

Towards a stronger Aviva

Aviva plc Annual report and accounts 2012

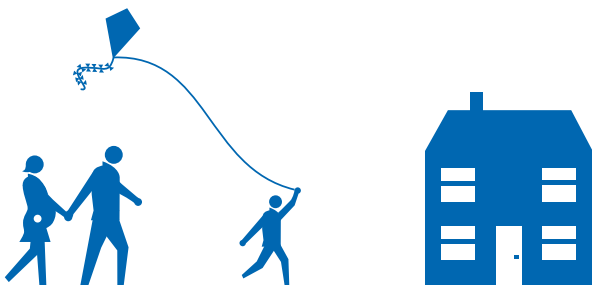


Aviva is a life, general and health insurance business and provides asset management services. We are the largest insurer in the UK* and we have strong businesses in selected international markets.

Our products help 34 million customers** enjoy the peace of mind that comes from managing the risks of everyday life. With us, they can save for a more comfortable retirement and protect – with insurance – the people and things that are important to them.

We're here to help people, businesses and communities get back on their feet when the unexpected happens. It is therefore our responsibility to make sure that our 317-year-old business will be there for our customers long into the future.

2012 was a year of change for Aviva. In this annual report you can read more about how we're taking steps to create a stronger Aviva.



View our reports online



2012 Annual report and accounts

We provide our annual report online which allows us to reduce the paper we print and distribute.

Visit Aviva plc
www.aviva.com/reports/2012ar



2012 Corporate responsibility report

Find out more about our commitment to acting as a responsible member of the international business community.

View our CR report here
www.aviva.com/reports/2012cr

* Based on aggregate 2011 UK life and pensions sales (PVNBP) and general insurance gross written premiums

** On an ongoing basis

What's inside

Inside the essential read

Our plan to change Aviva

In July 2012, we announced a plan designed to strengthen our capital position and transform Aviva: Focus, Strengthen, Perform.

Page 02

Chairman's statement	04
Group chief executive officer's statement	06
Chief financial officer's statement	10
Measuring our performance in 2012	14
Our business model	18
Market context	19
Market focus	20



Chairman's statement

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In the middle of 2012, we launched a radical repositioning of the Group, setting out an ambitious programme

Page 04



Group chief executive officer's statement

“

Actions to focus the business, strengthen the balance sheet and improve performance have been the right ones

Page 06



Chief financial officer's statement

“

We have improved profitability of new business, cash flows to Group and our operating capital generation

Page 10

Performance review

Financial and operating performance	26
Selected consolidated financial data	40
Information on the company	41
Organisational structure	48
Analysis of investments	50
Contractual obligations	55
Risk and capital management	56
Basis of preparation	60

Corporate responsibility

2012 Highlights	62
Our corporate responsibility strategy	62
Trust and transparency	64
Attracting and retaining talent	66
Community and Development	67
Climate change and environment	68
Key indicators	70
Accounting for Sustainability	72
Indices and benchmarks	75
Independent Assurance Report	76

Governance

Chairman's governance letter	78
Board of directors	80
Group Executive	83
Directors' report	85
Corporate governance report	89
Nomination Committee report	95
Audit Committee report	97
Risk Committee report	100
Corporate Responsibility Committee report	103
Directors' remuneration report	104

Shareholder information

Company address	122
Share capital	122
Related party disclosures	124
Dividend data	124
Guarantees securitised assets and off-balance sheet arrangements	125
Liquidity and capital resources	125
Regulation	129
Risks relating to our business	135

Financial statements IFRS

Independent auditors' report	146
Accounting policies	148
Consolidated financial statements	160
Consolidated income statement	160
Consolidated statement of comprehensive income	161
Reconciliation of Group operating profit to (loss)/profit for the year	162
Consolidated statement of changes in equity	164
Consolidated statement of financial position	166
Consolidated statement of cash flows	167
Notes to the consolidated financial statements	168
Financial statements of the Company	267

Other information

Glossary	274
Shareholder services	276

Our plan to change Aviva

In July 2012 we set out to reposition Aviva

Aviva has great strengths which we can build on. We have a focused portfolio of businesses under a strong brand; some, such as the UK, France and Canada are great cash generators, while others represent growth potential, such as Poland, Turkey and Singapore.

In early 2012, we reviewed all of our businesses in the light of legitimate concerns about our performance. We concluded that we must:

- build up capital and financial strength
- improve the profitability of underperforming parts of our business
- reduce costs and eliminate bureaucracy
- become a less complex organisation

Taking all this into account, in July 2012, we produced a plan designed to transform Aviva:

Focus, Strengthen, Perform

This plan is successfully addressing the immediate issues.

So far, we have exited a number of businesses, improved Aviva's capital position and there are plans to improve the operating performance of our underperforming businesses.

We will now take Aviva to the next phase of its turnaround.



Narrow focus

When we assessed our business we identified 58 distinct revenue-earning business areas. 15 of them were performing particularly well. 27 weren't realising their full potential and 16 were performing below acceptable levels. We decided to:

- Focus on businesses where we can produce attractive returns
- Improve underperforming businesses
- Exit businesses which we do not consider central to our future growth



Build financial strength

We resolved to improve our economic capital levels so that they are in line with our industry peers. We plan to do this by making disposals and reducing the amount of capital we allocate to businesses producing lower returns. Our goals were to:

- Maintain an economic capital coverage ratio of between 160% and 175%
- Reduce capital volatility



Improve performance

We concluded we must deliver better revenue growth, lower losses and claims, and improved profitability. We decided to:

- Develop new revenue growth, mainly in our core UK, European and Canadian markets
- Reduce annual expenses by £400 million by the start of 2014
- Change our culture to remove bureaucracy and ensure our people perform to their full potential

Chairman's statement



John McFarlane
Chairman



It is management's view, endorsed by the Board, and with firm regulatory support, that we prioritise the reduction of internal and external debt over dividend preservation.

Dear shareholder

Management is demonstrating professional execution as well as prudence. I am confident about the future of Aviva.

Mark has started very strongly. His focus going forward is on cash flow, earnings growth, and reducing leverage. This has my full endorsement as well as that of the Board.

Strong progress and momentum in reshaping the Group

In mid-2012, we launched a radical repositioning of the Group, setting out a relatively ambitious programme to bring the Group to a stronger, more stable position with improved earnings performance and operating cash generation in 2014 and beyond:

- Refocus on core, exit 16 non-core segments, and turnaround 27 segments
- Reduce exposure to southern Europe and capital hungry segments
- Improve productivity, performance and operating capital generation
- Strengthen economic capital and reduce leverage

As it turned out, we have had a very active period, but achieved a great deal in a short time.

Boosting capital was our main initial priority and I am pleased we were able to increase the economic capital surplus substantially by £3.5 billion from the end 2011 (130% coverage) to a pro-forma level of £7.1 billion (172% coverage), within our stated target range.

We have since exited seven of the most material "red" cells on time and at respectable prices, better and faster than was generally expected of us and action is being taken on the balance. Specifically, we announced the disposal of the US business, our stake in Delta Lloyd, and a number of smaller interests around the world, the settlement of our dispute with Bankia in Spain, a significant reduction in our exposure to Italy and Spain, and the exit of large bulk purchase annuities in the UK.

We also targeted improvement by the end of 2013 in 27 "amber" cells, through revenue increase, cost reduction, loss mitigation, or capital reduction. Seven of these have been brought to "green" status. As we stand, we now have nine red cells, 20 amber cells and 22 green cells.

We also reshaped our top management team, particularly with the appointment of a strong and decisive CEO, and made progress in the renewal of the Board.

Reducing leverage

The announced sale of the US, though strategically imperative, nevertheless resulted in a sharp reduction in net assets per share and a consequent increase in tangible leverage from 41% to 50%, which is high relative to the sector. We have therefore revised our forward plans to bring this to below 40%, by increasing retained earnings and by reducing debt.

Our achievements in 2012:

-  Narrow focus
-  Build financial strength
-  Improve performance



In March 2012 announced new operating targets for 2012



Shareholder consultation on remuneration announced at the AGM



Announced plan to remove the regional layer of the business



John McFarlane assumed executive role in May 2012

Key statistics in 2012

£1,888m

Adjusted operating profit before tax on a continuing basis

£1,427m

Adjusted operating profit before tax on a continuing basis after integration and restructuring costs

£3bn loss

Overall, an IFRS loss after tax primarily driven by the write-down from the disposal of our US business

19p

Total dividend

On 1 January 2013, we began the simplification of the Group's legal structure to improve governance over the UK general insurance business. This, when completed by the end of May 2013 is expected to formalise an inter-divisional balance of around £5.8 billion in the form of a collateralised loan. In response to these pressures, we have decided to bring down the level of both internal and external debt to lower, more prudent, levels.

The decision to reduce the dividend

At the same time, constraints, including regulatory, on capital and liquidity, are putting greater demands on resources, as does our transformation programme, particularly this year. While central liquidity balances are likely to improve with the settlement with Bankia and the completion of the sale of the US business, Group resources nevertheless contain insufficient provision for unknown risks, our desire to pay down internal and external debt, and to maintain prudent capital and liquidity levels.

In the circumstances therefore, we have taken the difficult decision to reduce the dividend to a level that can be cash covered in 2014 and to enhance the availability of resources for important long-term structural requirements.

Accordingly we declared a final 2012 dividend of 9 pence per share, bringing the full-year dividend down by 27% to 19 pence from 26 pence and the final by 44% from 16 pence.

I regret this has become necessary, but can assure shareholders we took this decision only after examining scrupulously all alternatives. The need to ensure that the current and future dividend is sustainable and covered by operating cash generation is fundamental. The broad transformation of the Group in the midst of continuing economic uncertainty also requires that we maintain and grow the level and flexibility of capital and liquid resources.

Zero bonuses for Executive Directors

While we appreciate the considerable progress that has been made on a number of fronts, we do not believe the overall situation of the Group warrants bonuses for executive directors for 2012 or pay rises for 2013.

Improved outlook

The turnaround programme continues apace. We are taking decisive action on costs and in improving business performance. 2013 though remains a transitional year through significant restructuring charges and the loss of earnings from subsidiaries earlier disposed.

We have forward business plans to 2015 that are robust, show significant improvement, and that the new dividend level is cash covered. Increased retained earnings and stronger liquidity should also permit reasonable reduction in internal and external debt levels, thus bringing overall leverage to a more reasonable level.

Management is demonstrating professional execution as well as prudence. I am confident about the future of Aviva, and for our prospects going forward.



John McFarlane
Chairman



New plan of Focus, Strengthen, Perform announced on 5 July 2012



Reduced shareholding in Delta Lloyd to under 20%



In September 2012, announced the sale of our business in Sri Lanka



Mark Wilson appointed as CEO to start in January 2013



Agreed to transfer Aseval to Bankia for £500 million

Group chief executive officer's statement



Mark Wilson
Group chief executive officer

“
My intention is that Aviva will have a robust balance sheet with strong and predictable cash flows, diversified earnings and capital, and lower leverage.

Investment thesis: “cashflow and growth”

Aviva is a company with a rich legacy, some strong businesses, an outstanding brand, a large customer base and very talented people.

I joined Aviva because I believe there is significant potential to be unlocked. Aviva is a turnaround story.

In my first few months at Aviva I have had the opportunity to visit a number of our businesses and to speak to many customers. What strikes me is the dedication and professionalism of those colleagues who look after customers' needs every day. Our customer service in many parts of the business is a genuine differentiator.

However, in recent years Aviva has not lived up to its potential and has disappointed shareholders. In 2012 our Chairman, John McFarlane, highlighted these issues and set out a clear plan. The actions in 2012 to focus the business, strengthen the balance sheet, and improve performance have been the right ones and progress has been made.

Aviva has delivered a large part of the disposal programme. In line with the plan laid out in July last year, in 2012 we narrowed the focus of our business through the announced sales of our most significant non-core businesses, including the sales of Delta Lloyd, USA, Sri Lanka, Malaysia and lastly Russia. In addition we have agreed to transfer Aseval to Bankia for £500 million.

As a result our capital position has improved markedly, with the economic capital surplus strengthening from £3.6 billion to £7.1 billion, giving a coverage ratio now of 172% on a proforma basis, well within our target range of 160%–175%.

This plan has successfully addressed the immediate capital and focus issues. We now need to take Aviva to the next phase of its turnaround.

Investment thesis: “cashflow and growth”

It is clear to me that Aviva has not articulated why investors should buy or hold Aviva shares – what investors should expect of us.

I believe there is a clear space in the market for a simple proposition: a diversified insurer that can provide sustainable and growing cash flows and that has good options for growth. Whilst many will focus on valuation methodologies – such as MCEV, TEV and EV – Aviva will focus the business on progressive cashflow generation.

My intention is that Aviva will have a robust balance sheet with strong and predictable cash flows, diversified earnings and capital, and lower leverage.

Following the progress made on the disposal programme, we are now a more focused portfolio of businesses. Some are cash generators, such as the UK, France and Canada, with upside potential whilst others provide opportunities for growth such as Poland, Turkey, and Singapore.

Put simply, our investment thesis is about progressive cashflow and growth, in that order.

Our 2013 priorities:

- Cashflow
- Simplicity
- Balance sheet



Focus the business on remitting cash flows to Group



Deliver in excess of £400 million cost savings



Improve operating performance, including turning around the 'amber cells'

Key statistics in 2012

£23bn
Gross written premiums

£311bn
Total funds under management

172%
Estimated proforma economic capital surplus ratio, as at 31 December 2012

Cashflow

Three core businesses

Aviva has scale positions in the three core business lines of life and savings, general insurance and fund management – all under a strong brand. We have businesses in attractive, established markets which generate strong cash flows and which offer cross-sell potential. Aviva is world class in many core areas of insurance. For example, our underwriting, analytics and claims expertise, especially in Canada and UK general insurance, are impressive. And we have clear strengths in distribution including direct, through intermediaries, and through bancassurance where we have over 100 agreements.

Focus on cashflow

We will manage the established markets for cash and ensure that the subsidiaries remit progressive cash dividends to the Group. Product development will be driven by a clear focus on sustainable cash flows. For example, in the UK we have managed the volume and pricing of our annuity business so that cash flows are brought forward and capital strain is lowered.

It is also about our scale: we have approximately 34 million customers, annual life and general insurance gross written premiums of around £23 billion and over £300 billion total funds under management.

Significant diversification benefits

Diversity, spreading the risk from one to many, is a central tenet of insurance. Aviva's diversity across our three core businesses and across selected markets gives earnings stability and capital benefits. For example, product line and geographic diversification brings a significant reduction in our economic capital requirements.

Robust balance sheet

Our focus is to ensure that we have a robust balance sheet which underpins the cash flows by managing our balance sheet exposures actively, focusing on economic capital as the principal measure. The outstanding issue to be addressed is our internal and external leverage position. We have a clear plan to tackle this.

Financial simplicity

The insurance business is perceived as complex. Aviva has also for some time been criticised for the complexity of its financial disclosure and business structure, and this problem has been exacerbated by our internal leverage. Our plans to reduce internal leverage and reorganise our structure will provide some of the clarity our shareholders desire.

Growth

Insurance expertise and scale drives cashflow growth in our established markets

Our established markets not only provide good cash flows but also offer potential for growth. Managing our substantial back books and focusing on improving persistency levels will increase the value from our existing customer base.

Valuation upside from gradual UK & European recovery

The majority of Aviva's business is concentrated in the UK and Europe. Over the last 12 months we have spent considerable time improving our risk profile. As a result, we are well positioned to benefit from a gradual UK and European recovery.

Exposure to growth markets in Europe and Asia

We have a number of businesses which offer growth potential in markets such as Poland,



Grow the value of life new business and improve general insurance COR



Continue to strengthen the management team



Simple, clear metrics

Turkey, and Singapore. These will be managed with a view to value growth under strict capital controls.

Reducing expenses

We will continue to focus on improving cost efficiencies and, particularly, on reallocating resources to initiatives where we can earn the highest returns and strong cash flows. We will deliver in excess of £400 million cost savings.

Upside from operational improvement

We have previously highlighted to the market there are elements of the Group which have underperformed for some time, where cash flows have not been optimised and where our expenses are too high. The turnaround of these amber cell businesses gives opportunity to create value for shareholders.

Balance sheet

Aviva's corporate structure was overly complex and far from optimal. Our internal leverage through the interdivisional balance was too high and created an unsatisfactory long-term exposure for the UK general insurance business. This internal leverage, together with external leverage, must be addressed.

Pat Regan explains the change to our corporate structure in more detail in his CFO statement. In summary, we have replaced the interdivisional balance between Group and UK general insurance with a formal loan and we plan to reduce this by £600 million in total over the next three years.

We have kept the FSA informed of our thinking in relation to these issues and they are supportive of the actions we are taking. With respect to our external leverage, we have a medium term target ratio of below 40%.

The de-risking and strengthening of our balance sheet is entirely aligned with our investment thesis and cashflow focus.

The immediate priority, therefore, is to reduce the Group's leverage and to pay an appropriate dividend.

Rebased dividend

For our cashflow and growth investment thesis to be delivered we must tackle the issue of leverage. As such we have only one course of action. The dividend needs to be rebased with reference to growth in cash flows and earnings.

For analysts covering the stock I am cognisant that there are two schools of thought. On the one hand, we have those that would suggest that with our successful disposal programme we have enough liquidity to pay dividends at the historic rate. Others would suggest that the business earnings are not sufficient to fund the dividend and therefore the dividend is too tight. The reality is that both of these arguments are right – we have enough short term liquidity to be able to pay the dividend, but cash flows from the business are too tight to sustain the historic level.

The recent disposals have resulted in our leverage ratio increasing further with the reduction in net assets. This leverage issue must be addressed and leverage will be reduced.

As a result of this, we have declared a final 2012 dividend of 9 pence per share, from 16 pence. This brings the full-year dividend down to 19 pence per share, from 26 pence. In addition we have also decided to eliminate the scrip. I acknowledge that whilst rebasing the dividend will disappoint some shareholders, this will be mitigated to some degree by eliminating the dilutive scrip element. This is a difficult decision and is absolutely necessary to ensure Aviva is put on a sound footing for the future. The removal of the scrip will stop further

Our 2013 priorities:

-  Cashflow
-  Simplicity
-  Balance sheet



Communicate a clear customer proposition



Completion of the disposal programme



Strategic realignment of Aviva Investors, a core business

Key statistics in 2012

34m
Customers worldwide

£29bn
Paid out in claims and benefits due in 2012

100
Bancassurance agreements

shareholder dilution, given that the scrip has had a dilutive impact of 16% over the last eight years. This measure improves earnings per share growth, is consistent with improving financial simplicity, and gives clarity to cash flows and the dividend.

Looking ahead, Aviva will have a progressive dividend policy, with reference to growth in cash flows and earnings. We would expect the 2013 interim dividend to rebase in line with the percentage reduction in the 2012 final dividend.

People

Achievement of Aviva's turnaround necessitates a strengthened management team.

The appointment of Nick Amin as Group transformation director improves our ability to deliver the turnaround plan. The appointments of David McMillan as CEO of Aviva Europe and Jason Windsor to the Group Executive, strengthen our executive team.

The appointment of Khor Hock Seng as CEO of Aviva Asia, reaffirms our commitment to selected markets in that region and gives us strong Asian leadership with deep market experience. Christine Deputy's appointment as our new Group HR Director gives us the necessary leadership and experience for our cultural change.

In addition, given the economic climate and the recent performance of the Group, I have implemented a pay freeze for the top 400 managers and focused our resources towards other levels. I believe very strongly in paying for performance. Our overall spend on bonuses at senior levels will match the business performance and will be based on rigorous differentiation between performance levels. We will focus the money available on our top performers who made the largest contribution.

Our priorities in 2013

Cashflow

- Focus businesses on cash flows to Group
- Deliver in excess of £400 million cost saves
- Improve operating performance
- Grow the value of life new business and improve general insurance COR

Simplicity

- Continue to strengthen the management team
- Communicate a clear customer proposition
- Continue the disposal programme
- Strategic realignment of Aviva Investors, a core business

Strength

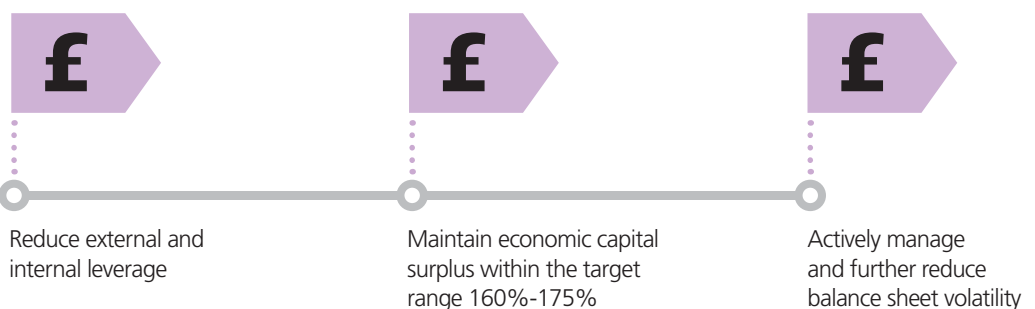
- Reduce external and internal leverage
- Maintain economic capital surplus within target range (160%–175%)
- Actively manage and further reduce balance sheet volatility

Outlook

To move forward, Aviva has had to make some difficult choices. The decisions we have made are realistic, provide clarity and address the uncertainty that has surrounded our stock. It is now up to Aviva to deliver the performance.



Mark Wilson
Group chief executive officer



Chief financial officer's statement



Patrick Regan
 Chief financial officer

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 The economic capital position has significantly improved but, as a result of the disposals we have made, leverage has increased.

Progress against turnaround plan

We have made good progress improving our capital strength and narrowing the Group's focus.

The agreed sale of the US has been a main contributor to a loss after tax of £3.1 billion. Operating performance is broadly in line with the previous year, but with higher restructuring costs as we transform the Company. Operating profit on an underlying basis¹ was down 4% in 2012 primarily due to adverse foreign exchange movements.

We have seen improvements in profitability of new business, cash flows to Group and good levels of operating capital generation. The economic capital position has significantly improved but, as a result of the disposals we have made, leverage has increased. We have also taken action to simplify the Group's corporate structure, formalising the inter-divisional balance into a loan of which we will pay down £600 million over the next three years.

Financial strength

The number one priority in 2012 was to improve Aviva's capital position. During the year we have taken a number of management actions and this, combined with market movements, means that our IGD and economic capital solvency surpluses have improved significantly.

We have simplified our portfolio of businesses and as a result Aviva will operate in 18 countries, from 30 three years ago. These changes, including the announced sales of Aviva USA and Delta Lloyd and the settlement of our agreement to transfer Aseval to Bankia in Spain, will result in a positive movement in our economic capital. On a proforma basis the estimated economic capital surplus improved to £7.1 billion with a coverage ratio of 172% as at 31 December 2012 (2011: £3.6 billion; 130% coverage).

In addition, we have now made the calculation more prudent to now include the pension deficit funding on a 10 year basis (previously five year basis). The IGD solvency surplus has improved to £3.8 billion as at 31 December 2012 (2011: £2.2 billion).

At the end of February 2013, our estimated pro forma economic capital coverage ratio was 175%.

We also took a number of steps to reduce the volatility of our capital position. In July we reduced our holding in Delta Lloyd from 41% to just under 20% and in January 2013 we sold our remaining stake.

Over the course of the year we also reduced our exposure to Italian sovereign debt with a gross sell down of €6.5 billion² this year from our shareholder and participating funds. After taking into account market movements and new business, the value of our net direct shareholder and participating fund holdings (net of NCI) in Italian sovereign debt is now £4.9 billion (2011: £6.4 billion) of which net direct shareholder exposure is £0.4 billion. Of the £4.9 billion Italian sovereign debt 74% is held in Italy.

Aviva's external debt and preference shares stood at £6.9 billion at the end of 2012. As a result of the reduction in net asset value from the disposals the external debt leverage ratio increased to 50%³. It is our intention to reduce this to below 40% over the medium term.

Loss after tax

The overall result for the year was a loss after tax of £3.1 billion (2011: profit after tax £60 million). For continuing operations, the loss after tax was £202 million.

Our performance:

-  Narrow focus
-  Build financial strength
-  Improve performance



In January 2012, agreed the sale of Czech, Hungarian and Romanian life businesses



Reduced Italian sovereign debt exposure during 2012



In December 2012, agreed sale of Aviva USA Corporation

¹ In 2012, operating profit on an underlying basis represents Aviva Group excluding Delta Lloyd and the United States.

² 2011 operating profit on an underlying basis represents Aviva Group excluding Delta Lloyd, United States and RAC.

³ Gross of non-controlling interests (NCI), purchases and redemptions

⁴ External debt and preference shares divided by total tangible capital employed

Key statistics in 2012

14.9%

Life new business internal rate of return excluding Delta Lloyd and United States

97%

General insurance combined operating ratio

278p

IFRS net asset value

The largest driver of the overall loss is the agreed sale of our US business. At HY12 we recognised an impairment of goodwill and intangibles of £0.9 billion related to that business, and at the full year we recognised a further impairment of £2.4 billion. This was partially offset by positive investment variances of £0.3 billion.

On a continuing basis loss after tax was £202 million. Drivers of this loss after tax are operating profits offset by integration and restructuring costs of £461 million, primarily reflecting the execution of the transformation plan; adverse investment variances of £634 million; net adverse post tax non-operating items in Delta Lloyd of £304 million (principally relating to movements in the Delta Lloyd Group curve), and loss on disposals of £164 million and other goodwill and intangible impairments of £188 million.

Operating profit per share (EPS) on a continuing basis was 39.2 pence (2011: 47.5 pence). Total EPS was negative 113.1 pence (2011: 5.8 pence) reflecting the loss on the sale of the US business.

Net asset value

IFRS net asset value per share was 278 pence (2011: 435 pence) reflecting the loss after tax, actuarial movements on the pension scheme, payment of the dividend and adverse foreign exchange movements. On a proforma basis (including the transfer of Aseval to Bankia in Spain) IFRS NAV is 284p.

The MCEV net asset value decreased to 422 pence (2011: 441 pence) primarily driven by operating profits, positive investment variances, actuarial movements on the pension scheme, payment of the dividend and adverse foreign exchange movements. The impact of the agreement to sell Aviva USA is positive under MCEV and offsets the goodwill and intangible impairments in other markets.

Operating performance

Operating profit on an underlying basis is £1.8 billion (2011: £1.9 billion), a 4% reduction

compared with 2011. This was driven primarily by adverse foreign exchange movements of £65 million. Operating profit on a constant currency basis, excluding Delta Lloyd and RAC, was stable reflecting slightly lower operating profits from our life business partly offset by a small increase in profits from our general insurance and health businesses.

Operating profit on an underlying basis after restructuring costs was £1.3 billion (2011: £1.6 billion). This includes restructuring costs of £461 million relating to our underlying businesses (2011: £261 million) mainly driven by the transformation of the business, the integration of Ireland into the UK business and preparations for Solvency II.

The IFRS return on equity was 10.3% (2011: 12.0%). This was driven by the overall reduction in operating profit for the period.

Life insurance

IFRS operating profit from our life insurance business fell by 5% to £1,831 million (2011: £1,926 million) primarily as a result of adverse foreign exchange movements.

In the UK, operating profit reduced to £887 million (2011: £917 million). On an underlying basis, excluding net one-off items in 2011 and 2012, operating profit improved by 2%. New business profitability increased by 17% to give an overall increase in new business income of 9%. Key drivers of this were increased protection sales and pricing actions together with lower bulk purchase annuity sales reflecting our focus on improving profitability. There was also a reduction in the proportion of lower margin Irish business following the closure of our joint venture with AIB. We continue to expand our protection business with an exclusive five year agreement with Tesco, building on the strong bancassurance franchise already in place in the UK.

The improvement in new business income has been offset by lower investment returns due to lower opening funds under management, reduced yields on shareholder assets and higher acquisition expenses due to changes in business mix.



On a pro forma basis estimated economic capital surplus coverage ratio of 172% as at 31 December 2012



IGD solvency surplus improved to £3.8bn as at 31 December 2012



In 2012, generated £2bn of operating capital, ahead of target

Key statistics in 2012

£1,888m

Adjusted operating profit before tax on a continuing basis

£1,427m

Adjusted operating profit before tax on a continuing basis after integration and restructuring costs

10.3%

IFRS return on equity

£2.0bn

Net operating capital generation

Net UK funds under management increased by £2.2 billion in 2012. This was driven by strong sales of individual annuities and GPP giving rise to net inflows of £1.2 billion for our non-profit business. Market and other movements were £5.3 billion, offset by net outflows from the UK with-profits book of £4.3 billion.

In **France**, life operating profit increased to £335 million (2011: £323 million) despite the weakening of the euro during the year. Although new business income reduced to £120 million (2011: £142 million) as a result of volume reductions, we reduced expenses and profitability was broadly stable. Participating business income was stable at £333 million with a small increase in average reserves (on a constant currency basis) and improved profitability.

In **Italy**, overall operating profit increased to £159 million (2011: £140 million). Our continued focus on improving product design and capital efficiency in a tough economic environment impacted both new business volumes and profitability. New business income reduced to £64 million (2011: £121 million). This was more than offset by improved expected return of £65 million (2011: £47 million) and lower expenses of £169 million (2011: £232 million).

In **Spain**, overall life operating profit was stable at £215 million (2011: £216 million) despite the weakening of the euro during the year. Within this total underwriting margin increased to £142 million (2011: £139 million) offset by a reduction in investment return to £143 million (2011: £158 million). The continuing difficult economic conditions and contraction in the mortgage market have resulted in a significant reduction in new business volumes. However, new business profitability was maintained and there were stable returns from the in-force portfolio. The agreed transfer of the Aseval business to Bankia will reduce new business volumes following the completion of the transaction in 2013.

In our other businesses, income in **Singapore** increased to £65 million (2011: £52 million) driven by growth in both new business volumes and profitability. In **Poland**, operating profit reduced to £153 million (2011: £167 million) although on a local currency basis the overall result remained stable. In our remaining businesses, continued difficult economic conditions resulted in lower operating profits.

The life new business IRR in our continuing operations was 14.9% (2011: 14.5%), with an increase in the UK offsetting reductions in some European markets, in particular Spain and Poland.

The value of new business reduced to £746 million as a result of an increase in the UK offset by reductions in Europe.

General insurance and health

General insurance and health operating profit increased marginally to £893 million (2011: £935 million, excluding RAC; £860 million). This is due to good performances in both the UK and Canada driven by the continued progress we have made in underwriting, claims and cost management. The combined operating ratio was 97.0% (2011: 97.5%).

In the **UK**, general insurance profit levels improved by 3%, excluding RAC, and the combined operating ratio was stable at 98% (2011: 98% excluding RAC) despite an increase in weather-related claims of £31 million compared to long-term average and latent claims reserve strengthening of £53 million. Our performance in UK general insurance continues to benefit from our focus on underwriting excellence and active management of claims costs and expenses.

Our general insurance business in **Canada** delivered another strong performance with an improvement in the combined operating ratio to 93% (2011: 95%) and a 9% increase in operating profits to £276 million (2011: £254 million) as a result of favourable prior year

Our performance:

-  Narrow focus
-  Build financial strength
-  Improve performance



Increased net cash remittances from the businesses to Group to £0.9bn in 2012



Realised £275m annualised cost savings during 2012



Sold remaining shareholding in Delta Lloyd in January 2013

Operating capital generation and dividends paid to Group by business unit

2012 (£ million)			
Total by country	OCG	Dividend	% remitted to Group
UK Life*	662	150	23%
UK GI	341	150	44%
France	330	202	61%
Canada	190	136	72%
Poland	124	70	56%
Spain	78	68	87%
Singapore	35	17	49%
Italy	75	–	–
Ireland	52	–	–
Other**	72	151	–
Total	1,959	944	48%
Incremental UK life dividend*		150	
Overall total	1,094		

* a dividend expected from UK Life of £300 million will be paid in 2013
** includes Aviva Re, US and Delta Lloyd

developments, continued underwriting discipline and the use of predictive analytics.

Fund management

In a challenging investment environment Aviva Investors' operating profit on a continuing basis (which excludes the contribution from Aviva Investors in the USA) was £42 million (2011: £53 million) with lower performance fees partially offset by cost savings from the strategic review.

Investment performance was ahead of target on both benchmark and peer group measures. We maintained or improved client satisfaction, meeting or exceeding our targets on all client surveys in 2012. Net sales fell year-on-year as a result of the refocus of our product offering.

Capital generation and cash flows

At full year 2012 Aviva generated £2.0 billion of operating capital (2011: £2.1 billion) ahead of the target we set at the start of the year. Operating capital generation from the in-force life portfolio was £2.0 billion (2011: £2.3 billion) while general insurance contributed £0.6 billion (2011: £0.6 billion).

Operating capital generation levels were driven by strong performances in UK Life and Italy which offset the impact of reductions from the sale of Delta Lloyd and our US life and annuities business.

Aviva increased the amount of cash remittances from the businesses to Group to £0.9 billion in 2012 (2011: £0.8 billion). France resumed dividend payments to Group and management actions in UK Life led to a significant increase in cash remitted to Group.

The table shows operating capital generation and dividends paid to Group by business units.

We continue to take a number of actions on capital efficiency and our corporate structures to increase cash remittances going forward.

Changes to Aviva's capital structure

We are taking action to reduce the complexity of the balance sheet and reduce internal leverage. Prior to 2013 in the Group's corporate structure, ALL (Aviva Insurance Limited) was both the underwriting company for the UK General Insurance business and the holding company for the majority of the Group's overseas subsidiaries. Prior to 2013 an inter-divisional loan balance of around £5 billion was in place between the UK General Insurance business and the Group and this was used over a number of years to purchase overseas subsidiaries and for other general corporate purposes.

This structure was complex from a corporate governance point of view; created the potential for dividend traps and made demonstrating that Aviva has appropriate resolution arrangements in place (a key requirement of the PRA/FSA) more difficult. A more straightforward structure has now been put in place with two separate legal entities — Aviva Group Holdings Ltd (as holding company) and Aviva Insurance Limited (as the general insurance underwriting company). As a result of this change the inter-divisional balance between the Group and UK General Insurance will be formalised into an interest bearing loan of around £5.8 billion between AGH and ALL. We have decided to reduce the size of this loan balance and will pay down £600 million in total over the next three years.

As a result of this change, which the FSA are supportive of, our corporate structure will be more transparent, the Group will have direct ownership of overseas subsidiaries and the exposure of our UK general insurance business to these will be reduced over time.



Patrick Regan
Chief financial officer



Measuring our performance in 2012

In the following pages you can read more about our 2012 performance, business model and the context in which we operate.

Key performance indicators

Adjusted operating profit¹

- This measures our operating profitability and excludes non-operating items such as impairments, investment volatility and losses arising on disposals.

Total adjusted operating profit

- Adjusted operating profit before tax for 2012 was £2,127 million (2011: £2,503 million).
- Adjusted operating profit after restructuring costs was £1,659 million (2011: £2,235 million).

Adjusted operating profit on a continuing basis

- Operating profit on a continuing basis of £1,888 million was down 10% in 2012 (down 6% excluding RAC which we sold in 2011), mainly due to adverse foreign exchange movements. Operating profit on a constant currency basis, excluding Delta Lloyd and RAC, was stable reflecting slightly lower operating profits from our life business partly offset by a small increase in profits from our general insurance and health businesses.
- Operating profit on a continuing basis after restructuring costs was £1,427 million (2011: £1,828 million). This includes restructuring costs of £461 million (2011: £261 million) mainly driven by the transformation of the businesses, the integration of the Ireland and UK businesses and preparations for Solvency II.

IFRS loss after tax

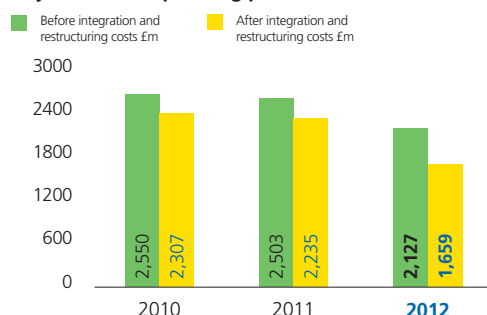
- This measures the total profit or loss during the year including operating profit and non-operating items such as investment variances, profit/loss from disposals and impairments.
- In 2012, the overall result was a loss after tax of £3,050 million (2011: £60 million profit).
- The largest driver of the overall loss was the agreed sale of our US business. At HY12 we recognised an impairment of goodwill and intangibles of £0.9 billion related to that business, and at the full year we recognised a further impairment of £2.4 billion.
- For continuing operations, the loss after tax was £202 million.

Life internal rate of return (IRR)

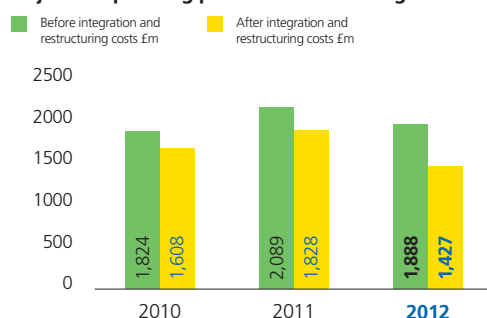
- We use IRR as a profitability measure of our life new business. We aim to achieve an internal rate of return in each of our life businesses of at least 13%.
- Our disciplined management of new business mix and focus on profit over volume have driven an improvement in our IRR to 14.9% (2011: 14.5%), (excluding US and Delta Lloyd), with an increase in the UK offsetting reductions in some European markets, in particular Spain and Poland.

Our performance

Adjusted total operating profit



Adjusted operating profit on a continuing basis



IFRS loss after tax £m

2012

£3,050m loss

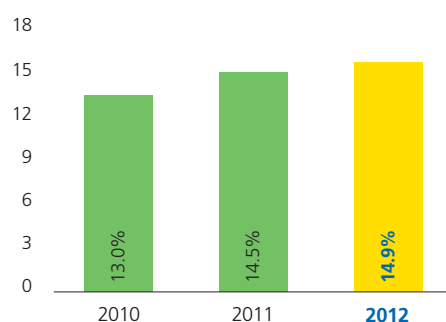
2011

£60m profit

2010

£1,892m profit

Life internal rate of return (IRR) %



¹ The Group's accounting policy for operating profit (also referred to as adjusted operating profit) remains consistent with prior periods and is set out in the basis of preparation.

Key performance indicators

General insurance combined operating ratio (COR)

- This is a standard industry metric used to measure the profitability of general insurance business. A percentage below 100% indicates that the general insurance business is being written at an underwriting profit.
- We aim to maintain a COR for the Group of 97% or better.
- Profitably in our general insurance business improved to 97% (2011: 98%) as we continue to benefit from our focus on underwriting excellence and active management of claims costs and expenses.

Economic capital surplus²

- This is an internal measure we use to calculate the financial strength of our business. A ratio of over 100% represents a surplus of available economic capital over our required economic capital.
- On 5 July 2012, we announced a new target economic capital range of 160-175% of required capital.
- On a pro forma basis, the estimated economic capital surplus improved to £7.1 billion as at 31 December 2012 (2011: £3.6 billion), with a coverage of 172% (2011: 130%). This positive movement is a result of improved market conditions and a range of management actions, including changes to our portfolio, such as the agreed sale of Aviva USA and transfer of Aseval to Bankia.

Net operating capital generation

- Operating capital generation measures the amount of surplus capital generated by our business and it supports our dividend to shareholders and our investment in new business.
- During 2012, Aviva generated £2.0 billion of net operating capital (2011: £2.1 billion) ahead of the target set at the start of the year.
- These levels include increases in UK Life and Italy, which offset the impact of reductions from the sale of Delta Lloyd, and a lower result from our US life and annuities business.
- Operating capital generation from the in-force life portfolio was £2.1 billion (2011: £2.3 billion) while non-life contributed £0.6 billion (2011: £0.6 billion), with £0.7 billion (2011: £0.8 billion) invested in new business.

Our performance

General insurance combined operating ratio %
(excluding Delta Lloyd and RAC)

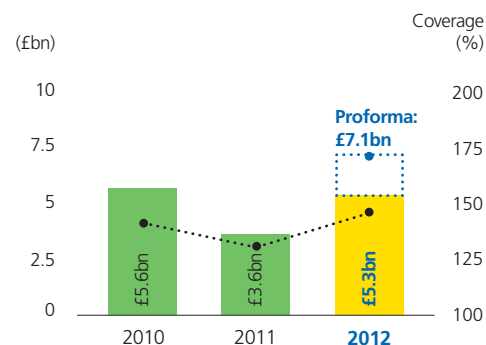
2012

97%

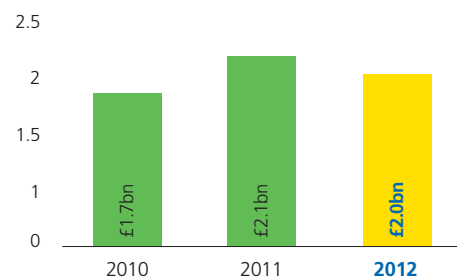
2011
98%

2010
98%

Economic capital surplus



Operating capital generation £bn



² The economic surplus represents an estimated unaudited position. The capital requirement is based on Aviva's own internal assessment and capital management policies. The term "economic capital" does not imply capital as required by regulators or other third parties. Pensions scheme risk is allowed for through ten years of stressed contributions.

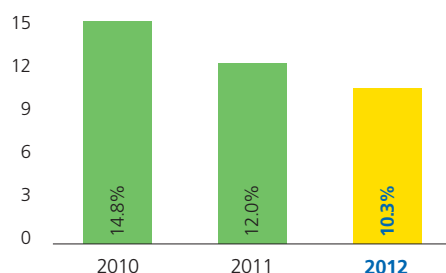
Key performance indicators

Return on equity shareholders' funds

- Return on equity shareholders' funds is calculated as total after-tax operating return, on opening equity shareholders' funds.
- In 2012, ROE was 10.3% (2011: 12.0%), driven by a reduction in our post-tax operating profit, which was due principally to the sale of RAC in 2011 and adverse foreign exchange movements.

Our performance

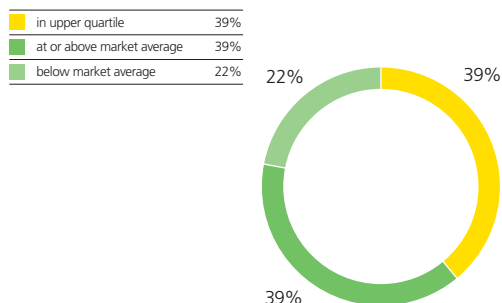
Return on equity shareholders' funds %



Customer advocacy

- Our Relationship Net Promoter Score® measures the likelihood of a customer recommending Aviva. It gives us a single, simple measure of customer experience which can drive improvements in customer loyalty.
- Our 2012 survey shows that the majority of our businesses are on par with, or better than, the market average for insurance companies globally.
- We are making continued progress and are committed to improving the performance across all our businesses.

Customer advocacy %



Employee engagement and leadership

- Employee engagement represents the degree to which people have a favourable opinion of Aviva as a place to work.
- We measure employees' views on Aviva through our annual global 'Employee Promise' survey and use the results to determine and implement actions with the aim of continuous improvement.
- Over time, our goal is to meet or exceed the global financial services benchmark norms.
- Despite the tough external environment and the levels of change within our business, engagement levels remained steady. This highlights our employees' commitment to Aviva.
- Given the extensive transformation and recent management changes at Aviva, it is not surprising that our independently assured ratings for senior leaders dropped to 61%. This is a significant concern which we are addressing through our cultures and values programme.

Employee engagement and leadership %



Developing communities



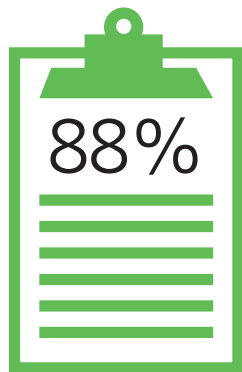
We contributed £11 million to communities in 2012, through volunteering and donations to organisations such as Railway Children, Save the Children and Oxfam. Our own community programme, Street to School, has helped more than 649,000 children across the world since 2009, exceeding our five year target in just three years.

Women in senior management



22% of our top 400 senior managers are women. Ensuring diversity throughout our business brings a more rounded perspective to our decision-making, risk management and leadership communications. We recognise that diversity takes many forms and we aspire to balanced leadership.

Business ethics



88% of our employees signed to say they had received, understood and accepted our Business Ethics code in 2012. We aim for 100%. The Corporate Responsibility Committee recognises that this is not good enough and we will focus on achieving our target in 2013.

Climate change and the environment



In 2012 we offset all of the CO₂ (or equivalent) emissions after minimising our environmental impact where possible. This means we are carbon neutral. We carefully source all of our carbon offset projects to ensure they also benefit community development. During 2012, we reduced emissions on a like for like basis by 12% compared to the previous year. 24% of the energy we use comes from renewable sources such as wave, wind and sun.

Volunteering hours



We believe a sustainable business is one that plays an active role in society. In 2012, our employees dedicated more than 56,000 hours to volunteering. There was also a 3% increase in the number of employees contributing through payroll giving.

Our business model

While insurance can appear to be a complicated business, the core of what we do is straightforward.

We are a well known **life, general insurance and asset management** business

- Aviva is the largest insurance company¹ in the UK
- In addition we have businesses in selected international markets including France, Canada, Poland and Singapore
- We have been in the insurance business for more than 300 years
- We have 31,200 employees² and 34 million customers

We provide:



Life insurance



General insurance



Asset management

We help **protect** customers from the **financial impact** of unforeseen events and help them **save** for a more **secure future**

- We provide a wide range of health insurance and general insurance products including motor and home
- We offer pensions, annuities, protection and savings products
- Our products are sold to individuals and businesses
- We sell products directly and through partners and third parties

Our products are sold through:



Direct – sales people and online



Independent vendors (IFAs, brokers)



Banks and other corporate partners

Managing risk and investments is fundamental to what we do and how we generate returns

- Customers pay insurance premiums which we use to pay claims; our scale enables us to pool the risks of many customers
- Customers invest their savings with us. We manage these investments to provide them with an income for a more secure future
- Making sure that customers stay with us for the long term is important to the future success of our business

Managing our business:



Underwrite risk



Administer funds



Aviva's brand attracts and retains customers and employees

Market context

Many social and economic factors will provide opportunities for the insurance and asset management industry. Here are some of them:

Customers across all our markets need to save more for a comfortable retirement

Growing pressure on Europe's pension systems caused by ageing populations is a widely acknowledged problem, with the ratio of retirees to workers set to increase. The Pension Gap report, produced by Aviva and Deloitte, shows the difference between the pension provision that people will need for an adequate standard of living in retirement and the pension amount they can currently expect to receive.

€1.9 trillion
pensions gap

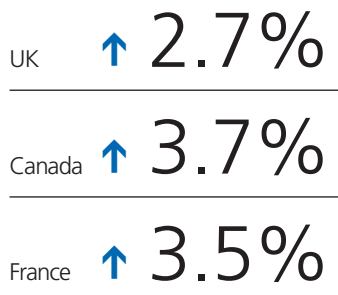
European citizens retiring in 2011–2051 would need to find an additional €1.9 trillion in savings every year to fully close the pensions gap

Source: www.aviva.com/europe-pensions-gap/; research conducted in 2010.

The non-life and protection market continues to grow

The market for general insurance, health insurance and protection continues to grow, despite the financial crisis. In an uncertain economic environment, consumers still buy insurance to protect the things that matter to them, such as their health, their homes and their cars.

Average annual growth in non-life premiums over five years



Source: Non-life premiums average annual growth (2006 – 2011) provided by Swiss Re; growth rates based on local currency.

Established and developing life insurance markets present significant opportunities

We operate in established insurance markets which provide opportunities for insurers to manage existing wealth, such as in the UK and France. We also operate in fast-growing, developing life insurance markets such as China, Poland and Turkey, which present opportunities for insurers to help customers accumulate assets.

Established markets

UK 2011
Life reserves (\$)

1.9trn

France 2011
Life reserves (\$)

1.8trn

Developing markets

China 2011
Life premiums (\$)

135bn

China 2006 – 2011
average annual growth

19% ↑

Poland 2011
Life premiums (\$)

9.2bn

Poland 2006 – 2011
average annual growth

9% ↑

Turkey 2011
Life premiums (\$)

1.6bn

Turkey 2006 – 2011
average annual growth

14% ↑

Source: FSA, FFSA; Swiss Re, growth rates based on local currency.

Market focus



David Barral
CEO UK & Ireland
life Insurance

“
In 2012, despite difficult economic conditions, we improved the profitability and capital efficiency of our business whilst maintaining a strong trading performance in our core products.

UK & Ireland life and pensions

- **UK operating profit £887m (2011: £917m)**
- **UK long-term sales, including investment sales, £12,140m (2011: £12,943m)**
- **UK life new business IRR 18% (2011: 15%)**

Aviva is the UK's leading life insurer. In the UK life business, operating profit was down 3% to £887 million although on an underlying basis this improved by 2% in the year. We improved our life new business IRR to 18% reflecting our focus on improving profitability and capital allocation.

This improvement was a result of the UK life business's focus on capital efficiency, including the withdrawal from large-scale bulk purchase annuities and other products, pricing actions on core products, cost savings and retention. This resulted in a 20% increase in operating capital generation to £662 million.

Despite difficult market conditions, long-term sales, excluding bulk purchase annuities, were up slightly at £11,953 million. This was driven by a strong performance in our core markets of "at retirement" (annuities and equity release) and protection where we grew sales respectively by 12% and 20%, which offset a reduction in bond sales. We continued to expand our distribution footprint, including an exclusive five year agreement with Tesco to distribute protection products.

Our health business performed strongly, with net written premiums up 12% at £528 million (2011: £473 million). We were voted Health Insurance Company of the Year for the third year in succession at the 2012 Health Insurance Awards.

Aviva has been campaigning for a long time to bring greater transparency to the annuity market to encourage customers to shop around on the open market to get the best annuity for their retirement. Aviva does not differentiate its pricing between internal and external customers, and we welcome the FSA's thematic review of annuities.

The UK industry is entering an uncertain period as an unprecedented level of regulatory change takes effect, including the Retail Distribution Review, Auto-Enrolment and Gender Directive. We are fully prepared and well-placed to benefit from the changes, with both a broad product range and extensive distribution network.

The integration of Aviva's Irish life business is progressing well, but Ireland remains a difficult market and profitability is not yet at acceptable levels. Ireland operating profit was down 89% at £5 million and sales were down 31% at £632 million due to the closure of our joint venture with AIB from 31 March 2012. Excluding this joint venture, operating profits were up 156% to £23 million and sales rose 9% to £530 million.



There in times of difficulty

When Tracy Harrison-Green's husband Andrew died suddenly aged just 43 an Aviva life insurance policy was a great help during a very difficult time. A £10 a month decreasing term policy that the couple took out when they married in 2003 automatically paid off their entire mortgage. Tracy, from York, says that buying the policy was the best financial decision she ever made. It meant that during a period of great personal tragedy, she didn't need to worry about finding the money to secure the roof over her head.



Robin Spencer
CEO, UK & Ireland
general insurance

“
Solid results in the UK, with satisfying progress being made to integrate and transform our Irish business.

UK & Ireland general insurance

- **UK general insurance operating profit of £448m (2011: £433m excluding RAC)**
- **UK combined operating ratio of 98% (2011: 98% excluding RAC)**
- **UK net written premiums of £4,062m (2011: £4,110m excluding RAC)**

Aviva is the leading general insurer in the UK. Although sales were lower, total like for like operating profit increased slightly, demonstrating our focus on disciplined underwriting to maintain profitability ahead of volumes. We delivered a UK general insurance COR of 98% despite the fact that 2012 was the second wettest year on record.

Our operating performance remains our number one priority, with an increasing focus on broker management, pricing analytics, cost control and capital allocation.

These results highlight the strength of our diversified portfolio and our risk selection, which has delivered good profitability in UK personal lines with combined operating ratios of 97% and 93% in motor and homeowner respectively. We have seen further modest growth in the UK motor market where we now have nearly 2.5 million customers. This represents an increase of more than 250,000 customers since the start of 2012 driven by the success of our Quotemehappy and multicar offerings. We are further developing our profitable homeowner business, assisted by a new partnership deal with insurance broker Gallagher Heath.

In UK commercial, the market remains challenging for brokers and customers, due to the ongoing economic conditions. We are focusing on improving our processes to ensure we provide commercial customers with insurance cover at an acceptable price and our shareholders with a good return on their capital.

We are focused on further improving our customer service. We have strengthened our underwriting disciplines and invested in pricing, risk selection and customer and broker facing systems. In 2012 customer advocacy scores improved as we achieved an 18 point improvement in our Relationship Net Promoter Score® and we reduced the number of complaints received by almost 30%. Brokers also recognised our excellent customer service by voting us Insurance Times General Insurer of the Year, for the second year running.

We continue to develop innovative insurance solutions such as 'Aviva Drive', a smartphone app which helps us to tailor insurance prices to customers' driving styles. We also launched 'Fast Track', an online trading platform which provides brokers with the facility to 'quote and buy' online in under five minutes.

During the year, we further restructured our Irish general insurance business to improve profitability. Additional actions to make further improvements continue in 2013.



An Olympic effort

When summer storms caused floods in the UK, Aviva was there to help. On two days of particularly bad weather in June we helped over 2,500 customers. Two weeks later, after more floods, we contacted customers who had previously claimed to see if they had suffered further damage and needed assistance. We helped the City of Newcastle Gymnastics Academy when they were completely devastated by floods, and lost almost every piece of Olympic training kit. Within 24 hours, our loss adjusters were on the scene and arranged a speedy interim payment. We also provided free cover at a temporary location to ensure the 800+ gymnasts could maintain their fitness levels.



David McMillan
CEO, Aviva Europe

“
Despite difficult economic conditions in continental Europe, the strength of our life insurance back book has allowed us to deliver a steady set of results.

Europe

France

- **Life operating profit £335m (2011: £323m) with new business IRR 11% (2011: 11%) and long-term savings sales £3,638m (2011: £4,047m)**
- **General insurance and health operating profit £95m (2011: £144m) with net written premiums of £1,002m (2011: £1,016m) and combined operating ratio of 95% (2011: 90%)**

Aviva France, the third-largest business in the Aviva Group, produced a solid performance with operating profit of £422 million (2011: £471 million).

Life operating profit increased, and, although sales were 4% lower on a local currency basis, we outperformed the individual life market, which fell 10% over the course of the year. Life new business IRR was flat.

General insurance sales rose by 6% on a local currency basis, due to an increase in both policy volumes and rates. Although general insurance profits were down compared to the previous year, the combined operating ratio remained strong at 95%.

Over the course of the year we increased our customer base to 3.2 million and received several awards for both our life and general insurance products.

Italy

- **Life operating profit £159m (2011: £140m) with new business IRR 12% (2011: 12%)**
- **Long-term savings sales £1,971m (2011: £2,993m)**
- **General insurance profit £20m (2011: loss of £35m) with NWP of £357m (2011: £416m) and COR of 100% (2011: 114%)**

Aviva Italy is the sixth-largest business in the Aviva Group. In 2012 operating profit increased despite a fall in GDP and market volatility. We have taken positive steps to maintain profitability putting in place various initiatives in our life and GI businesses which have improved our performance.

Life profitability improved due to our focus on products that are less capital intensive and the result has been a favourable change in our product mix.

General insurance profitability improved through pricing actions and disciplined claims management. General insurance sales were 8% lower than the previous year on a local currency basis.

Spain

- **Life operating profit £215m (2011: £216m)**
- **Life new business IRR of 21% (2011: 23%)**
- **Long-term savings sales of £1,295m (2011: £1,926m)**

Aviva Spain is the country's fifth largest long-term insurer by gross written premiums. We sell protection, long-term savings and pensions, health and accident insurance both directly and through bancassurance networks.

On a constant currency basis operating profit increased by 7%, while life and pensions sales have decreased by 28%. A substantial part of this reduction has been the result of management action focusing on the efficient use of capital. The business has focused on retaining highly profitable protection business, while developing capital efficient products, including unit linked savings. IRR remains strong at 21% (2011: 23%). In December, we reached a settlement with Bankia to transfer to them our entire holding in Aseval, a Spanish life insurance company.



Helping customers when disaster strikes

When two earthquakes struck the northern Italian region of Emilia Romagna in May forcing more than 45,000 people to leave their homes we were there to help. To make sure that all our customers were properly insured in difficult circumstances we extended the deadline for late payments on general insurance policies from 15 to 45 days and awarded late payment interest on life policies.

Market focus continued

Poland

- **Life operating profit £153m (2011: £167m)**
- **Life new business IRR 20% (2011: 24%)**
- **Long-term savings sales £373m (2011: £487m)**

Aviva is Poland's fourth largest life insurer. A combination of regulatory changes, adverse foreign exchange movements and the impact of the economic environment resulted in lower life insurance sales in 2012. Even so, we focused on becoming more efficient and our profitability in this market remained strong with an IRR of 20%.

We continued to improve our distribution and our bancassurance agreement with Santander provides us with a strong source of revenue so that we now have a 10% share of the individual life insurance market.

Turkey

In Turkey, our life and general insurance businesses generated an IFRS operating loss of £22 million (2011: £9 million loss). In life insurance we serve 2 million customers and are well positioned to benefit from our relationship with partner Akbank TAS, and their related banks, Citibank AS and Burgan Bank AS. Protection sales through our bancassurance channel were up by more than 50% compared to 2011.

Putting life insurance to work

Stomil Sanok, a Polish rubber products company, has over 1,700 employees and all of them are covered by Aviva's group life insurance. We have a service point on the company's premises where dedicated insurance advisors are available every day to assist employees with claims. Family benefits are a characteristic of life insurance contracts in Poland and when an employee has a baby Aviva representatives visit the family at home and work out which benefits they are entitled to.



Maurice Tulloch
President and CEO,
Aviva Canada

“
Our underwriting strength and commitment to our broker partners gives us a strong market position.

Canada

- **IFRS operating profit of £276m (2011: £254m)**
- **Combined operating ratio of 93% (2011: 95%)**
- **Net written premiums of £2,176m (2011: £2,083m)**

Aviva is Canada's second-largest general insurer. The business delivered a good financial result with a strong increase in profit. This performance was due to pricing sophistication, underwriting discipline, improved retention and strong underlying growth in new business. We also maintained a profitable mix of personal and commercial lines business.

We use predictive analytics to enhance our underwriting capabilities and further research and development is underway to enhance our pricing for weather-related perils.

The Canadian insurance business, unlike many other businesses in the Group is mostly intermediated; however we continue to address increasing customer demand for choice, simplicity and self-service by working with our brokers to help them compete with other channels.

Aviva Canada is committed to strong distribution relationships and maintained high satisfaction scores among its broker partners in 2012. Customer service has also improved further. Our claims Net Promoter Score® is +47, a strong result.

We delivered a strong underwriting result in personal lines due to our disciplined underwriting and lower claims frequency. Our efforts to transform and improve the profitability of the commercial lines business continued as we initiated actions to address underperforming segments.

Hurricane Sandy – looking after customers on both sides of the Atlantic

As those affected by Hurricane Sandy came to terms with its impact, our teams in Canada and the UK were busy making sure Aviva's customers got the help and support they needed. The teams worked together and took a proactive approach using the media, Aviva's websites and social media sites like Twitter and Facebook, to make sure customers had access to travel advice and assistance. Aviva also automatically extended customers' policies to give them 14 days' extra cover and peace of mind until they arrived home safely.



Khor Hock Seng
CEO, Aviva Asia

“
I am very much looking forward to working with our teams and partners to realise the potential of Aviva in Asia.

Asia

Singapore

- **Life operating profit £65m (2011: £52m)**
- **Life new business IRR 25% (2011: 31%)**
- **Long-term savings sales £817m (2011: £724m)**

Aviva is a top five life insurer in Singapore with over half a million customers, and one of the biggest providers of employee benefits and healthcare insurance. Long-term savings sales increased 28% on the previous year with bancassurance sales and sales of retirement products contributing significantly to this growth.

Our 11-year relationship with DBS, Singapore's largest bank, continues to go from strength to strength. Life operating profit and value of new business were up significantly on the previous year driven by strong protection sales and increased scale.

China

In China, bank interest rates remain high making our savings products less attractive. We have therefore shifted our focus towards the sale of protection products.

India

In India, despite regulatory changes creating uncertainty in the market, we extended our distribution agreement with Indusind Bank, India's leading private sector bank. We also launched an online sales portal for protection business. Online customers now account for 14% of new customers acquired and 4% of new business premium in India.

Making retirement planning simple

We know that many customers worry that planning for retirement might be complicated, so in 2012 Aviva's Singapore business launched a retirement plan specifically designed to be as simple as possible – it's called 'My Retirement'. All of the documentation is written in straightforward language and the product itself provides a capital guarantee, with guaranteed returns. It is designed to be simple, safe and sure.



Paul Abberley
Interim CEO, Aviva Investors

“
We have delivered a solid set of results in a challenging and competitive environment, with the business ahead of target on all key financial metrics.

Aviva Investors

- **Operating profit £42m (2011: £53m)**
- **Net funded external sales £1.7bn with a further £0.2bn of committed but unfunded sales (2011: £3.6bn)**
- **69% of institutional funds performed above benchmark (where a benchmark exists) with 68% of funds ahead of peer group**

In a challenging investment environment Aviva Investors' operating profit on a continuing basis (which excludes contribution from asset management activities undertaken for Aviva USA)

was £42 million (2011: £53 million) with lower performance fees partially offset by cost savings from the strategic review.

Investment performance was ahead of target on both benchmark and peer group measures. We maintained or improved client satisfaction, meeting or exceeding our targets on all client surveys in 2012. Net sales fell year-on-year as a result of the refocus of our product offering.

An integrated response to sustainability

As a long-term investor, Aviva Investors recognises the positive impact that embedding long-term sustainability into a business strategy can have on shareholder value. In 2012 Aviva Investors began to integrate the consideration of environmental, social and governance (ESG) issues on all the asset classes in which it invests. This includes appointing ESG champions on our investment desks.



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Performance review

In this section

Financial and operating performance	26
Selected consolidated financial data	40
Information on the company	41
Organisational structure	48
Analysis of investments	50
Contractual obligations	55
Risk and capital management	56
Basis of preparation	60

Financial and operating performance

Our main activities are the provision of products and services in relation to long-term insurance and savings, fund management and general insurance.

Factors affecting results of operations

Our financial results are affected, to some degree, by a number of external factors, including demographic trends, general economic and market conditions, government policy and legislation and exchange rate fluctuations. See 'Performance review – Risk and capital management' for more information on these and other risk factors. In addition, our financial results are affected by corporate actions taken by the Group, including acquisitions, disposals and other actions aimed at achieving our stated strategy. We believe that all of these factors will continue to affect our results in the future.

Group restructuring

During the year, the Group undertook the following actions which impacted the overall results and performance:

- The Group changed its organisational reporting structure, and the Group's operating segments were changed to align them with this revised structure. Further details of the reportable segments are given in 'Financial statements – note 4 – Segmental information'.
- The Group undertook restructuring and transformation activity to align our business operations with our strategy, including the Group's Simplify programme. Integration and restructuring costs of £468 million (2011: £268 million) include Simplify costs of £165 million, Ireland transformation costs (including the merger of the UK and Ireland businesses) of £130 million, £24 million in relation to the transformation of Aviva Investors, £30 million in respect of other restructuring activities and £119 million relating to the cost of preparing the businesses for the implementation of Solvency II.
- The Group also announced a number of disposals during the year, including the Group's US life and related internal asset management businesses ('US Life') which have been classified as discontinued operations for reporting of financial performance, and held for sale in the statement of financial position.

As a result of the held for sale classification, US Life has been written down to fair value less costs to sell which is the main driver for the loss from discontinued operations of £2,848 million and the Group's loss for the year of £3,050 million. Further details are given in 'Financial statements – note 3 – Subsidiaries'.

Demographic trends

Our results are affected by the demographic make-up of the countries in which we operate. The types of products that we sell reflect the needs of our customers. For example, in countries with a high proportion of older people, a larger proportion of our sales will reflect their needs for pre- and post-retirement planning. Our sales levels will also be impacted by our ability to help provide useful information to such policyholders on retirement planning and to offer products that are competitive and respond to such policyholders' needs.

