 million held by Resolution holding companies. Details on ASC movements are set out in section 2.2.

£m	**30 June 2013**	31 December 2012
Friends Life holding companies cash	**551**	464
Proposed dividend from FLL	**110**	250
Friends Life available shareholder cash	**661**	714
Resolution holding companies cash	**178**	136
Available shareholder cash	**839**	850

The following table outlines the key components of ASC by reference to the expected utilisation of the cash balances:

£m	**30 June 2013**	31 December 2012
Settlement of interim/final dividend	**100**	200
Prudence buffer in accordance with Group policy	**400**	400
Non-specified ASC holdings	**339**	250
Available shareholder cash	**839**	850

The ASC balance as at 30 June 2013 is held to cover the costs of the interim dividend and to maintain a prudence buffer of £400 million which is designed to cover an additional year of the Company's dividend cost, debt interest and the holding companies corporate costs. This prudence buffer is also designed to cover the Group CMP requirement to hold cash at FLG sufficient to meet one year of FLG's debt servicing costs. As this is expected to be met from capital retained in the life companies, this is not considered to be a restriction on the availability of FLG cash.

6.3 Economic capital position

The UK life operations perform a risk-based assessment of economic capital, incorporating management's estimate of the capital required to mitigate the risk of insolvency to a minimum of a 99.5% confidence level over a one year period ("the ICA"). At an individual life company level this is referred to as the Pillar 2 basis of capital management.

The Group's CMP is to maintain capital resources at the life company level to cover 125% of the capital requirements on an economic capital basis.

The Group also monitors a pro forma economic capital position at a Group level, which comprises:

- the surplus of FLL, excluding FPIL and Lombard, on an economic capital basis;
- the surpluses of the International life companies on an economic capital basis; and
- the fungible net assets of the other operating and holding companies.

The estimated Group economic capital surplus above capital requirements as at 30 June 2013 is strong at £3.7 billion (a coverage ratio of 192%), the increase since 31 December 2012 (surplus of £3.5 billion) primarily reflecting market movements.

The sensitivities to market shocks show that economic capital surplus at a Group level would have reduced by:

- an estimated £0.7 billion in the event of a combined 40% fall in equity markets and a 30% fall in property markets;
- an estimated £0.1 billion in the event of a 200bps fall in interest rates; and
- an estimated £0.7 billion in the event of a widening of corporate bond spreads of 200bps (of which one-third is assumed to relate to defaults).

The sensitivities reflect various modelling improvements and de-risking activities implemented since 31 December 2012.

6.4 Insurance Groups Capital Adequacy

In addition to individual company requirements, the Group is required to meet the IGCA requirements of the Insurance Groups Directive. Following the governance changes made in the first half of 2013 Resolution Limited is now deemed to be the ultimate EEA parent undertaking of the Group and as such the IGCA requirements are now monitored at the RSL level. The Group's capital policy is to maintain sufficient Group capital resources to cover 150% of Group CRR (excluding WPICC).

The balance sheet remains strong with an estimated IGCA surplus of £2.1 billion at 30 June 2013, with Group capital resources being 222% of Group CRR (excluding WPICC of £3.8 billion).

The movement in IGCA surplus over the period largely reflects the external dividend paid offset by the generation of surplus and the proceeds from the sale of the 30% stake in AmLife.

Movement in IGCA surplus	**£m**
1 January 2013	**2,154**
Surplus emerging	112
Proceeds from sale of AmLife	50
Dividend paid	(200)
Finance costs and other movements	(23)
30 June 2013	**2,093**

At 30 June 2013 the capital held to meet CMPs was £856 million (1 January 2013: £889 million) and the excess over the CMPs was £1,237 million (1 January 2013: £1,265 million).

At a Friends Life Group level, excluding the assets and liabilities of Resolution Limited and the other Resolution holding companies established in Guernsey, the estimated IGCA surplus was £1.9 billion representing a coverage ratio of 212% (31 December 2012: £2.0 billion, coverage 214%).

The sensitivities to market shocks show that IGCA surplus would have reduced by:

- an estimated £0.1 billion in the event of a combined 40% fall in equity markets and a 30% fall in property markets;
- an estimated £0.3 billion in the event of a 200bps fall in interest rates; and
- an estimated £0.5 billion in the event of a widening of corporate bond spreads of 200bps (of which one-third is assumed to relate to defaults).

6.5 Asset quality and exposure

The Group's financial assets as at 30 June 2013, excluding cash, are summarised as follows:

£bn	Unit-linked	With-profits	Non-profit	Shareholder	30 June 2013 Total	31 December 2012 Total
Shares, unit trusts and OEICs	**62.6**	**7.1**	**0.1**	**-**	**69.8**	63.9
Government securities	**7.5**	**8.7**	**2.1**	**0.1**	**18.4**	18.7
Corporate bonds and asset-backed securities	**6.0**	**8.5**	**8.1**	**0.2**	**22.8**	22.4
Derivatives	**-**	**0.2**	**-**	**-**	**0.2**	0.8
Deposits	**0.2**	**-**	**-**	**-**	**0.2**	0.2
Total 30 June 2013	**76.3**	**24.5**	**10.3**	**0.3**	**111.4**	-
Total 31 December 2012	70.7	24.9	10.2	0.2	-	106.0

Shareholder exposure to corporate bonds and asset-backed securities is analysed by fund and credit rating as follows:

£bn	Unit-linked funds	With-profits funds	Non-profit funds	Shareholder funds	30 June 2013 Total	31 December 2012 Total
Corporate bonds and asset-backed securities	**6.0**	**8.5**	**8.1**	**0.2**	**22.8**	22.4
less: policyholder exposure	**6.0**	**7.4**	**-**	**-**	**13.4**	13.2
Shareholder exposure	**-**	**1.1**	**8.1**	**0.2**	**9.4**	9.2
AAA		**0.1**	**1.0**	**-**	**1.1**	1.3
AA		**0.2**	**2.8**	**0.1**	**3.1**	3.0
A		**0.5**	**3.0**	**0.1**	**3.6**	3.4
BBB		**0.2**	**1.2**	**-**	**1.4**	1.2
Sub-BBB or rating not available		**0.1**	**0.1**	**-**	**0.2**	0.3
% Investment grade					**97.9%**	96.7%

97.9% of the corporate bond and asset-backed securities to which the shareholder funds are exposed are investment grade. The Group controls its exposures to corporate issuers by rating, type of instrument and type of issuer. The sub-investment grade bonds held in investment portfolios are monitored closely in order to maximise exit values. Where asset-backed securities and other complex securities are held, the Group monitors closely its exposures to ensure that the relevant structure, liquidity and tail credit risks are well understood and controlled.

No defaults have been experienced in the period to 30 June 2013. The Group holds default reserves to cover the risk of defaults and credit rating downgrades on corporate bonds that back all annuity business within Friends Life group. The reserves reflect assumed defaults over the outstanding terms to maturity of the bonds. The shareholder share of default reserves at 30 June 2013 was £0.5 billion (31 December 2012: £0.5 billion). This represents a haircut of 49% of the overall corporate bond spreads over gilts of equivalent term (31 December 2012: 43%).

The vast majority of the Group's exposure to sovereign debt holdings is to UK gilts. The Group has £6 million direct shareholder exposure (including shareholder fund exposure to non-profit and with-profits funds) to the higher risk government debts of Spain, Portugal, Italy, Ireland and Greece (31 December 2012: £7 million).

6.6 Financial strength ratings

The Group targets financial strength ratings in the single A range for its principal life business and expects them to remain there for the foreseeable future. Current financial strength ratings are set out below.

	Fitch	Moody's	Standard & Poor's
Friends Life Limited	A+ (strong)	A3 (strong)	A- (strong)

7 Principal risks and uncertainties

The Group included details of the principal risks and uncertainties related to its business on pages 61-64 of its 2012 Annual Report and Accounts. The Group actively manages its risk profile and the Group's risk appetite framework drives the identification and mitigation of strategic, financial and operational risks to support the achievement of its objectives. The principal risks and uncertainties to which the Group has been exposed during the first six months of 2013 are unchanged from those described in the 2012 Annual Report and Accounts. These were published under the following headings:

- Economic conditions
- Sustained low interest rates
- Integration and restructuring
- Regulatory and taxation change and compliance
- Principal valuation assumptions
- Outsourcing

All of these are expected to remain relevant and applicable for the remainder of 2013.

Economic conditions remain volatile and uncertain. These conditions are expected to continue in coming months given the ongoing uncertainty in the Eurozone's financial stability and the UK economy continues to be depressed. Whilst the Group actively manages its exposure to market risk, its performance remains sensitive to factors such as the level of equity markets, interest rates and credit spreads which impact the investment return earned by the Group and the valuation of its liabilities. In particular, sustained low interest rates could have a material impact on the Group's business.

Economic uncertainty also acts to depress demand for financial products. Eurozone instability is expected to continue to reduce the total market for the investment products offered by the Group's international businesses. In the UK, the position going forward is more difficult to predict as the impact of adverse economic conditions is going to be combined with the effects of regulatory changes such as auto-enrolment in workplace pensions and the recently implemented prohibition of payment of commission to advisers under the Retail Distribution Review. Auto-enrolment is expected to increase the corporate pensions market once established and so offers significant opportunities to the Group whereas prospects for growth in the protection market are likely to remain modest.

Overall the Group's integration and restructuring work is continuing as planned, highlighted by the successful completion of activities to separate the Group's infrastructure from that of AXA UK. Despite this progress, the combination of the restructuring and regulatory change agenda faced by UK life insurers, means that the Group is facing a challenging change agenda and this is expected to continue through this year and into 2014. The Group operates project management disciplines to mitigate the risks to delivery, in particular to monitor delivery relative to plan and budget, to identify and manage interdependencies between projects and to escalate any delivery issues. However, there remain operational risks to the delivery of the change agenda to the expected timetables and budgets.

Proposals for Solvency II continue to be the subject of debate. The Group is monitoring developments closely but while key legislative requirements remain to be agreed it is not possible to assess the capital implications for the Group and the scope for optimising the Solvency II capital position.

The reliance of the Group on outsource service providers is unchanged and the risk that an outsourcer is or becomes unable to provide the expected services or required standard and quality of services remains. To mitigate this, processes for managing all outsourcing contracts are actively monitored and managed, in particular in relation to service improvement plans.

The strategic decision by the Group to simplify its governance arrangements and move to a conventional governance structure was completed in March 2013 which reduced the regulatory risk associated with proposed changes to the listing rules.

As stated in note 1 to the condensed consolidated financial statements, the Directors are satisfied that the Group has sufficient resources to continue in operation for the foreseeable future, a period of not less than 12 months from the date of this report. Accordingly, they continue to adopt the going concern basis in preparing the condensed consolidated financial statements.

Going concern and Directors' responsibility statement

Going concern

The Directors have undertaken a going concern assessment in accordance with "Going Concern and Liquidity Risk: Guidance for UK directors of UK Companies 2009", published by the Financial Reporting Council in October 2009. As a result of this assessment, the Directors are satisfied that the Group and the Company have adequate resources to continue to operate as a going concern for the foreseeable future and have prepared the financial statements on that basis. In assessing whether the going concern basis is appropriate, the Directors have considered the information contained in the financial statements, the latest business plan profit forecasts, the latest working capital forecasts and estimated forecast solvency of the regulated subsidiaries of the Group. These forecasts have been subject to sensitivity tests and the Directors are satisfied that the Group and Company have adequate resources to continue in operational existence for the foreseeable future. Key information in respect of the Group's business activities, financial performance (including cash generation and financial strength) and risks is set out on pages 12 to 52.

Directors' responsibilities

Each of the Directors of the Company confirms that to the best of their knowledge:

- the condensed consolidated financial statements have been prepared in accordance with IAS 34*: Interim financial reporting* as adopted by the European Union;
- the interim results statement includes a fair review of the information required by Disclosure and Transparency Rule 4.2.7, namely important events that have occurred during the period and their impact on the condensed consolidated financial statements, as well as a description of the principal risks and uncertainties faced by the Company and the undertakings included in the condensed consolidated financial statements taken as a whole for the remaining six months of the financial year; and
- the interim results statement includes a fair review of material related party transactions and any material changes in the related party transactions described in the last annual report as required by Disclosure and Transparency Rule 4.2.8.

By order of the Board

Tim Tookey
Director
12 August 2013

Independent review report to Resolution Limited

Introduction

We have been engaged by the Company to review the condensed set of financial statements in the interim results statement for the six months ended 30 June 2013 which comprises the condensed consolidated income statement, the condensed consolidated statement of comprehensive income, the condensed consolidated statement of IFRS based operating profit, the condensed consolidated statement of financial position, the condensed consolidated statement of changes in equity, the condensed consolidated statement of cash flows and the related notes 1 to 12. We have read the other information contained in the interim results statement and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with guidance contained in International Standard on Review Engagements 2410 (UK and Ireland) “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our work, for this report, or for the conclusions we have formed.

Directors’ responsibilities

The interim results statement is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the interim results statement in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 1, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this interim results statement has been prepared in accordance with International Accounting Standard 34: *Interim financial reporting*, as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the interim results statement based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the interim results statement for the six months ended 30 June 2013 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

Ernst & Young LLP
London
12 August 2013

IFRS FINANCIAL INFORMATION

Condensed consolidated income statement

For the half year ended 30 June 2013	Notes	**2013 Half year £m**	Restated 2012 Half year £m	Restated 2012 Full year £m
Revenue				
Gross earned premiums	2	**1,044**	982	1,906
Premiums ceded to reinsurers	2	**(300)**	(325)	(602)
Net earned premiums	2	**744**	657	1,304
Fee and commission income and income from service activities	2	**434**	373	749
Investment return[(i)]		**7,231**	2,531	9,045
Total revenue		**8,409**	3,561	11,098
Other income	2	**20**	–	–
Claims, benefits and expenses				
Gross claims and benefits paid		**(2,337)**	(2,125)	(4,175)
Amounts receivable from reinsurers		**333**	340	680
Net claims and benefits paid		**(2,004)**	(1,785)	(3,495)
Change in insurance contract liabilities		**86**	335	8
Change in investment contract liabilities		**(4,991)**	(1,055)	(5,052)
Transfer from/(to) unallocated surplus		**1**	(71)	(4)
Movement in net asset value attributable to unit-holders		**(108)**	(25)	(118)
Movement in policyholder liabilities		**(5,012)**	(816)	(5,166)
Acquisition expenses		**(282)**	(274)	(614)
Administrative and other expenses[(i)]		**(705)**	(740)	(1,597)
Finance costs		**(79)**	(77)	(157)
Total claims, benefits and expenses		**(8,082)**	(3,692)	(11,029)
Share of loss of associates and joint venture		**–**	(2)	(3)
Profit/(loss) before tax from continuing operations		**347**	(133)	66
Policyholder tax	5	**(277)**	(34)	(258)
Profit/(loss) before shareholder tax from continuing operations		**70**	(167)	(192)
Total tax (charge)/credit	5	**(286)**	75	(107)
Policyholder tax	5	**277**	34	258
Shareholder tax	5	**(9)**	109	151
Profit/(loss) for the period		**61**	(58)	(41)
Attributable to:				
Equity holders of the parent[(ii)]		**45**	(74)	(72)
Non-controlling interests		**16**	16	31
Profit/(loss) for the period		**61**	(58)	(41)

Earnings per share from continuing operations	Notes	**2013 Half year pence**	2012 Half year pence	2012 Full year pence
Basic and diluted earnings per share	4	**3.17**	(5.37)	(5.17)

(i) As a result of the revision to IAS19: *Employee benefits*, curtailment gains of £10 million for the six months ended 30 June 2012 and £32 million for the year ended 31 December 2012 have been presented within administrative expenses, rather than within investment return. Refer to note 6 for further details.

(ii) All profit attributable to equity holders of the parent is from continuing operations.

Notes 1 to 12 form an integral part of these financial statements.

The condensed consolidated income statements for the half year ended 30 June 2012 and for the year ended 31 December 2012 include the results of AmLife Insurance Berhad and AmFamily Takaful Berhad (collectively "AmLife"). The condensed consolidated income statement for the half year ended 30 June 2013 includes the results of AmLife up until the date of its disposal on 4 January 2013.

Condensed consolidated statement of comprehensive income

For the half year ended 30 June 2013	Equity holders of the parent £m	Non-controlling interests £m	Total £m
Profit for the period	**45**	**16**	**61**
Other comprehensive income:			
Items that will not be reclassified to profit and loss:			
Remeasurements on defined benefit scheme	**(70)**	**–**	**(70)**
Income tax relating to items that will not be reclassified	**50**	**–**	**50**
Total items that will not be reclassified to profit and loss	**(20)**	**–**	**(20)**
Items that may be reclassified subsequently to profit and loss:			
Foreign exchange adjustments (i)	**28**	**–**	**28**
Shadow accounting (ii)	**(8)**	**–**	**(8)**
Total items that may be reclassified subsequently to profit and loss	**20**	**–**	**20**
Other comprehensive loss, net of tax	–	–	**–**
Total comprehensive income, net of tax	**45**	**16**	**61**

For the half year ended 30 June 2012	Equity holders of the parent £m	Non-controlling interests £m	Total £m
(Loss)/profit for the period	(74)	16	(58)
Other comprehensive income:			
Items that will not be reclassified to profit and loss:			
Remeasurements on defined benefit scheme	6	–	6
Revaluation of owner occupied properties	(1)	–	(1)
Shadow accounting(iii)	1	–	1
Income tax relating to items that will not be reclassified	2	–	2
Total items that will not be reclassified to profit and loss	8	–	8
Items that may be reclassified subsequently to profit and loss:			
Foreign exchange adjustments(i)	(13)	–	(13)
Total items that may be reclassified subsequently to profit and loss	(13)	–	(13)
Other comprehensive loss, net of tax	(5)	–	(5)
Total comprehensive (loss)/income, net of tax	(79)	16	(63)

For the year ended 31 December 2012	Equity holders of the parent £m	Non-controlling interests £m	Total £m
(Loss)/profit for the period	(72)	31	(41)
Other comprehensive income:			
Items that will not be reclassified to profit and loss:			
Remeasurements on defined benefit scheme	(42)	–	(42)
Revaluation of owner occupied properties	(2)	–	(2)
Shadow accounting (iii)	2	–	2
Income tax relating to items that will not be reclassified	7	–	7
Total items that will not be reclassified to profit and loss	(35)	–	(35)
Items that may be reclassified subsequently to profit and loss:			
Foreign exchange adjustments(i)	(17)	–	(17)
Shadow accounting (ii)	5	–	5
Total items that may be reclassified subsequently to profit and loss	(12)	–	(12)
Other comprehensive loss, net of tax	(47)	–	(47)
Total comprehensive (loss)/income, net of tax	(119)	31	(88)

(i) Foreign exchange adjustments relate to the translation of overseas subsidiaries.

(ii) Shadow accounting that may be reclassified subsequently to profit and loss is as a result of a gain £8 million (30 June 2012: £nil, 31 December 2012: loss of £5 million) in respect of foreign exchange adjustments on translation of overseas subsidiaries held by the with-profits fund of Friends Life Limited ("FLL").

(iii) Shadow accounting that will not be reclassified to profit and loss is in respect of a loss of £nil (30 June 2012: loss of £1 million, 31 December 2012: loss of £2 million) relating to the revaluation of owner occupied properties, held by the with-profits fund of FLL.

Condensed consolidated statement of IFRS based operating profit

For the half year ended 30 June 2013	Notes	**2013 Half year £m**	2012 Half year £m	2012 Full year £m
Profit/(loss) before tax from continuing operations		**347**	(133)	66
Policyholder tax	5	**(277)**	(34)	(258)
Profit/(loss) before tax excluding returns generated within policyholder funds		**70**	(167)	(192)
Non-recurring items	2	**37**	118	258
Amortisation and impairment of acquired present value of in-force business	7	**192**	204	417
Amortisation of other intangible assets	7	**41**	42	97
Interest payable on STICS		**(16)**	(16)	(31)
Short-term fluctuations in investment return		**(133)**	(18)	(275)
IFRS based operating profit before tax		**191**	163	274
Tax on operating profit		**(3)**	(7)	2
IFRS based operating profit after tax attributable to equity holders of the parent[(i)]		**188**	156	276

Earnings per share		**2013 Half year pence**	2012 Half year pence	2012 Full year pence
Operating earnings per share	4	**13.26**	11.32	19.84

(i) IFRS based operating profit excludes: (a) investment variances from expected investment return for non-linked business which is calculated using a longer term rate of return; (b) significant non-recurring items; and (c) amortisation and impairment of present value of acquired in-force business and other intangible assets and is stated after policyholder tax and the deduction of interest payable on STICS. Given the long-term nature of the Group's operations, IFRS based operating profit is considered to be a better measure of the performance of the Group and this measure of profit is used internally to monitor the Group's IFRS results.

Condensed consolidated statement of financial position

As at 30 June 2013	Notes	**30 June 2013 £m**	30 June 2012 £m	31 December 2012 £m
Assets				
Pension scheme surplus	6	**–**	37	33
Intangible assets	7	**4,115**	4,585	4,321
Property and equipment		**51**	56	53
Investment properties		**2,621**	2,897	2,735
Investments in associates and joint venture		**4**	35	4
Financial assets	8	**111,427**	102,945	105,990
Deferred acquisition costs		**881**	751	838
Reinsurance assets		**3,130**	3,332	3,153
Current tax assets		**–**	6	8
Insurance and other receivables		**1,453**	1,478	1,125
Cash and cash equivalents		**9,804**	8,672	9,449
Net assets of operations classified as held for sale		**–**	–	30
Total assets		**133,486**	124,794	127,739
Liabilities				
Insurance contracts		**37,175**	37,064	37,232
Unallocated surplus		**655**	723	656
Financial liabilities:				
Investment contracts		**83,679**	75,066	78,184
Loans and borrowings	9	**1,112**	1,115	1,099
Amounts due to reinsurers		**1,720**	1,795	1,767
Net asset value attributable to unit-holders		**808**	900	754
Provisions		**232**	212	278
Pension scheme deficit	6	**31**	–	–
Deferred tax liabilities		**1,066**	756	893
Current tax liabilities		**35**	5	21
Insurance payables, other payables and deferred income		**1,411**	1,375	1,157
Total liabilities		**127,924**	119,011	122,041
Equity attributable to equity holders of the parent				
Share capital		**4,225**	4,170	4,225
Other reserves		**1,008**	1,283	1,152
		5,233	5,453	5,377
Attributable to non-controlling interests		**329**	330	321
Total equity		**5,562**	5,783	5,698
Total equity and liabilities		**133,486**	124,794	127,739

Condensed consolidated statement of changes in equity

For the half year ended 30 June 2013	Attributable to equity holders of the parent				
	Share capital £m	**Other reserves £m**	**Total £m**	**Non-controlling interests £m**	**Total £m**
At 1 January 2013	**4,225**	**1,152**	**5,377**	**321**	**5,698**
Profit for the period	**–**	**45**	**45**	**16**	**61**
Other comprehensive loss	**–**	**–**	**–**	**–**	**–**
Total comprehensive income	**–**	**45**	**45**	**16**	**61**
Dividends on equity shares	**–**	**(200)**	**(200)**	**–**	**(200)**
Interest paid on STICS	**–**	**–**	**–**	**(7)**	**(7)**
Appropriations of profit	**–**	**(200)**	**(200)**	**(7)**	**(207)**
Tax relief on STICS interest	**–**	**4**	**4**	**–**	**4**
Share-based payments, net of settlements[i]	**–**	**7**	**7**	**(1)**	**6**
At 30 June 2013	**4,225**	**1,008**	**5,233**	**329**	**5,562**

For the half year ended 30 June 2012	Attributable to equity holders of the parent				
	Share capital £m	Other reserves £m	Total £m	Non-controlling interests £m	Total £m
At 1 January 2012	4,128	1,544	5,672	323	5,995
Loss/(profit) for the period	–	(74)	(74)	16	(58)
Other comprehensive loss	–	(5)	(5)	–	(5)
Total comprehensive (loss)/income	–	(79)	(79)	16	(63)
Dividends paid	–	(185)	(185)	–	(185)
Interest paid on STICS	–	–	–	(7)	(7)
Appropriations of profit	–	(185)	(185)	(7)	(192)
Tax relief on STICS interest	–	3	3	–	3
Shares issued in lieu of dividend	35	–	35	–	35
Reduction in own shares held by the Group	7	–	7	–	7
Share-based payments, net of settlements[i]	–	–	–	(2)	(2)
At 30 June 2012	4,170	1,283	5,453	330	5,783

Condensed consolidated statement of changes in equity

For the year ended 31 December 2012	Attributable to equity holders of the parent Share capital £m	 Other reserves £m	 Total £m	Non-controlling interests £m	Total £m
At 1 January 2012	4,128	1,544	5,672	323	5,995
(Loss)/profit for the year	–	(72)	(72)	31	(41)
Other comprehensive loss	–	(47)	(47)	–	(47)
Total comprehensive (loss)/income	–	(119)	(119)	31	(88)
Dividends paid	–	(283)	(283)	–	(283)
Interest paid on STICS	–	–	–	(31)	(31)
Appropriations of profit	–	(283)	(283)	(31)	(314)
Tax relief on STICS interest	–	7	7	–	7
Shares issued in lieu of dividend	90	–	90	–	90
Reduction in own shares held by the Group	7	–	7	–	7
Share-based payments, net of settlements[i]	–	3	3	(2)	1
At 31 December 2012	4,225	1,152	5,377	321	5,698

(i) The other reserves movement for share-based payment transactions relates to the expense, net of partial settlement, of the Lombard long-term incentive plan ("LTIP") along with the expense of the deferred share award plan ("DSAP") and the Friends Life group share awards plan.