In our long-term insurance and savings business we make assumptions about key non-economic factors, such as the mortality rate that we expect to be experienced by our policyholders. In countries where the life expectancy is growing, this will need to be reflected in our pricing models as lower mortality rates will increase profitability of life insurance products but will reduce the returns on annuity products. We review our assumptions against our own experience and industry expectations.

Economic conditions

Our results are affected by the economic conditions in our geographic markets and, consequently, by economic cycles in those markets. High levels of general economic activity typically result in high levels of demand for, and sales of, our products and services. Economic activity in turn is affected by government monetary and fiscal policy as well as by global trading conditions and external shocks such as terrorist activity, war and oil price movements.

During 2012, conditions remained challenging with continued concerns over levels of sovereign debt within the eurozone. Towards the year end, market sentiment started to improve which saw improvements in credit spreads. However, the challenging conditions in the economies of major European markets (including the UK) has led to lower demand for savings products. During 2011, concerns over slowing economic growth, higher levels of sovereign debt within, and to a lesser degree outside the eurozone, the stability and solvency of financial institutions, longer-term low interest rates in developed markets, inflationary threats as well as geopolitical issues contributed to increased volatility in the financial markets. The continued market volatility across global financial markets saw customers reassert their preference for less complex products and reduce their exposure to investment markets.

The European economies where the Group has operations were impacted in 2012 by forecast low or negative growth including: UK (-0.1%)¹; France (0.2%)¹; Spain (-1.3%)¹; and Italy (-2.2%)¹.

Capital and credit market conditions

An important part of our business involves investing client, policyholder and shareholder funds across a wide range of financial investments, including equities, fixed income securities and properties. Our results are sensitive to volatility in the market value of these investments, either directly because we bear some or all of the investment risk, or indirectly because we earn management fees for investments managed on behalf of policyholders. Investment market conditions also affect the demand for a substantial portion of our life insurance products. In general, rising equity price levels have a positive effect on the demand for equity-linked products, such as unit trusts and unit-linked life insurance products, and conversely have a negative effect on the demand for products offering fixed or guaranteed minimum rates of return. Declining equity price levels tend to have the opposite effects.

During 2012, the challenging conditions continued to impact the Group's performance. The total long-term business investment return variance was negative £278 million (2011: £1,616 million negative).

For continuing operations, negative long-term business investment variances of £620 million (2011: £897 million negative) mainly relates to the UK. This is mainly due to increasing the allowance for credit defaults on UK commercial mortgages to reflect uncertainty in the macro-economic environment, and the cost of de-risking activity. Elsewhere, positive variances in Spain and France were offset by a negative variance in Italy.

For 2011, the adverse life investment variances of £897 million related largely to the impact of lower risk-free interest rates, wider credit spreads and increased market volatility in the UK and Europe.

The positive variance of £342 million for discontinued operations relates to the US, driven by reductions in interest rates and credit spreads and the impact of favourable equity market performance on embedded derivatives. The prior period negative variance (2011: £719 million negative) includes the result for Delta Lloyd up to the partial disposal on 6 May 2011 of £820 million negative.

With-profits business

We write products through our with-profits funds mainly in our UK & Ireland operating segment, with a small fund in Singapore. These funds enable policyholders to participate in a large pool of diverse investments, therefore reducing their exposure to individual securities or asset classes. The investment pool is managed by us with returns to with-profits policyholders paid through bonuses which are added to the value of their policy. In order to provide an element of stability in the returns to policyholders, bonuses are designed to reduce policyholders' exposure to the volatility of investment returns over time and to provide an equitable share of surplus earned, depending on the investment and operating performance of the fund. Shareholders also have a participating interest in the with-profits funds and any declared bonuses. Generally, policyholder and shareholder participation in with-profits funds in the UK is split 90:10.

Shareholders' profits arising on with-profits business under IFRS depend on the total bonuses declared to policyholders on an annual basis.

The level of bonuses declared to policyholders is influenced by the actual returns on investments and our expectation of future rates of return. Whilst bonuses can never be negative, a predicted sustained fall in equity markets could lead to a reduction in regular and final bonus rates, thereby reducing both policyholder returns and shareholders' profit under IFRS. In 2011, low investment returns and the difficult economic outlook led to reductions in regular and final bonus rates. Better investment performance in 2012 meant that we have been able to increase the majority of final bonus rates.

General insurance and health underwriting cycle

Our general insurance and health business is comprised of our property and casualty insurance and health insurance operations. In 2012, general insurance and health sales accounted for 42% of Group net written premiums ("NWP") from continuing operations. Demand for general insurance is usually price-sensitive because of the limited degree of product differentiation inherent in the industry. As a result, the price of insuring property and casualty risks is subject to a cycle (called an underwriting cycle). In periods when the price of risk is high, the high profitability of selling insurance attracts new entrants and hence new capital into the market. Increased competition, however, drives prices down. Eventually the business becomes uneconomic and some industry players, suffering from losses, exit the market whilst others fail, resulting in lower capital invested within the market. Decreased competition leads to increasing prices, thereby repeating the cycle. Our various general insurance markets are not always at the same stage of the underwriting cycle.

In the UK, the personal motor market has seen rate reductions in 2012 reflecting intense competition and regulatory change. This follows a period of rate increases in previous periods in response to rising claims costs and frequencies. Challenging rating conditions also apply to other UK classes of business.

We expect the underwriting cycle to continue in the future but to be less pronounced than in the past because of structural changes to the industry over the past decade. Capital markets are imposing financial discipline by being increasingly more demanding about performance from insurance companies before extending new capital. Such discipline, together with the increased concentration of competitors within the market, recent natural disasters and the adoption of more advanced pricing methods, is expected to make the underwriting cycle less pronounced in the future.

Natural and man-made disasters

Our general insurance and health business results are affected by the amount of claims we need to pay out which, in turn, can be subject to significant volatility depending on many factors, including natural and man-made disasters. Natural disasters arise from adverse weather, earthquakes and other such natural phenomena. Man-made disasters include accidents and intentional events, such as acts of terrorism. These events are difficult to predict with a high degree of accuracy, although they generally occur infrequently at a material level. Our exposure to large disasters is somewhat reduced through our focus on personal lines business and small to medium sized commercial risks in the general insurance business. The Group cedes much of its worldwide catastrophe risk to third-party reinsurers but retains a pooled element for its own account gaining diversification benefit. See 'Financial statements IFRS – Note 56 – Risk management'.

In 2012, the UK and Ireland were impacted by flood losses and France by a severe freeze. In 2011, France and Ireland were impacted by storm and flood losses and Canada incurred losses from a wildfire in Slave Lake.

Government policy and legislation

Changes in government policy and legislation applicable to our business in many of the markets in which we operate, particularly in the UK, may affect the results of our operations. These include changes to the tax treatment of financial products and services, government pension arrangements and policies, the regulation of selling practices and the regulation of solvency standards. Such changes may affect our existing and future business by, for example, causing customers to cancel existing policies, requiring us to change our range of products and services, forcing us to redesign our technology, requiring us to retrain our staff or increase our tax liability. As a global business, we are exposed to various local political, regulatory and economic conditions, and business risks and challenges which may affect the demand for our products and services, the value of our investments portfolio and the credit quality of local counterparties. Our regulated business is subject to extensive regulatory supervision both in the UK and internationally. For details please refer to the section 'Shareholder information – Regulation'.

Exchange rate fluctuations

We publish our consolidated financial statements in pounds sterling. Due to our substantial non-UK operations, a significant portion of our operating earnings and net assets are denominated in currencies other than sterling, most notably the euro and the US dollar. As a consequence, our results are exposed to translation risk arising from fluctuations in the values of these currencies against sterling. Total foreign currency translation recognised in the income statement was a gain of £128 million (2011: £35 million loss).

We generally do not hedge foreign currency revenues, as we prefer to retain revenue locally in each business to support business growth, to meet local and regulatory market requirements and to maintain sufficient assets in local currency to match local currency liabilities.

Movements in exchange rates may affect the value of consolidated shareholders' equity, which is expressed in sterling. Exchange differences taken to other comprehensive income arise on the translation of the net investment in foreign subsidiaries, associates and joint ventures. This aspect of foreign exchange risk is monitored centrally against limits that we have set to control the extent to which capital deployment and capital requirements are not aligned. We use currency borrowings and derivatives when necessary to keep currency exposures within these predetermined limits, and to hedge specific foreign exchange risks when appropriate; for example, in any acquisition or disposal activity.

During 2012, sterling strengthened in value against the euro and marginally strengthened against the dollar, resulting in a foreign currency loss in other comprehensive income from continuing operations of £200 million (2011: £284 million loss).

The impact of these fluctuations is limited to a significant degree, however, by the fact that revenues, expenses, assets and liabilities within our non-UK operations are generally denominated in local currencies.

Acquisitions and disposals

Over the last two years we have completed and announced a number of transactions, some of which have had a material impact on our results. These transactions reflect our strategic objectives of narrowing our focus to businesses where we can produce attractive returns and exit businesses which we do not consider central to our future growth.

Activity in 2012

In March Aviva's distribution arrangement with Allied Irish Bank ("AIB") for long term business ceased and the bancassurance partnership with AIB is being unwound. A strategic review is underway to determine the most effective distribution channels going forward.

In July the Group sold 37.2 million shares in Delta Lloyd for £313 million (net of transaction costs), reducing our holding to 19.8% of Delta Lloyd's ordinary share capital, representing 18.6% of shareholder voting rights. As the Group no longer had significant influence over Delta Lloyd, we ceased to account for that company as an associate from 5 July 2012. Subsequent to the 2012 year end we disposed of our entire remaining holding.

In July, the Group sold its life businesses in the Czech Republic, Hungary and Romania to MetLife Inc., for £37 million. The sale of our Romania pensions business is still subject to regulatory approval and is expected to complete later in 2013.

In December we sold our controlling 58.4% interest in AVIVA NDB Holdings Lanka to a subsidiary of AIA group for a consideration of £31 million.

On 18 December we reached an agreement with Bankia S.A. to transfer our holding in our Spanish joint venture Aseval to Bankia for £494 million. The transfer is subject to regulatory approval and is expected to be completed no later than 30 April 2013. Due to the announced sale, Aseval has been treated as held for sale at the balance sheet date.

During the year the Group entered into negotiations to dispose of Aviva ZAO, its Russian long-term business subsidiary, and the requirements for that business to be classified as held for sale were met. The disposal of the business was announced in February 2013 for consideration of €35 million and is expected to complete in the first half of 2013.

In December 2012 the Group announced the disposal of its US life and related internal fund management business to Athene Holding Ltd for £1.0 billion, including the shareholder loan. The transaction is due to complete in 2013, subject to regulatory approvals. As a result of this announcement the results of the business for 2012 and comparative periods have been classified as a discontinued operation and it is held for sale at the balance sheet date.

Further details can be found in the section 'Financial statements IFRS – Note 3 – Subsidiaries'.

Subsequent events

In January 2013, we announced the sale of our 49% stake in CIMB Aviva Assurance Berhad and CIMB Aviva Takaful Berhad (together "CIMB-Aviva") to Sun Life Assurance Company of Canada for a consideration of £152 million. Further details can be found in 'Financial statements IFRS – Note 3c – Subsidiaries' and 'Financial statements – Note 18 – Interests in, and loans to, joint ventures'.

On 8 January 2013, we sold the remainder of our stake in Delta Lloyd at €12.65 per share resulting in total cash proceeds for Aviva of £353 million.

As noted above, on 27 February we announced the sale of our Russian Life business.

Activity in 2011

On 6 May 2011, the Group sold 25 million shares in Delta Lloyd reducing our holding to 42.7% (41.9% as at 31 December 2011) of Delta Lloyd's ordinary share capital, representing 40% (39.3% as at 31 December 2011) of shareholder voting rights. Accordingly, the Group ceased to consolidate the results of Delta Lloyd in its financial statements. Cash consideration of £380 million was received for the sale of shares, and £8 million of costs were attributable to the disposal transaction. The transaction resulted in the loss of control of a major geographical area of operations, previously presented as 'Delta Lloyd' in the segmental reporting note. The results of Delta Lloyd as a subsidiary for 2011 as well as those for the comparative periods were therefore classified as discontinued operations. The Group's share of the profits of its retained interest in Delta Lloyd as an associate are shown separately within continuing operations.

On 30 September 2011, the Group sold RAC Limited ("RAC") to The Carlyle Group for £977 million, realising a profit of £532 million. Aviva is continuing its commercial relationship with RAC, both as a key underwriter of motor insurance on RAC's panel and as a partner selling RAC breakdown cover to our customers. The Group has retained the RAC (2003) Pension Scheme which, at 31 December 2011, had an IAS 19 deficit of £51 million.

On 1 October 2011, the Group sold its Australian fund management business, Aviva Investors Australia Ltd, to nabInvest, National Australia Bank's direct asset management business, for £35 million, which included contingent consideration with a fair value of £3 million. This resulted in a profit on disposal of £20 million, increased to £23 million after recycling £3 million from currency translation reserve to the income statement.

Basis of earnings by line of business

Our earnings originate from three main lines of business: our long-term insurance and savings business, which includes a range of life insurance and savings products; general insurance and health, which focuses on personal and commercial lines; and fund management, which manages funds on behalf of our long-term insurance and general insurance businesses, external institutions, pension funds and retail clients. These lines of business are present in our various operating segments to a greater or lesser extent.

In the UK, we have major long-term insurance and savings businesses and general insurance businesses; in Europe we have long-term insurance and savings businesses in all countries in which we operate, large general insurance businesses in France, Ireland and Italy, and smaller general insurance operations in several other countries; in Canada we have a leading general insurance operation; in Asia we predominantly have long-term insurance and savings businesses. Our fund management businesses operate across Europe, Asia, North America and the UK.

Long-term insurance and savings business

For most of our life insurance businesses, such as those in the UK and France, operating earnings are generated principally from our in-force books of business. Our in-force books consist of business written in prior years and on which we continue to generate profits for shareholders. Nevertheless new business written in these markets, with the exception of our UK with-profits business which is discussed below, has a significant direct effect on our operating earnings. Under IFRS, certain costs incurred in acquiring new business must be expensed thereby typically giving rise to a loss in the period of acquisition, though the degree of this effect will depend on the pricing structure of product offerings. In certain higher growth markets, current year sales have a more significant effect on current year operating earnings.

UK with-profits business

With-profits products are designed to pay policyholders smoother investment returns through a combination of regular bonuses and final bonuses. Shareholders' profit emerges from this business in direct proportion to policyholder bonuses, as shareholders receive up to one-ninth of the value of each year's bonus declaration to policyholders. Accordingly, the smoothing inherent in the bonus declarations provides for relatively stable annual shareholders' profit from this business. The most significant factors that influence the determination of bonus rates are the return on the investments of the with-profits funds and expectations about future investment returns. Actual and expected investment returns are affected by, among other factors, the mix of investments supporting the with-profits fund, which in turn is influenced by the extent of the inherited estate within the with-profits fund.

The annual excess of premiums and investment return over operating expenses, benefit provisions and claims payments within our with-profits funds that are not distributed as bonuses and related shareholders' profit is transferred from the income statement to the unallocated divisible surplus. Conversely, if a shortfall arises one year, for example because of insufficient investment return, a transfer out of the unallocated divisible surplus finances bonus declarations and related shareholders' profit.

The unallocated divisible surplus consists of future (as yet undetermined) policyholder benefits, associated shareholders' profit and the orphan estate. The orphan estate serves as working capital for our with-profits funds. It affords the with-profits fund a degree of freedom to invest a substantial portion of the funds' assets in investments yielding higher returns than might otherwise be obtainable without being constrained by the need to absorb the cash-flow strain of writing large volumes of new business and the need to demonstrate solvency.

Other participating business

Outside of the UK, most of our long-term operations write participating business. This is predominantly savings or pensions business, where the policyholders receive guaranteed minimum investment returns, and additional earnings are shared between policyholders and shareholders in accordance with local regulatory and policy conditions. This may also be referred to as 'with-profits' business.

Other long-term insurance and savings business

Non-profit business falls into two categories: investment type business and risk cover and annuity business. Investment type business, which accounts for most of our non-profit business, includes predominantly unit-linked life and pensions business where the risk of investing policy assets is borne entirely by the policyholder. In addition, investment type business includes life and pensions business where the risk of investing policy assets is typically shared between policyholders and shareholders, subject to a minimum rate of investment return guaranteed to policyholders. Operating earnings arise from unit-linked business when fees charged to policyholders based on the value of the policy assets exceed costs of acquiring new business and administration costs. In respect of remaining investment type business, investment return generated from policy assets has an effect on operating earnings though this is often non-proportional. Finally, in respect of all investment type business, shareholders bear the risk of investing shareholder capital in support of these operations.

Risk cover business includes term assurance, or term life insurance business. Annuity business includes immediate annuities purchased for individuals or on a bulk purchase basis for groups of people. The risk of investing policy assets in this business is borne entirely by the shareholders. Operating earnings arise when premiums, and investment return earned on assets supporting insurance liabilities and shareholder capital, exceed claims and benefit costs, costs of acquiring new business and administration costs.

General insurance and health business

Operating earnings within our general insurance and health business arise when premiums and investment return earned on assets supporting insurance liabilities and shareholder capital exceed claims costs, costs of acquiring new business and administration costs.

Fund management

Fund management operating earnings consist of fees earned for managing policyholder funds and external retail and institutional funds on behalf of clients, net of operating expenses.

Arrangements for the management of proprietary funds are conducted on an arm's length basis between our fund management and insurance businesses. Such arrangements exist mainly in the UK, France, Ireland, and Canada. Proprietary insurance funds in other countries are externally managed.

Other business

Other business includes our operations other than insurance and fund management, including Group Centre expenses. In 2011 this also included the RAC roadside recovery operation in the UK up to its sale on 30 September 2011.

Financial highlights

The following analysis is based on our consolidated financial statements and should be read in conjunction with those statements. In order to fully explain the performance of our business, we discuss and analyse the results of our business in terms of certain financial measures which are based on 'non-GAAP measures' and which we use for internal monitoring and for executive remuneration purposes. We review these in addition to GAAP measures, such as profit before and after tax.

The remainder of the financial performance section focuses on the activity of the Group's continuing operations. Details of the performance of the United States which has been classified as discontinued can be found in the market performance section.

Non-GAAP measures**Sales**

The total sales of the Group consist of long-term insurance and savings new business sales and general insurance and health net written premiums.

Long-term insurance and savings new business sales

Sales of the long-term insurance and savings business consist of:

- Insurance and participating investment business
 - This includes traditional life insurance, annuity business and with-profits business.
 - There is an element of insurance risk borne by the Group therefore, under IFRS, these are reported within net written premiums.
- Non-participating investment business
 - This includes unit-linked business and pensions business.
 - The amounts received for this business are treated as deposits under IFRS and an investment management fee is earned on the funds deposited.
 - For new business reporting in the UK, companies continue to report non-participating investment business within their 'covered business' sales, in line with the historic treatment under UK GAAP.
- Non-covered business or investment sales:
 - These include retail sales of mutual fund type products.
 - There is no insurance risk borne by the Group therefore, under IFRS, these are treated as deposits and investment management fee income is earned on the funds deposited. These have never been treated as 'covered business' for long-term insurance and savings reporting so we show these separately as investment sales.

Sales is a non-GAAP financial measure and key performance indicator that we report to our key decision makers in the businesses in order to assess the value of new business from our customers and compare performance across the markets in which we operate. We consider sales to be a critical indicator of new business, and is the basis on which we provide analysis of our results to our shareholders and analysts. The non-GAAP measure of sales is also currently used internally in the determination of bonus awards as an executive performance measure.

For long-term insurance and savings new business, we define sales as the sum of the present value of new business premiums (PVNBP) of life, pension and savings products and investment sales.

PVNBP is equal to total single premium sales received in the year plus the discounted value of annual premiums expected to be received over the terms of newly incepted contracts and is calculated as at the date of sale. We adjust annual premiums to reflect the expected stream of business coming from this new business over future years. In the view of management, this performance measure better recognises the relative economic value of regular premium contracts compared with single premium contracts. PVNBP is a European insurance industry standard measure of new business.

For our long-term insurance and savings business, we believe that sales is an important measure of underlying performance and a better measure for new business than IFRS net written premiums. We consider that the use of sales over IFRS net written premiums provides a:

- Consistent treatment of long-term insurance and investment contracts: IFRS net written premiums do not include deposits received on non-participating investment contracts. Long-term insurance contracts and participating investment contracts both contain a deposit component, which are included in IFRS net written premiums, in addition to an insurance risk component. Therefore, to assess the revenue generated on a consistent basis between types of contracts, we evaluate the present value of new business sales of long-term insurance and investment products on the basis of total premiums and deposits collected, including sales of mutual fund type products such as unit trusts and Open ended investment companies (OEICs).
- Better reflection of the relative economic value of regular premium contracts compared to single premium contracts: Sales recognise the economic value of all expected contractual cash flows for regular premium contracts in the year of inception, whereas IFRS net written premiums only recognise premiums received in the year.
- Better reflection of current management actions in the year: IFRS net written premiums include premiums on regular premium contracts which incepted in prior years, and therefore reflect the actions of management in prior years.

In comparison with IFRS net written premiums, sales do not include premiums received from contracts in-force at the beginning of the year, even though these are a source of IFRS revenue, as these have already been recognised as sales in the year of inception of the contract. In addition, unlike IFRS net written premiums, sales do not reflect the effect on premiums of any increase or decrease in persistency of regular premium contracts compared with what was assumed at the inception of the contract.

PVNBP is not a substitute for net written premiums as determined in accordance with IFRS. Our definition of sales may differ from similar measures used by other companies, and may change over time.

General insurance and health sales

General insurance and health sales are defined as IFRS net written premiums, which are premiums written during the year net of amounts reinsured with third parties. For sales reporting, we use the GAAP measure for general insurance and health business.

The table below presents our consolidated sales for the three years ended 31 December 2012, 2011 and 2010 for our continuing operations, as well as the reconciliation of sales to net written premiums in IFRS.

	2012 £m	2011 £m	2010 £m
Continuing operations			
Long-term insurance and savings new business sales	25,232	27,461	28,839
General insurance and health sales	8,894	9,162	8,522
Total sales	34,126	36,623	37,361
Less: Effect of capitalisation factor on regular premium long-term business	(5,935)	(6,079)	(5,482)
Share of long-term new business sales from JVs and associates	(592)	(604)	(1,446)
Annualisation impact of regular premium long-term business	(239)	(533)	(357)
Deposits taken on non-participating investment contracts and equity release contracts	(4,607)	(4,573)	(3,795)
Retail sales of mutual fund type products (investment sales)	(4,586)	(3,473)	(3,387)
Add: IFRS gross written premiums from existing long-term business	3,936	4,305	3,547
Less: long-term insurance and savings business premiums ceded to reinsurers	(930)	(959)	(855)
Total IFRS net written premiums	21,173	24,707	25,586
Analysed as:			
Long-term insurance and savings net written premiums	12,279	15,545	17,064
General insurance and health net written premiums	8,894	9,162	8,522
	21,173	24,707	25,586

■ **Effect of capitalisation factor on regular premium long-term business**

PVNBP is derived from the single and regular premiums of the products sold during the financial period and is expressed at the point of sale. The PVNBP calculation is equal to total single premium sales received in the year plus the discounted value of regular premiums expected to be received over the term of the new contracts. The discounted value of regular premiums is calculated using the market consistent embedded value methodology proposed by the CFO Forum Principles.

The discounted value reflects the expected income streams over the life of the contract, adjusted for expected levels of persistency, discounted back to present value. The discounted value can also be expressed as annualised regular premiums multiplied by a weighted average capitalisation factor (WACF). The WACF varies over time depending on the mix of new products sold, the average outstanding term of the new contracts and the projection assumptions.

■ **Share of long-term new business sales from joint ventures and associates**

Total long-term new business sales include our share of sales from joint ventures and associates. Under IFRS reporting, premiums from these sales are excluded from our consolidated accounts, with only our share of profits or losses from such businesses being brought into the income statement separately.

■ **Annualisation impact of regular premium long-term business**

As noted above, the calculation of PVNBP includes annualised regular premiums. The impact of this annualisation is removed in order to reconcile the non-GAAP new business sales to IFRS premiums and will vary depending on the volume of regular premium sales during the year.

■ Deposits taken on non-participating investment contracts and equity release contracts

Under IFRS, non-participating investment contracts are recognised in the Statement of Financial position by recording the cash received as a deposit and an associated liability and are not recorded as premiums received in the Income Statement. Only the margin earned is recognised in the Income Statement.

■ Retail sales of mutual fund type products (investment sales)

Investment sales included in the total sales number represent the cash inflows received from customers to invest in mutual fund type products such as unit trusts and OEICs. We earn fees on the investment and management of these funds which are recorded separately in the IFRS income statement as 'fees and commissions received' and are not included in statutory premiums.

■ IFRS gross written premiums from existing long-term business

The non-GAAP measure of long-term and savings sales focuses on new business written in the year under review whilst the IFRS income statement includes premiums received from all business, both new and existing.

Adjusted operating profit

We report to our chief operating decision makers in the businesses the results of our operating segments using a financial performance measure we refer to as 'adjusted operating profit'. We define our segment adjusted operating profit as profit before income taxes and non-controlling interests in earnings, excluding the following items: investment return variances and economic assumption changes on long-term and non-long-term business, impairment of goodwill, joint ventures and associates, amortisation and impairment of other intangibles (excluding the acquired value of in-force business), profit or loss on the disposal and remeasurement of subsidiaries and associates, integration and restructuring costs and exceptional items.

Whilst these excluded items are significant components in understanding and assessing our consolidated financial performance, we believe that the presentation of adjusted operating profit enhances the understanding and comparability of the underlying performance of our segments by highlighting net income attributable to on-going segment operations.

Adjusted operating profit for long-term insurance and savings business is based on expected investment returns on financial investments backing shareholder and policyholder funds over the period, with consistent allowance for the corresponding expected movements in liabilities. The expected rate of return is determined using consistent assumptions between operations, having regard to local economic and market forecasts of investment return and asset classification. Where assets are classified as fair value through profit and loss, expected return is based on the same assumptions used under embedded value principles for fixed income securities, equities and properties. Where fixed interest securities are classified as available for sale, such as in the US, the expected return comprises interest or dividend payments and amortisation of the premium or discount at purchase. Adjusted operating profit includes the effect of variances in experience for non-economic items, such as mortality, persistency and expenses, and the effect of changes in non-economic assumptions. Changes due to economic items, such as market value movement and interest rate changes, which give rise to variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are disclosed as non-operating items.

Adjusted operating profit for non-long-term insurance business is based on expected investment returns on financial investments backing shareholder funds over the period. Expected investment returns are calculated for equities and properties by multiplying the opening market value of the investments, adjusted for sales and purchases during the year, by the longer-term rate of return. This rate of return is the same as that applied for the long-term business expected returns. The longer-term return for other investments is the actual income receivable for the period. Changes due to market value movement and interest rate changes, which give rise to variances between actual and expected investment returns, are disclosed as non-operating items. The impact of changes in the discount rate applied to claims provisions is also treated outside adjusted operating profit.

Adjusted operating profit is not a substitute for profit before income taxes and non-controlling interests in earnings or net income as determined in accordance with IFRS. Our definition of adjusted operating profit may differ from similar measures used by other companies, and may change over time.

The table below presents our consolidated adjusted operating profit for the three years ended 31 December 2012, 2011 and 2010, as well as the reconciliation of adjusted operating profit to loss/profit before tax attributable to shareholders' profits under IFRS.

	2012 £m	2011 £m	2010 £m
Continuing operations			
United Kingdom & Ireland	1,340	1,509	1,478
France	422	471	362
Canada	276	254	229
Italy, Spain and Other	414	334	400
Higher growth markets	202	229	170
Aviva Investors	42	53	63
Other Group Activities	(920)	(918)	(878)
Adjusted operating profit before tax (excl Delta Lloyd as an associate)	1,776	1,932	1,824
Share of Delta Lloyd's operating profit (before tax) as an associate	112	157	—
Adjusted operating profit before tax	1,888	2,089	1,824
Integration and restructuring costs	(461)	(261)	(216)
Adjusted operating profit before tax after integration and restructuring costs	1,427	1,828	1,608
Adjusting items:			
Investment return variances and economic assumption changes on long-term business	(620)	(897)	(229)
Short-term fluctuation in return on investments on non-long-term business	7	(266)	(199)
Economic assumption changes on general insurance and health business	(21)	(90)	(61)
Impairment of goodwill, associates and joint ventures and other amounts expensed	(60)	(392)	(23)
Amortisation and impairment of intangibles	(128)	(116)	(139)
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	(164)	565	163
Exceptional items	—	(57)	276
Share of Delta Lloyd's non-operating items (before tax) as an associate	(523)	10	—
Share of Delta Lloyd's tax expense, as an associate	107	(34)	—
Profit before tax attributable to shareholders' profits – continuing operations	25	551	1,396
(Loss)/profit before tax attributable to shareholders' profits – discontinued operations	(2,696)	(464)	1,044
(Loss)/Profit before tax attributable to shareholders' profits	(2,671)	87	2,440

Adjusting items (from continuing operations)

Year ended 31 December 2012

The negative investment return variances and economic assumption changes of £620 million (2011: £897 million negative) mainly relates to the UK, where the allowance for credit defaults on UK commercial mortgages has increased to reflect uncertainty in the macroeconomic environment and the cost of de-risking activity. Elsewhere, positive variances in Spain and France were offset by a negative variance in Italy.

Short term fluctuations and economic assumption changes on non-long term business of £7 million positive (2011: £266 million negative) reflected favourable market movements.

The impairment of goodwill, associates and joint ventures was £60 million in 2012 (2011: £392 million). This includes an impairment of £147 million in respect of the Group's Indian associate, an impairment of £76 million in relation to goodwill on the Spanish business, an impairment of £33 million in relation to the Italian business and a small write down of £9 million in respect of the Group's Korean joint venture. These impairments were partly offset by a reversal of the impairment recognised in 2011 in respect of our associate investment in Delta Lloyd of £205 million.

Loss on disposal of subsidiaries and associates was £164 million (2011: £565 million profit). This includes a loss of £129 million relating to the disposal of our associate stake in Delta Lloyd.

Integration and restructuring costs are £461 million (2011: £261 million). This includes costs relating to restructuring and transformation activity that has been taken to align our business operations with our strategy, including the Group's Simplify programme (£165 million), £130 million in Ireland which includes expenses associated with the merging of the UK and Irish business, £24 million for restructuring in Aviva Investors, £25 million in respect of restructuring activities and £117 million relating to preparing the businesses for the implementation of Solvency II.

Exceptional items in 2012 were £nil (2011: £57 million unfavourable).

Year ended 31 December 2011

The investment return variances and economic assumption changes on long-term insurance business in 2011 produced a £897 million charge (2010: £229 million charge). The short-term fluctuations and economic assumption changes on the non-life business produced a £266 million charge (2010: £199 million charge). This was due to unfavourable market movements in a number of our markets.

The impairment of goodwill, associates and joint ventures was £392 million in 2011 (2010: £23 million). An impairment of £217 million was recognised in respect of the associate, Delta Lloyd. The fair value was calculated based on the market price of the ordinary shares of Delta Lloyd NV quoted on the NYSE Euronext Amsterdam as at 31 December 2011. Following the announcement of the termination of Aviva Ireland's bancassurance distribution contract, management reviewed the recoverability of the goodwill associated with this business and an impairment loss of £120 million was recognised, reducing the carrying value of goodwill relating to this business to nil. The UK long-term business had an impairment of £29 million. In Italy, an impairment of £11 million was recognised in respect of Aviva Assicurazioni Vita Spa, as a result of a reduction in management's estimates for the future profitability of the business due to current economic circumstances. There was an impairment charge of £15 million recognised in respect of goodwill within interests in joint ventures relating to South Korea.

Amortisation of intangibles decreased by £23 million, or 17%, to £116 million (2010: £139 million).

Profit on disposal of subsidiaries and associates was £565 million (2010: £163 million). The profit comprised principally of a £532 million profit in relation to the sale of RAC, as described in note 3 to the IFRS financial statements.

Integration and restructuring costs for 2011 were £261 million (2010: £216 million). This includes costs associated with preparing the businesses for Solvency II implementation of £96 million, a £30 million charge in the UK relating to the reattribution of the inherited estate and expenditure relating to the Quantum Leap project (the Group's previous European restructuring program) in Europe of £51 million. Expenditure relating to other restructuring exercises across the Group amounted to £84 million.

Exceptional items in 2011 were £57 million unfavourable (2010: £276 million favourable) relating to a £22 million provision for compensation scheme costs for the leveraged property fund in Ireland, and a £35 million expense for the discounted cost of strengthening latent claims provisions in the UK written a significant number of years ago. In 2010, exceptional items mainly related to a £286 million benefit from the closure of the final salary section of the UK staff pension scheme.

Consolidated results of operations

The table below presents our consolidated sales from continuing operations for the three years ended 31 December 2012, 2011 and 2010.

Continuing operations	2012 £m	2011 £m	2010 £m
United Kingdom & Ireland	17,790	19,175	17,458
France	4,640	5,063	5,886
Canada	2,176	2,083	1,958
Italy, Spain and Other	3,849	5,665	7,484
Higher growth markets	2,944	3,039	2,959
Aviva Investors	2,727	1,598	1,616
Total sales	34,126	36,623	37,361

Sales (from continuing operations)

Year ended 31 December 2012

Total sales from continuing operations decreased £2,497 million or 7% to £34,126 million (2011: £36,623 million). This decrease was mainly driven by lower life and pension sales in the UK, Italy, and Spain, partly offset by higher investment sales.

Sales in the UK and Ireland decreased for long-term insurance and savings, by £1,088 million, or 8%, to £12,772 million (2011: £13,860 million). The decline in UK sales reflects lower sales of bulk purchase annuities following our decision to withdraw from this market, as well as falls in bonds and savings products. These were partly offset by increased sales of individual annuities and protection products. In Ireland, life sales are down due to the closure to new business of our joint venture with AIB from April 2012. General insurance and health sales decreased by £297 million, or 6%, to £5,018 million (2011: £5,315 million) mainly as a result of the disposal of RAC in 2011. Results across Europe have also been adversely impacted by the weakness of the euro and zloty. In our European operations, long term sales in France decreased £409 million, or 10% (4% decrease on a local currency basis), to £3,638 million (2011: £4,047 million) due to lower sales in the AFER (Association Francaise d'Epargne et de Retraite) product. Sales in Italy, Spain and Other decreased by £1,756 million, or 34% (29% decrease on a local currency basis) to £3,425 million (2011: £5,181 million) reflecting lower sales of protection and savings products due to the challenging economic environment. General insurance and health sales in France decreased by £14 million, or 1%, to £1,002 million (2011: £1,016 million) whilst sales in Italy and Other were down £60 million, or 12%, to £424 million (2011: £484 million) primarily due to declining credit protection and motor sales. Sales in Canada increased by £93 million, or 4%, to £2,176 million (2011: £2,083 million) due to a combination of improved retention levels and rate increases across both personal and commercial lines. Total sales in Higher growth markets decreased by £95 million, or 3%, to £2,944 million (2011: £3,039 million) with higher long-term sales in Singapore more than offset by lower sales in other markets. Aviva Investors sales increased by £1,129 million or 71%. The opening of distribution offices in Europe contributed to most of this growth.

Year ended 31 December 2011

Sales in 2011 were £36,623 million, a decrease of £738 million, or 2%, from £37,361 million in 2010. Sales in the UK and Ireland for long-term insurance and savings were £13,860 million, an increase of £1,337 million, or 11%, from £12,523 million in 2010 and general insurance and health was £5,315 million, an increase of £380 million, or 8%, from £4,935 million in 2010. Long term sales in France decreased by £871 million, or 18% to £4,047

million (2010: £4,918 million) and Italy, Spain and other decreased by £1,865 million, or 26%, to £5,181 million (2010: £7,046 million). The decrease in sales in France and Italy was primarily driven by management actions to reduce sales of participating business. Sales in France for general insurance and health increased by £48 million, or 5%, to £1,016 million (2010: £968 million) while sales in Italy and other increased £46 million or 11% to £484 million (2011: £438 million). General insurance sales in Canada increased by £125 million, or 6%, to £2,083 million (2010: £1,958 million). Total sales in Higher Growth markets increased £80 million, or 3%, to £3,039 million (2010: £2,961 million) due to higher life and pension sales from bancassurance channels in Asia.

The table below presents our consolidated income statement from continuing operations under IFRS for the three years ended 31 December 2012, 2011 and 2010, before the effects of taxation to shareholder profit.

Continuing operations	2012 £m	Restated ¹ 2011 £m	Restated ¹ 2010 £m
Income			
Gross written premiums	22,744	26,255	27,192
Premiums ceded to reinsurers	(1,571)	(1,548)	(1,606)
Premiums written net of reinsurance	21,173	24,707	25,586
Net change in provision for unearned premiums	(16)	(236)	(72)
Net earned premiums	21,157	24,471	25,514
Fee and commission income	1,273	1,465	1,451
Net investment income	21,106	4,341	16,746
Share of (loss)/profit of joint ventures and associates	(277)	(123)	141
(Loss)/profit on the disposal and re-measurement of subsidiaries and associates	(164)	565	163
	43,095	30,719	44,015
Expenses			
Claims and benefits paid, net of recoveries from reinsurers	(23,601)	(24,380)	(22,240)
Change in insurance liabilities, net of reinsurance	(430)	(2,284)	(2,837)
Change in investment contract provisions	(4,450)	1,478	(9,212)
Change in unallocated divisible surplus	(6,316)	2,721	362
Fee and commission expense	(4,472)	(4,326)	(5,500)
Other expenses	(2,845)	(2,779)	(2,116)
Finance costs	(735)	(776)	(682)
	(42,849)	(30,346)	(42,225)
Profit before tax	246	373	1,790
Tax attributable to policyholders' returns	(221)	178	(394)
Profit before tax attributable to shareholders' profits	25	551	1,396

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

Income (from continuing operations)

Year ended 31 December 2012

Net written premiums for continuing operations decreased by £3,534 million, or 14%, to £21,173 million (2011: £24,707 million). Long-term insurance and savings decreased by £3,266 million, or 21%, to £12,279 million (2011: £15,545 million) mainly reflecting lower sales in the UK and continental Europe. General and health insurance decreased by £268 million, or 3%, to £8,894 million (2011: £9,162 million). Excluding RAC in 2011, sales were broadly in line.

Year ended 31 December 2011

Net written premiums in 2011 were £24,707 million, a decrease of £879 million, or 3% (2010: £25,586 million). Long-term insurance and savings were £15,545 million, a decrease of £1,519 million, or 9% (2010: £17,064 million), driven by lower sales in Ireland, France and Italy. General and health insurance was £9,162 million, an increase of £640 million, or 8% (2010: £8,522 million), with growth primarily in the UK, France and Canada.

Net investment income (from continuing operations)

Year ended 31 December 2012

Net investment income for the year increased by £16,765 million, or 386%, to £21,106 million (2011: £4,341 million) reflecting

positive market performance and narrowing credit spreads on assets as market sentiment improved in the Eurozone. This led to significant increases in net unrealised gains on investments.

Year ended 31 December 2011

Net investment income was £4,341 million, a decrease of £12,405 million, or 74% (2010: £16,746 million). Investment returns were impacted by market volatility in 2011 resulting in higher unrealised losses on investments.

Other income (from continuing operations)

Year ended 31 December 2012

Other income, which consists of fee and commission income, share of loss after tax of joint ventures and associates, and (loss)/profit on disposal of subsidiaries and associates, decreased by £1,075 million, or 56%, to £832 million in 2012 (2011: £1,907 million). 2011 benefited from the profit on disposal of RAC (£532 million), whilst 2012 has seen a loss on disposal of our associate stake in Delta Lloyd, lower fee and commission income and higher losses from our share of JV's and associates.

Year ended 31 December 2011

Other income increased by £152 million, or 9%, to £1,907 million in 2011 (2010: £1,755 million). The increase was primarily due to the profit on disposal of RAC of £532 million, which was partly offset by a loss from Aviva's share of joint ventures and associates of £123 million (2010: £141 million profit).

Expenses (from continuing operations)

Year ended 31 December 2012

Claims and benefits paid net of reinsurance in 2012 decreased by £779 million, or 3%, to £23,601 million (2011: £24,380 million) mainly reflecting lower claims payments in our life businesses.

Changes in insurance liabilities in 2012 was a charge of £430 million (2011: £2,284 million charge). This was primarily due to changes in economic and non-economic assumptions.

The change in investment contract provisions was a charge of £4,450 million (2011: £1,478 million credit) as a result of improved investment market conditions causing an increase in contract liabilities.

The change in unallocated divisible surplus ("UDS") was a charge of £6,316 million (2011: £2,721 million credit). UDS in certain funds in Italy and Spain were negative as at 31 December 2012. The main driver of the movement is a charge in France due to an increase in fixed interest asset values from lower risk-free rates and credit spreads.

Fee and commission expense, other expenses and finance costs increased by £171 million to £8,052 million (2011: £7,881 million). See 'Financial Statements IFRS – Note 6 – Details of expenses'.

Year ended 31 December 2011

Claims and benefits paid net of reinsurance in 2011 increased by £2,140 million, or 10%, to £24,380 million (2010: £22,240 million) reflecting increased claims payments in our life businesses.

Changes in insurance liabilities in 2011 was a charge of £2,284 million (2010: £2,837 million). This was primarily due to changes in economic and non-economic assumptions.

The change in investment contract provisions was a £1,478 million credit (2010: £9,212 million charge) as a result of deteriorating investment market conditions across our regions causing a decrease in contract liabilities.

The change in UDS was a £2,721 million credit (2010: £362 million). UDS in Italy and certain funds in Spain and France were negative as at 31 December 2011, impacted by increased government bond yields. The change in UDS included losses of £17 million in Italy and £49 million in Spain relating to negative UDS considered unrecoverable.

Fee and commission expense, other expenses and finance costs decreased by £417 million to £7,881 million (2010: £8,298 million). See 'Financial Statements IFRS – Note 6 – Details of expenses'.

**Profit/(loss) before tax attributable to shareholders' profits
(from continuing operations)****Year ended 31 December 2012**

Profit before tax attributable to shareholders was £25 million (2011: £551 million profit). The decrease was primarily due to the increased tax charge attributable to policyholders' returns.

Year ended 31 December 2011

Profit before tax attributable to shareholders in 2011 was £551 million (2010: £1,396 million profit). The decrease was primarily due to the drop in net investment income.

Market performance**UK & Ireland life**

The table below presents sales, net written premiums, adjusted operating profit and profit before tax attributable to shareholders' profits under IFRS from our UK and Ireland long-term businesses for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Pensions	5,158	5,279	3,801
Annuities	3,211	3,832	3,170
Bonds	379	801	1,686
Protection	1,228	1,025	944
Equity release	434	317	436
UK	10,410	11,254	10,037
Ireland	632	917	938
Life and pension sales	11,042	12,171	10,975
Investment sales	1,730	1,689	1,548
Long term saving sales	12,772	13,860	12,523
UK Health net written premiums	528	473	428
Net written premiums	5,623	6,823	6,287
Adjusted operating profit before tax			
United Kingdom	887	917	848
Ireland	5	47	126
Life business	892	964	974
General insurance and health – UK health	14	12	12
Fund management	11	11	3
Non-Insurance	(7)	(10)	(8)
Total adjusted operating profit before tax	910	977	981
Integration and restructuring costs	(87)	(46)	(51)
Adjusted operating profit before tax after integration and restructuring costs	823	931	930
Profit before tax attributable to shareholders' profits	98	151	835

Year ended 31 December 2012

On a PVNBP basis, sales in the UK long-term insurance and savings business decreased by £844 million, or 7%, to £10,410 million (2011: £11,254 million). Protection sales were up 20% to £1,228 million (2011: £1,025 million), benefiting from a full year's sales from the distribution deal with Santander. Sales of annuities were down 16% to £3,211 million (2011: £3,832 million) following the decision to withdraw from the large scale bulk purchase annuity market. However, sales of individual annuities were up 10% to £3,024 million despite price increases to manage capital usage. Sales of Equity Release were up 37% to £434 million (2011: £317 million) as Aviva deployed risk based pricing expertise, developed in the annuities market, to this product. Pensions sales were down 2% to £5,158 million (2011: £5,279 million). Within this, Group Personal Pensions sales were up 9% to £3,231 million (2011: £2,961 million) as benefits were seen from increased levels of activity in the run up to Retail Distribution Review ("RDR") and Auto-Enrolment. Individual Pensions (including SIPP (self invested pension plan) were down 4% to £1,803 million (2011: £1,876 million) as a disciplined approach to pricing was maintained. Sales of Bonds were down 53% to £379 million (2011: £801 million), impacted by changes in distribution channels in advance of RDR.

Ireland sales were down 31% to £632 million (2011: £917 million) due to the closure to new business of the joint venture with Allied Irish Bank ("AIB") from April 2012. Non AIB business sales were £530 million (2011: £485 million), with the increase driven by sales of fixed rate deposit funds and the re-launch of protection business in the second half of 2012.

Net written premiums in our UK & Ireland long-term insurance and savings businesses decreased by £1,200 million, or 18%, to £5,623 million (2011: £6,823 million). The decrease is primarily due the reduction in BPA (bulk purchase annuities) premiums.

Adjusted operating profit before tax decreased by £67 million, or 7%, to £910 million (2011: £977 million). This mainly reflects lower profits in Ireland where the Life operations result fell to £5 million from £47 million in 2011, as the closure to new business of our joint venture with AIB became effective. The UK Life business saw profits fall by £30 million or 3% to £887 million, mainly due to a lower level of one-off items in 2012 (2011 included one-off benefits of £93 million relating to the Part VII transfers of the former RBS JV entities and £30 million relating to the release of tax provisions associated with the reattribution of the inherited estate). Profit before tax decreased by £53 million, or 35%, to £98 million for 2012 (2011: £151 million).

Year ended 31 December 2011

On a PVNBP basis, sales in our UK and Ireland long-term insurance and savings business were £11,254 million, an increase of £1,217 million, or 12% (2010: £10,037 million). In the UK, protection sales grew by 9%, including a 7% increase in core protection products. Pension sales increased by 39% and annuities increased by 21% supported by a 23% growth in bulk purchase annuities and a 20% increase in the sale of individual annuities. Bonds decreased 52% reflecting our continued stance on writing profitable business, the changing distributor landscape pre RDR, and relative attractiveness of bonds following tax treatment changes. Equity release sales decreased 27% following an exceptional performance in 2010 when the market was less competitive. Investment sales increased by 9%, reflecting growth in managed funds and good performance from global property. In Ireland, sales fell 2% to £917 million (2010: £938 million).

Net written premiums in our UK and Ireland long-term insurance and savings business were £6,823 million, an increase of £536 million, or 9% (2010: £6,287 million). The increase was primarily due to higher sales in the UK of group personal pensions and individual annuities, offset by lower sales of single premium bonds.

Adjusted operating profit was £977 million, a decrease of £4 million (2010: £981 million). An increase in the UK was offset by a decrease in Ireland. In the UK, the non-profit result was driven by strong performance in annuities, increased annual management charges and inclusion of the full results of RBS Life, following its purchase by Aviva at the end of 2010. Included in the result are one-off benefits of £93 million relating to the Part VII transfers of the former RBS JV entities, and £30 million relating to the release of tax provisions associated with the reattribution of the inherited estate. The with-profit result, which includes the shareholders' share of regular and terminal bonus payments, decreased from 2010 mainly driven by the absence of the final special distribution (2010: £84 million). In Ireland, the 2010 result included a release of reserves following a review of assumptions of £75 million.

Profit before tax was £151 million, a decrease of £684 million, or 82% (2010: £835 million) reflecting an adverse impact from market movements in 2011 and impairment of goodwill in Ireland.

UK & Ireland general insurance and health

The table below presents sales, net written premiums, adjusted operating profit and profit before tax attributable to shareholders' profits under IFRS from our UK and Ireland general insurance and health businesses for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Sales/net written premiums			
United Kingdom	4,062	4,371	4,048
Ireland GI	326	367	397
Ireland Health	102	104	62
	4,490	4,842	4,507
Adjusted operating profit before tax			
United Kingdom	448	508	457
Ireland GI	21	32	32
Ireland health	8	12	19
General insurance and health	477	552	508
Integration and restructuring costs	(154)	(37)	(48)
Profit before tax attributable to shareholders' profits	206	806	348

Year end 31 December 2012

UK and Ireland general insurance and health NWP decreased by £352 million, or 7%, to £4,490 million (2011: £4,842 million), mainly as a result of the disposal of RAC. Excluding RAC, NWP decreased by £48 million, or 1%, to £4,062 million (2011: £4,110 million). The UK has seen growth in personal motor, corporate and speciality risks and personal speciality lines. This has been offset by management actions to reduce exposure in unprofitable business segments.

Adjusted general insurance and health operating profit in 2012 decreased by £75 million, or 14%, to £477 million (2011: £552 million). Our UK general insurance operation has seen a decrease of £60 million, or 12%, to £448 million (2011: £508 million) reflecting the RAC which was sold in 2011. Excluding the RAC contribution of £75 million in 2011, this represented a like for like increase of 3% with the 2012 result benefiting from a favourable movement on prior year claims and an increase in long term investment return. 2012 was the second wettest year on record and whilst UKGI had more flood claims, weather-related claims were broadly in line with long-term average compared to the favourable experience in 2011. In Ireland, general insurance adjusted operating profit has decreased by £11 million, or 34%, to £21 million (2011: £32 million) reflecting the difficult environment with intense competition and the adverse effect of the economy on premium volumes.

Restructuring costs have increased £117 million to £154 million (2011: £37 million), mainly due to the transformation of the Irish business and the program to simplify the organisational structure within the UK.

Profit before tax decreased by £600 million, or 74%, to £206 million (2011: £806 million). 2011 benefited from the profit on disposal of RAC of £532 million. This combined with the increase in restructuring costs described above accounts for the majority of the year on year decrease.

Year end 31 December 2011

UK and Ireland general insurance and health NWP was £4,842 million, an increase of £335 million, or 7% (2010: £4,507 million). Performance was driven by the UK general insurance operation where NWP increased by £323 million, or 8%, to £4,371 million (2010: £4,048 million). In personal motor, NWP (excluding RAC) was £1,126 million, an increase of £272 million, or 32% (2010: £854 million) reflecting rating action, strong growth in direct sales and the roll out of direct pricing to brokers.

Adjusted general insurance and health operating profit in 2011 was £552 million, an increase of £44 million, or 9% (2010: £508 million). Our UK general insurance operation increased £51 million, or 11%, to £508 million (2010: £457 million). Excluding RAC, adjusted operating profit grew by £61 million, or 16%, to £433 million (2010: £372 million), with the 2011 result benefiting from favourable weather and a further improvement in underlying profitability. These factors were offset in part by small strengthening in prior year claims reserves (excluding adverse 2010 freeze development) of £37 million (2010: £87 million release). This primarily reflected adverse experience on 2010 commercial motor business (for some vans, taxis and scheme accounts) and on one historic professional indemnity account. We took rating action and selective exits with respect to these poor performing business lines.

Profit before tax was £806 million, an increase of £458 million, or 132% (2010: £348 million). The increase was driven by the profit on disposal of RAC in the UK of £532 million.

France

The table below presents sales, net written premiums, adjusted operating profit and profit before tax attributable to shareholders' profits under IFRS from our operations in France for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Sales			
Long-term insurance and savings business	3,638	4,047	4,918
General insurance and health	1,002	1,016	968
Total sales	4,640	5,063	5,886
Net written premiums	4,702	5,233	5,979
Adjusted operating profit before tax			
Long-term insurance and savings business	335	323	319
General insurance and health	95	144	76
Non-insurance	(8)	4	(34)
Total adjusted operating profit before tax	422	471	361
Integration and restructuring costs	(11)	(30)	(8)
Adjusted operating profit before tax after integration and restructuring costs	411	441	353
Profit before tax attributable to shareholders' profits	482	267	387

Year ended 31 December 2012

Total sales in France were down £423 million, or 8%, to £4,640 million (2011: £5,063 million) mainly due to a reduction in long-term insurance and savings sales. Total life and pensions sales decreased 10% to £3,638 million (2011: £4,047 million), a reduction of 4% on a local currency basis, with sales in the AFER product declining and sales through the Bancassurance channel remaining broadly flat.

France's net written premium was £4,702 million, down £531 million, or 10% (2011: £5,233 million) driven by the decrease in AFER sales and relatively flat sales in general insurance.

Adjusted operating profit for long-term insurance and savings business in 2012 was £335 million (2011: £323 million), an increase of £12 million or 4%.

General insurance and health adjusted operating profit decreased by £49 million, or 34%, to £95 million (2011: £144 million) due in part to the one-off release in 2011 of surplus reserve margins of £45 million. There was also adverse claims experience from the February 2012 freeze, partly offset by a decrease in personal motor bodily injury claims.

Restructuring costs in France were down £19 million, or 63%, to £11 million (2011: £30 million). 2011 included higher costs from the previous European restructuring programme.

Profit before tax attributable to shareholders' profits was £482 million, an increase of £215 million, or 81% (2011: £267 million).

Year ended 31 December 2011

In France, our focus on value over volume resulted in a decrease of £871 million, or 18%, in life and pension sales to £4,047 million (2010: £4,918 million). Sales in AFER decreased by £1,007 million, or 38%, to £1,639 million (2010: £2,646 million) offset by strong sales through Credit du Nord which increased by 13% to £1,407 million.

Our general insurance and health sales increased £48 million, or 5%, to £1,016 million (2010: £968 million) driven by pricing actions as we focused on value generation. Health net written premiums decreased £7 million, or 3%, to £227 million (2010: £234 million) reflecting customers reducing protection cover in a difficult economic environment.

France's net written premiums decreased £746 million, or 12%, to £5,233 million (2010: £5,979 million) primarily driven by lower sales.

Total adjusted operating profit increased £110 million, or 30%, to £471 million (2010: £361 million).

Our adjusted operating profit for long-term insurance and savings business in 2011 was £323 million (2010: £319 million).

General insurance and health adjusted operating profit increased by £68 million, or 89%, to £144 million (2010: £76 million) driven mainly by reserve margin releases.

France's profit before tax attributable to shareholders' profits was £267 million, down £120 million (2011: £387 million).

Canada

The table below presents sales, adjusted operating profit and IFRS profit before tax attributable to shareholders for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Sales/net written premiums	2,176	2,083	1,958
Adjusted operating profit before tax			
General insurance	276	254	222
Non-insurance	—	—	7
Total adjusted operating profit before tax	276	254	229
Integration and restructuring costs	(11)	(6)	(20)
Adjusted operating profit before tax after integration and restructuring costs	265	248	209
Profit before tax attributable to shareholders' profits	244	297	223

Year ended 31 December 2012

General insurance sales in Canada increased by £93 million, or 4%, to £2,176 million (2011: £2,083 million), due to a combination of improved retention levels and rate increases across both personal and commercial lines.

Adjusted operating profit improved by £22 million, or 9%, to £276 million (2011: £254 million) mainly due to favourable underwriting results partially offset by lower long-term investment return.

Restructuring costs have increased £5 million, or 83%, to £11 million (2011: £6 million) due to an increase in Solvency II costs and some Simplify transformation program costs.

Profit before tax attributable to shareholders' profits decreased by £53 million, or 18%, to £244 million (2011: £297 million).

Year ended 31 December 2011

General insurance sales in Canada increased by £125 million, or 6%, to £2,083 million (2010: £1,958 million), reflecting growth in both Personal and Commercial Lines.

Adjusted operating profit from general insurance improved by £32 million, or 14%, to £254 million (2010: £222 million) driven by growth in underwriting profit.

Profit before tax attributable to shareholders' profits increased by £74 million, or 33%, to £297 million (2010: £223 million).

Italy, Spain and Other

The table below presents sales and net written premiums, adjusted operating profit and profit before tax attributable to shareholders' profits under IFRS from our operations in Italy, Spain and Other for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Sales			
Long-term insurance and savings business			
Spain	1,295	1,926	2,084
Italy	1,971	2,993	4,456
Other	159	262	506
Total long term insurance and savings business	3,425	5,181	7,046
General insurance and health			
Italy & other	424	484	438
Total sales	3,849	5,665	7,484
Net written premiums	2,942	4,512	5,665
Adjusted operating profit before tax			
Long-term insurance and savings business			
Spain	215	216	179
Italy	159	140	119
Other	—	4	(6)
	374	360	292
General insurance and health			
Italy & other	53	(2)	96
Non-insurance	(13)	(24)	(7)
Total adjusted operating profit before tax	414	334	381
Integration and restructuring costs	(12)	(10)	(6)
Adjusted operating profit before tax after integration and restructuring costs	402	324	375
Profit/(loss) before tax attributable to shareholders' profits	340	(48)	224

Year ended 31 December 2012

Total long-term savings sales fell by £1,756 million, 34% to £3,425 million (2011: £5,181 million).

In Italy, lower savings and protection sales reflected the challenging conditions and decreased by £1,022 million, or 34%, to £1,971 million (2011: £2,993 million).

In Spain, life sales decreased by £631 million, or 33%, to £1,295 million (2011: £1,926 million) reflecting the continued tough economic conditions.

Our general insurance and health sales decreased by £60 million, or 12%, to £424 million (2011: £484 million). The decrease was driven by Italy where credit protection sales fell reflecting low levels of loan activity by partner banks and motor sales were also lower.

Net written premiums for the segment decreased £1,570 million, or 35%, to £2,942 million (2011: £4,512 million) due to lower sales as described above.

Total adjusted operating profit increased £80 million, or 24%, to £414 million (2011: £334 million).

General insurance and health adjusted operating profit increased by £55 million to £53 million profits (2011: £2 million loss) driven mainly by the Italian business which saw its combined operating ratio fall below 100%.

The profit before tax attributable to shareholders' profits was £340 million (2011: £48 million loss).

Year ended 31 December 2011

Long-term insurance and savings sales decreased £1,865 million, or 26%, to £5,181 million (2010: £7,046 million) and was primarily driven by management actions to reduce sales of capital intensive participating business.

In Italy, challenging conditions and management actions to focus on capital efficient products and move the product mix led to a fall in participating business sales, with life sales down £1,463 million, or 33%, to £2,993 million (2010: £4,456 million).

In Spain, sales decreased by £158 million, or 8%, to £1,926 million (2010: £2,084 million).

Our general insurance sales increased by £46 million, or 11%, to £484 million (2010: £438 million).

Net written premiums decreased by £1,153 million, or 20%, to £4,512 million (2010: £5,665 million) primarily driven by lower sales as described above.

Total adjusted operating profit decreased £47 million, or 12% to £334 million (2010: £381 million).

Loss before tax attributable to shareholders' profits was £48 million in 2011 (2010: £224 million profit). The loss primarily reflected negative investment variances.

In Italy, the UDS balance was £1,449 million negative as at 31 December 2011 (2010: £420 million negative). The method for estimation of the recoverable negative UDS balance was changed in 2011 to a real-world embedded value method. Further details on this including the impact of this change are set out in section 'Financial statements IFRS – Note 44 – Unallocated divisible surplus'.

Higher growth markets

The table below presents the sales, net written premiums, adjusted operating profit and profit before tax attributable to shareholders' profits under IFRS of Higher growth markets for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Sales			
Long-term insurance and savings business			
Asia	1,765	1,782	1,617
Poland (including Lithuania)	373	487	603
Other	403	320	295
Total long-term insurance and savings business	2,541	2,589	2,515
General insurance and health			
Asia	120	108	72
Poland (including Lithuania)	65	65	51
Other	89	91	100
Total general insurance and health	274	264	223
Investment sales	129	186	223
Total sales	2,944	3,039	2,961
Net written premiums	1,240	1,215	1,190
Adjusted operating profit before tax			
Long-term insurance and savings business			
Poland (including Lithuania)	153	167	157
Asia	69	108	70
Other	8	4	2
	230	279	229
General insurance and health			
Asia	(5)	(8)	(6)
Poland (including Lithuania)	9	(5)	(10)
Other	(26)	(12)	(12)
	(22)	(25)	(28)
Non-insurance and fund management	(6)	(25)	(29)
Total adjusted operating profit before tax	202	229	172
Integration and restructuring costs	(9)	(9)	(15)
Adjusted operating profit before tax after integration and restructuring costs	193	220	157
Profit before tax attributable to shareholders' profits	217	178	161

Year ended 31 December 2012

Total sales for the segment were £2,944 million, a decrease of £95 million or 3% (2011: £3,039 million). Long-term insurance and savings sales in Asia decreased by £17 million, or 1%, to £1,765 million (2011: £1,782 million) with higher sales in Singapore more than offset by lower sales in other markets. Long term sales in Poland decreased by £114 million, or 23%, to £373 million (2011: £487 million) as a result of lower appetite for unit-linked products and regulatory changes relating to pensions. Sales in other markets increased by £83 million or, 26%, to £403 million (2011: £320 million) driven by Turkey which saw a 35%

sales increase as a result of expansion of the bancassurance and direct sales channels.

Overall net written premiums in the general insurance and health business increased to £274 million (2011: £264 million).

In Asia, net written premiums in the general insurance and health business rose to £120 million (2011: £108 million) due to growth in Singapore.

Adjusted operating profit decreased by £27 million, or 12%, to £202 million (2011: £229 million). The change mainly reflects the non recurrence of a Hong Kong reserving change which benefited the results by £25 million in 2011.

Profit before tax attributable to shareholders increased by £39 million, or 22%, to £217 million (2011: £178 million).

Year ended 31 December 2011

Total sales increased by £78 million, or 3%, to £3,039 million (2010: £2,961 million) despite uncertain economic conditions and regulatory climates in China and India. The strong performance in Asia, up 10%, reflects the success of our existing bancassurance partnerships. Life and pension sales in Poland decreased 19% to £467 million as a result of legislation changes.

Net written premiums increased by £25 million, or 2%, to £1,215 million (2010: £1,190 million).

Adjusted operating profit increased by £57 million, or 33%, to £229 million (2010: £172 million). This includes a reserving change benefit in Hong Kong of £25 million in 2011.

Profit before tax increased by £17 million, or 11%, to £178 million (2010: £161 million).

Aviva Investors

The table below presents the investment sales, adjusted operating profit, profit before tax attributable to shareholders' profits under IFRS and funds under management of Aviva Investors for the three years ended 31 December 2012, 2011 and 2010. As set out in 'Financial Statements IFRS – note 3 – Subsidiaries', the internal asset management operations of Aviva Investors North America are being sold with the US life business and have been classified within discontinued operations.

	2012 £m	2011 £m	2010 £m
Continuing operations			
Investment sales	2,727	1,598	1,616
Fund management operating profit	39	50	60
Long-term insurance and savings business – Pooled Pensions operating profit ¹	3	3	3
Total adjusted operating profit before tax	42	53	63
Integration and restructuring costs	(33)	(30)	(28)
Adjusted operating profit before tax after integration and restructuring costs	9	23	35
Profit before tax attributable to shareholders' profits	2	36	29
Assets under management (including discontinued operations)	274,484	262,506	259,787

¹ Aviva Investors operating profit includes profit relating to the Aviva Investors Pooled Pension business.

Year ended 31 December 2012

Aviva Investors' adjusted operating profit for fund management from continuing operations decreased by £11 million, or 22%, to £39 million (2011: £50 million). The reduction in profits was as a result of lower performance fees, partially offset by lower operating expenditure driven by cost savings.

Profit before tax attributable to shareholders from continuing operations decreased by £34 million, or 94%, to £2 million (2011: £36 million), mainly due to the reduction in adjusted operating profit and a one-off profit in 2011 arising on the disposal of Aviva Investors Australia.

Aviva Investors' funds under management (including discontinued operations), increased by £11 billion, or 4%, to £274 billion (2011: £263 billion). This is due to capital appreciation more than offsetting negative net flows. Further details are given in 'Financial Statements IFRS – note 58 – Assets under management'.

Year ended 31 December 2011

Aviva Investors' adjusted operating profit for fund management was £50 million, a decrease of £10 million, or 17% (2010: £60 million). The fall in adjusted operating profit reflected the impact of ongoing investment in our global infrastructure and clients re-evaluating their risk appetite in the face of the continuing economic downturn which, in some instances, lead them to re-allocate towards lower fee-bearing asset classes, with a consequential impact on revenue.

Profit before tax attributable to shareholders from continuing operations was £36 million, an increase of £7 million, or 24% (2010: £29 million), which benefited from the £23 million profit recognised on the sale of our Australian asset management subsidiary, offset by an impairment charge made against the value of an intangible asset.

Aviva Investors' funds under management (including discontinued operations) were £263 billion, an increase of £3 billion, or 1% (2010: £260 billion). The increase was a result of positive net funded sales, and capital appreciation, partially offset by the impact of the sale of our business in Australia.

Corporate centre and Group debt costs and other interest (from continuing operations)

The table below presents corporate centre and Group debt costs and other interest from continuing operations for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Corporate centre	(136)	(138)	(143)
Group debt costs and other interest	(659)	(648)	(644)
Other Group operations	(204)	(204)	(176)

Year ended 31 December 2012

Corporate centre costs decreased by £2 million, to £136 million (2011: £138 million). This was driven by a reduction in central spend and share award costs, partly offset by higher project costs, including the impact of meeting greater financial and regulatory requirements.

Group debt and other interest costs increased by £11 million, or 2% to £659 million (2011: £648 million). This increase principally relates to higher interest costs on internal lending arrangements driven by changes in internal loan balances throughout the year. Group debt costs and other interest includes a net pension charge of £35 million (2011: £46 million). This represents the difference between the expected return on pension scheme assets and the interest charge on pension scheme liabilities.

Other Group operations costs have remained flat at £204 million (2011: £204 million). This includes balances described as non-insurance in the market sections above, and £48 million relating to the running costs of the Aviva Europe and North America regional offices, which have subsequently both closed. It also includes Group banking and finance charges of £26 million and marketing spend of £22 million.

Year ended 31 December 2011

Corporate centre costs were £138 million, a decrease of £5 million, or 3% (2010: £143 million). The decrease principally reflected a reduction in project spend of £18 million in the year, and was offset by central spend which increased by £11 million arising from continued commitment to meeting increased regulatory and reporting requirements.

Group debt and other interest costs were £648 million, an increase of £4 million, or 1% (2010: £644 million). This increase principally related to higher interest costs on internal lending arrangements driven by changes in internal loan balances throughout the year.

Group debt costs and other interest included net pension charge of £46 million (2010: £87 million). This represented the difference between the expected return on pension scheme assets and the interest charge on pension scheme liabilities.

Other Group operations incurred costs of £204 million (2010: £176 million).

Adjusted operating profit before tax (from continuing operations)**Year ended 31 December 2012**

Adjusted operating profit before tax decreased by £201 million, or 10%, to £1,888 million (2011: £2,089 million) for the reasons set out above.

Year ended 31 December 2011

Adjusted operating profit increased by £265 million, or 15%, to £2,089 million (2010: £1,824 million) for the reasons set out above.

**Discontinued operations
United States**

In December 2012 the Group announced the sale of its United States life and related internal asset management businesses (US Life) to Athene Holding Ltd for £1.0 billion after the repayment of an external loan. The transaction is expected to be completed in 2013. See 'Financial statements IFRS – Note 3 – Subsidiaries' for further details. As a result of this announcement the results of US Life for 2012 and comparative periods have been classified as discontinued operations. The table below presents sales, net written premiums, adjusted operating profit and IFRS profit/(loss) before tax attributable to shareholders for the three years ended 31 December 2012, 2011 and 2010.

	2012 £m	2011 £m	2010 £m
Sales			
Life	1,441	1,093	999
Annuities	2,598	2,839	3,729
Total sales	4,039	3,932	4,728
Net written premiums	3,589	3,620	4,485
Adjusted operating profit before tax			
Long-term insurance and savings business	200	197	174
Non-insurance	(16)	(11)	(6)
Fund management	55	37	34
Total adjusted operating profit before tax	239	223	202
Integration and restructuring costs	(7)	(7)	(9)
Adjusted operating profit before tax after integration and restructuring costs	232	216	193
(Loss)/profit before tax attributable to shareholders' profits	(2,696)	262	149

Year ended 31 December 2012

Sales increased by 3% to £4,039 million (2011: £3,932 million). Life sales were up 32% to £1,441 million (2011: £1,093 million) as the business focussed on accelerating the growth of the life insurance business. Sales of our annuity products declined by 8% to £2,598 million (2011: £2,839 million) as a result of pricing actions taken throughout the year. Net written premiums decreased by 1% to £3,589 million (2011: £3,620 million) as higher sales were offset by increased outward reinsurance premiums.

Adjusted operating profit increased by £16 million, or 7%, to £239 million (2011: £223 million). Long-term insurance and savings adjusted operating profit remained broadly flat at £200 million (2011: £197 million). Fund management operations generated profits of £55 million (2011: £37 million).

Loss before tax attributable to shareholders was £2,696 million (2011: £262 million profit) which mainly relates to the impairment to write the value of the business down to fair value less costs to sell.

Year ended 31 December 2011

Sales decreased by £796 million, or 17%, to £3,932 million (2010: £4,728 million).

Annuity sales in 2011 declined by £890 million, or 24%, to £2,839 million (2010: £3,729 million), primarily driven by a focus on value over volume, with strong annuity price competition and increased consumer demand for variable annuity products in the first half of 2011.

Life sales increased by £94 million, or 9%, to £1,093 million (2010: £999 million) reflecting a focus on growth in life business.

Net written premiums decreased by £865 million, or 19%, to £3,620 million (2010: £4,485 million) due to lower annuity sales.

Adjusted operating profit increased by £21 million, or 10%, to £223 million (2010: £202 million) as our in-force book grew and we maintained strong spread management and disciplined pricing in a competitive environment.

Profit before tax attributable to shareholders' profits increased by £113 million, or 76%, to £262 million (2010: £149 million). The increase was mainly as a result of improved operating results and favourable short term investment variances.

Delta Lloyd

On 6 May 2011, the Group sold 25 million shares in Delta Lloyd, reducing our holding at that date to 42.7% of Delta Lloyd's ordinary share capital, representing 40% of shareholder voting rights. As the Group no longer commanded a majority of shareholder voting rights, it no longer controlled Delta Lloyd. Accordingly, from 6 May 2011, the Group ceased to consolidate the results and net assets of Delta Lloyd and its results up to that date were shown as discontinued operations. For the period from 6 May 2011 to 5 July 2012, the Group had an associate interest in Delta Lloyd. In July 2012, following a further sell-down, the Group's holding fell to 19.8% of Delta Lloyd's ordinary share capital representing 18.6% of shareholder voting rights and for the remainder of 2012 it was treated as a financial investment. In January 2013, the Group sold the remainder of its holding in Delta Lloyd. The table below presents sales, net written premiums, adjusted operating profit and IFRS (loss)/profit before tax for Delta Lloyd as a subsidiary for the three years ended 31 December 2012, 2011 and 2010.

Discontinued operations	2012 £m	2011 £m	2010 £m
Sales			
Long-term insurance and savings business	—	1,255	3,793
General insurance and health	—	557	1,177
Total sales	—	1,812	4,970
Net written premiums		2,043	4,340
Total adjusted operating profit – discontinued operations	—	191	524
(Loss)/profit before tax attributable to shareholders' profits	—	(726)	895

Year ended 31 December 2012

The Group's share of the loss of its associate interest in Delta Lloyd to 5 July 2012 was £304 million.

Year ended 31 December 2011

Delta Lloyd's adjusted operating profit for the period to 6 May 2011, when it was deconsolidated, was £191 million.

The Group's share of the profits of its retained interest in Delta Lloyd as an associate for the remainder of 2011 was £133 million.

From the start of 2011 to the partial disposal on 6 May 2011, the AAA collateralised bond spread narrowed by about 80 basis points ("bps") as a result of changes in the underlying bond index. This movement was the main driver of the adverse life investment variance of £820 million and the loss before tax of £726 million seen in the first four months of 2011.

Selected consolidated financial data

This data is derived from our consolidated financial statements which have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU).

In December 2012 the Group announced the sale of its US Life and related internal asset management operations, which have been classified as held for sale in the statement of financial position and their results shown as discontinued operations.

The results presented as discontinued operations for 2011 and preceding years also include the results of Delta Lloyd N.V. which was deconsolidated during 2011. Between May 2011 and July 2012 Delta Lloyd was accounted for as an associate within continuing operations. In July 2012, following a further sell-down, the Group's shareholding fell below 20% and from July 2012 Delta Lloyd was treated as a financial investment within continuing operations at fair value through profit and loss.

Following a review of the classification of contracts issued by the Italian Life business, certain portfolios have been reclassified from participating insurance to participating investment contracts. This change has been reflected for all years in the table below. There is no impact on the result for any period as the result of this reclassification.

Income statement data

Amounts in accordance with IFRS	2012 £m	Restated 2011 £m	Restated 2010 £m	Restated 2009 £m	Restated 2008 £m
Continuing operations					
Income					
Gross written premiums	22,744	26,255	27,192	25,690	25,428
Premiums ceded to reinsurers	(1,571)	(1,548)	(1,606)	(2,294)	(1,613)
Premiums written net of reinsurance	21,173	24,707	25,586	23,396	23,815
Net change in provision for unearned premiums	(16)	(236)	(72)	552	296
Net earned premiums	21,157	24,471	25,514	23,948	24,111
Fee and commission income	1,273	1,465	1,451	1,552	1,672
Net investment income/(expense)	21,106	4,341	16,746	19,902	(17,946)
Share of (loss)/profit after tax of joint ventures and associates	(277)	(123)	141	(463)	(1,101)
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	(164)	565	163	122	(8)
	43,095	30,719	44,015	45,061	6,728
Expenses					
Claims and benefits paid, net of recoveries from reinsurers	(23,601)	(24,380)	(22,240)	(21,080)	(23,425)
Change in insurance liabilities, net of reinsurance	(430)	(2,284)	(2,837)	(1,119)	7,219
Change in investment contract provisions	(4,450)	1,478	(9,212)	(11,096)	10,880
Change in unallocated divisible surplus	(6,316)	2,721	362	(1,479)	4,452
Fee and commission expense	(4,472)	(4,326)	(5,500)	(4,081)	(4,038)
Other expenses	(2,845)	(2,779)	(2,116)	(3,583)	(2,668)
Finance costs	(735)	(776)	(682)	(755)	(847)
	(42,849)	(30,346)	(42,225)	(43,193)	(8,427)
Profit/(loss) before tax	246	373	1,790	1,869	(1,699)
Tax attributable to policyholders' returns	(221)	178	(394)	(217)	1,068
Profit/(loss) before tax attributable to shareholders' profits	25	551	1,396	1,652	(631)
Tax attributable to shareholders' profits	(227)	(134)	(345)	(440)	294
(Loss)/profit after tax from continuing operations	(202)	417	1,051	1,212	(337)
(Loss)/profit after tax from discontinued operations	(2,848)	(357)	841	103	(548)
Total (loss)/profit for the year	(3,050)	60	1,892	1,315	(885)

Amounts in accordance with IFRS	Per share	Per share	Per share	Per share	Per share
(Loss)/profit per share attributable to equity shareholders:					
Basic (pence per share)	(113.1)p	5.8p	50.4p	37.8p	(36.8)p
Diluted (pence per share)	(113.1)p	5.7p	49.6p	37.5p	(36.8)p
Continuing operations – Basic (pence per share)	(15.2)p	11.1p	37.6p	35.3p	(15.7)p
Continuing operations – Diluted (pence per share)	(15.2)p	10.9p	37.0p	35.0p	(15.8)p

Amounts in accordance with IFRS	Per share	Per share	Per share	Per share	Per share
Dividends paid per share	19.0p	26.0p	25.5p	24.0p	33.0p

Amounts in accordance with IFRS	Millions	Millions	Millions	Millions	Millions
Number of shares in issue at 31 December	2,946	2,906	2,820	2,767	2,658
Weighted average number of shares in issue for the year	2,910	2,845	2,784	2,705	2,643

Statement of financial position data

Amounts in accordance with IFRS	2012 £m	Restated 2011 £m	Restated 2010 £m	Restated 2009 £m	Restated 2008 £m
Total assets	315,689	312,376	370,107	354,391	354,562
Gross insurance liabilities	113,091	147,379	174,742	168,699	172,550
Gross liabilities for investment contracts	110,494	113,366	120,745	112,408	109,859
Unallocated divisible surplus	6,931	650	3,428	3,866	2,325
Core structural borrowings	5,139	5,255	6,066	5,489	5,525
Other liabilities	68,674	30,363	47,401	48,843	49,730
Total liabilities	304,329	297,013	352,382	339,305	339,989
Total equity	11,360	15,363	17,725	15,086	14,573

History and development of Aviva

General

Aviva, a public limited company incorporated under the laws of England and Wales, provides customers with long-term insurance and savings, general and health insurance, and fund management products and services. Over the last few years we have simplified and streamlined Aviva, focusing on markets where we can produce attractive returns.

We are committed to serving our customers well in order to build a strong, sustainable business which makes a positive contribution to society and which our people are proud to work for.

Our history

The Group was formed by the merger of CGU plc and Norwich Union plc on 30 May 2000. CGU plc was renamed CGNU plc on completion of the merger, and subsequently renamed Aviva plc on 1 July 2002.

CGU plc and Norwich Union plc were both major UK-based insurers operating in the long-term insurance business and general insurance markets. Both companies had long corporate histories. Hand in Hand, which was incorporated in 1696, was acquired by Commercial Union in 1905, which itself was incorporated in 1861. General Accident plc was incorporated in 1865. Norwich Union plc was founded as a mutual society in 1797 and operated as such until 1997 when it demutualised and became an English public limited company. CGU plc was formed in 1998 from the merger of Commercial Union plc and General Accident plc.

In 2011 and 2012 the Group has undertaken and announced a number of disposals as we have continued the process of streamlining our business. Further details of these can be found in the sections 'Financial statements IFRS – note 3 – Subsidiaries', 'note 18 – Interests in, and loans to, joint ventures' and 'note 19 – Interests in, and loans to, associates'.

Business overview

Our aims and strategy

In July 2012, we announced our new strategic plan which has three main objectives:

■ Narrow focus

We aim to focus on fewer business segments where we believe we can produce attractive returns with a high probability of success.

■ Build financial strength

We will achieve target economic capital levels in line with our industry peers, reduce capital volatility and bring leverage down to a conservative level. We announced new target economic capital levels of 160-175%.

■ Improve financial performance

We aim to deliver a higher level of revenue growth, lower losses and claims and higher return on capital, notwithstanding the subdued economic environment in developed markets. During 2012 we announced a new expense reduction target of £400 million.

Our business

Overview

Following the announcement in the second quarter of 2012 relating to the restructuring of the Group, the Group's operating segments were changed to align them with the new management reporting structure. The new operating segments are: UK & Ireland; France; Canada; Italy, Spain and Other; Higher growth markets and Aviva Investors. In December we announced the sale of our United States life, savings and related internal fund management business and this has been classified as a discontinued operation for the purposes of reporting financial performance.

Due to the size of the UK & Ireland segment, it has been split into separate Life and General Insurance segments, which undertake long-term insurance and savings business and general insurance, respectively. Aviva Investors, our fund management business, operates across most markets providing fund management services to third-party investors and to our long-term insurance businesses and general insurance operations.

Our business operates across three main market sectors – life insurance and savings; general and health insurance; and fund management.

Life insurance and savings business

Long-term insurance and savings business from continuing operations accounted for approximately 74% of our total business based on worldwide total sales from continuing operations for the year ended 31 December 2012. We reported total long-term insurance and savings new business sales from continuing operations of £20.6 billion and investment sales of £4.6 billion for the year ended 31 December 2012. Our focus remains on growing our business profitably and improving our operational efficiency so that we can fully benefit as our major markets return to economic growth.

Market position

In the UK we are a market leader and have a market share of 12% based on annual premium equivalent (APE)¹ according to the Association of British Insurers (ABI) data as at 30 September 2012. Sales of life, investment and general insurance products in the UK represented 49% of our worldwide sales for the year ended 31 December 2012. Further details of our position in each market are set out in the market sections below.

Brands and products

We have operated under the Aviva brand globally since 2010.

Our long-term insurance and savings businesses offer a broad range of life insurance and savings products. Our products are split into the following categories:

- Pensions – is a means of providing income in retirement for an individual and possibly his or her dependants. Our pension products include personal and group pensions, stakeholder pensions and income drawdown.
- Annuities – is a type of policy that pays out regular amounts of benefit, either immediately and for the remainder of a person's lifetime, or deferred to commence from a future date. Immediate annuities may be purchased for an individual and his or her dependants or on a bulk purchase basis for groups of people. Deferred annuities are asset accumulation contracts, which may be used to provide benefits in retirement, and may be guaranteed, unit-linked or index-linked.
- Protection – is an insurance contract that protects the policyholder or his or her dependants against financial loss on death or ill-health. Our product ranges include term assurance, mortgage life insurance, flexible whole life and critical illness cover.
- Bonds and savings – are accumulation products with single or regular premiums and unit-linked or guaranteed investment returns. Our product ranges include single premium investment bonds, regular premium savings plans, mortgage endowment products and funding agreements.
- Investment sales - comprise retail sales of mutual fund type products such as unit trusts, individual savings accounts ("ISAs") and open ended investment companies ("OEICs").
- Other - includes equity release and structured settlements.

Some of our insurance and investment contracts contain a discretionary participation feature, which is a contractual right to receive additional benefits as a supplement to guaranteed benefits. These are referred to as participating contracts.

¹ APE is a recognised sales measure in the UK and is the total of new annual premiums plus 10% of single premiums.

General insurance and health insurance

General insurance and health insurance accounted for 26% of our total worldwide sales for the year ended 31 December 2012. In the year ended 31 December 2012, we reported general and health insurance net written premiums of £8.9 billion.

Market position

We are a leading general insurer in the United Kingdom and Canada and also have general insurance operations in France, Italy, Ireland, Poland and Turkey. We sell health products in the UK, Ireland, Singapore and Indonesia. In the year ended 31 December 2012, 52% of our total general insurance and health new business from continuing operations was written in the UK.

Brands and products

Our general insurance business operates under the Aviva brand globally and concentrates on the following products:

- Personal lines – motor, household, travel and creditor;
- Commercial lines – fleet, liability and commercial property insurance;
- Health insurance – private health insurance, income protection and personal accident insurance, as well as a range of corporate healthcare products; and
- Corporate and specialty risks – products for large clients or where the risk is specialised.

Distribution

Customers can buy our products through a range of distribution channels, including:

- Direct – In many of our markets, customers can buy our products over the telephone or via the internet. This method of distribution is most commonly available for simple, low cost products which do not require advice.
- Direct sales force – In some of our European and Asian markets we operate direct sales forces that only sell Aviva's products and the sales forces receive commission on the products they sell.
- Intermediaries – We offer a range of long-term insurance, savings, retirement, general insurance and health insurance products which can be bought through an intermediary, such as an independent financial adviser or an insurance broker. Intermediaries receive a commission on sales of Aviva's products.
- Corporate partnerships, bancassurance and joint ventures – Aviva is a corporate partner for many organisations, including banks and other financial institutions, who wish to offer their customers insurance products. We have various distribution agreements with bancassurance partners and joint ventures across the markets in which we operate. In return for offering our products to their customers, the bank or joint venture partners receive a commission as a percentage of sales and in some cases achieve extra commission if agreed target levels of sales are met. Certain agreements have a profit sharing element based on a predetermined percentage. In some cases, if the agreed targets are not met, certain terms of the contract can be renegotiated. Under the joint venture agreements, the cost of running the venture are often split between the partners.

Further details of the distribution channels specific to each market are included in the following market analysis.

Fund management

Aviva Investors, our fund management business, provides fund management services to Aviva's long-term insurance and savings, and general insurance operations as well as to third-party investors. The main fund management operations are in the UK, North America, Europe, Asia Pacific and the Middle East. All sales of retail fund management products are included in our long-term insurance and savings business sales.

In December 2012 it was announced that the internal asset management operations of Aviva Investors North America would be sold alongside the United States life business.

Market position

Aviva Investors was ranked 43rd globally by assets under management, according to the Towers Watson World 500 largest asset managers study 2011 ranking of asset managers by assets under management. Total worldwide funds managed by Aviva Investors at 31 December 2012 was £274 billion, including £38 billion relating to the United States Life and related internal asset management operations which are classified as discontinued operations in the financial statements. The substantial majority of this relates to Aviva's insurance and savings operations.

Brands and products

Aviva Investors operates under a single brand across our markets. Our business invests in most significant asset classes on behalf of institutional, pension fund and retail clients. In the US, Aviva Investors also own an asset management company called River Road Asset Management LLC.

Developed markets

UK & Ireland life

Business overview and strategy

In 2012, Aviva began combining its UK and Irish life insurance businesses under a single management structure, with the aim of allowing Ireland to leverage the scale and expertise that exists in the UK.

The UK business is a leading long-term insurance and savings provider with an overall market share of 12%, based on third quarter 2012 ABI returns. The Irish business is a large life and pension provider in Ireland.

Our strategy is to hold leading positions in workplace savings, individual annuities and protection whilst delivering strong margins and an Internal Rate of Return (IRR) in excess of the Group's target, overall and at a product level.

Our Irish long-term business is carried out through a subsidiary, Aviva Life Holdings Ireland Limited ("ALHI"), which is 75% owned by Aviva and 25% owned by Allied Irish Bank ("AIB"). ALHI holds four subsidiaries, one of which is Ark Life Assurance Company Limited ("Ark Life") which carries out bancassurance business via a distribution agreement with AIB. The original distribution agreement was renewable in 2011 but, on 15 December 2011, AIB notified the Group that they did not wish to renew it and the existing shareholders' agreement governing ALHI was terminated. The termination of this agreement triggered the ability for both parties to exercise put and call options that will result in the unwind of the original structure such that the Ark Life business returns 100% to AIB and the Group will purchase the 25% minority stake in ALHI. The formal exercise of these options was approved on 17 January 2012 and, as a result, the Ark Life business became held for sale on that date. Completion of the transaction is subject to agreement of terms with AIB and regulatory approval. Completion is expected in the next 12 months.

Market and competition

The UK industry has entered a period of significant regulatory change, with the Retail Distribution Review (RDR) and Auto-Enrolment, transforming the way that long-term savings products are bought and sold. We have been selling a full suite of RDR compliant products since September 2012 and during 2012 processed our first schemes under Auto-Enrolment. We also hold leading positions in the protection and annuities marketplaces which are largely unaffected by the RDR.

The UK long-term savings market is highly competitive and we consider our main competitors to be Standard Life, Prudential, Legal & General, and Lloyds Banking Group.

In Ireland, the economic environment remains challenging. The life insurance market in Ireland is largely consolidated. We consider our main competitors to be Bank of Ireland Life, Irish Life, Canada Life and Friends First.

Products

In the UK, we provide a comprehensive product range focused on both the consumer and corporate market with an approximate 70:30 split. The pensions and 'at retirement' products we offer include stakeholder and personal pensions, equity release, annuities, income drawdown and with-profits products. Our annuity offerings include immediate life, enhanced, fixed-term annuities and with-profits pension annuities. We provide a number of traditional life insurance products, including level-term, decreasing-term (with or without critical illness), guaranteed whole life insurance, and guaranteed lifelong protection plans. Our savings and investment products include ISAs, investment bonds, funds, base rate trackers, investments with guarantees and with-profits products.

In Ireland, our long-term insurance and savings business offers a wide range of protection, bonds, savings and pension products. Our protection products include life insurance, mortgage protection, specified illness and guaranteed and whole life cover products. The pension range covers retirement and investment products including government personal retirement savings accounts (PRSA) schemes.

Distribution

We have a multi-distribution strategy, which means we sell our products through intermediaries, corporate partners, in the workplace, and directly to customers. We are a leading provider in the UK intermediary market with a 12.5% share.²

In 2012, in the UK, we agreed an exclusive distribution deal with Tesco for the sale of protection products, following the extension of our distribution agreements with Santander and Barclays in 2011. We are also the provider of choice to the Royal Bank of Scotland and other leading organisations including the Post Office. We remain committed to building on our existing relationships and distribution partnerships as well as to growing our workplace and direct channels.

UK & Ireland general insurance Business overview and strategy

In 2012, Aviva continued to combine its UK and Irish general insurance businesses, allowing Ireland to leverage the scale and expertise that exists in the UK. We are a leading general insurer in both the UK and Ireland with market shares of 10.5%³ and 15.1%⁴ respectively, and have approximately 9 million customers. We employ around 11,000 people and operate from a number of locations throughout the UK and Ireland, including Norwich, Perth, Glasgow, London, Dublin and Galway.

We focus on personal and commercial insurance. In the UK we hold top three positions in all our major classes of business⁵. In Ireland we are a leader in general insurance⁴ and health insurance. We believe our key strengths include underwriting excellence, claims and cost management and excellent customer service. We focus on the fundamentals of the insurance business to maximise returns through the insurance cycle and provide stability of earnings.

Market

The UK is the third largest insurance market in the world.⁵ In 2011, the top four companies had a 32%³ share of the general insurance market.

The UK and Ireland general insurance markets are cyclical in nature and remain very competitive, particularly in personal lines, where the market is highly commoditised.

Following significant premium rate increases in recent years in response to rising claims costs and frequencies, the UK personal motor market has seen rate reductions in 2012 reflecting intense competition and regulatory change. Challenging conditions also apply to other UK classes of business, with rating increases typically limited to low single digits. In Ireland, the market remains challenging reflecting the economic downturn, increased competition and market contraction of 3% in 2010 and a further 5% in 2011.

In the UK our main competitors are Direct Line Group, RSA, The Admiral Group, AXA, Zurich, Lloyds Banking Group, Allianz and Ageas. In Ireland, our competitors include RSA, AXA, Zurich and Liberty.

Products

We provide a wide range of general insurance products both in the UK and Ireland. In the UK we have a business mix of approximately 60% personal lines and 40% commercial lines. Our UK personal products include motor, home and travel insurance. Our UK commercial products include motor, property and liability insurance for small and medium size enterprises ("SMEs") and the larger UK Corporate and Speciality Risks market.

In Ireland our products include property, motor, travel, farm and business insurance and our health insurance business provides products for both the personal and company sector.

Distribution

We have a multi-distribution strategy. Our personal products are sold directly to customers over the phone and through our websites www.aviva.co.uk, www.aviva.ie and www.quotemehappy.com, via brokers and through corporate partnerships. Our Quotemehappy insurance products are also available through price comparison websites. For commercial insurance, we focus on broker distribution and believe that independent brokers remain the best source of advice for business customers.

In Ireland, to deliver further efficiency benefits, we closed our network of high street branches and transferred customers to both One Direct and strategic broker partners, which ensured they retained access to local face-to-face solutions for their insurance needs.

France

Business overview and strategy

France is the fourth largest insurance market in the world⁵. Aviva France operates through two main companies: Aviva Vie and Antarius (JV structure with Crédit Du Nord). Aviva France, one of the top ten insurance businesses in France, is ranked seventh in life insurance (excluding bancassurance) and tenth in general insurance as measured by gross written premiums, according to L'Argus de l'Assurance, as at 31 December 2011. Our health business has a 1.8% share of the market based on 2011 premium income⁶. Aviva France's strategy is to continue to diversify and grow our business profitability.

Market

The life insurance market is driven by individual savings and dominated by bancassurance, which has accounted for around 60% of the life insurance market over the past decade according to the FFSA. We believe that the current volatility in the financial markets has affected customer confidence but that over a longer period, multi-funds policies and unit-linked funds are the best insurance vehicles for performance. We believe the long-term insurance and savings market in France has longer-term growth potential due to the ageing population and the growing need for private pensions.

The general insurance market in France is mature and highly competitive. For several years, price competition was high as insurers sought market share, particularly in the personal lines

² ABI Stats Q3 2012

³ Source: Datamonitor analysis of market share based on 2011 GWP

⁴ Source: Irish Insurance Federation, 2011

⁵ New Swiss Re Sigma Study (World Insurance 2011)

⁶ Source: Fédération française des sociétés d'assurance (FFSA)

market. In our opinion, the market has now entered a phase of price increases that currently makes up the majority of its marginal growth.

Products

Aviva France provides a wide range of insurance solutions: life and long-term savings, general insurance and asset management through Aviva Investors France. The products sold through our life channel are long-term savings, pensions and regular premium products and a broad range of protection products, primarily for individuals, and with a focus on the unit-linked market.

We have a longstanding relationship with the Association Française d'Épargne et de Retraite (AFER) which is the largest retirement savings association in France with 735,000 members as at 31 December 2011, to manufacture and distribute the AFER savings product. In the general insurance market our product range includes household, motor, health and legal protection products and also a range of insurance products for farms, craftsmen, tradesmen and small to medium sized entities and specific products for building firms and motor fleets.

Distribution

Aviva France has developed a multi-distribution model combining retail, direct and bancassurance networks through owned distribution channels, independent networks and partnerships. Our retail networks sell through 896 tied agents, a direct sales force made up of more than 280 advisors and 700 Union Financière de France (UFF) consultants (Aviva France also holds a majority stake in UFF) and more than 1,000 active brokers in the life, health and construction markets. Direct distribution is sold through Eurofil for personal general insurance, Aviva Direct for health and protection and Epargne Actuelle for the AFER product. Eurofil is the second largest direct general insurer and Aviva Direct is the leading provider of direct protection in France according to the FFSA as at December 2011. We operate in the bancassurance market through our partnership with Crédit du Nord, a subsidiary of Société Générale, selling life, savings, protection and general insurance products. This partnership gives Aviva access to over 1.9 million customers, as at December 2011.

Canada

Business overview and strategy

Aviva Canada is the country's second largest general insurer⁷ Through its distribution partners it provides a range of personal and commercial lines insurance products to nearly three million policyholders. It has an 8.4% market share and a top five position in all major provinces.⁷ Aviva Canada employs approximately 3,800 people and operates from a head office in Toronto, with other offices located throughout Canada.

We believe that we are well placed for continued growth and that our success is underpinned by our two strategic priorities of building strong broker relationships and maintaining sophisticated pricing and underwriting. We believe the transformation of our personal lines business over the last few years has ensured the business is highly competitive. We expect that continued refinement to our models will allow us to leverage this position to positively react to market opportunities. We will continue to address increasing customer demand for choice, simplicity and self-service by working with our broker partners on processes and technology solutions in order to help them compete with other channels.

Market

As the eighth largest⁸ in the world, Canada's general insurance market is established and stable. The four largest provinces generate around 89% of total premiums with Ontario, the largest, representing 48% of total Canadian premiums.⁹

The Canadian general insurance industry is highly fragmented with many small players and no dominant consumer brand. Steady consolidation has resulted in the top five companies representing 40% of the market and the top two companies, Intact Financial and Aviva, controlling 24% of the market.⁹ The rest of the industry includes several national carriers as well as smaller, provincially based or niche companies.

Whilst direct and affinity channels are gradually increasing in market share, the traditional broker channel accounts for over 65% of distribution.¹⁰ In addition to the growth of direct and affinity channels, insurance carriers are increasingly supporting and controlling distribution through investment in brokers.

Products

The general insurance products that we provide through our Canadian companies are:

- Personal, home and motor insurance;
- Small and medium-size enterprise commercial insurance, including motor, property, liability, boiler and machinery, and surety; and
- Niche personal insurance products including holiday and park model trailers, hobby farms, boats as well as antique, classic and custom cars.

Distribution

We operate in Canada through a distribution network focused on approximately 1,700 independent group and retail brokers who distribute our core personal and commercial line products. In addition, we work closely with both independent and wholly owned specialty brokers to distribute specialty personal line products.

Italy, Spain and Other

Italy

Business overview and strategy

Aviva Italy is the country's sixth largest life insurer, with a market share of 4.44% based on 2011 premiums (excluding Eurovita)¹¹ and is the 12th largest general insurance company with a market share of 1.54%¹². We have approximately 2.5 million customers across both the Life and General Insurance businesses.

Aviva Italy has set up a transformation plan to navigate through the current challenging economic environment and consolidate its business structure. Aviva Italy aims to reinforce its business partnerships with three of the five largest Italian banks and with 500 agents.

Market

The Italian life market is dominated by the top 10 providers which represent around 79% of the total market share¹³. The life insurance industry in Italy reported a decline in volumes as of 30 September 2012 with gross written premiums down by 10.2% compared to the same period in 2011, whilst the the general insurance segment decreased by 2.1% in the same period¹⁴.

In 2012 the Italian insurance industry went through three major changes:

- The Italian government introduced new legislation (Decreto Monti) which has led insurance companies to transform both their product ranges and their customer relationships (eg. separate private area for customers on the company website; black box service for motor insurance; new quotation tools);
- Two of the leading general insurance companies announced their merger: Unipol and Fondiaria Sai;

10 Axco Insurance Report for Canada

11 Associazione Nazionale fra le Imprese Assicuratrici (ANIA)

12 ANIA as at 31 December 2011

13 ANIA: www.ania.it/PUBBLICAZIONI/Premi_de_Lavoro_diretto_Italiano_.html

14 IVASS (Istituto per la Vigilanza sulle Assicurazioni)

7 MSA Research Inc., 2011 online database.

8 New Swiss Re Sigma Study (World insurance 2011)

9 MSA Research Inc., 2011 online database

- The insurance regulator went through a restructure and as of 1 January 2013 is reporting to the Bank of Italy. It is now called IVASS (Istituto per la Vigilanza sulle Assicurazioni).

Products

Our long-term insurance and savings business offers a wide range of products covering protection, bonds and savings and pensions.

We are focussed on less capital intensive products. We have reduced product guarantees and launched three new life products all with improved economic returns and reduced capital consumption.

We have increased our share of unit-linked business and reduced our with-profit sales, to manage down our exposure to this sector. We have been focusing to further develop our offering in protection where we are one of the market leaders.

Our general insurance business in Italy mainly provides motor and home insurance products to individuals, as well as small commercial risk insurance, including marine insurance, to businesses. In 2013 we will further develop our partnership with Banco Popolare distributing motor insurance through their branches.

Distribution

Our products are distributed through bancassurance partnerships with UniCredit Group, Banco Popolare Group and Unione di Banche Italiane (UBI). These partnerships give us access to more than 5,900 branches. In addition, we also have approximately 5,500 sales advisers, and 600 insurance (multi-mandate) agents and brokers as at the end of 2012.

Spain

Business overview and strategy

Aviva Spain is the country's fifth largest long-term insurer by gross written premiums with a market share of 5% in the third quarter of 2012.¹⁵ Aviva Spain sells protection, long-term savings and pensions, health and accident insurance through a bancassurance network based on joint ventures with six banks. We also sell through Aviva Vida y Pensiones, the wholly-owned Aviva branded long-term insurance company and through our exclusive distribution agreement with Spanish mutual insurance company Pelayo.

Our strategy in Spain is to maintain our bancassurance footprint and further develop our retail operations and attract new partners when the opportunities arise. In December 2012, we announced our intention to sell our share of our joint venture with Aseval to Bankia S.A for £494 million. We expect this transaction to be completed during the second quarter of 2013.

Market

The Spanish market is significantly affected by the current economic climate and the financial sector continues to be under pressure as a result of the ongoing restructuring process and mergers taking place. Any opportunities arising from these will be considered by Aviva on their merits. In relation to distribution agreements with bancassurance partners, Aviva is protected financially within our contracts with Spain's savings banks ("the cajas") from any detrimental affect arising from these mergers.

The top positions in the long-term life insurance market are dominated by bank-owned or bank-insurer joint ventures, with the overall bancassurance channel accounting for more than 74% of gross written premiums at the end of 2011¹⁶ in the Spanish life insurance market.

Customers in Spain are accustomed to receiving advice through banking channels, and we continue to use our relationship with our partners to capitalise on this whilst developing our retail agents and broker distribution network.

Products

We offer a wide range of bonds, savings, and protection products. Investment products include both unit linked and traditional plans, where profit sharing is regularly used to increase the policy return. Our traditional plans include savings schemes and income products. Pension savings products have valuable tax advantages. We offer a flexible range of individual and group pension plans with alternative investment choices. We also offer protection products, covering both mortgages and credit loans typically providing cover for the family in the event of death or disability. The ongoing focus is on less capital intensive products.

Distribution

Through bancassurance partnerships we have established subsidiaries to distribute our products with each of the banks as set out below:

- Unicorp Vida – in conjunction with Unicaja since 2001;
- CxG – in conjunction with Caixa Galicia since 2001;
- Caja España Vida – in conjunction with Caja España since 2001;
- Caja Granada Vida – in conjunction with Caja Granada since 2002;
- Cajamurcia Vida – in conjunction with Cajamurcia since 2007; and
- Aseval – in conjunction with Bancaja (now Bankia) since 2000 (sale announced December 2012 as set out in 'Financial statements IFRS – note 3 – Subsidiaries').

Aviva Vida y Pensiones distributes our products through professional intermediaries (financial advisers, agents and brokers), supported by a branch office network and call centres. In 2012 we saw the start of distribution through Pelayo's network of 200 branches and approximately 1,000 exclusive agents.

Our distribution relationships have enabled us to maintain our position as the largest provider of individual protection products in the market¹⁷.

Other

The Italy, Spain and Other segment also includes our Romanian pensions business, which is held for sale as at 31 December 2012, our reinsurance and run-off businesses and the results of our life businesses in Hungary, the Czech Republic and Romania up until the date of sale in July 2012.

Higher growth markets

Business overview and strategy

The higher growth markets segment covers our operations in nine markets in Asia as well as Poland, Lithuania, Turkey and Russia.

As at 30 June 2012, our Singapore subsidiary ranks fifth by APE according to the Life Insurance Association,¹⁸ providing employee benefits and healthcare insurance. In Singapore, we have a strong relationship with the Development Bank of Singapore (DBS).

In China, through our 50% joint venture with COFCO Ltd, we are ranked in the top five among the foreign life insurers in terms of APE.¹⁹ We have a presence in 12 provinces and over 50 branches. Due to regulatory changes in bancassurance, we are developing alternative distribution channels to reach high net worth customers.

In India, with a distribution network of 140 branches, we operate in partnership with the Dabur Group through a 26% interest in Aviva Life Insurance Company India Ltd. Tighter regulations on unit-linked products are driving an industry shift towards traditional products such as endowment and health policies. As at 31 August 2012, we ranked ninth among the

15 Investigación Cooperativa entre Entidades Aseguradoras y Fondos de Pensiones (ICEA).
16 ICEA in the publication 'Canales de Distribución - Estadística 2011'.

17 ICEA at 30 September 2012

18 Life Insurance Association

19 APE data released by National Insurance Industry Communication Club

private life insurance companies in India based on APE according to the Insurance Regulatory and Development Authority (IRDA).²⁰

In Asia we are focused on creating franchise value through organic growth. Increasing the value of our new business remains our first priority. We are achieving this through scale benefits and by focusing our product mix on higher margin products.

As of 30 June 2012, our Polish life operation is the fourth largest overall life insurer in Poland (including JV Life), with a market share of 7% based on total premium income according to the Polish Financial Supervision Authority (KNF).²¹ Our product strategy for pensions in Poland is to retain our status as one of the market leaders in terms of assets and customers. We have updated our pay and bonus structure for our sales force to link compensation directly with the value generated by the sale.

We also operate in Turkey (offering both general insurance and life products) and Russia (life operations).

Russia is held for sale at 31 December 2012 and we announced the disposal in February 2013.

Market

We believe the fundamentals of the Asian markets are strong. The Asian Development Bank predicts GDP growth for emerging markets in Asia of 7.2% in 2012.²² Despite inflationary pressures, we believe Asia's strong domestic demand and intra-regional trade is likely to sustain this growth momentum, with China and India driving the overall trend. We expect Asia to be the fastest growing region for life insurance globally, with the potential for 15-20% average market growth per annum over the next decade. We believe that South East Asia in particular offers one of the highest insurance margins in the world. By strengthening our multi-channel distribution capability as well as managing our product portfolio for margin and profit, we believe we are well-positioned to continue delivering strong growth in franchise value.

Outside of Asia, the Polish market for protection products has seen significant growth since 1999, although penetration rates remain relatively low according to KNF statistics. We expect the insurance market in Turkey to continue to grow as its economy matures.

Products

Our Asian businesses offer a range of protection, bonds and savings and pension products, including universal life, participating and non-participating endowments, unit-linked single and regular premium life insurance, other savings and pensions products and a range of accident and health insurance products.

Outside of Asia, our life business in Poland provides a broad range of unit-linked, annuities and bonds and savings products and health insurance. For institutions we offer group life insurance and employee pension programmes, which are both unit-linked products. Our pension business offers a standard product for all customers as part of the privately managed second pillar pensions market. We offer general insurance products to both commercial entities and individuals in Poland. For institutions we offer selected commercial lines risks. For individuals we offer home, accident and travel insurance, which are primarily sold by tied agents, as well as motor insurance, which is sold primarily through our direct operation. In Russia, we sell a wide range of products including personal and group life as well as personal accident policies. In Turkey, we sell life and savings products including unit-linked pensions, supplemented by protection insurance and other savings products. Our Turkish general insurance operations sell personal motor, household, commercial property, small and medium size enterprises, personal accident, marine and travel insurance.

Distribution

Across Higher growth markets we operate a multi-distribution strategy. In Singapore, we have a core bancassurance relationship with DBS Bank. In China and South Korea, we distribute the majority of our products through bancassurance and IFAs. In Hong Kong, India and Malaysia, bancassurance is the main distribution channel. We are investing in other channels, such as direct marketing, to diversify our sources of revenue.

Outside of Asia, the direct sales force and bancassurance is the main distribution channel for most of the Polish group and is made up of 2,200 tied insurance agents. Our biggest relationship is a joint venture with Bank Zachodni WBK (a subsidiary of Banco Santander) that sells both life and general insurance products through the bank's network of over 620 branches.²³ We also co-operate with independent insurance agencies and brokers. Our mutual funds are also sold in brokerage houses and our individual products are supported by call centre and website sales. We also have a direct platform (internet and call centre) for distribution of motor insurance. In Turkey, we operate through a multi-channel distribution framework consisting of bancassurance, direct sales force, corporate sales, agencies, telemarketing and brokers. In Russia we focus on bancassurance, where we sell through 21 banks and through brokers.

Aviva Investors

Business overview and strategy

Aviva Investors was established in 2008 when the Aviva Group combined all of its major fund management components into a single global fund management business. As at 31 December 2012, we had £274 billion in assets under management including £38 billion relating to the United States Life and related internal asset management operations which are classified as discontinued operations in the financial statements. Aviva Investors offers a range of investment management services, most notably in the UK, Europe, the US and Asia Pacific.

Our largest clients are the long-term insurance, savings, and general insurance businesses of Aviva, to whom we provide bespoke asset management services across a broad spectrum of asset classes.

We provide external clients with bespoke segregated solutions or offer access to a variety of fund ranges. Our principal target clients for the larger segregated solutions tend to be large pension funds and financial institutions such as insurance companies and banks.

Our strategy is to grow our share of higher-margin, external business, offering client-focused solutions and products to our customers across our international network.

Products and distribution

Our products cover a broad range of asset classes. In Europe, we have a range of SICAVs (open-ended collective investment schemes), which are domiciled in France, Luxembourg and Poland. These funds have different share classes depending on the size and type of investor. Our traditional distribution model for these funds focuses on wholesale distributors, asset allocators and small to mid-size institutional investors.

In the UK, we largely sell segregated mandates and specialist funds to pension schemes, local authorities and insurance companies. We also supply products to the retail and wholesale markets, principally through UK domiciled equity, bond and real estate funds. These are promoted to investors via IFAs, fund platforms, fund supermarkets and discretionary asset managers. In addition, we have a range of pooled pension funds which are aimed at the smaller pension fund market. These funds are normally defined benefit schemes and tend to be advised by investment consultants.

²⁰ http://www.irda.gov.in/ADMINCMS/cms/fmGeneral_List.aspx?DF=MBFL&mid=3.1.8

²¹ KNF: www.knf.gov.pl/images/A_Informacje_Ilkw_2011k_tcm75-27692.xls

²² Asian Development outlook 2011 update, December 2011.

²³ Bank Zachodni WBK: <http://indywidualni.bzwbk.pl/kontakt/wyszukiwarka-placowek-i-bankomatow/wyszukiwarka-placowek-i-bankomatow.html>

We manage hedge funds in the UK and the US. These funds are generally registered offshore and are promoted to institutional clients, family offices and wealth managers. They include both fund of fund and single strategy funds across fixed interest and convertibles markets. In the US we also have an asset management company called River Road Asset Management LLC.

We also have a range of specialist property funds. These funds are targeted at specialist real estate buyers and large institutions (mostly pension funds and local authorities), and provide real estate solutions to a wide range of risk appetites, ranging from secure income generating funds to leveraged growth funds.

We have six money market funds, domiciled in Dublin and Paris, addressing the sterling and euro money market segments. These funds are sold by a specialist sales team and target corporate treasury functions.

Discontinued operations

United States

Business overview and strategy

On 21 December 2012, the Group announced that it had agreed to sell its United States life operations, consisting of our United States life and annuities business (Aviva USA) and the related asset management operations of Aviva Investors North America, to Athene Holding Ltd. Completion of the sale is expected in 2013. As the disposal will result in the loss of a major geographical area of operations, previously presented as "United States" in the segmental reporting note, the results of Aviva USA for all periods presented in the income statement have been classified as a discontinued operation. Aviva USA has been classified as held for sale in the statement of financial position as at 31 December 2012.

Market

Aviva USA is a leading provider of fixed indexed life insurance and fixed indexed annuities in the USA. According to AnnuitySpecs.com, as of 30 September 2012, Aviva USA is ranked first in the market for the sale of fixed indexed life products with a 14% market share, and second for the sale of fixed indexed annuities with a 13% market share.²⁴

Products

Aviva USA offers both protection and savings products, with traditional fixed as well as indexed accumulation options that pay interest based on the movement of a market index. Depending on such movement, indexed policies can deliver higher returns than traditional fixed products, especially when interest rates are low. Indexed products also serve to protect the customer's investment and provide a guaranteed income even when the market is down.

Aviva USA also offers a range of optional extras or 'riders' that can be added to policies to meet customised individual needs.

In the savings market, Aviva USA's fixed annuity portfolio offers tax-advantaged savings opportunities and protection against the risk of outliving one's assets. Some of these products include a guaranteed lifetime withdrawal benefit that allows customers to make guaranteed minimum withdrawals from their annuity for the entirety of their lives.

Distribution

Aviva USA uses a multi-channel distribution strategy by focusing on more than 50 key distribution partners. Its distribution channels include career marketing organisations, independent marketing organisations, brokerage general agents and personal producing agents. Its network covers all 50 states with agents largely contracted through key distribution partners.

Delta Lloyd

Delta Lloyd is a financial services provider in the Netherlands and Belgium, operating in the life insurance and pensions, general insurance, fund management and selected banking markets.

The Group ceased to control Delta Lloyd on 6 May 2011 and its results for 2011 up to that date and prior years are presented as discontinued operations.

As explained in 'Financial Statements IFRS – note 3 – Subsidiaries', and 'Financial Statements IFRS – note 19 – Interests in, and loans to, Associates', for the period from 7 May 2011 to 5 July 2012, the Group had an associate interest in Delta Lloyd. From 6 July 2012, following a further selldown, the Group's stake was treated as a financial investment. The Group's share of Delta Lloyd's results as an associate and its interest in Delta Lloyd as a financial investment are both included in 'other Group activities' within continuing operations.

In January 2013, the Group sold its remaining stake in Delta Lloyd.

Organisational structure

Organisational structure

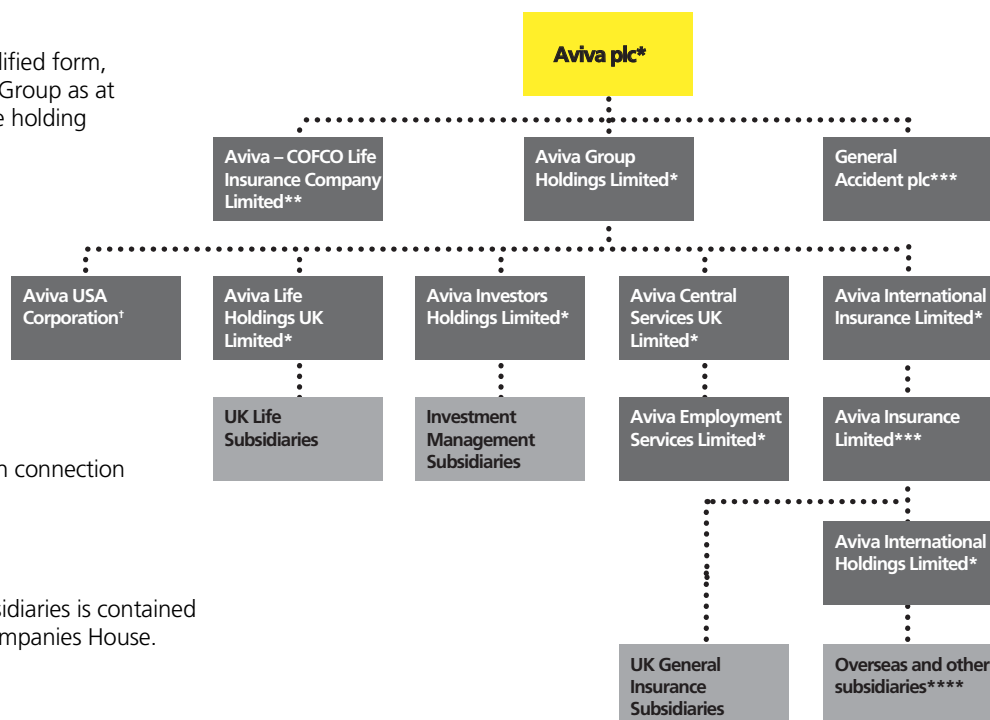
The following chart shows, in simplified form, the organisational structure of the Group as at 31 December 2012. Aviva plc is the holding company of the Group.

Parent company

Aviva plc

Subsidiaries

The principal subsidiaries of the Company are listed below by country of incorporation. All are wholly-owned, directly or indirectly, and transact insurance or reinsurance business, fund management activities or services in connection therewith, unless otherwise stated.



A complete list of the Group's subsidiaries is contained in the Group's annual return to Companies House.

- * Incorporated in England and Wales
- ** Incorporated in People's Republic of China.
Aviva plc has a 50% interest in the joint venture
- *** Incorporated in Scotland
- **** Includes certain investment management businesses
- † Incorporated in the United States

United Kingdom

Aviva Annuity UK Limited
 Aviva Central Services UK Limited
 Aviva Consumer Products UK Limited
 Aviva Employment Services Limited
 Aviva Equity Release UK Limited
 Aviva Health UK Limited
 Aviva Insurance Limited
 Aviva Insurance Services UK Limited
 Aviva International Insurance Limited
 Aviva Investors Global Services Limited
 Aviva Investors Pensions Limited
 Aviva Investors UK Fund Services Limited
 Aviva Investors UK Funds Limited
 Aviva Life & Pensions UK Limited
 Aviva Life Services UK Limited
 Aviva Risk Management Solutions UK Limited
 Aviva UKGI Investments Limited
 Gresham Insurance Company Limited
 The Ocean Marine Insurance Company Limited

Barbados

Victoria Reinsurance Company Ltd

Bermuda

Aviva Re Limited

Canada

Aviva Canada Inc. and its principal subsidiaries:
 Aviva Insurance Company of Canada
 Elite Insurance Company
 Pilot Insurance Company
 Scottish & York Insurance Co. Limited
 S&Y Insurance Company
 Traders General Insurance Company

France

Aviva France SA and its principal subsidiaries:
 Antarius S.A. (50.0%)
 Aviva Assurances S.A. (99.9%)
 Aviva Investors France S.A. (99.9%)
 Aviva Vie SA (99.9%)
 Aviva Epargne Retraite (99.9%)
 Eurofil S.A. (99.9%)
 Union Financière de France Banque (Banking) (74.3%)

Hong Kong

Aviva Life Insurance Company Limited

Indonesia

PT Asuransi Aviva Indonesia (60.0%)

Ireland

Aviva Insurance Europe SE
 Aviva Health Group Ireland Limited (70.0%)
 Aviva Life & Pensions Ireland Limited (75.0%)

Italy

Aviva Italia Holding S.p.A and its principal subsidiaries:
 Avipop Assicurazioni S.p.A (50.0%)
 Avipop Vita S.p.A (50.0%)
 Aviva S.p.A (51.0%)
 Aviva Assicurazioni Vita S.p.A (50.0%)
 Aviva Italia S.p.A
 Aviva Previdenza S.p.A (55.0%)
 Aviva Vita S.p.A (25.5%)
 Eurovita Assicurazioni S.p.A (41.0%)

Lithuania

Uždaroji akcinė gyvybės draudimo ir pensijų bendrovė
"Aviva Lietuva"

Poland

Aviva Powszechne Towarzystwo Emerytalne Aviva BZ WBK S.A.
(90.0%)
Aviva Towarzystwo Ubezpieczen na Zycie SA (90.0%)
Aviva Towarzystwo Ubezpieczen Ogolnych SA (90.0%)

Russia

Closed Joint Stock Insurance Company Aviva (Zao)

Singapore

Aviva Ltd
Navigator Investment Services Limited

Spain

Aseguradora Valenciana S.A., de Seguros y Reaseguros (Aseval)
(50.0%)
Aviva Vida y Pensiones, SA de seguros y reaseguros
Caja Espana Vida, Compania de Seguros y Reaseguros (50.0%)
Caja Murcia Vida y Pensiones, de Seguros y Reaseguros S.A.
(50.0%)
Caja Granada Vida, de Seguros y Reaseguros, S.A. (25.0%)
CxG Aviva Corporación CaixaGalicia de Seguros y Reaseguros,
S.A. (50.0%)
Unicorp Vida, Compania de Seguros y Reaseguros (50.0%)

Turkey

Aviva Sigorta A.S. (98.6%)

United States

Aviva USA Corporation and its principal subsidiaries:
Aviva Life and Annuity Company
Aviva Investors North America, Inc.
River Road Asset Management, LLC

Associates and joint ventures

The Group has ongoing interests in the following operations that are classified as associates or joint ventures. Further details of those operations that were most significant in 2012 are set out in notes 18 and 19 to the financial statements.

United Kingdom

The Group has interests in several property limited partnerships. Further details are provided in note 18 to the financial statements.

China

Aviva-COFCO Life Insurance Co. Limited (50.0%)

India

Aviva Life Insurance Company India Limited (26.0%)

Italy

Banca Network Investimenti SpA (50.0%)

Malaysia

CIMB Aviva Assurance Berhad (49.0%)
CIMB Aviva Takaful Berhad (49.0%)

South Korea

Woori Aviva Life Insurance Co, Ltd (47.3%)

Turkey

AvivaSA Emeklilik ve Hayat A.S (49.8%)

Vietnam

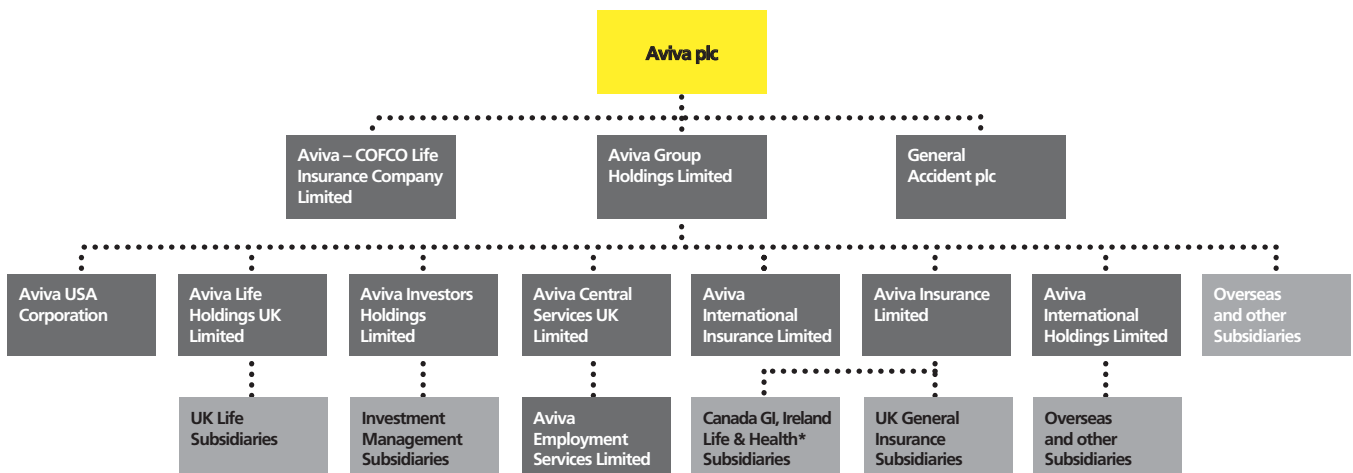
Vietinbank Aviva Life Insurance Company Limited (50.0%)

Group Restructuring

On 28 February 2013, a major restructuring of the Group was completed, which will have economic effect from 1 January 2013. Prior to the restructure, Aviva Insurance Limited ("AIL") acted both as the main UK general insurance underwriter as well as a holding company for the Group's non-UK operations. In order to enhance the governance relating to AIL and reduce the UK general insurance policyholders exposure to the non-UK operations, Aviva International Holdings Limited ("AIH"), the owner of the majority of the non-UK operations has been transferred to Aviva Group Holdings Limited ("AGH") in consideration for a loan from AIL, secured on the non-UK operations by way of the shareholding in the UK holding companies including AIH. At the same time, the shares in AIL, held by Aviva International Insurance Limited ("AIL") were transferred to AGH in consideration for a loan secured on the shares of AIL.

The impact of the above restructuring is to reduce the complexity of the current Group corporate structure resulting in a greater degree of direct control of subsidiaries creating a flatter, more transparent corporate structure.

The following chart shows, in simplified form, the organisational structure of the Group after the completion of the restructure:



*Subject to regulatory approval

Analysis of investments

We invest our policyholders' funds and our own funds in order to generate a return for both policyholders and shareholders. The financial strength of the Group and both our current and future operating results and financial performance are, therefore, in part dependent on the quality and performance of our investment portfolios in the UK, Europe, North America and Asia.

For additional information on our financial investments, see 'Financial statements IFRS – Note 25 – Financial investments'.

For a quantitative analysis of funds under management by Aviva and third-party fund managers, see 'Financial statements IFRS – Note 58 – Assets under management'.

Investment strategy

Our investment portfolio supports a range of businesses operating in a number of geographical locations. Our aim is to match the investments held to support a line of business to the nature of the underlying liabilities, whilst at the same time considering local regulatory requirements, the level of risk inherent within different investments, and the desire to generate superior investment returns, where compatible with this stated strategy and risk appetite.

Long-term insurance and savings business

As stated above, we aim to optimise investment returns whilst ensuring that sufficient assets are held to meet future liabilities and regulatory requirements. As different types of life insurance business vary in their cash flows and in the expectations placed upon them by policyholders, we need to hold different types of investments to meet these different cash flows and expectations.

The UK with-profits business is comprised largely of long-term contracts with some guaranteed payments. We are therefore able to invest a significant proportion of the funds supporting this business in equities and real estate. This is because the long-term nature of these contracts allows us to take advantage of the long-term growth potential within these classes of assets, whilst the level of guaranteed payments is managed to mitigate the level of risk that we bear in relation to the volatility of these classes of assets.

Non-UK participating business, annuities and non-participating contracts in all countries, have a high level of guaranteed future payments. We endeavour to match the investments held against these types of business to future cash flows. We therefore have a policy of generally holding fixed income securities and mortgage loans with appropriate maturity dates.

With unit-linked business, the primary objective is to maximise investment returns, subject to following an investment policy consistent with the representations that we have made to our unit-linked product policyholders.

General insurance and health business

The general insurance and health business is comprised of shorter-term liabilities than the long-term insurance business. Furthermore, all the risk attaching to the investments is borne by our shareholders. As a result, the investment portfolio held to cover general insurance liabilities contains a higher proportion of fixed income securities than the portfolio held to cover life insurance liabilities.

Property partnerships

As part of their investment strategy, the UK and certain European policyholder funds have invested in a number of property limited partnerships ("PLPs"), either directly or via property unit trusts ("PUTs"), through a mix of capital and loans. The nature of our involvement in property partnerships is set out in the second and third paragraphs of the Investment vehicles section of 'Financial Statements IFRS – Accounting policies – (D) Consolidation principles'. Property partnerships are accounted for as subsidiaries, joint ventures or financial investments depending on our participation and the terms of each partnership agreement. For each property partnership accounted for as a subsidiary, joint venture or financial investment, we are exposed to falls in the value of the underlying properties which are reflected as unrealised gains/losses on investment properties, our share of joint venture results and unrealised gains/losses on financial investments, respectively. However, the majority of these are in policyholder funds (rather than shareholder funds) so such losses are offset by changes in the amounts due to policyholders or unitholders, or UDS.

Analysis of investments

We distinguish between policyholder, participating fund and shareholder investments, which are terms used to reflect the differing exposure to investment gains and losses. Policyholder assets are connected to our unit-linked business, where the policyholder bears the investment risk on the assets in the unit-linked funds. Our exposure to loss on policyholder assets is limited to the extent that income arising from asset management charges is based on the value of assets in the funds. Participating fund assets relate to some of our insurance and investment contracts which contain a discretionary participation feature, which is a contractual right to receive additional benefits as a supplement to guaranteed benefits. Our exposure to investment losses on participating funds is generally limited to our participation in the fund. Shareholder assets are other assets held within our businesses that are not backing unit-linked liabilities or participating funds.

Investments held at 31 December 2012 and 31 December 2011 are listed below:

	Policyholder assets £m	Participating fund assets £m	Shareholder assets £m	Total assets analysed £m	Less assets of operations classified as held for sale £m	Carrying value in the statement of financial position £m
2012						
Investment property	4,172	6,079	582	10,833	(18)	10,815
Loans	605	5,562	21,767	27,934	(3,397)	24,537
Financial investments						
Debt securities	16,472	83,497	61,654	161,623	(33,617)	128,006
Equity securities	22,500	9,854	1,423	33,777	(1,248)	32,529
Other investments	23,704	4,258	2,131	30,093	(1,550)	28,543
Total	67,453	109,250	87,557	264,260	(39,830)	224,430
Total %	25.5%	41.3%	33.2%	100.0%		100.0%
2011	64,215	108,171	83,773	256,159	(347)	255,812
2011 %	25.1%	42.2%	32.7%	100.0%		100.0%

As the table indicates, approximately 33.2% of total investments can be directly attributed to shareholders. The apportionment of our shareholder assets is predominantly weighted towards debt securities and loans. In comparison, policyholder and participating funds contain a greater proportion of equities and other investments (e.g. unit trusts), reflecting the underlying investment mandates.

We carry investments on our statement of financial position at either fair value or amortised cost. At 31 December 2012, approximately 97% of the Group's total investments were carried at fair value on the statement of financial position.

Financial investment balances included in the remainder of these disclosures include financial investments of operations classified as held for sale. For more information about financial investments analysed according to their accounting classification and valuation approach, as well as the cost, unrealised gains and losses, impairments, fair value and other information concerning financial investments, see 'Financial statements IFRS – Note 25 – Financial investments'.

Debt securities

Participating fund asset and shareholder debt securities analysed by credit rating and sector

Participating fund asset and shareholder debt securities analysed by credit rating and product type as at 31 December 2012 are set out in the table below. Government and corporate debt securities are further analysed by type of issuer.