Condensed consolidated statement of cash flows

For the half year ended 30 June 2013	**2013 Half year £m**	2012 Half year £m	2012 Full year £m
Operating activities			
Profit/(loss) for the period	**61**	(58)	(41)
Adjusted for:			
Net realised and unrealised gains on assets at fair value	**(5,338)**	(734)	(5,630)
Finance costs	**79**	77	157
Amortisation and impairment of intangible assets	**233**	246	514
Depreciation of property and equipment	**3**	2	5
Movement in deferred acquisition costs	**(40)**	(110)	(195)
Total tax charge/(credit)	**286**	(75)	107
Purchase of shares and other variable yield securities	**(12,918)**	(7,733)	(22,536)
Proceeds from sale of shares and other variable yield securities	**13,380**	8,145	23,045
Purchase of loans, debt securities and other fixed income securities	**(10,163)**	(12,212)	(23,841)
Proceeds from sale of loans, debt securities and other fixed income securities	**10,825**	12,748	26,166
Purchase of investment properties	**(9)**	(34)	(51)
Proceeds from sale of investment properties	**90**	108	228
Decrease in insurance contract liabilities	**(57)**	(200)	(32)
Increase in investment contract liabilities	**4,391**	475	3,532
(Decrease)/increase in unallocated surplus	**(1)**	71	4
(Decrease)/increase in provisions	**(46)**	(16)	50
Net movement in receivables and payables	**(210)**	(367)	(214)
Pre-tax cash inflow from operating activities	**566**	333	1,268
Tax paid	**(44)**	(46)	(70)
Net cash inflow from operating activities	**522**	287	1,198
Investing activities			
Disposal of held for sale assets, net of cash transferred	**50**	–	–
Additions to internally generated intangible assets	**(2)**	(1)	(4)
Net additions of property and equipment	**(1)**	–	(2)
Net cash inflow/(outflow) from investing activities	**47**	(1)	(6)
Financing activities			
Purchase of ultimate parent company shares in settlement of incentive schemes	**(1)**	(4)	(4)
Proceeds from issue of long-term debt	**–**	–	349
Repayment of long-term debt	**–**	(60)	(423)
Finance costs	**(110)**	(124)	(170)
STICS interest	**(7)**	(7)	(31)
Net movement in other borrowings, net of expenses	**12**	(19)	(20)
Dividends paid to equity holders of the parent	**(200)**	(150)	(193)
Net cash outflow from financing activities	**(306)**	(364)	(492)
Increase/(decrease) in cash and cash equivalents	**263**	(78)	700
Balance at beginning of period	**9,449**	8,791	8,791
Exchange adjustments on the translation of foreign operations	**92**	(41)	(42)
Balance at end of period	**9,804**	8,672	9,449

Notes to the condensed consolidated accounts

1. Basis of preparation

The interim financial statements of the Company as at and for the half year ended 30 June 2013 comprise the condensed consolidated interim financial statements of the Company and its subsidiaries (together referred to as "the Group") and the Group's interests in associates and jointly controlled entities.

The annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union ("EU"). The condensed consolidated interim financial statements as at and for the half year ended 30 June 2013 have been prepared in accordance with the Disclosure and Transparency Rules of the Prudential Regulation Authority, with IAS 34: *Interim financial reporting* as adopted by the EU and with accounting policies adopted in respect of the financial statements for the year ended 31 December 2012, as updated by changes that are intended to be made in the full year 2013 financial statements as a result of changes to IFRS.

These condensed interim financial statements do not comprise statutory accounts within the meaning of section 435 of the Companies Act 2006. Statutory accounts for the year ended 31 December 2012 were approved by the Board of Directors on 25 March 2013. The report of the auditors on those accounts was unqualified, did not contain an emphasis of matter paragraph and did not contain any statement under section 498 of the Companies Act 2006. These condensed interim financial statements have been reviewed by Ernst & Young LLP and their review opinion appears after the business review.

Below is a list of new standards and changes to existing standards that have been issued by the International Accounting Standards Board ("IASB") which are effective from 1 January 2013.

- IFRS 13: *Fair value measurement* establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The standard is applied prospectively. The application of IFRS 13 has not materially impacted the fair value measurements carried out by the Group.
- IFRS 13 also requires specific disclosures on fair values, some of which have been incorporated into revisions to IAS 34, requiring disclosure in interim condensed consolidated financial statements. The Group provides these disclosures in note 8.
- IAS 19: *Employee benefits* (Revised 2011): IAS 19R includes a number of amendments to the accounting for defined benefit plans, including elimination of the corridor approach and recognition of all actuarial gains and losses in other comprehensive income ("OCI") under the heading of 'Remeasurements on defined benefit pension schemes' as they occur; to immediately recognise all past service costs; and to replace interest cost and expected returns on plan assets with a net interest amount, calculated by applying the discount rate used to measure the defined benefit obligation to the net defined benefit liability/(asset). The amendments must be made retrospectively.
- Elimination of the corridor approach has no impact on the results of the Group, as the existing policy is to recognise all actuarial losses in OCI as they occur. The change in accounting for net interest income/expense, which represents a change in accounting policy, has not impacted profit before tax or the statement of comprehensive income in prior periods or the period ended 30 June 2013.
- The income statement has been restated for the requirement to present curtailments gains within administrative and other expenses; previously, curtailment gains of £10 million at 30 June 2012 and £32 million at 31 December 2012 were included within investment return.

Amendments to IAS 1: *Presentation of financial statements:*

- Presentation of items of other comprehensive income: The amendments introduce a grouping of items presented in OCI. The items that could be reclassified to profit and loss at a future point in time, e.g. foreign exchange adjustments, are required to be presented separately from items that will never be reclassified.
- Clarification of the requirement for comparative information: The amendment clarifies the difference between voluntary additional comparative information and the minimum required comparative information.

- An opening statement of financial position (known as the 'third balance sheet') must be prepared when an entity applies an accounting policy retrospectively, makes retrospective restatements, or reclassifies items in its financial statements, provided any of those changes have a material effect on the statement of financial position at the beginning of the preceding period. The amendment clarifies that the third balance sheet does not have to be accompanied by comparative information in the related notes. Under IAS 34, the minimum items required for the interim condensed financial statements do not include a third balance sheet.
- Amendment to IAS 32: *Financial instruments: presentation* clarifies that income taxes arising from distributions to equity holders are accounted for in accordance with IAS 12: *Income taxes*. The amendment removes existing income tax requirements from IAS 32 and requires entities to apply the requirements in IAS 12 to any income tax arising from distributions to equity holders. The amendment does not impact the Group.
- Amendment to IAS 34: *Interim financial reporting* clarifies the requirements in IAS 34 relating to segment information for total assets and liabilities for each reportable segment to enhance consistency with the requirements in IFRS 8: *Operating segments*. The Group's existing disclosures already comply with this amendment.
- Amendments to IFRS 7: *Financial instruments: disclosure* requires an entity to disclose information about rights to set-off financial instruments and related arrangements (e.g. collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The amendments do not impact the Group.

The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

The Directors are satisfied that the Group has sufficient resources to continue in operation for the foreseeable future, a period of not less than 12 months from the date of this report. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

The presentation currency of the Group is Sterling. Unless otherwise stated the amounts shown in these financial statements are in millions of pounds Sterling (£ million).

Unless otherwise stated, the carrying amount of financial assets and liabilities not measured at fair value is considered to be the same as their fair value.

The 2012 comparatives include the results of the associates AmLife Insurance Berhad and AmFamily Takaful Berhad (collectively "AmLife") which were disposed of by the Group on 4 January 2013. The results for the period include a profit on disposal of £20 million.

2. Segmental information

(a) Summary

Segmental information is presented on the same basis as internal financial information used by the Group to evaluate operating performance.

The Group's reportable segments under IFRS 8: *Operating segments* are as follows:

- UK, comprising Corporate Benefits, Protection and Retirement Income market-facing businesses;
- Heritage, comprising the bulk of the UK business that is no longer actively marketed;
- FPI, comprising Friends Provident International Limited ("FPIL"), the overseas life assurance business within the UK life and pensions subsidiaries and the Group's share of AmLife (prior to its disposal on 4 January 2013); and
- Lombard.

Corporate functions are not strictly an operating segment, but are reported to management and are provided in the analysis below to reconcile the Group's reportable segments to total profit.

In previous reporting periods, UK and Heritage were reported as a single segment. The comparatives have been restated to provide separate disclosure of UK and Heritage for the full year to 31 December 2012. Comparatives in respect of the six months to 30 June 2012 are not available and the cost to develop them would be excessive. Total UK and Heritage has been disclosed for all periods for comparison purposes.

(b) Operating segment information

(i) IFRS based operating profit

For the half year ended 30 June 2013	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Total £m
Life and pensions operating profit	**45**	**142**	**187**	**58**	**21**	**–**	**266**
Longer-term shareholder investment return	**5**	**(37)**	**(32)**	**–**	**–**	**1**	**(31)**
Other expense	**(5)**	**–**	**(5)**	**–**	**–**	**(13)**	**(18)**
Development costs	**(19)**	**(2)**	**(21)**	**(4)**	**(1)**	**–**	**(26)**
IFRS based operating profit/(loss) before tax	**26**	**103**	**129**	**54**	**20**	**(12)**	**191**
Tax on operating profit							**(3)**
IFRS based operating profit after tax attributable to equity holders of the parent							**188**
Operating earnings per share (pence)							**13.26**

For the half year ended 30 June 2012	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Total £m
Life and pensions operating profit	182	27	10	–	219
Longer-term shareholder investment return	(26)	–	–	9	(17)
Other expense	(1)	(2)	–	(14)	(17)
Development costs	(18)	(4)	–	–	(22)
IFRS based operating profit/(loss) before tax	137	21	10	(5)	163
Tax on operating profit					(7)
IFRS based operating profit after tax attributable to equity holders of the parent					156
Operating earnings per share (pence)					11.32

For the year ended 31 December 2012	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Total £m
Life and pensions operating profit/(loss)	4	379	383	(28)	30	–	385
Longer-term shareholder investment return	1	(41)	(40)	–	–	17	(23)
Other expense	(1)	–	(1)	(3)	–	(34)	(38)
Development costs	(36)	(6)	(42)	(6)	(2)	–	(50)
IFRS based operating (loss)/profit before tax	(32)	332	300	(37)	28	(17)	274
Tax on operating profit							2
IFRS based operating profit after tax attributable to equity holders of the parent							276
Operating earnings per share (pence)							19.84

(ii) Reconciliation of IFRS based operating result before tax to profit before tax from continuing operations

For the half year ended 30 June 2013	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Total £m
IFRS based operating profit/(loss) before tax	**26**	**103**	**129**	**54**	**20**	**(12)**	**191**
Non-recurring items [(i)(ii)(iii)]	**(15)**	**(131)**	**(146)**	**20**	**–**	**89**	**(37)**
Amortisation of acquired value of in-force business	**(25)**	**(101)**	**(126)**	**(41)**	**(25)**	**–**	**(192)**
Amortisation of intangible assets	**(21)**	**(2)**	**(23)**	**(3)**	**(15)**	**–**	**(41)**
Interest payable on STICS	**–**	**16**	**16**	**–**	**–**	**–**	**16**
Short-term fluctuations in investment return [(viii)]	**38**	**89**	**127**	**3**	**–**	**3**	**133**
Profit/(loss) before policyholder and shareholder tax	**3**	**(26)**	**(23)**	**33**	**(20)**	**80**	**70**
Policyholder tax	**3**	**274**	**277**	**–**	**–**	**–**	**277**
Profit/(loss) before tax from continuing operations	**6**	**248**	**254**	**33**	**(20)**	**80**	**347**

For the half year ended 30 June 2012	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Total £m
IFRS based operating profit/(loss) before tax	137	21	10	(5)	163
Non-recurring items[(iv)]	(127)	–	(1)	10	(118)
Amortisation of acquired value of in-force business	(132)	(44)	(28)	–	(204)
Amortisation of other intangible assets	(23)	(4)	(14)	(1)	(42)
Interest payable on STICS	16	–	–	–	16
Short-term fluctuations in investment return[(viii)]	30	(5)	–	(7)	18
Loss before policyholder and shareholder tax	(99)	(32)	(33)	(3)	(167)
Policyholder tax	34	–	–	–	34
Loss before tax from continuing operations	(65)	(32)	(33)	(3)	(133)

For the year ended 31 December 2012	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Total £m
IFRS based operating (loss)/profit before tax	(32)	332	300	(37)	28	(17)	274
Non-recurring items[(v)(vi)(vii)]	(9)	(264)	(273)	–	(1)	16	(258)
Amortisation and impairment of acquired value of in-force business	(52)	(216)	(268)	(94)	(55)	–	(417)
Amortisation and impairment of other intangible assets	(42)	(4)	(46)	(22)	(28)	(1)	(97)
Interest payable on STICS	–	31	31	–	–	–	31
Short-term fluctuations in investment return[(viii)]	52	246	298	(4)	(1)	(18)	275
(Loss)/profit before policyholder and shareholder tax	(83)	125	42	(157)	(57)	(20)	(192)
Policyholder tax	2	256	258	–	–	–	258
(Loss)/profit before tax from continuing operations	(81)	381	300	(157)	(57)	(20)	66

(i) UK non-recurring items for the half year ended 30 June 2013 include £(12) million of costs in respect of the transition and service improvement elements of the outsourcing agreement with Diligenta, £(2) million of costs relating to the 2013 capital optimisation programme and £(1) million of Solvency II and finance systems development costs.

(ii) Heritage non-recurring items for the half year ended 30 June 2013 include £(57) million in respect of separation and integration costs partially offset by a £47 million provision release, £(28) million of costs in respect of the transition and service improvement elements of the outsourcing agreement with Diligenta partially offset by a £10 million release of reserves, £(9) million of Solvency II and finance systems development costs and £(5) million of costs relating to the 2013 capital optimisation programme. Also included within Heritage is a cost of £(89) million in respect of a charge for deficit funding relating to the Group's defined benefit pension scheme, the income for which is reported within the Corporate segment results.

(iii) FPI non-recurring items of £20 million for the half year ended 30 June 2013 relate to the profit on disposal of the Group's entire 30% holding in Amlife.

(iv) UK & Heritage non-recurring items for the half year ended 30 June 2012 include £(39) million of separation and integration costs in respect of the UK Life project, £(47) million in respect of Solvency II and finance system developments, £(40) million of costs in respect of the transition and service improvement elements of the outsourcing arrangement with Diligenta offset partially by £13 million release of reserves, non-recurring costs of £(13) million related to capital restructuring and £(1) million of other costs. Lombard non-recurring costs relate to £(1) million of Solvency II costs. Corporate non-recurring items of £10 million represent curtailment gains arising on the defined benefit pension scheme, relating to reduced future anticipated costs of the scheme due to the Diligenta outsourcing arrangement.

(v) UK non-recurring items of £(9) million for the year ended 31 December 2012 relate to costs in respect of the transition and service improvement elements of the outsourcing arrangement with Diligenta.

(vi) Heritage non-recurring items for the year ended 31 December 2012 include £(124) million of costs in respect of the separation and integration program, £(75) million in respect of Solvency II and finance system developments, £(73) million of costs in respect of the transition and service improvement elements of the outsourcing arrangement with Diligenta offset partially by £31 million release of reserves, non-recurring costs of £(17) million related to the 2012 capital optimisation programme and other non-recurring costs of £(6) million.

(vii) Corporate non-recurring items of £16 million for the year ended 31 December 2012 include a curtailment gain of £32 million arising on the defined benefit pension scheme, of which £22 million relates to the closure of the scheme to future service accrual and £10 million to reduced future anticipated costs due to the Diligenta outsourcing arrangement. This is partially offset by £(16) million of costs in relation to the transition of Resolution Operations LLP ("ROL"), with £(14) million recognised within FLG corporate and £(2) million recognised within RSL corporate. The transition costs include £(10) million mainly in relation to the costs of transferring an operating agreement, under which the Company outsources most of its operations, from ROL to the Group, and the recognition of an onerous lease provision in respect of the ROL offices to be taken on by the Group; a further £(6) million relates to restructuring activities. It is expected that the majority of this expenditure will be incurred in 2013. Lombard non-recurring costs relate to £(1) million of Solvency II costs.

(viii) Includes shareholder investment return short-term fluctuations and investment variances arising from the mismatching of fixed-interest assets and the liabilities they are backing as well as the impact of credit default assumptions. This latter variance reflects profits or losses in excess of the expected investment return on the assets and the impact of the corresponding economic assumption changes on the liabilities. In the year ended 31 December 2012, this includes a £99 million benefit within Heritage that relates to the release of unit-linked tax loss provisions as a result of updated fund growth estimates.

(iii) Revenue and expenses

For the half year ended 30 June 2013	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Elimination of inter-segment amounts[ii] £m	Total £m
Gross earned premiums on insurance and investment contracts	**1,411**	**1,010**	**2,421**	**667**	**872**	**–**	**–**	**3,960**
Investment contract premiums[i]	**(1,073)**	**(375)**	**(1,448)**	**(596)**	**(872)**	**–**	**–**	**(2,916)**
Gross earned premiums	**338**	**635**	**973**	**71**	**–**	**–**	**–**	**1,044**
Premiums ceded to reinsurers	**(57)**	**(241)**	**(298)**	**(2)**	**–**	**–**	**–**	**(300)**
Net earned premiums	**281**	**394**	**675**	**69**	**–**	**–**	**–**	**744**
Fee and commission income	**160**	**150**	**310**	**70**	**54**	**–**	**–**	**434**
Investment return	**1,642**	**4,854**	**6,496**	**564**	**166**	**47**	**(42)**	**7,231**
Total revenue	**2,083**	**5,398**	**7,481**	**703**	**220**	**47**	**(42)**	**8,409**
Intersegment revenue	**–**	**–**	**–**	**–**	**–**	**42**	**(42)**	**–**
Total external revenue	**2,083**	**5,398**	**7,481**	**703**	**220**	**5**	**–**	**8,409**
Other income[iii]	**–**	**–**	**–**	**20**	**–**	**89**	**(89)**	**20**
Net claims and benefits paid	**(85)**	**(1,910)**	**(1,995)**	**(9)**	**–**	**–**	**–**	**(2,004)**
Movement in insurance and investment contract liabilities	**(1,622)**	**(2,615)**	**(4,237)**	**(554)**	**(114)**	**–**	**–**	**(4,905)**
Transfer from/(to) unallocated surplus	**–**	**4**	**4**	**(3)**	**–**	**–**	**–**	**1**
Movement in net assets attributable to unit-holders	**(42)**	**(66)**	**(108)**	**–**	**–**	**–**	**–**	**(108)**
Acquisition expenses	**(183)**	**(31)**	**(214)**	**(46)**	**(22)**	**–**	**–**	**(282)**
Administrative and other expenses	**(145)**	**(458)**	**(603)**	**(74)**	**(104)**	**(13)**	**89**	**(705)**
Finance costs	**–**	**(74)**	**(74)**	**(4)**	**–**	**(43)**	**42**	**(79)**
Total claims, benefits and expenses	**(2,077)**	**(5,150)**	**(7,227)**	**(690)**	**(240)**	**(56)**	**131**	**(8,082)**
Intersegment expenses	**–**	**(131)**	**(131)**	**–**	**–**	**–**	**131**	**–**
Total external claims, benefits and expenses	**(2,077)**	**(5,019)**	**(7,096)**	**(690)**	**(240)**	**(56)**	**–**	**(8,082)**
Profit/(loss) before tax from continuing operations	**6**	**248**	**254**	**33**	**(20)**	**80**	**–**	**347**
Policyholder tax	**(3)**	**(274)**	**(277)**	**–**	**–**	**–**	**–**	**(277)**
Shareholder tax	**1**	**8**	**9**	**(6)**	**11**	**(23)**	**–**	**(9)**
Segmental result after tax	**4**	**(18)**	**(14)**	**27**	**(9)**	**57**	**–**	**61**

(i) Accounted for as deposits under IFRS.
(ii) Eliminations include intersegment loan interest. Intersegment transactions are undertaken on an arm's length basis.
(iii) Includes profit on the disposal of AmLife (see note 2(d)) and internal recharges on pension deficit reduction contributions.

For the half year ended 30 June 2012	UK & Heritage £m	FPI £m	Lombard £m	Restated Corporate £m	Elimination of inter-segment amounts[(ii)] £m	Restated Total £m
Gross earned premiums on insurance and investment contracts	2,842	610	948	–	–	4,400
Investment contract premiums[(i)]	(1,904)	(566)	(948)	–	–	(3,418)
Gross earned premiums	938	44	–	–	–	982
Premiums ceded to reinsurers	(325)	–	–	–	–	(325)
Net earned premiums	613	44	–	–	–	657
Fee and commission income	273	48	52	–	–	373
Investment return[(iii)]	1,890	32	607	50	(48)	2,531
Total revenue	2,776	124	659	50	(48)	3,561
Intersegment revenue	1	–	–	47	(48)	–
Total external revenue	2,775	124	659	3	–	3,561
Other income	–	–	–	–	–	–
Net claims and benefits paid	(1,782)	(3)	–	–	–	(1,785)
Movement in insurance and investment contract liabilities	(116)	(40)	(564)	–	–	(720)
Transfer to unallocated surplus	(71)	–	–	–	–	(71)
Movement in net assets attributable to unit-holders	(25)	–	–	–	–	(25)
Acquisition expenses	(216)	(37)	(21)	–	–	(274)
Administrative and other expenses[(iii)]	(563)	(70)	(106)	(1)	–	(740)
Finance costs	(68)	(4)	(1)	(52)	48	(77)
Total claims, benefits and expenses	(2,841)	(154)	(692)	(53)	48	(3,692)
Intersegment expenses	(38)	(1)	–	(9)	48	–
Total external claims, benefits and expenses	(2,803)	(153)	(692)	(44)	–	(3,692)
Share of loss of associates and joint venture	–	(2)	–	–	–	(2)
Loss before tax from continuing operations	(65)	(32)	(33)	(3)	–	(133)
Policyholder tax	(34)	–	–	–	–	(34)
Shareholder tax	98	5	14	(8)	–	109
Segmental result after tax	(1)	(27)	(19)	(11)	–	(58)

(i) Accounted for as deposits under IFRS.

(ii) Eliminations include intersegment premiums and loan interest. Intersegment transactions are undertaken on an arm's length basis.

(iii) As a result of the revision to IAS19: *Employee benefits*, curtailment gains of £10 million have been presented within administrative expenses, rather than within investment return. Refer to note 6 for further details.

For the year ended 31 December 2012	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Restated Corporate £m	Elimination of inter-segment amounts[(ii)] £m	Restated Total £m
Gross earned premiums on insurance and investment contracts	3,389	2,596	5,985	1,268	2,377	–	–	9,630
Investment contract premiums[(i)]	(2,814)	(1,383)	(4,197)	(1,150)	(2,377)	–	–	(7,724)
Gross earned premiums	575	1,213	1,788	118	–	–	–	1,906
Premiums ceded to reinsurers	(85)	(512)	(597)	(5)	–	–	–	(602)
Net earned premiums	490	701	1,191	113	–	–	–	1,304
Fee and commission income	310	259	569	75	105	–	–	749
Investment return[(iii)]	1,476	6,108	7,584	305	1,154	96	(94)	9,045
Total revenue	2,276	7,068	9,344	493	1,259	96	(94)	11,098
Intersegment revenue	–	1	1	–	–	93	(94)	–
Total external revenue	2,276	7,067	9,343	493	1,259	3	–	11,098
Other income	–	–	–	–	–	–	–	–
Net claims and benefits paid	(234)	(3,243)	(3,477)	(18)	–	–	–	(3,495)
Movement in insurance and investment contract liabilities	(1,348)	(2,283)	(3,631)	(347)	(1,066)	–	–	(5,044)
Transfer to unallocated surplus	–	(1)	(1)	(3)	–	–	–	(4)
Movement in net assets attributable to unit-holders	(50)	(68)	(118)	–	–	–	–	(118)
Acquisition expenses	(372)	(111)	(483)	(89)	(42)	–	–	(614)
Administrative and other expenses[(iii)]	(353)	(842)	(1,195)	(183)	(207)	(12)	–	(1,597)
Finance costs	–	(138)	(138)	(8)	(1)	(104)	94	(157)
Total claims, benefits and expenses	(2,357)	(6,686)	(9,043)	(648)	(1,316)	(116)	94	(11,029)
Intersegment expenses	–	(77)	(77)	(1)	–	(16)	94	–
Total external claims, benefits and expenses	(2,357)	(6,609)	(8,966)	(647)	(1,316)	(100)	–	(11,029)
Share of loss of associates and joint venture	–	(1)	(1)	(2)	–	–	–	(3)
(Loss)/profit before tax from continuing operations	(81)	381	300	(157)	(57)	(20)	–	66
Policyholder tax	(1)	(257)	(258)	–	–	–	–	(258)
Shareholder tax	21	100	121	26	22	(18)	–	151
Segmental result after tax	(61)	224	163	(131)	(35)	(38)	–	(41)

(i) Accounted for as deposits under IFRS.

(ii) Eliminations include intersegment loan interest. Intersegment transactions are undertaken on an arm's length basis.

(iii) As a result of the revision to IAS19: *Employee benefits*, curtailment gains of £32 million have been presented within administrative expenses, rather than within investment return. Refer to note 6 for further details.