	Ratings						Total £m
	AAA £m	AA £m	A £m	BBB £m	Less than BBB £m	Non-rated £m	
2012 – Participating fund assets							
Government							
UK government	10,610	4	28	—	—	11	10,653
Non-UK government	6,779	11,830	1,677	10,471	833	10	31,600
Corporate							
Public utilities	18	93	1,712	1,012	20	17	2,872
Convertibles and bonds with warrants	—	—	21	284	4	19	328
Other corporate bonds	3,881	4,955	11,902	9,731	1,739	2,369	34,577
Certificate of deposits	—	6	42	12	614	—	674
Structured	307	58	132	47	39	1	584
Wrapped credit	—	57	12	22	2	—	93
Other	402	120	534	397	570	93	2,116
Total	21,997	17,123	16,060	21,976	3,821	2,520	83,497
Total %	26.3%	20.5%	19.2%	26.3%	4.6%	3.1%	100.0%
2011	30,540	11,204	24,004	9,786	1,465	2,451	79,450
2011 %	38.4%	14.1%	30.2%	12.3%	1.8%	3.2%	100.0%

2012 – Shareholder assets	Ratings						Total £m
	AAA £m	AA £m	A £m	BBB £m	Less than BBB £m	Non-rated £m	
Government							
UK government	3,251	81	4	—	—	197	3,533
Non-UK government	4,582	4,557	1,208	1,671	40	50	12,108
Corporate							
Public utilities	27	185	3,797	1,776	45	153	5,983
Convertibles and bonds with warrants	6	—	19	112	2	—	139
Other corporate bonds	1,349	3,143	12,250	11,577	1,394	4,885	34,598
Certificate of deposits	—	143	58	21	165	3	390
Structured	3,027	554	304	143	177	15	4,220
Wrapped credit	1	201	81	80	38	46	447
Other	45	13	59	44	63	12	236
Total	12,288	8,877	17,780	15,424	1,924	5,361	61,654
Total %	19.9%	14.4%	28.8%	25.0%	3.1%	8.8%	100.0%
2011	13,011	7,831	17,903	12,101	2,416	5,338	58,600
2011 %	22.2%	13.4%	30.6%	20.7%	4.1%	9.0%	100.0%

We grade debt securities according to external credit ratings issued at the balance sheet date. The credit rating used for each individual security is the median rating of the available ratings from the major credit rating agencies. If a credit rating is available from only one of these rating agencies then this rating is used. If an individual security has not been given a credit rating by any of the major rating agencies, the security is classified as 'non-rated'.

For the table above we have expressed our rating using a rating scale whereby investment grade debt securities are classified within the range of AAA (extremely strong) to BBB (good) ratings, with AAA being the highest possible rating. Debt securities which fall outside this range are classified as less than BBB. This rating scale is analogous with that used by major rating agencies.

At 31 December 2012, the proportion of our shareholder debt securities that are investment grade increased to 88.1% (2011: 86.9%). The remaining 11.9% of shareholder debt securities that do not have an external rating of BBB or higher can be split as follows:

- 3.1% are debt securities that are rated as below investment grade;
- 3.7% are US private placements which are not rated by the major rating agencies, but are rated as investment grade by the Securities Valuation Office of the National Association of Insurance Commissioners ("NAIC"), a US national regulatory agency; and,
- 5.1% are not rated by the major rating agencies or the NAIC.

Of the securities not rated by an external agency or NAIC most are allocated an internal rating using a methodology largely consistent with that adopted by an external rating agency, and are considered to be of investment grade credit quality; these include £2.4 billion of debt securities held in our UK Life business, predominantly made up of private placements and other corporate bonds, which have been internally rated as investment grade.

Total wrapped credit

In respect of the wrapped credit investments, the table below shows the credit rating of the securities as they are officially rated, and an estimate of their rating without the guarantee. As rating agencies do not provide credit ratings for individual wrapped credit securities without consideration of the insurance guarantee, the credit ratings disclosed in the table below are based on internal best estimates.

2012	2012						2011	
	Rating with insurance guarantee		Rating without insurance guarantee		Rating with insurance guarantee		Rating without insurance guarantee	
	Fair value £m	% of total	Fair value £m	% of total	Fair value £m	% of total	Fair value £m	% of total
Wrapped credit								
AAA	1	0.2%	—	0.0%	—	0.0%	—	0.0%
AA	269	48.3%	29	5.2%	292	43.8%	32	4.8%
A	94	16.8%	124	22.3%	127	19.0%	150	22.5%
BBB	104	18.7%	160	28.7%	131	19.6%	207	31.0%
Less than BBB	42	7.6%	43	7.7%	51	7.7%	51	7.7%
Non-rated	47	8.4%	186	33.4%	66	9.9%	214	32.1%
Not available without insurance guarantee	—	0.0%	15	2.7%	—	0.0%	13	1.9%
	557	100.0%	557	100.0%	667	100.0%	667	100.0%
RMBS agency								
AAA	907	100.0%	907	100.0%	1,378	100.0%	1,378	100.0%

Exposures to peripheral European countries

Included in our debt securities and other financial assets are exposures to peripheral European countries. All of these assets are valued on a mark to market basis under IAS 39, and therefore our statement of financial position and income statement already reflect any reduction in value between the date of purchase and the balance sheet date. The significant majority of these holdings are within our participating funds where the risk to our shareholders is governed by the nature and extent of our participation within those funds.

Net of non-controlling interests, our direct shareholder and participating fund asset exposure to the government (and local authorities and agencies) of Italy is £4.9 billion (2011: £6.4 billion), a decrease of £1.5 billion. Gross of non-controlling interests, 82% of our shareholder asset exposure to Italy arises from investment exposure of our Italian business.

Direct sovereign exposures to Greece, Ireland, Portugal, Italy and Spain (net of non-controlling interests, excluding policyholder assets)

	Participating		Shareholder		Total
	31 December 2012 £bn	31 December 2011 £bn	31 December 2012 £bn	31 December 2011 £bn	
Greece	—	—	—	—	—
Ireland	0.4	0.3	—	0.2	0.5
Portugal	0.3	0.2	—	—	0.2
Italy	4.5	5.6	0.4	0.8	6.4
Spain	0.9	0.8	0.5	0.3	1.1
Total Greece, Ireland, Portugal, Italy and Spain	6.1	6.9	0.9	1.3	8.2

Direct sovereign exposures to Greece, Ireland, Portugal, Italy and Spain (gross of non-controlling interests, excluding policyholder assets)

	Participating		Shareholder		Total
	31 December 2012 £bn	31 December 2011 £bn	31 December 2012 £bn	31 December 2011 £bn	
Greece	—	—	—	—	—
Ireland	0.4	0.4	—	0.2	0.6
Portugal	0.3	0.2	—	—	0.2
Italy	8.5	9.7	0.6	1.1	10.8
Spain	1.3	1.0	0.9	0.6	1.6
Total Greece, Ireland, Portugal, Italy and Spain	10.5	11.3	1.5	1.9	13.2

Equity securities

The table below analyses our investments in equity securities by sector.

2012	Policyholder £m	Participating £m	Shareholder £m	Total £m
Public utilities	2,571	1,095	18	3,684
Banks, trusts and insurance companies	3,904	2,395	959	7,258
Industrial, miscellaneous and all other	15,935	6,340	123	22,398
Non-redeemable preference shares	90	24	323	437
Total	22,500	9,854	1,423	33,777
Total %	66.6%	29.2%	4.2%	100.0%
2011	20,602	10,788	1,293	32,683
2011 %	63.0%	33.0%	4.0%	100.0%

At 31 December 2012, shareholder investment in equity securities amounted to £1,423 million. The investments include a strategic holding in Italian banks of £289 million (£148 million net of non-controlling interests).

Of our £7,258 million exposure to equity investments in banks, trusts and insurance companies, £959 million relates to shareholder investments, which includes our strategic holding as mentioned above.

Other investments

The table below analyses other investments by type.

2012	Policyholder £m	Participating £m	Shareholder £m	Total £m
Unit trusts and other investment vehicles	22,823	3,171	762	26,756
Derivative financial instruments	41	432	1,117	1,590
Deposits and credit institutions	515	44	180	739
Minority holdings in property management undertakings	14	555	15	584
Other	311	56	57	424
Total	23,704	4,258	2,131	30,093
Total %	78.8%	14.1%	7.1%	100.0%
2011	23,233	5,078	2,066	30,377
2011 %	76.5%	16.7%	6.8%	100.0%

Property

Our global headquarters are located in St. Helen's, 1 Undershaft, London, England, EC3P 3DQ. In addition, we have major offices in the following locations:

- UK: UK Life, York; UK General Insurance, Norwich; Aviva Investors, London;
- Asia: Singapore;
- North America: Scarborough, Ontario, Canada and West Des Moines, Iowa, USA; and
- Europe: Paris, France; Dublin, Ireland; Madrid, Spain; Warsaw, Poland; and Milan, Italy.

As of 31 December 2012, we owned and occupied land and buildings for our own use with a total book value of £245 million (2011: £215 million). We believe that these facilities are adequate for our present needs in all material respects. We also hold other properties, both directly and indirectly, for investment purposes, valued at £9,075 million at 31 December 2012 (2011: £9,848 million).

Contractual obligations

Contractual obligations

Contractual obligations with specified payment dates at 31 December 2012 included the following:

	Less than one year £m	Between one and three years £m	Between three and five years £m	After five years £m	Total £m
Insurance and investment contracts					
Long-term business					
— Insurance contracts – non-linked ¹	7,044	15,195	11,633	75,415	109,287
— Investment contracts – non-linked ²	57,547	—	—	—	57,547
— Linked business ²	66,099	—	—	—	66,099
General insurance ³	6,176	3,848	1,957	3,475	15,456
	136,866	19,043	13,590	78,890	248,389
Other contractual obligations ⁴					
Borrowings	1,699	921	1,686	12,409	16,715
Operating lease obligations	136	238	183	587	1,144
Capital commitments	21	18	3	—	42
Payables and other financial liabilities ⁵	8,567	289	345	1,606	10,807
Net asset value attributable to unitholders	11,146	—	—	—	11,146
Total	158,435	20,509	15,807	93,492	288,243

Reconciliation to the statement of financial position	£m
Total contractual obligations above	288,243
Effect of discounting contractual cash flows for insurance contracts	(24,804)
Contractual undiscounted interest payments ⁶	(7,910)
Difference between carrying value of borrowings and undiscounted cash flows of principal	(611)
Contractual cash flows under operating leases and capital commitments	(1,186)
Difference between derivative liabilities contractual cash flows and carrying value	(1,366)
Liabilities of operations classified as held for sale	41,411
Non-contractual/short-term obligations	
— Unallocated divisible surplus ⁷	6,931
— Provisions ⁸	1,119
— Current and deferred tax liabilities	659
— Other liabilities	1,843
Total liabilities per statement of financial position	304,329

- Amounts shown in respect of long-term insurance contracts represent estimated undiscounted cash flows for the Group's life assurance contracts. In determining the projected payments, account has been taken of the contract features, in particular that the amount and timing of the contractual payments reflect either surrender, death or contract maturity. In addition, the undiscounted amounts shown include the expected payments based on assumed future investment returns on assets backing insurance and investment contract liabilities. The projected cash flows exclude the unallocated divisible surplus of with-profits funds (see below).
- All linked contracts and almost all non-linked investment contracts may be surrendered or transferred on demand. For such contracts the earliest contractual maturity is therefore at the current statement of financial position date, for a surrender amount approximately equal to the current statement of financial position liability. Although we expect surrenders, transfers and maturities to occur over many years, the total liability for linked non-linked investment contracts is shown in the less than one year column above.
- Amounts shown in respect of general insurance contracts are based on undiscounted estimates of future claim payments, including for those classes of business for which discounted provisions are held, see 'Financial statements IFRS – Note 39 – Insurance liabilities'. The timing of cash flows reflects a best estimate of when claims will be settled.
- The Group has no material finance leases for property and equipment.
- Includes obligations for repayment of collateral received under stock lending arrangements and derivative transactions amounting to £4,460 million.
- When subordinated debt is undated or loan notes perpetual, the interest payments have not been included beyond 15 years. Annual interest payments for these borrowings are £72 million. Contractual undiscounted interest payments are calculated using fixed interest rates or prevailing market floating rates as applicable.
- The unallocated divisible surplus represents the excess of assets over liabilities, including policyholder 'asset share' liabilities in the UK, which reflect the amount payable under the realistic Peak 2 reporting regime of the FSA. Although accounted for as a liability, as permitted by IFRS 4, there is currently no expected payment date for the unallocated divisible surplus.
- Provisions include pension obligations, which have been excluded from the contractual obligations table above, due to the uncertainty of the amount and timing of future cash flows. The Group operates both funded defined benefit and funded defined contribution pension schemes, full details of which are provided in 'Financial Statements IFRS – Note 47 – Pension obligations'. We have a contractual obligation to fund these schemes. However, the amount and timing of the Group's cash contributions to these schemes is uncertain and will be affected by factors such as future investment returns and demographic changes. Our cash funding of defined contribution schemes is based on percentages of salary. Our cash contribution to defined benefit schemes is agreed in advance with scheme trustees. The Company and trustees have agreed to a long-term funding plan where contributions, together with anticipated growth on scheme investments are expected to eliminate the funding deficits over time. Contributions to these and the other schemes are regularly reviewed in light of changes in expectations of investment returns and other assumptions. The discounted scheme liabilities have an average duration of 20 years in the main UK scheme, 21 years in the RAC scheme, 22 years in the Irish scheme and 13 years in the Canadian scheme.

Risk management objectives

As a global insurance group, risk management is at the heart of what we do and is the source of value creation as well as a vital form of control. It is an integral part of maintaining financial stability for our customers, shareholders and other stakeholders.

Our sustainability and financial strength are underpinned by an effective risk management process which helps us identify major risks to which we may be exposed, establish appropriate controls and take mitigating actions for the benefit of our customers and investors. The Group's risk strategy is to invest its available capital to optimise the balance between return and risk whilst maintaining an appropriate level of economic (i.e. risk-based) capital and regulatory capital in accordance with our risk appetite. Consequently, our risk management objectives are to:

- Embed rigorous risk management throughout the business, based on setting clear risk appetites and staying within these;
- Allocate capital where it will make the highest returns on a risk-adjusted basis; and
- Meet the expectations of our customers, investors and regulators that we will maintain sufficient capital surpluses to meet our liabilities even if a number of extreme risks materialise.

Aviva's risk management framework has been designed and implemented to support these objectives. The key elements of our risk management framework comprise our risk appetite; risk governance, including risk policies and business standards, risk oversight committees and roles & responsibilities; and the processes we use to identify, measure, manage, monitor and report (IMMMR) risks, including the use of our risk models and stress and scenario testing. These elements are expanded in the Financial statements IFRS – Note 56.

Principal risks and uncertainties

In accordance with the requirements of the FSA Handbook (DTR 4.1.8) we provide a description of the principal risks and uncertainties facing the Group here and in note 56. Our disclosures covering 'risks relating to our business' in line with reporting requirements of the Securities Exchange Commission (SEC) provide more detail and can be found in the shareholder information section 'Risks relating to our business'.

Risk environment

Financial market conditions during 2012 were volatile although positive overall, benefiting from the expansionary monetary policies followed by central banks across a number of economies in the second half of the year. However, the continued political and economic uncertainty relating to the Eurozone combined with the high levels of debt in many western economies continues to act as a brake on economic growth and raises the likelihood of a low growth, low interest rate environment persisting for some time.

Reflecting the wider financial and economic conditions, both UK and international regulatory authorities have implemented, or are in the process of considering, enhanced regulatory requirements intended to prevent future crises arising or assure the stability of institutions under their supervision. A good example of this in the UK is the Prudential Regulatory Authority's (PRA) proposed focus on ensuring that firms have adequate resolution arrangements in place.

Further regulatory uncertainty arose from the ongoing discussions regarding the technical standards for, and the implementation date of, Solvency II. Aviva continues to actively participate in the development of Solvency II through key European industry working groups.

Risk profile

The types of risk to which the Group is exposed have not changed significantly over the year and remain credit, market, insurance, asset management, liquidity, operational and reputational risks as described in note 56 of the IFRS financial statements.

Reflecting Aviva's objective of building financial strength and reducing capital volatility, the Group has taken steps to amend its risk profile. These include a net sell down of approximately €3.6 billion (gross of minority interests) Italian government bonds, a reduction in credit exposure to European financial institutions and a move towards a more general reduction in credit risk predominantly achieved through the sale of the Group's US subsidiary (which remains subject to regulatory approval). Restrictions on non-domestic investment in sovereign and corporate debt from Greece, Ireland, Italy, Portugal and Spain remain in place and balance sheet volatility was further reduced through the sell down of Delta Lloyd in July 2012. As described in note 56, a number of foreign exchange rate, credit and equity hedges are also in place. The reduction in credit and equity exposure noted above also reflects a broader move towards a more balanced risk profile.

Subsequent to the year end, the Group has also taken action to improve its access to dividends from the Group's insurance and asset management businesses by undertaking a corporate restructuring whereby Aviva Group Holdings (AGH) has purchased from Aviva Insurance Limited (AIL) its interest in the majority of its overseas businesses. This purchase has been funded by intercompany loans. It is planned to pay down the intercompany loan balances over time, in addition to meeting the Groups normal operating expenses, taxes, interest on our external debt, dividends and repayment of maturing debt.

Going forward, the Groups focus is on fewer businesses as is reflected in the sale of Aviva's Czech Republic, Hungarian and Romanian life businesses, the sale of Aviva's interest in our Sri Lankan joint venture, our remaining stake in Delta Lloyd and the agreed sale of the US business, the Romanian pensions business, Aviva Russia, and our stake in the Malaysian joint venture CIMB. The process of exiting these non-core businesses will reduce the amount of the Group's capital employed in less economically profitable areas, decrease balance sheet volatility and required capital, and will allow capital to be re-employed in businesses that enhance the Group's return on risk based capital. Execution risk is inherent in the completion of all strategic transactions, with a corresponding potential impact on capital requirements and liquidity.

As a result of the sale of businesses (in particular the US), the Group's future earnings have been reduced and the tangible net asset value of the Group has fallen (leading to an increase in the leverage ratio to close to 50%). We have plans in place to improve earnings through managing the deployment of capital to maximise return and expense reduction (though clearly execution risk remains). These additional earnings, combined with higher retained profits, should enable us to reduce our external leverage ratio to 40% in the medium term and reduce internal leverage.

Capital management

Capital management objectives

The primary objective of capital management is to optimise the balance between return and risk, whilst maintaining economic and regulatory capital in accordance with risk appetite. Aviva's capital and risk management objectives are closely interlinked, and support the dividend policy and earnings per share growth, whilst also recognising the critical importance of protecting policyholder and other stakeholder interests.

Overall capital risk appetite, which is reviewed and approved by the Aviva Board, is set and managed with reference to the requirements of a range of different stakeholders including shareholders, policyholders, regulators and rating agencies. Risk appetite is expressed in relation to a number of key capital and risk measures, and includes an economic capital risk appetite of holding sufficient capital resources to enable the Group to meet

its liabilities in extreme adverse scenarios, on an ongoing basis, calibrated at a level consistent with a AA range credit rating. In managing capital we seek to:

- maintain sufficient, but not excessive, financial strength in accordance with risk appetite, to support new business growth and satisfy the requirements of our regulators and other stakeholders giving both our customers and shareholders assurance of our financial strength;
- optimise our overall debt to equity structure to enhance our returns to shareholders, subject to our capital risk appetite and balancing the requirements of the range of stakeholders;
- retain financial flexibility by maintaining strong liquidity, including significant unutilised committed credit facilities and access to a range of capital markets;
- allocate capital rigorously across the Group, to drive value adding growth through optimising risk and return; and
- declare dividends with reference to factors including growth in cash flows and earnings.

In line with these objectives, the capital generated and invested by the Group's businesses is a key management focus. Operating capital generation, which measures net capital generated after taking into account capital invested in new business (before the impact of non-operating items) is a core regulatory capital based management performance metric used across the Group. This is embedded in the Group's business planning process and other primary internal performance and management information processes.

Capital is measured and managed on a number of different bases. These are discussed further in the following sections.

Accounting basis:

Capital employed by segment and financing of capital

The table below shows how our capital, on an MCEV basis²⁶, is deployed by segment and how that capital is funded.

	2012 £m	2011 £m
Long-term savings	16,337	14,148
General insurance and health	6,089	5,875
Fund management	225	184
Other business	(1,059)	(1,102)
Corporate ¹	(588)	508
Delta Lloyd	—	776
United States	365	361
Total capital employed	21,369	20,750
Financed by:		
Equity shareholders' funds	12,434	12,829
Non-controlling interests	2,214	1,476
Direct capital instruments and fixed rate tier 1 notes	1,382	990
Preference shares	200	200
Subordinated debt	4,337	4,550
External debt	802	705
Total capital employed	21,369	20,750

¹ 'Corporate' includes centrally held tangible net assets, the staff pension scheme surplus and also reflects internal lending arrangements. These internal lending arrangements, which net out on consolidation, arise in relation to the following:

- Aviva Insurance Limited (AI) acts as both a UK general insurer and as the primary holding company for our foreign subsidiaries. Internal capital management mechanisms in place allocate a portion of the total capital of the company to the UK general insurance operations, giving rise to notional lending between the general insurance and holding company activities. These mechanisms also allow for some of the assets of the general insurance business to be made available for use across the Group.
- Subsequent to the year end, the Group has taken action to improve its access to dividends from the Group's insurance and asset management business by undertaking a corporate restructure. This will see the Group's interest in the majority of its overseas businesses move to Aviva Group Holdings Limited from Aviva Insurance Limited.
- Certain subsidiaries, subject to continuing to satisfy stand-alone capital and liquidity requirements, loan funds to corporate and holding entities. These loans satisfy arm's length criteria and all interest payments are made when due.

Total capital employed is financed by a combination of equity shareholders' funds, preference capital, subordinated debt and borrowings.

At 2012 we had £21.4 billion (2011: £20.8 billion) of total capital employed in our trading operations measured on an MCEV basis.

In May 2012 we issued US\$650 million of Fixed Rate Tier 1 Notes. The Notes are perpetual and may be called from November 2017. The Notes qualify as Innovative Tier 1 capital under current regulatory rules and are expected to be treated as Fixed Rate Tier 1 capital under Solvency II transitional rules. The transaction had a positive impact on Group IGD solvency and Economic Capital measures. In June 2012 US\$300 million of Lower Tier 2 floating rate notes were redeemed at first call.

Financial leverage, the ratio of external senior and subordinated debt to MCEV capital and reserves, was 35.1% (2011: 36.7%). Fixed charge cover, which measures the extent to which external interest costs, including subordinated debt interest and preference dividends, are covered by MCEV operating profit was 5.1 times (2011: 8.9 times). The impact of the agreement to sell Aviva USA has meant that financial leverage under IFRS is higher at 52.6% (FY11: 37.1%).

Regulatory capital – overview

Individual regulated subsidiaries measure and report solvency based on applicable local regulations, including in the UK the regulations established by the Financial Services Authority (FSA). These measures are also consolidated under the European Insurance Groups Directive (IGD) to calculate regulatory capital adequacy at an aggregate Group level, where we have a regulatory obligation to have a positive position at all times. This measure represents the excess of the aggregate value of regulatory capital employed in our business over the aggregate minimum solvency requirements imposed by local regulators, excluding the surplus held in the UK and Ireland with-profit life funds. The minimum solvency requirement for our European businesses is based on the Solvency 1 Directive. In broad terms, for EU operations, this is set at 4% and 1% of non-linked and unit-linked life reserves respectively and for our general insurance portfolio of business is the higher of 18% of gross premiums or 26% of gross claims, in both cases adjusted to reflect the level of reinsurance recoveries. For our major non-European businesses (the US and Canada) a risk charge on assets and liabilities approach is used.

Regulatory capital – Group European Insurance Groups Directive

	UK Life funds £bn	Other business £bn	2012 £bn	2011 £bn
Insurance Groups Directive (IGD) capital resources	5.2	9.2	14.4	14.1
Less: capital resource requirement (CRR)	(5.2)	(5.4)	(10.6)	(11.9)
Insurance Groups Directive (IGD) excess solvency	—	3.8	3.8	2.2
Cover of EU minimum (calculated excluding UK Life funds)			1.7 times	1.3 times

²⁶ MCEV: market consistent embedded value: In preparing the MCEV information, the directors have done so in accordance with the MCEV principles with the exception of stating held for sale operations at their expected fair value, as represented by expected sale proceeds, less cost to sell.

The EU Insurance Groups Directive (IGD) regulatory capital solvency surplus has increased by £1.6 billion since 31 December 2011 to £3.8 billion. The key movements over the period are set out in the following table:

	£bn
IGD solvency surplus at 31 December 2011	2.2
Operating profits net of other income and expenses	0.9
Dividend and appropriations, net of shares issued in lieu of dividends	(0.7)
Market movements including foreign exchange ¹	1.3
Pension scheme funding	(0.2)
Movement in hybrid debt	0.2
UK reinsurance transactions	0.1
Increase in Capital Resources Requirement	(0.1)
Other regulatory adjustments	0.1
Estimated IGD solvency surplus at 31 December 2012	3.8

¹ Market movements include the impact of equity, credit spread, interest rate and foreign exchange movements net of the effect of hedging instruments.

Regulatory capital – UK Life with-profits fund

The available capital of the with-profits funds is represented by the realistic inherited estate. The estate represents the assets of the long-term with-profits funds less the realistic liabilities for non-profit policies within the funds, less asset shares aggregated across the with-profits policies and any additional amounts expected at the valuation date to be paid to in-force policyholders in the future in respect of smoothing costs, guarantees and promises. Realistic balance sheet information is shown below for the three main UK with-profit funds: Old With-Profit Sub-Fund (OWPSF), New With-Profit Sub-Fund (NWPSF) and With-Profit Sub-Fund (WPSF). These realistic liabilities have been included within the long-term business provision and the liability for insurance and investment contracts on the consolidated IFRS statement of financial position at 31 December 2012 and 31 December 2011.

	Estimated realistic assets £bn	Estimated realistic liabilities ¹ £bn	Estimated realistic inherited estate ² £bn	Capital support arrangement ³ £bn	Estimated risk capital margin £bn	2012 Estimated excess available capital £bn	2011 Estimated excess available capital £bn
NWPSF	17.3	(17.3)	—	0.7	(0.4)	0.3	0.7
OWPSF	2.9	(2.6)	0.3	—	(0.1)	0.2	0.2
WPSF ⁴	18.3	(16.5)	1.8	—	(0.5)	1.3	1.0
Aggregate	38.5	(36.4)	2.1	0.7	(1.0)	1.8	1.9

¹ These realistic liabilities include the shareholders' share of future bonuses of £0.3 billion (31 December 2011: £0.3 billion). Realistic liabilities adjusted to eliminate the shareholders' share of future bonuses are £36.0 billion (31 December 2011: £38.8 billion). These realistic liabilities make provision for guarantees, options and promises on a market consistent stochastic basis. The value of the provision included within realistic liabilities is £1.8 billion, £0.3 billion and £3.5 billion for NWPSF, OWPSF and WPSF respectively (31 December 2011: £1.9 billion, £0.3 billion and £3.1 billion for NWPSF, OWPSF and WPSF respectively).

² Estimated realistic inherited estate at 31 December 2011 was £nil, £0.3 billion and £1.6 billion for NWPSF, OWPSF and WPSF respectively.

³ This represents the reattributed estate of £0.7 billion at 31 December 2012 (31 December 2011: £1.1 billion) held within NPSF1 (a non-profit fund within UKLAP included within other UK life operations).

⁴ The WPSF fund includes the Provident Mutual (PM) fund, which has realistic assets and liabilities of £1.7 billion and therefore does not impact the realistic inherited estate.

Investment mix

The aggregate investment mix of the assets in the three main with-profits funds at 31 December 2012 was:

	2012 %	2011 %
Equity	23%	22%
Property	16%	17%
Fixed interest	51%	54%
Other	10%	7%

The equity backing ratios, including property, supporting with-profit asset shares are 71% in NWPSF and OWPSF, and 64% in WPSF.

Economic capital

We use a risk-based capital model to assess economic capital requirements and to aid in risk and capital management across the Group. The model is based on a framework for identifying the risks to which business units, and the Group as a whole, are exposed. Where appropriate, businesses also supplement these with additional risk models and stressed scenarios specific to their own risk profile. When aggregating capital requirements at

business unit and Group level, we allow for diversification benefits between risks and between businesses, with restrictions to allow for non-fungibility of capital where appropriate. This means that the aggregate capital requirement is less than the sum of capital required to cover all of the individual risks. The capital requirement reflects the cost of mitigating the risk of insolvency to a 99.5% confidence level over a one year time horizon (equivalent to events occurring in 1 out of 200 years) against financial and non-financial tests.

The financial modelling techniques employed in economic capital enhance our practice of risk and capital management. They enable understanding of the impact of the interaction of different risks allowing us to direct risk management activities appropriately. These same techniques are employed to enhance product pricing and capital allocation processes. Unlike more traditional regulatory capital measures, economic capital also recognises the value of longer-term profits emerging from in-force and new business, allowing for consideration of longer-term value emergence as well as shorter-term net worth volatility in our risk and capital management processes. We continue to develop our economic capital modelling capability for all our businesses as part of our development programme to increase the focus on economic capital management and meeting the emerging requirements of the Solvency II framework and external agencies.

Solvency II

The development of Solvency II continues in 2012 with a view to complete discussions about legislation. The key priority is concluding the discussions on the Omnibus II directive to provide clarity about the implementation date as well as the role of transitionals in the Level 2. Once this is concluded we expect the European Commission to complete the development of the Level 2 implementing measures that will establish the technical requirements governing the practical application of Solvency II. Aviva continues to actively participate in these developments through the key European industry working groups and by engaging with the FSA and HM Treasury to inform the ongoing negotiations in Brussels.

Rating agency

Credit ratings are an important indicator of financial strength and support access to debt markets as well as providing assurance to business partners and policyholders over our ability to service contractual obligations. In recognition of this we have solicited relationships with a number of rating agencies. The agencies generally assign ratings based on an assessment of a range of financial factors (e.g. capital strength, gearing, liquidity and fixed charge cover ratios) and non-financial factors (e.g. strategy, competitive position, and quality of management).

Certain rating agencies have proprietary capital models which they use to assess available capital resources against capital requirements as a component in their overall criteria for assigning ratings. Managing our capital and liquidity position in accordance with our target rating levels is a core consideration in all material capital management and capital allocation decisions.

The Group's overall financial strength is reflected in our credit ratings. The Group's rating from Standard and Poor's is A+ ("strong") with a Stable outlook; Aa3 ("excellent") with a Negative outlook from Moody's; and A ("excellent") with a Stable outlook from A.M. Best.

Financial flexibility

The Group's borrowings are comprised primarily of long dated hybrid instruments with maturities spread over many years, minimising refinancing risk. In addition to central liquid asset holdings of £1.4 billion, the majority of which was held within Aviva Insurance Limited at the 2012 year end, the Group also has access to unutilised committed credit facilities of £2.1 billion provided by a range of leading international banks.

Capital generation and utilisation

The active management of the generation and utilisation of capital is a primary Group focus, with the balancing of new business investment and shareholder distribution with operating capital generation a key financial priority.

Operating capital generation for the full-year 2012 was £2.0 billion. Life business generated £2.1 billion of capital (2011: £2.3 billion), with a further £0.6 billion (2011: £0.6 billion) generated by the general insurance and fund management businesses and other operations. Capital invested in new business was £0.7 billion (2011: £0.8 billion), and continues to benefit from management actions to improve capital efficiency. The £0.7 billion of capital investment is primarily in life new business with the impact of capital investment in non-life business broadly neutral over the period.

	2012 £bn	2011 £bn
Operating capital generation:		
Life in-force profits ¹	2.1	2.3
General insurance, fund management and non-insurance profits	0.6	0.6
Operating capital generation before investment in new business	2.7	2.9
Capital invested in new business	(0.7)	(0.8)
Operating capital generation after investment in new business	2.0	2.1

¹ The Life in-force profits in 2012 exclude the negative impact of a true up relating to a prior estimate of required capital, which is included in the MCEV Free Surplus Emergence, as this does not impact the actual capital generated in 2012.

Operating capital generation comprises the following components:

- Operating Free surplus emergence, including release of required capital, for the life in-force business (net of tax and non-controlling interests);
- Operating profits for the general insurance and non-life businesses (net of tax and non-controlling interests);
- Capital invested in new business. For life business this is the impact of initial and required capital on free surplus. For general insurance business this reflects the movement in required capital, which has been assumed to equal the regulatory minimum multiplied by the local management target level. Where appropriate movements in capital requirements exclude the impact of foreign exchange and other movements deemed to be non-operating in nature.
- Post disposal on 6 May 2011, all Delta Lloyd capital generation, including life business, has been included within general insurance, fund management and other operations profits on an IFRS basis.

The amount of operating capital remitted to Group is dependent upon a number of factors including non-operating items and local regulatory requirements.

As well as financing new business investment, the operating capital generated is used to finance corporate costs, service the Group's debt capital and to finance shareholder dividend distributions. After taking these items into account the net operating capital generated after financing is £0.5 billion.

	2012 £bn	2011 £bn
Operating capital generation after investment in new business	2.0	2.1
Interest, corporate and other costs	(0.8)	(0.6)
External dividend net of scrip	(0.7)	(0.5)
Net operating capital generation after financing	0.5	1.0

Basis of preparation

Basis of preparation

This review complies with the recommendations of the European Union ("EU") Modernisation Directive, the Companies Act 2006 (Contents of Directors' Report: Business Review) and is in line with current best practice. It is addressed to, and written for, the members of Aviva plc with the aim of providing a fair review of our business development, performance and position at the current time. In producing this review, we aim to present a view that is balanced and comprehensive and that is consistent with the size and complexity of our business. The review is written in the context of the risks and uncertainties facing our business. We anticipate that the format and content of the review will evolve over time, along with developments in our business and the external environment.

Key performance indicators

The Companies Act requires that a fair review of the business contains financial and, where applicable, non-financial key performance indicators ("KPIs"). We consider that our financial KPIs are those that communicate to the members the financial performance and strength of the Group as a whole.

These KPIs comprise:

- adjusted operating profit, before and after integration and restructuring costs;
- IFRS profit/loss after tax;
- life internal rate of return
- general insurance combined operating ratio
- economic capital surplus;
- net operating capital generation; and
- return on equity shareholders funds.

Management also use a variety of other performance indicators ("OPIs") in both running and assessing the performance of individual business segments and units, rather than the Group as a whole. OPIs include measures such as new business margin and value of new business.

In addition to reporting on our financial performance, it is important that as a forward-thinking company we are aware of our wider responsibilities and report on the non-financial aspects of our performance. We consider that our employees and customers are fundamental to the success of our business; as such, they form the basis for our non-financial measures, and include:

- employee engagement and leadership; and
- customer advocacy.

Accounting basis of preparation

In addition to presenting our results and financial position on an International Financial Reporting Standards basis, we also use non-GAAP measures based on Market Consistent Embedded Value principles²⁷. Further details of non-GAAP measures are given in the section Performance Review – Financial and Operating Performance.

Details of the accounting basis of preparation including critical accounting policies and estimates are set out in Financial Statements – Accounting Policies.

Forward-looking statements

This business review contains 'forward-looking statements' about:

- our future plans;
- our current goals; and
- our expectations of our future financial condition, performance and results.

By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events that are beyond our control. For example, certain insurance risk disclosures are dependent on our choices about assumptions and models, which by their nature are estimates. As such, actual future gains and losses could differ materially from those that we have estimated. Other factors that could cause actual results to differ materially from those estimated by the forward-looking statements include, but are not limited to:

- global economic business conditions;
- monetary and interest rate policies;
- foreign currency exchange rates;
- equity and property prices;
- the impact of competition, inflation and deflation;
- changes to regulations, taxes and legislation;
- the timing and impact of acquisitions and business combinations in relevant industries;
- natural and other disasters;
- changes to consumer saving and spending habits; and
- our success in managing the above factors.

Consequently, our actual future financial condition, performance and results of operation could differ materially from the plans, goals and expectations set out in our forward-looking statements. We undertake no obligation to update the forward-looking statements contained in this review or any other forward-looking statements we make.

Longer-term investment return

The long-term nature of most of our operations means that short-term realised and unrealised gains and losses are shown as an adjustment to operating profit. We focus instead on operating profit incorporating a longer-term investment return ("LTIR"). The rates of return that we use for equity and property in our LTIR methodology are aligned with the rates that we use under MCEV²⁷ principles. For fixed interest securities, we include the amortisation of premiums or discounts arising on purchase, thereby producing an LTIR that is equivalent to the gross redemption yield.

Future accounting developments

We continue to take an active role in the development of new accounting standards, via industry forums and working parties, and reviewing and providing comment on proposals from the IASB. Phase II of the IASB's project on insurance contracts continues to be the most significant area of development for us alongside the ongoing project to revise accounting for financial instruments (IFRS 9), given the important interaction between the two. We fully support the timely development of global standards for both insurance contract accounting and financial instruments that reflect the economics of our business, and continue actively to engage in the debate, working directly and through the CFO Forum of leading European insurers to achieve this. We continue to monitor other major IASB projects, including revenue recognition and leasing.

²⁷ MCEV: market consistent embedded value: In preparing the MCEV information, the directors have done so in accordance with the MCEV principles with the exception of stating held for sale operations at their expected fair value, as represented by expected sale proceeds, less cost to sell.

Corporate responsibility

In this section

2012 Highlights	62
Our corporate responsibility strategy	62
Trust and transparency	64
Attracting and retaining talent	66
Community development	67
Climate change and environment	68
Key indicators	70
Accounting for Sustainability	72
Indices and benchmarks	75
Independent Assurance Report	76

Corporate responsibility

Aviva aims to be trusted, respected, sustainable and recognised for making a real contribution to society. Our corporate responsibility strategy supports these aims. Providing peace of mind is our social purpose and central to our overall business strategy. Aviva recognises, as an insurer that we have a fundamental part to play in society in enabling business growth, by providing protection and in tackling global issues such as climate change. In this report we highlight how we are addressing the issues that are material to our business and help us address issues in society as a whole. We focus on trust and transparency, attracting and retaining talent, environment and climate change, and community development. The report that follows contains a summary of the progress and performance of our corporate responsibility strategy, aligned to these material issues, in 2012. A more detailed review is available online at www.aviva.com/corporate-responsibility/reports

The highlights below are directly related to our key performance indicators and give a snapshot of our performance during 2012.

Highlights from 2012 include:

- Helped over 649,000 children since 2009 through our Street to School campaign.
- Community investment of £11 million including cash, in kind donations, and skills based volunteering.
- One of the top 4 global organisations in the FTSE4Good, Silver in the DJSI SAM Yearbook, and ranked 32nd in the Stonewall equality index.
- Maintained employee engagement at 68%, increased employee pride by 3% to 75%.
- Reduced our carbon footprint by 12% on a relative basis.

Our corporate responsibility strategy

Our business of insurance has underpinned the development of market economies, enabling business growth and building more resilience into people's lives. In addition to the social benefits of increased insurance penetration we seek to deepen our impact on society through the way we invest the talent of our people, as well as financial resources.

Aviva's approach to corporate responsibility is a key pillar of our business strategy. It underwrites our ability to deliver on our promises to our customers and to extend the positive contribution we make to society. As a responsible corporation we deal with matters in society relevant to our business. We therefore focus on:

- being trusted and transparent; demonstrating our sustainability to our stakeholders
- attracting and retaining the right people by creating a work environment that inspires pride and that enables people to give of their best
- controlling our environmental and climate impacts and influencing the actions of others
- acting responsibly in our communities, considering the impact of what we do

During 2012 we have considered our material issues and our strategy through the lens of our key stakeholder groups. We understand that;

- To be the most recommended insurer – customers tell us our values are key. We must demonstrate responsibility and integrity, sharing our social purpose and the information they need to enable them to make the right choices
- To be an investment of choice – investors tell us that companies with transparent and well managed environmental, social and governance (ESG) issues deliver higher performance
- To be the employer of choice for our people – employees tell us that if we create an environment where they feel they can make a difference, can thrive and be proud of what we stand for then they are more likely to deliver high performance, exceptional customer service and develop their career with us
- To be a partner of choice, with superior service, responsiveness and innovation – partners tell us to keep influencing product and service design to encourage customer behaviour change, in a way that demonstrates we are experts at managing risk

We believe that when corporate responsibility is embedded in the business, it drives trust and gives a sustainable competitive advantage, creating differentiation and market penetration.

During 2012 we have continued our journey towards truly embedded corporate responsibility. In the execution of our strategy we seek to enable the whole Aviva business to embed sustainability considerations into business strategy, processes, products and services and the way we manage risk.

Our corporate responsibility strategy is underpinned by a globally consistent corporate responsibility Business Standard. We have continued the roll out of our framework and tools to equip the business and unlock innovation in a sustainable way. Finally, we have created a new structure with an enhanced role for corporate responsibility business partners to work even more closely with the leadership of our markets and functions. These things help all of us at Aviva to turn this strategy into meaningful action and the kind of socially and commercially valuable outcomes described in this report.



FTSE4Good

Opportunities during 2013

As the transformation of Aviva continues we will focus on the contribution corporate responsibility can make to building the company's financial strength and resilience, reducing risk and volatility, and improving earnings performance.

Aviva's focus on core business and high performance has been helpful in setting our 2013 corporate responsibility strategy. Whilst our material issues remain unchanged we have refreshed our priorities to make sure all our activity is aligned to the business strategy. This means ensuring robust risk management and compliance, protecting the progress and leadership we have delivered and focusing investment on programmes that create maximum measurable shared value for our stakeholders. It also means paying attention to how we can deliver these outcomes in the most efficient and effective way in our capital constrained markets.

These developments have strengthened our commitment to the embedding of sustainability across the business as core to the way we do business.

As we shape our business for long-term success we are also conscious of the value our expertise can bring within the wider debate. We remain committed to taking a lead role where appropriate and to learn from and collaborate with others as we seek a secure and sustainable future for all.

We aspire to upper-quartile performance for financial services in our employee promise survey, notably in those areas that relate to leadership and engagement. This year, following significant organisational change, we did not meet our target. We recognise the need to focus our attention on this in 2013 and remain committed to our aspirations.

Governance

Aviva has a well-established governance structure providing strong leadership and direction. Our Corporate Responsibility Committee is chaired by non-executive director, Gay Huey Evans, and comprises two other non-executive directors, Scott Wheway and Euleen Goh. Ms Goh retired at the end of 2012.

The Committee reviews strategy and policy, receives market and functional reports four times a year and approves this report. In 2012, it received a report from all market groups and paid close attention to the embedding environmental, social and governance issues into our mainstream investment practices as well as our policy against investing in cluster munitions manufacturers. The Committee also received reports from the IT and procurement teams, as well as reviewing the health, safety and wellbeing strategy. The Corporate Responsibility Committee's report can be found on page 103.

The Aviva Board receives both annual and ad hoc updates on corporate responsibility strategy, activities and progress. Our corporate responsibility programme is regularly on the agenda at executive management committees. The group and market CEOs have corporate responsibility key performance indicators included in their role profiles. 10% of all senior managers' bonuses are targeted on leadership and engagement Employee Promise Survey scores.

Stakeholder communications and engagement

Open dialogue with our stakeholders helps us to define priorities and shape our approach. By being open and transparent about what we do and how we run our business we believe we demonstrate a high degree of integrity. This in turn, helps the process of continuing to build trust in Aviva for all of our stakeholders. We report here about our engagement with investors and governments, as well as our senior leadership participation on external forums. Engagement with our employees is discussed under Attracting and retaining talent, and our customer engagement is covered in our Customer section.

Key to this is the way that we report our corporate responsibility commitments and performance. We prepare stand-alone detailed annual reports for the Carbon Disclosure Project, UN Global Compact, ClimateWise, and Principles for Responsible Investment. As well as providing a narrative corporate responsibility report we prepare an Accounting for Sustainability statement using the Connected Reporting Framework to demonstrate the costs associated with our energy, natural resource use and waste management. We also use this statement to demonstrate the financial impacts of our community investment and customer advocacy commitments. The Accounting for Sustainability statement is provided on page 72.

We are committed to providing full disclosure to investors and as such respond to EIRIS, SAM, Sustainalytics and Vigeo for inclusion in the FTSE4Good, Dow Jones Sustainability Indices, Ethibel and ECPI indices. This year we have again been ranked as one of the top four companies in the FTSE4Good ESG ratings. We hold a similarly high position in the STOXX ESG Global Leaders index.

As a large investor we engage with companies to promote transparent and effective governance and engagement among the companies we invest in. We have supported the development of good governance in the UK and beyond for many years, and we take our own stewardship responsibilities seriously, complying with all the principles of the Financial Reporting Council's UK Stewardship Code. In particular, we use proxy voting to challenge poor management approaches and to protect the value of investments. While we aim to support the companies we invest in, we intervene strongly where we believe more sustainable practices should be implemented.

We know that our investors want us to be open and clear about our future strategy. We believe this includes commentary on our sustainability practices, which aims to help us become the most trusted, respected and sustainable insurance company, recognised for making a real contribution to society. We encourage companies, especially publicly listed and large companies, to consider integrating sustainability information into their reporting cycle. We encourage industry, interested governments and relevant stakeholders with the support of the United Nations system, as appropriate, to develop models for best practice and facilitate action for the integration of sustainability reporting. Aviva has shown longstanding leadership within Principles for Responsible Investment (PRI), where Paul Abberley sits on the Advisory Council, and Sustainable Stock Markets. In addition Aviva provided a significant contribution to the UN Global Compact input and recommendations for the Rio+20 Summit regarding sustainability reporting. The Aviva convened Corporate Sustainability Reporting Coalition were successful in securing text in the outcome document and are now keen to continue UN collaboration to see implementation.

We believe that collaboration with international partners and our peers is vital to progress the issues of business and society today. This year we have helped to develop the UN Principles for Sustainable Insurance and co-sponsored a publication on the rights of children working and/or living on the street. Our senior leaders continue to be represented on industry and global forums. We have advanced our work with the Chief Risk Officer (CRO) Forum, represented by John Lister, chief risk and capital officer, raising awareness within the industry of sustainability challenges and reputational risks related to cluster munitions and oil sands.

Following the Davies review, chief marketing and communications officer, Amanda Mackenzie has continued to engage in the debate on women on Boards. In December she took part in a round table discussion in Brussels with Commissioner Reading and MEPs. Our Chairman John McFarlane is part of the City UK advisory board which seeks to increase trust in financial services. We have senior level representation at the CBI with our Chairman sitting on the Presidents Committee and CEO of Aviva Investors on the Infrastructure Committee. We are also pleased to have been able to support the Prime Minister's Dementia Challenge Champion Group during the year.

As a long-term business, we help Governments tackle some of their key issues – fiscal, demographic, the savings gap, and infrastructure. We have continued to engage closely with governments this year, sharing our insight as both the owner and investor of capital, giving a useful double perspective to aid their public policy development. Specifically we have responded to:

- The House of Lords EU Select Committee B inquiry on Women on Boards
- The Environmental Audit Committee Inquiry into the outcomes of the Rio+20 Earth Summit
- The Business, Innovation and Skills Select Committee inquiry into Corporate Long-termism and the equity markets
- The European Commission's Rio outcomes consultation – Ensuring Sustainable Development Globally: EU Follow-Up to Rio+20

We continue to engage with policy makers on major issues facing society such as the ageing society and corporate sustainability in Westminster and Brussels.

In addition to these consultations we have engaged with MPs on the Street to School programme with our UK partner Railway Children to raise awareness of children at risk on our streets in the UK and have attended several meetings with Education Ministers to support their public policy outreach. In February we co-launched research in the House of Commons on the effectiveness of Railway Children's REACH model.

Trust and transparency

Building and maintaining trust in Aviva by our customers, our business partners, suppliers, shareholders and employees, is of prime importance within a sector that sees some of the lowest levels of trust in society.

We know trust is partly determined by the social purpose that the organisation demonstrates through the communication of its brand and the way it runs its business. People want a relationship with an organisation that they trust will do what they say they will. That's why providing peace of mind and the much needed support during the most difficult and challenging times in our customers lives is important to us.

Our customers

At Aviva we recognise that we carry a huge responsibility. We're the people our customers turn to for the big things in life; planning retirement, securing investments, an accident, an illness, even a death in the family. They're often unsure of what to do, confused, stressed, even frightened about what the future might hold. At Aviva we pride ourselves on doing all that we can to help, both in the services we offer, and in the way in which we offer them. We need to give them every bit of support and reassurance that we can. We can act quickly and decisively when the situation demands it or we can allow our customers time and space if that's what they prefer. Either way, we respond with sensitivity and empathy, and we know that just a friendly word can mean a lot. They may seem like little things, but we believe they're little things that can make a big difference.

Customer research

As the leading insurer in the UK with a significant international market presence we are actively involved in the issues facing the insurance market. We engage in broad ranging research and discussion topics with consumers, our industry bodies, the Financial Services Authority (FSA) and governmental stakeholders. This year we have published reports into three main areas, family finances, real retirement, and the pensions gap. In addition to this we have led discussion and published research on behavioural economics, the open market option and workplace savings. We continue to work to understand the perceptions and needs in our markets.

Once again we have conducted our wide-ranging Aviva Customer Attitudes survey – now running for over nine years, in 25 countries, asking more than 220,000 people what they think about risk, savings, retirement, financial advice and other important issues. By listening carefully to what consumers tell us, and responding quickly and effectively to meet their needs we can build better, more trusting, relationships with customers. The latest results show that consumers remain cautious about the general economic situation and are nervous about taking high levels of risk, for example:

- 43% of people think that the general economic situation in their country will get worse in the next 12 months
- 26% of people globally are relying on their savings to live day by day
- 28% agree that they have enough savings/investments to cope with the unexpected
- 57% state that they are worried that they won't have enough money when they retire to provide an adequate standard of living
- 25% have not considered or do not know how much monthly income they will need to get by/survive in retirement

We also take time to listen to our own customers through our Net Promoter Score® (NPS) survey, our leading, group-wide measure of customer advocacy, measured and benchmarked twice a year. This survey drives annual action planning, ensuring we act on what we learn, as well as being a constituent of our executive directors' annual remuneration.

We followed up our 2011 Mind the Gap report with research that shows consumers appear to be in denial over retirement planning with UK and US the most likely to not know how much or have not considered how much income they will need in retirement. We also found that India, China and Singapore have the highest proportion of consumers wanting to continue working beyond retirement whilst France, UK and Italy have the lowest proportion wanting to work beyond retirement age. We understand the implications for our business and industry and continue to engage with governments and consumer societies to improve uptake of savings. Indeed in Spain, The Experts' Forum of the Aviva Savings and Pensions Institute has recommended that the Government introduce reforms in taxation on long-term savings and pensions products to encourage people to save for their retirement. Further, our call to action for governments following our research is to:

- Engage people by providing annual statements to all citizens showing a forecast of pension retirement income from all sources, all in one place
- Empower people with an interactive tool (such as a pension calculator) demonstrating how saving more earlier in life can improve their retirement income

Our Family finances report shows the typical UK family could afford to save an extra £53 a month however, saving is not top of families' priority lists. While most families admit they could put something extra aside, their savings experience tends to be more "as and when" rather than a conscious part of their regular financial planning.

Please see <http://www.aviva.com/research-and-discussion/>

Business ethics

We aspire to the highest standards of conduct and set out our principles in our business ethics code. This stipulates fairness, honesty and transparency in all we do. The Code is one of the tools we have to remind all employees of the behaviour expected which in turn drives the culture at Aviva. Employees in all countries in which we operate are required to uphold the laws of the host country and to conduct themselves according to the business ethics code. Everyone at Aviva has a part to play in upholding our standards and we raise awareness of these responsibilities through our induction programmes. The Code is made available to all employees who are required to read and sign it on an annual basis. In Aviva France all employees agree to adhere to the Code in their employment contract and take part in annual training.

We aim for a sign-off of 100% of employees. This year we have not met our target, and the achieved outcome is lower than we aim for at 88%. The corporate responsibility committee recognise that this is not good enough and we will focus on achieving the target in 2013.

In addition to our business ethics code, Aviva has a code of ethics for senior management as required by section 406 of the Sarbanes-Oxley Act 2002 and the rules issued by the Securities and Exchange Commission. This code can be found on Aviva's website: www.aviva.com/investor-relations/corporate-governance/code-of-ethics

Financial crime

Aviva has a zero-tolerance approach to financial crime including bribery and corruption, fraud, money laundering and sanctions violations. We require our global businesses to comply with the Financial Crime Standard. This Standard sets out mandatory requirements to ensure businesses implement and maintain risk-based, comprehensive financial crime prevention programmes. The Standard and financial crime prevention programmes are reviewed and updated consistent with legal and regulatory developments. Every instance of financial crime, both internal and external fraud, is recorded and investigated independently.

We encourage our employees to raise any concerns they might have through their managers or Right Call – an Aviva-wide malpractice reporting service. Right Call enables all employees to report any suspicions or concerns in a confidential manner for independent investigation. During 2012, 63 incidents (2011: 69) were recorded across the Group, 24 internal, 17 external and 22 after further investigation were not considered as financial fraud. All cases were referred for independent investigation with 52 reaching conclusion and 11 cases currently remaining under investigation.

Fair pay

We reported last year that we were to pay all of our employees in the UK a living wage nationally from April 2012. We have now implemented this change to incorporate the annual Living Wage increases. We have also become an advisory council member of the Living Wage Foundation and were pleased to support the Foundation in the delivery of Living Wage week this year. We continue to work with our suppliers to encourage their national Living Wage status.

Responsible investment

As an insurer we have a fiduciary responsibility to look after our customer's money. We seek to do that in a responsible and ethical manner to the benefit of the customer and society as a whole. In April 2012 we revised our investment approach to implement environmental, social and governance (ESG) considerations into our investment decisions. This refreshed strategy is ongoing; by the end of 2012 33% of funds under management are covered by this approach. We plan to complete the roll out to all funds by year end 2013.

Aviva maintains a list of companies that we do not invest in due to ethical reasons. During 2012 we delivered a project to divest from holding organisations involved in cluster munitions and anti-personnel mine manufacture. We have held such a policy since 2008 and have now extended this policy to all policyholder funds.

We believe well-governed companies operating responsibly and sustainably should have the mechanisms in place to support their long-term growth and shareholder value. With this in mind, we promote transparent and effective governance and engagement with the companies in which we invest. Our ESG voting policy is used to engage with companies regarding, environment, climate change, health and safety, supply chain labour standards, human rights and bribery and corruption issues. Our voting covers over 1,800 companies in the MSCI universe. This year we saw an increase from 'against' to 'abstain' in our voting trends suggesting an improvement in companies ESG reporting.

As mentioned earlier in this report, Aviva is very active in advocating for better disclosure of ESG issues from listed companies. Our work with the Sustainable Stock Exchanges initiative aligns to this with regards to encouraging greater corporate transparency.

Attracting and retaining talent

As a global financial services organisation we recognise our role in attracting, developing and retaining talent within our workforce in order to deliver our strategic priorities, and ensure that we create an engaging and high performance orientated culture, that potential employees want to join and where our employees want to stay to develop their careers.

Delivering on our strategic imperatives requires a compelling vision and strong leadership which harnesses the energy, dedication and belief of all our employees. At Aviva we believe that everyone has a role in creating and contributing to our culture, although our senior leaders will undoubtedly set the tone. Supported by a strong global HR function Aviva has a clear purpose – to bring to life our employee promise in order to deliver exceptional business performance. At the heart of our approach are the fundamental principles of:

- Differentiating and rewarding our top performers
- Collaborating, encouraging innovation and seeking to do things once, globally
- Developing our internal capability through appropriate stretch opportunities
- Building an emerging talent pipeline, and
- Taking personal accountability

In 2012, we have continued to advance our people agenda by maintaining one global approach to talent management, performance management, leadership, and embarking upon enabling a values-driven culture to be at the heart of everything we do.

Essential learning

All employees within the UK business are required to complete nine modules of essential learning on annual basis. This training covers the essential elements of working for Aviva and includes health and safety, financial crime, wellbeing and business ethics modules. This programme not only delivers training in a consistent way to all employees, it allows for system reminders and management information. We are gradually rolling out this essential learning package to other markets, with Aviva Investors and Aviva France coming online in 2013.

Employee promise

Within the context of a challenging year, we have maintained an employee engagement of 68% globally, and seen improvements in our employees' sense of pride in working at Aviva, 75% (2011: 72%) our employees' propensity to recommend our products and services, 72% (2011: 70%) and their ability to manage an appropriate work life balance, 76% (2011: 67%).

Moving forward, our focus will be on enabling Aviva to achieve its strategic priorities and vision by:

- Developing a high performance culture, driven by living our organisational values and taking action when behaviours are not aligned
- Ensuring there is a direct relationship between an employees' performance and their reward
- Developing our leadership capability, particularly at the point of key transitions
- Ensuring our employees are able to thrive, through appropriate engagement and wellbeing programmes, and
- Continuing to ensure that our talent pipeline support both our capability and diversity ambition, whilst contributing positively to the government's wider youth employment agenda.

Developing a high performance culture

In 2012, we recognised that sustainable performance and competitive differentiation would be achieved by building a values based culture. Creating an inspiring vision and strategy that enables individuals to bring their full selves to work, through the alignment of their personal and organisational values is a critical leadership role. We started our journey with an all employee cultural values assessment. Through this we now understand our employee's personal values and beliefs, which we can look to harness in order to build greater organisational commitment. A high performance culture relies on strong leadership and the alignment of organisational structures, systems and processes. In light of this, we have aligned our performance management, reward and leadership development programmes to our desired values.

As we move forward, the journey will be led from the top of the organisation, with senior leadership engagement critical to the delivery of a high performance ethic and organisational success.

Focusing on transition points for our leaders

Critical to the high performance culture we seek, is the capability of our leaders who need to be decisive, agile, inclusive, and innovative.

In 2012, we refreshed our leadership development strategy in partnership with Oxford Saïd Business School. In building leadership capability, Aviva's main focus is on development at key transition points in the leader's career. We believe that successful leadership transitions, measured through shorter time to performance and value-added effort, are increased when leaders are supported in their transition through appropriate learning and development opportunities.

Together with the global Front Line Manager Programme and our senior management group induction, we are helping our leaders to continually grow and stay relevant in our changing world, reaching high performance in as short a time as possible.

Employee wellbeing

Providing a safe and healthy environment for employees, contractors, customers and visitors remains a priority across Aviva. Whilst we have well established policies and systems in place to ensure health, safety and minimise risks, we aim to create a supportive working environment that encourages our employees to perform at their best whilst finding the right balance between work and home life. To help our employees manage their health and wellbeing we have developed various flexible working practices and wellbeing initiatives. This continues to build our organisational health which is critical to our businesses performance. Some of the options available include, part-time working, home working, flexible hours, career breaks, employee assistance programmes, fitness centres, discounted health club memberships and subsidised travel and 'bike checks' for commuters.

We continuously review our approach to health, safety and wellbeing and during 2013 we will be developing a more integrated wellbeing approach to provide excellent services to our employees, strengthen our focus on mental health in the workplace and improve our organisational health insight.

Diversity and inclusion

In addition to delivering a range of initiatives in 2012, we also refreshed our approach to inclusion. There are three themes to our approach:

- **Careers:** we want to be the employer of choice for our people such that they choose to invest their working lives with us
- **Capability:** we want our leaders to have the skills and capabilities required to build high-performing teams in a diverse business environment
- **Culture:** we want to be 'most recommended', not only by our customers but also by our people. To do that, we need a culture and work environment that builds pride among our people

This allows flexibility around local business related priorities while creating a model for aligning agendas to a common framework.

Being respectful of each other's differing backgrounds, cultures, needs and views is key. Our diversity and inclusion practices remain aligned with the United Nations Universal Declaration of Human Rights and the International Labour Organisation's core labour standards. In addition, our global Corporate Responsibility standard includes a set of minimum requirements for all Aviva businesses with regard to diversity, equality, and human rights. Our Employee Promise Survey is one way that we confirm that our commitment to diversity and inclusion is reflected in the way we work. In 2012, 76% of employees reported that Aviva had an environment where people from diverse backgrounds can succeed. We continue to take a special interest in gender diversity, because it is an area that is relevant in all our global markets and the business case for gender balance in leadership is indisputable. Globally, women are a majority of Aviva's population at 54%. The percentage of women in senior management has improved to 22% (2011: 20%), the gender balance on our Group Executive stands at 25% and 24% of the board were women during 2012. We remain committed to achieving 25% female board composition by the end of 2015.

Our employee network groups make an important contribution to the organisation and in the community. Most notable of these are the Women's Network and Aviva Pride. We improved our ranking to 32nd (2011: 98th) on the Stonewall Workplace Equality Index. This result reflects our continuing efforts to develop an inclusive environment for all of our people.

Community development

We know that a sustainable business must make a real contribution to the society it operates in. As well as providing employment to 31,211 people we also provide peace of mind to our 38 million customers.

Our approach to community development is based on building partnerships across three main strategic themes of our business: education, life trauma and financial literacy. We are actively contributing to the Millennium Development Goals and we demonstrate our commitment to being at the leading edge of addressing environmental, social, and governance issues through our UN Global Compact LEAD membership.

Globally, we contributed over £11 million in cash, gifts in-kind, project and volunteering costs to community development in 2012, a 12% decrease from 2011 (2011: £12.4 million) a reduction due to the reducing scale of our business and a shift in our global marketing strategy. Our contribution is magnified by the wider investment we leverage together with our stakeholders such as employee fundraising. Employees are allocated three days volunteering leave per year and in 2012 we built our volunteering offering into our HR systems. This takes advantage of the skills development that can be gained, as well as the value contributed to our communities, and embeds the CR Standard further in to our day to day work. In 2012, 18% of employees took part in volunteering equating to 56,357 hours. There was also a 3%

increase in the number of employees contributing through payroll giving, totalling £939,176. This increase in participation is significant because we know it demonstrates pride in working for Aviva.

We have continued to improve our measurement approach in recording our inputs and outputs more accurately, in order to demonstrate the wider benefit of our investment and to support the continuous improvement of our programmes.

Aviva has a clear track record of working with field experts in community development across the public and charity sector. We recognise the importance of our partnerships with organisations such as the UN Office of the High Commissioner for Human Rights, UK Athletics, Save the Children, Consortium for Street Children, and Oxfam to enable us to develop and share best practice programmes and to work effectively in areas of community advocacy. This partnership work helped us to develop our Child Safeguarding guidelines as an aid to employees working or volunteering with children on Aviva's behalf.

We recognise the mutual benefit of our community development activity; our employees feel engaged and proud, our communities benefit and our brand reputation is enhanced.

Street to School

Aviva's Street to School programmes help young people move away from the street and into education and training. We focus on education because we know that education is insurance.

Street to School has now helped over 649,000 children around the world, exceeding our five-year target in just three years. Since the programme started in 2009 we have invested over £13 million in cash and in-kind donations. We commit at least 50% of our community development budget to Street to School.

2012 saw us increase the depth and breadth of our Street to School work. We have continued to create innovative cause related marketing opportunities. In the UK a child runs away from home and into danger every five minutes. Aviva, Railway Children and Mumsnet have created an online space that helps parents talk to their children about this difficult subject and find guidance. For every interaction on the Mumsnet site, we are donating £2 to Railway Children to help vulnerable young people at risk on Britain's streets.

In Indonesia we have created a partnership with PLAN UK to work in conjunction with the Ministry of Social Affairs raising awareness of birth registration for street children. The Ministry have identified that around 230,000 children in street situations in Indonesia. The project aims to register 1,500 children living or working on the streets over a two year period.

We have also stepped up our advocacy, supporting the International Day for Street Children and delivering a pioneering partnership with the UN High Commissioner for Human Rights. The report we co-sponsored on the rights of children working and/or living on the street was welcomed by the Human Rights Council in March 2012. We are now actively working with our partners to turn the report's recommendations into global action. Over the next few years we want to help drive real change in the cause and act as a catalyst to inspire others to join us in raising awareness of the issues and ensuring children involved with the street have the same rights and opportunities as all children, especially their right to education.

Community projects

The other half of our community development approach can be found in the following examples:

- Aviva was one of the first companies to sign up to the Oxfam 365 Alliance. This emergency fund supports relief operations and helps Oxfam respond to humanitarian disasters where public funding may be limited. Thanks to this alliance, 6.5 million people facing 27 emergency situations across the globe were reached in 2011-12

- 'Paying for It' launched by Aviva in 2007, continued to take economic citizenship teaching into schools throughout the UK using trained Aviva volunteers and now with 3,500 teachers using our resources
- Our grassroots sport programmes in the UK reach out to hundreds of thousands of children every year to help them develop a healthy and active lifestyle
- In Canada, the Aviva Community Fund gives members of the public and our brokers the opportunity to turn great ideas into action to benefit their local communities. This innovative use of social media encouraged over 2.8m votes to be cast for various community projects in 2012. A total of \$1 million will be shared among projects such as a youth addiction and support program in Glace Bay, Nova Scotia; a secondary school science and nutrition program in Vancouver, BC; animal rescue programs in Spruce Grove, Alberta and Sprucedale, Ontario; and a new splash pad in Canora, Saskatchewan

Access to insurance

To improve insurance access and service for vulnerable people in the UK, we have created an internal 'dementia taskforce'. We also now include Alzheimer's Society materials in our training programme. To help low-income households, we work with social landlords and broker partners to provide tenants with easily accessible and affordable home contents insurance. Less than half of low-income households in the UK have contents insurance while a third take out loans to replace items. This compounds the risk of indebtedness.

We believe in providing micro-insurance products to extend the value of insurance and the peace of mind that it offers to low income families. In India we work with the micro-insurance company Bhartiya Samruddhi Finance to give us the technology to process product purchases within 24 hours. Delivery through their vast rural branch network helps us serve our financially excluded and rural customers better and faster and enables us to provide them world class services at low cost.

In Singapore, we have been the official provider of term life and critical illness cover for the Singapore armed forces since 1983, extending to their role in UN Peacekeeping and humanitarian services. To date we have provided life and illness cover to over 125,000 servicemen and women.

Climate change and environment

Protecting the environment to mitigate against and adapt to man-made climate change are key priorities for Aviva that we believe require action today, not tomorrow. Following the sale of our businesses in USA, Sri Lanka and Malaysia we have restated our 2010 baseline and restate it to our 2010 baseline of 132,244 tonnes CO₂e. Our long term reduction target remains at 20% by 2020, from this restated baseline. Our relative annual target reduction is set at 5% to help us achieve the longer-term target. We also aim to increase our use of renewable electricity, this year we've increased the amount we purchase to 24% (2011: 7%).

Aviva plc – operational carbon footprint covering 100% of employees GHG Emissions data from 1 Jan 2012 to 31 Dec 2012

Tonnes CO ₂ e	2012	2011
Scope 1	23,849	44,471
Scope 2	75,733	97,988
Scope 3	26,920	22,655
Absolute CO ₂ footprint*	126,502	165,115
Carbon offsetting	(132,827)	(173,371)
Total net emissions	(6,325)	(8,256)

Scope 1 – operational emissions from owned sources e.g. gas, vehicle fleet as part of product/service.

Scope 2 – operational emission from non-owned sources e.g. electricity.

Scope 3 – business activity emissions from non-owned sources – e.g. business travel.

As a major international real estate manager, we are conscious of the implications that a changing climate can have on our property

investments. In the UK we are continuing our work in this area ensuring that our entire portfolio has energy performance certificates and will meet minimum performance regulation in 2018. The Real Estate area of Aviva Investors also works with the Aviva General Insurance's Geographic Information System team so that they can understand the potential flood risk applicable to properties which they intend to add to the investment portfolio.

Aviva France has signed a national partnership with the French Chambers of Commerce to promote an Environment Management System dedicated to small and medium businesses: EnVol. As one of the main partners, we offer a 5% discount on professional's insurance policies when the customer obtains the EnVol certification. This rewards them for having assessed their environmental impact and defined a plan to reduce it.

The role of insurers in climate change

The insurance industry has a fundamental part to play in society's responses to climate change. As a major insurer Aviva has first-hand understanding of the impact of extreme weather events on our customers. On their behalf, we are committed to help mitigate the threat of climate change and support everyone in society to adapt to changes caused by man-made emissions already in the atmosphere. Our industry can also draw on its knowledge of historical weather data to identify patterns of change, applying our understanding of risk to map future temperature scenarios and determine likely impacts.

We believe that climate change must be tackled now. As extreme weather events become more frequent and more severe, they become more challenging to insure. It is in everyone's interest that insurance remains affordable and available so that people affected by severe weather events can recover quickly from unavoidable impacts. Aviva fully supports the ABI's discussions with Government on finding a viable solution to keep insurance affordable and available for those at high risk of flooding, when the Statement of Principles ends in June. Regardless of the outcome of these discussions, we firmly believe that all parties – including central and local Government, insurers and home owners – need to play their part in protecting homeowners who are living in fear of flooding.

We have been able to respond well to the extreme rainfall experienced in the UK in 2012, answering calls to our call centres within an average of eight seconds and even being able to go door-to-door where imminent flooding is expected to advise customers to move valuable and sentimental items upstairs to avoid damage.

Industry leadership and participation

We have joined forces with other leading organisations to provide a collective industry voice and specialist sector-specific influence to support the climate change agenda. We have joined the EU Corporate Leaders Group on Climate Change (EU CLG) which seeks to communicate the support of business for the European Union to move to a low carbon society, and to work in partnership with the institutions of the EU to make this a practical reality. Aviva Investors signed the EU CLG's letter which calls for policy makers to introduce a clear carbon price framework in a stable and timely manner.

We were a founder member of the ClimateWise Principles and continue to be represented on the management committee. During 2012 we were involved in ClimateWise collaborations on research into sustainable claims management and understanding the roles of different stakeholders in improving the resilience of cities to a changing climate in North America. Aviva has been represented on the CBI Energy and Climate Change Board since its creation in 2007. We continue to be represented at a senior level on this board.

We firmly believe that engaging our employees to raise awareness and address environmental impacts is an essential part of delivering our environmental strategy. For the second year running 76% of our employees agree that we make business

choices that support the environment. Following the launch of our insurance cover for the environmental goods and services section, for UK ClimateWeek 2012 we conducted a survey to understand intermediary attitudes to environmental management within their own business and whether they believed focusing on it further would win business for them. 20% of brokers advised they had seen an increased interest in the demand for products in support of the environmental goods and services sector. 69% thought that they could take more advantage of the interest seen in this area.

Investing in low carbon energy infrastructure

In a challenging macro-economic environment institutional investors are looking for diversified sources of stable income. In August 2012, Aviva Investors acquired a residential solar project totalling 23 megawatts of capacity making it the largest investment of this kind in the UK and the company's first of this type. The assets are spread across 7,000 homes. The assets are held in the Realm Infrastructure Funds, which are mainly targeted at UK pension fund investors and is in keeping with the strategy of producing long term profitability with a reduced appetite for risk. Aviva Investors also acquired the Almatret wind farm near Lerida in Spain in the same month.

Environmental Regulations

Aviva is compliant with the UK Government's Carbon Reduction Energy Efficiency scheme. In 2012, we purchased and surrendered 91,590 carbon allowances at a cost of nearly £1.1 million.

Going forward we are preparing for the UK Government's Mandatory Carbon Reporting which applies to companies listed on the London Stock Exchange. We will be reporting in line with this in next year's Annual Report and Accounts.

Affiliations and engagements

We work closely with leading organisations to share good practice, identify emerging issues and improve our performance. Here are just a few of the organisations we collaborated with in 2012:

- Consortium for Street Children
- CRO Forum
- ClimateWise
- UNEP Finance Initiative
- CBI Energy and Climate Change Board
- HRH Prince of Wales Accounting for Sustainability
- Institute of Business Ethics
- UN Global Compact LEAD
- UN Human Rights Commissioner
- UN Principles for Sustainable Insurance
- UN Principles for Responsible Investment
- UN Women Empowerment Principles
- ORC Global Diversity Forum; and
- Business in the Community

Key indicators

CR Indicator	2009	2010	2011	2012	2012 target
Trust and Transparency					
<u>Business ethics</u>					
*% of employees signing of receipt, understanding and acceptance of our Business Ethics Code on an annual basis	90%	32%	89%	88%	100% of employees
*% of employees completing the Bribery and Corruption training	79%	n/a	89%	88%	100% of employees
<u>Customers</u>					
*% of businesses that are in or above the upper quartile relative to the local market average (NPS score)	50%	50%	52%	39%	Maintain or improve past performance
*% of employees who rate us favourably on customer index	67%	69%	73%	75%	Maintain or improve past performance
Climate change and environment					
*% of remaining CO ₂ e emissions offset annually	100%	100%	100%	100%	Offset remaining CO ₂ e emissions at Group level
*CO ₂ e emissions (tonnes) – absolute	104,351	127,685	165,115	126,502	
*CO ₂ e emissions (tonnes) – relative	n/a	n/a	144,550	126,502	Reduce relative CO ₂ e emissions by 5%
*Water consumption (m ³) – absolute	751,750	690,369	509,657	559,144	Reduce water use by 4%
*Waste generated (tonnes) – absolute	11,812	12,042	8,645	10,153	Reduce waste generated by 4%
*Proportion of recycled waste	79%	75%	73%	71%	80% or above
*% of employees who feel that Aviva makes business choices that support the environment	62%	71%	76%	76%	Meet/exceed GFS benchmark (2012: 60%)
Attracting and retaining talent					
*% of women in senior management	22%	21%	20%	22%	Increase percentage of women in senior management group
*% of employees who feel that Aviva is doing a good job of retaining the most talented people	New KPI	New KPI	New KPI	42%	Meet/exceed GFS benchmark (2012: 50%)
*% of employees who feel we have created an environment where people with diverse backgrounds can succeed	New KPI	73%	78%	76%	Meet/exceed GFS benchmark (2012: 81%)
*% of employees who rate us favourably on leadership index	66%	64%	70%	61%	Meet/exceed GFS benchmark (2012: 70%)
*% of employees who rate us favourably on engagement index	64%	63%	68%	68%	Meet/exceed GFS benchmark (2012: 71%)
Suppliers					
*% of “Managed Supply” spend where supplier accepted Code of Behaviour – UK only	New KPI	New KPI	31%	30%	Increase % from previous year
*% of “Managed Supply” spend where supplier has successfully completed the CR element of the Supplier process – UK only	New KPI	New KPI	New KPI	71%	
*Number of business units that use the ‘Supplier Hospitality register’ and ‘Register of Interests’	11	15	19	19	Increase from previous year
Developing communities					
*Amount of community investment	£8.0m	£11.4m	£12.4m	£11m	Total community investment at/above previous year
% of employees participating in volunteering	16%	17%	20%	18%	Increase the % of employee participation in volunteering
Number of employee hours spent volunteering	79,900	57,250	60,390	56,357	Increase the % of employee participation in volunteering
*% of investment in Aviva ‘Street to School’	New KPI	52%	54%	58%	50% of cash donations
*% of employees who feel that Aviva does a good job of contributing to the communities in which we live and work	62%	66%	76%	76%	Meet/exceed GFS benchmark (2012: 62%)

*Denotes that this KPI has been assured by PricewaterhouseCoopers LLP

Met/exceeded 2012 target ✓ Missed 2012 target ✗

Change Met target 2013 target			Notes
(1)%	✗	100% of employees	Business ethics: While our target remains at 100% it is inevitable that not all employees will be able to sign the code each year due to maternity leave, sick leave etc. This year we have not met our target, and the achieved outcome is lower than we aim for at 88% due to a change in system use in the UK and significant structural changes to our business.
(1)%	✗		
(13)%	✗	Improve past performance	Customers: Using NPS methodology we calculate the performance of businesses relative to their local market. Our Customer Advocacy section on page 74 outlines this further. Following changes to our overall business structure, the number of markets now ranked within the upper quartile is 39% – one market less than the previous year.
2%	✓	Improve past performance	Absolute CO ₂ e data – CO ₂ e data includes emissions from our buildings, business travel, outsourced data centres, water and waste to landfill.
	✓	Offset 100% remaining CO ₂ emissions at Group level	
(23)%	✓	Reduce relative CO ₂ emissions by 5%	Relative CO ₂ e data – The relative comparison uses the 2012 basis for reporting (as above), and the adjusted relative data for 2011 encompassing structural changes that occurred in 2011.
(12)%	✓	Reduce water use by 4%	
10%	✗	Reduce waste generated by 4%	Baseline change – Due to the sale of our businesses in USA, Sri Lanka and Malaysia it is now necessary to revisit our 2010 baseline and restate it to account for these material structural changes. Our restated 2010 baseline, which we use to understand our progress on a long term basis is 132,244 CO ₂ e. Our long term reduction target remains at 20% reduction by 2020, from this restated baseline
17%	✗	Reduce waste generated by 4%	
(2)%	✗	80% or above	
			Water consumption – In 2012 improvements in the scope of local environmental reporting has meant that Ireland, Hong Kong, Aviva Investors North America and Solus Accident Repair Centres are reporting water for the first time. Hence the increase in total water consumption reported.
0%	✓	Meet/exceed GFS benchmark	GFS stands for the Global Financial Services benchmark. This is a tough external benchmark that we use as a stretch target. In the equivalent regional benchmarks we are consistently performing above the benchmark.
2%	✓	Increase percentage of women in senior management group	People: Our EPS results reflect the wider organisational change of our business. Our targets are external benchmarks which we are working towards.
n/a	✗	Meet/exceed GFS benchmark	
(2)%	✗	Meet/exceed GFS benchmark	
(9)%	✗	Meet/exceed GFS benchmark	
0%	✗	Meet/exceed GFS benchmark	
n/a	✗		Suppliers: Due to changes in the way that we manage our procurement, we are unable report a Group figure this year. It is our aspiration to report the Group figure going forward.
n/a			
0	✗	Increase previous year	Hospitality register: this figure has remained static however, more Aviva businesses are now compliant with this KPI, and we have removed those businesses we have divested.
(12)%	✗	Total community investment at/above previous year	
(2)%	✗	Increase the % of employee participation in volunteering	
(6)%	✗	Increase the % of employee participation in volunteering	
4%	✓	50%	
0%	✓	Meet/exceed GFS benchmark	

Accounting for Sustainability

We also report our performance using Accounting for Sustainability's connected reporting framework, which integrates financial and non-financial data to provide a comprehensive picture of our impacts. We were one of the first companies to help develop the framework and have used this approach for environmental reporting in our Annual Report and Accounts since 2007. We continue to explore ways to extend this framework and have included customer and community indicators since 2009.

We have reported the following indicators for 2012:

- Greenhouse gas emissions;
- Waste;
- Resource usage;
- Customer advocacy; and
- Community development.

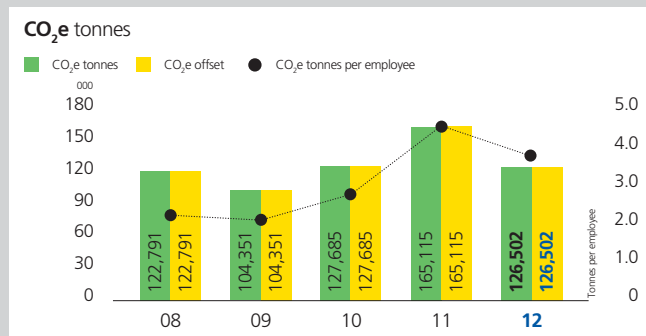
Greenhouse gas emissions

Direct Company impacts

Cash flow performance

The most material direct environmental impact that Aviva creates are greenhouse gas emissions. We emit greenhouse gases through our company operations generated from energy used in our buildings, fugitive emissions, business travel, water and disposal of waste to landfill. We also include emissions from our outsourced data centres in the UK and Canada. The scope of Aviva's emissions includes all operations where we have day to day control; including joint ventures. 126,502 tonnes of carbon dioxide (tCO₂e) or equivalent were emitted by Aviva into the atmosphere in 2012.

Carbon offsets from the voluntary carbon market have been purchased to cover our footprint plus an additional 5% extra to allow for any inconsistencies in reporting. The cost of offsetting, £530,000, will be funded by the areas of the business that have created the emissions on a 'polluter pays' basis.



Performance, strategy and targets

Aviva's relative emissions have reduced this year by 12%. This is a combination of improvements in energy efficiency and increased use of technology. Our renewable electricity on a worldwide basis is 24% (2011: 7%) of our total electricity consumption.

Due to structural changes to the business we set a new baseline in 2010 for our long term carbon reduction target. Following the sale of the Aviva businesses in the USA, Sri Lanka and Malaysia we are restating our 2010 to account for these. As a result our restated baseline is 132,244 tCO₂e. Our long term target to 2020 remains at a 20% reduction using this baseline year figure. Our Group annual carbon reduction target still stands at 5%.

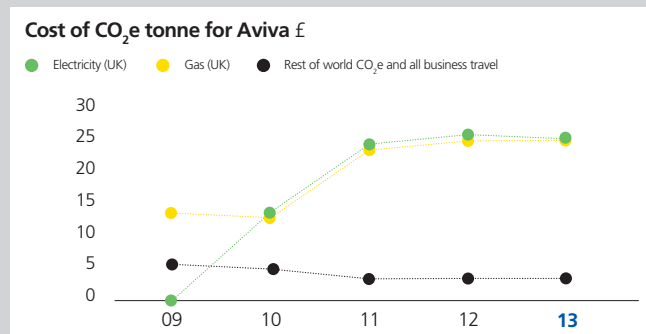
Our use of communication technologies has continued to increase in 2012. 2,717 meetings were held by telepresence in 2012 (2011: 2,579), as well as 12,844 webexs and other technologies. We have estimated the cost of travel avoidance from the use of telepresence in 2012 as £2.7 million and 1,988 tonnes in carbon savings. Our business travel kilometers have reduced overall by 5%, however air travel has increased by 2% on the year.

Some of the monies in the Sustainability Fund, mentioned in last year's report have now been employed in voltage optimisation technology in the UK. The return on investment is expected to be 47 months and the saving initially will be fed back into the fund to enable further investments to be made. This fund was created to help our long term carbon reduction target, and combat the impact of rising energy costs and potentially bolster our energy security over the next decade.

The UK businesses were financially impacted in 2012 by the cost of the Carbon Reduction Commitment Energy Efficiency Scheme (CRCEES). The total CO₂ emissions in respect of CRCEES for 2011/2012 financial year were 97,729 tCO₂e (2010/2011: 105,418 tCO₂e) with a cost to the business of just under £1.1 million.

Aviva's operational carbon boundaries differ from those reported for the CRCEES as that also includes energy emissions from our portfolio of properties included in funds which we manage and have responsibility for. Aviva's position in the CRCEES Performance League table in 2011 was 899 out of a total of 2103 participating organisations.

The graph below shows the cost of carbon per tonne for Aviva. These figures take into account the cost of CRC, the Climate Change Levy and the cost of purchasing carbon credits. The cost of carbon varies depending on the source of the emissions and the geography of where the emissions are created. These also change over time. The only aspect of the costs which benefits the environment is the carbon offsetting element.



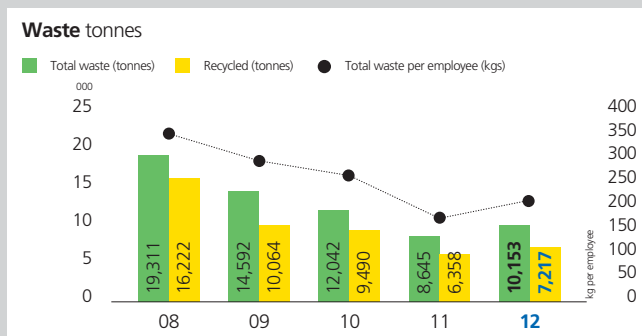
Waste

Direct company impacts

Hazardous and non-hazardous waste

Total disposal cost for hazardous and non-hazardous waste in the UK was £681,000 (2011: £596,000), which includes UK landfill tax and capital expenditure. On a worldwide basis the cost of offsetting the greenhouse gas emissions related to waste is approximately £2,056.

In the UK, total capital expenditure for storage and recycling of waste was £100,000 (2011: zero). Overall total waste increased by 17% over the period, and waste diverted from landfill decreased to 71% (2011: 73%). In the UK, this rose to 95% from a figure of 94% last year. We have failed to meet our UK target of zero to landfill by end 2012 due to the lack of suitable recycling infrastructure in some areas of the country.



Performance, strategy and targets

Due to the improved quality of reporting our total waste has increased by 17% to 10,153 tonnes. The total of actual waste recycled however, has increased from 6,358 tonnes in 2011 to 7,217 tonnes.

Indirect impacts

Products/suppliers/investors

In an effort to reduce the amount of waste generated through our claims fulfilment processes, we continue to work with peers through an ABI working group to understand how we can raise standards in this area across the industry.

Industry benchmark information

- 200kg of waste per employee per year; and
- recycling rate of 60–70% (BRE Office toolkit).

Targets

- annual 4% reduction in total waste;
- annual recycling rate greater than 80%; and
- long-term target – zero to landfill for UK operations by 2015 and worldwide by 2020.

Resource usage

Direct Company impacts

Water

The operating cost of water is £1.2million (2011: £1.1 million) with a CO₂ equivalent of 586 tCO₂ (2011: 503tCO₂). On a worldwide basis the cost of offsetting the greenhouse gas emissions related to water is approximately £2,000.

Energy intensity

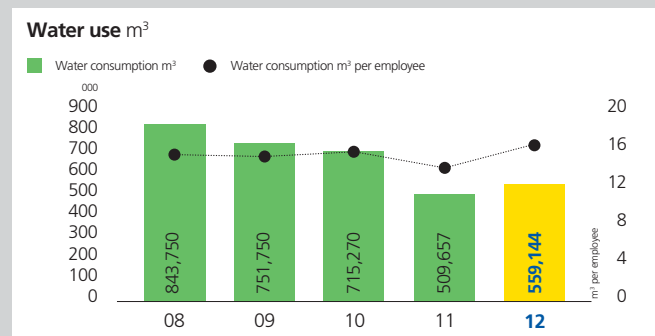
The total cost of buildings related energy in 2012 was £17.3 million (2011: £18.3 million). The equivalent cost per square metre is £21.66. The cost of UK CRCEES regulation of £1.1 million is an additional cost (2011: £1.3 million).

Paper usage

We currently do not track the cost of paper on a global basis.

Environmental incidents

During 2012 there were no environmental incidents as a result of our operations (2011: none).



Indirect impacts

Performance, strategy and targets

Water consumption increased by 10% in 2012, this was mainly due to improved reporting around this resource. Without additional business units reporting, we have increased by 0.95%.

Industry benchmark information

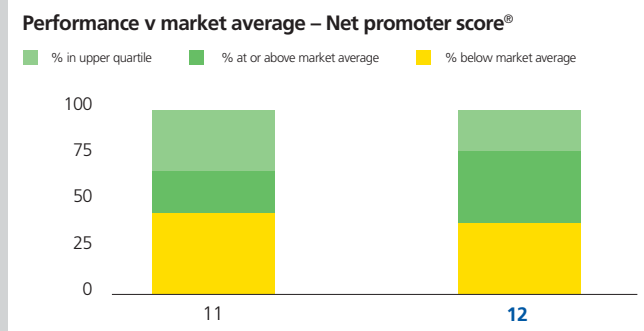
- Water: 4 cubic metres per employee per year (Water Key Performance Indicators and benchmarks for offices and hotels. C657 CIRIA www.ciria.org).
- Office paper: 4,000–5,000 sheets per employee per annum (Gartner research).

Customer advocacy

Direct company impacts

At Aviva, the Net Promoter Score® is how we track our progress towards our ambition to become the most recommended insurer. This KPI is derived from the annual benchmarked Relationship NPS survey conducted across all markets. This measure is widely regarded as a predictor of future growth, with analysis showing connections to retention, repeat purchase and referrals.

Non-financial indicator



Our performance, strategy and targets

The 2012 Relationship Net Promoter Score (RNPS) survey results show that the vast majority of markets are on par with or better than the market average – a slight improvement on the prior year. Following changes to our overall business structure, the number of markets now ranked within the upper quartile is 39% – one market less than the previous year.

Building customer advocacy is core to our business objectives with our long term target to have all markets in the upper quartile relative to their local competition. To achieve this, analysis of the survey highlights key drivers and priorities by market, which markets use to develop an action plan. The 2013 action plans show some common areas of improvement, including how we engage with customers through ongoing communications, how we build products that customers need and understand, and ensuring that we are available to customers through the service channels they choose (such as digital and mobile).

Indirect impacts

Acting in our customers' best interests is in the best interests of our business. Recent analysis has shown us that there is a strong correlation between customer advocacy and both brand awareness and consideration. There are two key benefits from this: higher awareness and consideration can lead to better business performance through increased new business; and indicates a potentially more sustainable business since a solid reputation creates longer-term protection for a brand.

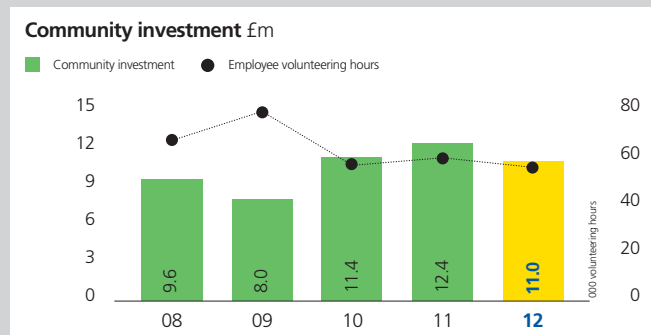
Through the Systems Thinking approach, our UK business has seen improved efficiency as a result of projects to improve customer advocacy. For example, our Direct GI business reduced complaints by 66% as a result of focusing on customer needs and a market leading maturity proposition in the Life business delivered improved NPS, retention and reduced overheads.

In the last year, the proportion of our people who say they would recommend our products and services remains slightly below the Global Financial Services benchmark. Our analysis tells us that employee advocacy and customer advocacy are highly correlated, therefore improving our performance is a high priority if we are to build our reputation with our people and our customers.

Community development

Direct company impacts

Our global investment in charitable and community development projects in 2012 was £11 million (2011: £12.4 million). This includes cash, time and in-kind donations as well as project and volunteering costs calculated using the London Benchmarking Group (LBG) model. We also helped leverage an additional £3 million of investment where our activity attracted further contributions from our wide network of stakeholders (2011: £2.8 million) including employees.



Our performance, strategy and targets

Our global community development strategy, focusing on financial literacy, education and life trauma, aligns to our corporate vision and channels financial support and the expertise of our employees into projects where we can see positive societal impacts. Our total investment was £1.5 million lower than in 2011 due to a reduction in the scale of our business and a change in marketing strategy that had previously contributed a significant percentage of our total investment. This cause related marketing, used to deliver community development advocacy will rise again in 2013.

We delivered 56,357 hours of volunteering in 2012 (2011: 60,392) and we have maintained a high score for employee engagement regarding the way we act in our communities placing us 14% above the Global Financial Services benchmark. Our rigorous social impact measurement also helped us to achieve a top ranking in the FTSE4Good index and improve our DJSI scoring in this area by 25%.

Due to the changes in our business structure the community media value and reach has been less well measured. This will be corrected in 2013 as the business benefits are an important element of our work in this area. Overall we have positively impacted 2 million (2011: 1.3 million) due to the momentum of Street to School and the addition of grass roots rugby.

Our flagship Street to School initiative has now impacted over 649,000 children since it started in 2009 (target 500,000 by 2015).

Indirect impacts

After working alongside both NGO, Government and UN agencies we are increasingly committed to national and international leverage of best practice and advocacy activity. In 2012 we delivered a pioneering partnership with High Commissioner for Human Rights to sponsor a report welcomed by UN Human Rights Council. Also during 2012 we conducted a review of our Street to School goals analysing our impacts and consulting a wide range of internal and external stakeholders. Going forward, we will begin to shift our focus beyond just being a corporate champion of street children to being a cross sector catalyst for action for street children. We believe this type of collaboration is essential to achieve the recognition and realisation of street child rights, help deliver the Millennium Development Goals and increase the wellbeing of all in our global communities.

Indices and benchmarks

During 2012 Aviva has been included in some key responsible investment indices:



FTSE4Good

Aviva has been included in the FTSE4Good since its inception in 2001. FTSE4Good rank as one of the top four global organisations in their ESG ratings.



STOXX ESG global leader

Aviva is rated as a Global ESG leader and are rated us as one of the top ten companies in their index for our governance structure.

Additionally, Aviva are proud to have been recognised by the following:



Stonewall

We have improved our ranking to 32nd in the Stonewall Equality Index 2013, up from 98th in 2012.

CARBON DISCLOSURE PROJECT

Carbon disclosure project –

We achieved a carbon disclosure score of 78%, with a rating of B – indicating the climate change strategy is integrated but not fully established across all initiatives.

We have also won awards specifically for our Street to School programme:

- CRY Child rights award, India
- Marketing society awards for excellence, Cause related marketing in the UK
- Out of the box PR – India PR and Corporate Communications awards
- Great wall of education, India – highly commended, TVE Corporate Sustainability Awards
- Best foreign insurance company – Aviva Cofco won for its successful branding, for understanding its customer's needs and for being a responsible organisation.



Aviva are a member of the Dow Jones sustainability index. This year we increased our score to become a silver member of the SAM sustainability yearbook.



Oekom

We have been rated as a prime investment by Oekom.



We have been ranked for the second year running as 3rd in the FTSE 100 by Carbon Clear.

PwC Independent Assurance Report to the Directors of Aviva plc

The Directors of Aviva plc ("Aviva") engaged us to provide limited assurance on the information described below and set out in Aviva's Annual Report and Accounts for the year ended 31 December 2012.

Our conclusions

As a result of our procedures nothing has come to our attention that indicates the Selected Information for the year ended 31 December 2012 has not been prepared in all material respects with the Reporting Criteria.

What we are assuring ("Selected Information")

The selected corporate responsibility (CR) data for the year ended 31 December 2012 marked with the symbol * presented in the Annual Report and Accounts 2012 on pg 70. The scope of our work was restricted to the Selected Information for the year ended 31 December 2012 and does not extend to information in respect of earlier periods or to any other information in the Annual Report and Accounts 2012.

How the information is assessed ("Reporting Criteria")

We assessed the Selected Information using Aviva's Reporting Criteria as set out at www.aviva.com/corporate-responsibility/reports¹.

Professional standards applied² and level of assurance³

We have used ISAE 3000 (limited level of assurance) and we have complied with the ICAEW Code of Ethics.

Understanding reporting and measurement methodologies

There are no globally recognised and established practices for evaluating and measuring the Selected Information. The range of different, but acceptable, techniques can result in materially different reporting outcomes that may affect comparability with other organisations. The Reporting Criteria used as the basis of Aviva's reporting should therefore be read in conjunction with the Selected Information and associated statements reported on Aviva's website.

Work done

Considering the risk of material misstatement of the Selected Information, we:

- made enquiries of Aviva's management, including the CR team and those with responsibility for CR management and Group CR reporting;
- evaluated the design of the key structures, systems, processes and controls for managing, recording and reporting the Selected Information. This included visiting two markets, the UK and Canada, and analysing a further seven markets selected on the basis of their inherent risk and materiality to the Group, to understand the key processes and controls for reporting site performance data to the Group CR team;
- performed limited substantive testing on a selective basis of the Selected Information at corporate head office and in relation to the UK and Canada markets to check that data had been appropriately measured, recorded, collated and reported; and
- assessed the disclosure and presentation of the Selected Information.

Aviva's responsibilities

The Directors of Aviva are responsible for:

- designing, implementing and maintaining internal controls over information relevant to the preparation of the Selected Information that is free from material misstatement, whether due to fraud or error;
- establishing objective Reporting Criteria for preparing the Selected Information;
- measuring Aviva's performance based on the Reporting Criteria; and
- the content of the Annual Report and Accounts 2012.

Our responsibilities

We are responsible for:

- planning and performing the engagement to obtain limited assurance about whether the Selected Information is free from material misstatement, whether due to fraud or error;
- forming an independent conclusion, based on the procedures we have performed and the evidence we have obtained; and
- reporting our conclusion to the Directors of Aviva.

This report, including our conclusions, has been prepared solely for the Directors of Aviva as a body in accordance with the agreement between us, to assist the Directors in reporting Aviva's corporate responsibility performance and activities. We permit this report to be disclosed in the Annual Report and Accounts for the year ended 31 December 2012, to enable the Directors to show they have addressed their governance responsibilities by obtaining an independent assurance report in connection with the Selected Information. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Directors as a body and Aviva for our work or this report except where terms are expressly agreed between us in writing.

**PricewaterhouseCoopers LLP,
Chartered Accountants, London
6 March 2013**

¹ The maintenance and integrity of Aviva's website is the responsibility of the Directors; the work carried out by us does not involve consideration of these matters and, accordingly, we accept no responsibility for any changes that may have occurred to the reported Selected Information or Reporting Criteria when presented on Aviva's website.

² We have complied with International Standard on Assurance Engagements 3000 – 'Assurance Engagements other than Audits and Reviews of Historical Financial Information' issued by the IAASB, and with the applicable independence and competency requirements of the Institute of Chartered Accountants in England and Wales (ICAEW) Code of Ethics. To comply with those standards, our work was carried out by an independent and multi-disciplinary team of sustainability and assurance specialists.

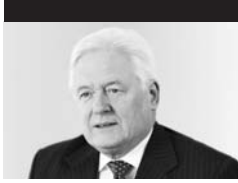
³ Assurance, defined by the International Auditing and Assurance Standards Board (IAASB), gives the user confidence about the subject matter assessed against the reporting criteria. Reasonable assurance gives more confidence than limited assurance, as a limited assurance engagement is substantially less in scope in relation to both the assessment of risks of material misstatement and the procedures performed in response to the assessed risks.

Governance

In this section

Chairman's governance letter	78
Board of directors	80
Group Executive	83
Directors' report	85
Corporate governance report	89
Nomination Committee report	95
Audit Committee report	97
Risk Committee report	100
Corporate Responsibility Committee report	103
Directors' remuneration report	104

Chairman's governance letter



John McFarlane
Chairman

“
Strong corporate governance is the cornerstone of a successful organisation.

I have taken corporate governance incredibly seriously throughout my career as a leader of major financial services organisations around the world, and will continue to do so at Aviva. This is also firmly the position of our Board. A system of good governance keeps shareholder interests front of mind, and ensures a balanced outcome for stakeholders in general. Tone is always set from the top, and we have therefore made a number of changes in 2012 to enhance but also simplify the Group's governance arrangements. As a cornerstone of this, the way authority is delegated throughout the Group was revised to give greater empowerment to businesses whilst strengthening central controls over the major risks in the Company, and these are subject to regular scrutiny by the Board Committees.

UK Corporate Governance Code

The UK Corporate Governance Code (Code) sets out the standards of corporate governance that UK premium listed companies must meet. The Company aims to meet all the Code requirements and I am pleased to confirm that the Company has complied with most of the principles and provisions of the Code throughout the year. However, there is one area of non-compliance to which I should draw your attention and which relates to my role as executive chairman for part of the year.

I joined the Board as chairman designate in September 2011 with the intention of learning about the Group and the business in order to succeed Lord Sharman as chairman on 1 July 2012. However, as we approached the 2012 annual general meeting, the Company came under strong shareholder pressure to accelerate change, and the Board asked me, as a former seasoned CEO, to take executive responsibility for the Group, and to seek and appoint a new Group Chief Executive Officer (Group CEO). Consequently, in the period from 1 July to 31 December 2012 whilst we did not comply with the Code requirement for the separation of the roles of chief executive and chairman, this was clearly in the interest of shareholders, and firm action was taken during this period to put the Group on to a firmer footing, that may not otherwise have taken place in such a short timeframe. This included major changes to the composition of the Board. We appointed Mark Wilson as Group CEO from 1 January 2013 and this regularised the position, such that we are now compliant with the Code.

Further details of how the Company has applied the Code principles and complied with its provisions are set out in the Corporate Governance Report on pages 89 to 94.

Role of the Board

The Board is responsible to shareholders for promoting the long term success of the Company, and in particular, for setting the Group's strategic aims, monitoring management's performance against these strategic aims, setting the Group's risk appetite and ensuring the Group is adequately resourced and that effective controls are in place in the business. The Board sets the values, tone and culture of the Group. As a regulated Group, the Board also has a duty to protect the interests of policyholders.

Effectiveness of the Board

The effectiveness of the Board is vital to the success of the Group and we undertake a rigorous evaluation each year in order to assess how well the Board, its Committees, the directors and myself are performing and how our effectiveness could be improved. Given the significant changes to the Board during the year I felt that an internal effectiveness review led by myself would be appropriate for 2012. The review was carried out using questionnaires followed by discussion at Board and Committee meetings and through meetings between myself and each director individually. The review focused on the effectiveness of the Board and each Committee, how efficiently time at meetings was used, and the appropriateness of the balance of skills, knowledge and experience represented by Board and Committee members. Overall, the directors concluded that the Board and its Committees operated effectively and agreed that the actions identified for focus and improvement in previous reviews had been addressed and implemented during the year. Areas identified for greater Board focus in 2013 included allocating a greater proportion of time to in-depth discussion of the markets in which the Group operates and their competitive position and re-focusing strategy discussions on long-term strategy, as well as continuing to monitor the Group's capital and liquidity position. I also concluded that each director contributes effectively and demonstrates full commitment to his/her duties.

Board changes

There have been a number of changes to the Board during the year and in early 2013:

- **Lord Sharman** retired from the Board and as chairman on 30 June 2012. He chaired the Board during a period of significant economic uncertainty, bringing extensive experience in the international financial services industry to bear during his tenure.
- **Andrew Moss**, group chief executive, left the Group in May 2012 having led the consolidation of our international presence and the integration of 40 brands into the very powerful single Aviva brand.
- **Mark Wilson** replaced Andrew Moss as Group CEO with effect from 1 January 2013.
- **Igal Mayer**, chief executive of Aviva Europe, resigned in April 2012 when the Group was restructured into Developed Markets and Higher Growth Markets.
- **Leslie Van de Walle** resigned as a non-executive director in May 2012 to pursue other activities.
- **Mary Francis** stepped down from the Board in October 2012 to pursue other interests. Mary had previously been chairman of the Risk Committee.
- **Euleen Goh** resigned from the Board at the end of the year to concentrate on her commitments in Asia.
- **Trevor Matthews**, executive director and chairman, Developed Markets, will step down from the Board prior to the 2013 AGM.
- **Richard Goeltz**, senior independent director, and **Russell Walls**, chairman of the Audit Committee, will both have completed nine years service in May 2013 and will retire from the Board on 8 May 2013. Both have been senior and valuable members of the Board.
- **Glyn Barker** joined the Board as a non-executive director in February 2012 and will become chairman of the Audit Committee on 8 May 2013.

At the same time, we are actively refreshing the Board with new non-executive appointments:

- **Sir Adrian Montague** joined the Board in January 2013 bringing strong insurance and plc credentials, and will become senior independent director on 8 May 2013.
- **Bob Stein** joined the Board in January 2013 bringing strong insurance and actuarial skills.
- We are actively searching for two additional female non-executive directors.

On behalf of the Board I would like to thank all the directors for their contribution to the Company during the year, and particularly those who have retired, or will retire, in 2013 for their dedicated service.



John McFarlane
Chairman
6 March 2013

Board of directors



John McFarlane
Chairman
(Born June 1947)

Appointed to the Board in September 2011 and became executive chairman in July 2012 and non-executive chairman following the appointment of Mark Wilson as Group CEO on 1 January 2013. Currently a non-executive director of Westfield Holdings Ltd (retail mall developer and operator) and Old Oak Holdings Ltd (financial holding company). Former chief executive officer of Australia and New Zealand Banking Group Ltd (banking), executive director of Standard Chartered plc (banking), head of Citicorp and Citibank UK and Ireland, and managing director of Citicorp Investment Bank Ltd (banking). Former director and council member of the London Stock Exchange (financial services) and former non-executive director of the Royal Bank of Scotland Group plc (banking), National Westminster Bank plc (banking), Capital Radio plc (media), The Securities Association (UK securities regulator), the Auditing Practices Board (auditing regulator) and the Business Council of Australia. Former chairman of the Australian Bankers Association and president of the International Monetary Conference. He is chairman of the Board and the Nomination Committee. He has substantial global listed company experience and an excellent track record spanning over 30 years in the UK and international financial services industry.

As executive chairman, he was instrumental in driving forward the Company's strategic plan to narrow the focus of the Group's business portfolio, build financial strength and improve financial performance. He successfully managed the implementation of a culture and values change programme, cutting bureaucracy and delayering the organisation. He has extensive experience in banking, including investment, corporate and retail banking, and in general management, insurance, strategy, risk and cultural change. His wide-ranging board and executive experience provides him with the requisite skills for his chairmanship of the Company and the Board.



Mark Wilson
Group chief executive officer
(Born August 1966)

Appointed to the Board as Group CEO designate in December 2012 and became Group CEO on 1 January 2013. Formerly chief executive officer and president of AIA Group (insurance), and former chief executive of AXA China and AXA South East Asia (insurance). He also previously held a number of senior management positions at National Mutual in New Zealand (insurance).

He has over 25 years of operational and executive experience in the insurance industry across life assurance, general insurance and asset management, in both mature and growth markets. He has extensive experience of leading major international insurance companies and has an excellent track record as a focused and inspirational business leader. At AIA Group and AXA, he successfully developed and implemented short, medium and long-term strategies, delivered robust change programmes and developed and transformed business performance and cultures in challenging market conditions.



Patrick Regan
Chief financial officer
(Born March 1966)

Appointed to the Board in February 2010 as chief financial officer and, since April 2012, has assumed responsibility for Aviva USA. He is chairman of Aviva Investors and is currently a member of the supervisory board of Delta Lloyd N.V.

Formerly group chief financial officer and chief operating officer of Willis Group Holdings Ltd (insurance broking), group financial controller for RSA Insurance Group plc (insurance) and finance and claims director, UK general insurance for AXA Insurance (insurance). He also held a number of senior management positions at GE Capital (financial services) and specialised in corporate finance and investigations at Grant Thornton (professional services).

He has extensive global experience in various executive functions within the insurance industry. He also has an excellent track record of driving change programmes and corporate actions to deliver improved profitability. He has been instrumental in

improving the Group's financial strength, resilience and performance against the backdrop of a challenging macro-economic and regulatory environment. He has brought his significant financial acumen and analytical skills to bear in driving forward the change agenda and in successfully delivering the Group's strategic priorities.



Trevor Matthews
Executive director and chairman,
Developed Markets
(Born March 1952)

Appointed to the Board in December 2011 as chief executive, Aviva UK. In April 2012, he became chairman of the UK & Ireland board and was appointed executive director and chairman, Developed Markets. Currently chairman of the Financial Skills Partnership and a commissioner for the UK Commission for Employment and Skills. Previously chief executive officer and vice chairman of Friends Life (life assurance) and chief executive officer of Friends Provident plc (life assurance). Former chief executive of Standard Life Assurance Company Ltd (life assurance), president and chief executive officer of Manulife Japan (life assurance) and executive vice president, Canadian operations and chairman, Manulife Bank, Toronto (financial services). He has also held senior management positions at National Australia Bank (banking) and Legal & General Assurance Holdings Australia Ltd (insurance).

He has over 40 years of experience in the financial services industry with a track record of achievement in the insurance sector globally. He has brought to the Board an in-depth operational and functional knowledge of insurance, both in the UK and overseas. He will be stepping down from the Board prior to the 2013 AGM.



Glyn Barker
Independent non-executive director
(Born September 1953)

Appointed to the Board in February 2012. Currently chairman of Irwin Mitchell (law firm), a non-executive director of Transocean Ltd (offshore drilling) and The Berkeley Group Holdings plc (construction) and a trustee of the English National

Opera. Formerly vice-chairman UK of PricewaterhouseCoopers LLP with responsibility for leading the executive team for the Europe, Middle East, Africa and India region and was previously UK managing partner, UK head of assurance and a member of the UK management board of PricewaterhouseCoopers LLP. He is a member of the Audit, Nomination and Risk Committees.

He has extensive experience as a business leader and a trusted adviser to FTSE 100 companies and their boards on a wide variety of corporate and finance issues. He brings to the Board a deep understanding of accounting and regulatory issues together with in-depth transactional and financial services experience. He will become chairman of the Audit Committee on 8 May 2013.



Richard Karl Goeltz
Senior independent non-executive director
(Born September 1942)

Appointed to the Board in May 2004 and became senior independent non-executive director in January 2009. Currently a non-executive director of the New Germany Fund (investment trust), the Central Europe and Russia Fund (investment trust) and the European Equity Fund (investment trust), and is also a member of the Council and Court of Governors of the London School of Economics and Political Science. Former non-executive director of the Warnaco Group Inc. (clothing), vice-chairman and chief financial officer of American Express Company (financial services) and director and chief financial officer of NatWest Group plc (banking). Former non-executive director of Delta Air Lines, Inc. (transport) and Federal Home Loan Mortgage Corporation (Freddie Mac) (financial services) and a former member of the Accounting Standards Board (UK).

He has a strong financial background and has over 20 years' experience in the financial services industry. He has held a broad range of executive and non-executive positions in major global corporations. His experience of audit and governance committees has been invaluable in providing effective oversight as a member of the Company's Audit Committee.

He is currently a member of the Audit and Nomination Committees and will retire from the Board, as senior independent non-executive director, and from the Audit and Nomination Committees after nine years of service to the Board on 8 May 2013.



Michael Hawker AM
Independent non-executive director
(Born October 1959)

Appointed to the Board in January 2010. Currently a non-executive director of Macquarie Group Ltd (banking) and Macquarie Bank Ltd (banking), Washington H Soul Pattinson Pty Ltd (investment), International Rugby Development Ltd (rugby), and IRFB Services (Ireland) Ltd (rugby). He is chairman and non-executive director of the Australian Rugby Union and SANZAR Pty Limited (rugby union) and is a non-executive director/trustee of the George Institute for Global Health (UK). He is a member of the advisory council at General Enterprise Management Services International Ltd (private equity), and council member of the International Rugby Board. Formerly chief executive and managing director of Insurance Australia Group (insurance), group chief executive of business and consumer banking at Westpac Banking Corporation (banking) and chairman of the Insurance Council of Australia. Senior fellow of the Financial Services Institute of Australasia and a fellow of the Australian Institute of Company Directors. He is chairman of the Risk Committee and a member of the Audit, Nomination and Remuneration Committees. He will step down as a member of the Remuneration Committee on 8 May 2013.

He has a wealth of knowledge and experience gained over a long career in the banking and insurance industries, in both executive and non-executive roles in Europe, Asia and Australia. He has been a highly effective chairman of the Risk Committee during a period of significant volatility in the external economic environment.



Gay Huey Evans
Independent non-executive director
(Born July 1954)

Appointed to the Board in October 2011. Currently a non-executive director of the London Stock Exchange Group plc (financial services), Clariden Leu (Europe) Ltd (financial services), Bank Itau BBA International Limited (banking) and the Financial Reporting Council. Member of the management board and of the panel of finance experts of the Panel of Recognised International Market Experts in Finance (PRIME Finance), and a trustee of Wellbeing of Women (UK) (charity) and The Wigmore Hall Trust (charity). Formerly chair of the International Swaps and Derivatives Association, Inc. (ISDA) (financial trade association), vice-chairman, investment banking & investment management at Barclays Capital (banking) and she held senior management positions at Citi Alternative Investments (EMEA) (banking), the Financial Services Authority (UK regulator) and Bankers Trust Company (banking). She is chairman of the Corporate Responsibility Committee and a member of the Nomination and Remuneration Committees.

She has over 30 years of experience within the financial services industry, having held key positions in government and in a number of global financial and banking institutions. In addition to the financial expertise she brings to the Board, her experience at the Financial Services Authority continues to provide an insight into the priorities and focus of the Group's lead regulator.



Sir Adrian Montague CBE
Independent non-executive director
(Born February 1948)

Appointed to the Board in January 2013. Currently chairman of 3i Group plc (private equity) and Anglian Water Group Ltd (utilities), deputy-chairman and senior independent director of UK Green Investment Bank plc (investment bank) and a non-executive director of Skanska AB (construction). Formerly chairman of Friends Provident plc (life insurance), British Energy Group plc (utilities), Michael Page International plc (recruitment), and Cross London Rail Links Ltd (Crossrail), and was formerly deputy-chairman of Network Rail Ltd (railway network authority) and Partnerships UK plc (public private partnership). He was also previously chief executive of the Treasury Taskforce. He is a member of the Audit, Corporate Responsibility and Nomination Committees. He will become senior independent non-executive director on 8 May 2013.

Sir Adrian brings his significant experience of the financial services industry and in government and regulatory circles to the Board.



Bob Stein
Independent non-executive director
(Born February 1949)

Appointed to the Board in January 2013. Currently a non-executive director and vice-chair of the audit committee of Assurant, Inc (US specialty insurance) and is a trustee emeritus of the board of trustees of the Actuarial Foundation. He spent most of his working life at Ernst & Young in the US, where he held a number of managing partner roles in the actuarial, insurance and financial services practices in the US and globally, culminating in being managing partner, global actuarial practice. He is a member of the Nomination, Risk and Remuneration Committees.

He brings significant accounting and financial services experience to the Board.



Russell Walls
Independent non-executive director
(Born February 1944)

Appointed to the Board in May 2004. Currently non-executive director of Biocon Ltd (biopharmaceuticals), Signet Jewelers Ltd (retail), Syngene Ltd (contract research pharmaceuticals), and Mytrah Energy Ltd (wind power producer). Former group finance director of BAA plc (transport), Wellcome plc (pharmaceuticals) and Coats Viyella plc (textiles), treasurer and trustee of the British Red Cross (charity) and a member of the Finance Commission of the International Federation of the Red Cross (charity). Formerly senior independent director and chairman of the audit committee of Stagecoach Group plc (transport) and Hilton Group plc (leisure) and a non-executive director of Delphic Diagnostics Ltd (medical), and Mersey Docks and Harbour Company (transport).

He has a strong financial background and a wealth of international experience across a range of sectors. With his deep financial acumen, analytical approach and extensive audit experience over a long financial career, he has been a robust Audit Committee chairman against a backdrop of macro-economic instability and changes to the audit environment.

He is currently chairman of the Audit Committee and a member of the Nomination and Risk Committees and will retire from the Board, as Audit Committee chairman and from the Nomination and Risk Committees after nine years of service to the Board on 8 May 2013.



Scott Wheway
Independent non-executive director
(Born August 1966)

Appointed to the Board in December 2007. Former chief executive officer of Best Buy Europe (retail services), director of The Boots Company plc (now known as The Boots Company Ltd) (pharmacy) and managing director and retail director of Boots the Chemist at Alliance Boots plc, and director of the British Retail Consortium. He formerly held a number of senior executive positions at Tesco plc (retail services), including chief executive of Tesco in Japan. He is chairman of the Remuneration Committee and a member of the Corporate Responsibility and Nomination Committees.

He has a wealth of business experience in the retail sector and his understanding of customer priorities has been greatly beneficial in driving the customer agenda and excellence in customer service within the business. He has chaired the Remuneration Committee with vigour and has rebuilt the Group's standing with its significant investors in relation to the Group's remuneration policy. Following the issues raised at the 2012 annual general meeting, he led an extensive consultation exercise with the Company's major shareholders and a significant review of the Group's remuneration policies and practices.

Group Executive

The Group Executive is made up of the executive directors and the senior executives whose biographies appear below. The Group Executive meets weekly as a forum for the Group CEO to discuss the strategic, financial, reputational and commercial aspects of the Group. The forum does not have decision-making authority in its own right and authority rests with each of the members (within their respective remits).

David Barral **Chief executive officer, Aviva UK & Ireland Life** **(Born March 1962)**

Appointed chief executive officer, Aviva UK Life in June 2011. In March 2012 he took on additional responsibility for Aviva's Life business in Ireland, becoming chief executive officer, Aviva UK & Ireland Life. He became a member of the Group Executive in April 2012.

He was formerly chief operating officer for Aviva UK Life responsible for customer propositions, pricing and customer operations.

He joined Aviva in 1999 as director of independent financial advisor business and was appointed distribution director in 2005 covering independent financial advisor (IFA), retail, partnership and employee benefit channels. In 2008 he was appointed marketing director and led the Aviva rebrand for the UK Life business.

During his time at Aviva, he has spearheaded much of the UK Life and pensions business' activities to champion the customer, including supporting a move to the open market option for UK annuity customers.

Prior to joining Aviva, he spent 20 years in financial services including roles in sales, marketing, operations and business transformation at organisations including Eagle Star, Prudential and Morgan Grenfell.

Paul Boyle **Chief audit officer** **(Born July 1959)**

Joined Aviva in November 2010 as chief audit officer and became a member of the Group Executive in August 2012.

He was formerly the first chief executive of the Financial Reporting Council (FRC), the UK's independent regulator responsible for promoting confidence in corporate reporting and governance, from 2004 until 2009. Whilst in this role, he led the establishment of the International Forum of Independent Audit Regulators serving as its chairman or vice-chairman from 2006 until 2009. Before joining the FRC, he was a member of the leadership team at the Financial Services Authority, serving as chief operating officer from 2000 until 2004. He has also held senior management roles in WH Smith Group plc and Cadbury Schweppes plc.

Kirstine Cooper **Group general counsel and company secretary** **(Born August 1964)**

Joined Aviva in 1991 and is the group general counsel and company secretary for Aviva plc and heads the Office of the Chairman. She was appointed to the Group Executive in May 2012 and leads the legal and company secretarial function for Aviva globally.

She is a lawyer and worked in the legal function at Aviva's legacy companies before leading the property division of General Accident and the group legal function of CGU for eight years. She was formerly deputy group company secretary and legal counsel of Aviva plc. Since her appointment as group general counsel and company secretary she has created Aviva's first global legal leadership team.

Carole Jones **Acting group HR director** **(Born June 1960)**

Joined Aviva in 1990 and is acting group HR director with responsibility for managing human resources across the Group. She joined the Group Executive in July 2012.

She has been with the Group for more than 20 years, initially as HR manager in the UK Life and General Insurance businesses. In 2006 she was appointed acting human resources director for the Group's Norwich Union Life business in the UK, and in 2008 she relocated to the US where she led the HR function for Aviva's North American region until she returned to the UK as director of HR strategy & organisational development in 2011. She was appointed acting group HR director in July 2012.

John Lister **Group chief risk and capital officer** **(Born April 1958)**

Joined Aviva in 1986 and is the group chief risk and capital officer. He has overall responsibility for managing capital across Aviva, preparing the business for Solvency II and ensuring that an appropriate risk management framework is in place.

He has more than 25 years' experience working in the UK Life business. He is an actuary and spent the first nine years of his career in a variety of senior actuarial roles across the UK Life business before becoming its chief actuary in 2005. In 2009 he became finance director of Aviva UK Life, and in April 2012 he was appointed group chief capital officer.

His role was expanded in July 2012 and he became group chief capital and risk officer, with responsibility for the Group's risk and capital functions, and a member of the Group Executive reporting to Mark Wilson for risk matters and Patrick Regan for capital matters.

Amanda Mackenzie **Chief marketing and communications officer** **(Born December 1963)**

Joined Aviva in March 2008 and is chief marketing and communications officer with responsibility for all Group marketing, communications and public affairs. She is also the executive sponsor for diversity and inclusion. She joined the Group Executive in 2008.

She oversaw the rebrand of the Group and set up the global marketing and communications function.

She has 25 years of marketing and advertising experience, including director roles at British Airways Airmiles, BT and British Gas. She is a non-executive director at Mothercare plc.

David McMillan **Chief executive officer, Aviva Europe** **(Born February 1966)**

Joined Aviva in November 2002 and is chief executive officer Aviva Europe with accountability for the Group's businesses in Italy, Lithuania, Poland, Russia, Spain and Turkey. He is also chairman of Aviva France SA. He joined the Group Executive in April 2012.

He was previously group transformation director with responsibility for managing the implementation of Aviva's strategic plan across the Group, refocusing and optimising the Group's business portfolio, achieving financial strength, improving performance, and building a high-performance ethic across Aviva.

He was previously chief executive officer, Aviva UK & Ireland General Insurance, chief operating officer for Aviva UK General Insurance, chairman of Aviva Global Services and non-executive director of Aviva Health and began his career with Aviva as director of partnerships (bancassurance).

Prior to joining Aviva, he spent 12 years as director of management consultancy with PricewaterhouseCoopers LLP. His role involved leading projects spanning mergers and acquisitions, retail banking, organisational strategy and change.

Cathryn Riley
Chief operations officer
(Born April 1962)

Joined Aviva in 1996 and is chief operations officer with responsibility for IT, business change and shared services across the Group. She joined the Group Executive in May 2011.

She joined Commercial Union in 1996 and subsequently held a number of senior roles in its successor companies, CGU and Norwich Union. She served as operations director and retail director at Norwich Union and spent seven years in various executive roles within Aviva's UK General Insurance business. She has also previously served as managing director Norwich Union Healthcare, business services director of Norwich Union Life, chief operating officer Aviva UK Life, chief operating officer and chief information officer of Aviva Europe and UK commercial director. She is currently a non-executive director of Equitable Life.

Robin Spencer
Chief executive officer, Aviva UK & Ireland General Insurance
(Born January 1970)

Joined Aviva in 1995 and is chief executive officer, UK & Ireland General Insurance with responsibility for leading Aviva's largest general insurance business. He joined the Group Executive in January 2010.

He was previously group chief risk officer, chief financial officer and subsequently president and chief executive officer of Aviva Canada. Prior to that, he was global finance transformation director.

He previously worked in Group Finance in London and held a number of senior finance roles with Norwich Union Insurance, including finance director for London & Edinburgh, a subsidiary of Aviva. Prior to joining Aviva, he spent five years with Procter & Gamble in the UK.

Maurice Tulloch
President and chief executive officer,
Aviva Canada
(Born March 1969)

Joined Aviva in 1992 and is president and chief executive officer of Aviva Canada with responsibility for the strategic direction and operation of Canada's second largest property and casualty insurer, and the second largest general insurance operation in the Group. He joined the Group Executive in July 2012.

He was previously executive vice-president and chief operating officer, Aviva Ontario and specialty distribution and previously held several senior management positions in the Group.

He is chair of the Insurance Bureau of Canada (IBC), chair of the Property & Casualty Insurance Compensation Corporation (PACICC) Board, chair of the Insurance Institute of Canada (IIC) Board and a member of the General Insurance Statistical Agency (GISA) Board.

He is a member of IBC's National Auto Insurance Committee, GISA's Executive Committee and Statistical Plan Committee, Toronto Financial Services Alliance (TFSA) Leadership Council Committee, and the Financial Services Commission of Ontario (FSCO) CEO Advisory Committee.

Jason Windsor
Chief strategy and development officer
(Born August 1972)

Joined Aviva in May 2010 and is the chief strategy and development officer, with additional executive responsibility for overseeing Aviva Investors. He joined the Group Executive in February 2013.

He was formerly chief strategy & planning officer with responsibility for mergers, acquisitions and disposals, the Group's strategic financial plan and oversight of Aviva's Investor Relations function.

Prior to joining Aviva, he was managing director in the Financial Institutions Group at Morgan Stanley, with management responsibility for the European asset management sector.

Directors' report

The directors submit their Annual Report and Accounts for Aviva plc, together with the consolidated financial statements of the Aviva group of companies, for the year ended 31 December 2012.

The Performance Review on pages 25 to 60, the Corporate Responsibility Report on pages 61 to 76, Shareholder Information on pages 121 to 144 (which includes the risks relating to our business), the Corporate Governance Report on pages 89 to 94, and the Directors' Remuneration Report on pages 104 to 120 are incorporated into this Directors' Report by reference and, together with this Directors' Report constitute the Business Review required under the Companies Act 2006 and the Management Report required under Disclosure and Transparency Rule 4.1.5R. Details of material acquisitions and disposals made by the Group during the year are contained in note 3.

Results

The Group's results for the year are shown in the consolidated income statement on page 160.

Principal activity

The Company is the holding company of the Aviva plc group of companies (Group) whose principal activities are the provision of general insurance, life assurance, long term savings and fund management services.

Dividends

The directors are recommending a final dividend of 9.00 pence per ordinary share (2011: 16.00 pence), which, together with the interim dividend of 10.00 pence per ordinary share paid on 16 November 2012 (2011: 10.00 pence), produces a total dividend for the year of 19.00 pence per ordinary share (2011: 26.00 pence). The total cost of ordinary dividends paid in 2012 was £757 million (2011: £738 million). Subject to shareholder approval at the 2013 Annual General Meeting, the final dividend for 2012 will be paid on 17 May 2013 to all holders of ordinary shares on the Register of Members at the close of business on 22 March 2013 (and approximately five business days later for holders of the Company's American Depositary Receipts).

Share capital and control

The issued ordinary share capital of the Company was increased by 40,259,323 ordinary shares during the year. 3,335,566 shares were allotted under the Group's employee share and incentive plans and 36,923,757 shares were allotted under the Aviva Scrip Dividend Scheme for the May 2012 and November 2012 dividends. At 31 December 2012 the issued ordinary share capital totalled 2,945,972,261 shares of 25 pence each and the issued preference share capital totalled 200 million shares of £1 each. Accordingly, the issued and paid-up ordinary share capital constituted 79% of the Company's total issued share capital and the issued preference share capital constituted 21% of the Company's total issued share capital at 31 December 2012. All the Company's shares in issue are fully paid up and the ordinary and preference shares have a Premium and Standard listing respectively on the London Stock Exchange. The Company is listed on the New York Stock Exchange (NYSE) in the form of American Depositary Shares, referenced to ordinary shares, under a depositary agreement with Citibank. Details of the Company's share capital and shares under option at 31 December 2012 and shares issued during the year are given in notes 29 to 32.

The rights and obligations attaching to the Company's ordinary shares and preference shares, together with the powers of the Company's directors, are set out in the Company's articles of association, copies of which can be obtained from Companies House and the Company's website at www.aviva.com/investor-relations/corporate-governance/articles-of-association, or by writing to the group company secretary.

With the exception of restrictions on transfer of the ordinary shares under the Company's employee share incentive plans whilst the shares are subject to the rules of the plans, there are no restrictions on the voting rights attaching to the Company's ordinary shares or the transfer of securities in the Company.

Where, under an employee share incentive plan operated by the Company, participants are the beneficial owners of shares but not the registered owners, the voting rights are normally exercised at the discretion of the participants. No person holds securities in the Company carrying special rights with regard to control of the Company. The Company is not aware of any agreements between holders of securities that may result in restrictions in the transfer of securities or voting rights. Unless expressly specified to the contrary in the articles of association, the articles of association may only be amended by special resolution of the Company's shareholders in general meeting. There are a number of agreements that take effect, alter or terminate upon a change of control of the Company, such as commercial contracts and joint venture agreements. None are considered to be significant in terms of their potential impact on the business of the Group as a whole. All of the Company's employee share incentive plans contain provisions relating to a change of control. Outstanding awards and options would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions and pro rata reduction as may be applicable under the rules of the employee share incentive plans.

At the Annual General Meeting (AGM) in 2013, shareholders will be asked to renew the directors' authority to allot new securities. Details are contained in the 2013 Notice of Annual General Meeting (Notice of AGM).

Authority to purchase own shares

At the Company's 2012 AGM, shareholders renewed the Company's authorities to make market purchases of up to 290 million ordinary shares, up to 100 million 8¾% preference shares and up to 100 million 8⅜% preference shares. These authorities were not used during the year or up to the date of this Report. At the 2013 AGM, shareholders will be asked to renew these authorities for another year and the resolution will once again propose a maximum aggregate number of ordinary shares which the Company can purchase of less than 10% of the issued ordinary share capital. Details are contained in the Notice of AGM. The Company held no treasury shares during the year or up to the date of this Report.

Major shareholdings

The table below shows the holdings of major shareholders in the Company's issued ordinary share capital in accordance with the Disclosure and Transparency Rules as at 31 December 2012 and 5 March 2013.

Shareholding interest

Shareholder	At 31 December 2012		At 5 March 2013	
	Notified holdings	Nature of holding	Notified holdings	Nature of holding
BlackRock, Inc ¹	5.15%	Indirect	5.15%	Indirect
Legal & General Group plc ²	3.98%	Direct	3.98%	Direct
AXA S.A. ¹	3.86%	Direct & indirect	3.86%	Direct & indirect

¹ Holding includes holdings of subsidiaries.

² Interest held by Legal & General Assurance (Pensions Management) Ltd.

Directors

The directors as at the date of this Report are shown together with their biographical details on pages 80 to 82. During the year and up to the date of this Report, the following Board appointments, resignations and retirements occurred:
Glyn Barker – appointed 27 February 2012
Igal Mayer – resigned 19 April 2012
Leslie Van de Walle – resigned 2 May 2012
Andrew Moss – resigned 8 May 2012

Lord Sharman of Redlynch – retired 30 June 2012
 Mary Francis – resigned 3 October 2012
 Mark Wilson – appointed 1 December 2012 and became
 Group CEO on 1 January 2013
 Euleen Goh – resigned 31 December 2012
 Sir Adrian Montague – appointed 14 January 2013
 Bob Stein – appointed 28 January 2013

Directors' interests and indemnity arrangements

At no time during the year did any director hold a material interest in any contract of significance with the Company or any of its subsidiary undertakings other than an indemnity provision between each director and the Company and employment contracts between each executive director and a Group company. There is no arrangement or understanding with any shareholder, customer, supplier, or any other external party, to appoint a director or a member of the Group Executive. The Company has purchased and maintained throughout the year, directors' and officers' liability insurance in respect of itself and its directors. The directors also have the benefit of the indemnity provision contained in the Company's articles of association. The Company has executed deeds of indemnity for the benefit of each director of the Company, and each person who was a director of the Company during the year, in respect of liabilities that may attach to them in their capacity as directors of the Company or of associated companies. These indemnities were granted at different times according to the law in place at the time and where relevant are qualifying third-party indemnity provisions as defined by section 234 of the Companies Act 2006. These indemnities were in force throughout the year and are currently in force. Details of directors' remuneration, service contracts, employment contracts and interests in the shares of the Company are set out in the Directors' Remuneration Report.