(iv) Assets and liabilities

As at 30 June 2013	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Elimination of inter-segment amounts (i) £m	Total £m
Segment assets	**23,969**	**79,038**	**103,007**	**8,999**	**20,785**	**2,170**	**(1,479)**	**133,482**
Investment in joint venture	**–**	**4**	**4**	**–**	**–**	**–**	**–**	**4**
Total assets	**23,969**	**79,042**	**103,011**	**8,999**	**20,785**	**2,170**	**(1,479)**	**133,486**
Total liabilities	**22,846**	**76,340**	**99,186**	**8,709**	**20,404**	**1,104**	**(1,479)**	**127,924**

As at 30 June 2012	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Elimination of inter-segment amounts(i) £m	Total £m
Segment assets	97,680	7,746	18,550	2,097	(1,314)	124,759
Investments in associates and joint venture	5	30	–	–	–	35
Total assets	97,685	7,776	18,550	2,097	(1,314)	124,794
Total liabilities	93,390	7,439	18,164	1,332	(1,314)	119,011

As at 31 December 2012	UK £m	Heritage £m	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Elimination of inter-segment amounts(i) £m	Total £m
Segment assets	21,725	77,530	99,255	8,306	19,485	2,102	(1,443)	127,705
Investments in associates held for sale and joint venture	–	4	4	30	–	–	–	34
Total assets	21,725	77,534	99,259	8,336	19,485	2,102	(1,443)	127,739
Total liabilities	20,609	74,560	95,169	8,014	19,116	1,185	(1,443)	122,041

(i) Eliminations mainly comprise intercompany loans.

(c) Geographical segmental information

In presenting geographical segmental information, revenue is based on the geographical location of customers. The Group has defined two geographical areas: UK and the rest of the world.

For the half year ended 30 June 2013	**UK £m**	**Rest of the world £m**	**Total £m**
Gross earned premiums	**973**	**71**	**1,044**
Fee and commission income	**321**	**113**	**434**
Revenue from external customers	**1,294**	**184**	**1,478**
Investment return			**7,231**
Premiums ceded to reinsurers			**(300)**
Total revenue			**8,409**

For the half year ended 30 June 2012	UK £m	Rest of the world £m	Restated Total £m
Gross earned premiums	937	45	982
Fee and commission income	281	92	373
Revenue from external customers	1,218	137	1,355
Investment return			2,531
Premiums ceded to reinsurers			(325)
Total revenue			3,561

For the year ended 31 December 2012	UK £m	Rest of the world £m	Restated Total £m
Gross earned premiums	1,785	121	1,906
Fee and commission income	587	162	749
Revenue from external customers	2,372	283	2,655
Investment return			9,045
Premiums ceded to reinsurers			(602)
Total revenue			11,098

(d) Disposal of investment in associate undertakings

On 4 January 2013 the Company disposed of its entire holding of 30% of the ordinary share capital of both AmLife Insurance Berhad and AmFamily Takaful Berhad (collectively “AmLife”) to AmBank Group of Malaysia for RM 245 million (£50 million) resulting in a profit on disposal of £20 million.

The Group’s share of the carrying value of AmLife at the date of sale on 4 January 2013 is shown below:

	£m
Carrying value at date of disposal	**30**
Disposal proceeds	**50**
Profit on disposal recognised through other income	**20**

3. Appropriations of profit

(a) Dividends paid on ordinary shares

A final dividend in respect of 2012 of 14.09 pence per share was paid on 20 May 2013 totalling £200 million. As required by IFRS, the costs of these dividends are taken directly to reserves. An interim dividend of 7.05 pence per ordinary share will be paid on 4 October 2013 to all shareholders on the register at the close of business on 6 September 2013.

As required by IAS 10: *Events after the reporting period*, dividends declared after the statement of financial position date are not accrued in these accounts.

(b) STICS interest

The STICS are accounted for as equity instruments under IFRS and consequently the interest on the STICS is recorded in the financial statements as though it were a dividend.

Interest on the 2003 STICS is paid in equal instalments in May and November each year at a rate of 6.875%. During the half year ended 30 June 2013, interest of £7 million (30 June 2012: £7 million, 31 December 2012: £14 million) was paid to the 2003 STICS holders.

Interest on the 2005 STICS is paid annually at a rate of 6.292%. During the half year ended 30 June 2013, interest of £nil (30 June 2012: £nil, 31 December 2012: £17 million) was paid to the 2005 STICS holders. The annual interest payment of £17 million for 2013 was made on 1 July 2013.

4. Earnings per share

(a) Basic and operating earnings per share from continuing operations

Earnings per share have been calculated based on the profit after tax and on the operating profit after tax attributable to equity holders of the parent and the weighted number of shares in issue. The Directors consider that operating earnings per share provides a better indication of the performance of the Group.

	2013 Half year earnings £m	**2013 Half year per share pence**	2012 Half year earnings £m	2012 Half year per share pence	2012 Full year earnings £m	2012 Full year per share pence
Profit/(loss) after tax attributable to equity holders of the parent	**45**	**3.17**	(74)	(5.37)	(72)	(5.17)
Add back:						
-short-term fluctuations in investment return	**(133)**	**(9.38)**	(18)	(1.30)	(275)	(19.76)
-non-recurring items	**37**	**2.61**	118	8.56	258	18.54
-amortisation and impairment of acquired intangible assets	**233**	**16.44**	246	17.85	514	36.94
-tax charge/(credit) on items excluded from operating profit	**6**	**0.42**	(116)	(8.42)	(149)	(10.71)
Operating profit after tax attributable to equity holders of the parent	**188**	**13.26**	156	11.32	276	19.84

(b) Diluted basic earnings per share from continuing operations

There were no dilutive factors for the half years ended 30 June 2013 and 2012, or for the full year ended 31 December 2012.

(c) Weighted average number of ordinary shares

For the half year ended 30 June 2013	**Actual**	**Weighted**
Issued ordinary shares at beginning of period	**1,418,109,028**	**1,418,109,028**
Number of ordinary shares at end of period	**1,418,109,028**	**1,418,109,028**

For the half year ended 30 June 2012	Actual	Weighted
Issued ordinary shares at beginning of period	1,376,188,989	1,376,188,989
Own shares held by the Group	(2,661,384)	(2,661,384)
	1,373,527,605	1,373,527,605
Effect of:		
– scrip dividend (final 2011)	15,484,945	3,441,099
– reduction in own shares held by the Group	2,661,384	1,345,477
Number of ordinary shares at end of period	1,391,673,934	1,378,314,181

For the year ended 31 December 2012	Actual	Weighted
Issued ordinary shares at beginning of period	1,376,188,989	1,376,188,989
Own shares held by the Group	(2,661,384)	(2,661,384)
	1,373,527,605	1,373,527,605
Effect of:		
– scrip dividend (final 2011)	15,484,945	9,477,125
– scrip dividend (interim 2012)	26,435,094	6,283,752
– reduction in own shares held by the Group	2,661,384	1,999,674
Number of ordinary shares at end of period	1,418,109,028	1,391,288,156

5. Taxation

(a) Tax recognised in the income statement

	2013 Half year £m	2012 Half year £m	2012 Full year £m
Current tax			
UK corporation tax at 23.25% (2012: 24.5%)	**67**	24	68
Adjustments in respect of prior periods	**(6)**	(1)	(4)
Overseas taxation	**8**	12	11
Total current tax charge	**69**	35	75
Deferred tax			
Origination and reversal of temporary differences	**217**	(113)	31
Adjustments in respect of prior periods	**–**	3	1
Total deferred tax charge/(credit)	**217**	(110)	32
Total tax charge/(credit)	**286**	(75)	107
Analysis:			
– policyholder tax	**277**	34	258
– shareholder tax	**9**	(109)	(151)
Total tax charge/(credit)	**286**	(75)	107

Policyholder tax is tax on the income and investment returns charged to the policyholders of linked and with–profits funds. Shareholder tax is tax charged to shareholders on the profits of the Group.

Legislation was enacted to decrease the rate of corporation tax from 24% on 1 April 2012 to 23% on 1 April 2013. Under IFRS, deferred tax is calculated using rates substantively enacted by the statement of financial position date and as such the reduction to a 23% rate has been taken into account in deferred tax balances. The average rate of corporation tax for the full calendar year is 23.25%.

Further incremental rate reductions were announced in the Chancellor's Autumn Statement on 5 December 2012 and Budget on 20 March 2013 and included in the 2013 Finance Bill. These will reduce the rate to 21% from 1 April 2014 and to 20% from 1 April 2015. The Bill only received Royal Assent in July 2013, after the balance sheet date, and therefore the changes in tax rate have not been taken into account in these financial statements; however the combined benefit to the Group's net assets of these reductions is estimated to be approximately £90 million.

(b) Factors affecting tax recognised in the period

	2013 Half year £m	2012 Half year £m	2012 Full year £m
Profit/(loss) before tax from continuing operations	**347**	(133)	66
Profit/(loss) before tax from continuing operations determined with reference to the average rate of corporation tax in the UK of 23.25% (2012: 24.5%)	**81**	(33)	16
Effects of:			
- non-taxable income	**(109)**	(22)	(120)
-deductions not allowable for tax purposes	**10**	5	26
-tax on reserving and other IFRS adjustments	**(14)**	6	24
-overseas tax	**–**	(6)	(10)
-valuation of excess expenses	**–**	12	–
-valuation of tax losses	**(28)**	(30)	(75)
-valuation of unrealised capital losses	**67**	(14)	43
-adjustments in respect of prior periods	**2**	(1)	(2)
-reduction in corporation tax rate to 23% (2012: 24%)	**–**	(30)	(61)
-non taxable result of the Resolution holding companies	**–**	4	8
-policyholder tax	**277**	34	258
Total tax charge/(credit)	**286**	(75)	107

(c) Impact of new life tax regime

Legislation in respect of the new life tax regime became effective from 1 January 2013. As a result, the impact of the change in the new tax regime in both current and deferred tax measures has been fully reflected in the IFRS financial statements as at 30 June 2013.

6. Staff pension schemes

(a) Introduction

The Group operates a defined benefit scheme, the Friends Provident Pension Scheme ("FPPS"), which closed to active membership as at 31 December 2012. On 1 January 2013, the Group set up a defined contribution scheme 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 13.2% depending on contribution levels selected by members and the platform has a minimum employer plus member contribution level of 9% 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 May 2013. FPIL and Sesame Bankhall Group ("SBG") operate defined contribution arrangements. Lombard does not operate a pension scheme.

(b) FPPS defined benefit scheme overview

On an IAS 19(R): *Employee benefits* basis, a gross surplus of £39 million has been recognised in respect of the FPPS at 30 June 2013 (30 June 2012: £78 million, 31 December 2012: £62 million). A deficit reduction plan was entered into during January 2013 based on the triennial valuation as at 30 September 2011, which showed a deficit on a funding basis of £185 million. That plan set out a new schedule of deficit reduction contributions of £175 million, in addition to a £20 million payment which was made in July 2012 and £20 million already scheduled for payment in July 2013 under the previous deficit reduction plan. The new recovery plan commenced in January 2013 with a payment of £1.5 million, and a further £1.5 million has been paid in July 2013 in addition to the £20 million previously agreed. Further deficit reduction contributions totalling £172 million will be paid into the scheme, with payments of £21.5 million to be made by 31 July each year for the next eight years from 2014 to 2021.

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. An additional liability of £70 million has been recognised at 30 June 2013 (30 June 2012: £41 million, 31 December 2012: £29 million), reflecting the 35% tax that would arise on any notional refund in respect of the resultant IAS 19 surplus of £203 million (£194 million of deficit reduction contributions at a present value of £164 million plus the current surplus of £39 million). A deferred tax asset of £44 million (30 June 2012: £10 million, 31 December 2012: £5 million) has also been recognised to reflect tax relief at a rate of 23% (30 June 2012: 24%, 31 December 2012: 23%) that is expected to be available on the deficit reduction contributions, in future periods.

The scheme's assets, which are administered by four external investment managers, are held under the control of the Trustee and used to secure benefits for the members of the scheme and their dependants in accordance with the Trust Deed and Rules.

The Trustee board consists of a chairman who is appointed by the employer and six additional directors of which three are employer-appointed directors and three are member nominated trustee directors.

An analysis of the amounts recognised in the financial statements in respect of the FPPS is set out below.

(i) Amounts recognised in the condensed consolidated statement of financial position

	30 June 2013 £m	30 June 2012 £m	31 December 2012 £m
IAS 19 pension surplus (excluding deficit reduction contribution)	**39**	78	62
Authorised payments surplus charge (penal tax) at 35% of available surplus following deficit reduction contributions	**(70)**	(41)	(29)
Net pension (deficit)/surplus (excluding deficit reduction contribution)	**(31)**	37	33

(ii) Movement in IAS 19 pension surplus

	2013 Half year £m	Restated[iv] 2012 Half year £m	Restated[iv] 2012 Full year £m
Pension surplus at 1 January	**62**	52	52
Current service cost[i]	**(1)**	(4)	(7)
Past service cost[i][ii]	**–**	10	32
Net interest cost on defined benefit scheme [i][iii]	**1**	2	3
Employer contributions	**6**	3	27
Remeasurements on defined benefit scheme	**(29)**	15	(45)
Pension surplus (excluding authorised payments surplus charge)	**39**	78	62
Deficit reduction contributions	**164**	40	20
Available surplus subject to authorised payments surplus charge	**203**	118	82

(i) Recognised in the condensed consolidated income statement. The total gain recognised in the income statement for the half year ended 30 June 2013 is £nil million (30 June 2012: gain of £8 million, 31 December 2012: gain of £28 million).

(ii) The restated past service cost for 2012 includes two credits resulting from curtailment gains arising within the FPPS. The credit of £10 million for the six months ended 30 June 2012 is as a result of the curtailment gain on the Diligenta outsourcing agreement entered into by the Group in January 2012. The additional credit of £22 million for the year ended 31 December 2012 arises as a result of the closure of the FPPS to future accrual in the second half of the year.

(iii) The actual return on plan assets was £105 million (30 June 2012: £19 million, 31 December 2012: £64 million).

(iv) As a result of the revision to IAS19: *Employee benefits*, comparatives have been restated as follows:

- Service cost is now split into current service cost and past service cost.
- Curtailment gains of £10 million for the six months ended 30 June 2012 and £32 million for the year ended 31 December 2012 are now presented as a past service cost.
- Actuarial gains and losses are now presented as remeasurements of the defined benefit scheme.
- Interest cost and expected return on plan assets have been replaced with net interest cost on defined benefit scheme calculated by applying the discount rate used to measure the define benefit obligation to the net defined benefit liability/(asset).

(iii) Analysis of pension surplus/(deficit) and related deferred tax balances

As at 30 June 2013	**Pension surplus/(deficit) £m**	**Deferred tax £m**
Gross IAS 19 pension surplus and related deferred tax liability	**39**	**(9)**
Irrecoverable element of deficit reduction contributions (authorised payments surplus charge on available surplus)	**(70)**	**–**
Restriction of liability due to authorised payments surplus charge	**–**	**9**
Tax relief available on deficit reduction contributions	**–**	**44**
Net pension deficit and related deferred tax asset	**(31)**	**44**

As at 30 June 2012	Pension surplus £m	Deferred tax £m
Gross IAS 19 pension surplus and related deferred tax liability	78	(19)
Irrecoverable element of deficit reduction contributions (authorised payments surplus charge on available surplus)	(41)	–
Restriction of liability due to authorised payments surplus charge	–	19
Tax relief available on deficit reduction contributions	–	10
Net pension surplus and related deferred tax asset	37	10

As at 31 December 2012	Pension surplus £m	Deferred tax £m
Gross IAS 19 pension surplus and related deferred tax liability	62	(14)
Irrecoverable element of deficit reduction contributions (authorised payments surplus charge on available surplus)	(29)	–
Restriction of liability to authorised payments surplus charge	–	14
Tax relief available on deficit reduction contributions	–	5
Net pension surplus and related deferred tax asset	33	5

(iv) Amounts recognised in the condensed consolidated statement of comprehensive income

	2013 Half year £m	2012 Half year £m	2012 Full year £m
Actuarial (losses)/gains	**(29)**	15	(45)
Reverse authorised payments surplus charge on opening surplus	**29**	32	32
Irrecoverable element of deficit reduction contributions (authorised payments surplus charge on available surplus)	**(70)**	(41)	(29)
Remeasurements on defined benefit scheme	**(70)**	6	(42)
Taxation	**50**	2	7
Remeasurements on defined benefit scheme after tax	**(20)**	8	(35)

A tax credit of £39 million (30 June 2012: £nil, 31 December 2012: tax charge of £(5) million) in respect of deficit reduction contributions and credits of £11 million (30 June 2012: £2 million, 31 December 2012: £12 million) in respect of other movements in the pension scheme are included in the aggregate tax line of the condensed consolidated statement of comprehensive income.

7. Intangible assets

Movements in intangible assets are as follows:

For the half year ended 30 June 2013	**AVIF**	**Other**	**Total**
Cost	**£m**	**£m**	**£m**
At 1 January 2013	**5,505**	**560**	**6,065**
Other additions	**–**	**2**	**2**
Foreign exchange adjustments	**33**	**9**	**42**
At 30 June 2013	**5,538**	**571**	**6,109**
Amortisation and impairment			
At 1 January 2013	**1,497**	**247**	**1,744**
Amortisation charge for the period[(i)]	**192**	**41**	**233**
Foreign exchange adjustments	**12**	**5**	**17**
At 30 June 2013	**1,701**	**293**	**1,994**
Carrying amounts at 30 June 2013	**3,837**	**278**	**4,115**

For the half year ended 30 June 2012	AVIF	Other	Total
Cost	£m	£m	£m
At 1 January 2012	5,521	560	6,081
Other additions	–	1	1
Foreign exchange adjustments	(19)	(5)	(24)
At 30 June 2012	5,502	556	6,058
Amortisation and impairment			
At 1 January 2012	1,084	150	1,234
Amortisation charge for the period[(i)]	204	42	246
Foreign exchange adjustments	(5)	(2)	(7)
At 30 June 2012	1,283	190	1,473
Carrying amounts at 30 June 2012	4,219	366	4,585

For the year ended 31 December 2012	AVIF	Other	Total
Cost	£m	£m	£m
At 1 January 2012	5,521	560	6,081
Other additions	–	4	4
Foreign exchange adjustments	(16)	(4)	(20)
At 31 December 2012	5,505	560	6,065
Amortisation and impairment			
At 1 January 2012	1,084	150	1,234
Amortisation charge for the period[(i)]	412	83	495
Impairment charge for the period[(i)(ii)]	5	14	19
Foreign exchange adjustments	(4)	–	(4)
At 31 December 2012	1,497	247	1,744
Carrying amounts at 31 December 2012	4,008	313	4,321

(i) Amortisation and impairment charges are included within administrative and other expenses in the condensed consolidated income statement.

(ii) Includes a £12 million impairment of goodwill and £2 million impairment of distributor relationships in respect of Financial Business Partners AG (“fpb AG”) part of the FPI segment. AVIF impairment of £5 million has been recognised within the Overseas Life Assurance Business (“OLAB”) in the FPI segment, as a result of assumption changes and worsening persistency.

In determining the fair value of identified intangible assets, appropriate valuation methodologies were applied, given the nature of the intangible assets acquired.

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.

For each type of asset, the useful economic life was determined, being the period over which the asset is expected to contribute directly or indirectly to future cash flows. The value of the assets will be amortised over the respective useful economic lives.

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 consolidated statement of financial position as AVIF. The AVIF is based on the value of in-force business calculated on a market consistent embedded value basis.

An analysis of intangible assets by significant cash generating unit (“CGU”) is shown below. UK and Heritage intangible assets have been allocated to separate UK and Heritage CGUs, consistent with the Group’s revised operating segmentation. This revised split is not available for the half year ended 30 June 2012 and the costs to develop would be excessive.

As at 30 June 2013	Cost £m	Amortisation and impairment £m	Net book value £m
UK	**1,213**	**(402)**	**811**
Heritage	**3,032**	**(818)**	**2,214**
FPI	**1,076**	**(427)**	**649**
Lombard	**785**	**(344)**	**441**
Corporate	**3**	**(3)**	**–**
Total	**6,109**	**(1,994)**	**4,115**

As at 30 June 2012	Cost £m	Amortisation and impairment £m	Net book value £m
UK & Heritage	4,244	(910)	3,334
FPI	1,076	(315)	761
Lombard	735	(245)	490
Corporate	3	(3)	–
Total	6,058	(1,473)	4,585

As at 31 December 2012	Cost £m	Amortisation and impairment £m	Net book value £m
UK	1,213	(356)	857
Heritage	3,032	(715)	2,317
FPI	1,076	(383)	693
Lombard	741	(287)	454
Corporate	3	(3)	–
Total	6,065	(1,744)	4,321

Impairment

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.

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.

As at 30 June 2013, based on an impairment review of each of the CGUs, the Directors are satisfied that none of the Group's intangible assets are impaired. Following an impairment review at 31 December 2012, FPI AVIF in respect of its OLAB operation and other intangible assets in respect of fpb AG, the Group’s distributor of German business, were impaired by £(5) million and £(14) million respectively.

8. Financial assets

The Group's financial assets are summarised by measurement category as follows:

	30 June 2013 £m	30 June 2012 £m	31 December 2012 £m
Fair value through profit or loss (note 8 (a))	**111,421**	102,939	105,984
Loans at amortised cost (note 8 (g))	**6**	6	6
Total financial assets	**111,427**	102,945	105,990

(a) Analysis of financial assets at fair value through profit or loss

As at 30 June 2013	**With-profits £m**	**Unit-linked £m**	**Non-linked annuities £m**	**Non-linked other £m**	**Share holder £m**	**Total £m**
Shares and other variable yield securities	**7,110**	**62,485**	**–**	**139**	**15**	**69,749**
Debt securities and other fixed income securities:						
Government securities	**8,647**	**7,541**	**1,013**	**1,072**	**97**	**18,370**
Corporate bonds	**8,533**	**5,991**	**6,776**	**1,311**	**192**	**22,803**
Derivative financial instruments	**185**	**48**	**19**	**7**	**24**	**283**
Deposits with credit institutions	**–**	**216**	**–**	**–**	**–**	**216**
Total financial assets held at fair value	**24,475**	**76,281**	**7,808**	**2,529**	**328**	**111,421**

As at 30 June 2012	With-profits £m	Unit-linked £m	Non-linked annuities £m	Non-linked other £m	Share holder £m	Total £m
Shares and other variable yield securities	6,332	53,333	–	107	10	59,782
Debt securities and other fixed income securities:						
Loaned government securities[(i)]	–	–	–	205	–	205
Other government securities	8,723	7,970	1,104	962	156	18,915
Corporate bonds	8,923	5,899	6,234	1,227	277	22,560
Derivative financial instruments	915	52	110	10	–	1,087
Deposits with credit institutions	–	390	–	–	–	390
Total financial assets held at fair value	24,893	67,644	7,448	2,511	443	102,939

(i) On 11 May 2011, the Group provided a £200 million collateralised loan to Barclays Bank plc which matured on 31 August 2012. UK government securities were loaned and the assets remained on the statement of financial position up until 31 August 2012 as substantially all the risks and rewards of ownership were retained by the Group.

As at 31 December 2012	With-profits £m	Unit-linked £m	Non-linked annuities £m	Non-linked other £m	Share holder £m	Total £m
Shares and other variable yield securities	6,801	56,940	–	125	13	63,879
Debt securities and other fixed income securities:						
Government securities	8,903	7,617	1,018	1,074	79	18,691
Corporate bonds	8,533	5,891	6,546	1,302	124	22,396
Derivative financial instruments	675	22	107	8	–	812
Deposits with credit institutions	–	206	–	–	–	206
Total financial assets held at fair value	24,912	70,676	7,671	2,509	216	105,984

The unit-linked column and with-profits column include £781 million (30 June 2012: £879 million; 31 December 2012: £744 million) of financial assets comprising £582 million of shares and other variable yield securities, £108 million of corporate bonds and £91 million of government securities (30 June 2012: £706 million of shares and other variable yield securities, £100 million of corporate bonds and £73 million of government securities; 31 December 2012: £535 million of shares and other variable yield securities, £87 million of government securities and £122 million of corporate bonds) relating to the minority interests in the OEICs that have been consolidated as the Group holding is 50% or more.

For unit-linked funds, the policyholders bear the investment risk and any change in asset values is matched by a broadly equivalent change in the liability.

Asset backed securities (excluding those held by the linked funds) amount to £4,102 million (30 June 2012: £3,218 million; 31 December 2012: £3,940 million) and 97% (30 June 2012: 95%; 31 December 2012: 96%) of these are at investment grade as set out in 8(f).

(b) Determination of fair value hierarchy

In accordance with the requirements of IFRS 13: *Fair value measurement* assets which are measured at fair value have been classified into three categories as set out below. Financial assets at fair value include shares and other variable yield securities, government securities, corporate bonds (including ABS), derivative financial instruments and deposits with credit institutions.

Level 1 – quoted prices (unadjusted) in active markets for identical assets. An active market is one in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis. Examples include listed equities and bonds in active markets and quoted unit trusts/OEICs.

Level 2 – inputs other than quoted prices included within Level 1 that are observable for the asset, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category generally includes assets that are priced based on models using market observable inputs. Examples include certain corporate bonds, certificates of deposit and derivatives.

Level 3 – inputs for the asset that are not based on observable market data. Assets with single price feeds and/or limited trading activity are included in this category. Examples include unlisted equities and private equity investments.

The majority of the Group's assets held at fair value are valued based on quoted market information or market observable data. Approximately 6% (9% excluding unit-linked assets) are based on valuation techniques where significant observable market data is not available or the price is not observable from current market transactions. However, the fair value measurement objective of these assets remains the same, that is, an exit price from the perspective of the Group.