Financial instruments

Group companies use financial instruments to manage certain types of risks, including those relating to credit, foreign currency exchange, cash flow, liquidity, interest rates, and equity and property prices. Details of the objectives and management of these instruments are contained in the Risk and Capital Management section on pages 56 to 59, the Shareholder Information section on pages 121 to 144 and an indication of the exposure of the Group companies to such risks is contained in note 56 to the consolidated financial statements.

Health and safety

Aviva is committed to providing a safe and healthy working environment for all staff, contractors and anyone who is or may be affected by the business' undertakings. The Group's health and safety standard sets out the range of policies, procedures and systems required to manage risks and promote wellbeing. This includes appropriate staff consultation through nominated health and safety representatives. The Group CEO has overall accountability for health and safety across the organisation. Health and safety performance is regularly reviewed through the Corporate Responsibility Committee.

Charitable donations

Aviva takes its corporate citizenship seriously and recognises the role it plays in the communities in which it operates and the role they play in its business. The Group's flagship community development programme is 'Street to School'. Further details of this and the Group's other charitable, community and corporate responsibility initiatives are disclosed in the Corporate Responsibility Report on pages 61 to 76.

During 2012, £5.7 million was donated in cash to UK-based charities by the Company and its subsidiaries. A total of £8.9 million was donated by the Group world-wide.

Political donations

At the 2012 AGM, shareholders passed a resolution, on a precautionary basis, to authorise the Company to make political donations and/or incur political expenditure (as such terms are defined in sections 362 to 379 of the Companies Act 2006), in each case in amounts not exceeding £100,000 in aggregate. As the authority granted will expire on 9 May 2013, renewal of this authority will be sought at this year's AGM. Further details are available in the Notice of AGM. The definitions of political donations and political expenditure used in the Companies Act 2006 are broad in nature and this authority is sought to ensure that any activities undertaken throughout the Group, which could otherwise be construed to fall within these provisions, can be undertaken without inadvertently infringing them. It is not the policy of the Company to make donations to EU political organisations or to incur other political expenditure.

During the year, the Aviva USA Political Action Committee, which is funded solely by voluntary contributions from employees of Aviva USA Corporation (a subsidiary of the Company), made contributions to six candidate campaigns and industry political action committees. The total sum of the donations made was \$32,500 and the donations were used to support candidates for nomination and/or election to public office.

Group employees

The Group's statement on its employees is set out in the Corporate Responsibility Report. In summary, the Group's commitment to communication and dialogue with employees continues. The existence of a Group-wide intranet enables engagement and communication with employees throughout the Group. It also helps management to share information, ideas and opportunities quickly and to achieve a common awareness on the part of all employees of the financial and economic factors affecting the performance of the Company. A strong emphasis is placed on the provision of news and information through a range of media. Employees have opportunities to voice their opinions and ask questions through intranet sites, question and answer sessions with the Group CEO, via telephone conferencing, opinion surveys and the Group's Employee Promise Survey which is open to all employees. Face-to-face briefings and team meetings are actively encouraged and are held in business units across the Group. The Group's businesses in the UK have established employee consultative forums and a European Consultative Forum convenes annually to discuss matters impacting the business across Europe. The Group ensures that involvement of employees in its performance is encouraged by allowing eligible employees in the UK to participate in the Group's employee share ownership plans.

Employee practice

The Group respects all fundamental human rights and is guided in the conduct of its business by the provisions of the United Nations Universal Declaration of Human Rights and the International Labour Organization core labour standards. The Group also supports the United Nations Global Compact Principles. The Group is committed to providing equal opportunities to all employees, irrespective of their gender, sexual orientation, marital status, race, nationality, ethnic origin, disability, age, religion or union membership status. Aviva is an inclusive employer and values diversity among its employees. These commitments extend to recruitment and selection, training, career development, flexible working arrangements, promotion and performance appraisal.

Creditor payment policy and practice

It is the Group's policy to pay creditors when they fall due for payment and the Company follows the government endorsed Prompt Payment Code which can be found at www.promptpaymentcode.org.uk. Terms of payment are agreed with suppliers when negotiating each transaction and the

policy is to abide by those terms, provided that the suppliers also comply with all relevant terms and conditions. In respect of Group activities in the UK, the amounts due to trade creditors at 31 December 2012 represented 17.9 days of average daily purchases through the year (2011: 22.2 days).

Disclosure of information to the auditor

In accordance with section 418 of the Companies Act 2006, the directors in office at the date of approval of this Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor, PricewaterhouseCoopers LLP (PwC), is unaware and each director has taken all steps that ought to have been taken as a director to be aware of any relevant audit information and to establish that PwC is aware of that information.

Change of auditor

Following a tender process in 2011, PwC was appointed as the Company's external auditor commencing with the 2012 financial year and its appointment was approved by shareholders at the 2012 AGM. PwC is subject to annual re-election and resolutions on its appointment and seeking authorisation for the directors to set the auditor's remuneration are included in the Notice of AGM.

Annual General Meeting

The 2013 AGM of the Company will be held on Thursday, 9 May 2013 at the Barbican Centre, Silk Street, London EC2Y 8DS at 11am. The Notice of AGM convening the meeting describes the business to be conducted thereat.

Related party transactions

Details of related party transactions are disclosed in note 59 which is incorporated into this Report by reference.

Value of interests in land

Any difference between market value and the value included in the balance sheet regarding the Group's interests in land are disclosed in notes 20 and 21 and are incorporated into this Report by reference.

Events after the reporting period

On 8 January 2013 the Company announced its intention to sell the Group's remaining stake in Delta Lloyd N.V., a Dutch listed insurance company. The sale took place by way of an accelerated book build offering and the Group's entire remaining holding of 34,288,795 ordinary shares in Delta Lloyd N.V. was sold at a price of €12.65 per share. The sale completed on 14 January 2013.

On 17 January 2013 the Company announced it had agreed to sell the Group's stake in its Malaysian joint ventures, CIMB Aviva Assurance Berhad and CIMB Aviva Takaful Berhad, to Sun Life Assurance Company of Canada for £152 million payable in cash. The deal is subject to regulatory approval and is expected to complete during the first half of 2013.

On 27 February 2013 the Company announced it had agreed to sell Aviva Russia to Blagosostoyanie, a non-state pension fund in Russia, for a consideration of €35 million payable in cash. The sale is subject to approval by the Federal Antimonopoly Service of the Russian Federation and it is expected that the sale will complete during the first half of 2013.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Essential Read on pages 1 to 24, which includes the Market Focus section on pages 20 to 24. The Performance Review is set out on pages 25 to 60 and includes the Risk and Capital Management section on pages 56 to 59. In addition, the financial statements sections include notes on the Group's borrowings (note 48); its contingent liabilities and other risk factors (note 51); its capital structure and position (note 53); management of its risks including market, credit and liquidity risk (note 56); and derivative financial instruments (note 57).

The Group has considerable financial resources together with a diversified business model, with a spread of businesses and geographical reach. As a consequence, the directors believe that the Group is well placed to manage its business risks successfully.

After making enquiries, the directors have a reasonable expectation that the Company and the Group as a whole have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

Directors' responsibilities

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

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

- Select suitable accounting policies and then apply them consistently;
- Make judgements and accounting estimates that are reasonable and prudent;
- State whether applicable IFRS as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' responsibility statement

Each of the directors listed on pages 80 to 82 confirm that, to the best of their knowledge:

- The Group financial statements, which have been prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit/(loss) of the Group; and
- The Directors' Report and the Management Report include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

By order of the Board on 6 March 2013.



Mark Wilson
Group chief executive officer



Patrick Regan
Chief financial officer

This Report sets out the role and activities of the Board, its effectiveness, and how the Group is governed. The Board's role is to provide entrepreneurial leadership of the Company within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board believes that a strong system of governance is essential to help the business run smoothly and aid effective decision making in order to support the achievement of the Group's objectives.

The UK Corporate Governance Code

As a UK listed company, Aviva seeks to comply with the UK Corporate Governance Code 2010 (the Code). An amended version of the Code was issued in September 2012 which is applicable to companies with a UK premium listing with financial years beginning on or after 1 October 2012; the Company will report on its compliance with the 2012 version of the Code in its 2013 Annual Report and Accounts.

It is the Board's view that the Company has been fully compliant throughout the accounting period with the relevant provisions of the Code with the exception of the following:

- Provision A.2.1 states that the roles of chairman and chief executive should not be exercised by the same individual and provision A.3.1 states that the chairman should be independent on appointment to the Board. John McFarlane joined the Board as chairman designate in 2011 with the intention that he would take over the chairmanship of the Company on the retirement of Lord Sharman in June 2012. However, due to the unforeseen departure of Andrew Moss in May 2012, the Board asked John McFarlane to take on executive responsibility for running the Company in the interim period until a new Group CEO was appointed. As a result from 1 July 2012 until 1 January 2013 John McFarlane acted as executive chairman. He became non-executive chairman on 1 January 2013 on the appointment of Mark Wilson as Group CEO. The Board believes that this non-compliance with the Code was justified in the circumstances given the timing of Andrew Moss' departure and the need to ensure the continued effective operation of the Company until a new Group CEO could be identified and appointed. The Board was satisfied that there was a sufficient balance between executive and non-executive directors on the Board during this period to ensure that no one individual had unfettered decision-making powers.
- Provision E.1.1 states that the senior independent director should attend sufficient meetings with a range of major shareholders to listen to their views in order to help develop a balanced understanding of the issues and concerns of major shareholders. Whilst Richard Goeltz did not meet with major shareholders during 2012, throughout the year John McFarlane and, separately, the chairman of the Remuneration Committee, undertook a programme of meetings with major shareholders to take soundings regarding the Company and to understand their concerns.

Further details of how the Company has applied the Code principles and complied with its provisions are set out in this Report, the Reports of each Board Committee and the Directors' Remuneration Report.

Further information on the Code can be found on the Financial Reporting Council's website at www.frc.org.uk.

The Board

The Board is responsible to shareholders for promoting the long term success of the Company and, in particular, for setting the Group's strategic aims, monitoring management's performance against the strategic aims, setting the Group's risk appetite, ensuring the Group is adequately resourced and ensuring that effective controls are in place in the business. The Board also sets

the values and the culture of the Group and has a duty to protect the interests of policyholders.

The specific duties of the Board are clearly set out in its terms of reference which address a wide range of corporate governance issues and lists those items that are specifically reserved for decision by the Board. Matters requiring Board approval include:

- Group strategy and business plans;
- Financial reporting and controls, capital structure and dividend policy;
- Group risk appetite and framework;
- Corporate governance;
- Remuneration policy;
- Significant transactions and expenditure; and
- Other matters (e.g. appointment and removal of the group company secretary and chief risk and capital officer, Board and Committee succession planning and the constitution of Board Committees).

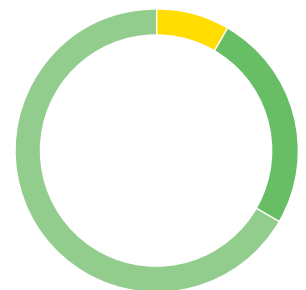
The Board's terms of reference also set out those matters that must be reported to the Board, such as senior leadership changes, significant litigation or material regulatory breaches, and cover how matters requiring consideration by the Board that arise between scheduled meetings should be dealt with.

The directors

As at the date of this Report the Board comprises the chairman, Group CEO, two further executive directors and eight independent non-executive directors. The following charts show the balance of the Board between executive and non-executive representation, length of tenure and the diversity of the Board in terms of gender and nationality.

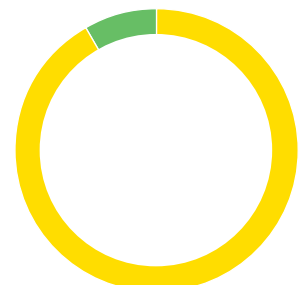
Balance of executive and non-executive directors

Chairman	1
Executive directors	3
Non-executive directors	8



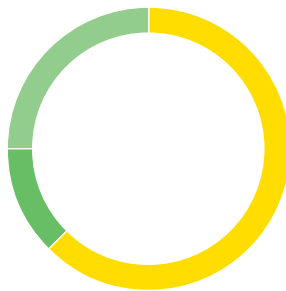
Gender split of directors

Male	11
Female	1

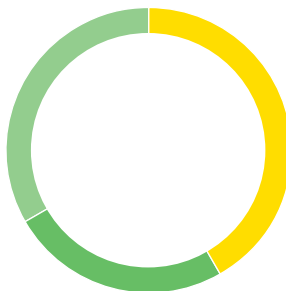


Length of tenure of non-executive directors

0-3 years	5
3-6 years	1
6-9 years	2
+9 years	0

**Geographical mix**

UK	5
US	3
Other	4



The Board's policy is to appoint and retain non-executive directors who can apply their wider business knowledge and experiences to their understanding of the Aviva Group, and to review and refresh regularly the skills of the Board. In line with Code requirements regarding the independence of non-executive directors, several non-executive directors, including the chairman, retired in 2012 or are due to retire in 2013. The Report of the Nomination Committee sets out the work carried out during the year on succession planning which culminated in the appointment of Sir Adrian Montague and Bob Stein as non-executive directors in January 2013 and Mark Wilson joining the Board in December 2012 and becoming Group CEO on 1 January 2013.

It is the Board's view that independent non-executive directors need to be able to present objective, rigorous and constructive challenge to management, drawing on their wider experiences to question assumptions and viewpoints and where necessary defend a given position. The independent non-executive directors should also assist management in the development of the Company's strategy. To be effective, an independent director needs to acquire a sound understanding of the industry and the Company so as to be able to evaluate properly the information provided. Having considered the matter carefully, the Board is of the opinion that all of the current non-executive directors are independent and free from any relationship or circumstances that could affect, or appear to affect, their independent judgement. Accordingly, over half of the Board members, excluding the chairman, are independent non-executive directors. All of the current directors that served during 2012 were subject to a formal performance evaluation during 2012 except Mark Wilson as he only joined the Board in December 2012. Non-executive directors who had served on the Board for more than six years were subject to a particularly rigorous review of their independence. As at the date of this Report, Richard Goeltz and Russell Walls have served on the Board for more than six years and they will both be retiring from the Board on 8 May 2013 having completed nine years of service. Biographical details including a summary of the skills and experience the directors bring to the Board are set out on pages 80 to 82.

Each director must be able to devote sufficient time to the role in order to discharge his or her responsibilities effectively. On average, directors spend at least 41 days a year on Company

business, with the chairmen of the Audit, Risk and Remuneration Committees spending substantially more.

The chairman and Group CEO

Role profiles are in place for the chairman and Group CEO which clearly set out the duties of each role. The chairman's priority is leadership of the Board and ensuring its effectiveness; the Group CEO's priority is the management of the Group. The Board has delegated the day-to-day running of the Group to the Group CEO within certain limits, above which matters must be escalated to the Board for consideration and approval. As noted above, the roles of chairman and Group CEO were combined and undertaken by John McFarlane prior to the 2013 AGM until the end of the year. The Board agrees with the principle in the Code requiring these roles to be carried out by separate individuals. However, due to unforeseen circumstances during the year the Board unanimously agreed that it was in the best interests of the Company for the benefit of its shareholders to combine the roles for a short period until a new Group CEO could be recruited. From 1 January 2013 the roles are no longer combined.

Senior independent director

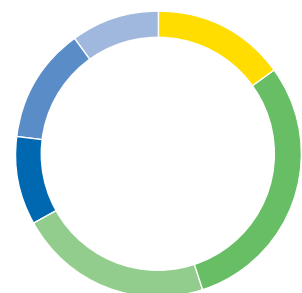
Richard Goeltz has served as the senior independent director since January 2009 and as an independent non-executive director for nearly nine years. Sir Adrian Montague will take over this role on 8 May 2013 when Richard Goeltz retires from the Board. The role of the senior independent director is to provide a sounding board for the chairman, to serve as an intermediary for the other directors where necessary and to be available to shareholders should they have concerns that they have been unable to resolve through normal channels, or when such channels would be inappropriate. During the year, the non-executive directors, led by Richard Goeltz, have met twice without the chairman present and he led the review of the chairman's performance during the year.

Board activities during 2012

The work of the Board follows an agreed annual work plan and principally falls under six main areas. The following chart shows how the Board allocated its time during 2012.

Allocation of Board agenda time

Succession planning, Board composition and effectiveness	15%
Group strategy, business plans and performance monitoring	30%
Financial reporting and controls, capital structure and dividend policy	22%
Corporate governance	10%
Group risk management policies, risk appetite and framework	13%
Others	10%



The Board monitored the performance of the Group and its compliance with the governance framework described below through regular:

- Group CEO reports highlighting issues such as strategic planning and execution; updates on ongoing corporate transactions; financial forecasts and results; the Group's vision and values; the external environment; personnel changes and market and competitor developments;
- Chief financial officer reports on a range of issues including financial results and forecasts; capital; operational performance; strategic initiatives; pensions funding deficit; investor relations and rating agency updates; risk appetite; corporate transactions and progress against Solvency II;
- Reports and recommendations from each Board Committee; and
- Reports from business units and functions.

As part of its annual work plan, the Board reviewed and approved all financial results announcements, the Annual Report and Accounts, the operational plan and dividend payments; considered succession plans for the Board and Group Executive; approved all changes to the composition of the Board and its Committees; reviewed the performance of the group chief executive; received regular updates on progress against strategy; considered personnel issues including the results of the annual employee promise survey; and reviewed public policy trends.

In addition, the Board undertook the following specific activities during the year:

- Agreed a revised strategic plan to narrow the focus of the Group, build financial strength and improve financial performance;
- Approved the Group transformation project to implement the revised strategic plan;
- Appointed PwC as the Company's auditor following a tender process;
- Approved the sale of Aviva USA Corporation;
- Approved a further sale of Aviva's stake in Delta Lloyd N.V.;
- Approved the issue of Tier 1 hybrid debt;
- Approved the project to merge the Group's Irish General Insurance business into the UK General Insurance business;
- Reviewed the progress of the project to reorganise and flatten the Group's legal entity structure; and
- Considered and approved a new IT strategy.

The Board held one meeting in France during the year to gain a deeper understanding of the operations of the French business.

Board effectiveness

The effectiveness of the Board is vital to the success of the Group and the Company undertakes a rigorous evaluation each year in order to assess how well the Board, its Committees, the directors and the chairman are performing. The aim is to improve the effectiveness of the Board and its Committees and the Group's overall performance. The evaluation process for 2012 was led by the chairman and supported by the group company secretary. For a number of years the Board effectiveness review had been facilitated by external consultants. However, given the number of changes to the composition of the Board during the year the chairman considered that it would be more appropriate to carry out the 2012 effectiveness review internally using questionnaires tailored to the Board and each Committee. The results were discussed by the Board and each of the Committees and actions agreed. The review focused on the effective operation of the Board and each Committee, the effective use of meeting time, the appropriateness of the balance of skills, knowledge and experience of the Committee members, and identified key areas of focus for the Board and each Committee for 2013. Overall, the directors concluded that the Board and its Committees operated effectively and agreed that the issues identified for action or improvement in previous reviews had been implemented or addressed during the year. Areas identified for greater Board focus in 2013 included allocating a greater proportion of time to in-depth discussions of the markets in which the Group operates and their competitive positions and re-focusing strategy discussions towards the Group's long-term strategy, as well as continuing to monitor the Group's capital and liquidity position. The focus of the Board Committees in 2013 are detailed in each Committee's Report.

The review of the performance of the chairman, led by the senior independent director, concluded that the chairman continued to lead the Board effectively and had been instrumental in the progress which the Company and the Group had made during the year to deliver the Group's strategy.

The chairman assessed the performance of the executive directors in their capacity as directors of the Company and also assessed the performance of the non-executive directors. To assess the executive directors in respect of their executive duties a

separate process was carried out by the chairman measuring performance against each executive director's role objectives.

The chairman concluded that each director contributes effectively and demonstrates full commitment to his/her duties.

Induction, training and development

The Board believes strongly in the development of all of its employees and directors and it is a requirement of each director's appointment that they commit to continuing their development.

During the year, directors attended a number of internal courses, including on Solvency II, the Internal Model approval process and how rating agencies rate insurance companies. Training sessions have also been built into the Board's and Committees' work plans for 2013.

The Board has a comprehensive induction programme for new executive and non-executive directors which is tailored to their particular needs and which consists of several separate training sessions over a number of months. These include presentations from key members of senior management, visits to the Group's main operating businesses and functions, and meetings with the external auditor and one of the Company's corporate brokers. Further or follow-up meetings are arranged where a director requires a deeper understanding on a particular issue. All new directors also receive induction materials which includes the current strategic and operational plan, recent Board and Committee minutes and meeting packs, organisational structure charts, role profiles, a history of the Group, and relevant policies, procedures and governance material.

Directors' attendance

The Company requires directors to attend all meetings of the Board and the Committees on which they serve and to devote sufficient time to the Company in order to perform their duties. The attendance of the directors at the Board meetings held in 2012 is shown in the table below and the attendance at Committee meetings is shown in the Committee reports.

Board attendance 2012

Director	Number of meetings attended	Percentage attendance ¹
Glyn Barker (appointed 27 February 2012)	11	79% ²
Mary Francis (retired 3 October 2012)	9	90% ²
Richard Karl Goeltz	15	100%
Euleen Goh (retired 31 December 2012)	15	100%
Michael Hawker	14	93% ²
Gay Huey Evans	15	100%
John McFarlane	14	93% ²
Trevor Matthews	14	93% ²
Igal Mayer (resigned 19 April 2012)	2	50% ²
Andrew Moss (resigned 8 May 2012)	5	71% ²
Patrick Regan	14	93% ²
Lord Sharman (retired 30 June 2012)	8	100%
Leslie Van de Walle (retired 2 May 2012)	3	60% ²
Russell Walls	15	100%
Scott Wheway	14	93% ²
Mark Wilson (appointed 1 December 2012)	2	100%

¹ This shows the percentage of meetings which the director attended during the year whilst a member of the Board.
² The director was unable to attend Board meeting(s) due to prior commitments and the meetings being called at short notice or where a conflict of interest prevented the director from taking part in the meeting.

During 2012, there were fifteen Board meetings held, of which, eight were scheduled Board meetings and seven were additional Board meetings called at short notice. In addition the Board delegated responsibility for certain items, such as giving final approval to proposals broadly agreed by the full Board, to specially created sub-Committees of the Board which met seven times during 2012.

The chairman and the non-executive directors met several times in the absence of the executive directors and the non-executive directors met in the absence of the chairman, including one meeting chaired by the senior independent director to appraise the chairman's performance.

Conflicts of interest

In line with the Companies Act 2006, the Company's articles of association allow the Board to authorise potential conflicts of interest that may arise and to impose such limits or conditions as it thinks fit. The decision to authorise a conflict of interest can only be made by non-conflicted directors (those who have no interest in the matter being considered) and in making such a decision the directors must act in a way they consider in good faith will be most likely to promote the Company's success. The Board's procedure to regularly review and approve actual and potential conflicts of interest as they arise and prior to the appointment of new directors operated effectively during the year.

Governance structure

The Board is responsible for promoting the long term success of the Company for the benefit of shareholders. This includes ensuring that an appropriate system of governance is in place throughout the Group. To discharge this responsibility, the Board has established frameworks for risk management and internal control using a 'three lines of defence' model and reserves to itself the setting of the Group's risk appetite. In-depth monitoring of the establishment and operation of prudent and effective controls in order to assess and manage risks associated with the Group's operations is delegated to the Audit Committee and the Risk Committee which report regularly to the Board. However, the Board retains ultimate responsibility for the Company's systems of internal control and risk management and their effectiveness. These frameworks play a key role in the management of risks that may impact the fulfilment of the Board's objectives. They are designed to identify and manage, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or losses. These frameworks are regularly reviewed and comply with the Turnbull Guidance (Internal Control: Revised Guidance for Directors).

Risk Management Framework

The Risk Management Framework (RMF) is designed to identify, measure, manage, monitor and report significant risks to the achievement of business objectives and is embedded throughout the Group. It is codified through risk policies and business standards which set out the risk strategy, appetite, framework and minimum requirements for the Group's world-wide operations. Further details on procedures for the management of risks are given in note 56.

Internal controls

Internal controls facilitate effective and efficient business operations, the development of robust and reliable internal reporting and compliance with laws and regulations.

A Group Reporting Manual including International Financial Reporting Standards (IFRS) requirements and a Financial Reporting Control Framework (FRCF) are in place across the Group. FRCF relates to the preparation of reliable financial reporting and preparation of local and consolidated financial statements in accordance with IFRS and with the requirements of the Sarbanes-Oxley Act of 2002. The FRCF process follows a risk-based approach, with management identification, assessment (documentation and testing), remediation (as required), reporting and certification over key financial reporting-related controls.

The Board has delegated to the Group CEO the day-to-day management of the Company and approval of specific issues up to set financial limits including limits on revenue and capital expenditure, reinsurance spend and the settlement of claims. In turn the Group CEO has delegated some of his authority to his direct reports. There is a similar delegated authority framework in place throughout the Group.

First line

Management are responsible for the application of the RMF, for implementing and monitoring the operation of the system of internal control and for providing assurance to the Audit Committee, the Risk Committee and the Board.

The Group Executive members and each business unit chief executive officer are responsible for the implementation of group strategies, plans and policies, the monitoring of operational and financial performance, the assessment and control of financial, business and operational risks and the maintenance and ongoing development of a robust control framework and environment in their areas of responsibility.

The chief financial officer has established the Asset Liability Committee (ALCO) which assists him in discharging his responsibilities in relation to management of the Group's balance sheet within risk appetite and to provide financial risk management oversight. This includes recommending financial and insurance risk appetites and limit frameworks, evaluating the asset and liability impact of strategies and business plans, financial risk oversight, monitoring and management of the Group's capital and liquidity position, transaction risk oversight, stress and scenario testing, and identification of emerging financial risks.

Management regularly undertakes quality assurance procedures over the application of the FRCF process and FRCF controls. The results of the FRCF process are signed off by business unit chief executives and chief financial officers and FRCF compliance is reported up to the Disclosure Committee and the Audit Committee.

The Disclosure Committee is chaired by the chief financial officer and reports to the Audit Committee. It oversees the design and effectiveness of the Group's disclosure controls, for both financial and non-financial information, evaluates the Group's disclosure controls and reviews and endorses the Group's key periodic external reports, including the consolidated financial statements.

Second line

The Risk function is accountable for the quantitative and qualitative oversight and challenge of the identification, measurement, monitoring and reporting of significant risks and for developing the RMF.

As the business responds to changing market conditions and customer needs, the Risk function regularly monitors the appropriateness of the Company's risk policies and the RMF to ensure they remain up to date. This helps to provide assurance to the various risk oversight committees that there are appropriate controls in place for all core business activities, and that the processes for managing risk are understood and followed consistently across the Group.

To assist with the execution of his duties the chief risk and capital officer has established the Operational Risk and Reputation Committee (ORRC) which oversees operational risks and reputation impacts arising from activities across the Group. It oversees the operational risk elements of the implementation and maintenance of the risk policies and business standards, the Group's adherence to the Operational Risk Policy, and the adequacy and implementation of the RMF throughout the Group.

Third line

The Internal Audit function provides independent and objective assessment on the robustness of the RMF and the appropriateness and effectiveness of internal control to the Audit and Risk Committees, business unit audit committees and the Board. Further information on the activities of the Internal Audit function is contained within the Audit Committee Report.

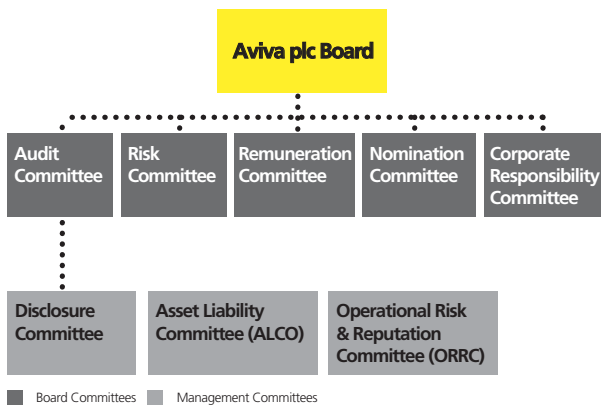
Board oversight

The Risk Committee assists the Board in its oversight of risk and risk management across the Group and makes recommendations on risk appetite to the Board. The responsibilities and activities of the Risk Committee are set out in the Risk Committee Report on pages 100 to 102.

The Audit Committee, working closely with the Risk Committee, is responsible for assisting the Board in discharging its responsibilities for the integrity of the Company's financial statements, the effectiveness of the system of internal financial controls and for monitoring the effectiveness, performance and objectivity of the internal and external auditors. The responsibilities and activities of the Audit Committee are set out in the Audit Committee Report on pages 97 to 99.

Both the Audit and Risk Committees report regularly to the Board on their activities and make recommendations and escalate significant risk exposures to the Board as appropriate. They ensure that mitigating actions are taken when risks are, or are expected to move, out of appetite.

The chart below shows the Board and Committee structure that oversees the Company's frameworks for risk management and internal control.



Further details on procedures for the management of risk operated by the Group are given in note 56.

Effectiveness of controls

To support an assessment of the effectiveness of the Group's governance, internal control and risk management systems, the chief executive officer of each business unit is required to certify that:

- There are sound risk management and internal control systems that are effective and fit for purpose in place across the business; and
- Material existing or emerging risks within the business have been identified and assessed and the business operates in a manner which conforms to the minimum requirements outlined in Group risk policies and business standards.

The chief risk officer of each business unit must certify that:

- The Risk function has reviewed and challenged the process supporting the business unit chief executive officer's certification, and is satisfied that it can provide reasonable assurance of the material accuracy and completeness of the business unit chief executive officer's assessment; and
- No material gaps exist in the RMF, as it applies to the business unit.

Any material risks not previously identified, control weaknesses or non-compliance with the Group's risk policies and business standards or local delegations of authority, must be highlighted as part of this process. This is then supplemented by investigations carried out at Group level and ultimately a Group CEO and group chief risk and capital officer certification for Aviva plc. In respect of 2012 and in view of the recent start of the Group CEO, the certification was made by the chief financial officer instead of the Group CEO. The effectiveness assessment also draws on the regular cycle of assurance activity carried out during the year.

The Audit Committee, working closely with the Risk Committee, on behalf of the Board, last reviewed the effectiveness of the systems of internal control and risk management in March 2013, covering all material controls, including financial, operational and compliance controls and the risk management framework and processes.

The necessary actions have been or are being taken to remedy any significant failings and weaknesses identified from these reviews. The Board confirms that there is an ongoing process for identifying, measuring, managing, monitoring and reporting the significant risks faced by the Group, which has been in place for the year under review and up to the date of approval of the Annual Report and Accounts.

Communication with shareholders

The Company places considerable importance on communication with shareholders and engages with them on a wide range of issues.

The Group has an ongoing programme of dialogue and meetings between the executive directors and institutional investors, fund managers and analysts managed by the Company's Investor Relations function. At these meetings a wide range of relevant issues including strategy, performance, management, remuneration and governance are discussed within the constraints of information already made public, to understand any issues of concern to investors.

During the year, the chairman and the chairman of the Remuneration Committee met with the Company's major institutional investors. In addition, the senior independent director was available to meet with major investors to discuss any areas of concern that could not be resolved through normal channels of investor communication. In 2012 the Board, through the Remuneration Committee chairman, consulted with institutional investors on executive remuneration.

The Company's AGM provides a valuable opportunity for the Board to communicate with private shareholders. There is a dedicated email address and a query facility on the Company's website which shareholders can use to ask questions on the business of the AGM. The details of these are highlighted in the shareholder information section of the Notice of AGM. A presentation on the Group's performance is given at the AGM and made available on the website after the meeting at www.aviva.com/agm. Whenever possible, all directors attend the AGM and shareholders are invited to ask questions related to the business of the meeting during the meeting and have an opportunity to meet with the directors following the conclusion of the meeting. All the directors on the Board at the time of the 2012 AGM attended the meeting.

New York Stock Exchange listing requirements

The Company's ordinary shares are admitted to the New York Stock Exchange (NYSE) and are traded as American Depositary Shares. As a foreign company listed on the NYSE, the Company is required to comply with the NYSE corporate governance rules to the extent that these rules apply to foreign private issuers. As a foreign private issuer, the Company is therefore required to comply with NYSE Rule 303A.11 by making a disclosure of the differences between the Company's corporate governance practices and NYSE corporate governance rules applicable to US companies listed on NYSE. These differences are summarised below together with Aviva's approach to compliance:

NYSE Listing Rules	UK Corporate Governance Code	Aviva approach
<p>Independence criteria for directors Independent directors must form the majority of the board of directors. A director cannot qualify as independent unless the Board affirmatively determines that the director has no material relationship with the company. NYSE rules prescribe a list of specific factors and tests that US companies must use for determining independence.</p>	<p>At least half the Board, excluding the chairman, should comprise independent non-executive directors, as determined by the Board. The Code sets out its own criteria that may be relevant to the independence determination, but the Board is permitted to conclude affirmative independence notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, so long as it states its reasons.</p>	<p>The majority of the Board comprises independent non-executive directors who are deemed independent under the Code.</p>
<p>Non-executive director meetings Non-management directors of each listed company must meet at regularly scheduled executive sessions without management and, if that group includes directors who are not independent, listed companies should at least once a year schedule an executive session including only independent directors.</p>	<p>The chairman should hold meetings with the non-executive directors without the executive directors present.</p>	<p>The independent non-executive directors meet without executive directors present at least once annually.</p>
<p>Committees US companies are required to have a nominating/corporate governance committee. In addition to identifying individuals qualified to become Board members, this committee must develop and recommend to the Board a set of corporate governance principles.</p>	<p>The Company is required to have a nomination committee but not a corporate governance committee.</p>	<p>The Company has a Nomination Committee. The Board as a whole is responsible for the corporate governance of the Group and oversees this through reports to the Board and its Committees.</p>
<p>Code of business conduct and ethics Companies are required to adopt and disclose a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers.</p>	<p>Not required under the Code.</p>	<p>The Company has adopted a Business Ethics Code to which all employees are bound and a Code of Ethics for senior management, to comply with the Sarbanes-Oxley Act of 2002.</p>
<p>Shareholder approval of equity-compensation plans Shareholders must be given the opportunity to vote on all equity-compensation plans and 'material revisions' to those plans, with limited exceptions. Detailed definitions of 'material revisions' are provided by NYSE.</p>	<p>Shareholder approval is necessary for certain equity-compensation plans and 'significant changes' thereto, subject to certain exceptions. The Code does not provide a detailed definition or explanation of what are considered to be 'significant changes'.</p>	<p>All new equity-compensation plans or amendments to existing plans that are required to be approved by shareholders under the Code are put to shareholders for approval.</p>

By order of the Board

John McFarlane
Chairman
6 March 2013

Nomination Committee report

This Report provides details of the role of the Nomination Committee and the work it has undertaken during the year.

Committee role and responsibilities

The Board strongly believes that good governance and strong, responsible, balanced leadership by the Board are critical to creating long-term shareholder value and business success. The Committee assists the Board by regularly reviewing the composition of the Board and conducting a rigorous and transparent process when recommending or renewing the appointment of directors to the Board. The key responsibilities of the Committee are to:

- Evaluate and review the balance of skills, knowledge, and experience of the Board, taking into account the Company's risk appetite and strategy;
- Monitor succession plans for the appointment of non-executive directors, the group chief executive and other executive directors to the Board;
- Identify and nominate suitable candidates for appointment to the Board, including chairmanship of the Board and its Committees, against a specification of the role and capabilities required for the appointment;
- Assess the independence of each of the non-executive directors;
- Assess directors' conflicts of interest as they arise;
- Review the external interests and time commitments of the directors to ensure that each has sufficient time to undertake his/her duties to the Company; and
- Approve a report on the Committee's activities for inclusion in the Company's Annual Report and Accounts.

The full terms of reference for the Committee can be found on the Company's website at www.aviva.com/terms-of-reference and are also available from the group company secretary.

Committee membership and attendance

As at the date of this Report, the Committee comprises the chairman and all the Company's independent non-executive directors. Prior to leaving the Group, Andrew Moss was also a member of the Committee. The table below shows the Committee members during the year and their attendance at Committee meetings:

Membership and attendance

Committee member	Number of meetings attended	Percentage attendance ¹
John McFarlane (Chairman) ²	6	100%
Lord Sharman ³	1	50%
Glyn Barker ⁴	4	100%
Mary Francis ⁵	3	75%
Richard Karl Goeltz	6	100%
Euleen Goh ⁴	4	100%
Michael Hawker ⁴	4	100%
Gay Huey Evans ⁴	4	100%
Andrew Moss ⁵	1	50%
Russell Walls	6	100%
Scott Wheway ⁴	4	100%

¹ This shows the percentage of meetings which the Committee member attended during the year whilst a member of the Committee. A number of Committee members could not attend meetings called at short notice or where they had a conflict of interest.

² Attended all meetings, became chairman of the Committee on 1 July 2012.

³ Lord Sharman retired from the Board and as chairman of the Committee on 30 June 2012.

⁴ Appointed to the Committee on 1 July 2012.

⁵ Resigned on 3 October 2012.

⁶ Resigned on 8 May 2012. The Committee notes that the UK Corporate Governance Code does not preclude the group chief executive from membership of the Committee.

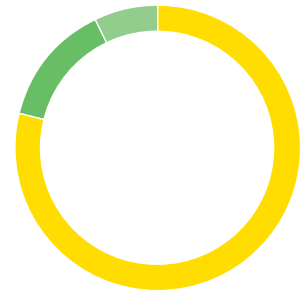
The Committee met on six occasions in 2012, of which three were scheduled meetings and three were additional meetings called at short notice. The group company secretary acts as the secretary to the Committee. Members of the Committee took no part in any discussions concerning their own circumstances. The chairman of the Committee reported to meetings of the Board on the Committee's work and the Board receives a copy of the agenda and the minutes of each meeting of the Committee.

Committee activities during 2012

During 2012 the Committee was principally focused on two particular issues: identifying the successor for the group chief executive and the recruitment of new non-executive directors as part of the continual cycle to refresh the Board and maintain an appropriate balance of skills, knowledge and experience. These issues are discussed in detail below. The chart below shows how the Committee allocated its time during 2012.

Nomination committee – allocation of agenda time

Board composition and succession planning	79%
Independence and conflicts of interest	14%
Others (including corporate governance)	7%



Group chief executive officer search

The Committee led the process for the recruitment of a new group chief executive following the departure of Andrew Moss in May 2012. The Committee approved the search brief and engaged Spencer Stuart to identify suitable candidates. The brief included finding candidates with strong insurance experience, a track record of running large global organisations, and the skills and leadership qualities to unite and motivate the Group's employees and to embed a high-performance culture.

A shortlist of candidates were interviewed by the chairman, the senior independent director and two non-executive directors. The preferred candidates met with all non-executive directors and the successful candidate met with the Financial Services Authority (FSA). The Remuneration Committee led on the development of an appropriate remuneration package for the role and approved the final package to be offered to the successful candidate. Both the Remuneration and Nomination Committees were mindful of shareholder views when considering the remuneration package for the role. Having considered all the skills, experience and personal attributes of the preferred candidates, the Committee recommended Mark Wilson be appointed to the role and to the Board. The Board appointed Mark Wilson as a director with effect from 1 December 2012 and as Group CEO from 1 January 2013. He has extensive experience in leading major international insurance companies across life insurance, general insurance and asset management. Spencer Stuart does not have any other connection with the Company.

Non-executive director search

As part of the continual cycle to refresh the Board, the Committee led the process to recruit two new non-executive directors to succeed Richard Goeltz and Russell Walls who will both retire from the Board, having completed nine years of service, on 8 May 2013. The Committee engaged The Zygus Partnership to identify suitable candidates. The Committee prepared comprehensive candidate search briefs with an emphasis on finding a candidate who could become the next senior independent director and a candidate with strong life assurance experience. Shortlisted candidates were interviewed by the chairman, the senior independent director and two non-executive directors and, additionally, executive and non-executive directors met with the preferred candidates. Following FSA approval, the Board accepted the Committee's recommendations and appointed Sir Adrian Montague and Bob Stein as non-executive directors on 14 and 28 January 2013 respectively.

The Committee further recommended to the Board that Sir Adrian Montague be appointed as senior independent

director prior to the 2013 AGM to succeed Richard Goeltz. The Committee believes that Sir Adrian has the requisite skills and experience to be an effective senior independent director. The Committee has also recommended that Glyn Barker be appointed as chairman of the Audit Committee to succeed Russell Walls prior to the 2013 AGM. Glyn Barker was formerly vice-president, UK of PwC and has a deep understanding of accounting and regulatory issues together with in-depth transactional and assurance experience. In his role at PwC he did not carry out external audit work for the Company and the Committee is satisfied that his former connection to PwC does not compromise the external auditor's independence.

The Zygos Partnership has no other connection with the Company.

Diversity

The Committee strongly believes that diversity throughout the Group and at Board and senior management level is a driver of business success. Diversity brings a broader, more rounded perspective to decision making and risk management, making the Board and senior management more effective. During the year, candidate searches were conducted and Board appointments were made, on merit, against the criteria identified by the Committee having regard to the benefits of diversity on the Board, including gender.

However, with the retirement of Euleen Goh and Mary Francis during the year to concentrate on other commitments the Board currently only has one female non-executive director, representing 10% of the Board. In its last report the Committee stated that it intends to maintain a minimum of 25% female representation on the Board by the end of 2013. The Company remains committed to having a diverse Board in terms of gender as well as diversity of experience, skills and knowledge, background and nationality. Recruitment of additional non-executive directors is ongoing and the Committee is taking diversity into account in the selection process. At the date of this Report, 29% (2011: 18%) of Group Executive members and 21% (2011: 20%) of senior executives in the Company were female. It is the Company's intention to increase this number as it is recognised that a higher number of women in senior management will create a stronger talent pipeline and is better for business.

Other activities

During the year the Committee recommended Committee composition changes to the Board and has been involved in the ongoing process to recruit a new chief executive officer for Aviva Investors and a new group HR director. The Committee also reviewed the independence of each non-executive director, all directors' conflicts of interest and the balance of skills, knowledge, experience and diversity on the Board prior to recommending directors' re-election at the AGM. Following consideration of these issues the Committee recommended the election or re-election of each director standing for election or re-election at the 2013 AGM.

Committee performance and effectiveness

The Board undertook an annual review of the Committee's performance and effectiveness and the results of the review will be incorporated into the Committee's processes and activities for 2013.

Nomination Committee Report

This Nomination Committee Report was reviewed and approved by the Board on 6 March 2013.

John McFarlane

Chairman, Nomination Committee

Audit Committee report

This Report provides details of the role of the Audit Committee and the work it has undertaken during the year.

Committee role and responsibilities

The purpose of the Committee is to assist the Board in discharging its responsibilities for monitoring the integrity of the Group's financial statements, assessing the effectiveness of the Group's system of internal controls and monitoring the effectiveness, independence and objectivity of the internal and external auditors. Whilst the Board as a whole has a duty to act in the best interests of the Company, the Committee has a particular role, acting independently of management, to ensure that the interests of shareholders are properly protected in relation to financial reporting and the effectiveness of the Group's systems of financial internal controls. The key responsibilities of the Committee are to:

- Review the significant issues and judgements of management, and the methodology and assumptions used in relation to the Group's financial statements and formal announcements on the Group's financial performance including the reserving position relating to the Group's life assurance and general insurance operations;
- Review the Group's going concern assumptions;
- Assess the effectiveness of the Group's system of internal controls, including financial reporting, financial controls and the Internal Audit function;
- Consider and review the performance of the chief audit officer, and agree with management his effectiveness and his remuneration;
- Consider and make recommendations to the Board on the appointment, reappointment, dismissal or resignation and remuneration of the external auditor; and
- Assess the independence and objectivity of the external auditor and approve and monitor the application of the external auditor business standard.

In preparation for the new Code requirement that will apply to Aviva during the 2013 reporting period, revised terms of reference for the Committee were adopted in January 2013.

The full terms of reference for the Committee can be found on the Company's website at www.aviva.com/terms-of-reference and are also available from the group company secretary.

Committee membership and attendance

The Committee comprises independent non-executive directors only. The table below shows the Committee members during the year and their attendance at Committee meetings:

Membership and attendance

Committee member	Number of meetings attended	Percentage attendance ¹
Russell Walls (Chairman)	13	100%
Glyn Barker ²	3	75%
Mary Francis ³	9	90%
Richard Karl Goeltz	12	92%
Euleen Goh ⁴	12	92%
Michael Hawker	12	92%

¹ This shows the percentage of meetings which the Committee member attended during the year whilst a member of the Committee. A number of the Committee members were unable to attend meetings called at short notice.

² Appointed to the Committee on 8 August 2012.

³ Resigned from the Board and the Committee on 3 October 2012.

⁴ Resigned from the Board and the Committee on 31 December 2012.

The Committee met on thirteen occasions in 2012, of which two meetings were called at short notice. Two of the meetings were held jointly with the Risk Committee to focus on the business of Aviva France and the Group's capital and liquidity position, and five of the meetings were held in relation to the Group's financial results only. Training and information sessions were held during the year on the Group tax and treasury functions and the integrated assurance framework. The group company secretary acts as the secretary to the Committee.

The chairman, Group CEO, chief financial officer, chief audit officer and the external auditor normally attended Committee meetings. Other members of senior management were also invited to attend as appropriate to present reports. The Committee regularly held private sessions to discuss issues to be raised with management in the main meeting, and met separately with senior management, with the chief audit officer without management present and with the external auditor without management present during the year. The Committee chairman held regular meetings with management and the chief audit officer, and with the external audit partner to ensure he was aware of issues that needed to be raised at the Committee. The Committee chairman reported to subsequent Board meetings on the Committee's work and the Board received copies of the agenda and minutes of each Committee meeting.

In performing its duties, the Committee had access to the services of the chief audit officer, the group company secretary, senior financial management and external professional advisers.

Committee expertise

The Committee members have significant financial experience and expertise.

Russell Walls, a Fellow Chartered Certified Accountant, is former group finance director of BAA plc, Wellcome plc and Coats Viyella plc. Richard Goeltz is a former chief financial officer of American Express Company and NatWest Group plc and a former member of the Accounting Standards Board.

Glyn Barker is a chartered accountant and has held a number of senior positions at PwC where, most recently, he was UK vice chairman. Michael Hawker, a Senior Fellow of the Financial Services Institute of Australasia, is a former chief executive officer and managing director of Insurance Australia Group.

The Board is satisfied that each of the current Committee members has recent and relevant financial experience and also meets US requirements to be an audit committee financial expert.

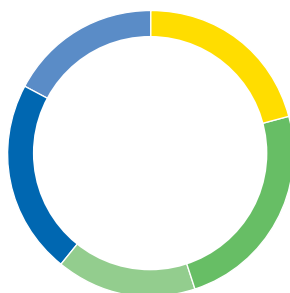
Glyn Barker will succeed Russell Walls as Committee chairman on 8 May 2013. As former vice-chairman of PwC, Glyn Barker has a recent connection with the Group's current auditor. However, he did not perform any audit work and had no responsibility for the audit business of PwC. PwC has concluded that Glyn Barker was not in the chain of command for the audit engagement team in the two years prior to his retirement, and has confirmed that he does not have any significant ongoing financial connection with the firm with respect to his pension arrangements. As he retired from PwC before PwC was appointed as the Company's auditor and as he complies with the rules of the US Securities and Exchange Commission and the Auditing Practices Board's Ethical Standards on auditor independence the Committee is satisfied that PwC is independent of the Company.

Committee activities during 2012

The work of the Committee followed an agreed annual work plan and principally fell under four main areas: financial statements and accounting policies, internal controls, the oversight of the internal audit function and the oversight of external audit. The Committee's work in each of these areas is described below. The group company secretary assisted the Committee chairman in planning the Committee's work, and ensured that the Committee received information and papers in a timely manner. The chart on the next page shows how the Committee allocated its time during 2012.

Audit committee – allocation of agenda time

Financial reporting	21%
External audit, auditor engagement and policy	24%
Internal audit and controls	16%
Financial reporting control framework and financial reporting developments	22%
Others (including governance, tax, treasury and dividends)	17%

**Financial statements and accounting policies**

In conjunction with members of management and the internal and external auditors, the Committee reviewed the Group's financial announcements, including the Annual Report and Accounts and associated documentation, the half year results and the interim management statements, and the going concern statement in relation to the Annual Report and Accounts. The Committee placed particular emphasis on their fair presentation and the reasonableness of the judgement factors and appropriateness of significant accounting policies used in their preparation.

During the year, the Committee considered the treatment of various assets in the Group's accounts and the accounting assumptions applied to the results, including the reclassification of Delta Lloyd from an associate to an investment following a further disposal of the Group's holding in Delta Lloyd; the 'held for sale' classification of Aviva's US business; the impairment assumptions for the US business and the Group's Spanish bancassurance joint ventures; and the impact of unwinding the Irish joint venture arrangements with Allied Irish Bank. A number of new accounting standards were issued by the International Accounting Standards Board at the end of 2011 which become effective in 2013 and the Committee monitored the action taken by management to ensure compliance with the new standards. The Committee also considered the changes to the Code and associated guidance relating to audit committees and the Committee's Report in the 2013 Annual Report and Accounts will include disclosure of the significant issues it has considered in relation to the Group's financial statements. During the year the Committee also received reports on the adequacy of the Group's life assurance and general insurance reserves, reviewed the audit representation letters prior to signature on behalf of the Board to ensure that the information provided to the external auditor was complete and appropriate and monitored management's responsiveness to the external auditor's findings and recommendations.

Internal control

During the year the Committee received quarterly updates on the effectiveness of the Group's financial reporting control framework and discussed rectification of any deficiencies in controls. In that respect, the Committee focused on the work by management to improve the internal control framework in Aviva Investors, where a new controls assurance team had been established, and enhancing controls around end-user computing policies and practices and monitoring US IT change management.

The Committee reported to the Board regarding the effectiveness of the Group's overall risk management and internal control systems including the risk management system in relation to the financial reporting process. The Committee worked closely with the Risk Committee in its overall review of the Company's systems of risk management and internal controls. The Committee encouraged continuous improvements in the effectiveness of internal controls where appropriate.

The system of internal controls extends to the Group's business units, each of which has an audit committee that provides an oversight role for its business. Membership of these

business unit audit committees is very largely comprised of non-executive directors. The chief audit officer attended business unit audit committee meetings throughout the year and reported back on their effectiveness to the Committee. During 2012 the members of the Committee attended several business unit audit committee meetings, including those in the US, Italy, Canada and Aviva Investors. Revised terms of reference for business unit audit committees were discussed and implemented within the business units together with a new induction pack for business unit audit and risk committee members.

The Committee's terms of reference require it to establish and monitor procedures for dealing with complaints from employees in relation to accounting issues. The Committee reviews the procedures annually and received regular updates from the chief audit officer on any significant complaints received. A description of the Company's systems of internal control is included in the Corporate Governance Report on pages 89 to 94.

Internal audit

Internal Audit reports to the Board (primarily via the Audit and Risk Committees) and to management on the effectiveness of the Company's system of internal controls and the adequacy of this system to manage business risk and to safeguard the Group's assets and resources.

Internal audit charter and business standard

The Committee approved a new Internal Audit charter and an Internal Audit business standard in early 2012. The charter sets out the purpose, functions, scope and responsibilities of the Internal Audit function and how it maintains independence from the first and second line management of the Group. The three main functions of Internal Audit are to:

- Assess and report on the effectiveness of the design and operation of the framework of controls which enable risk to be assessed and managed;
- Investigate and report on cases of suspected financial crime and employee fraud; and
- Undertake advisory projects for management provided that they do not threaten the function's actual or perceived independence from management.

The Internal Audit business standard sets out the business requirements of senior management across the Group in order to support Internal Audit in achieving its objectives and requires businesses to design and operate processes and controls to satisfy the mandatory requirements in the standard based on the size and complexity of the business and the nature of the risks and challenges it faces. The standard also includes controls around local legal and regulatory risks. Any breaches of the standard must be reported to the chief audit officer and others as appropriate.

Annual plan and focus of reviews in 2012

Internal Audit's 2012 annual plan was reviewed and approved by the Committee. Planned reviews were prioritised following a risk-based assessment of the business and a review against the Group's risk policies. The reviews carried out covered an extensive sample of controls over all risk types, business units and regulated entities and covered 'business as usual' activities and an assessment of change programmes. The Committee received quarterly reports from the chief audit officer on audit reviews carried out, management's response to the findings and progress in addressing identified issues. During 2012, Internal Audit carried out assurance reviews over inherent risks throughout the Group. Reviews were focused on, but not limited to, areas such as major projects including Solvency II and the Aviva Ireland Transformation Programme; maintenance of controls during the management restructuring programme; IT availability, security and recoverability; financial reporting and disclosure; financial risk, central liquidity and capital management; and the internal control

environment at Aviva Investors. The chief audit officer increased management's focus throughout the year on management's progress on closing overdue audit issues where further improvement is still required.

The Committee assessed the effectiveness of the Internal Audit function against criteria provided by the Institute of Chartered Accountants in England and Wales and by the Institute of Internal Auditors and concluded that the function was effective. An independent review is carried out every five years and the next independent review is due to be carried out in 2013.

Chief audit officer

The chief audit officer had direct access to the Board chairman, the Committee chairman and the Committee members. The Committee worked with the chief financial officer to determine the chief audit officer's objectives and evaluate his levels of achievement, and to approve the chief audit officer's remuneration. His annual performance related bonus was unconnected to the Group's financial performance. During the year the chief audit officer became a member of the Group Executive and his reporting line changed from the Group CEO to the chief financial officer. The chief audit officer's membership of the Group Executive assisted the relationship between Internal Audit and management. Notwithstanding his appointment to the Group Executive, his independence was maintained as the Group Executive, acting as a committee, has no decision making authority and assurances were received from management that adequate safeguards had been put in place to maintain the independence, authority and standing of the chief audit officer and the Internal Audit function. Following the senior management restructuring which took place during the year the Internal Audit function aligned itself to the new structure and the Committee remained satisfied that the Internal Audit function had sufficient resources to undertake its duties.

External auditor

PwC was appointed by the Board as the Company's external auditor on 22 March 2012 for the 2012 reporting period and was re-appointed by shareholders at the 2012 AGM. The Committee led the tender and selection process through which PwC was appointed and has recommended to the Board that PwC be re-appointed by shareholders at the 2013 AGM. There are no contractual obligations that restrict the Committee's choice of external auditor.

Given the resignation of Ernst & Young LLP as external auditor in early 2012 and that PwC has only just completed its first full year audit, no external auditor effectiveness review was carried out in 2012. A review will be conducted in 2013.

The Company has an external auditor business standard in place which is aimed at safeguarding and supporting the independence and objectivity of the external auditor. The standard is in full compliance with all UK, US and International Federation of Accountants (IFAC) rules and takes into account the Auditing Practices Board Ethical Standards for Auditors.

As discussed above, the Committee believes that Glyn Barker's connection with PwC does not compromise PwC's independence.

The standard regulates the appointment of former audit employees to senior finance positions in the Group and sets out the approach to be taken by the Group when using the non-audit services of the principal external auditor. It distinguishes between (i) those services where an independent view is required and those that should be performed by the external auditor (such as statutory and non-statutory audit and assurance work); (ii) prohibited services where the independence of the external auditor could be threatened and must not be used; and (iii) other non-audit services where the external auditor may be used. Non-audit services where the external auditor may be used include: non-recurring internal controls and risk management reviews (excluding outsourcing of internal audit work), advice on financial

reporting and regulatory matters, due diligence on acquisitions and disposals, project assurance and advice, tax compliance services, and employee tax services. During the year the Committee received quarterly reports of compliance against the standard.

The Group paid £13.5 million to PwC for audit services in 2012, relating to the statutory audit of the Group and Company financial statements, the audit of Group subsidiaries, and audit-related assurance services (2011: £17.3 million to Ernst & Young LLP).

Prior to 2012, PwC was a significant provider of consulting services to the Group. The level of fees for non-audit services in 2012 below includes fees billed in the year relating to projects that commenced prior to PwC's appointment as external auditor. All of these services are in compliance with applicable UK, US and International Federation of Accountants independence rules. We do not expect PwC's non-audit fees to continue at this level in the future.

The fees for other services, which included MCEV supplementary reporting, assurance on the Group's 2012 Corporate Responsibility Report, advice on accounting, risk and regulatory matters, reporting on internal controls, reporting on the Group's Individual Capital Assessment and Economic Capital, work in relation to preparing the business for Solvency II implementation, and work on capital transactions, were £18.3 million to PwC (2011: £11.2 million to Ernst & Young LLP), giving a total fee to PwC of £31.8 million (2011: £28.5 million to Ernst & Young LLP). In addition the Group paid £1 million to Ernst & Young LLP in 2012 in relation to the 2011 audit.

The 2012 fees for other non-audit services for continuing operations of £7.7 million includes advice to our European businesses in relation to the risk management aspects of Solvency II (£1.9 million), £1.9 million relating to four regulatory advice engagements, £0.7 million relating to restructuring at Aviva Investors, £0.3 million for risk training, £0.3 million supporting an industry-wide competition review, £0.3 million for an additional claims reserves review and £2.3 million for other services. The 2012 fees for tax compliance services of £0.4 million includes fees for one engagement in Higher Growth markets of £0.3 million, and fees for corporate finance transactions of £0.3 million relates to an engagement for an Aviva Investors property fund. In line with the external auditor business standard, the Committee satisfied itself that for these engagements, robust controls (including appropriate levels of review) were in place to ensure that PwC's objectivity and independence was safeguarded, and concluded that it was in the interests of the Company to purchase these services from PwC due to their specific expertise. Further details are provided in note 12.

Committee performance and effectiveness

The Committee undertook an annual review of its performance and effectiveness which concluded that overall the Committee was effective in carrying out its duties. The Committee agreed that its priorities for 2013 should include continuing to monitor Group liquidity jointly with the Risk Committee, ensuring that appropriate controls remain in place during the continued restructuring of the Group, closely monitoring reserving and actuarial assumptions changes, and considering compliance with the relevant new requirements of the UK Corporate Governance Code.

Audit Committee Report

This Audit Committee Report was reviewed and approved by the Board on 6 March 2013.

Russell Walls

Chairman, Audit Committee

Risk Committee report

This Report provides details of the role of the Risk Committee and the work it has undertaken during the year.

Committee role and responsibilities

The purpose of the Committee is to assist the Board in its oversight of risk within the Group through reviewing the Group's risk appetite and risk profile, the effectiveness of the Group's risk management framework and the methodology and assumptions used in determining the Group's capital requirements. The Committee also works with the Remuneration Committee to ensure that risk is properly considered in setting the Group's remuneration policy. The Committee oversees all aspects of risk management in the Group, including market, credit, liquidity, insurance and operational risk (including franchise risk), and their impact on both financial and non-financial goals.

The key responsibilities of the Committee are to:

- Review the Group's risk appetite and future risk strategy, particularly in relation to economic (i.e. risk-based) capital, liquidity, reputation and operational risk, and make recommendations on risk appetite to the Board;
- Review the Group's risk profile against its risk appetite and strategy and review the drivers of changes, if any, in the Group's risk profile;
- Review the design, completeness and effectiveness of the risk management framework relative to the Group's activities;
- Assess the adequacy and quality of the risk management function and the effectiveness of risk reporting within the Group;
- Review the methodology and assumptions used in the Group's models for determining its economic and regulatory capital requirements; and
- Work with the Remuneration Committee, to ensure that risk is considered in setting the overall remuneration policy for the Group.

Revised Committee terms of reference were adopted in January 2013 following an annual refresh. The full terms of reference for the Committee can be found on the Company's website at www.aviva.com/terms-of-reference, and are also available from the group company secretary.

Committee membership and attendance

The Committee comprises independent non-executive directors only. The table below shows the Committee members during the year and their attendance at Committee meetings.

Membership and attendance

Committee member	Number of meetings attended	Percentage attendance ¹
Michael Hawker (Chairman)	11	100%
Glyn Barker ²	7	88%
Mary Francis ³	8	100%
Leslie Van de Walle ⁴	3	100%
Russell Walls	11	100%

¹ This shows the percentage of meetings which the Committee member attended during the year whilst a member of the Committee.

² Glyn Barker joined the Committee on 2 May 2012. He was unable to attend the Committee meeting held on 4 December 2012 due to prior commitments and this meeting being called at short notice.

³ Mary Francis resigned from the Committee on 3 October 2012.

⁴ Leslie Van de Walle resigned from the Committee on 2 May 2012.

The Committee met on eleven occasions in 2012, of which nine were scheduled Committee meetings and two were additional Committee meetings called at short notice. Two of the meetings were held jointly with the Audit Committee to consider the business of Aviva France and the Group's capital and liquidity position. The Committee followed a programme of attending meetings of business unit risk committees and, during the year, members of the Committee attended meetings in the US and

Canada. The group company secretary acted as the secretary to the Committee.

In November, the Committee chairman hosted a two-day conference for the chairmen of the boards and risk committees of the Group's principal subsidiaries. The agenda included discussions on Solvency II; revisions to the timing of implementation of Solvency II and the impact on the Group's capital regime; the FSA's perspective of the roles and responsibilities of the Board, the Committee and the business unit boards and risk committees under Solvency II; calculation of economic capital and the internal model; and an in-depth analysis of the Group's key risk types.

The chairman of the Company, Group CEO, chief risk and capital officer, chief financial officer and the chief audit officer normally attended all Committee meetings. Other members of senior management were also invited to attend as appropriate to present reports. It was the Committee's practice to hold private sessions at the beginning of each meeting to discuss issues to be raised with management in the main meeting, and to meet with the Group CEO, chief finance officer and chief risk and capital officer without any other members of management being present.

The Committee chairman reported to the subsequent meeting of the Board on the Committee's work and the Board received a copy of the agenda and the minutes of each Committee meeting. Throughout the year, the Committee chairman sat on the Audit and Remuneration Committees to ensure that risk considerations were fully reflected in the decisions of those Committees.

In performing its duties, the Committee had access to the services of the chief risk and capital officer, chief audit officer, the group company secretary and external professional advisers.

External environment

The external environment was once again one of much international economic uncertainty. Doubts about the strength and economic recovery rates in the OECD, political uncertainty in the world's two largest economies with leadership changes in China and presidential elections in the United States, and the increased regulatory and capital burden on the financial services industry, dampened the risk appetite of investors.

This resulted in the continued reduction in OECD interest rates, further quantitative easing from the US, Japanese, UK and European Governments, high levels of OECD unemployment, and times of excessive volatility in credit spreads.

Towards the end of the year, the emergence of early growth in the US, greater clarity surrounding the political changes in the US and China, and a continuation of low interest rates saw a rally in the equity markets and a tightening of credit spreads and lower volatility.

The question one asks, is whether these perceived improvements in the world's economic environment are sustainable or short lived?

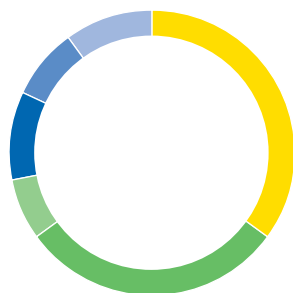
Committee activities during 2012

The work of the Committee followed an agreed annual work plan, which evolved throughout the year in response to the changing macro-economic and regulatory environment and changes in the Company's strategy. The group company secretary and the group chief capital and risk officer assisted the Committee chairman in planning the Committee's work, and ensured that the Committee received information and papers in a timely manner.

The chart below shows how the Committee allocated its time during 2012.