The fair values of these assets are generally provided by external parties. During the year, the Group has performed independent reviews of pricing models to ensure that appropriate methodologies have been applied. The approach taken for each class of specific unlisted investment is as follows:

Corporate bond valuations are generally obtained from brokers and pricing services. Where the number of transactions has declined under the current market conditions, valuations have become more subjective. Bond prices provided by pricing services are based on the best estimate of market price determined by market makers based on a variety of factors and are considered to be observable prices. In determining fair value, market makers will take into account transactions they have observed in identical or similar assets as well as movements in market indices and any other factors that they regard as relevant. In some cases, consensus prices have been based on fewer, and potentially more historic, transactions.

Exchange-traded derivatives are valued using active market prices. The values of over-the-counter derivative financial instruments are estimated by applying valuation techniques, using pricing models or discounted cash flow methods. Where pricing models are used, inputs – including future dividends, swap rates and volatilities – based on market data at the statement of financial position date are used to estimate derivative values. Where discounted cash flow techniques are used, estimated future cash flows and discount rates are based on current market swap rates at the valuation date.

Investment properties and properties occupied by the Group are measured at fair value at least annually at the statement of financial position date. Fair values are measured by external independent valuers on the basis of open market value using methods set out in the Royal Institute of Chartered Surveyors' guidelines (“RICS Red Book”). The valuations used are based on valuation techniques using multiples of future rental incomes. The rental multiples are based on multiples observed in recent similar transactions in the market. Key assumptions include occupancy and rental income.

Methods considered when determining fair values of unlisted shares and other variable yield securities include discounted cash flow techniques and net asset valuation. Regular checks are performed of tolerance levels for changes such as percentage movements in prices, excess movements and inter vendor price comparisons, where tolerance levels are pre-defined for security types.

The fair value of the investments in property limited partnerships is taken as the Group's appropriate share of the net asset value of the partnerships. The net asset value is based on the latest external market valuation of the underlying property investments, which is updated at least every six months. The valuation would be adjusted in the event of a significant market movement in the period between the last market valuation and the reporting date.

Private loans are valued using discounted cash flows, which are carried out by Investment Managers and reviewed by management. The interest rate used when calculating the present value is derived from the UK Gilts Curve, adjusting the spread by the movement in the most appropriate IBoxx GBP Corp Curve associated with the loan rating, where available. All spreads are reviewed on a quarterly basis and any spreads that appear inappropriate taking into consideration loan details (loan sector, maturity, and rating), available market proxies, comparable instruments and underlying securities are recalibrated accordingly.

The Group has invested in a mortgage loan issued by AXA Equitable in the US. The mortgage loan is secured against the property. The loan is valued by external real estate advisors using discounted cash flows. The discount rate used in the calculation is determined by adding an appropriate spread (based on property type, prevailing interest rates and the current mortgage spread over US treasuries) to the yield of an appropriate US Treasury Bond with the maturity closest to the maturity of the loan. The loan is denominated in US dollars. As at 30 June 2013, the loan was valued at £86 million (30 June 2012: £85 million, 31 December 2012: £80 million).

Participation in investment pools mainly relates to property investments. Property is independently valued in accordance with the methods set out in the RICS Red Book on the basis of open market values as at each year end.

The requirements of IFRS 13 also require financial liabilities at fair value to be categorised into Level 1, 2 or 3 hierarchies. Financial liabilities at fair value include unit-linked contracts, amounts due to reinsurers, net asset value attributable to unit-holders (non-controlling interest in the OEICs that are consolidated) and derivative financial instruments. The classifications take into account the types of inputs used to determine the fair value measurements. For unit-linked funds this has been undertaken on a fund-by-fund basis. For the net asset value attributable to unit-holders, this has been analysed in the same proportion as the underlying consolidated investments categorisation.

The Group is unable to reliably measure the fair value of investment contracts with discretionary participation features due to the lack of a robust basis to measure the supplemental discretionary returns arising on with-profits contracts and because there is not an active market for such instruments. These liabilities have therefore been excluded from the fair value hierarchy analysis below.

An analysis of financial assets and liabilities held at fair value in accordance with the fair value hierarchy is set out below. The table shows both the total financial assets and liabilities and the total excluding unit-linked assets and liabilities, as shareholders have no direct exposure to profits or losses on unit-linked assets (other than through investment management and annual management fees).

Recurring fair value measurements

As at 30 June 2013	Including unit-linked Level 1 £m	Level 2 £m	Level 3 £m	Total £m	Excluding unit-linked Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Non-financial assets held at fair value								
Investment properties	**–**	**–**	**2,621**	**2,621**	**–**	**–**	**1,267**	**1,267**
Owner-occupied property	**–**	**–**	**40**	**40**	**–**	**–**	**40**	**40**
Financial assets held at fair value								
Shares and other variable yield securities	**60,513**	**5,849**	**3,387**	**69,749**	**5,434**	**598**	**1,232**	**7,264**
Debt securities and other fixed income securities:								
Government securities	**17,875**	**489**	**6**	**18,370**	**10,666**	**157**	**6**	**10,829**
Corporate bonds (including ABS)	**16,174**	**5,349**	**1,280**	**22,803**	**12,563**	**3,620**	**629**	**16,812**
Derivative financial instruments	**59**	**224**	**–**	**283**	**21**	**214**	**–**	**235**
Deposits with credit institutions	**216**	**–**	**–**	**216**	**–**	**–**	**–**	**–**
Total assets held at fair value	**94,837**	**11,911**	**7,334**	**114,082**	**28,684**	**4,589**	**3,174**	**36,447**
Financial liabilities held at fair value								
Unit-linked investment contracts	**–**	**72,635**	**–**	**72,635**	**–**	**–**	**–**	**–**
Amounts due to reinsurers	**–**	**1,720**	**–**	**1,720**	**–**	**1,720**	**–**	**1,720**
Net asset value attributable to unit-holders	**808**	**–**	**–**	**808**	**20**	**–**	**–**	**20**
Derivative financial instruments	**55**	**334**	**–**	**389**	**33**	**330**	**–**	**363**
Total liabilities held at fair value	**863**	**74,689**	**–**	**75,552**	**53**	**2,050**	**–**	**2,103**

There are no non-recurring fair value measurements at 30 June 2013.

As at 31 December 2012	Including unit-linked Level 1 £m	Level 2 £m	Level 3 £m	Total £m	Excluding unit-linked Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Non-financial assets held at fair value								
Investment properties	–	–	2,735	2,735	–	–	1,284	1,284
Owner-occupied property	–	–	40	40	–	–	40	40
Financial assets held at fair value								
Shares and other variable yield securities	53,459	7,608	2,812	63,879	5,156	555	1,228	6,939
Debt securities and other fixed income securities:								
Government securities	18,209	474	8	18,691	10,917	152	5	11,074
Corporate bonds (including ABS)	15,595	5,653	1,148	22,396	12,121	3,788	596	16,505
Derivative financial instruments	52	760	–	812	32	758	–	790
Deposits with credit institutions	206	–	–	206	–	–	–	–
Total assets held at fair value	87,521	14,495	6,743	108,759	28,226	5,253	3,153	36,632
Financial liabilities held at fair value								
Unit–linked investment contracts	–	67,428	–	67,428	–	–	–	–
Amounts due to reinsurers	–	1,767	–	1,767	–	1,767	–	1,767
Net asset value attributable to unit–holders	754	–	–	754	17	–	–	17
Derivative financial instruments	8	222	–	230	4	220	–	224
Total liabilities held at fair value	762	69,417	–	70,179	21	1,987	–	2,008

Comparative figures for the half year ended 30 June 2012 are not available and the costs to develop them would be excessive.

The Group's policy is to recognise transfers into and transfers out of levels 1, 2 and 3 as of the date the statement of financial position is prepared.

Derivative financial instruments and amounts due to reinsurers are managed on the basis of net exposure, after taking into account related collateral, with fair value determined on the basis of the price of the net position.

For the Friends Life Group plc £162 million subordinated debt due 2021, Friends Life Group plc £500 million subordinated debt due 2022 and the Friends Life Group plc $575 million reset perpetual subordinated debt, the fair value measurements (as disclosed in note 9) are categorised as Level 1.

(c) Transfers between Level 1 and Level 2

During the period, £368 million of corporate bonds, shares and other variable yield securities were transferred from Level 1 to Level 2 and £2,460 million of corporate bonds, shares and other variable yield securities were transferred from Level 2 to Level 1. These movements arose from changes in the availability of current quoted prices, market activity and available quoted price methodology applied for the classification of shares and other variable yield securities. There were no significant transfers between Level 1 and Level 2 for other assets.

(d) Level 3 assets

The following table shows a reconciliation of Level 3 assets which are recorded at fair value.

	Investment property	Owner-occupied property	Shares and other variable yield securities	Government bonds	Corporate bonds (including ABS)	Total assets held at fair value
	£m	£m	£m	£m	£m	£m
As at 1 January 2013	**2,735**	**40**	**2,812**	**8**	**1,148**	**6,743**
Total (losses)/gains in consolidated income statement[(i)]	**(33)**	**–**	**2**	**–**	**7**	**(24)**
Purchases	**9**	**–**	**33**	**–**	**183**	**225**
Sales	**(91)**	**–**	**(250)**	**–**	**(114)**	**(455)**
Net transfer from/(to) Level 1 and Level 2 [(ii)]	**–**	**–**	**712**	**(2)**	**26**	**736**
Foreign exchange adjustments	**1**	**–**	**78**	**–**	**30**	**109**
As at 30 June 2013	**2,621**	**40**	**3,387**	**6**	**1,280**	**7,334**
Total unrealised (losses)/gains for the period included in profit or loss for assets held at 30 June 2013	**(32)**	**–**	**(9)**	**–**	**4**	**(37)**

(i) Gains and their reversal on owner occupied property are recognised in the condensed consolidated statement of comprehensive income, losses and their reversal are recognised in the income statement. All other gains and losses on assets held at fair value are recognised in the income statement.

(ii) Amounts were transferred from Level 1 and 2 because of a lack of observable market data, resulting from a decrease in market activities for the securities. Amounts were transferred to Level 1 and Level 2 because observable market data became available for the securities.

	Shares and other variable yield securities £m	Government bonds £m	Corporate bonds (including ABS) £m	Total financial assets held at fair value £m
At 1 January 2012	3,210	5	1,259	4,474
Total gains/(losses) in consolidated income statement	66	(1)	46	111
Purchases	1,262	–	305	1,567
Sales	(1,340)	–	(526)	(1,866)
Net transfer (to)/from Level 1 and Level 2	(349)	4	84	(261)
Foreign exchange adjustments	(37)	–	(20)	(57)
At 31 December 2012	2,812	8	1,148	3,968
Total unrealised gains/(losses) for the year included in profit or loss for assets held at 31 December 2012	57	(1)	37	93

Comparative figures for the half year ended 30 June 2012 and comparative figures for investment property and owner occupied property for the year ended 31 December 2012 are not available and the costs to develop them would be excessive.

The Group's Securities Pricing Committee provides oversight of the valuation of securities, including the review of valuation methodologies, appropriateness of prices provided by external valuers, and fair value hierarchy disclosures made by the Group.

IFRS 13 requires the disclosure, where available, of quantitative information relating to significant unobservable inputs used to derive the valuation of investments classified within the fair value hierarchy as level 3. The majority of the Group's investments are valued by third parties, resulting in limited availability of unobservable inputs used. Available unobservable inputs are as follows:

- Corporate bonds include £334 million of private loans; credit rating assumptions, ranging between AA- and BB-, have been used to derive discounted cash flow fair values.
- Shares and other variable yield securities include private equity investments, £217 million of which are valued using multiples of earnings before interest, tax, depreciation and amortisation ranging between 5 and 11.5.
- Investment properties have typically been valued based on equivalent rental multiples, ranging between 4 and 30.

(e) Level 3 financial assets sensitivity analysis

	As at 30 June 2013		As at 31 December 2012	
	Carrying amount	**Effect of reasonably possible alternative assumptions**	Carrying amount	Effect of reasonably possible alternative assumptions
	£m	**£m**	£m	£m
Unit-linked investments	**2,806**	**–**	2,139	–
Shares and other variable yield securities	**1,232**	**246**	1,228	246
Government bonds	**6**	**1**	5	1
Corporate bonds (including ABS)	**629**	**63**	596	60
	4,673	**310**	3,968	307

For unit–linked funds, the policyholders bear the investment risk and any change in asset values is matched by a broadly equivalent change in the liability. Shareholder profits from annual management charges levied on such funds will, however, vary according to the change in asset values leading to some limited investment risk.

For shares and other variable yield securities, where there is no active market, the price at year end could reasonably be expected to be higher or lower by approximately 20%.

For government bonds and corporate bonds, it could reasonably be expected that the current prices could be higher or lower by approximately 10% to reflect changes in the credit ratings of the underlying bonds.

(f) Creditworthiness of financial assets

The following table gives an indication of the level of creditworthiness of those categories of assets which are neither past due nor impaired and are most exposed to credit risk using principally ratings prescribed by Standard & Poor's and Moody's. Assets held within unit–linked funds have been excluded from the tables below as the credit risk on these assets is borne by the policyholders rather than the shareholders. The carrying amount of assets included in the statement of financial position represents the maximum credit exposure.

As at 30 June 2013	AAA £m	AA £m	A £m	BBB £m	BB £m	B £m	Not rated £m	Total £m
Corporate bonds	**320**	**3,784**	**4,904**	**3,248**	**352**	**61**	**41**	**12,710**
Asset-backed securities	**1,397**	**787**	**1,356**	**450**	**56**	**36**	**20**	**4,102**
Derivative financial instruments	**–**	**2**	**214**	**–**	**–**	**–**	**19**	**235**
Reinsurance assets	**–**	**2,979**	**150**	**–**	**–**	**–**	**1**	**3,130**
Cash and cash equivalents	**2,334**	**436**	**1,818**	**13**	**–**	**–**	**38**	**4,639**
Total	**4,051**	**7,988**	**8,442**	**3,711**	**408**	**97**	**119**	**24,816**
%	**16%**	**33%**	**34%**	**15%**	**2%**	**0%**	**0%**	**100%**

As at 30 June 2012	AAA £m	AA £m	A £m	BBB £m	BB £m	B £m	Not rated £m	Total £m
Corporate bonds	1,966	2,906	4,856	3,297	312	36	70	13,443
Asset backed securities	1,017	864	758	420	136	14	9	3,218
Derivative financial instruments	–	16	993	–	–	–	26	1,035
Reinsurance assets	–	3,196	135	–	–	–	1	3,332
Cash and cash equivalents	1,864	675	1,663	–	19	–	9	4,230
Total	4,847	7,657	8,405	3,717	467	50	115	25,258
%	19%	30%	33%	15%	2%	0%	1%	100%

As at 31 December 2012	AAA £m	AA £m	A £m	BBB £m	BB £m	B £m	Not rated £m	Total £m
Corporate bonds	1,037	3,043	5,035	2,945	417	44	44	12,565
Asset backed securities	1,493	1,007	873	423	67	58	19	3,940
Derivative financial instruments	–	6	760	–	–	–	24	790
Reinsurance assets	–	3,021	131	–	–	–	1	3,153
Cash and cash equivalents	2,579	270	1,644	–	25	–	86	4,604
Total	5,109	7,347	8,443	3,368	509	102	174	25,052
%	20%	29%	34%	14%	2%	0%	1%	100%

The direct exposure of the Group to the debt of the governments of Ireland, Italy, Portugal and Spain (being countries where the risk of credit default has been perceived as higher) in shareholder and annuity funds is set out in the table below. There is no exposure to Greece. Where the Group holds securities issued by financial companies, it has considered the company's financial strength and the ability of the domicile government to provide financial support in the event of stress.

	30 June 2013			30 June 2012			31 December 2012		
	Govt. debt	**Corporate debt**	**Total**	Govt. debt	Corporate debt	Total	Govt. debt	Corporate debt	Total
	£m	**£m**	**£m**	£m	£m	£m	£m	£m	£m
Ireland	**–**	**39**	**39**	–	37	37	–	38	38
Portugal	**–**	**6**	**6**	–	8	8	–	5	5
Italy	**6**	**114**	**120**	7	152	159	7	145	152
Spain	**–**	**144**	**144**	–	168	168	–	146	146
Total	**6**	**303**	**309**	7	365	372	7	334	341

	Ireland £m	Portugal £m	Italy £m	Spain £m	Total £m
Corporate exposure:					
Domestic banks	**–**	**–**	**14**	**7**	**21**
Domestic non-bank financials	**14**	**–**	**21**	**–**	**35**
Non-domestic banks	**–**	**–**	**–**	**75**	**75**
Domestic non-financials	**25**	**6**	**79**	**61**	**171**
Non-domestic non-financials	**–**	**–**	**–**	**1**	**1**
Total 30 June 2013	**39**	**6**	**114**	**144**	**303**
Total 30 June 2012	37	8	152	168	365
Total 31 December 2012	38	5	145	146	334

(g) Loans

	30 June 2013 £m	30 June 2012 £m	31 December 2012 £m
Mortgage loans	**2**	2	2
Other loans	**4**	4	4
Total loans	**6**	6	6

(h) Assets backing unit-linked liabilities

The net assets backing the insurance and investment contract liabilities relating to unit-linked business are included within the relevant balances in the condensed consolidated statement of financial position and are analysed as follows:

	30 June 2013 £m	30 June 2012 £m	31 December 2012 £m
Shares and other variable yield securities	**62,485**	53,333	56,940
Debt securities and other fixed income securities	**13,532**	13,869	13,508
Derivative financial instruments	**48**	52	22
Deposits with credit institutions	**216**	390	206
Total financial assets held at fair value	**76,281**	67,644	70,676
Investment properties	**1,354**	1,592	1,451
Insurance and other receivables	**864**	457	723
Cash and cash equivalents	**5,165**	4,443	4,835
Total assets	**83,664**	74,136	77,685
Net asset value attributable to unit-holders[(i)] and other payables	**(2,161)**	(1,207)	(1,743)
Total unit-linked net assets	**81,503**	72,929	75,942

(i) Represents consolidation adjustments in respect of OEICs which the Group is deemed to control.

9. Loans and borrowings

The Group's loans and borrowings are as follows:

	Coupon %	**30 June 2013 £m**	30 June 2012 £m	31 December 2012 £m
Subordinated liabilities:				
Lombard undated subordinated loans	Various	**–**	2	1
Friends Life Group plc £162 million LT2 subordinated debt 2021	12.00	**180**	182	181
Friends Life Group plc £500 million LT2 subordinated debt 2022	8.25	**497**	496	496
Friends Life Group plc $575 million UT2 perpetual subordinated debt	7.875	**371**	–	346
Deferred consideration notes:				
Series A deferred consideration notes	6.00	**–**	174	–
Series B deferred consideration notes	7.25 – 6.50	**–**	189	–
Reinsurance:				
Lombard financial reinsurance treaties	Various	**4**	6	4
FPI financial reinsurance treaties	Various	**43**	53	57
Other:				
Amounts owed to credit institutions (overdrafts)		**17**	13	14
Total loans and borrowings		**1,112**	1,115	1,099

Unless otherwise stated below, the carrying values of interest bearing loans and borrowings closely approximate fair value.

Subordinated liabilities

The FLG LT2 subordinated debt 2021 is 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 FLG. The fair value of this subordinated debt as at 30 June 2013 is £204 million (30 June 2012: £178 million, 31 December 2012: £215 million).

On 21 April 2011, FLG issued a £500 million LT2 subordinated debt instrument with a coupon of 8.25% and a maturity of 2022, which is irrevocably guaranteed on a subordinated basis by FLL. This debt is carried at amortised cost being £500 million principal less capitalised issue costs of £3 million (30 June 2012: £4 million, 31 December 2012: £4 million). The fair value of this subordinated debt as at 30 June 2013 is £525 million (30 June 2012: £440 million, 31 December 2012: £554 million).

On 8 November 2012, FLG issued a US$575 million UT2 reset perpetual subordinated debt instrument with a coupon of 7.875%, which is irrevocably guaranteed on a subordinated basis by FLL. This debt is carried at amortised cost being the US$575 million principal translated at the effective exchange rate less capitalised issue costs of £8 million. 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 fair value of this subordinated debt at 30 June 2013 is £396 million (30 June 2012: £nil, 31 December 2012: £378 million). A derivative instrument was entered into on 8 November 2012 to manage the risks associated with fluctuations in exchange rates on the issue of this debt.

Deferred consideration notes

On 15 September 2010, the Company issued fixed rate, unsecured loan notes with an aggregate principal amount of £500 million to AXA UK plc in connection with the acquisition of the AXA UK Life Business. The terms of the deferred consideration notes allowed for the Company to redeem in part or in full at any time. On 20 November 2012, the Company made a full repayment of £362.7 million representing the outstanding principal at that time.

Financial reinsurance

FLL has three financial reinsurance contracts with Munich Reinsurance Company UK Limited ("Munich Re") to finance new German unit–linked pensions business written in the years ended 31 December 2010, 2011 and 2012 respectively. The total amount owed to Munich Re under these financial reinsurance arrangements as at 30 June 2013 was £26 million (30 June 2012: £31 million, 31 December 2012: £37 million).

During 2013, FPIL entered into a financial reinsurance agreement with Munich Re to finance new Rest of World Premier regular premium savings business written between 1 January 2013 and 31 December 2013 in certain territories. The total amount owed to Munich Re under this financial reinsurance agreement as at 30 June 2013 was £8 million (30 June 2012: £nil, 31 December 2012: £nil).

In 2012, FPIL entered into a financial reinsurance agreement with Munich Re to finance new Rest of World Premier regular premium savings business written between 1 January 2012 and 31 December 2012. The total amount owed to Munich Re under this financial reinsurance agreement as at 30 June 2013 was £9 million (30 June 2012: £16 million, 31 December 2012: £20 million).

In 2011, FPIL entered into a financial reinsurance agreement with Munich Re to finance new Hong Kong Premier regular premium savings business written between 1 January 2011 and 31 December 2011. The total amount owed to Munich Re under this financial reinsurance agreement as at 30 June 2013 was £nil (30 June 2012: £6 million, 31 December 2012: £nil)

Other

Amounts owed to credit institutions (overdrafts) include £8 million (30 June 2012: £4 million, 31 December 2012: £4 million) relating to credit balances held within OEICs that have been consolidated as the Group's holding is 50% or more. Such overdrafts are fully repayable out of the assets of the OEICs.

The Group benefits from a £250 million (2012: £500 million) multi–currency revolving credit facility with Barclays Bank plc, Royal Bank of Canada, HSBC Bank plc and The Royal Bank of Scotland plc, with Barclays Bank plc as agent. The £250 million facility was entered into by FLL on 10 May 2013 and replaces the previous £500 million facility entered into by FLG. If a third party, who does not presently have control of FLG or FLL, acquires such control, FLL must notify the agent immediately. In this circumstance, the lenders are not obliged to fund utilisation and may notify the agent to cancel their commitments under the facility. This would have the effect of rendering all of their loans repayable within ten business days from the date of notice. As at the date of this report, the facility remains undrawn.

10. Contingent liabilities

In the normal course of its business, the Group is subject to matters of litigation or dispute or regulatory uncertainty. While there can be no assurances at this time, the Directors believe, based on the information currently available to them, that it is not probable that the ultimate outcome of any of these matters will have a material adverse effect on the financial condition of the Group.

11. Related parties

In the ordinary course of business, the Group and its subsidiary undertakings carry out transactions with related parties, as defined by IAS 24: *Related party disclosures*. Material transactions for the year are set out below.

Details of the Group's pension schemes are provided in note 6.

(a) Services provided by related parties

	30 June 2013		30 June 2012		31 December 2012	
	Income earned in period	**Receivable at period end**	Income earned in period	Receivable at period end	Income earned in year	Receivable at year end
	£m	**£m**	£m	£m	£m	£m
Joint venture	**2**	**–**	2	–	5	–

(b) Other related parties

Operating agreement - ROL

Until 28 March 2013, the Company had outsourced most of its operating functions to Resolution Operations Limited ("ROL") under the terms of an Operating Agreement. The Operating Agreement was novated to the Group as a result of a business sale agreement entered into by the Company on 10 December 2012, which completed on 28 March 2013. Costs of £10 million (30 June 2012: £nil) relating to the transfer of the operating agreement from ROL to the Group were recognised at 31 December 2012 of which £3 million remained unspent at 30 June 2013.

Under the terms of the agreement:

- The Company paid ROL an annual operating fee; under which the total amount charged in the period ended 30 June 2013 amounted to £5 million (30 June 2012: £9 million, 31 December 2012: £18 million).
- The Company could, subject to certain conditions, advance funds to ROL for development work on new projects outside the UK Life Project. No funding remains in place at 30 June 2013 (30 June 2012: £1 million, 31 December 2012: £1 million).
- Subject to certain exceptions, members of the Resolution Group were restricted from selling or pledging as security for a loan any of their shares in the Company held as at 13 January 2012, with a total number of locked–up shares of 8,247,184. As a result of the termination of the Operating Agreement these shares ceased to be subject to the lock–up agreement although Resolution Capital Limited has confirmed that these shares will not be sold until at least December 2013.

Resolution Holdco No.1 LP

The Company has a 99.99% interest in, and is the general partner in, Resolution Holdco No.1 LP, a Guernsey limited partnership. The limited partner in Resolution Holdco No.1 LP is RCAP UK LP. The Company entered into the limited partnership in 2008 for the purpose of making acquisitions and rewarding the Resolution Group for value created in the limited partnership from those acquisitions. This arrangement remains in place.

Resolution (Brands) Limited

The Company is a party to a trademark licence agreement with Resolution (Brands) Limited, a company wholly owned by Clive Cowdery, under which the Group has paid a fee of £113,668 for the use of the "Resolution" brand in respect of the year commencing 4 December 2012. The existing Trademark Licence with Resolution (Brands) Limited remains in force substantially on its current terms, although from 27 March 2013 an annual termination right came into force together with an agreement that there would be no future fees payable for use of the brand.

12. Post balance sheet events

Further incremental rate reductions were announced in the Chancellor's Autumn Statement on 5 December 2012 and Budget on 20 March 2013 and included in the 2013 Finance Bill. These will reduce the rate to 21% from 1 April 2014 and to 20% from 1 April 2015. The Bill only received Royal Assent in July 2013, after the balance sheet date, and therefore the changes in tax rate have not been taken into account in these financial statements. The accounting implications of these amendments are detailed in note 5.

Statement of Directors’ responsibilities in respect of the Market Consistent Embedded Value (MCEV) basis

The Directors of Resolution Limited have chosen to prepare supplementary information in accordance with European Insurance CFO Forum (“MCEV Principles”), issued in October 2009. When compliance with the MCEV Principles is stated, those principles require the Directors to prepare supplementary information in accordance with the methodology contained in the MCEV Principles and to disclose and explain any non-compliance with the guidance included in the MCEV Principles.

In preparing the MCEV supplementary information, the Directors have:

- done so in accordance with the MCEV Principles and fully complied with the guidance included therein;
- determined assumptions on a realistic basis, having regard to past, current and expected future experience and to any relevant external data, and then applied them consistently;
- made estimates that are reasonable and consistent; and
- described the basis on which business that is non-covered has been included in the supplementary information, including any material departures from the accounting framework applicable to the Group condensed consolidated IFRS financial statements.

By order of the Board

Tim Tookey
Director
12 August 2013

INDEPENDENT REVIEW REPORT TO RESOLUTION LIMITED

Introduction

We have been engaged by the Company to review the set of MCEV financial statements in the interim results statement for the six months ended 30 June 2013 which comprises the consolidated income statement – MCEV basis, the earnings per share – MCEV basis, the consolidated statement of comprehensive income – MCEV basis, the consolidated statement of changes in equity – MCEV basis, the consolidated statement of financial position – MCEV basis, the Group MCEV analysis of earnings and the related notes 1 to 11. We have read the other information contained in the interim results statement and considered whether it contains any apparent misstatements or material inconsistencies with the information in the MCEV financial statements.

We have reported separately on the condensed financial statements of Resolution Limited prepared on an IFRS basis for the six months ended 30 June 2013. The information contained in the MCEV financial statements should be read in conjunction with the condensed set of financial statements prepared on an IFRS basis.

This report is made solely to the Company in accordance with guidance contained in International Standard on Review Engagements 2410 (UK and Ireland) "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The MCEV financial statements in the interim results statement are the responsibility of, and have been approved by, the Directors. The Directors are responsible for preparing the MCEV financial statements in accordance with the Market Consistent Embedded Value Principles issued in October 2009 by the CFO forum ("the MCEV Principles") and the basis of preparation set out in note 1.

Our responsibility

Our responsibility, as set out in our engagement letter with you dated 7 August 2013, is to express to the Company a conclusion on the MCEV financial statements based on our review.

Scope of review

We conducted our review in accordance with ISRE 2410. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the set of MCEV financial statements in the interim results statement for the six months ended 30 June 2013 is not prepared, in all material respects, in accordance with the MCEV Principles and the basis of preparation set out in note 1.

Ernst & Young LLP
London
12 August 2013

MCEV FINANCIAL INFORMATION

Consolidated income statement – MCEV basis

For the half year ended 30 June 2013

	Notes	**2013 Half year £m**	2012 Half year £m	2012 Full year £m
Life and pensions				
Value of new business	6	**97**	97	194
Expected existing business contribution		**126**	165	325
Operating experience variances		**(31)**	(15)	(56)
Operating assumption changes		**34**	14	(9)
Other operating variances		**30**	19	27
Development costs	9	**(26)**	(22)	(50)
Life and pensions covered business operating profit before tax	3	**230**	258	431
Other income and charges		**(6)**	(8)	(21)
Life and pensions operating profit before tax		**224**	250	410
Corporate income and charges		**(10)**	(15)	(28)
Operating profit before tax		**214**	235	382
Economic variances	3	**228**	242	154
Amortisation and impairment of non-covered business intangible assets		**–**	(1)	(15)
Non-recurring items and non-operating variances	3	**(33)**	(91)	(127)
Profit from continuing operations before tax		**409**	385	394
Tax on operating profit		**(54)**	(63)	(120)
Tax on other activities		**(34)**	(26)	(6)
Profit for the period[(i)]		**321**	296	268

(i) Profit for the period is attributable to equity holders of the parent.

Notes 1 to 11 form an integral part of these financial statements.

The consolidated income statement for the half year ended 30 June 2012 and for the year ended 31 December 2012 include the results of AmLife Insurance Berhad and AmFamily Takaful Berhad (collectively "AmLife"). The consolidated income statement for the half year ended 30 June 2013 includes the results of AmLife up until the date of disposal on 4 January 2013.

Earnings per share – MCEV basis

For the half year ended 30 June 2013

	Note	**2013 Half year pence**	2012 Half year pence	2012 Full year pence
Earnings per share				
Operating earnings per share on MCEV basis after tax, attributable to equity holders of the parent				
– Basic and diluted	4	**11.28**	12.48	18.83
Earnings per share on MCEV basis after tax, attributable to equity holders of the parent				
– Basic and diluted	4	**22.64**	21.48	19.26

MCEV operating profit arises from continuing operations, incorporates an expected investment return and excludes:

- amortisation and impairment of non-covered business intangible assets;
- the effect of economic variances (including the impact of economic assumption changes); and
- significant non-recurring items and non-operating items.

Given the long-term nature of the Group's operations, operating profit is considered to be a better measure of the performance of the Group and this measure of profit is used internally to monitor the Group's MCEV results.

Consolidated statement of comprehensive income – MCEV basis

For the half year ended 30 June 2013

	2013 Half year £m	2012 Half year £m	2012 Full year £m
Profit for the period	**321**	296	268
Remeasurement (losses)/gains on defined benefit pension schemes, net of tax	**(20)**	8	(35)
Foreign exchange adjustments	**35**	(18)	(16)
Other comprehensive income/(loss) for the period, net of tax	**15**	(10)	(51)
Total comprehensive income for the period[(i)]	**336**	286	217

(i) Total comprehensive income for the period is attributable to equity holders of the parent.

Consolidated statement of changes in equity – MCEV basis

For the half year ended 30 June 2013

	2013 Half year £m	2012 Half year £m	2012 Full year £m
Opening ordinary shareholders' equity	**5,831**	5,796	5,796
Disposal of AmLife as at 4 January 2013	**7**	–	–
Total comprehensive income for the period	**336**	286	217
Issue of share capital (net of capitalised expenses and movement in RSL shares held by subsidiaries)	**–**	42	97
Dividends on equity shares	**(200)**	(185)	(283)
Share-based payments	**6**	–	4
Increase in MCEV reserves for the period	**149**	143	35
Closing ordinary shareholders' equity	**5,980**	5,939	5,831

Consolidated statement of financial position – MCEV basis

As at 30 June 2013

	30 Jun 2013 £m	30 Jun 2012 £m	31 Dec 2012 £m
Assets			
Pension scheme surplus	**–**	37	33
VIF covered business excluding assets of operations classified as held for sale	**4,410**	4,078	4,230
Intangible assets	**8**	26	9
Property and equipment	**51**	56	53
Investment properties	**2,621**	2,897	2,735
Investment in associates and joint venture	**–**	30	–
Financial assets	**111,427**	102,945	105,990
Deferred acquisition costs	**86**	91	88
Reinsurance assets	**3,130**	3,332	3,153
Current tax assets	**–**	6	8
Insurance and other receivables	**1,454**	1,500	1,133
Cash and cash equivalents	**9,804**	8,672	9,449
Assets of operations classified as held for sale	**–**	–	43
Total assets	**132,991**	123,670	126,924
Liabilities			
Insurance contracts	**37,241**	37,121	37,294
Unallocated surplus	**655**	710	656
Financial liabilities			
– investment contracts	**82,698**	74,060	77,276
– loans and borrowings	**1,618**	1,330	1,641
– amounts due to reinsurers	**1,720**	1,795	1,767
Net asset value attributable to unit holders	**808**	900	754
Provisions	**234**	214	223
Pension scheme deficit	**31**	–	–
Deferred tax liabilities	**619**	273	362
Current tax liabilities	**38**	5	21
Insurance payables, other payables and deferred income	**1,347**	1,320	1,096
Total liabilities	**127,009**	117,728	121,090
Equity attributable to:			
– Equity holders of the parent	**5,980**	5,939	5,831
– Non-controlling interests	**2**	3	3
Total equity	**5,982**	5,942	5,834
Total equity and liabilities	**132,991**	123,670	126,924

Group MCEV analysis of earnings

For the half year ended 30 June 2013

			2013 Half year	2012 Half year	2012 Full year
	Covered business £m	**Non-covered business £m**	**Total business £m**	Total business £m	Total business £m
Opening Group MCEV	**4,923**	**908**	**5,831**	5,796	5,796
Opening adjustments:					
- disposal of AmLife	**(43)**	**50**	**7**	–	–
Adjusted opening Group MCEV	**4,880**	**958**	**5,838**	5,796	5,796
Operating MCEV earnings	**181**	**(21)**	**160**	172	262
Non-operating MCEV earnings	**92**	**69**	**161**	124	6
Total MCEV earnings	**273**	**48**	**321**	296	268
Other movements in IFRS net equity	**–**	**(20)**	**(20)**	15	(28)
Closing adjustments:					
– capital and dividend flows	**(233)**	**39**	**(194)**	(150)	(189)
– foreign exchange variances	**35**	**–**	**35**	(18)	(16)
Closing Group MCEV	**4,955**	**1,025**	**5,980**	5,939	5,831

Notes to the MCEV results

1. Basis of preparation

Introduction

Resolution Limited is presenting the results and financial position for its life and pensions business on the MCEV basis and for its other businesses on the IFRS basis. The MCEV basis is in compliance with the European Insurance CFO Forum MCEV Principles[i] ("the MCEV Principles"), issued in June 2008, and re-issued in amended form in October 2009. In accordance with guidance issued by the CFO forum in September 2011, no allowance has been made for the impacts of the developing Solvency II regulatory regime.

This MCEV supplementary information presents results for the Group.

The MCEV results were approved by the Board of Directors on 12 August 2013.

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Segmental analysis and definitions

The results for 30 June 2013 and 31 December 2012 have been shown for UK and Heritage divisions separately, as well as a combined total for the two divisions. There is no split available for the 30 June 2012 comparative results, and as such these are presented as a combined "UK & Heritage" result.

Following the simplification of governance arrangements, the results and comparatives for the non-covered business of Resolution Limited and Friends Life group have been combined.

MCEV methodology

Overview

The MCEV basis of reporting is designed to recognise profit as it is earned over the term of a life insurance policy. The total profit recognised over the lifetime of the policy is the same as that recognised under the IFRS basis of reporting, but the timing of recognition is different.

Covered business

Covered business comprises all life and pensions business written by Friends Life group in the UK and through overseas life insurance subsidiaries and associates (collectively referred to as "life and pensions covered business").

The external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022 are formally allocated to covered business on the basis that all obligations to make payments in respect of this debt are guaranteed by FLL. The external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022 are included within the MCEV at market value, based on listed ask prices.

Non-covered business

The Group's non-covered business includes the IFA distribution businesses, the management services businesses, Friends Life Investments ("FLI") and the net pension deficit of FPPS on an IAS 19 basis. Corporate net assets held at Friends Life and Resolution holding company level, certain holding company costs, the deferred consideration notes issued by Resolution Limited (until the date of their repayment on 20 November 2012) are all non-covered business.

Whilst the management services businesses and FLI are classified as non-covered, the expenses and cash flows of those businesses are linked to the life and pensions businesses via service and investment management agreements. The cash flows of the companies are calculated on the "look-through" principle and are allowed for when setting appropriate expense and tax assumptions.

Segmental reporting under MCEV

The covered business within the Friends Life group has been split into the following segments in line with IFRS reporting:

- UK;
- Heritage;
- FPI; and
- Lombard.

On 4 January 2013 the Company disposed of its entire holding of 30% of the ordinary share capital of AmLife to AmBank Group of Malaysia for RM 245 million (£50 million) resulting in a profit on disposal of £7 million on an MCEV basis.

Corporate functions are not strictly an operating segment, but are reported to management, and are provided to reconcile the Group's reportable segments to the total result. Corporate includes the external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021, the external LT2 subordinated debt 2022, internal LT2 subordinated debt 2020, corporate costs and the cost of holding any required capital in excess of the operating segment capital policy.

New business

New business within the life and pensions covered business includes:

- premiums from the sale of new policies;
- payments on recurring single premium policies, except existing stakeholder-style pensions business where, if a regular pattern in the receipt of premiums for individuals has been established, the regular payment is treated as a renewal of an existing policy and not new business;
- non-contractual increments on existing policies;
- new entrants to existing schemes in the corporate benefits business; and
- immediate pension annuity contracts arising from internal vestings.

New business in 2012 also included Department for Work and Pensions rebate premiums, which are no longer received.

New business includes certain new corporate benefit schemes that have been transferred within Friends Life to new auto-enrolment platforms. These are only included in new business where the transfer was instigated by the client and where significant new business activities have been undertaken by Friends Life.

The MCEV new business definition is consistent with the quarterly new business disclosures.

Calculation of embedded value

The reported Group MCEV provides an estimate of the total consolidated MCEV of the Group and comprises the MCEV in respect of the life and pensions covered business, together with the IFRS net assets in respect of the non-covered business, excluding intangible assets relating to future new business.

The MCEV provides an estimate of the value of shareholders' interest in the covered business, excluding any value that may be generated from future new business. The MCEV comprises the sum of the shareholders' net worth of the life and pensions covered business and the value of in-force covered business. The shareholders' net worth of the life and pensions covered business includes the listed debt of the external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022 at market value, based on listed ask prices.

The MCEV is calculated on a post-tax basis. Where gross results are presented, these have been calculated by grossing up the post-tax results for covered business at the appropriate rate of corporation tax for each segment. For non-covered business the gross results are presented gross of any IFRS tax attributed.

(a) Shareholders' net worth

The shareholders' net worth of the life and pensions covered business consists of free surplus and required capital.

Free surplus is the market value of any assets allocated, but not required, to support the in-force covered business at the valuation date. Required capital is the market value of assets, attributed to the covered business over and above that required to back liabilities for covered business, whose distribution to shareholders is restricted. The Group's required capital is set at the greater of local regulatory capital requirements and those requirements arising from internal capital management policies, which include economic risk capital objectives. The economic risk capital is determined from internal models, based on the Group's risk appetite. The level of required capital is shown in note 9.

(b) Value of in-force covered business

The value of in-force covered business consists of:

- present value of future profits; less
- time value of financial options and guarantees;
- frictional costs of required capital; and
- cost of residual non-hedgeable risks.

Present value of future profits ("PVFP")

The value of existing business is the present value of the future distributable profits available to shareholders from the in-force covered business. Future profits are projected using best estimate non-economic assumptions and market consistent economic assumptions.

The non-economic assumptions include: the behaviour of customers (e.g. persistency), mortality, morbidity, the level of expenses required to maintain the book of business, tax and the regulatory environment. The assumptions are a reflection of best estimates of the likely behaviours, outcomes, or circumstances in the future. The estimates are made, typically, on an annual basis following experience investigations based on the data available at the time both from the book of business and externally sourced information. The aim is to set assumptions at a level that reflects recent or current experience.

The PVFP includes the capitalised value of profits and losses arising in subsidiary companies providing investment management, administration and other services to the extent that they relate to covered business. This is referred to as the "look-through" into investment management and service company expenses. In addition expenses arising in holding companies that relate directly to acquiring or maintaining covered business have been allowed for.

In valuing shareholders' cash flows, allowance is made in the cash flow projections for taxes in the relevant jurisdiction affecting the covered business. Tax assumptions are based on best estimate assumptions, applying local corporate tax legislation and practice together with known future changes and taking credit for any deferred tax assets.

The economic assumptions are market consistent whereby, in principle, each cash flow is valued in line with the price of similar cash flows that are traded in the capital markets. For example, an equity cash flow is valued using an equity risk discount rate, and a bond cash flow is valued using a bond risk discount rate. If a higher return is assumed for equities, the equity cash flow is discounted at this higher rate.

In practice, for liabilities where the payouts are either independent or move linearly with market movements, a method known as the "certainty equivalent approach" has been applied whereby all assumed assets earn the reference rate and all cash flows are discounted using the reference rate. This gives the same result as applying the method in the previous paragraph.

Time value of financial options and guarantees ("TVOG")

The PVFP is based on a single deterministic projection of future economic assumptions. However, a single projection does not fully reflect the potential for extreme events and the resulting impact of options and guarantees on the shareholder cash flows. While the PVFP allows for the intrinsic value of an option or guarantee under a single set of economic assumptions, it does not reflect the potential range of future economic scenarios on the shareholder cash flows. Stochastic modelling techniques are used to assess the impact of potential future economic scenarios on an option or guarantee and to determine the average value of shareholder cash flows under a number of market consistent scenarios.

The TVOG is calculated as the difference between the average value of shareholder cash flows under a number of market consistent scenarios, and the intrinsic value under a single projection within the PVFP.

The material financial options and guarantees are those in the with-profits funds of the subsidiary life companies of Friends Life group, in the form of the benefits guaranteed to policyholders and the guaranteed annuity rates associated with certain policies. The risk to shareholders is that the assets of the with-profits funds are insufficient to meet these guarantees. While shareholders are entitled to only a small share of profits in the with-profits funds (e.g. via one-ninth of the cost of bonus), they can potentially be exposed to the full cost of fund assets being insufficient to meet policyholder guarantees. The TVOG has been assessed using a stochastic model derived from the current Realistic Balance Sheet ("RBS") model. This model has been calibrated to market conditions at the valuation date. Allowance has been made under the different scenarios for management actions, such as altered investment strategy, consistent with the RBS model. The TVOG would be markedly higher without the hedging activities and management actions currently undertaken. No allowance has been made for the impact of dynamic policyholder behaviour under the different scenarios, however the impact is not considered to be material for Friends Life.

Only modest amounts of new with-profits business are written and the guarantee levels offered are lower, hence there is no material impact in respect of the TVOG on the value of new business.

Frictional costs of required capital

The value of in-force covered business includes a deduction for the additional costs to an investor of holding the assets backing required capital through investment in a life company, rather than investing in the asset directly. These additional frictional costs comprise taxation and investment expenses on the assets backing the required capital.

The frictional costs of required capital are calculated as the difference between the market value of assets backing required capital and the present value of future releases of that capital allowing for future investment return (net of frictional costs) on that capital. The calculation allows for the run-off of the required capital over time using projections of the run-off of the underlying risks and regulatory requirements.

Details of the level of required capital are set out in note 9.

Cost of residual non-hedgeable risks ("CNHR")

The main area of non-hedgeable risk relates to non-financial risks, such as insurance and operational risks, where no deep, liquid market exists to fully mitigate the risk. Allowance for non-financial risk is made directly within:

- the PVFP via an appropriate choice of best estimate assumptions and with the impact of variability of the risk on the level, and hence cost, of required capital; and
- the TVOG for the impact of variations of non-financial risks on the possibility of shareholders needing to meet the guarantees within the with-profits funds of the subsidiary life companies of Friends Life group.

The CNHR covers those non-hedgeable risks that are not already allowed for fully in the PVFP or in the TVOG. The most significant of these risks are those for which the impact of fluctuations in experience is asymmetric; where adverse experience has a higher impact on shareholder value than favourable experience and the best estimate assumptions do not reflect this asymmetry. The areas identified as having the potential for material asymmetry are operational risk, persistency risk and reinsurance counterparty default risk.

The CNHR has been calculated by considering the financial cost to shareholders of the impact of asymmetric risks and with regard to the results of risk-based capital modelling. The risk-based capital is calculated using internal models, consistent with those used in the Group's Individual Capital Assessment, with:

- a 99.5% confidence level over one year;
- allowance for diversification between non-hedgeable risks;
- no allowance for diversification between non-hedgeable and hedgeable risks; and
- no allowance for diversification between covered and non-covered business.

The CNHR impacts both the value of existing business and new business.

Participating business

Future regular bonuses on participating business are projected in a manner consistent with current bonus rates and expected future market consistent returns on assets deemed to back the policies.

Future terminal bonuses are assumed to be set at a level to exhaust all the assets deemed to back the policies over the future lifetime of the in-force with-profit policies.

The PVFP includes the shareholders' share of future profits from the with-profits funds, based on the assumed bonus rates.

There may be some extreme future economic scenarios in which total assets in each of the with-profits funds are not sufficient to pay all policyholder claims and the resulting shortfall would be met by shareholders. Stochastic modelling techniques are used to assess the impact of future economic scenarios on the with-profits funds' ability to pay all policyholder claims and to determine the average additional cost to shareholders arising from future projected shortfalls. This cost to shareholders has been included in the TVOG.

Consolidation adjustments

The effect of transactions and reinsurance arrangements between life insurance subsidiary companies has been included in the results split by segment in a consistent manner. No elimination is required on consolidation.

Goodwill and intangible assets

Goodwill and intangible assets relating to the non-covered business are included on an IFRS basis. Intangible assets recognised under IFRS relating to the value of future new business, such as distribution relationships and brand value, have been excluded from the Group MCEV.

Exchange rates

The results and cash flows of overseas subsidiaries and joint ventures have been translated at the average exchange rates for the period and the assets and liabilities have been translated at the period end rates. Translation differences are shown as foreign exchange adjustments in the consolidated statement of comprehensive income. Exchange rate driven movements in MCEV earnings are reported within economic variances.

Details of the exchange rates used are shown in note 9.

2. Analysis of MCEV earnings

The following tables show the movement in the MCEV of the Group. The analysis is shown separately for free surplus, required capital and the value of the in-force covered business. All figures are shown net of tax.

For the half year ended 30 June 2013

	Covered business					
Net of tax	**Free surplus £m**	**Required capital £m**	**VIF £m**	**Total £m**	**Non-covered business £m**	**Total MCEV £m**
Opening Group MCEV	**641**	**40**	**4,242**	**4,923**	**908**	**5,831**
Opening adjustments:						
– acquired/divested businesses	**(3)**	**(25)**	**(15)**	**(43)**	**50**	**7**
Adjusted opening Group MCEV	**638**	**15**	**4,227**	**4,880**	**958**	**5,838**
Value of new business	**(110)**	**35**	**151**	**76**	**–**	**76**
Expected existing business contribution:						
– expected existing business contribution: reference rate	**7**	**(4)**	**16**	**19**	**–**	**19**
– expected existing business contribution: in excess of reference rate	**2**	**(24)**	**101**	**79**	**–**	**79**
Transfers from VIF and required capital to free surplus	**297**	**(5)**	**(292)**	**–**	**–**	**–**
Operating experience variances and development costs	**(37)**	**–**	**(5)**	**(42)**	**–**	**(42)**
Operating assumption changes	**(11)**	**7**	**30**	**26**	**–**	**26**
Other operating items	**(2)**	**–**	**25**	**23**	**(21)**	**2**
Operating Group MCEV earnings	**146**	**9**	**26**	**181**	**(21)**	**160**
Economic variances	**62**	**17**	**103**	**182**	**–**	**182**
Other non-operating items	**(114)**	**–**	**24**	**(90)**	**69**	**(21)**
Total Group MCEV earnings	**94**	**26**	**153**	**273**	**48**	**321**
Other movements in IFRS net equity	**–**	**–**	**–**	**–**	**(20)**	**(20)**
Closing adjustments:						
– capital and dividend flows	**(249)**	**17**	**(1)**	**(233)**	**39**	**(194)**
– foreign exchange variances	**–**	**4**	**31**	**35**	**–**	**35**
Closing Group MCEV	**483**	**62**	**4,410**	**4,955**	**1,025**	**5,980**

For the half year ended 30 June 2012

	Covered business					
Net of tax	Free surplus £m	Required capital £m	VIF £m	Total £m	Non-covered business £m	Total MCEV £m
Opening Group MCEV	821	747	3,844	5,412	384	5,796
Value of new business	(157)	44	190	77	–	77
Expected existing business contribution:						
– expected existing business contribution: reference rate	13	(5)	30	38	–	38
– expected existing business contribution: in excess of reference rate	7	(22)	105	90	–	90
Transfers from VIF and required capital to free surplus	293	(12)	(281)	–	–	–
Operating experience variances and development costs	(43)	3	10	(30)	–	(30)
Operating assumption changes	–	–	11	11	–	11
Other operating variances	17	–	(2)	15	(29)	(14)
Operating Group MCEV earnings	130	8	63	201	(29)	172
Economic variances	6	40	148	194	–	194
Other non-operating items	(82)	(32)	37	(77)	7	(70)
Total Group MCEV earnings	54	16	248	318	(22)	296
Other movements in IFRS net equity	–	–	–	–	15	15
Closing adjustments:						
– capital and dividend flows	(308)	17	–	(291)	141	(150)
– foreign exchange variances	(1)	(3)	(14)	(18)	–	(18)
Closing Group MCEV	566	777	4,078	5,421	518	5,939

3. Segmental analysis of MCEV earnings

The table below shows a further breakdown of the MCEV earnings. All earnings are shown on a gross of tax basis with attributed tax shown separately.