Risk committee – allocation of agenda time

Risk appetite, risk management and risk reporting	35%
Group capital, liquidity management and stress testing	30%
Preparation for Solvency II	7%
Regulatory and governance	10%
Business protection and IT security	8%
Others (including internal audit)	10%



During the year the Committee focused on the following areas:

Risk appetite monitoring

Against a backdrop of significant market volatility during the year, the Committee received regular detailed reports on key risk exposures, emerging and potential risks, and the drivers of risk throughout the Group. It assessed and challenged the appropriateness of the Group's overall risk appetite and approved revised economic capital risk appetites by risk type. The Committee monitored the Group's exposure against these appetites, particularly in relation to European sovereign debt holdings and counterparty and credit exposure and, throughout the year, discussed and agreed the actions to be taken to reduce exposure and to address or mitigate risks that had become out of appetite. It also agreed a comprehensive, revised capital management framework by which capital issues would be escalated to the Committee and the Board. Mindful of the potential economic, social and regulatory impact of a Eurozone default, the Committee monitored significant market and Group level contingency planning to produce tailored 'financial event response plans'.

Capital and liquidity management

Throughout the year, the Committee closely monitored the Group's economic capital and liquidity positions against risk appetite and targets, and considered in detail the results of stress and scenario testing at Group and local market level. Given the volatility in market conditions during the year, the Committee challenged the appropriateness of the Group's regulatory and economic capital surplus and liquidity targets and, after detailed consideration, recommended to the Board revised, strengthened targets. The Committee gave particular focus to considering and approving a programme of strategic, economic and operational actions to be undertaken to strengthen and provide greater resilience to the Group's capital and liquidity positions, and monitored the results and effectiveness of the programme.

Methodology and assumptions

In early 2012, the Committee considered and approved the methodology and assumptions used to calculate the economic capital for the 2012 Individual Capital Adequacy (ICA) submission.

Preparing for Solvency II

The Committee closely monitored the evolving position in relation to the implementation of the Solvency II Directive. Notwithstanding the eventual agreement in October 2012 to delay implementation until 2014, the Committee continued to have oversight of all aspects of the Group's programme to implement the Solvency II Directive. Throughout the year, the Committee received detailed progress reports on the development of the models used to calculate economic capital requirements and the techniques used to validate the results. The Committee also reviewed the detailed contingency plans in relation to the Group's internal model and had oversight of the

programme of board training and preparations for legal entity sign-off to the Group's Internal Model Approval Process (IMAP) submission. Following confirmation of the delay to implementation of the Solvency II Directive, the Committee reviewed the revised management programme to deliver enhancements to the economic capital model in the interim period.

Risk management and governance

The Committee had an ongoing programme of receiving reports from local risk committee chairmen or chief executive officers on the risk environment and issues arising in the Group's businesses and in respect of particular product lines. During the year, the Committee received reports on the businesses in Italy, Spain, France, the UK and the European region as a whole, and in respect of the Corporate and Speciality Risks business in the UK and business lines in France. The Committee also received updates on issues concerning IT and data security and on the Group's reinsurance programme. The Committee received regular reports from the chief risk and capital officer and monitored the effectiveness of the Company's Risk Management Framework which is described in more detail in the Corporate Governance Report on pages 89 to 94 and in note 56.

Throughout the year, the Committee had significant oversight of the development of a comprehensive Group-wide restructuring programme, designed to better align legal and management structures throughout the organisation and to optimise governance practices at Group and subsidiary level. In addition, as part of the annual refresh of the suite of risk policies and business standards which underpin the RMF, the Committee reviewed and approved the updated policies and approved a sign-off process in respect of the business standards.

At the end of the year, the Committee commenced an analysis of the Group's asset and investment portfolio and the framework by which business units set their investment strategies. Further analysis will continue in 2013.

Regulatory oversight

The Committee maintained oversight of the regulatory risks throughout the organisation and discussed the specific management actions identified to address or mitigate issues which arose during the year. The Committee also considered the impact of the changes in the UK and European regulatory landscape, particularly in light of the shift in UK regulatory focus ahead of the split of the FSA into the Prudential Regulation Authority and the Financial Conduct Authority in 2013, and of increasing policyholder protectionism by European regulators.

Fraud and financial crime

The Committee reviewed compliance with controls against financial malpractice including fraud, and of the arrangements for employees to report in confidence any concerns about lack of probity (whistleblowing). It received updates on, and approved enhancements to, the financial crime prevention programme, which was designed to further embed and ensure enforcement of the Group's anti-bribery and corruption policies and to provide on-going training for the Group's businesses and employees.

Personnel and remuneration policy

During the year, the Committee approved the appointment of the group chief risk and capital officer. In early 2013 it approved his objectives for the coming year and reviewed his performance against 2012 objectives. The Committee also assessed senior management's performance against the agreed common risk objective and considered the appropriateness of the risk metrics when setting senior management remuneration policy.

Internal controls

Working with the Audit Committee, the Committee monitored the adequacy of the RMF. Throughout the year, the Group's Internal Audit function continued to provide the Committee with independent and objective reports on the appropriateness, effectiveness and sustainability of the Company's system of internal controls. Key control issues reported by Internal Audit to management and to the Committee members were monitored on a quarterly basis until the related risk exposures had been properly mitigated.

More detail on the management of risk is contained in note 56.

Committee performance and effectiveness

The Committee undertook an annual review of its performance and effectiveness which concluded that overall the Committee was effective in carrying out its duties. In addition to undertaking its agreed annual programme of activities, the Committee agreed that its priorities for 2013 should be to continue to focus on capital and liquidity issues; to monitor the Group's preparedness for Solvency II; to review the quality and mix of the Group's asset portfolio; to monitor the Group's customer agenda and to oversee management actions to improve IT resilience.

Risk Committee Report

This Risk Committee Report was reviewed and approved by the Board on 6 March 2013.

Michael Hawker

Chairman, Risk Committee

Corporate Responsibility Committee report

This Report provides details of the role of the Corporate Responsibility Committee and the work it has undertaken during the year.

Committee role and responsibilities

The purpose of the Committee is to set guidance and direction and to oversee the policies and progress of the Group's corporate responsibility (CR) activities. The key responsibilities of the Committee are to:

- Assist the Board in the development of the Group's strategy on CR related issues and monitor external developments.
- Review the Group's CR, environment and climate change business standard to ensure it continues to meet the Group's CR strategy and objectives;
- Review and monitor the Group's CR risks and, working with the Risk Committee, ensure that the Group's CR risks are properly considered;
- Review and approve the CR Report in the Company's Annual Report and Accounts and provide for an appropriate form of assurance; and
- Review the overall CR content contained within the Group's financial reports.

Revised terms of reference were adopted in January 2013. The responsibility of the Committee was expanded to include providing oversight for the Board in respect of the Group's conduct with customers and reviewing the overall corporate governance of the Group and business standards as they relate to the culture, values and reputational risks of the Group. The full terms of reference for the Committee can be found on the Company's website at www.aviva.com/terms-of-reference and are also available from the group company secretary.

Committee membership and attendance

The Committee comprises independent non-executive directors only. The table below shows the Committee members during the year and their attendance at Committee meetings.

Membership and attendance

Committee member	Number of meetings attended	Percentage attendance ¹
Gay Huey Evans (Chairman)	4	100%
Euleen Goh ²	4	100%
Andrew Moss ³	2	100%
Lord Sharman ⁴	2	100%
Scott Wheway	4	100%

¹ This shows the percentage of meetings which the Committee member attended during the year whilst a member of the Committee.

² Euleen Goh resigned from the Committee in December 2012.

³ Andrew Moss resigned from the Committee in May 2012.

⁴ Lord Sharman retired from the Committee in June 2012.

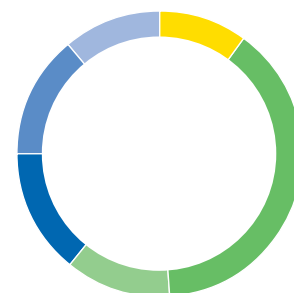
The Committee met on four occasions in 2012. The group company secretary or her nominee acts as the secretary to the Committee. The executive chairman attended all meetings of the Committee and the group CR director, the group HR director, the chief marketing and communications officer and other members of senior management also attended meetings by invitation. The chairman of the Committee reported to the subsequent meeting of the Board on the Committee's work and the Board received a copy of the agenda and the minutes of each meeting of the Committee.

Committee activities during 2012

The following chart shows how the Committee allocated its time during 2012, with key activities set out in more detail below:

Corporate responsibility committee – allocation of agenda time

Climate change and environment	10%
CR strategy, reporting and governance	39%
Business unit review	12%
Stakeholder recognition and business ethics	14%
Street to school programme	14%
Customers and employees	11%



CR Strategy Performance and Risk Management

During the year the Committee reviewed and approved the Group CR strategy and functional plan for 2012-2014 and monitored progress made by the Group's businesses against each of the CR key performance indicators. Updates were given on CR programme activities such as the Street to School programme; business ethics; health, safety and wellbeing; and stakeholder recognition. The Committee also focused on ensuring a strengthening of CR performance across the Group through enhanced employee engagement, influencing key stakeholders and by further encouraging diversity and inclusion throughout the Group. The Committee continued to monitor risks relating to the Group's CR activities together with associated risk mitigation initiatives.

Assurance

In respect of the 2011 reporting year, independent assurance on the Group's CR and related activities and reporting was provided to the Committee by Ernst & Young LLP. For the 2012 reporting year, PwC was appointed to provide independent assurance. Members of the Committee were interviewed as part of the external assurance process and the subsequent report; and management's action plan; were reviewed by the Committee to assist in strengthening and setting the future direction of the CR programme. Internal Audit reported to the Committee on any relevant matters from its reviews and will provide support for the Committee going forward.

Corporate Responsibility Report

During the year, the Committee approved the scope and content of the Company's 2012 CR Report, which provides a summary of the Group's CR performance in 2012. The Report is set out on pages 61 to 76 and can be found at www.aviva.com/reports. The Report will be put to an advisory vote of shareholders at the 2013 AGM and further details of the relevant resolution are set out in the Notice of AGM.

Committee performance and effectiveness

The Committee undertook an annual review of its performance and effectiveness which concluded that overall the Committee was effective in carrying out its duties. Committee members identified areas for greater focus in 2013 and the Committee's remit will be extended to provide an increased focus on corporate governance, oversight of the brand, values and reputation of the Group and the Group's conduct with customers.

Corporate Responsibility Committee Report

This Corporate Responsibility Committee Report was reviewed and approved by the Board on 6 March 2013.

Gay Huey Evans

Chairman, Corporate Responsibility Committee

Directors' remuneration report



Scott Whewey
Chairman, Remuneration
Committee

Dear shareholder

On behalf of the Board, I am pleased to present the Directors' Remuneration Report for the year ended 31 December 2012.

Our on-going commitment to shareholders

Whilst we have traditionally had good shareholder support for our remuneration policies over many years, we believe in 2011 we clearly got it wrong. As a result, the Committee has worked over the last year to make changes that will give us a better framework for the decisions we take. Specifically, we agreed the following:

- We introduced 'underpin' metrics to 2012 bonuses to ensure that bonus payouts were more closely aligned to shareholder experience. We will consider these metrics annually until alternative arrangements are agreed;
- We will make any future buyouts on the hire of senior executives on a strict 'like for like' basis; and
- We will continue a regular dialogue with shareholders and take account of their feedback.

We have met our major institutional shareholders and the main proxy agencies on many occasions over the last year. We have consulted them on these changes and will continue the open and honest discussions we have established.

Putting the changes into practice

These changes have impacted our operational practices and our decisions in the 2013 reward round. Key agreed outcomes have been:

- Base pay – the Committee has frozen executive directors' base pay for 2013;
- Annual bonus – the Committee has not awarded bonuses to executive directors for 2012. Our annual bonus plan is based on key financial, employee and customer performance indicators. Solely taking into account performance against these measures at Group level (assuming 'on-plan' personal performance), the bonus outcome for 2012 would have been 52% of maximum. However, we have taken account of the underpin metrics to ensure bonus outcomes that are better aligned with the creation of shareholder value. Following careful consideration of those metrics the Committee decided that executive directors would not receive a bonus for 2012;
- Chairman fees – John McFarlane indicated he did not wish any increase in the fees paid to him when he undertook his executive role in the period from May 2012 to 31 December 2012; and
- ACAP/ACDT – the Aviva Capital Accumulation Plan (ACAP) and the Aviva Cash Deferral Trust (ACDT) will close from 31 March 2014. Payments in lieu of pension have been standardised at senior management levels and a small number of individual arrangements above the

standard level have been closed from 31 March 2013.

Linking pay to the Group's strategic plan

We believe our remuneration policy and practice is now more closely linked to the main strategic priorities of the Group:

- Improve financial performance – remuneration is heavily weighted towards pay that is dependent on the outcomes against the key performance indicators of our business, notably profit and Return on Equity (ROE);
- Build capital and financial strength – variable pay is strongly aligned to the measurement of the financial strength of our business. Furthermore, economic capital performance is carefully considered before bonus payments are made to ensure that the Group's financial strength continues to improve; and
- Focus on core businesses – through the measurement of a number of key financial, operational and longer term return measures, overall remuneration is closely aligned to the achievement of the Group's strategic objectives.

Appointment of Group chief executive officer

The Board was delighted to announce, on 20 November 2012, the appointment of Mark Wilson as Group CEO. He joined the Board on 1 December 2012 and took up the role of Group CEO from 1 January 2013. Details of his remuneration arrangements were announced at the time of his appointment.

We are committed to maintaining an open, transparent dialogue with shareholders. I hope you will find this Report clear and informative.

Scott Whewey
Chairman, Remuneration Committee

This Report sets out the details of the remuneration policy and practices for the Company's directors, describes its implementation and discloses the amounts paid in respect of 2012. It also provides details of the role of the Remuneration Committee and the work it has undertaken during the year. In addition to meeting statutory requirements, particularly the regulations on directors' remuneration reports pursuant to the Companies Act 2006 and Schedule 8 of the Large and Medium-sized Companies and Group (Accounts and Reports) Regulations 2008, the Committee has complied with best practice guidelines in producing this Report, including guidance issued by the Association of British Insurers and the National Association of Pension Funds.

In this Report, the sections headed 'Share awards', 'Share options', 'Directors' remuneration in 2012' and 'EDs' pension arrangements' along with their associated footnotes have been audited in accordance with the Companies Act 2006.

Committee role and responsibilities

The Remuneration Committee is responsible for reviewing and making recommendations to the Board regarding the remuneration policy of the Group and for reviewing compliance with the policy. The Committee is further responsible for monitoring the level and structure of remuneration for the senior management of the Group.

The key responsibilities of the Committee are to:

- Make recommendations to the Board regarding the Group's remuneration policy in respect of the Board chairman, executive directors (EDs), members of the Group Executive and members of senior management;
- Work with the Risk Committee to ensure that risk and risk appetite are properly considered in setting the remuneration policy for the Group;
- Review and determine the remuneration of the chairman of the Board and the terms of employment and remuneration of individual EDs and Group Executive members, including any specific recruitment or severance terms;
- Review and recommend to management the level and structure of senior management remuneration;
- Approve the Aviva Investors' reward strategy, including any changes to the strategy and agree the total bonus pool, receive remuneration details of Aviva Investors' 'material' employees, and approve any new share and incentive plans or any changes to existing share and incentive plans;
- Recommend to the Board the establishment of any employee share plans, exercise all the Board's powers in relation to the operation of all share and incentive plans and the Group's all employee share ownership plan; and
- Select, appoint and determine terms of reference for independent remuneration consultants to advise the Committee on remuneration policy and levels of remuneration.

Revised Committee terms of reference were adopted in January 2013 following an annual refresh. The responsibilities of the Committee were clarified to include:

- Having regard to remuneration trends across the Group when setting remuneration policy for directors;
- Ensuring that remuneration arrangements for all employees are commensurate with promoting ethical behaviour;
- Ensuring the effectiveness of the process for assessing the senior management group for talent and succession planning purposes, ensuring appropriate reward for performance and a consistent approach to the development of talent throughout the Group;
- Extending the list of employees whose remuneration is reviewed by the Committee to include a wider senior management group, those in controlled functions and identified staff;
- Approving any exceptional remuneration activity that is outside the agreed reward policy;
- Annually approving the list of FSA Code Staff and any severance packages for Code Staff; and
- Approving the Group remuneration business standard.

The full terms of reference for the Committee can be found on the Company's website at www.aviva.com/terms-of-reference and are also available from the group company secretary.

Committee membership and attendance

The Committee comprises independent non-executive directors only. Table 1 below shows the Committee members during the year and their attendance at Committee meetings.

Table 1: Committee membership and attendance

Committee member	Number of meetings attended	Percentage attendance ¹
Scott Wheway (Chairman)	12	100%
Michael Hawker ²	10	83%
Gay Huey Evans ³	8	100%
Leslie Van de Walle ⁴	4	100%

Notes

- 1 This shows the percentage of meetings which the Committee member attended during the year whilst a member of the Committee.
- 2 Michael Hawker was unable to attend two meetings held in April 2012 due to prior commitments and the meetings being called at short notice.
- 3 Gay Huey Evans attended all of the meetings held following her appointment to the Committee on 2 May 2012.
- 4 Leslie Van de Walle resigned from the Committee on 2 May 2012.

The Committee met twelve times during 2012 of which eight were scheduled Committee meetings and four were additional Committee meetings called at short notice to deal with specific issues as they arose during 2012.

Lord Sharman and subsequently John McFarlane normally attended all meetings of the Committee. Gay Huey Evans attended two meetings by invitation prior to being appointed to the Committee. The group company secretary acted as secretary to the Committee. The chairman of the Committee reported to meetings of the Board on the Committee's work and the Board received a copy of the agenda and the minutes of each meeting of the Committee.

The persons listed in table 2 materially assisted the Committee in considering executive remuneration and attended meetings by invitation during the year.

Table 2: Attendees of the Committee during 2012

Attendee	Position	Comments
Lord Sharman	Chairman of the Company	Attended by invitation
John McFarlane	Chairman designate and then executive chairman	Attended by invitation
Andrew Moss	Group chief executive	Attended by invitation
Kirstine Cooper	Group general counsel and company secretary	Attended as secretary to the Committee
John Ainley	Group HR director	Attended as an executive responsible for advising on remuneration
Carole Jones	Acting group HR director	Attended as an executive responsible for advising on remuneration policy
David Hope	HR director, centres of expertise	Attended as an executive responsible for advising on remuneration policy
Tracey O'Rourke	Group reward and HR policy director	Attended as an executive responsible for advising on remuneration policy
Andrew Pooley	Executive reward director	Attended as an executive responsible for advising on remuneration policy
David Rogers	Chief accounting officer	Attended to advise on matters relating to the performance measures and targets for the Group's share incentive plans
Jason Windsor	Chief strategy and planning officer	Attended to advise on matters relating to the performance measures and targets for the Group's share incentive plans
Amanda Mackenzie	Chief marketing and communications officer	Attended to advise on matters relating to customer target setting

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

In addition to the attendees listed in the table above, Mark Wilson (Group CEO), Russell Walls (non-executive director), Glyn Barker (non-executive director), Patrick Regan (chief financial officer), Paul Boyle (chief audit officer), Rupert McNeill (HR director, centres of expertise) and Bob Orme (director of reward and performance) attended Committee meetings during the year, none of whom were present at meetings when their own remuneration was being discussed.

FIT Remuneration Consultants (FIT) acted as independent advisors to the Committee until May 2012 (having been appointed as advisor to the Committee in August 2011). FIT is a member of the Remuneration Consultants Group and adheres to its Code of Conduct. It provided no other services to the Company during the year.

During the year, the Committee received advice on executive remuneration matters from Deloitte LLP which is a member of the Remuneration Consultants Group and adheres to its Code of Conduct. Deloitte LLP was appointed as advisor to the Committee on 4 December 2012. In addition during the year, management received advice on remuneration matters and taxation from Deloitte LLP and on remuneration matters from Linklaters LLP.

Committee activities during 2012

The Committee takes its responsibility to shareholders very seriously and following the 2012 annual general meeting (AGM) undertook an enhanced engagement programme with major institutional shareholders. The Committee considered the following matters during the year:

Routine remuneration matters:

Consideration of remuneration matters within the Committee's terms of reference, specifically including:

- Consideration and recommendation to the Board of the Group's policy and practices concerning base salaries and benefits-in-kind for EDs and senior management;
- Consideration and approval of the level of bonus awards in respect of the 2011 financial year and approval of the associated grant of share awards under the Annual Bonus Plan (ABP) for EDs and senior management;
- Performance testing of subsisting Long Term Incentive Plan (LTIP) grants which vested in the 2012 financial year; and subsisting One Aviva Twice the Value (OATTV) Plan grants which did not vest and which expired;
- Setting targets for the bonus awards for the 2012 financial year and approving the associated grant of awards under the ABP;
- Approval of 2012 LTIP grants to the EDs and senior management and the associated performance conditions for these grants;
- Reviewing the likely outcomes against the ABP 2012 targets and agreeing underpin measures;
- Approval of the grant of share awards under the Aviva Investors LTIP for the 2012 financial year;
- Approval of the award of Free Shares to UK employees in respect of 2011 under the Aviva All Employee Share Ownership Plan (AESOP); awards to Irish employees under the Aviva Group Employee Share Ownership Scheme; and the invitation to UK employees to participate in the Aviva Savings Related Share Option Scheme and to Irish employees to participate in the Aviva Ireland Save As You Earn Scheme;
- Initial consideration of targets for bonus awards for the 2013 financial year and of 2013 LTIP targets;
- Review of the shareholding requirements of EDs and Group Executive members;
- Review of share plan dilution limits;
- Review of the standard employment terms within employment contracts of EDs and senior management; and
- Review of senior management remuneration at Aviva Investors and of FSA Code Staff.

Non-routine remuneration matters:

- Approval of the departure terms of EDs and members of the Group Executive who left the Group during 2012;
- Consideration and approval of the remuneration arrangements for new members of the Group Executive following the restructuring of the Group and for other senior managers; and
- Review and, as appropriate, approval of any exceptional remuneration proposals for senior managers outside the agreed Group remuneration policy.

Remuneration policy:

- Approval of amendments to the rules of discretionary share plans regarding the reduction in categories of automatic 'good leavers' and the early vesting of awards;
- Review of the policy for buying out unvested awards when recruiting EDs and senior managers;
- Review of pension arrangements for senior management, including the approval of recommendations in relation to contributions into the ACAP; and
- Approval of the cessation of the free share element of the AESOP and the introduction of a matching shares element in 2013.

Governance:

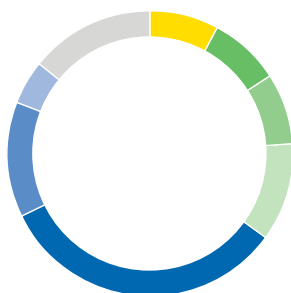
- Approval of the 2011 Directors' Remuneration Report;
- Consideration of the structure of the 2012 Directors' Remuneration Report;
- Review of the Committee's 2012 and 2013 work plan;
- Annual approval of the Remuneration business standard;
- Review and consideration of regulatory developments, including the consultation by the Department for Business, Innovation and Skills on revised remuneration reporting regulations; and
- Consideration of, and agreement on, the appropriate overview of Aviva Investors' remuneration matters.

Shareholder feedback:

- Consultation with major institutional shareholders in respect of their concerns regarding elements of the 2011 Directors' Remuneration Report.

**Remuneration Committee –
Allocation of board agenda time**

■ Pensions	8%
■ Regulatory/ Governance/ Reporting	8%
■ Committee governance (effectiveness, workplan)	8%
■ Liaison with shareholders	11%
■ Director and senior manager objectives, performance, salaries and bonuses	33%
■ Share plans, inc. awards, grants, performance testing	13%
■ Aviva Investors	5%
■ Remuneration policy	14%

**Governance****FSA's Remuneration Code: Aviva Investors**

The FSA's Remuneration Code applies to Aviva Investors and two small 'firms' (as defined by the FSA) within the UK & Ireland Life business. These businesses are subject to the requirement of the FSA's Remuneration Code. Remuneration disclosures for Aviva Investors can be found at www.avivainvestors.com/about_us/our_approach_to_remuneration/index.htm and for the UK & Ireland Life firms at www.aviva.com/media/news/item/fsa-remuneration-code-disclosure-15575/.

Aviva's reward principles and arrangements are designed accurately and appropriately to incentivise and reward employees for achieving stated business goals in a manner that is consistent with the Company's approach to sound and effective risk management.

Committee performance and effectiveness

The Committee undertook an annual review of its performance and effectiveness which concluded that overall the Committee was effective in carrying out its duties. In addition to undertaking an annual programme of activities in 2013, the Committee identified a number of areas for increased focus in 2013.

Remuneration policy in practice

Table 3 below sets out the purpose of key elements of our remuneration structure, how they relate to the Company's strategy and how they will operate, highlighting any changes from 2012.

Table 3: Remuneration policy for EDs

Element	Purpose and link to strategy	Operation for 2013	Changes and associated rationale
Base salary	To provide a core reward for undertaking the role, at a level needed to recruit and retain individuals.	Annual review, with changes taking effect from 1 April each year. This review is informed by: <ul style="list-style-type: none"> Relevant pay data including market practice among the 25 FTSE listed companies either side of Aviva in terms of market capitalisation. Levels of increase for the broader UK employee population. Individual and business performance. 	Taking into account both the Company's performance and the prevailing economic climate, no increases are being made to EDs' base salaries for 2013.
Benefits	To provide employees with market competitive benefits at a level needed to recruit and retain individuals.	Benefits are provided on a market competitive basis and include a cash car allowance, Private Medical Insurance (PMI) and life insurance.	No changes proposed.
Pension	To provide a market competitive level of provision for post-retirement income.	All EDs are eligible to participate in a defined contribution plan up to the annual limit. Any amounts above the annual or lifetime limits are paid in cash.	Payments will no longer be made into the ACAP or the ACDT after 31 March 2014. These were discretionary savings vehicles into which payments in lieu of pension were made and held for at least five years.
ABP	To incentivise executives to achieve the annual business plan. Deferral provides alignment with shareholders and aids retention of key personnel.	Maximum opportunity of 150% of base salary with 75% of base salary payable for plan performance. Performance is assessed against a range of key financial, employee and customer performance indicators and personal objectives. Two-thirds of any bonus awarded is deferred into shares which vest after three years. Additional shares are awarded at vesting in lieu of dividends paid on the deferred shares. Unvested awards are subject to clawback in the event of misconduct or materially adverse misstatement of accounts.	Bonus payments will take account of achievements in relation to Economic Value Added, Economic Capital, and absolute and relative Total Shareholder Return (TSR) to ensure payouts are closely aligned with the shareholder experience.
LTIP	To motivate executives to achieve the Company's longer-term objectives, to align executive interests with those of shareholders and to aid the retention of key personnel.	The plan rules allow for awards to be made up to a maximum of 350% of base salary (and up to 450% of base salary for US employees in exceptional circumstances). In 2013, an award of 300% of base salary will be made to the Group CEO and 225% of base salary to Patrick Regan. No grant will be made to Trevor Matthews who will cease to be an ED prior to the 2013 AGM. Awards will vest subject to the achievement of the following performance targets over a three year performance period: <ul style="list-style-type: none"> 50% of awards vest based on absolute ROE^{1,3} performance; and 50% based on relative TSR² against a comparator group. Unvested awards are subject to clawback in the event of misconduct or materially adverse misstatement of accounts.	The definition of ROE has been refined. The TSR comparator group was reviewed and refocused on the insurance sector. Further details on both of these changes are set out on pages 111 and 112.
Shareholding requirements	To strengthen alignment between executives and shareholders.	Shareholding of 150% of base salary for EDs, and 200% for the Group CEO. EDs are required to retain 50% of the net shares released from executive share plans until the requirements are met.	No change.
Recruitment awards	To secure the required talent in order for Aviva to deliver its strategic plans whilst ensuring any recruitment award represents good value for shareholders.	Any buyout awards will not be more generous than the awards being forfeited and will be made on an equivalent basis, including phased delivery and the application of performance conditions where appropriate.	A revised buyout policy was approved by the Remuneration Committee in 2012.

Notes:

1 ROE is used as an absolute measure of performance, and is commonly used amongst our peers. Targets are set annually within the context of the Company's three-year business plan. Vesting depends upon performance over the three-year period against a target return.

2 Relative TSR is a commonly used method of determining performance against a set of suitable peers, providing a view of relative performance against those peers. TSR is calculated by measuring total capital gains (or losses) accruing in the period if shares are held continuously and dividends paid are immediately reinvested in new shares. The impact of short-term increases (or decreases) in share price on TSRs is reduced by averaging share price across the three months prior to the start and end of the performance period.

3 ROE performance is the same metric described as ROCE performance in the 2011 Directors' Remuneration Report. This is a change in nomenclature only; the definition of the metric has not changed from 2011 to 2012. The definition of ROE in respect of the 2013 has been refined and is described on page 112.

Consideration of wider employee pay

When setting the policy for EDs' remuneration, the Committee has regard to the pay and employment conditions elsewhere within the Group. In particular, the Committee has sight of:

- Salary increases for the general employee population;
- Group-wide benefit offerings (including pensions);
- Overall spend on annual bonus; and
- Participation levels in the annual bonus and LTIP.

The Company does not directly consult with employees when formulating ED pay policy. However it does take into account information provided by the HR function and feedback from employee opinion surveys.

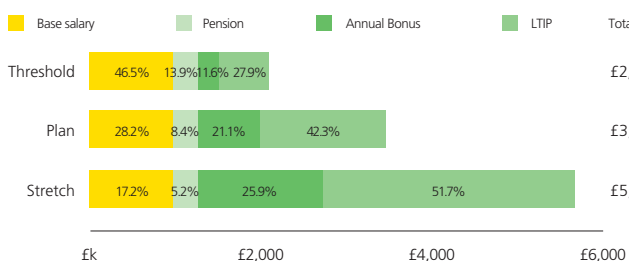
Remuneration scenarios

The charts below illustrate how much the current EDs could earn under different performance scenarios (assuming a constant share price):

- Threshold – Threshold bonus of 25% of base salary and 20% vesting under the LTIP.
- Plan – Plan bonus of 75% of base salary and 50% vesting under the LTIP.
- Stretch – Stretch bonus of 150% of base salary and maximum vesting under the LTIP.

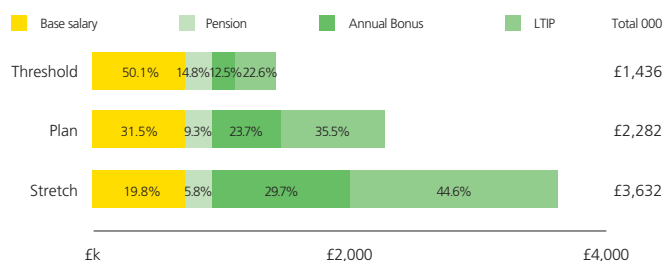
Mark Wilson

Remuneration scenarios – Mark Wilson



Patrick Regan and Trevor Matthews¹

Remuneration scenarios – Patrick Regan and Trevor Matthews



1. Scenarios for Patrick Regan and Trevor Matthews are the same as their base salaries are identical. Trevor Matthews will step down from the Board prior to the 2013 AGM. The above scenarios therefore applied to him for 2012, but will not apply for 2013.

Total remuneration earned in respect of 2012

The Committee recognises the need for transparency on the link between remuneration decisions and performance. We have therefore set out below detail of pay earned by the current EDs in respect of performance to December 2012 and how payments under both the ABP and LTIP have been determined.

Table 4 below sets out the total remuneration earned by each current ED who served during 2012.

Table 4: Total ED remuneration in respect of 2012

	Patrick Regan	Trevor Matthews
Base salary	£698,750	£720,000
Annual bonus (cash and deferred elements)	—	—
LTIP vesting (2010 award) ¹	£607,302	—
Pension contributions ²	£193,103	£212,304
Benefits	£34,114	£85,370
Total remuneration earned in respect to 2012	£1,533,269	£1,017,674

Notes

- 1 Patrick Regan's 2010 LTIP award relates to the three-year performance period ending on 31 December 2012. 69.83% of the award is due to vest in March 2013. An assumed Aviva ordinary share price of 373.00 pence has been used to determine the value of the award.
- 2 Pension contributions consist of employer contributions into the defined contribution section of the Aviva Staff Pension Scheme, excluding salary exchange contributions made by the employees, plus payments in lieu of pension above the lifetime or annual allowance caps.
- 3 Mark Wilson joined the board as an ED on 1 December 2012, and became Group CEO on 1 January 2013. He received no emoluments in respect of 2012.

Further explanatory notes, and information on former EDs who served during 2012, are set out on page 110.

Annual bonus

Table 5 below sets out the Group's performance against its financial, employee and customer KPIs in 2012 and how these would have translated into bonus payments.

Table 5: Group performance in 2012 against its KPIs

	KPIs	Weighting (% of total bonus opportunity)*		
		Plan (%)	Stretch (%)	Actual outcome (%)
Business measures (70%)	Total Capital Generation	10	18.75	18.75
	IFRS Operating Profit	5	18.75	4.48
	Economic Gain	5	5	0
	Internal Rate of Return (IRR)	2.5	5	5
	Volume – Total long-term savings	1.25	1.25	1.25
	Volume – Net written premium	1.25	1.25	0.92
	Customer	5	10	6.43
	Employee	5	10	0
Personal measures (30%) (shown at 'on – plan')	Personal – individual strategic	12.5	25	12.5
	Personal – Common Risk Objective	2.5	5	2.5
	Total	50	100	51.83

*Percentages do not necessarily add up due to rounding.

Solely taking into account Group business and 'on-plan' personal measures would have resulted in a bonus of 78% of salary for EDs in respect of 2012 performance, although business unit performance would also be taken into account reflecting the remit of each ED.

The Committee has taken into account the 'underpin' measures, namely Economic Value Added, Economic Capital, absolute and relative TSR, as described below, to ensure that any bonus payments are more closely aligned to shareholders' experience. Following careful consideration of these metrics by the Committee, it agreed that no ED would receive a bonus in respect of 2012.

LTIP

The award made to Patrick Regan in 2010 was subject to performance conditions set out in table 6 below.

Table 6: LTIP performance conditions

	Threshold (30% vests)	Maximum (100% vests)
ROE performance over three years	31.5%	37.5%
Relative TSR performance	Median	Upper quintile and above

ROE over the three year performance period was 36.9% leading to 46.5% of the maximum 50% vesting. Relative TSR performance resulted in a ranking of 7 out of 15, leading to 23.33% of the maximum 50% vesting. Correspondingly 69.83% of the award is due to vest in March 2013.

Former directors

Igal Mayer

Igal Mayer resigned from the Board on 19 April 2012 and left the Company on 31 May 2012. He is receiving base salary for 12 months in lieu of notice (less gross base salary paid between 19 April 2012 and 31 May 2012), amounting to CAD \$899,732.20. This is being paid in instalments and is subject to mitigation. He also received payment for ten days' accrued but untaken holiday entitlement.

The deferred elements of Mr Mayer's bonuses earned for 2009, 2010 and 2011 were released to him on the first dealing day following his departure date. Mr Mayer received no bonus in respect of the financial year 2012. All unvested LTIP and OATTV plan awards lapsed, with no shares being released from these awards.

Legal fees of £25,000 were paid to Mr Mayer's solicitor in respect of advising on his departure. He will also be eligible to claim for tax compliance services fees until April 2013, up to a maximum of £65,000.

Andrew Moss

Andrew Moss resigned from the Board on 8 May 2012 and left the Company on 31 May 2012. He is receiving base salary in lieu of 12 months' notice (less gross base salary paid between 8 May 2012 and 31 May 2012), amounting to £898,462 in accordance with his contractual entitlements. This is being paid in instalments and is subject to mitigation. In addition, he received £300,000 in full and final settlement of all claims that he might have to a bonus under his contract. Mr Moss will retain the benefit of £209,000 (being 5/12^{ths} of the annual payment made in April 2012) under the ACAP (i.e. the equivalent of a money purchase pension plan). He also received payment for half a day accrued but untaken holiday entitlement.

The 2010 and 2011 bonuses that were deferred into shares lapsed in accordance with the rules of the ABP, as did outstanding awards under the LTIP and the OATTV plans. 75% of the element of the 2009 bonus that was deferred into shares will vest in accordance with the rules of the relevant plan and 25% lapsed upon Mr Moss leaving the Group.

Legal fees of £25,000 were paid to Mr Moss's solicitor in respect of advising on his departure. He also claimed for outplacement services of £20,000.

Remuneration for 2013

Shareholder context

The result of the shareholder vote at the Company's 2012 AGM in respect of the 2011 Directors' Remuneration Report is set out in table 7 below.

Table 7: Result of the vote on Directors' Remuneration Report at 2012 AGM

	For	Against
2012 vote	45.59%	54.41%

Aviva recognises that pay was not sufficiently linked to performance in 2011. As set out in the Remuneration Committee chairman's letter, following consultation with our major institutional shareholders, a number of changes have been made:

- We introduced 'underpin' metrics in respect of bonuses for 2012 and have committed to consider these 'underpin' metrics for future years (until any alternative arrangements are agreed following consultation) to ensure annual bonus pay-outs are more closely aligned to the shareholder experience. Taking into account performance against these measures, the Remuneration Committee will use its discretion to revise bonus outcomes where appropriate. Such discretion, if applied, would only be used to reduce the outcome;
- Future buyouts will be made on a 'like-for-like' basis in line with best market practice; and
- We have also reviewed and changed senior management contracts and the 'good leaver' definition in our share plan rules.

Appointment of Group CEO

Mark Wilson joined the Board on 1 December 2012 and took up the role of Group CEO on 1 January 2013. As announced at the time of his appointment, his remuneration details are as follows:

- Base salary – £980,000 per annum, subject to review in 2014;
- Annual bonus – 75% of base salary for plan performance and 150% of base salary for stretch performance;
- LTIP – he is eligible for an LTIP grant of up to 350% of base salary subject to meeting specific performance conditions over a three year performance period. His 2013 grant will be at 300% of base salary;
- Relocation expenses – he is eligible to claim reasonable and appropriate relocation expenses of up to £200,000 (inclusive of any benefit-in-kind liability which may arise) in respect of relocation from Hong Kong to the UK. If any additional reasonable expenses above this limit are incurred in the course of Mr Wilson's relocation the Remuneration Committee has agreed to consider reimbursement of such additional expenses up to a further limit to be agreed; and
- Benefits – a cash car allowance and PMI.

Base salaries

As highlighted in the Remuneration Committee chairman's letter, EDs' base salaries will not be increased in 2013.

Table 8: EDs' base salaries

	1 April 2012 salary	1 April 2013 salary	Change from 2012
Patrick Regan	£720,000	£720,000	0%
Trevor Matthews	£720,000	£720,000	0%

Annual bonus

As summarised in table 3, the maximum bonus opportunity for all EDs will remain unchanged for the 2013 financial year at 150% of base salary, with two-thirds of any bonus earned subject to compulsory deferral for three years. Unvested awards are subject to clawback and risk of forfeiture during this period.

Annual performance is measured against a range of key financial, employee and customer performance indicators, which account for 70% of the maximum, and against personal objectives, which account for 30% of the maximum.

To align with the business priorities for 2013, the financial measures at Group level will be: net capital returns' profit before tax; MCEV value of new business (for the Life business); combined operating ratio (for the General Insurance business); and total expenses. Personal objectives will include common objectives for effective leadership and risk management.

As highlighted previously, bonus outcomes will also be subject to consideration of our performance against our underpin metrics (Economic Value Added, Economic Capital and TSR).

LTIP

As summarised in table 6, the LTIP vests subject to the degree of achievement of two equally weighted performance measures, absolute ROE and relative TSR performance, which have been chosen to reflect shareholders' long-term interests. For 2013, a grant of 225% of base salary will be made to Patrick Regan and 300% of base salary to Mark Wilson. No grant will be made to Trevor Matthews who will cease to be a director prior to the 2013 AGM.

ROE targets

ROE targets determine the vesting of 50% of any LTIP award and are set annually within the context of the Company's three-year business plan. Vesting depends upon performance over the three-year period against a target return. The 2012 LTIP award ROE targets are set out in table 9.

Table 9: 2012 LTIP ROE Targets

Achievement of ROE targets over the three-year performance period	Percentage of shares in award that vest based on achievement of ROE targets ¹
Less than 30% (2011: less than 33%)	0%
30% (2011: 33%)	10%
Between 30% and 37.5% (2011: Between 33% and 40.5%)	Pro rata between 10% and 50% on a straight line basis
37.5% and above (2011: 40.5% and above)	50%

Notes

¹ The percentage of shares in award that vest based on achievement of ROE targets is the same in 2011 and 2012.

The definition of ROE was refined in early 2013. ROE will now be calculated as IFRS profit after tax and non-controlling interest, excluding the impact of investment variances and economic assumption changes, over average IFRS equity (excluding pension scheme net surplus/deficit) attributable to ordinary shareholders of the Company.

TSR targets

Relative TSR determines the vesting of the other 50% of any LTIP award. To ensure that Aviva's performance is measured against appropriate comparators with similar business operations and geographic footprints, some minor changes were made to the TSR comparator group for 2013. Companies focused on banking were excluded and some more relevant comparators within the insurance sector were added to ensure a robust group.

For the 2013 LTIP grant, performance will therefore be assessed against the following companies: Aegon, Allianz, AXA, CNP Assurances, Direct Line Group, Generali, Legal & General, MetLife, Old Mutual, Prudential, Resolution Limited, Royal & Sun Alliance, Standard Life and Zurich.

TSR vesting operates as set out in table 10 below.

Table 10: TSR vesting schedule for the 2012 LTIP award

TSR position over the three-year performance period	Percentage of shares in award that vests based on achievement of TSR targets
Below median	0%
Median	10%
Between median and upper quintile	Pro rata between 10% and 50% on a straight line basis
Upper quintile and above	50%

For the 2010, 2011 and 2012 LTIP grants, relative TSR is assessed against the following companies: Aegon, Ageas (formerly known as Fortis until January 2011), Allianz, AXA, Generali, ING, Legal & General, Lloyds Banking Group, Prudential, Resolution Limited, Royal Bank of Scotland, Royal & Sun Alliance, Standard Life and Zurich.

All employee share plans

EDs are eligible to participate in a number of HMRC-approved all employee share plans on the same basis as other eligible employees.

These plans included a free share element under the AESOP. Under this element of the AESOP, eligible employees can receive up to a maximum of £3,000 per annum in shares based upon the profits of the Company's UK businesses. The shares are free of tax subject to a retention period. Free shares were awarded in 2012. However, this element of the AESOP has since been discontinued and no awards will be made in 2013. The partnership share element of the AESOP, which the Company also operates, allows participants to invest up to £125 per month out of their gross salary in the Company's shares. There is currently no matching element to this investment by the Company. However a matching element is due to be introduced in April 2013 through which the Company will match every purchased share with two matching shares for the first £40 of a participant's monthly contribution. For as long as the employee remains employed by the Company, matching shares will be subject to forfeiture if purchased shares are withdrawn from the AESOP within three years of purchase. From May 2013 participants will also be eligible to receive Dividend Shares through the AESOP. Shares awarded to, or investments made by, EDs through the AESOP are included in table 20 of this Report.

The Aviva Savings Related Share Option Scheme and Aviva Savings Related Share Option Scheme 2007 allow eligible employees to acquire options over the Company's shares at a discount of up to 20% of their market value at the date of grant. In order to exercise these options, participants must have saved through a three, five, or seven year HMRC-approved savings contract, subject to a maximum savings limit of £250 per month. In 2012, only three and five year contracts were offered. Details of options granted to EDs under these schemes are included in table 19.

Share ownership requirements

The Company has an internal shareholding requirement such that the Group CEO is required to build a shareholding in the Company equivalent to 200% of base salary and each ED is required to build a shareholding in the Company equivalent to 150% of base salary.

The EDs, including the Group CEO, are required to retain 50% of the net shares released from deferred annual bonuses and LTIPs until the shareholding requirement is met. There is no target date for meeting the share ownership requirement.

Unvested share awards including shares held in connection with compulsory bonus deferrals are not taken into account in applying this test. Table 11 below shows the position at 31 December 2012, based on that day's closing middle market price of an ordinary share of the Company of 373.00 pence.

Table 11: EDs' share ownership requirements as at 31 December 2012¹

	Basic salary	Shareholding excluding restricted shares	Value of shareholding based on a share price of 373.00 pence ²	Percentage of basic salary	Shareholding requirement
Patrick Regan	£720,000	191,279	£713,470.67	99% (2011: 47%)	150%
Trevor Matthews	£720,000	104,595	£390,139.35	54% (2011: 0%)	150%

Notes

¹ Mark Wilson joined the Board as an ED on 1 December 2012 and became Group CEO on 1 January 2013. He is entitled to receive a base salary of £980,000 per annum with effect from 1 January 2013 and did not receive a salary in 2012. As Group CEO, he will be required to build a shareholding in the Company equivalent to 200% of his base salary. He did not hold any Aviva shares as at 31 December 2012.

² Based on the closing middle market price of an ordinary share of the Company on 31 December 2012.

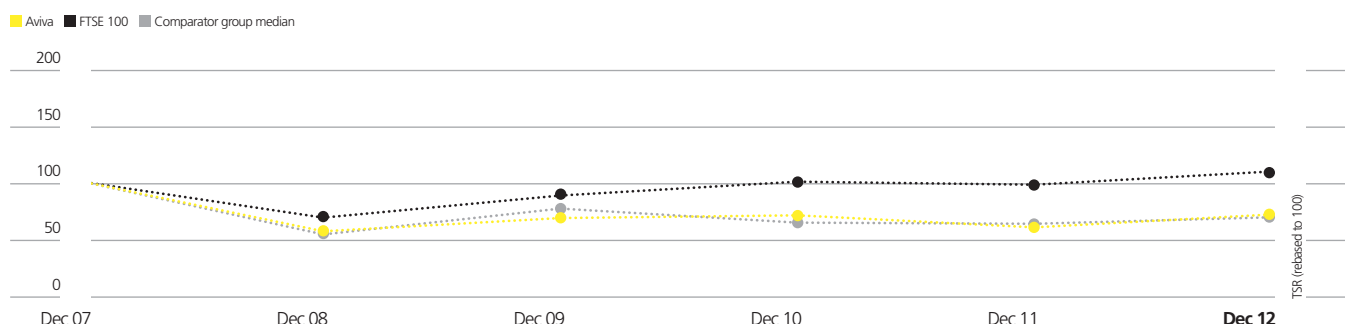
Pension

EDs participate in a defined contribution plan under which they can elect to receive 31% of base salary from the Company minus a contribution of 8% of base salary up to the Scheme Specific Earnings cap (£138,000 in 2012/2013). Above the annual or life-time allowance, a cash alternative in lieu of pension is offered subject to a limit of 31% of base salary minus the 8% contribution.

Performance graph

Table 12 below compares the TSR performance of the Company over the past five years with the TSR of the FTSE 100 Return Index. This index has been chosen because it is a recognised equity market index of which Aviva is a member. The companies which comprise the current LTIP comparator group for TSR purposes are listed in the 'TSR targets' section above. The TSR graph for the comparator group has been plotted using the 15 companies (including Aviva) in the comparator group for the 2007 grant, the 16 companies (including Aviva) in the comparator group for the 2008 grant, the 15 companies (including Aviva) in the comparator group for the 2009 and 2010 grants, and the 14 companies (excluding Aviva) in the comparator group for the 2011 and 2012 grants.

Table 12: Aviva plc five-year TSR performance against the FTSE 100 Return Index and the median of the comparator group



EDs' employment contracts

The key employment terms and conditions of each of the current EDs, as stipulated in their employment contracts, are set out in table 13 below.

Table 13: EDs' key terms and conditions of employment

Provision	Policy
Notice period	
By the director	6 months.
By the Company	12 months, rolling. No notice or payment in lieu to be paid where the Company terminates for cause.
Termination payment	Pay in lieu of notice up to a maximum of 12 months' base salary. This may be increased by a discretionary redundancy payment (where appropriate) but any such further termination payment is capped at 12 months' base salary. Any amount is subject to phased payment and mitigation requirements.
Remuneration and benefits	As described in this Report the operation of the ABP and LTIP is at the Company's discretion and, in the case of the ACAP and ACDT, at the trustees' discretion.
Expenses	Reimbursement of expenses reasonably incurred in accordance with their duties.
Car allowance	Car allowance is received in accordance with the terms of the relevant scheme in operation for the Company as varied from time to time.
Holiday entitlement	30 working days plus public holidays.
Other benefits	Other benefits include PMI and participation in the Company's staff pension scheme.
Private medical insurance	Private medical insurance is provided for the ED and the ED's family or the ED can choose to opt out of this benefit or take a lower level of cover and receive 75% of the difference in the cash value of this benefit which will be paid through salary on a monthly basis.
Sickness	In line with senior management terms, i.e. 100% of base salary for 52 weeks, and 75% thereafter.
Non-compete	During employment and for six months after leaving.
Contract dates	Director: Date current contract commenced: Mark Wilson 1 January 2013 Patrick Regan 22 February 2010 Trevor Matthews 2 December 2011 ³ Igal Mayer 19 January 2011 ¹ Andrew Moss 1 January 2007 ²

Notes

- 1 Igal Mayer resigned from the Board on 19 April 2012 and left the Company on 31 May 2012.
- 2 Andrew Moss resigned from the Board on 8 May 2012 and left the Company on 31 May 2012.
- 3 Trevor Matthews will resign from the Board prior to the 2013 AGM.

External board appointments

The Company recognises that its EDs can benefit from serving in a personal capacity as a non-executive director of non-Aviva Group companies. At the same time, it is conscious of the corporate governance recommendations that EDs should take account of the time commitment required by a non-executive director (NED) position and ensure that any such role does not impact their ability to carry out fully their executive duties. The Company therefore has a policy of normally allowing senior executives to serve as a NED of one external company, subject to approval by the Board, and for the individual to retain any board fees. None of the EDs held external NED appointments during 2012. Following the disposal of the Group's interests in Delta Lloyd N.V. in January 2013, Patrick Regan, who was until that time a Company-nominated member on the supervisory board of Delta Lloyd N.V., continued to be a member of the supervisory board in a personal capacity. From that point he has therefore held an external NED appointment. During the time he was a Company-nominated member on the supervisory board of Delta Lloyd N.V. he did not receive a board fee.

Non-executive directors

The NEDs, including the chairman of the Company, have letters of appointment which set out their duties and responsibilities. The key terms of the appointments are set out in table 14 below.

Table 14: NED key terms of appointment

Provision	Policy		
Period	In line with the requirement of the UK Corporate Governance Code, all NEDs are subject to annual re-election by shareholders at each AGM.		
Termination	By the director or the Company at their discretion without compensation upon giving one month's written notice for NEDs and three months' written notice for the chairman of the Company.		
Fees	As set out in table 15.		
Expenses	Reimbursement of travel and other expenses reasonably incurred in the performance of their duties.		
Time commitment	Each director must be able to devote sufficient time to the role in order to discharge his or her responsibilities effectively and spend a minimum of 25 days a year on Company business. NEDs spend an average of 41 days a year on Company business, with the chairmen of the Audit, Remuneration and Risk Committees spending substantially more.		
Appointment dates	Director	Date of last appointment on letter of appointment	Appointment end date on letter of appointment
	Glyn Barker	3 May 2012	AGM 2013
	Mary Francis ¹	3 May 2012	AGM 2013
	Richard Karl Goeltz ²	3 May 2012	AGM 2013
	Euleen Goh ³	3 May 2012	AGM 2013
	Michael Hawker	3 May 2012	AGM 2013
	Gay Huey Evans	3 May 2012	AGM 2013
	John McFarlane	3 May 2012	AGM 2013
	Lord Sharman ⁴	3 May 2012	AGM 2013
	Leslie Van de Walle ⁵	4 May 2011	AGM 2012
	Russell Walls ⁶	3 May 2012	AGM 2013
	Scott Wheway	3 May 2012	AGM 2013

Notes

1 Mary Francis resigned from the Board on 3 October 2012.

2 Richard Karl Goeltz will retire from the Board prior to the 2013 AGM.

3 Euleen Goh resigned from the Board on 31 December 2012.

4 Lord Sharman retired from the Board on 30 June 2012.

5 Leslie Van de Walle resigned from the Board on 2 May 2012.

6 Russell Walls will retire from the Board prior to the 2013 AGM.

It is the Company's policy to set the fees paid to the chairman of the Company and NEDs taking account of the median market payments in international companies of similar size and complexity. NEDs receive a basic annual fee in respect of their Board duties. A further fee is paid to NEDs in respect of membership and, where appropriate, chairmanship of Board committees.

Fees are reviewed annually and are set by the Board to attract individuals with the required range of skills and experience. In determining the level of fees paid to the NEDs, the Board receives recommendations from the EDs, who consider the NEDs' duties and responsibilities, together with the time commitment required in preparing for and attending meetings, and the amounts paid by competitors and similar-sized companies.

The Chairman of the Company and NEDs do not participate in any incentive or performance plans or pension arrangements and they also do not receive an expense allowance.

The Company's articles of association provide that the total aggregate remuneration paid to the Chairman of the Company and NEDs will be determined by the Board within the limits set by shareholders. The current aggregate limit of £2 million was approved by shareholders at the Company's 2012 AGM. EDs are remunerated under their employment contracts and receive no additional fee for serving as Board directors.

Following a review of the fees for holding the position of the senior independent director or a committee chairman or in respect of committee membership, the Board agreed to the fee changes shown in table 15 below. These increases were effective from 1 April 2012. The Board does not intend to increase the fees in 2013. The total amount paid to NEDs in 2012 was £1.5 million.

Table 15: NEDs' fees from 1 April 2012

Role	Fee from 1 April 2011	Fee from 1 April 2012
Chairman of the Company ¹	£550,000	£550,000
Chairman designate ^{1,2}	N/A	£275,000
Board membership fee	£65,000	£65,000
Additional fees are paid as follows:		
Senior independent director	£25,000	£35,000
Committee chairman (inclusive of committee membership fee)		
– Audit	£35,000	£45,000
– Corporate Responsibility	£10,000	£20,000
– Remuneration	£30,000	£35,000
– Risk	£35,000	£45,000
Committee membership		
– Audit	£10,000	£15,000
– Corporate Responsibility	£7,500	£10,000
– Nomination	£7,500	£7,500
– Remuneration	£10,000	£12,500
– Risk	£10,000	£15,000

Notes

1 Inclusive of Board membership fee and any committee membership fees.

2 The fee for the chairman designate was effective from the commencement of the role on 1 January 2012 until 30 June 2012.

Chairman

John McFarlane became chairman designate on 1 January 2012. The fees for his role as chairman of the Company had been set at £550,000 per annum. He became interim executive deputy chairman in May 2012 following Andrew Moss' departure and executive chairman of the Company on 1 July 2012 until 31 December 2012. Despite the increased responsibilities and time commitment required, John McFarlane indicated that he did not wish to be considered for any additional fee in respect of his role and his fees remained at £550,000 per annum.

Employment contracts and letters of appointment

EDs' employment contracts and NEDs' letters of appointment are available for inspection at the Company's registered office during normal hours of business, and at the place of the Company's 2013 AGM from 10.45am on 9 May 2013 until the close of the meeting.

Directors' remuneration in 2012 (audited information)

Table 16 below sets out the remuneration paid or payable to the directors in respect of the year to 31 December 2012.

Table 16: Directors' remuneration in 2012^{9, 10}

	Base salary/fees		Bonus ¹		In-Lieu Pension		Benefits ²		Total	
	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000
Chairman/executive chairman										
John McFarlane ³	413	24	—	—	—	—	145	11	558	35
Executive directors										
Trevor Matthews ⁴	720	58	—	45	188	—	85	51	993	154
Patrick Regan ⁵	699	626	—	765	153	—	34	32	886	1,423
Non-executive directors⁶										
Glyn Barker	76	—	—	—	—	—	1	—	77	—
Richard Karl Goeltz	119	107	—	—	—	—	1	—	120	107
Michael Hawker	137	93	—	—	—	—	—	—	137	93
Gay Huey Evans	96	15	—	—	—	—	—	—	96	15
Russell Walls	129	118	—	—	—	—	2	—	131	118
Scott Wheway	112	103	—	—	—	—	—	—	112	103
Former executive directors¹¹										
Igal Mayer ⁷	193	606	—	632	—	—	408	455	601	1,693
Andrew Moss ⁸	338	951	—	1,156	216	480	16	98	570	2,685
Former non-executive directors¹¹										
Mary Francis	76	113	—	—	—	—	1	—	77	113
Euleen Goh	92	83	—	—	—	—	—	—	92	83
Lord Sharman	275	536	—	—	—	—	20	33	295	569
Leslie Van de Walle	30	85	—	—	—	—	—	—	30	85
Total emoluments of directors⁹	3,505	3,518	—	2,598	557	480	713	680	4,775	7,276

Notes

- As disclosed elsewhere in this Report, following careful consideration the Committee decided that EDs would not receive a bonus for 2012.
- The benefits disclosure includes the cost, where appropriate, of PMI, life assurance, accommodation, travel and car benefits. All the numbers disclosed include the tax charged on the benefits, where applicable. No directors received an expense allowance during the year.
- The chairman received travel related benefits, and medical insurance during his period as executive chairman. In accordance with the terms of his appointment, as disclosed in the 2011 Directors' Remuneration Report, he received reimbursement for such costs reasonably incurred in connection with his relocation to the UK during the 12 month period from the date of his appointment up to a maximum of £125,000, plus reimbursement of the costs incurred in respect of advice sought on the legal and tax implications of his appointment, together with any VAT or equivalent tax payable thereon.
- Trevor Matthews received contributions in lieu of pension above the pension annual allowance limit. The figure shown represents contributions paid or payable for 2012. Cash payments were made for the period January to March 2012. A payment into the ACDT was made in April 2012, covering the period April 2012 to March 2013. The portion of the payment relating to 2012 is shown here.
- Patrick Regan received contributions in lieu of pension above the pension annual allowance limit, paid as cash. The figure shown represents contributions paid or payable for 2012.
- NEDs are reimbursed for expenses, and any tax arising on those expenses is settled directly by Aviva.
- Figures shown for Igal Mayer have been converted from Canadian dollars to pounds sterling at the average exchange rate for 2012 of CAD \$1.58: £1.00. As disclosed in the 2011 Directors' Remuneration Report, Mr Mayer was entitled to first class return flights between Toronto and London, and a travel allowance of up to £40,000 per annum for his spouse and dependent children for travel to and from Toronto and London. Aviva also met the cost of rental accommodation in London and utility costs, as well as assistance in preparing his tax returns in line with standard policy. Aviva met the cost of any taxes due on these benefits. Mr Mayer is entitled to receive a further £594,451 in termination payments. This is made up of a payment in lieu of notice (paid in instalments) and legal fees as set out on page 110.
- Andrew Moss received no bonus for 2012, although details of a £300,000 payment in full and final settlement of all claims that he might have a bonus are set out elsewhere in this Report. Mr Moss received a contribution in lieu of pension of £503,000 into the ACAP in April 2012, although only £209,000 of this payment was allowed to vest as part of his departure terms. The remaining £294,000 lapsed. He also received a cash supplement in lieu of pension of £6,769. Mr Moss is entitled to receive a further £923,462 in termination payments. This is made up of a payment in lieu of notice (paid in instalments) and legal fees as set out on page 110.
- For the purposes of the disclosure required by Schedule 5 to the Large & Medium-sized Companies and Groups (Accounts & Reports) Regulation 2008, the total aggregate emoluments of the directors in respect of 2012 was £6.3 million (2011: £7.7 million). The 2012 figure includes the emoluments for all the directors set out in table 16 and the termination benefits payable to Mr Moss and Mr Mayer as set out in Notes 7 and 8 above. The total aggregate emoluments for 2011 included in table 16 excludes those directors that resigned from office prior to 1 January 2012. Those directors are Mark Hodges (2011 emoluments: £278,722), Andrea Moneta (2011 emoluments: £76,116) and Carole Pivnicka (2011 emoluments: £85,000). The total aggregate emoluments for 2011 including those directors was £7.7 million.
- Mark Wilson joined the Board as an ED on 1 December 2012, and became Group CEO on 1 January 2013. He received no emoluments in respect of 2012 and so is not included in this table.
- The remuneration figures shown in the table are for or relate to the period during which the director was a director of the Company.

EDs' pension arrangements (audited information)

The position of the EDs with respect to accumulated pension benefits under the defined benefits section of the Aviva Staff Pension Scheme (ASPS) is set out in table 17 below.

Table 17: EDs' pension benefits^{5, 8}

	Igal Mayer ⁷ £000	Andrew Moss £000	Trevor Matthews £000	Patrick Regan £000
Benefit type	Defined benefit/defined contribution	Defined benefit	Defined contribution	Defined contribution
Accrued annual pension at 31 December 2011 ¹	431.9	22.5	—	—
Accrued annual pension at 31 December 2012 ⁷	447.3	23.6	—	—
Gross increase in accrued pension over the year	15.4	1.1	—	—
Increase (decrease) in accrued pension net of inflation over the year	8.5	—	—	—
Employee contribution during the year	—	—	—	—
Defined contribution/defined benefit employer contributions during the year ²	96.3	—	32.9	50.0
Transfer value of accrued pension at 31 December 2011 ⁴	7,677.5	529.5	—	—
Transfer value of accrued pension at 31 December 2012 ⁴	8,730.9	545.3	—	—
Change in transfer value during the period less employee contributions ³	1,053.4	15.8	—	—
Transfer value of net increase (decrease) in accrued pension less employee contributions ⁶	166.8	—	—	—
Age at 31 December 2012 (years)	51	54	60	46

Notes

- Accrued pensions shown are the amounts that would be paid annually on retirement based on service to the end of the year (or date of leaving if earlier).
- The defined contribution employer contributions during the year for Patrick Regan and Trevor Matthews include salary exchange contributions of £9,534 and £8,280 respectively.
- The change in transfer value allows for fluctuations in the transfer value due to factors beyond the control of the Company and directors, such as changes in market conditions.
- The transfer values have been calculated in line with the relevant legislation and using actuarial assumptions agreed by the trustee. The transfer value at 31 December 2011 previously provided for Igal Mayer included the value of the early retirement subsidies for which Mr Mayer did not qualify following his resignation during 2012.
- No former directors received any increase in retirement benefits in excess of the amount to which they were entitled, on the later of the date when the benefits first became payable, or 31 March 1997.
- The transfer value of net increase (decrease) in accrued pension shows the value of the increase (decrease) in accrued pension net of the inflation, over the year, net of contributions. This is zero for UK based employees as there is no further accrual of benefits and accrued benefits are increased up to retirement in line with inflation.
- Igal Mayer is a member of the Aviva Canada Pension Plan, and the figures shown for him have been converted from Canadian dollars to pounds sterling at the average exchange rate for 2012 of CAD \$1.58 : £1.00. Igal Mayer received contributions into the defined contribution section of the Aviva Canada pension plan. The value of his defined benefit pension plan, whilst no longer subject to future service accrual, remained subject to revaluation by reference to salary during 2012.
- Benefits deriving from additional voluntary contributions (AVCs) paid by directors are excluded from the amounts below.

Developments in 2013

On 7 February 2013, Aviva announced that Trevor Matthews, executive director and chairman, Developed Markets, will step down from the Board prior to the 2013 AGM. Mr Matthews' departure terms are not yet agreed, and will be reported in the 2013 Directors' Remuneration Report.

On 14 January 2013, Aviva announced that Sir Adrian Montague had joined the Board as a non-executive director with effect from the same date.

On 28 January 2013, Aviva announced that Bob Stein had joined the Board as a non-executive director with effect from the same date.

On 6 March 2013, Aviva announced that Richard Karl Goeltz, senior independent director, and Russell Walls, non-executive director, will step down from the Board prior to the 2013 AGM.

Share awards (audited information)

Table 18 below sets out the current position (or the position as at the date of resignation of the director from the Board) of those share-based awards made to the EDs who served during 2012 under current remuneration arrangements.