For the half year ended 30 June 2013

	Covered business							
Gross of tax	**UK £m**	**Heritage £m**	**UK & Heritage £m**	**FPI £m**	**Lombard £m**	**Corporate £m**	**Non-covered business £m**	**Total £m**
Value of new business	**89**	**(8)**	**81**	**4**	**12**	**–**	**–**	**97**
Expected existing business contribution	**30**	**106**	**136**	**9**	**18**	**(37)**	**–**	**126**
Operating experience variances	**–**	**(14)**	**(14)**	**1**	**(18)**	**–**	**–**	**(31)**
Operating assumption changes	**–**	**34**	**34**	**–**	**–**	**–**	**–**	**34**
Other operating variances	**–**	**30**	**30**	**–**	**–**	**–**	**–**	**30**
Development costs	**(19)**	**(2)**	**(21)**	**(4)**	**(1)**	**–**	**–**	**(26)**
Life and pensions covered business operating profit/(loss) before tax	**100**	**146**	**246**	**10**	**11**	**(37)**	**–**	**230**
Other income and charges	**–**	**–**	**–**	**–**	**–**	**–**	**(6)**	**(6)**
Life and pensions operating profit/(loss) before tax	**100**	**146**	**246**	**10**	**11**	**(37)**	**(6)**	**224**
Corporate income and charges	**–**	**–**	**–**	**–**	**–**	**–**	**(10)**	**(10)**
Operating profit/(loss) before tax	**100**	**146**	**246**	**10**	**11**	**(37)**	**(16)**	**214**
Economic variances	**63**	**105**	**168**	**36**	**2**	**22**	**–**	**228**
Other non-operating items	**4**	**(126)**	**(122)**	**–**	**–**	**–**	**89**	**(33)**
Profit/(loss) before tax	**167**	**125**	**292**	**46**	**13**	**(15)**	**73**	**409**
Attributed tax on operating result	**(22)**	**(34)**	**(56)**	**1**	**(3)**	**9**	**(5)**	**(54)**
Attributed tax on other activities	**(18)**	**12**	**(6)**	**(2)**	**–**	**(6)**	**(20)**	**(34)**
Profit/(loss) after tax	**127**	**103**	**230**	**45**	**10**	**(12)**	**48**	**321**

For the half year ended 30 June 2012

Gross of tax	Covered business UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Non-covered business £m	Total £m
Value of new business	67	18	12	–	–	97
Expected existing business contribution	170	12	18	(35)	–	165
Operating experience variances	3	(8)	(10)	–	–	(15)
Operating assumption changes	9	–	5	–	–	14
Other operating variances	19	–	–	–	–	19
Development costs	(18)	(4)	–	–	–	(22)
Life and pensions covered business operating profit/(loss) before tax	250	18	25	(35)	–	258
Other income and charges	–	–	–	–	(8)	(8)
Life and pensions operating profit/(loss) before tax	250	18	25	(35)	(8)	250
Corporate income and charges	–	–	–	–	(15)	(15)
Operating profit/(loss) before tax	250	18	25	(35)	(23)	235
Economic variances	200	(2)	12	32	–	242
Other non-operating items	(102)	2	(1)	–	9	(92)
Profit/(loss) before tax	348	18	36	(3)	(14)	385
Attributed tax on operating profits	(61)	1	(6)	9	(6)	(63)
Attributed tax on other activities	(18)	2	(2)	(6)	(2)	(26)
Profit/(loss) after tax	269	21	28	–	(22)	296

UK covered business

The life and pensions covered business operating profit before tax for the UK segment was £100 million in the period to 30 June 2013 (30 June 2012: £250 million for UK & Heritage).

VNB

Further details of the calculation and analysis of the VNB are discussed in note 6.

Expected existing business contribution

The expected existing business contribution is the sum of two components:

- the expected earnings over the period assuming the opening assets earn the beginning of period reference rate; and
- the additional expected earnings (in excess of the beginning of period reference rate) consistent with management's expectation for the business.

The reference rate is based on the one-year swap return plus, for UK immediate annuity business only, an illiquidity premium equivalent to 75bps (30 June 2012: 90bps) at the beginning of the period.

The additional earnings are the excess over the reference rate and reflect management's long-term expectation of asset returns, based on assumed asset mix.

The total expected contribution of £30 million (30 June 2012: £170 million for UK & Heritage) comprises £27 million (30 June 2012: £145 million for UK & Heritage) from applying expected rates of return to the value of in-force at the start of the period and £3 million (30 June 2012: £25 million for UK & Heritage) of expected return on shareholders' net assets.

The expected contribution from the value of in-force of £27 million reflects the expected rates of return applied to the opening value of in-force of £925 million at 1 January 2013 (£2,885 million at 1 January 2012, for UK & Heritage).

The UK expected contribution on shareholders' net assets of £3 million reflects the return based on the reference rate.

Operating experience variances

Operating experience variances relate to variances between actual experience and that anticipated in the projection assumptions.

Operating experience variances totalled £nil million (30 June 2012: £3 million for UK & Heritage) and comprise the following elements:

- At 31 December 2012 a provision of £33 million was held in the UK & Heritage divisions to cover adverse persistency experience as a result of the RDR; £30 million of this has been released in the UK division offsetting the adverse experience during the first half of the year;
- £(5) million charge from heavier than assumed mortality experience, in particular in the individual protection business;
- £2 million benefit from better than assumed morbidity experience, in particular on the group income protection business;
- £2 million benefit from actual expenses being lower than long-term expense assumptions; and
- £1 million benefit from other sources.

Operating assumption changes

There have been no changes to operating assumptions in the period to 30 June 2013 (30 June 2012: £9 million for UK & Heritage).

Other operating variances

Other operating variances of £nil million comprise a number of small, offsetting items (30 June 2012: £19 million for UK & Heritage).

Development costs

Development costs of £(19) million (30 June 2012: £(18) million for UK & Heritage) relate to costs that are expected to enhance current propositions and generate future profits which are not captured in the MCEV. These costs relate principally to:

- the development and delivery of the retirement income annuity business strategy;
- the development of the corporate investment platform;
- the development of business systems for the introduction of auto-enrolment; and
- the development of the protection proposition development.

Heritage covered business

The life and pensions covered business operating profit before tax for the Heritage segment was £146 million in the period to 30 June 2013 (30 June 2012: £250 million for UK & Heritage).

VNB

Further details of the calculation and analysis of the VNB are discussed in note 6.

Expected existing business contribution

The expected existing business contribution is the sum of two components:

- the expected earnings over the period assuming the opening assets earn the beginning of period reference rate; and
- the additional expected earnings (in excess of the beginning of period reference rate) consistent with management's expectation for the business.

The reference rate is based on the one-year swap return plus, for Heritage immediate annuity business only, an illiquidity premium equivalent to 75bps (30 June 2012: 90bps) at the beginning of the period.

The additional earnings are the excess over the reference rate and reflect management's long-term expectation of asset returns, based on assumed asset mix.

The total expected contribution of £106 million (30 June 2012: £170 million for UK & Heritage) comprises £98 million (30 June 2012: £145 million for UK & Heritage) from applying expected rates of return to the value of in-force at the start of the period and £8 million (30 June 2012: £25 million for UK & Heritage) of expected return on shareholders' net assets.

The expected contribution from the value of in-force of £98 million reflects the expected rates of return applied to the opening value of in-force of £2,267 million at 1 January 2013 (£2,885 million at 1 January 2012, for UK & Heritage).

The Heritage expected contribution on shareholders' net assets of £8 million primarily reflects the return based on the reference rate.

Operating experience variances

Operating experience variances relate to variances between actual experience and that anticipated in the projection assumptions.

Operating experience variances totalled a charge of £(14) million (30 June 2012: benefit of £3 million for UK & Heritage) and comprise the following elements:

- £3 million benefit from better than assumed persistency experience. This is after a release of the RDR provision of £3 million;
- £10 million benefit from better than assumed mortality experience, in particular on the life protection business and long term care business;
- £(9) million charge in respect of statutory provisions established in respect of legacy pensions business;
- £(6) million charge from actual expenses being higher than long-term expense assumptions, the majority of which relates to costs incurred during the period that will not form part of the on-going cost base;
- £(4) million charge from tax variances; and
- £(8) million from a number of other small items.

Operating assumption changes

An operating assumptions benefit of £34 million has been recognised during the period (30 June 2012: £9 million for UK & Heritage) reflecting savings on future investment expenses following the recapture of certain asset portfolios by FLI.

Other operating variances

Other operating variances of £30 million (30 June 2012: £19 million for UK & Heritage) comprise:

- £15 million benefit from an increase in deferred tax assets on pensions business following a review of methodology;
- £9 million benefit from modelling changes; and
- £6 million net benefit from other sources.

Development costs

Development costs of £(2) million (30 June 2012: £(18) million for UK & Heritage) relate to costs that are expected to enhance current propositions and generate future profits which are not captured in the MCEV. These costs relate to a number of small development projects.

FPI covered business

The life and pensions covered business operating profit before tax for the FPI segment was £10 million (30 June 2012: £18 million).

VNB

Further details of the calculation and analysis of the VNB are discussed in note 6.

Expected existing business contribution

The expected contribution of £9 million (30 June 2012: £12 million) reflects the expected return on the opening value of in-force of £515 million at 1 January 2013 (30 June 2012: £502 million at 1 January 2012).

Operating experience variances

Operating experience variances of £1 million (30 June 2012: £(8) million) comprise:

- £3 million benefit from mortality experience being better than anticipated; and
- £(2) million charge from other operational elements and other minor variances.

Operating assumption changes

The operating assumption changes in the period to 30 June 2013 are in respect of required capital and local statutory reserving and as such do not affect the MCEV operating profit (30 June 2012: £nil).

Other operating variances

There are no material other operating variances in the period to 30 June 2013 (30 June 2012: £nil).

Development costs

Development costs of £(4) million (30 June 2012: £(4) million) relate to the development of the International platform.

Lombard covered business

The life and pensions covered business operating profit before tax for the Lombard segment was £11 million (30 June 2012: £25 million).

VNB

Further details of the calculation and analysis of the VNB are discussed in note 6.

Expected existing business contribution

The expected contribution of £18 million (30 June 2012: £18 million) reflects the expected return on the opening value of in force of £535 million at 1 January 2013 (30 June 2012: £457 million at 1 January 2012). The impact of the higher opening value of in force has been offset by the lower expected rates of return.

Operating experience variances

Operating experience variances of £(18) million (30 June 2012: £(10) million) comprise:

- £(11) million charge resulting from persistency experience being worse than anticipated in a number of territories, including Belgium. At 31 December 2012, an £8 million provision was established for short-term adverse persistency experience in the Belgian market. £5 million of this provision has been used to meet the adverse experience on this business during the first half of 2013;
- £(1) million charge from share-based payments representing the fair value charge of the Lombard long-term incentive plans;
- £1 million benefit from better than assumed mortality experience; and
- £(7) million charge from a number of smaller items including the renegotiation of terms with intermediaries and custodian banks.

Operating assumption changes

There are no operating assumption changes in the period to 30 June 2013 (30 June 2012: £5 million).

Other operating variances

There are no material other operating variances in the period to 30 June 2013 (30 June 2012: £nil).

Development costs

Development costs of £(1) million (30 June 2012: £nil) relate to the development of new products during the first half of the year.

Corporate covered business

Corporate includes the external STICS, the external UT2 subordinated debt with associated currency swap, the external LT2 subordinated debt 2021, the external LT2 subordinated debt 2022 and the cost of holding any required capital in excess of the operating segment capital policy.

The expected existing business contribution of £(37) million (30 June 2012: £(35) million) represents the expected interest costs arising on the debt held within the life and pensions covered business with the increase driven by the issuance of the new UT2 subordinated debt and associated currency swap; partially offset by market movements.

Non-covered business

The non-covered business reported an operating loss of £(16) million (30 June 2012: £(23) million) which comprises £(11) million of corporate costs and the £(5) million operating result of Sesame Bankhall, including the regulatory fine.

Economic variances

Economic variances combine the impact of changes to economic assumptions with the investment return variances to expected investment returns over the period. The total economic variances were £228 million (30 June 2012: £242 million) and these comprise:

- £189 million due to the narrowing of credit spreads;
- £164 million as a result of better than expected investment returns on equities;
- £44 million of foreign exchange movements, primarily due to the weakening of Sterling against the Euro;
- £22 million from a decrease in the market value of debt;
- £(110) million from an increase in interest rates, primarily due to the fall in shareholder fixed interest assets;
- £(51) million from an increase in inflation; and
- £(30) million of other minor economic variances.

Other non-operating items

Total other non-operating items of £(33) million (30 June 2012: £(92) million) comprise:

- £(24) million from the initial costs associated with the outsourcing agreement with Diligenta; partially offset by the utilisation of the provision established against these costs (discussed in note 9);
- £(7) million of costs related to the capital optimisation programme;
- £(6) million of non-recurring project costs within the covered business in respect of Solvency II costs and financial reporting improvements net of £4 million provision release;
- £(5) million of non-recurring project costs, net of provision releases, within the covered business in respect of separation and integration of UK and Heritage businesses; and
- £9 million benefit from tax related non-operating items including a £38 million benefit on the UK value of in-force business of changing the ultimate corporation tax rate effective from April 2015 from 21% to 20%, following the Chancellor's Budget in March 2013.

Heritage non-operating expenses include £(89) million in respect of a charge for deficit funding relating to the Group's defined benefit pension scheme, the income for which is reported within the Corporate segment results.

4. Earnings per share

Basic and operating earnings per share

Half year ended 30 June 2013	**Earnings £m**	**Per share pence**
Profit after tax attributable to ordinary equity holders of the parent	**321**	**22.64**
Economic variances	**(228)**	**(16.08)**
Non-recurring items and non-operating variances	**33**	**2.33**
Tax credit on items excluded from operating profit	**34**	**2.40**
Operating profit after tax attributable to ordinary equity holders of the parent	**160**	**11.28**

Half year ended 30 June 2012	Earnings £m	Per share pence
Profit after tax attributable to ordinary equity holders of the parent	296	21.48
Economic variances	(242)	(17.56)
Amortisation of non-covered business intangible assets	1	0.07
Non-recurring items and non-operating variances	91	6.60
Tax credit on items excluded from operating profit	26	1.89
Operating profit after tax attributable to ordinary equity holders of the parent	172	12.48

Year ended 31 December 2012	Earnings £m	Per share pence
Profit after tax attributable to ordinary equity holders of the parent	268	19.26
Economic variances	(154)	(11.07)
Amortisation of non-covered business intangible assets	15	1.08
Non-recurring items and non-operating variances	127	9.13
Tax credit on items excluded from operating profit	6	0.43
Operating profit after tax attributable to ordinary equity holders of the parent	262	18.83

Diluted earnings per share from continuing operations

There were no dilutive factors for the half years ended 30 June 2013 and 30 June 2012, or for the full year ended 31 December 2012.

Weighted average number of ordinary shares

For the half year ended 30 June 2013	**Actual**	**Weighted**
Issued ordinary shares at beginning of period	**1,418,109,028**	**1,418,109,028**
Number of ordinary shares at end of period	**1,418,109,028**	**1,418,109,028**

For the half year ended 30 June 2012	Actual	Weighted
Issued ordinary shares at beginning of period	1,376,188,989	1,376,188,989
Own shares held by the Group at the beginning of the period	(2,661,384)	(2,661,384)
Effect of:		
– scrip dividend (final 2011)	15,484,945	3,441,099
– reduction in own shares held by the Group	2,661,384	1,345,477
Number of ordinary shares at end of period	1,391,673,934	1,378,314,181

For the year ended 31 December 2012	Actual	Weighted
Issued ordinary shares at beginning of period	1,376,188,989	1,376,188,989
Own shares held by the Group at beginning of period	(2,661,384)	(2,661,384)
Effect of:		
– scrip dividend (final 2011)	15,484,945	9,477,125
– scrip dividend (interim 2012)	26,435,094	6,283,752
– reduction in own shares held by the Group	2,661,384	1,999,674
Number of ordinary shares at end of period	1,418,109,028	1,391,288,156

5. Reconciliation of equity attributable to ordinary shareholders

Ordinary shareholders' equity on the MCEV basis reconciles to equity attributable to ordinary shareholders on the IFRS basis as follows:

	30 Jun 2013 £m	30 Jun 2012 £m	31 Dec 2012 £m
Equity attributable to ordinary shareholders on an IFRS basis	**5,233**	5,453	5,377
Less items only included on an IFRS basis (net of tax):			
– IFRS reserving and other IFRS adjustments	**(38)**	527	(32)
– Deferred front end fees	**54**	42	47
– Deferred acquisition costs	**(749)**	(620)	(708)
– Acquired present value of in-force	**(3,061)**	(3,305)	(3,159)
– Other intangible assets	**(210)**	(271)	(246)
Add items only included on a MCEV basis (net of tax):			
– Adjustment for long-term debt to market value	**341**	35	310
Net worth on a MCEV basis	**1,570**	1,861	1,589
Value of in-force covered business	**4,410**	4,078	4,242
Equity attributable to ordinary shareholders on a MCEV basis	**5,980**	5,939	5,831

6. New business

The following tables set out the analysis of new business in terms of volumes and profitability.

New business volumes have been shown using two measures:

- Present Value of New Business Premiums ("PVNBP") is equal to the total single premium sales received in the period plus the discounted value of regular premiums expected to be received over the lifetime of new contracts, and is expressed at point of sale;
- Annual Premium Equivalent ("APE") is calculated as the new regular premium per annum plus 10% of single premiums.

The MCEV new business definition is consistent with the quarterly new business disclosures.

The premium volumes and projection assumptions used to calculate the present value of regular premiums within PVNBP are the same as those used to calculate the value of new business.

The value of new business is calculated using economic assumptions at the beginning of the period for all products except immediate annuities. For annuity business, as the contribution is sensitive to the interest rate at outset, the appropriate rate for each month's new business is used.

The value of new business is calculated using operating assumptions at the end of period for all products. The operating assumptions are consistent with those used to determine the embedded value.

The value of new business is shown after the effects of the frictional costs of holding required capital and share-based payments, and after the effect of the costs of residual non-hedgeable risks on the same basis as for the in-force covered business.

New business value

	New business premiums							
Half year ended 30 June 2013	**Single £m**	**Regular £m**	**APE £m**	**Average annual premium multiplier (i)**	**PVNBP £m**	**Post-tax VNB £m**	**Pre-tax VNB £m**	**New business margin %**
UK Corporate Benefits	**251**	**228**	**253**	**4.2**	**1,213**	**10**	**13**	**1.1**
UK Protection	**–**	**39**	**39**	**7.4**	**290**	**25**	**32**	**11.0**
UK Retirement Income(ii)	**324**	**–**	**32**	**–**	**324**	**34**	**44**	**13.6**
UK total	**575**	**267**	**324**	**4.7**	**1,827**	**69**	**89**	**4.9**
Heritage	**105**	**16**	**27**	**4.8**	**181**	**(6)**	**(8)**	**(4.4)**
FPI	**318**	**47**	**79**	**5.1**	**557**	**4**	**4**	**0.7**
Lombard	**872**	**–**	**87**	**–**	**872**	**9**	**12**	**1.4**
Total	**1,870**	**330**	**517**	**4.7**	**3,437**	**76**	**97**	**2.8**

(i) Defined as (PVNBP less total amount of single premiums)/(total annualised amount of regular premiums) this is shown as zero for UK Retirement Income and Lombard as these businesses have only single premium business therefore PVNBP is the same as the premiums received in the period.

(ii) The value of new business for annuities shown in the table above has been valued assuming an illiquidity premium recalculated monthly, the average illiquidity premium over the six months to 30 June 2013 is 80 bps (see note 9).

Half year ended 30 June 2012	New business premiums Single £m	Regular £m	APE £m	Average annual premium multiplier [(i)]	PVNBP £m	Post-tax VNB £m	Pre-tax VNB £m	New business margin %
UK Corporate Benefits	579	233	291	4.2	1,552	8	10	0.6
UK Protection	–	44	44	6.4	282	21	28	9.9
UK Retirement Income[(ii)]	187	–	19	–	187	19	25	13.4
UK total	766	277	354	4.5	2,021	48	63	3.1
Heritage	340	26	60	4.7	461	3	4	0.9
FPI	286	75	104	5.5	697	17	18	2.6
Lombard	948	–	95	–	948	9	12	1.3
Total	2,340	378	613	4.7	4,127	77	97	2.4

(i) Defined as (PVNBP less total amount of single premiums)/(total annualised amount of regular premiums) this is shown as zero for UK Retirement Income and Lombard as these businesses have only single premium business therefore PVNBP is the same as the premiums received in the period.

(ii) The value of new business for annuities shown in the table above has been valued assuming an average illiquidity premium of 90bps over the six months to 30 June 2012.

UK

The VNB from the UK segment was £89 million (30 June 2012: £63 million), comprising:

- UK Corporate Benefits VNB of £13 million (30 June 2012: £10 million), reflecting the benefits of migration to target platforms and the associated lower costs;
- UK Protection VNB of £32 million (30 June 2012: £28 million), with the benefit of migration to the lower cost strategic platform partially offset by lower volumes of business written; and
- UK Retirement Income VNB of £44 million (30 June 2012: £25 million), driven by a significant increase in the volume of business written.

Heritage

Heritage VNB was £(8) million (30 June 2012: £4 million), reflecting that Heritage writes products no longer actively marketed and VNB in 2012 also included Department for Work and Pensions rebate premiums, which are no longer received.

FPI

FPI VNB was £4 million (30 June 2012: £18 million) for the period; mainly reflecting a reduction in new business volumes and the strengthening of the basis assumptions following the strategic review in the fourth quarter of 2012.

Lombard

Lombard VNB was £12 million (30 June 2012: £12 million) for the period; a reduction in volumes has been offset by the expense benefits from the implementation of strategic development plans.

__New business performance metrics__

New business written requires an initial capital investment to meet the set-up costs and capital requirements.

The IRR provides a measure of the return to shareholders on this initial capital investment. It is equivalent to the discount rate at which the present value of the after-tax cash flows expected to be earned over the lifetime of the business written is equal to the initial capital invested, including setting aside the required capital, to support the writing of the business. The Lombard IRR (and therefore the blended Group IRR) takes account of the Luxembourg regulatory regime in which DAC is an allowable asset.

The cash payback on new business is the time elapsed until the total of expected (undiscounted) cash flows is sufficient to recoup the initial capital invested, including the release of the required capital, to support the writing of new business.

New business key performance metrics

	Half year ended 30 June 2013			Half year ended 30 June 2012		
	Pre-tax value of new business £m	**Internal rate of return on new business %**	**Cash payback on new business Years**	Pre-tax value of new business £m	Internal rate of return on new business %	Cash payback on new business Years
UK Corporate Benefits	**13**	**7.6**	**12**	10	6.8	12
UK Protection	**32**	**15.0**	**7**	28	9.8	9
UK Retirement Income	**44**	**>25.0**	**1**	25	>25.0	1
UK total	**89**	**16.7**	**7**	63	11.2	9
Heritage[(i)]	**(8)**	**(0.9)**	**n/a**	4	4.2	15
FPI[(ii)]	**4**	**5.0**	**12**	18	10.5	8
Lombard	**12**	**13.8**	**7**	12	14.1	8
Total	**97**	**11.2**	**9**	97	10.0	10

(i) The investment in writing new business in the Heritage segment, which specifically focuses on products no longer actively marketed, is not expected to be recouped and results in a negative IRR.

(ii) For FPI, the strengthening of basis assumptions following the strategic review has driven the increase in the cash payback period to 12 years (30 June 2012: 8 years) and the reduction in IRR.

7. Segmental analysis of Group MCEV

	30 June 2013									31 December 2012
	Free Surplus £m	**Required capital £m**	**Total net worth £m**	**PVFP £m**	**TVOG £m**	**Frictional costs £m**	**CNHR £m**	**Total VIF £m**	**Total £m**	Total £m
UK	**1**	**320**	**321**	**1,102**	**–**	**(36)**	**(54)**	**1,012**	**1,333**	1,227
Heritage	**420**	**1,194**	**1,614**	**2,627**	**(122)**	**(77)**	**(117)**	**2,311**	**3,925**	4,080
UK & Heritage	**421**	**1,514**	**1,935**	**3,729**	**(122)**	**(113)**	**(171)**	**3,323**	**5,258**	5,307
FPI	**64**	**26**	**90**	**540**	**–**	**(2)**	**(22)**	**516**	**606**	612
Lombard	**(2)**	**82**	**80**	**603**	**–**	**(4)**	**(28)**	**571**	**651**	615
Corporate(i)										
– IFA and distribution	**28**	**–**	**28**	**–**	**–**	**–**	**–**	**–**	**28**	39
– Pension asset of FPPS	**13**	**–**	**13**	**–**	**–**	**–**	**–**	**–**	**13**	38
– Other(ii)	**984**	**(8)**	**976**	**–**	**–**	**–**	**–**	**–**	**976**	816
Gross MCEV(iii)	**1,508**	**1,614**	**3,122**	**4,872**	**(122)**	**(119)**	**(221)**	**4,410**	**7,532**	7,427
FLG corporate–external STICS	**–**	**(450)**	**(450)**	**–**	**–**	**–**	**–**	**–**	**(450)**	(443)
FLG corporate–external debt (iv)	**–**	**(1,102)**	**(1,102)**	**–**	**–**	**–**	**–**	**–**	**(1,102)**	(1,153)
Net MCEV	**1,508**	**62**	**1,570**	**4,872**	**(122)**	**(119)**	**(221)**	**4,410**	**5,980**	5,831

(i) Corporate excludes external STICS, the external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022.

(ii) Other includes £180 million (31 December 2012: £133 million) in respect of the Resolution holding companies.

(iii) For the purposes of this table “Gross” refers to the MCEV gross of the clean market value of the external STICS, the external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022. The accrued interest and tax adjustment on market valuation is included in the gross MCEV of Corporate.

(iv) The Corporate external debt comprises: the external LT2 subordinated debt 2021; the external LT2 subordinated debt 2022; and the external UT2 subordinated debt with associated currency swap.

7.1 Required capital

Each life company within the Group has an individual capital management policy which, whilst aligned to Group policies, will take account of local regulatory requirements. All the life companies in the Group meet their individual capital management policies.

Required capital within MCEV is calculated and allocated to business units based on the Group's capital management policy of holding 150% of the Group CRR (excluding WPICC) even where this allocation is in excess of local capital management policies. In practice the extra required capital held to meet the Group's capital management policy can be covered by any of the companies within the Group.

The external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022 are included within the MCEV at market value, as detailed in note 9.

7.2 PVFP

The PVFP at 30 June 2013 includes a £5 million (31 December 2012: £9 million) deduction in respect of a short term persistency provision established in Lombard relating to specific markets. A provision against worsening short-term persistency as a result of the Retail Distribution Review (31 December 2012: £25 million, net of tax) has been fully released against adverse persistency experience in UK & Heritage during the first half of the year.

7.3 TVOG

The TVOG at 30 June 2013 of £122 million (31 December 2012: £126 million), is split between £86 million (31 December 2012: £90 million) market risk and £36 million (31 December 2012: £36 million) non-market risk. The non-market risks include lapses, annuitant longevity, and operational risk within the with-profits fund. The allowance for non-market risks is made by consideration of the impact of extreme scenarios from the Group's economic capital model.

7.4 Frictional costs of holding required capital

The projected required capital for life company subsidiaries is derived from the Group's capital management policy which is to hold the greater of 150% of Pillar 1 CRR excluding WPICC and 125% Pillar 2 CRR including any Individual Capital Guidance.

Additionally, the Group capital management policy in respect of FLG is to hold 150% of Group CRR excluding WPICC (31 December 2012: 150%). The cost of holding any additional capital is shown in the FLG covered business segment.

7.5 CNHR

The cost of residual non-hedgeable risk of £221 million (31 December 2012: £222 million) is presented as an equivalent annual cost of capital charge of 1.3% (31 December 2012: 1.5%) on projected risk-based Group required capital for all non-hedgeable risk. In line with management's view of the business, allowance has been made for diversification benefits within the non-hedgeable risks of the covered business.

8. Segmental analysis of Group MCEV earnings

The tables below show a further breakdown of the Group MCEV earnings comprising the MCEV earnings for the life and pensions covered business and the IFRS earnings for the non-covered businesses.

All figures are shown net of attributed tax.

	Covered business							
Half year ended 30 June 2013	**UK £m**	**Heritage £m**	**UK & Heritage £m**	**FPI £m**	**Lombard £m**	**Corporate £m**	**Non-covered business £m**	**Total £m**
Opening Group MCEV	**1,227**	**4,080**	**5,307**	**612**	**615**	**(1,611)**	**908**	**5,831**
Opening adjustments:								
– disposal of AmLife	**–**	**–**	**–**	**(43)**	**–**	**–**	**50**	**7**
Adjusted opening Group MCEV	**1,227**	**4,080**	**5,307**	**569**	**615**	**(1,611)**	**958**	**5,838**
Operating MCEV earnings	**78**	**112**	**190**	**11**	**8**	**(28)**	**(21)**	**160**
Non-operating MCEV earnings	**49**	**(9)**	**40**	**34**	**2**	**16**	**69**	**161**
Total Group MCEV earnings	**127**	**103**	**230**	**45**	**10**	**(12)**	**48**	**321**
Other movements in IFRS net equity	**–**	**–**	**–**	**–**	**–**	**–**	**(20)**	**(20)**
Closing adjustments:								
– capital and dividend flows	**(21)**	**(258)**	**(279)**	**(8)**	**(9)**	**63**	**39**	**(194)**
– foreign exchange variances	**–**	**–**	**–**	**–**	**35**	**–**	**–**	**35**
Closing Group MCEV	**1,333**	**3,925**	**5,258**	**606**	**651**	**(1,560)**	**1,025**	**5,980**

Half year ended 30 June 2012	Covered business UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Non-covered business £m	Total £m
Opening Group MCEV	5,341	571	541	(1,041)	384	5,796
Operating MCEV earnings	190	19	19	(27)	(29)	172
Non-operating MCEV earnings	79	2	9	27	7	124
Total Group MCEV earnings	269	21	28	–	(22)	296
Other movements in IFRS net equity	–	–	–	–	15	15
Closing adjustments:						
– capital and dividend flows	(373)	31	–	51	141	(150)
– foreign exchange variances	–	(1)	(17)	–	–	(18)
Closing Group MCEV	5,237	622	552	(990)	518	5,939

Year ended 31 December 2012	Covered business UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Non-covered business £m	Total £m
Opening Group MCEV	5,341	571	541	(1,041)	384	5,796
Operating MCEV earnings	381	(79)	80	(57)	(63)	262
Non-operating MCEV earnings	243	(16)	10	(228)	(3)	6
Total Group MCEV earnings	624	(95)	90	(285)	(66)	268
Other movements in IFRS net equity	–	–	–	–	(28)	(28)
Closing adjustments:						
-capital and dividend flows	(658)	136	–	(285)	618	(189)
-foreign exchange variances	–	–	(16)	–	–	(16)
Closing Group MCEV	5,307	612	615	(1,611)	908	5,831

9. MCEV assumptions

9.1 Economic assumptions – deterministic calculations

Economic assumptions are derived actively, based on market yields on risk-free fixed interest assets at the end of each reporting period.

Reference rates – risk free

The risk free reference rate is determined with reference to the swap yield curve appropriate to the currency of the cash flows. For some business types, where the impact on the VIF is small, a long-term risk free reference rate has been used.

For annuity business the swap yield curve is extrapolated where necessary, assuming the last observable forward rate is constant thereafter, to provide rates appropriate to the duration of the liabilities.

No adjustment has been made to the reference rate for current sovereign debt market conditions because the exposure of the Group to such debt is minimal.

	Reference rate – risk free		
	30 Jun 2013 %	30 Jun 2012 %	31 Dec 2012 %
UK & Heritage			
Long-term rate	**2.70**	2.20	1.90
Swap yield curve			
– Term 1 year	**0.67**	1.06	0.67
– Term 5 years	**1.57**	1.27	1.03
– Term 10 years	**2.66**	2.17	1.93
– Term 15 years	**3.17**	2.68	2.58
– Term 20 years	**3.41**	2.97	2.94
FPI long-term rate	**2.70**	2.20	1.90
Lombard long-term rate	**2.43**	2.24	2.13

Reference rate – Illiquidity premium adjustment

The updated MCEV Principles recognise that the inclusion of an illiquidity premium within the reference rate is appropriate where the liabilities are not liquid.

In this regard, the methodology adopted for the valuation of immediate annuities in the UK & Heritage uses a reference rate that has been increased above the swap yield curve to allow for an illiquidity premium. This reflects the fact that, for these products, the backing asset portfolio can be held to maturity and earns risk-free returns in excess of swaps. Any illiquidity premia in respect of assets backing other product types are recognised within the MCEV as and when they are earned.

The illiquidity premium has been evaluated by considering a number of different sources of information and methodologies. Two of the main approaches being commonly used to determine the illiquidity premium within the life insurance industry are:

- a "negative basis trade", which attributes a component of the difference between the spread on a corporate bond and a credit default swap (for the same issuing entity, maturity, seniority and currency) as being the illiquidity premium; and
- structural models – such as that used by the Bank of England in their analysis of corporate bond spreads – that use option pricing techniques to decompose the spread into its constituent parts including default risk, credit risk premium and a residual illiquidity premium.

Both of these methods have been used to help inform the extent of the illiquidity premium within the asset portfolios backing immediate annuity business.

No illiquidity premium has been applied for any other covered business.

The reference rate has been adjusted for immediate and some deferred annuities as set out in the table below.

	Embedded value			New business		
	30 Jun 2013	30 Jun 2012	31 Dec 2012	**30 Jun 2013**	30 Jun 2012	31 Dec 2012
UK & Heritage immediate annuities	**75 bps**	90 bps	75 bps	**80 bps**(i)	90 bps	85 bps(ii)

(i) Investment strategy for annuity new business targets assets with higher illiquidity premiums than the back book portfolio. The average illiquidity premium over the first 6 months was 80bps.

(ii) Average illiquidity premium over the year, illiquidity premium changed from 90bps to 80bps from 1 July 2012.

Expected asset returns in excess of reference rates

Margins are added to the reference rates to obtain investment return assumptions for equity, property and corporate bonds. These risk premia reflect management's expectations of asset returns in excess of the reference rate from investing in different asset classes. As a market consistent approach has been followed, these investment return assumptions affect the expected existing business contribution and the economic variances within the analysis of MCEV earnings, but do not affect the opening or closing embedded values. In addition, they will affect the additional disclosures of the payback periods.

For equities and property, the excess is calculated as the difference between the long-term rate of return and the one-year risk free reference rate. The long-term rate of return is derived using a 10 year swap rate plus a risk premium of 3% for equities (3% at 30 June 2012 and 31 December 2012) and 2% for property (2% at 30 June 2012 and 31 December 2012).

For cash and government bonds no excess over the one-year risk free reference rate has been assumed for UK, Heritage or FPI. Lombard assumes the long-term rate is achieved. For corporate bonds, the return is based on the excess of actual corporate bond spreads on the reporting date, less an allowance for defaults, over the one-year risk free reference rate for UK, Heritage and FPI. For Lombard the corporate bond return is derived using the long-term rate plus a risk premium of 1% (1% at 30 June 2012 and 31 December 2012).

For annuity business the excess return reflects the excess of the bond portfolio over the reference rate including the illiquidity premium adjustment.

Expense inflation

Maintenance expenses for UK, Heritage and FPI business are assumed to increase in the future at a rate of 1% (1% at 30 June 2012 and 31 December 2012) per annum in excess of the assumed long-term rate of inflation. Long-term inflation assumptions are set relative to gilt curves at appropriate durations.

Maintenance expenses for Lombard are assumed to increase in the future at a rate of 0.75% (0.75% at 30 June 2012 and 31 December 2012) per annum in excess of the assumed long-term rate of inflation. This is derived from an inflation swap curve based on a Euro-zone price index taking into account the run-off profile of the business.

	Expense inflation		
	30 Jun 2013 %	30 Jun 2012 %	31 Dec 2012 %
UK	**4.00**	3.40	3.70
Heritage	**4.00**	3.40	3.70
FPI	**4.00**	3.40	3.70
Lombard	**2.80**	2.70	3.00

Exchange rates

The results and cash flows of all businesses, except Lombard are calculated in Sterling. The results and cash flows for Lombard are calculated in Euros and converted to Sterling at the following rates:

	Exchange rates		
	30 Jun 2013	30 Jun 2012	31 Dec 2012
Closing exchange rate	**0.857**	0.809	0.811
Average exchange rate	**0.848**	0.823	0.813

Other economic assumptions

Bonus rates on participating business have been set at levels consistent with the economic assumptions.

The MCEV allows for distribution of profit between the policyholders and shareholders within the following with-profits funds at the current rate of one-ninth of the cost of bonus:

- Friends Life FP With-Profits Fund ("FLFP WPF")
- Friends Life FLAS With-Profits Fund ("FLFLAS WPF")
- Friends Life FLC Old With-Profits Fund ("FLFLC OWPF")
- Friends Life FLC New With-Profits Fund ("FLFLC NWPF")
- Friends Life FLWL With-Profits Fund ("FLFLWL WPF")

In addition it is assumed that the shareholder interest in the non-profit business of the FLFP WPF continues at the current rate of 60% of future profits.

Following the Part VII transfer of business from FLC to FLL, the requirement to retain the FLC reattributed inherited estate ("RIE") to support FLFLC OWPF and FLFLC NWPF along with other previously existing with-profit fund support arrangements have been incorporated into one FLL Scheme effective from 28 December 2012.

The FLL Scheme rules require that a test be undertaken every five years to determine the level of shareholder capital support required for FLFLC OWPF and FLFLC NWPF. The test also determines whether it is possible to distribute any of the inherited estate retained in the FLFLC OWPF in the form of Special Bonuses (and associated transfer to the shareholders' fund). The latest five yearly test was undertaken as at 31 December 2010.

The remaining RIE in the FLL NPF is predominantly in the form of the VIF of non-profit business written within the fund. To the extent that this VIF emerges into cash during the period 28 December 2012 to the next five year test date at 31 December 2015, the cash may be available to be transferred to the FLL shareholders' fund subject to passing the relevant financial strength tests. The MCEV allows for best estimate projections of the amounts to be transferred in future.

9.2 Economic assumptions – stochastic calculations

Model

The time value of financial options and guarantees and the OLAB return of premium guarantee are determined using a Barrie & Hibbert economic scenario generator and are calculated using 2,000 simulations. The with-profits model is consistent with the model used for the Realistic Balance Sheet and is calibrated to market conditions at the valuation date using the gilt risk-free curve and implied volatilities in the market. The OLAB return of premium guarantee model is calibrated to market conditions at the valuation date using a Euro swap curve and implied volatilities in the market. Correlations between the asset classes are derived from historic data.

Swaption implied volatilities - with-profits time value of financial options and guarantees

	30 Jun 2013 Swap term				30 Jun 2012 Swap term				31 Dec 2012 Swap term			
Option term	**10 yrs %**	**15 yrs %**	**20 yrs %**	**25 yrs %**	10 yrs %	15 yrs %	20 yrs %	25 yrs %	10 yrs %	15 yrs %	20 yrs %	25 yrs %
UK Sterling												
10 years	**18**	**17**	**16**	**15**	18	18	18	18	18	17	16	15
15 years	**18**	**17**	**16**	**16**	15	16	16	16	18	17	16	16
20 years	**16**	**16**	**15**	**15**	14	14	14	14	16	16	15	15
25 years	**16**	**16**	**16**	**15**	13	13	13	13	16	16	16	15

Swaption implied volatilities - OLAB return of premium guarantee

	30 Jun 2013 Swap term				31 Dec 2012 Swap term			
Option term	**10 yrs %**	**15 yrs %**	**20 yrs %**	**30 yrs %**	10 yrs %	15 yrs %	20 yrs %	30 yrs %
Euro								
10 years	**24**	**23**	**22**	**21**	24	24	23	20
15 years	**24**	**23**	**21**	**20**	27	26	24	20
20 years	**24**	**22**	**20**	**18**	26	24	21	17
25 years	**23**	**20**	**18**	**16**	23	20	18	15

Comparatives for the six months ended 30 June 2012 are not available.

Equity and property implied volatilities - with-profits time value of financial options and guarantees

Equity volatility is calibrated to market implied volatility and is a reasonable fit to the implied volatility of the FTSE 100 put options held by the with-profits funds. Property holdings are modelled assuming an initial volatility of 15% (30 June 2012: 15%, 31 December 2012: 15%) and a running yield of 4.3% (30 June 2012: 4.3%, 31 December 2012: 4.3%). Sample implied volatilities are shown in the table below.

	30 Jun 2013		30 Jun 2012		31 Dec 2012	
Option term	**Equity %**	**Property %**	Equity %	Property %	Equity %	Property %
5 years	**24**	**15**	27	15	24	15
10 years	**26**	**15**	27	15	26	15
15 years	**27**	**15**	27	15	27	15

Equity implied volatilities - OLAB return of premium guarantee

Equity volatility is calibrated to put options on the EUROSTOXX50 index as an objective measure of market implied volatility. Sample implied "at-the-money" volatilities are shown in the table below.

	30 Jun 2013	31 Dec 2012
Option term	**Equity %**	Equity %
5 years	**22**	25
10 years	**25**	25
15 years	**26**	25

Comparatives for the six months ended 30 June 2012 are not available.

9.3 Other assumptions

Required capital

Required capital under MCEV amounted to £62 million (£777 million at 30 June 2012, £40 million at 31 December 2012). The changes in required capital have mainly resulted from the issuance of the new UT2 subordinated debt in the second half of 2012 partially offset by the decrease in the market value of external debt over the first six months of 2013.

The projected required capital is derived from the Group's capital management policy which is to hold, within life company subsidiaries, the greater of 150% Pillar 1 CRR excluding WPICC and 125% of ICA plus ICG. In addition the Group's capital management policy is to hold 150% of Group CRR excluding WPICC, and any cost of holding this additional capital is shown within the Corporate covered business segment. These policies are unchanged from 30 June 2012 and 31 December 2012.

Taxation

The opening and closing embedded values in respect of covered business are determined on an after tax basis. The tax assumptions used are based upon the best estimate of the actual tax expected to arise. The attributable tax charge and profit before tax are derived by grossing up the profit after tax at the appropriate tax rates for each of the UK, Isle of Man and Luxembourg. Deferred tax is provided on the mark-to-market revaluation of the external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022 allocated to the life and pensions covered business within Corporate. For UK and OLAB business the appropriate tax rate has been calculated as the average rate of corporation tax applicable over the period, and hence the rate applicable for 2013 reflects the reduction in corporation tax that took effect from April 2013.

For non-covered business, attributed tax is consistent with the IFRS financial statements.

	Tax rates		
	30 Jun 2013 %	30 Jun 2012 %	31 Dec 2012 %
UK	**23.5**	24.5	24.5
Heritage	**23.5**	24.5	24.5
FPI			
– OLAB (UK)	**23.5**	24.5	24.5
– FPIL (Isle of Man)	**0.0**	0.0	0.0
Lombard	**22.5**	23.8	22.5

The PVFP for UK, Heritage and OLAB business includes allowance for the annual reductions in corporation tax announced in the Emergency Budget in June 2010 and the further reductions of 1% announced in each of the Budgets in April 2011, April 2012 and April 2013. The MCEV allows for anticipated future annual reductions in corporation tax from 24% to 20% over the period to 2015 (31 December 2012: 24% to 21% over the period to 2014) and for an ultimate rate of 20% from April 2015 (31 December 2012: 21% from April 2014).

Legislation in respect of the new life tax regime was included in Finance Act 2012, which received Royal Assent on 17 July 2012. The new life tax regime took effect from 1 January 2013 and a best estimate of its effect is therefore included in MCEV, being a forward looking measure. There remains an element of risk and uncertainty in estimating its effects given that the legislation is newly introduced therefore the outcomes may be subject to change as a result of either legislative update or by development in interpretation.

VAT in the UK of 20.0% (30 June 2012: 20.0%, 31 December 2012: 20.0%) less expected recoveries has been included on relevant investment management expenses and, where applicable, on outsourced administration contracts.

Demographic assumptions

Other assumptions (for example mortality, morbidity and persistency) are a reflection of the best estimate of the likely behaviours, outcomes or circumstances in the future. Typically the estimates are made on an annual basis following experience investigations based on the data available at the time both from the book of business and externally sourced information. The aim is to set assumptions at a level that reflects recent experience, unless there are reliable indicators that suggest their adoption would result in a significant variance compared to these assumptions in the future. In some instances, there may be little or no direct experience to use in setting assumptions and the future outcome is therefore uncertain.

The RDR came into effect from 1 January 2013 and a £33 million provision (gross of tax) was held at 31 December 2012, to cover negative variances expected on initial commission business written pre-RDR in 2012 where long-term assumptions were expected to be temporarily inadequate. Following the release of £33 million against adverse experience in the first half of 2013, this provision has been reduced to £nil million (gross of tax) as at 30 June 2013.

Future improvements in annuitant mortality have been assumed to be in accordance with the projections published by the Continuous Mortality Investigation ("CMI") in 2011, with a long-term rate of 1.25% per annum (30 June 2012: 1.25%, 31 December 2012: 1.25%).

Expense assumptions

The management expenses (including those relating to holding companies) attributable to the covered businesses have been analysed between expenses relating to the acquisition of new business, maintenance of in-force business (including investment management expenses) and development expenses.

Future maintenance expense assumptions reflect the expected ongoing expense levels required to manage the in-force business.

Productivity gains have generally only been included to the extent they have been achieved by the end of the reporting period.

In June 2009 Friends Life Services Limited ("FLSL") entered into a 15 year agreement with Capita Life & Pensions Regulated Services Limited ("Capita") to outsource the administration of mature traditional life and pensions policies. The maintenance expense assumptions for the relevant business allow for the agreed service fees with Capita. In addition allowance is made for the initial significant development expenditure and anticipated longer term savings as a result of a reduction in costs, which result in an overall expense overrun in FLSL.

Strategic development plans for the Lombard business have resulted in projected short-term expense overruns which have been allowed for by reducing the PVFP by £1 million for a projected overrun to 2013 (31 December 2012: £2 million for a projected overrun to 2013).

In November 2011 Friends Life announced a 15 year agreement with Diligenta to outsource IT and Programmes and in-house Customer Service functions (along with HR, Finance and Business Risk services that support these functions). This agreement resulted in significant longer term cost reductions and an overall increase to MCEV. Allowance was made in 2011 for the initial significant development expenditure, with the establishment of a specific provision. In the first half of 2013, initial development costs of £(40) million have been incurred in relation to the Diligenta arrangement which have been partially offset by a £16 million utilisation of the remaining £92 million provision. The net cost of £(24) million is shown in the consolidated income statement within other non-operating items.

Other one-off costs shown within non-recurring items can be categorised as:

- Solvency II and Finance Transformation project costs;
- Separation and Integration costs;
- Capital restructuring costs; or
- Corporate acquisitions/disposal costs.

Any other one-off costs that do not fall into these categories are treated as operating exceptional costs within operating experience variances.

The MCEV makes provision for certain development costs to the extent that these are known with sufficient certainty and in line with current plans.

Development costs of £26 million (30 June 2012: £22 million, 31 December 2012: £50 million) have been excluded from the calculation of unit costs and have been recognised in operating profits. Development costs relate to investment in activities expected to create value in the future, but where that expected value cannot be anticipated within the current period's financial results until the value is realised.

Development costs

	Half year ended 30 Jun 2013 £m	Half year ended 30 Jun 2012 £m	Year ended 31 Dec 2012 £m
UK	**19**	n/a	n/a
Heritage	**2**	n/a	n/a
UK & Heritage	**21**	18	42
FPI	**4**	4	6
Lombard	**1**	–	2
Total	**26**	22	50

Non-hedgeable risks

A charge equivalent to 1.3% (30 June 2012: 2%, 31 December 2012: 1.5%) has been applied to the projected risk-based group required capital for all non-hedgeable risks over the remaining lifetime of in-force business.

In line with management's view of the business, allowance has been made for diversification benefits within the non-hedgeable risks of the covered business.

Other assumptions

The external STICS, external UT2 subordinated debt with associated currency swap, external LT2 subordinated debt 2021 and external LT2 subordinated debt 2022 are included within the MCEV at market value, based on listed ask price.

30 June 2013	**Principal £m**	**Clean market value of debt £m**	**Accrued interest £m**	**Tax adjustment on market valuation £m**	**Value of debt included in Corporate(i) £m**
STICS 2003	**210**	**198**	**2**	**2**	**202**
STICS 2005	**268**	**252**	**17**	**(1)**	**268**
LT2 subordinated debt 2021	**162**	**204**	**2**	**(11)**	**195**
LT2 subordinated debt 2022	**500**	**525**	**8**	**(9)**	**524**
UT2 subordinated debt (ii)	**356**	**396**	**4**	**(12)**	**388**
Currency swap	**–**	**(23)**	**–**	**6**	**(17)**
Total	**1,496**	**1,552**	**33**	**(25)**	**1,560**

30 June 2012	Principal £m	Clean market value of debt £m	Accrued interest £m	Tax adjustment on market valuation £m	Value of debt included in Corporate(i) £m
STICS 2003	210	133	2	18	153
STICS 2005	268	165	17	20	202
LT2 subordinated debt 2021	162	178	2	(5)	175
LT2 subordinated debt 2022	500	440	8	12	460
Total	1,140	916	29	45	990

31 December 2012	Principal £m	Clean market value of debt £m	Accrued interest £m	Tax adjustment on market valuation £m	Value of debt included in Corporate(i) £m
STICS 2003	210	193	2	4	199
STICS 2005	268	250	8	1	259
LT2 subordinated debt 2021	162	215	12	(16)	211
LT2 subordinated debt 2022	500	554	29	(21)	562
UT2 subordinated debt (ii)	356	378	4	(8)	374
Currency swap	–	6	–	–	6
Total	1,496	1,596	55	(40)	1,611

(i) The value of debt included in the corporate category is the market value of debt, including accrued interest, and the tax asset/liability on the market value adjustment.

(ii) The UT2 subordinated debt was issued in US dollars with principal of $575 million, equivalent to £356 million at issue in November 2012.

The deferred consideration notes, issued in September 2010 in connection with the acquisition of the AXA UK Life Business, were repaid on 20 November 2012 (balance outstanding at 30 June 2012: £363 million; 31 December 2012: £nil).

10. Comparison of MCEV and IFRS classification and segments

The covered business segments within MCEV are consistent with the IFRS business segments.

The split of the MCEV by IFRS business segment is shown in the tables below:

	MCEV classification						
Half year ended 30 June 2013	**UK £m**	**Heritage £m**	**FPI £m**	**Lombard £m**	**Corporate £m**	**Non-covered business(i) £m**	**Total MCEV by IFRS segments £m**
IFRS segment							
UK	**1,333**	**–**	**–**	**–**	**–**	**23**	**1,356**
Heritage	**–**	**3,925**	**–**	**–**	**–**	**3**	**3,928**
FPI	**–**	**–**	**606**	**–**	**–**	**2**	**608**
Lombard	**–**	**–**	**–**	**651**	**–**	**16**	**667**
Corporate	**–**	**–**	**–**	**–**	**(1,560)**	**981**	**(579)**
Total MCEV (by MCEV segments)	**1,333**	**3,925**	**606**	**651**	**(1,560)**	**1,025**	**5,980**

(i) The non-covered business includes £180 million within Corporate representing the MCEV of the Resolution holding companies.

	MCEV classification					
Half year ended 30 June 2012	UK & Heritage £m	FPI £m	Lombard £m	Corporate £m	Non-covered business(i) £m	Total MCEV by IFRS segments £m
IFRS segment						
UK & Heritage(ii)	5,237	–	–	–	21	5,258
FPI	–	622	–	–	(2)	620
Lombard	–	–	552	–	6	558
Corporate	–	–	–	(990)	493	(497)
Total MCEV (by MCEV segments)	5,237	622	552	(990)	518	5,939

(i) The non-covered business includes £(61) million within Corporate representing the MCEV of the Resolution holding companies.

(ii) The split of MCEV between UK and Heritage divisions is not available for 30 June 2012.

Year ended 31 December 2012	UK £m	Heritage £m	FPI £m	Lombard £m	Corporate £m	Non-covered business[(i)] £m	Total MCEV by IFRS segments £m
	MCEV classification						
IFRS segment							
UK	1,227	–	–	–	–	26	1,253
Heritage	–	4,080	–	–	–	12	4,092
FPI	–	–	612	–	–	1	613
Lombard	–	–	–	615	–	5	620
Corporate	–	–	–	–	(1,611)	864	(747)
Total MCEV (by MCEV segments)	1,227	4,080	612	615	(1,611)	908	5,831

(i) The non-covered business includes £133 million representing the MCEV of the Resolution holding companies.

11. FLG annualised return on embedded value

	Half year 2013		Half year 2012		Full year 2012	
	£m	**% p.a.**	£m	% p.a.	£m	% p.a.
Value of new business	**97**	**2.7**	97	2.8	194	2.8
Expected existing business contribution[(i)]	**163**	**4.6**	200	5.7	400	5.7
Operating experience variances	**(31)**	**(0.9)**	(15)	(0.4)	(56)	(0.8)
Operating assumption changes	**34**	**0.9**	14	0.4	(9)	(0.1)
Other operating variance	**30**	**0.8**	19	0.5	27	0.4
Development costs	**(26)**	**(0.7)**	(22)	(0.6)	(50)	(0.7)
Other income and charges[(i)]	**(6)**	**(0.2)**	–	–	(5)	(0.1)
FLG MCEV operating profit before tax and financing	**261**	**7.2**	293	8.4	501	7.2
Impact of financing[(i)]	**(37)**	**0.8**	(43)	0.2	(91)	–
Attributed tax charge on MCEV operating profit	**(54)**	**(1.9)**	(63)	(2.2)	(120)	(2.1)
FLG MCEV operating profit after tax	**170**	**6.1**	187	6.4	290	5.1
Economic variances	**228**	**8.2**	242	8.4	154	2.7
Other non-operating items	**(33)**	**(1.2)**	(92)	(3.2)	(140)	(2.5)
Attributed tax on other activities	**(34)**	**(1.3)**	(26)	(0.9)	(6)	(0.1)
FLG MCEV profit after tax	**331**	**11.8**	311	10.7	298	5.2
Remeasurement (losses)/gains on defined benefit pension schemes	**(20)**	**(0.7)**	8	0.3	(35)	(0.5)
Foreign exchange adjustments	**35**	**1.3**	(18)	(0.7)	(16)	(0.3)
Total return on FLG MCEV over the period	**346**	**12.4**	301	10.3	247	4.4

(i) Impact of financing comprises the expected impact of financing of covered debt of £37 million for half year 2013 (£35 million for half year 2012, £75 million for full year 2012). Previously it also contained the impact of financing the non-covered debt of £200 million which was repaid in November 2012 (with an impact of financing of £8 million for half year 2012 and £16 million for full year 2012). These amounts have been deducted from the expected existing business contribution and other income and charges respectively.

The table above provides an analysis of the return on FLG embedded value, excluding the Resolution holding companies. The starting FLG embedded value for 2013 is £5,698 million, net of the market-consistent value of debt instruments of £1,596 million and having excluded £133 million in respect of the Resolution holding companies. The 2013 embedded value has been adjusted to allow for the timing of dividend payments.

The starting embedded value for 2012 is £5,949 million, net of the market-consistent value of debt instruments of £1,159 million and having excluded £(153) million in respect of the Resolution holding companies. The 2012 embedded value has been adjusted to allow for the timing of dividend payments, the repayment of the internal LT2 subordinated debt 2020 issued to Resolution holding companies by FLG and the new external UT2 subordinated debt and associated currency swap issued during the period.

The FLG MCEV operating return before tax and financing is based on the gross FLG MCEV (i.e. before the market-consistent value of debt). The return includes both covered and non-covered business. The impact of the financing item reflects the leverage on the return on embedded value created within FLG through the use of debt instruments, net of the cost of financing these instruments.

Appendices

Appendix 1: New business information

Analysis of Life and Pensions new business

In classifying new business premiums, the following basis of recognition is adopted:

- single new business premiums consist of those contracts under which there is no expectation of continuing premiums being paid at regular intervals;
- regular new business premiums consist of those contracts under which there is an expectation of continuing premiums being paid at regular intervals, including repeated or recurrent single premiums where the level of premiums is defined, or where a regular pattern in the receipt of premiums has been established;
- non-contractual increments under existing group pensions schemes are classified as new business premiums;
- transfers between products where open market options are available are included as new business; and
- regular new business premiums are included on an annualised basis.

Regular and single premiums

	Regular premiums			Single premiums		
	HY 2013 £m	HY 2012 £m	Change %	**HY 2013 £m**	HY 2012 £m	Change %
UK division						
– Corporate Benefits	**228**	233	(2)	**251**	579	(57)
– Protection	**39**	44	(11)	**-**	-	-
– Retirement Income	**-**	-	-	**324**	187	73
Heritage division	**16**	26	(38)	**105**	340	(69)
Total UK and Heritage	**283**	303	(7)	**680**	1,106	(39)
FPI	**47**	75	(37)	**318**	286	11
Lombard	**-**	-	-	**872**	948	(8)
Total International division	**47**	75	(37)	**1,190**	1,234	(4)
Total Life and Pensions	**330**	378	(13)	**1,870**	2,340	(20)

	Regular premiums			Single premiums		
	Q2 2013 £m	Q2 2012 £m	Change %	**Q2 2013 £m**	Q2 2012 £m	Change %
UK division						
– Corporate Benefits	**133**	117	14	**106**	285	(63)
– Protection	**21**	26	(19)	**-**	-	-
– Retirement Income	**-**	-	-	**179**	96	86
Heritage	**8**	12	(33)	**50**	234	(79)
Total UK and Heritage	**162**	155	5	**335**	615	(46)
FPI	**23**	38	(39)	**159**	150	6
Lombard	**-**	-	-	**405**	505	(20)
Total International division	**23**	38	(39)	**564**	655	(14)
Total Life and Pensions	**185**	193	(4)	**899**	1,270	(29)

Group new business - APE

APE represents annualised new regular premiums plus 10% of single premiums.

	HY 2013 £m	HY 2012 £m	Change %	**Q2 2013 £m**	Q2 2012 £m	Change %
UK division						
– Corporate Benefits	**253**	291	(13)	**144**	145	(1)
– Protection	**39**	44	(11)	**21**	26	(19)
– Retirement Income	**32**	19	68	**17**	10	70
Heritage division	**27**	60	(55)	**14**	36	(61)
Total UK and Heritage	**351**	414	(15)	**196**	217	(10)
FPI	**79**	104	(24)	**39**	53	(26)
Lombard	**87**	95	(8)	**40**	51	(22)
Total International division	**166**	199	(17)	**79**	104	(24)
Total Life and Pensions	**517**	613	(16)	**275**	321	(14)

FPI

APE by region (actual exchange rates)	**HY 2013 £m**	HY 2012 £m	Change %
North Asia	**19**	32	(41)
South Asia	**11**	13	(15)
Middle East	**20**	24	(17)
Europe (Excl UK)	**10**	12	(17)
UK	**9**	10	(10)
Rest of World	**10**	11	(9)
Malaysia (AmLife)	**-**	2	(100)
Total	**79**	104	(24)

Lombard

APE by region (actual exchange rates)	**HY 2013 £m**	HY 2012 £m	Change %
UK and Nordic	**34**	30	13
Northern Europe	**1**	14	(93)
Southern Europe	**48**	41	17
Rest of World	**4**	10	(60)
Total including large cases	**87**	95	(8)
Of which: Large cases (greater than €10m)	**24**	33	(27)
Total excluding large cases	**63**	62	2

New business APE at constant exchange rates

All amounts in currency in the tables above other than Sterling are translated into Sterling at a monthly average exchange rate. The estimated new business assuming constant currency rates would be as follows:

	HY 2013 £m	HY 2012 £m	Change %	**Q2 2013 £m**	Q2 2012 £m	Change %
FPI	**79**	104	(24)	**39**	53	(26)
Lombard	**85**	95	(11)	**40**	51	(22)

New Business - Present value of new business premiums ("PVNBP")

PVNBP equals new single premiums plus the expected present value of new regular premiums. Premium values are calculated on a consistent basis with the EV contribution to profits from new business. Start of period assumptions are used for the economic basis and end of period assumptions are used for the operating basis. A risk-free rate is used to discount expected premiums in future years. The impact of operating assumption changes across a whole reporting period will normally be reflected in the PVNBP figures for the final quarter of the period that the basis changes relate to. No change in operating assumptions will be reflected in the PVNBP for the first quarter. All amounts in currency other than Sterling are translated into Sterling at a monthly average exchange rate.

	HY 2013 £m	HY[i] 2012 £m	Change %	Q2 2013 £m	Q1 2013 £m
UK division					
– Corporate Benefits	**1,213**	1,552	(22)	668	545
– Protection	**290**	282	3	171	119
– Retirement Income	**324**	187	73	179	145
Heritage division	**181**	461	(61)	91	90
Total UK and Heritage	**2,008**	2,482	(19)	1,109	899
FPI	**557**	697	(20)	264	293
Lombard	**872**	948	(8)	405	467
Total International division	**1,429**	1,645	(13)	669	760
Total Life and Pensions	**3,437**	4,127	(17)	1,778	1,659

Appendix 2: Additional new business and in-force information

Analysis of new business strain

At product level, new business is monitored on a "cash strain" basis which excludes movements in required capital and is stated before tax and other adjustments. Tax and other items include the cumulative adjustments for tax and long-term investment return which use different assumptions across the MCEV, regulatory ("or cash") and IFRS bases. IFRS strain also includes DAC/DFF and other IFRS adjustments. The reconciliation from MCEV free surplus to cash strain to IFRS strain is set out below.

UK and Heritage

£m	**UK**	**Heritage**	**2013 Half year**	2012 Half year	2012 Full year
MCEV value of new business, free surplus impact	**(38)**	**(20)**	**(58)**	(98)	(161)
Movement in required capital, tax and other items	***27***	***4***	***31***	*38*	*70*
New business cash strain	**(11)**	**(16)**	**(27)**	(60)	(91)
DAC/DFF	***6***	***5***	***11***	*19*	*35*
Other IFRS adjustments	***(2)***	***3***	***1***	-	*(3)*
IFRS New business strain	**(7)**	**(8)**	**(15)**	(41)	(59)

FPI

£m	**Core**	**Non-core**	**2013 Half year**	2012 Half year	2012 Full year
MCEV value of new business, free surplus impact	**(24)**	**(16)**	**(40)**	(47)	(101)
Movement in required capital, tax and other items	***1***	***(6)***	***(5)***	*(1)*	*(3)*
New business cash strain	**(23)**	**(22)**	**(45)**	(48)	(104)
DAC/DFF	***47***	***9***	***56***	*81*	*175*
Other IFRS adjustments	***(35)***	***-***	***(35)***	*(57)*	*(124)*
IFRS New business strain	**(11)**	**(13)**	**(24)**	(24)	(53)

Lombard

£m	**2013 Half year**	2012 Half year	2012 Full year
MCEV value of new business, free surplus impact	**(12)**	(12)	(23)
Movement in required capital, tax and other items	**-**	-	*4*
New business cash strain	**(12)**	(12)	(19)
DAC/DFF	***(4)***	*(6)*	*(11)*
IFRS New business strain	**(16)**	(18)	(30)

Analysis of IFRS in-force surplus

At product level, in-force surplus is monitored on a "cash surplus" basis which excludes movements in DAC/DFF and other IFRS adjustments. The reconciliation from to cash surplus to the IFRS surplus is set out below.

UK and Heritage

£m	UK	Heritage	**2013 Half year**	2012 Half year	2012 Full year
In-force cash surplus	**39**	**134**	**173**	166	395
DAC/DFF	***(6)***	***(5)***	***(11)***	*(1)*	*(12)*
Other IFRS adjustments	***17***	***24***	***41***	*31*	*12*
IFRS In-force surplus	**50**	**153**	**203**	196	395

FPI

£m	Core	Non-core	**2013 Half year**	2012 Half year	2012 Full year
In-force cash surplus	**53**	**27**	**80**	49	68
DAC/DFF	***(16)***	***(7)***	***(23)***	(3)	(16)
Other IFRS adjustments	***18***	***4***	***22***	*5*	*43*
IFRS In-force surplus	**55**	**24**	**79**	51	95

Lombard

£m	**2013 Half year**	2012 Half year	2012 Full year
In-force cash surplus	**23**	11	28
DAC/DFF	***14***	*17*	*32*
IFRS In-force surplus	**37**	28	60

Appendix 3: International division additional information

Analysis of International division

MCEV

Half year ended 30 June 2013

£m	**Core**			**Non-core**	**Total**
	FPI	Lombard	**International**	FPI	**International**
Net assets	90	80	**170**	-	**170**
VIF	420	571	**991**	96	**1,087**
Total MCEV	**510**	**651**	**1,161**	**96**	**1,257**

Appendix 4: Value share

RCAP UK LP ("RCAP"), an entity established by current and former partners and employees of ROL, is entitled to share in the value created in the Company's subsidiary undertaking, Resolution Holdco No. 1 LP ("Holdco"), which owns the Friends Life group.

This arrangement was established at the time the Company was formed and, in broad terms, entitles RCAP, as an associate of the Company's original sponsor Resolution Capital Limited, to 10% of all distributions made from Holdco where the accumulated value of the deployed equity capital contributed into Holdco (as set out below), plus an agreed return, has been returned to the Company or its shareholders, or there has been a change of control of the Group.

Deployed equity capital has been contributed to Holdco, by the Company and RCAP, to fund the acquisitions of both Friends Provident Group plc in 2009 and the majority of AXA S.A.'s UK life business in 2010. The agreed return is currently 4% per annum. There is no time limit applying to the value share arrangements which are also not affected by termination of the Operating Agreement.

Total gross equity deployed in Holdco is approximately £4,056 million and the accumulated value of net equity deployed (at 4% per annum and after the return of £965 million of capital returned to the Company to date) is approximately £3,573 million as shown below.

Date	Accumulated value of net equity deployed at 4% per annum (£m)
31 December 2011	3,844
30 June 2012	3,758
31 December 2012	3,752
30 June 2013	3,573

The Company's share price does not itself influence whether payments are made under the terms of the value share. This depends on the aggregate amount of distributions made to the Company by Holdco, including to fund payments to shareholders (dividends or returns of capital), or there being a relevant change of control event.

Definitions

AmFamily means AmFamily Takaful Berhad

AmLife means, collectively, AmFamily and AmLife Insurance Berhad

Annual Premium Equivalent ("APE") represents annualised new regular premiums plus 10% of single premiums.

Annualised return on embedded value is calculated as the MCEV operating profit after tax over the period divided by the net Group MCEV at the start of the period adjusted to allow for the timing of dividend payments and any acquisitions or disposals through the period. Where the period is not a full year, the calculated rate is then annualised.

Asset quality is the percentage of corporate bonds and asset-backed securities in the shareholder and non-profit funds at investment grade compared to the total of such assets in these funds.

Available shareholder cash ("ASC") represents cash available to cover corporate costs, to service debt issued by Resolution holding companies and, subject to shareholder approval, to pay dividends or return to shareholders. ASC reflects the deduction of working capital from free surplus.

AXA UK Life Businesses means the traditional and protection businesses, a majority of the corporate benefits business and a minority of the wealth management business carried on by AXA UK which were acquired by the Group in September 2010 and which includes FLWL from November 2011.

Board means the Resolution Limited Board.

Cash payback on new business is the time at which the value of the expected cash flows, after tax, is sufficient to have recouped the capital invested to support the writing of the business. The cash flows are calculated on the same assumptions and expense basis as those used for the contribution from new business.

Company means Resolution Limited.

Distributable Cash Target ("DCT") is £400 million per annum. The contribution to DCT is the increase in FLG ASC after interest and before dividends to Resolution holding companies and is the amount that could be paid to Resolution holding companies without reducing the MCEV of FLG, excluding investment variances and non-recurring items.

Equity Backing Ratio ("EBR") is the proportion of equities and property backing asset shares.

Free surplus at the end of the period represents the excess of net worth (equivalent to shareholder resources) over required capital and inadmissible items on an MCEV basis for covered businesses plus IFRS net assets, less required capital and inadmissible assets on an IGCA basis for non-covered businesses and holding companies. Free surplus comprises ASC plus working capital.

Free surplus generated comprises the movement in free surplus over the period adjusted for capital, foreign exchange and other reserve movements.

Friends Life or Friends Life group means Friends Life Group plc (and its subsidiaries and subsidiary undertakings from time to time including Friends Provident from November 2009, the AXA UK Life Business from September 2010, BHA from January 2011 and FLWL from November 2011).

Friends Life holding companies means Friends Life Group plc, Friends Life FPG Limited and Friends Life FPL Limited.

Group means Resolution Limited and its subsidiaries and subsidiary undertakings from time to time.

Group embedded value on an MCEV basis ("Group MCEV") is the equity attributable to equity holders of the parent as shown in the consolidated statement of financial position - MCEV basis.

Heritage division means Friends Life's UK business comprising products that are no longer actively marketed to new customers and legacy products that have previously been closed to new business.

IFRS based operating profit/(loss) is the profit (or loss) based on longer-term investment return excluding: (i) all investment return variances from expected investment return which is calculated on a long-term rate of return, (ii) policyholder tax, (iii) returns attributable to minority interests in policyholder funds (iv), significant non-recurring items, (v) amortisation and impairment of acquired intangible assets and present value of acquired in-force business; and is stated after deducting interest payable on STICS.

IFRS profit/(loss) after tax is the profit (or loss) after tax as shown in the consolidated income statement.

IGCA surplus is the Insurance Groups Capital Adequacy surplus capital as defined by the PRA in the Insurance Groups Directive. It is calculated as the surplus of the available capital resources over the capital resources requirement. It excludes the surplus capital held within the long-term funds.

Internal rate of return ("IRR") on new business is equivalent to the discount rate at which the present value of the after tax cash flows expected to be earned over the lifetime of the business written is equal to the capital invested to support the writing of the business. With the exception of investment return, all assumptions and expenses are consistent with those used for calculating VNB. IRR assumes best estimate investment returns after an allowance for default risk, whereas VNB assumes (market consistent) risk-free rates. IRR also takes into account the funding and release of regulatory capital requirements.

MCEV operating profit/(loss) is the MCEV profit (or loss) based on expected investment return and excludes: (i) amortisation and impairment of non-covered business acquired intangible assets, (ii) effect of economic variances (including the impact of economic assumption changes) and (iii) significant non-recurring items.

MCEV profit/(loss) after tax is the MCEV profit (or loss) after tax as shown in the consolidated income statement - MCEV basis.

New business margins are defined as the pre-tax VNB generated by each product type, divided by the PVNBP for that product.

New Life Tax Regime ("NLTR") refers to legislation enacted in the Finance Act 2012 and supporting regulations. NLTR applies to life insurance companies with effect from 1 January 2013 and has not altered the "I minus E" basis of taxation.

Pillar 1 surplus is the excess of capital resources over capital resource requirements calculated in accordance with regulatory requirements.

Pillar 2 surplus is the excess of capital resources over the capital calculated on an economic basis required to ensure that the regulated entities can meet their liabilities, with a high likelihood, as they fall due. The result is reviewed and may be modified by the PRA. Pillar 2 requirements are not generally disclosed.

Present value of new business premiums ("PVNBP") represents new single premiums plus the expected present value of new business regular premiums expressed at the point of sale.

Required capital of the Group is based on the most onerous capital management policy for the Group, currently IGCA.

Resolution Holding companies means the Company, Resolution Holdco No. 1 LP and Resolution Holdings (Guernsey) Limited.

Resolution Operations LLP ("ROL") is a privately owned advisory and operating firm which, as part of the Resolution Group, has provided services to Resolution Limited within the framework of an operating agreement. On 27 March 2013, under a Business Sale Agreement, ROL transferred to the Company business activities that related to the services provided to the Company and the ROL employees who provided the services. At the same time, ROL ceased to provide services to the Company.

Shareholder resources are a measure of the tangible assets available to the life and pensions business and attributable to shareholders. The movement in shareholder resources provides a view of the sustainability of the business model. Shareholder resources are based on shareholders' invested net assets included within the embedded value.

Sustainable Free Surplus ("SFS") is the free surplus generated within FLG based on expected investment return less investment in new business and excludes operating assumption changes, amortisation and impairment of non-covered business, acquired intangible assets, effect of economic variances (including the impact of economic assumption changes) and significant non-recurring items.

Value of new business ("VNB") relates to new business written in the reporting period and reflects the present value of future cash flows on that block of business. It is calculated using economic assumptions at the beginning of the period except for immediate annuities for which the assumptions used are appropriate for each month's new business on account of their interest rate sensitivity. It is also calculated using year end operating assumptions consistent with those used to determine the year end MCEV embedded value. VNB is shown after the effects of the frictional costs of holding required capital and share-based payments, and after the effect of the costs of residual non-hedgeable risks.

Working capital, as a component of the Group's cash and capital management framework, represents free surplus assets set aside to cover known future requirements and amounts necessary to maintain sufficient flexibility to facilitate compliance with the Group capital policy, additional regulatory requirements and any other assets restricted in their availability to shareholders.

Abbreviations

ABI	Association of British Insurers
ABS	Asset-Backed Securities
AGM	Annual General Meeting
ALM	Asset and Liability Management
AMC	Annual Management Charge
APE	Annual Premium Equivalent
ASC	Available Shareholder Cash
AVIF	Acquired Value of In-Force
AXA IM	AXA Investment Management
BHA	The acquired business formerly known as Bupa Health Assurance Limited
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CGU	Cash Generating Unit
CMPs	Capital Management Policies
CNHR	Cost of Non-Hedgeable Risk
COP	Capital Optimisation Programme
CRO	Chief Risk Officer
CRR	Capital Resource Requirements
DAC	Deferred Acquisition Costs
DCN	Deferred Consideration Notes
DCT	Distributable Cash Target
DFF	Deferred Front End Fees
DPF	Discretionary Participation Features
EEA	European Economic Area
EU	European Union
FAL	Friends Annuities Limited (formerly known as AXA Annuity Company Limited)
FCA	Financial Conduct Authority
FLAS	Friends Life Assurance Society Limited (formerly known as Sun Life Assurance Society plc)
FLC	Friends Life Company Limited (formerly known as AXA Sun Life plc)
FLG	Friends Life Group plc (formerly known as Friends Provident Holdings (UK) plc)
FLI	Friends Life Investments
FLL	Friends Life Limited (formerly known as Friends Provident Life and Pensions Limited)
FLMS	Friends Life Management Services Limited
FLPL	Friends Life and Pensions Limited
FLSL	Friends Life Services Limited (formerly known as AXA Sun Life Services plc)
FLWL	Friends Life WL Limited (formerly known as Winterthur Life UK Limited or WLUK)
fpb	Financial Business Partners AG
FPI	A segment within the International division comprising FPIL, OLAB and (to the date of its disposal) AmLife
FPIL	Friends Provident International Limited

FPL	Friends Life FPL Limited
FPPS	Friends Provident Pension Scheme
FRA	Flexible Retirement Account
FRS	Financial Reporting Standards
FUM	Funds Under Management
HNWI	Higher Net Worth Individuals
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICA	Individual Capital Assessment
ICG	Individual Capital Guidance
IFA	Independent Financial Adviser
IFRIC	IFRS Interpretation Committee
IFRS	International Financial Reporting Standards
IGCA	Insurance Groups Capital Adequacy
IRR	Internal Rate of Return
LTIP	Long-Term Incentive Plan
LT2	Lower Tier 2
MCEV	Market Consistent Embedded Value
NBS	New Business Strain
NGP	New Generation Pension
NLTR	New Life Tax Regime
NPF	Non-Profit Fund
OCI	Other Comprehensive Income
OEIC	Open Ended Investment Company
OLAB	Overseas Life Assurance Business
OMO	Open Market Option
PBSE	Post-Balance Sheet Event
PIIGS	Portugal, Ireland, Italy, Greece and Spain
PPFM	Principles and Practices of Financial Management
PRA	Prudential Regulation Authority
PUP	Paid Up Policies
PVFP	Present Value of Future Profits
PVNBP	Present Value of New Business Premiums
RDR	Retail Distribution Review
RICS	Royal Institution of Chartered Surveyors
RIE	Re-attributed Inherited Estate
ROEV	Return on Embedded Value
ROL	Resolution Operations LLP
RPI	Retail Prices Index
RSL	Resolution Limited. In respect of MCEV disclosures, RSL denotes Resolution Limited and its subsidiary undertakings
SBG	Sesame Bankhall Group
SFS	Sustainable Free Surplus
STICS	Step-up Tier one Insurance Capital Securities
TVOG	Time Value of financial Options and Guarantees

UT2	Upper Tier 2
VIF	Value of In-Force
VNB	Value of New Business
WLUK	Friends Life WL Limited (formerly Winterthur Life UK Limited)
WPF	With-Profits Fund
WPICC	With Profits Insurance Capital Component