Table 18: LTIP, ABP, OATTV Plan, CFO Recruitment Share Awards Plan and Conditional Share Award

	At 1 January 2012 Number	Awards granted during year ¹⁴ Number	Awards vesting during year ¹ Number	Awards lapsing during year Number	At 31 December 2012 ¹¹ Number	Market price at date awards granted ¹ Pence	Market price at date awards vested Pence	Normal Vesting Date
Patrick Regan								
<i>Aviva Long Term Incentive Plan</i>								
2010 ²	233,160	—	—	—	233,160	387.70		Mar-13
2011 ²	311,059	—	—	—	311,059	435.60		Mar-14
2012 ³	—	425,223	—	—	425,223	331.50		Mar-15
<i>Aviva Annual Bonus Plan</i>								
2011	102,741	—	—	—	102,741	435.60		Mar-14
2012	—	151,700	—	—	151,700	331.50		Mar-15
<i>CFO Recruitment Share Awards Plan⁷</i>								
2010 (RRSA) ⁵	170,393	13,414 ⁶	98,610	—	85,197	394.20	356.80	Feb-12, 13 ⁸
2010 (BRDSA) ⁵	43,231	—	—	—	43,231	387.70		Mar-13
2010 (OATTV) ²	55,051	—	—	—	55,051	387.70		Mar-13
Trevor Matthews								
<i>Aviva Long Term Incentive Plan</i>								
2011 ²	373,271 ¹⁰	—	—	—	373,271 ¹⁰	300.80		Mar-14
2012 ³	—	482,142	—	—	482,142	331.50		Mar-15
<i>Aviva Annual Bonus Plan</i>								
2012	—	8,928	—	—	8,928	331.50		Mar-15
<i>Conditional Share Award⁹</i>								
2011	653,721	—	217,907	—	435,814	320.80	356.80	Mar-12, 13,14

Table 18: LTIP, ABP, OATTV Plan, CFO Recruitment Share Awards Plan and Conditional Share Award (continued)

	At 1 January 2012 Number	Awards granted during year ¹⁴ Number	Awards vesting during year ⁴ Number	Awards lapsing during year Number	At 31 December 2012 ¹¹ Number	Market price at date awards granted ¹ Pence	Market price at date awards vested Pence	Normal Vesting Date
Andrew Moss¹²								
<i>Aviva Long Term Incentive Plan</i>								
2009 ³	632,324	—	516,419	115,905	—	245.00	344.80	Mar-12
2010 ²	419,365	—	—	—	419,365	387.70		Mar-13
2011 ²	586,117	—	—	—	586,117	435.60		Mar-14
2012 ³	—	785,714	—	—	785,714	331.50		Mar-15
<i>Aviva Annual Bonus Plan</i>								
2009	115,365	58,446 ⁶	173,811	—	—	245.00	344.80	Mar-12
2010	104,702	—	—	—	104,702	387.70		Mar-13
2011	158,393	—	—	—	158,393	435.60		Mar-14
2012	—	229,342	—	—	229,342	331.50		Mar-15
<i>One Aviva, Twice The Value bonus plan</i>								
2009 ³	195,876	—	—	195,876	—	245.00		Mar-12
2010 ²	177,770	—	—	—	177,770	387.70		Mar-13
Igal Mayer¹³								
<i>Aviva Long Term Incentive Plan</i>								
2009 ³	192,871	—	157,517	35,354	—	245.00	344.80	Mar-12
2010 ²	433,296 ¹⁰	—	—	—	433,296 ¹⁰	387.70		Mar-13
2011 ²	362,056	—	—	—	362,056	435.60		Mar-14
2012 ³	—	472,873	—	—	472,873	331.50		Mar-15
<i>Aviva Annual Bonus Plan</i>								
2010	51,155	—	—	—	51,155	387.70		Dec-12
2011	96,722	—	—	—	96,722	435.60		Mar-14
2012	—	125,989	—	—	125,989	331.50		Mar-15
<i>One Aviva, Twice The Value bonus plan</i>								
2009 ³	64,486	—	—	64,486	—	245.00		Mar-12
2010 ²	38,366	—	—	—	38,366	387.70		Mar-13

- Notes**
- The actual price used to calculate the ABP and LTIP awards is based on a three day average closing middle market price of an ordinary share of the Company. These were in 2009: 256 pence, 2010: 386 pence, 2011: 434 pence and 2012: 336 pence. The three day average closing middle market price of an ordinary share of the Company used to grant the 2009 OATTV Plan awards were in 2009: 256 pence and 2010: 386 pence. The five day average closing middle market price of an ordinary share of the Company used to grant the Replacement Restricted Share Award (RRSA) in 2010 was 380.22 pence. The three day average closing middle market price of an ordinary share of the Company used to grant the Bonus Replacement Deferred Share Award (BRDSA) in 2010 was 386 pence. The three day average closing middle market price of an ordinary share of the Company used to grant the Conditional Share Award in 2011 was 309 pence.
 - The performance periods for these awards begin at the commencement of the financial year in which the award is granted.
 - The performance conditions for awards which were granted or which vested during 2012 are explained elsewhere in this Report. The performance periods for these awards begin at the commencement of the financial year in which the award is granted.
 - The award date for the awards granted in 2009 which vested in 2012 was 26 March 2009, the award date for the award granted in 2010 which vested in 2012 was 11 March 2010 and the award date for the award granted in 2011 which vested in 2012 was 2 December 2011. The awards which vested in 2012 were released with the net amount being settled in shares and the balance settled in cash and used to pay the resulting tax liability. The monetary value of awards will be calculated by multiplying the relevant number of shares by the closing middle market price of an ordinary share of the Company at the date of vesting.
 - The shares comprising these awards are restricted shares which are beneficially owned by Patrick Regan and held in trust on his behalf under the terms of a restricted share award agreement. As outlined in the 2010 Directors' Remuneration Report, income tax and National Insurance Contributions liabilities were paid on the RRSA on 11 March 2010 and on the BRDSA on 30 March 2010.
 - These figures relate to shares issued in lieu of dividends accrued during the deferral period.
 - The awards under the CFO Recruitment Share Awards Plan were granted to Patrick Regan following his recruitment in 2010. As disclosed in the 2010 Directors' Remuneration Report, the RRSA will vest in tranches subject to Mr Regan meeting his personal performance targets, the OATTV is subject to the same performance conditions as the OATTV Plan awards granted to other EDs in 2010 and the BRDSA is not subject to performance conditions and will vest on the third anniversary of the date of grant subject to Mr Regan remaining in employment with the Company.
 - The performance target attached to the second tranche of the RRSA was met and this tranche vested on 8 March 2012 being the first dealing day following the normal vesting date where no dealing restrictions were in place.
 - The Conditional Share Award was granted to Trevor Matthews following his recruitment in 2011. As disclosed in the 2011 Directors' Remuneration Report, this award is not subject to performance conditions and will vest in tranches subject to Trevor Matthews remaining in employment with the Company. Trevor Matthews will cease to be a director of the Company prior to the 2013 AGM. The treatment of his awards will be determined on his ceasing to be an employee of the Company.
 - These shares were awarded as Phantom Units which will be cash settled on vesting and no shares will be transferred or allotted.
 - The information shown in this column for Andrew Moss is as at his resignation from the Board on 8 May 2012 and for Igal Mayer is as at his resignation from the Board on 19 April 2012.
 - 25% of Andrew Moss' 2010 ABP award and 100% of his 2011 and 2012 ABP awards, 2010, 2011 and 2012 LTIP awards and 2010 OATTV award lapsed on his leaving the Company on 31 May 2012. The remaining 75% of his 2010 ABP award will vest on the normal vesting date.
 - Igal Mayer's ABP awards vested on 1 June 2012, the first business day after leaving the Company on 31 May 2012. Mr Mayer's 2010, 2011 and 2012 LTIP awards and 2010 OATTV award lapsed on his leaving the Company on 31 May 2012.
 - The aggregate net value of share awards granted to the directors in the period was £8.9 million (2011: £12.1 million). The net value has been calculated by reference to the closing middle market price of an ordinary share of the Company at the date of grant. This excludes shares issued in lieu of dividends.

Share options (audited information)

Details of the EDs who were in office for any part of the 2012 financial year and hold or held options over ordinary shares of the Company pursuant to the Company's share based incentive plans are set out in table 19 below.

Savings-related share options refer to options granted under the HMRC-approved Aviva Savings Related Share Option Scheme 2007. Options are normally exercisable during the six-month period following the end of the relevant (three, five and seven year) savings contract.

Executive share options (approved) refer to options granted under the HMRC-approved schedule to the Aviva Executive Share Option Plan 2005. Options will be exercisable on 30 March 2013 to the extent that the LTIP awards granted in 2010 have vested. Any gain made on exercise of these options will be used to reduce the number of shares vesting under the LTIP. Therefore, the vesting of the options will not increase the overall number of shares received by the EDs from their LTIP awards.

Table 19: EDs' options over Aviva plc shares

	At 1 January 2012 Number	Options granted during year Number	Options exercised during year Number	Options lapsing during year Number	At 31 December 2012 Number	Exercise Price Pence	Exercise Period ³
Patrick Regan							
Savings-related options 2010	2,903	—	—	—	2,903	310.0	Dec 13 – May 14
Executive share options (approved) 2010	7,772	—	—	—	7,772	386.0	Mar 13
Andrew Moss¹							
Executive share options (approved) 2010	7,772	—	—	—	7,772	386.0	Mar 13
Igal Mayer²							
Savings-related options 2011	5,923	—	—	—	5,923	268.0	Dec 18 – May 19

Notes

1 The information shown for Andrew Moss is as at the date of his resignation from the Board on 8 May 2012. Mr Moss' executive share options lapsed on leaving the Company on 31 May 2012.

2 The information shown for Igal Mayer is as at his resignation from the Board on 19 April 2012. Mr Mayer's savings-related options lapsed on leaving the Company on 31 May 2012.

3 Any unexercised options will lapse at the end of the exercise period.

The closing middle market price of an ordinary share of the Company on 31 December 2012 was 373.00 pence, and the closing middle market price of an ordinary share of the Company during the year ranged from 255.30 pence to 384.00 pence. During the year, no share options were exercised by directors (2011: nil).

EDs did not pay for the award of any share options. The savings related options are granted under an all-employee share scheme and are not subject to performance conditions. The executive share options are linked to awards under the LTIP which are subject to performance conditions (ROE and relative TSR). Additional information can be found in the sections titled 'LTIP', 'ROE targets' and 'TSR targets' on pages 111 and 112.

Dilution

Awards granted under the Aviva employee share plans are met by the funding of two employee trusts administered by external trustees that acquire shares in the market. The current practice is that new issue shares will generally only be issued where it is not practicable or permissible to use the trust. However, the funding policy is kept under review by the Committee and the Board. Details of the shares currently held in the employee trusts are set out in note 31.

During 2012, loans totalling £21.3 million were made to RBC Trustees (CI) Ltd and loans totalling £11.6 million were made to EES Trustees International Ltd to ensure sufficient shares were available to meet the Company's on-going liabilities.

The Company monitors the number of shares issued under the Aviva employee share plans and their impact on dilution limits. The Company's usage of shares compared to the relevant dilution limits set by the Association of British Insurers (ABI) in respect of all share plans (10% in any rolling ten-year period) and executive share plans (5% in any rolling ten-year period) was 3.53% and 2.06% respectively on 31 December 2012.

Directors' interests in Aviva shares

The interests held by each person who was a director during the 2012 financial year and their connected persons in the ordinary shares of the Company are shown in table 20 below. All the disclosed interests are beneficial. The table also summarises the interests in shares held through the Company's various share incentive plans.

Table 20: Directors' interests in Aviva shares⁹

	Shares ¹		ABP ²		LTIP ³		OATTV Plan ⁴		Options ⁵	
	1 January 2012 ⁷	31 December 2012 ⁸	1 January 2012	31 December 2012	1 January 2012	31 December 2012	1 January 2012	31 December 2012	1 January 2012	31 December 2012
Glyn Barker ⁷	—	—	—	—	—	—	—	—	—	—
Mary Francis	4,700	4,700	—	—	—	—	—	—	—	—
Richard Karl Goeltz ⁶	17,500	17,500	—	—	—	—	—	—	—	—
Euleen Goh	—	—	—	—	—	—	—	—	—	—
Michael Hawker	5,000	5,000	—	—	—	—	—	—	—	—
Gay Huey Evans	—	—	—	—	—	—	—	—	—	—
Trevor Matthews	—	104,595	653,721 ¹⁰	444,742 ¹⁰	373,271 ¹¹	855,413 ¹²	—	—	—	—
Igal Mayer ¹⁷	226,150	312,575	147,877	273,866	988,223 ¹⁵	1,268,225 ¹⁵	102,852	38,366	5,923	5,923
John McFarlane	10,000	10,000	—	—	—	—	—	—	—	—
Andrew Moss ¹⁸	572,216	603,815	378,460	492,437	1,637,806	1,791,196	373,646	177,770	7,772	7,772
Patrick Regan	312,335	319,707	316,365	382,869	544,219	969,442	55,051 ¹³	55,051 ¹³	10,675	10,675
Lord Sharman	38,426 ¹⁴	40,176 ¹⁴	—	—	—	—	—	—	—	—
Leslie Van de Walle	17,485 ¹⁶	17,485 ¹⁶	—	—	—	—	—	—	—	—
Russell Walls	8,000	8,000	—	—	—	—	—	—	—	—
Scott Wheway	13,579	13,579	—	—	—	—	—	—	—	—
Mark Wilson	—	—	—	—	—	—	—	—	—	—

Notes

- ¹ 'Shares' are the directors' beneficial holdings in the ordinary shares of the Company and in respect of the EDs include any shares held in trust under the AESOP, being shares purchased by them under the partnership element of the AESOP and any shares granted under the free share element of the AESOP. In respect of Patrick Regan, it also includes the remaining restricted shares held in trust from his RRSA and BRDSA awarded under the rules of the CFO Recruitment Share Awards Plan. In respect of Andrew Moss, it also includes the remaining restricted shares held in trust from his 2009 and 2010 ABP awards (220,067 shares held at 1 January 2012 and 104,702 shares held at 8 May 2012 the date he ceased to be a director).
- ² ABP relates to entitlements to shares arising through the Aviva Annual Bonus Plan 2005 and the Aviva Annual Bonus Plan 2011. Under these plans, some of the earned bonuses are paid in the form of conditional shares and deferred for three years. For Andrew Moss, this includes the restricted shares referred to in note 1 above. The transfer of the shares to the director at the end of the period is not subject to the attainment of performance conditions but the shares can be forfeited if the ED leaves service before the end of the period. In respect of Patrick Regan, 213,624 shares held at 1 January 2012 and 128,428 shares held at 31 December 2012 represent the outstanding shares from the RRSA and BRDSA awarded under the rules of the CFO Recruitment Share Awards Plan and are restricted shares. In respect of Trevor Matthews, 653,721 shares held as at 1 January 2012 and 435,814 shares held as at 31 December 2012 represent the unvested shares awarded under the terms of the Conditional Share Award.
- ³ Awards granted under the LTIP which vest only if the performance conditions are achieved.
- ⁴ OATTV Plan awards were granted as a match to the bonus plan awards under the ABP and vest only if the performance conditions are achieved.
- ⁵ 'Options' are options over shares granted under the SAYE and the Aviva Executive Share Option Plan 2005.
- ⁶ In addition to his ordinary shareholding Richard Karl Goeltz held 14,000 8.25% Capital Securities on 1 January 2012 and 31 December 2012.
- ⁷ The information given in this column is as at 1 January 2012 or the date of appointment of the director (Glyn Barker: 27 February 2012; Mark Wilson: 1 December 2012). On appointment neither of the directors held any shares, awards or options.
- ⁸ The information given in this column is as at 31 December 2012 or the date on which a director ceased to be a director of the Company (Mary Francis: 3 October 2012; Igal Mayer: 19 April 2012; Andrew Moss: 8 May 2012; Lord Sharman: 30 June 2012 and Leslie Van de Walle: 2 May 2012).
- ⁹ The interests of connected persons to the directors are included in the directors' interests given in the table.
- ¹⁰ These shares include the balance of the Conditional Share Award.
- ¹¹ These shares were awarded as phantom units in 2011 which will be cash settled on vesting and no shares will be transferred or allotted.
- ¹² These shares represent the phantom units awarded as per note 11 and the LTIP award granted in 2012.
- ¹³ These shares represent the OATTV awarded under the rules of the CFO Recruitment Share Awards Plan.
- ¹⁴ These shares include 100 American Depository Shares (the equivalent of 200 Aviva ordinary shares). The opening balance figure for Lord Sharman differs from the closing balance figure at 31 December 2011 due to scrip dividend shares issued in November 2011 not being included in the closing balance figure at 31 December 2011.
- ¹⁵ These LTIP awards include 433,296 phantom units which will be cash settled on vesting and for which no shares will be transferred or allotted.
- ¹⁶ The opening balance figure for Leslie Van de Walle differs from the closing balance figure at 31 December 2011 due to scrip dividend shares issued in November 2011, to his spouse through a nominee account, not being included in the closing balance figure at 31 December 2011. In addition to his ordinary shareholding, Leslie Van de Walle held 897,000 5.9021% £500m Direct Capital Instrument (DCI) on 1 January 2012 and 2 May 2012. The DCIs were held by his spouse through a nominee account.
- ¹⁷ Igal Mayer's ABP awards vested on 1 June 2012, the first business day after his leaving the Company on 31 May 2012. Mr Mayer's 2010, 2011 and 2012 LTIP awards and 2010 OATTV award lapsed on his leaving the Company on 31 May 2012.
- ¹⁸ 25% of Andrew Moss' 2010 ABP award, and 100% of his 2011 and 2012 ABP awards and 2010 OATTV award lapsed on his leaving the Company on 31 May 2012. The remaining 75% of his 2010 ABP award will vest on the normal vesting date.

There were no changes to the current directors' interests in Aviva shares during the period 1 January 2013 to 5 March 2013.

Approval by the Board

This Directors' Remuneration Report was reviewed and approved by the Board on 6 March 2013.

Scott Wheway

Chairman, Remuneration Committee

Shareholder information

In this section

Company address	122
Share capital	122
Related party disclosures	124
Dividend data	124
Guarantees, securitised assets and off-balance sheet arrangements	125
Liquidity and capital resources	125
Regulation	129
Risks relating to our business	135

Shareholder information

Company address

The Company's registered office is St Helens, 1 Undershaft, London, EC3P 3DQ.
The Company's telephone number is +44 (0)20 7283 2000.

Share capital

The Company has four classes of shares:

- Ordinary Shares of £0.25 each which constitute equity security and hold voting rights;
- Cumulative Irredeemable Preference Shares of £1 each, which entitle holders to attend and vote at general meetings only when dividends on such shares are in arrears. Cumulative irredeemable preference shareholders may also attend general meetings and vote on particular proposals when such proposals relate to an alteration of the rights attaching to such shares, a reduction of capital (other than through a redemption or repurchase of shares) or a winding up of business. On a winding up, they carry a preferential right of return of capital ahead of the ordinary shares;
- Sterling New Preference Shares of £1 each, which have such rights and terms (including terms related to the redemption of shares, ranking and entitlement to dividend and capital) as the Board determines; and
- Euro New Preference Shares of €1 each, which have such rights and terms (including, terms related to the redemption of such shares, ranking and entitlement to dividend and capital) as the Board determines.

Issued share capital

The Company had an aggregate issued and outstanding ordinary share capital of £736 million as of 31 December 2012. The following table sets out information about the issued and outstanding classes of equity as of 31 December 2012.

Share class	Shares issued and outstanding			Shares covered by outstanding option		
	2012 Million	2011 Million	2010 Million	2012 Million	2011 Million	2010 Million
Ordinary Shares, nominal value 25p	2,946	2,905	2,820	25	30	27
8.375% Cumulative Irredeemable Preference Shares, nominal value £1	100	100	100	—	—	—
8.75% Cumulative Irredeemable Preference Shares, nominal value £1	100	100	100	—	—	—

The Companies Act 2006 abolished the requirement for a company to have an authorised share capital and the articles of association adopted by the Company on 28 April 2010 reflect this. Directors are still limited as to the number of shares they can allot, as the allotment authority continues to be required under the Act, save in respect of employee share schemes. Ordinary shares in issue in the Company rank *pari passu*. All the ordinary shares in issue carry the same right to receive all dividends and other distributions declared, made or paid by the Company.

The Company is not permitted under English law to hold its own ordinary shares. Whilst the Company is presently authorised to repurchase up to 290 million ordinary shares, any shares that are repurchased must be cancelled. Details of the Company's dividends are set out below under 'Dividend data'. The Company's preference shares rank, as to the payment of dividends and capital, as set out in note 32.

Share options and awards

The Company maintains a number of active stock option and share award schemes. Details of these schemes are set out in 'Financial statements IFRS – Note 30 – Group's share plans'.

Share Investment Plan

The Company's UK resident employees of participating companies can buy ordinary shares in the Company by making monthly contributions from their gross salary. Contributions can be a minimum of £5 and a maximum of £125 per month (or, if less, 10% of gross salary). Contributions are held in a trust by an independent trustee and shares are allocated within 30 days of the employee's monthly contribution date. Employees can withdraw their shares from the trust at any time on payment of income tax and National Insurance Contributions (NIC). However, after five years shares can be withdrawn from the trust free of income tax and NIC.

There is currently no matching element to this investment by the Company. However a matching element is due to be introduced in April 2013 through which the Company will match every purchased share with two matching shares for the first £40 of a participant's monthly contribution. Matching shares will be subject to forfeiture if purchased shares are withdrawn from the Aviva All Employee Share Ownership Plan (AESOP) within three years of purchase, as long as the employee remains employed by the Company. From May 2013 participants will also be eligible to receive Dividend Shares through the AESOP.

Shares to satisfy options and awards

Since July 2008, it has been the Company's practice to satisfy all awards and options using shares purchased in the market and held by employee trusts except where local regulations make it necessary to issue new shares.

At 31 December 2012, 10,053,515 shares were held by the employee share trusts as compared to 13,284,476 at 31 December 2011, in both instances following the share purchases and distributions to individual employees throughout the year. These shares have an aggregate nominal value of £2,513,379 and market value £37,499,611 as of 31 December 2012, compared to £3,321,119 and £39,959,704 at 31 December 2011, respectively. Shares held by separate employee share trusts on behalf of specific individuals have not been included in these amounts. Further details are given in 'Financial statements IFRS – Note 31 – Shares held by employee trusts.'

History of share capital

The following table sets out information about the history of the Company's ordinary shares over the last three full calendar years.

	Number of shares outstanding
At 1 January 2010	2,766,611,374
Shares issued under the Group's Employee and Executive Share Option Schemes ¹	722,968
Shares issued in lieu of dividends ²	52,814,300
At 31 December 2010	2,820,148,642
Shares issued under the Group's Employee and Executive Share Option Schemes ¹	1,574,706
Shares issued in lieu of dividends ²	83,989,590
At 31 December 2011	2,905,712,938
Shares issued under the Group's Employee and Executive Share Option Schemes ¹	3,335,566
Shares issued in lieu of dividends ²	36,923,757
At 31 December 2012	2,945,972,261

¹ For more information on our various option schemes, see note 30 in the financial statements.

² The issue of shares in lieu of cash dividends is considered a bonus issue under the terms of the Companies Act 2006 and the nominal value of the shares is charged to the share premium account.

The Companies Act 2006 abolished the requirement for a company to have an authorised share capital and the articles of association adopted by the Company on 28 April 2010 reflect this. Directors are still limited as to the number of shares they can at any time, allot as the allotment authority continues to be required in the Act save in respect of employee share schemes.

There were no changes to the voting rights of any class of shares during 2010, 2011 or 2012, other than issuances in connection with our various employee option schemes and under the Company's scrip dividend scheme. The Company did not issue shares for consideration other than cash during 2010, 2011 or 2012. In addition, at the Company's general meetings in 2010, 2011 and 2012, shareholders authorised the limited dis-application of Section 561 of the Companies Act 2006 to permit the Company to issue new equity securities for cash without applying shareholders' statutory pre-emptive rights.

Related party disclosures

Related party transactions

For more information relating to related party transactions, including more information about the transactions described below, please see 'Financial Statements IFRS – Note 59 – Related party transactions'.

Subsidiaries

Transactions between the Company and its subsidiaries are eliminated on consolidation.

Key management compensation

The total compensation to those employees classified as key management, being those having authority and responsibility for planning, directing and controlling the activities of the Group, including the executive and non-executive directors is as follows:

	2012 £m	2011 £m	2010 £m
Salary and other short-term benefits	4.7	6.7	8.1
Post-employment benefits	1.9	1.7	1.6
Equity compensation plans	4.8	5.9	6.4
Termination benefits	1.5	0.7	—
Other long term benefits	0.4	2.8	2.5
Total	13.3	17.8	18.6

Various directors and key management of Aviva may from time to time purchase insurance, asset management or annuity products, from Aviva Group companies in the ordinary course of business on substantially the same terms, including interest rates and security requirements, as those prevailing at the time for comparable transactions with other persons.

Apart from the disclosed transactions discussed above and in the 'Governance' section of this report, no director had an interest in shares, transactions or arrangements that requires disclosure under applicable rules and regulations.

Other related parties

The Group received income from and paid expenses to other related parties from transactions made in the normal course of business. Loans to other related parties are made on normal arm's length commercial terms.

Services provided to other related parties

	2012		2011		2010	
	Income earned in year £m	Receivable at year end £m	Income earned in year £m	Receivable at year end £m	Income earned in year £m	Receivable at year end £m
Associates	—	—	—	—	47	—
Joint ventures	23	103	23	125	18	375
Employee pension schemes	12	6	13	9	10	2
	35	109	36	134	75	377

In addition to the amounts disclosed for associates and joint ventures above, at 31 December 2012 amounts payable at year-end were £nil, and expenses incurred during the period were £5 million.

Transactions with joint ventures in the UK relate to the property management undertakings, the most material of which are listed in note 18(b). Our interest in these joint ventures comprises a mix of equity and loans, together with the provision of administration services and financial management to many of them. Our UK life insurance companies earn interest on loans advanced to these entities, movements in which may be found in note 18(a).

Our fund management companies also charge fees to these joint ventures for administration services and for arranging external finance.

Our UK fund management companies manage most of the assets held by the Group's main UK staff pension scheme, for

which they charge fees based on the level of funds under management. The main UK scheme holds investments in Group-managed funds and insurance policies with other Group companies, as explained in note 47(e)(iii).

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms. Details of guarantees, indemnities and warranties provided on behalf of related parties are given in note 51(g).

Loans to joint ventures

We make loans to our property management joint ventures to fund property developments which we undertake with our joint venture partners. Movements in these loans may be found in 'Financial Statements IFRS – Note 18 – Interests in, and loans to, joint ventures'. Total loans at 31 December 2012 and at the end of each of the last three financial years are shown in the table below:

	2012 £m	2011 £m	2010 £m
Loans to joint ventures	92	100	375

Dividend data

The Company has a policy to pay a progressive dividend with reference to growth in cash flows and earnings. Under UK company law, we may only pay dividends if the company has 'distributable profits' available. 'Distributable profits' are accumulated, realised profits not previously distributed or capitalised, less accumulated, unrealised losses not previously written off based on IFRS. Even if distributable profits are available, we pay dividends only if the amount of our net assets is not less than the aggregate of our called-up share capital and undistributable reserves and the payment of the dividend does not reduce the amount of our net assets to less than that aggregate.

As a holding company, the Company is dependent upon dividends and interest from our subsidiaries to pay cash dividends. Many of the Company's subsidiaries are subject to insurance regulations that restrict the amount of dividends that they can pay to us.

Historically, the Company has declared an interim and a final dividend for each year (with the final dividend being paid in the year following the year to which it relates). Subject to the restrictions set out above, the payment of interim dividends on ordinary shares is made at the discretion of our Board, whilst payment of any final dividend requires the approval of the Company's shareholders at a general meeting. Preference shares are irredeemable and dividends on preference shares are made at the discretion of our Board.

The Company pays cash dividends in pounds sterling, although the articles of association permit payment of dividends on ordinary shares in other currencies and in forms other than cash, such as ordinary shares. If dividends on ordinary shares held by the American Depositary Shares (ADS) depositary are paid in pounds sterling, the ADS depositary will convert the pounds sterling that it receives on behalf of the ADS holders into US dollars according to the prevailing market rate on the date that the ADS depositary actually receives the dividends.

For the 2007 final dividend and previous final and interim dividends, shareholders on record were provided with the opportunity to elect to receive dividends in the form of newly issued ordinary shares through the Aviva Scrip Dividend Scheme. For the 2008 interim dividend, the Aviva Scrip Dividend Scheme was replaced by a dividend reinvestment plan (DRIP). For those shareholders participating in the DRIP, the Company paid a cash dividend, which was then used to buy existing shares on the open market. For the 2008 final dividend, Aviva withdrew the DRIP and

reintroduced the Aviva Scrip Dividend Scheme. For the 2012 final dividend, the Aviva Scrip Dividend Scheme has been withdrawn.

An interim dividend is generally paid in November of each year. A final dividend is proposed by the Company's Board after the end of the relevant year and generally paid in May. The following table shows certain information regarding the dividends that we paid on ordinary shares for the periods indicated in pounds sterling and converted into US dollars at the noon buying rate in effect on each payment date.

Year	Interim dividend per share (pence)	Interim dividend per share (cents)	Final dividend per share (pence)	Final dividend per share (cents)
2007	11.90	24.37	21.10	41.31
2008	13.09	19.69	19.91	30.31
2009	9.00	14.75	15.00	23.55
2010	9.50	15.20	16.00	25.80
2011	10.00	15.70	16.00	25.27
2012	10.00	15.85	9.00	na

Guarantees, securitised assets and off-balance sheet arrangements

As a normal part of our operating activities, various Group companies have given financial guarantees and options, including interest rate guarantees, in respect of certain long-term assurance and fund management products, as set out in Note 41. These are accounted for on-balance sheet as either part of the host insurance contract or as financial instruments under IFRS.

Information on operating lease commitments can be found in Note 52(b).

It is standard business practice for our Group companies to give guarantees, indemnities and warranties in connection with disposals of subsidiaries and associates to third parties. As of 31 December 2012, we believe no material loss will arise in respect of these guarantees, indemnities and warranties. Principal warranties include the accuracy and completeness of the statement of financial position at an agreed specified date, details of outstanding litigation, regulatory matters, material contractual commitments, the position on tax filings and other customary matters together with any specific items identified during due diligence. In addition, specific clauses cover such items as regulatory approvals and licences, the basis of calculation regarding actuarial insurance liabilities, reinsurance contracts and the status of employee pension plans. Their exact terms are tailored to each disposal and are set out in the respective sale and purchase agreement. Similarly, the open warranty periods, within which the purchaser could claim, and limits on the maximum amount potentially recoverable will vary for each item covered in each disposal.

There are a number of outstanding claims on recent disposals, none of which are material. There are also open claim periods on other recent disposals on which we have neither received, nor expect to receive, any such claims. We believe that there is no material exposure in this respect.

We have loans receivable, secured by mortgages, which have then been securitised through non-recourse borrowings by special purpose entities in our UK Life business, as set out in Note 24. These special purpose entities have been consolidated and included in the statement of financial position, as we retain the residual interest in them.

Limited liability partnerships classified as joint ventures

As part of their investment strategy, the UK and certain European long-term business policyholder funds have invested in a number of property limited partnerships (PLP), either directly or via property unit trusts (PUT), through a mix of capital and loans. The PLPs are managed by general partners (GP), in which the long-term business shareholder companies hold equity stakes and which themselves hold nominal stakes in the PLPs. The PUTs are managed by a Group subsidiary.

Accounting for the PUTs and PLPs as subsidiaries, joint ventures or other financial investments depends on the shareholdings in the GPs and the terms of each partnership agreement. If a partnership is managed by a contractual agreement where the parties have joint control but no individual party exerts overall control, notwithstanding that the Group's partnership share or economic interest in the PLP (including its indirect stake via the relevant PUT and GP) may be greater than 50%, such PUTs and PLPs have been classified as joint ventures. Of the PLPs accounted for as joint ventures at 31 December 2012, the Group's economic interest exceeded 50% in respect of one partnership, The Mall Limited Partnership, in which the Group had a 50.52% economic interest.

Note 18 provides a list of the principal PLPs accounted for as joint ventures, as well as summarised information on the income, expenses, assets and liabilities of the Group's interests in its joint ventures in aggregate. In respect of these PLPs, there are no significant contingent liabilities to which we are exposed, nor do we have any significant contingent liabilities in relation to our interests in them. External debt raised by the PLPs is secured on their respective property portfolios, and the lenders are only entitled to obtain payment of both interest and principal to the extent there are sufficient resources in the respective PLPs. The lenders have no recourse whatsoever to the policyholder and shareholders' funds of any companies in the Aviva Group. At 31 December 2012, we had £157 million capital commitments to these PLP joint ventures.

Liquidity and capital resources

Treasury function

The treasury function of our business is managed by our centralised treasury team, headed by the Group treasurer. The Group treasurer acts as owner of Group business standards for liquidity and foreign exchange risk management within the Group risk governance and oversight framework. Changes in policy require the agreement of the chief risk and capital officer. These policies are independently implemented and monitored by each of our businesses. Our central treasury team is split into distinct functions: a Group team, which develops our overall treasury strategy and our treasury team at Aviva Investors, which manages and monitors our treasury and cash flow positions for our holding companies. Each business unit is responsible for monitoring its own cash and liquidity positions, as well as its ongoing funding requirements. It is our policy to make the majority of our financing arrangements at the parent company level for our business units, primarily through external borrowings and equity offerings. This enables us to achieve the efficiencies afforded by our collective size. A number of our business units also raise debt on their own behalf.

Our principal objective in managing our liquidity and capital resources is to maximise the return on capital to shareholders, while enabling us to pay dividends, service our debt and our holding companies' cash flows. In the context of a financial services company where our working capital is largely representative of our liquidity, we believe that our working capital is sufficient for our present operational requirements. For additional information, see 'Note 56 – Risk management – liquidity risk'.

Extraordinary market conditions

Starting in mid-September 2008, the global financial markets experienced unprecedented disruption, adversely affecting the business environment in general, as well as financial services companies in particular. Markets have improved but continue to be fragile, particularly given the Eurozone sovereign debt crisis. A return to adverse financial market conditions could significantly affect our ability to meet liquidity needs and obtain capital, although management believes that we have liquidity and capital resources to meet business requirements under current market conditions.

At 31 December 2012, total consolidated cash and cash equivalents net of bank overdrafts amounted to £23,248 million, an increase of £847 million over £22,401 million in 2011.

Processes for monitoring and managing liquidity risk, including liquidity stress models, have been enhanced to take into account the extraordinary market conditions, including the impact on policyholder and counterparty behaviour, the ability to sell various investment assets and the ability to raise incremental funding from various sources. Management has taken steps to strengthen liquidity in light of its assessment of the impact of market conditions, such as issuing \$650 million Fixed Rate Tier 1 notes in May 2012, and intends to continue to monitor liquidity closely.

Management of capital resources

We seek to maintain an efficient capital structure using a combination of equity shareholders' funds, preference capital, subordinated debt and borrowings. This structure is consistent with our risk profile and the regulatory and market requirements of our business.

In managing our capital, we seek to:

- Match the profile of our assets and liabilities, taking into account the risks inherent in each business;
- maintain financial strength to support new business growth whilst still satisfying the requirements of policyholders, regulators and rating agencies;
- retain financial flexibility by maintaining strong liquidity, access to a range of capital markets and significant unutilised committed credit lines;
- allocate capital efficiently to support growth and repatriate excess capital where appropriate; and
- manage exposures to movements in exchange rates by aligning the deployment of capital by currency with our capital requirements by currency.

We are subject to a number of regulatory capital tests and employ realistic scenario tests to allocate capital and manage risk. The impact of these regulatory capital tests on our ability to transfer capital around the Group through dividends and capital injections is discussed later in this section under the headings 'Sources of liquidity' and 'Capital injections'.

At 31 December 2012, the Group had £21.4 billion (31 December 2011: £20.8 billion) of total capital employed on an MCEV basis in our trading operations which is financed by a combination of equity shareholders' funds, preference capital, direct capital instruments, subordinated debt and internal and external borrowings.

In 2012, the total capital employed increased by £0.6 billion. The increase is primarily driven by the Group's post tax profits, offset by actuarial losses on staff pension schemes and the payment of the dividend.

In addition to external funding sources, we have a number of internal debt arrangements in place. These have allowed the assets supporting technical liabilities to be invested into the pool of central assets for use across the Group. They have also enabled us to deploy cash from some parts of the business to others in order to fund growth. Although intra-Group loans in nature, they are counted as part of the capital base for the purpose of capital management. All internal loans satisfy arm's length criteria and all interest payments have been made when due.

Management of debt

Aviva plc is the principal financing vehicle in our centralised funding strategy. Our senior debt obligations are supported by guarantees from our principal UK non-life trading subsidiaries. We also manage our external debt in line with rating agency limits applicable for entities with a rating in the AA range. We aim to maintain a balance of fixed and floating rate debt, and manage the maturity of our borrowings and our undrawn committed facilities to avoid bunching of maturities. We aim to maintain

access to a range of funding sources, including the banking market, the commercial paper market and the long-term debt capital markets. We issue debt in a variety of currencies, predominantly sterling, euros and US dollars, based on investor demand at the time of issuance and management of the Group's foreign exchange translation exposures in the statement of financial position.

In May 2012, we issued \$650 million of Fixed Rate Tier 1 notes callable in 2017. In June 2012, we repaid a \$300 million subordinated debt instrument at its first call date.

At 31 December 2012, our total external borrowings, including subordinated debt and securitised mortgage loans, amounted to £8.3 billion (2011: £8.5 billion). Of the total borrowings, £5.1 billion (2011: £5.3 billion) are considered to be core borrowings and are included within the Group's capital employed. The balance of £3.2 billion (2011: £3.2 billion) represents operational debt issued by operating subsidiaries. We also have substantial committed credit facilities available for our use. At 31 December 2012, we had undrawn committed credit facilities expiring within one year of £0.4 billion (2011: £1.0 billion) and £1.7 billion in credit facilities expiring after more than one year (2011: £1.1 billion). Of these facilities, £750 million was allocated in 2012 (2011: £750 million) to support our commercial paper programme.

Further information on the maturity profile, currency and interest rate structure of our borrowings is presented in 'Financial statements IFRS – Note 48 – Borrowings'. Commercial paper is issued for terms up to 12 months and is generally reissued at maturity. The earliest repayment date for other debt instruments is a €650 million subordinated debt instrument with a first call date of 2 October 2013 at the option of the company. At this time Aviva will have the option of repaying the debt or accepting a step-up in the coupon and deferring repayment until future coupon dates or 2023 at the latest.

The table below presents our debt position for the periods indicated:

	2012 £m	2011 £m
Core structural borrowings		
Subordinated debt	4,337	4,550
Debenture loans	199	199
Commercial paper	603	506
	5,139	5,255
Operating borrowings		
Operational borrowings at amortised cost	1,868	1,889
Operational borrowings at fair value	1,332	1,306
	3,200	3,195
	8,339	8,450
Less: Amounts classified as held for sale	(145)	—
Total	8,194	8,450

In the UK, we have raised non-recourse funding secured against books of mortgages. This funding has been raised through the use of special-purpose entities. The beneficial interest in the books of mortgages has been passed to these special-purpose entities. These entities, which are owned by independent trustees, have funded this transfer through the issue of loan notes.

The value of the secured assets and the corresponding non-recourse funding was £1,332 million (2011: £1,306 million). We continue to receive fees from these special purpose entities in respect of loan administration services.

These special purpose entities have been consolidated as we retain the residual interest in them. The transactions and reasons for consolidation are discussed further within 'Financial statements IFRS – Note 24 – Securitised mortgages and related assets'.

Undrawn borrowings

At 31 December 2012, we had £2.1 billion (2011: £2.1 billion) undrawn committed central borrowing facilities available to us, provided by a range of leading international banks, all of which have investment grade credit ratings. We have allocated £750 million to support the credit rating of Aviva's commercial paper programme. Undrawn borrowings are analysed below:

	2012 £m	2011 £m
Expiring within one year	420	955
Expiring beyond one year	1,725	1,160
Total	2,145	2,115

Our committed central borrowing facilities have two financial covenants:

- Borrowings (excluding non-recourse indebtedness) may not exceed total shareholders' funds. At 31 December 2012, borrowings were 62% of total shareholders funds.
- Total shareholders' funds to exceed 32% of non-life net written premiums for the previous 12 months. At 31 December 2012, total shareholders funds were 140% of non-life net written premiums.

Total shareholders' funds are defined as the aggregate of nominal share capital of Aviva and the IFRS retained profits and reserves, plus the value of in-force long-term business, on a consolidated basis.

Sources of liquidity

In managing our cash flow position, we have a number of sources of liquidity, including:

- dividends from operating subsidiaries;
- external debt issuance;
- internal debt and central assets; and
- funds generated by the sale of businesses.

Aviva plc's principal sources of liquidity is dividends and liquid resources provided by its subsidiaries, associates and joint ventures. The level of dividends is based on two primary factors: the financial performance and the local solvency and capital requirements of our individual business units.

The table below shows liquid resources provided to Group Centre from operating companies, subsidiaries, associates and joint ventures in 2012:

	2012 Amounts received £m
UK life insurance	150
UK general insurance	150
Canada	136
France	217
Spain	68
Poland	70
Other operations	153
Total	944

Subsequent to the year end, the Group has taken action to improve its access to dividends from the Group's insurance and asset management businesses by undertaking a corporate restructuring whereby Aviva Group Holdings ("AGH") has purchased from Aviva Insurance Limited ("AIL") its interest in the majority of its overseas businesses.

Under UK company law, dividends can only be paid if a company has distributable reserves sufficient to cover the dividend. At 31 December 2012, Aviva plc itself had distributable reserves of £3,037 million, which would have covered three years of historic dividend payments to our shareholders. In UK Life, our largest operating subsidiary, distributable reserves, which could be paid to Aviva plc via its intermediate holding company, are created mainly by the statutory long-term business profit transfer

to shareholders. While the UK insurance regulatory laws applicable to UK Life and our other UK subsidiaries impose no statutory restrictions on an insurer's ability to declare a dividend, the rules require maintenance of each insurance company's solvency margin, which might impact their ability to pay dividends to the parent company. Our other life and general insurance, and fund management subsidiaries' ability to pay dividends and make loans to the parent company is similarly restricted by local corporate or insurance laws and regulations. In all jurisdictions, when paying dividends, the relevant subsidiary must take into account its capital position and must set the level of dividend to maintain sufficient capital to meet minimum solvency requirements and any additional target capital expected by local regulators. These minimum solvency requirements, which are consolidated under the European Insurance Group Directive, are discussed later in this section under the heading 'Regulatory capital position'. We do not believe that the legal and regulatory restrictions constitute a material limitation on the ability of our businesses to meet their obligations or to pay dividends to the parent company, Aviva plc.

The Group has received and expects to receive proceeds on completion of the disposals as disclosed in 'Financial statements IFRS – Note 3 – Subsidiaries'.

Aviva plc has established two main programmes for the issuance of external debt by Aviva plc. For short-term senior debt issuance we have a £2 billion commercial paper programme which allows debt to be issued in a range of currencies. At 31 December 2012, the outstanding debt issued under this programme was £603 million (2011: £506 million excludes commercial paper issued by Delta Lloyd). More details of movements in debt can be found on page 126 in the 'Management of debt section'.

For longer term debt we have established a Euro Medium Term Note (EMTN) programme. This programme has documentation readily available to allow quick issuance of long-term debt with a variety of terms and conditions. Debt issued under this programme may be senior debt or regulatory qualifying debt and may have a fixed or floating interest rate. At 31 December 2012, the outstanding debt issued under this programme was £2,076 million (2011: £1,894 million).

Application of funds

We use funds to pay dividends to our shareholders, to service our debt and to pay our central Group cash flows.

In 2012, total cash paid by the Company as ordinary and preference dividends and coupon payments on direct capital instruments and Fixed Rate Tier 1 notes amounted to £720 million, compared with £506 million in 2011.

In 2012, our total interest costs on central borrowings were £317 million. This compared with £324 million of interest paid on central borrowings in 2011. Total corporate centre expenses in 2012 were £136 million compared with £138 million in 2011.

An additional application of our funds is the acquisition of businesses. In 2012, cash paid for the acquisition of subsidiaries, joint ventures and associates from continuing operations net of cash acquired amounted to £129 million, compared with cash paid of £114 million in 2011.

Capital injections

We make capital injections into our businesses where necessary to ensure that they meet their local solvency requirements and also to support development of their operations. Capital is provided either by equity or, where a local holding company is in place, may be via loans with the holding company subsequently injecting equity capital in the regulated operating company. Each capital injection is subject to central review and approval by the Board of the relevant holding company and needs to meet our required internal rates of return. To the extent that capital injections are provided or funded by regulated entities, then we have to consider the impact on regulatory capital of the capital injection.

Otherwise our ability to make capital injections into our businesses is not materially limited by applicable legal and regulatory restrictions. Total capital injections into the business units were £169 million and £296 million in 2012 and 2011 respectively.

Consolidated cash flows

The cash and cash equivalents consist of cash at banks and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value.

For the purposes of the cash flow statement, cash and cash equivalents also include bank overdrafts, which are included in payables and other financial liabilities on the balance sheet.

Year ended 31 December 2012

Net cash from operating activities

Total net cash from operating activities increased by £2,636 million to a £2,294 million inflow in 2012 (2011: £342 million outflow). The increase is primarily due to an increase in flows from the net purchase/sale of operating assets.

Net cash from investing activities

Net cash from investing activities decreased by £93 million to £15 million outflow (2011: £78 million inflow). The decrease is mainly a result of a decrease in cash inflows from disposal of subsidiaries, joint ventures and associates, partly offset by lower cash used in discontinued operations.

Net cash out flow on financing activities

Net cash used in financing activities decreased by £654 million to an outflow of £1,119 million (2011: £1,773 million outflow). The decrease is due to proceeds from the issuance of a Fixed Rate Tier 1 notes, and lower cash used in discontinued operations partly offset by higher dividend payments.

Net cash and cash equivalents

At 31 December 2012, total consolidated net cash and cash equivalents, net of bank overdrafts, amounted to £23,248 million, an increase of £847 million over £22,401 million in 2011.

Currency

Our exposures to movements in exchange rates and the management of these exposures is detailed in 'Performance review – Financial and operating performance – Exchange rate fluctuations'.

Year ended 31 December 2011

Net cash from operating activities

Total net cash from operating activities decreased by £2,149 million to £342 million outflow in 2011 (2010: £1,807 million inflow). The decrease is primarily due to higher claims in the long-term business.

Net cash used in investing activities

Net cash from investing activities decreased by £271 million to £78 million utilised (2010: £349 million utilised). The decrease is a result of cash used in discontinued operations.

Net cash out flow on financing activities

Net cash used in financing activities was £420 million higher at £1,773 million (2010: £1,353 million). The increase is due to a higher repayment of borrowings during the year.

Net cash and cash equivalents

At 31 December 2011, total consolidated net cash and cash equivalents amounted to £22,401 million, an decrease of £2,294 million over £24,695 million in 2010.

Currency

Our exposures to movements in exchange rates and the management of these exposures is detailed in 'Performance review – Financial and operating performance – Exchange rate fluctuations'.

Regulatory capital position

Individual regulated subsidiaries measure and report solvency based on applicable local regulations, including in the UK the regulations established by the FSA. These measures are also consolidated under the European Insurance Groups Directive (IGD) to calculate regulatory capital adequacy at an aggregate group level, where we have a regulatory obligation to have a positive position at all times.

This measure represents the excess of the aggregate value of regulatory capital employed in our business over the aggregate minimum solvency requirements imposed by local regulators, excluding the surplus held in the UK and Ireland with-profit life funds. The minimum solvency requirement for our European businesses is based on the Solvency 1 Directive. In broad terms, for EU operations, this is set at 4% and 1% of non-linked and unit-linked life reserves respectively and for our general insurance portfolio of business is the higher of 18% of gross premiums or 26% of gross claims, in both cases adjusted to reflect the level of reinsurance recoveries. For our major non-European businesses (the US and Canada) a risk charge on assets and liabilities approach is used.

European Insurance Groups Directive

	UK Life funds £bn	Other business £bn	2012 £bn	2011 £bn
Insurance Groups Directive (IGD) capital resource	5.2	9.2	14.4	14.1
Less: capital resources requirement (CRR)	(5.2)	(5.4)	(10.6)	(11.9)
Insurance Groups Directive (IGD) excess solvency	—	3.8	3.8	2.2
Cover of EU minimum (calculated excluding UK Life funds)			1.7 times	1.3 times

The EU IGD regulatory capital solvency surplus has increased by £1.6 billion since 31 December 2011 to £3.8 billion. The key movements over the period are set out in the following table:

	£bn
IGD solvency surplus at 31 December 2011	2.2
Operating profits net of other income and expenses	0.9
Dividend and appropriations, net of shares issued in lieu of dividends	(0.7)
Market movements including foreign exchange ¹	1.3
Pension scheme funding	(0.2)
Movement in hybrid debt	0.2
UK reinsurance transactions	0.1
Increase in Capital Resources Requirement	(0.1)
Other regulatory adjustments	0.1
Estimated IGD solvency surplus at 31 December 2012	3.8

¹ Market movements include the impact of equity, credit spread, interest rate and foreign exchange movements net of the effect of hedging instruments.

Capital commitments

Contractual commitments for acquisitions or capital expenditures of investment property, property and equipment and intangible assets, which have not been recognised in our consolidated financial statements, are as follows:

	2012 £m	2011 £m	2010 £m
Investment property	6	23	63
Property and equipment	36	36	160
Total	42	59	223

Contractual obligations for future repairs and maintenance on investment properties are £nil (2011: £nil, 2010: £1 million). We have capital commitments to our joint ventures of £157 million

(2011: £258 million, 2010: £45 million) and to other investment vehicles of £nil (2011: £nil, 2010: £nil). These commitments are expected to be funded through operational cash flow without recourse to core structural borrowings.

Regulation

Compliance

In both our insurance and fund management businesses, matters may arise as a result of industry-wide issues, inspection visits or other regulatory activity, requiring discussion and resolution with industry regulators. The Group needs to ensure that procedures are in place to address any regulatory concerns, and that such procedures are properly planned, managed and resourced. Corrective action is undertaken, when necessary, with progress reported to relevant regulatory bodies in a timely manner.

Overview of regulation as it affects our business

Our principal insurance and fund management operations are in the UK, Europe, North America and the Asia Pacific region. We are therefore subject to financial services regulation and local regulatory supervision in all these areas, as individually covered below.

As the Group's parent company is based in the UK, both EU legislation and the rules of the FSA can impact Aviva's business practices worldwide. Regulators supervising the Group co-ordinate on a cross-border basis through a 'college'.

The European Union

In addition to its UK businesses, Aviva is active in other EU member states through wholly owned subsidiary and joint venture companies. These companies are subject to the laws and regulations of the EU member state in which they are based, but are also affected by higher level EU legislation, which will continue to have a significant influence on the legislative environment in the UK and other EU markets.

The EU operates by promulgating directives that must be implemented into local national legislation within each EU member country. These directives set minimum standards for national legislatures to meet, with each legislature able to decide how they should be implemented. National governments may not pass laws which fail to meet the minimum standards set out in a directive, but are generally free to impose legal requirements which go beyond those required. Directives are written at a fairly high level, with more detail being provided at national level through legislation developed in accordance with the local legal system. Even greater detail may be imposed through the rules and regulations of national regulators and, for financial services businesses these rules can be extensive.

The EU may also impose requirements directly on countries through regulation. EU financial services regulation is based on the principle of 'home country control', which makes the home country regulator responsible for monitoring compliance with all applicable regulation.

Key directives of particular relevance to the financial services industry, and so to Aviva's businesses in the EU include:

Third Life and Non-Life Directives

These directives implemented the home country control principle for life and non-life insurance business in the mid-1990s and placed the responsibility for such issues as solvency, actuarial reserves, investment of assets, and certain governance issues on the home country regulator. Most companies licensed to conduct insurance business in one member state may rely on their home country regulation to 'passport' into all other member states to conduct business without having to be separately licensed in each. The general exception is selling activity which continues to be regulated by the state in which the sale takes place.

Insurance Groups Directive (IGD)

The IGD requires member states to introduce the following measures to strengthen supervision of insurance companies which are part of a group:

- An adjustment margin to the solvency calculation in relation to participating interests in other insurance undertakings in order to eliminate 'double-gearing' (the use of the same regulatory capital in more than one entity of a group).
- An additional parent undertaking solvency margin calculation analogous to the adjusted margin test referred to above, to be applied at the level of the parent undertaking.
- The introduction of new solo supervision requirements, including rules as to internal control within the insurance undertaking regarding the production of information relevant to supplementary supervision, the exchange of information within the group and the supervision of intra-group transactions.
- Further provisions aimed at ensuring co-operation between competent regulatory authorities of member states.

Since 31 December 2006, the group capital resources requirement (the parent undertaking solvency calculation mentioned above) has been a 'hard' test (i.e. it constitutes a requirement to maintain the group capital resources, rather than simply to make the calculation) for UK-based companies operating under FSA rules.

Reinsurance Directive

Adopted on 16 November 2005, this directive requires that all reinsurance undertakings be authorised in their home member state. To obtain that authorisation, they need to meet strict requirements, but are then free to operate anywhere in the EU through the single market passport process.

Distance Marketing Directive

Under the Distance Marketing Directive, EU member states are required to implement a framework of rules and guidance in order to protect consumers by:

- setting minimum standards for information that must be provided to consumers before entering into a financial services contract by 'distance means'; and
- for certain products and services, giving a cooling-off period in which a consumer may cancel a contract without penalty.

Insurance Mediation Directive

This requires EU member states to establish a framework to:

- ensure that insurance and reinsurance intermediaries have been registered on the basis of a minimum set of professional and financial requirements;
- ensure that registered intermediaries will be able to operate in other member states by availing themselves of the freedom to provide services or by establishing a branch; and
- impose requirements on insurance intermediaries to provide specified minimum information to potential customers.

Markets in Financial Instruments Directive (MiFID)

MiFID, which superseded the earlier Investment Services Directive, builds on the home country control principle, extending the range of 'core' investment services and activities that may be passported from one member state to another, clarifying the allocation of responsibilities between home and host country jurisdictions, and introducing greater harmonisation governing the organisation and conduct of business of investment firms.

Solvency II

The agreed Solvency II Level 1 Directive was published in November 2009. Solvency II represents a fundamental change in European regulation and will result in a more sophisticated economic risk-based capital approach. Its objectives are to establish a solvency system that is better aligned to the true risks of insurers, and aims to enable supervisors to protect policyholder

interests as effectively as possible in accordance with common principles across the EU.

Since approval, the focus has been on developing the technical standards and requirements necessary to determine how the directive will be applied in practice, and expected amendments to the Solvency II Directive (Omnibus II Directive) following the creation of the new European Supervisory Authorities (ESAs) in September 2010. It is still not clear when these developments, including the implementation requirements will become legislation.

The European Insurance and Occupational Pensions Authority (EIOPA), replaced CEIOPS on 1 January 2011. A proposed amending directive was published in January 2011 ('Omnibus II Directive') to update Solvency II. Omnibus II set out powers for EIOPA to issue binding guidance/standards, changes to specific aspects of Solvency II and delays to the implementation of Solvency II. The details of Omnibus II are still being negotiated and it is not clear when Omnibus II will become legislation. Solvency II is currently set to apply to insurers from 1 January 2014. This date is expected to be changed in 2013.

EIOPA proposes to issue guidelines for supervisors in 2013 as interim measures to address the uncertainty caused by the ongoing delays to Solvency II and encourage harmonisation of supervisory approach across jurisdictions while Solvency I remains in force. These guidelines are expected to cover systems of governance, ORSA, internal model application procedures and reporting to supervisors. The FSA has proposed changes to its ICAS regime following the continuing delay. These changes will allow companies to use the work done in preparation for Solvency II for ICA.

This highlights the need for continued and engaged industry participation. Aviva continues to actively participate, through the key European industry working groups, who provide the voice of the industry, in ongoing discussions in Brussels.

Future EU developments

During 2013 the European Commission will be undertaking a review of the European System of Financial Supervision (ESFS). The ESFS includes the three sector specific European Supervisory Authorities (ESAs) that have powers to make binding rules and drive supervisory consistency and convergence through a single rule book.

There are a number of European dossiers that are expected to progress during 2013, including Packaged Retail Investment Products (PRIIPs) that will introduce common product disclosure standards and sales conduct rules, the review of the Insurance Mediation Directive (IMD) and the MiFID, the European Market Infrastructure Regulation (EMIR) that will introduce central clearing for standard Over the Counter (OTC) derivatives, the Directive for Institutions of Occupational Retirement Provisions (IORP) that sets rules for occupational pension schemes, and the Alternative Investment Fund Managers Directive (AIFMD) that will introduce a regime governing the marketing of alternative investments to EU investors.

United Kingdom

The Financial Services Authority

In the UK, the FSA is currently the single regulator for those individuals and firms conducting defined regulated activities in the financial services sector. The FSA has the authority to make rules and issue guidance, taking into account relevant EU directives, in relation to a wide sphere of activity encompassing the governance of the conduct of business by, and the prudential supervision of, individuals and firms authorised by the FSA to conduct such business ('Authorised Persons' or 'Authorised Firms').

Under the Financial Services and Markets Act 2000 (FSMA) no person may carry on, or purport to carry on, a regulated activity by way of business in the UK unless he is an Authorised Person or an exempt person. A firm granted permission by the FSA to carry on regulated activities becomes an Authorised Person for the

purposes of FSMA. 'Regulated activities' are prescribed in the FSMA (Regulated Activities) Order 2001 and include banking, insurance and investment business, stakeholder pension schemes, insurance mediation and certain mortgage mediation and lending activities.

Authorised Firms must at all times meet specified threshold conditions, including possession of adequate resources for the carrying on of their business, and being fit and proper to conduct that business, having regard to all the circumstances. Authorised Firms must also operate in accordance with the FSA's Principles for Business. These are 11 high level principles for conducting financial services business in the UK, including maintenance of adequate systems and controls, treating customers fairly, and communicating with customers in a manner that is clear, fair and not misleading.

The FSA regime is based on the principle that firms should have effective systems and controls, including robust risk management, which are appropriate to the size, complexity and diversity of their business.

It should be noted that during 2013 the FSA will be replaced by two separate regulatory bodies, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

The FSA's regulation of the Group

A number of the Group's UK subsidiaries are directly authorised and regulated by the FSA, including our insurance companies (e.g. the UK Life and UK General Insurance companies), asset managers (Aviva Investors) and intermediaries (UK Healthcare). Aviva plc, although not directly authorised by the FSA, does itself come within the scope of some regulation as the ultimate insurance holding company in the Group.

As Aviva is a UK-based group, the FSA has the responsibility of acting as lead regulator (i.e. the cross-sector supervisory co-ordinator) for the Group within the EU.

Approved persons and controllers

The FSA places great emphasis on the principle of senior management responsibility. The directors of, and senior managers carrying out FSA defined controlled function roles in, any of the Group's regulated entities are individually registered with the FSA under the 'Approved Person' regime, and can be held directly accountable to the FSA for control failings in those entities. A number of senior managers at Group level have also been registered as Approved Persons for the regulated subsidiaries, even though they are neither directors nor senior managers of these firms. This recognises that these managers exert significant influence over the regulated subsidiaries, because they are responsible for key parts of the Group's control framework on which the regulated subsidiaries place reliance.

The FSA regulates from a legal entity perspective, even though Aviva tends to operate by business unit. However, the FSA also expects that Aviva's regulated subsidiaries operate within an overall framework of Group governance and controls. Its rules expressly provide that any systems and controls which operate on a Group basis will be taken into account in determining the adequacy of a regulated subsidiary's systems and controls. The robustness of these Group controls is therefore subject to scrutiny and challenge by the FSA.

The FSA regulates the acquisition and increase of control over Authorised Firms. Under FSMA, any person proposing to acquire control of, or increase control over certain thresholds of, an Authorised Firm must first obtain the consent of the FSA. The Authorised Firm must also inform the FSA of any such proposed acquisition or increase. In considering whether to grant or withhold its approval of the acquisition or increase of control, the FSA must be satisfied both that the acquirer is a fit and proper person and that the interests of consumers would not be threatened by this acquisition or increase of control. Control over a UK Authorised Firm is acquired if the acquirer:

- holds 10% (or 20% if the Authorised Firm is an insurance intermediary) or more of the shares, or voting power, in that firm, or a parent undertaking of the firm; or
- is able to exercise significant influence over the management of the firm by virtue of the acquirer's shares or voting power in that company or a parent undertaking of the firm.

Increases in control require the consent of the FSA when they reach thresholds of 20%, 30% and 50% of the shares or voting power of the firm (or its parent).

In order to determine whether a person or a group of persons is a 'controller' for the purposes of FSMA, the holdings (shares or voting rights) of the person and any other person 'acting in concert', if any, are aggregated.

FSA conduct of business rules

The FSA's Conduct of Business (COB) and Insurance: Conduct of Business (ICOB) Rules apply to every Authorised Firm carrying on relevant regulated activities, and regulate the day-to-day conduct of business standards to be observed by all Authorised Persons in carrying out regulated activities.

The COB and ICOB Rules are principle based, and the scope and range of obligations imposed on an Authorised Firm will vary according to the scope of its business and range of the Authorised Firm's clients. Generally speaking, however, the obligations imposed on an Authorised Firm by the COB and ICOB Rules will include the need to classify its clients according to their level of sophistication, provide them with information about the Authorised Firm, meet certain standards of product disclosures (including fee and remuneration arrangements), ensure that promotional material which it produces is clear, fair and not misleading, assess suitability when advising on certain products, control the range and scope of advice given, manage conflicts of interest, report appropriately to its clients and provide certain protections in relation to client assets.

Capital and solvency rules for insurers

The FSA rules require that a UK insurer (including those within the Group) must hold capital resources equal to at least the Minimum Capital Requirement (MCR). Insurers with with-profits liabilities of more than £500 million (which is the case with Aviva's with-profits fund) must hold capital equal to the higher of MCR and the Enhanced Capital Requirement (ECR). The ECR is intended to provide a more risk responsive and 'realistic' measure of a with-profits insurer's capital requirements, whereas the MCR is broadly equivalent to the previous required minimum margin, and satisfies the minimum EU standards.

Determination of the ECR involves the comparison of two separate measurements of the Authorised Firm's financial resources requirements, which the FSA refers to as the 'twin peaks' approach. The two separate peaks are:

- the requirement comprised by the mathematical reserves plus the 'long term insurance capital requirement' (the LTICR), together known as the 'regulatory peak'; and
- a calculation of the 'realistic' present value of the insurer's expected future contractual liabilities together with projected 'fair' discretionary bonuses to policyholders, plus a risk capital margin, together known as the 'realistic peak'.

All insurers must also carry out an Individual Capital Assessment (ICA) to calculate the amount of capital needed to back their business. If the FSA decides that the final ICA amount is insufficient, it may draw up its own Individual Capital Guidance (ICG) for the firm, which can be imposed as a requirement on the scope of the Authorised Firm's permission.

Day-to-day supervision

The FSA takes a risk-based approach to its regulatory activity, concentrating its resources on those firms and activities which it

assesses pose the greatest potential threats to its four statutory objectives of:

- maintaining confidence in the UK financial system;
- contributing to the protection and enhancement of stability of the UK financial system;
- securing the appropriate degree of protection for consumers; and
- reducing the extent to which it is possible for a regulated business to be used for a purpose connected with financial crime.

Given our size and our share of the UK retail market, a major issue within our business which causes concern for the FSA may have a significant impact on these objectives.

The FSA therefore maintains a 'close and continuous' relationship with us, with day-to-day supervision of Aviva conducted by a dedicated team within its Prudential and Conduct Business Units. In practice, this means that a wide range of Group, regional and UK business unit senior managers have regular scheduled meetings with the FSA, and other meetings and discussions on specific issues take place as the need occurs. This adds up to weekly or even daily FSA interaction at UK region, business unit and Group level, and the sharing of detailed information about the Group.

The FSA has also, periodically, conducted formal Advanced Risk-Responsive Operating framework (ARROW) reviews of Aviva to assess the level of risk posed by the Group to each of the FSA's objectives. The last full risk assessment was conducted in 2011/2012.

Areas of potential risk or weakness where the FSA particularly requires Aviva to focus attention are formally set out in a Risk Mitigation Plan (RMP), with both risk assessment and RMP issues up-dated on an ongoing basis between each ARROW review.

The majority of RMP actions set by the FSA after the 2011/2012 ARROW review have been actioned by Aviva, and the remainder are being progressed in accordance with timescales agreed with the FSA.

The FSA has highlighted in its Business Plan 2012/2013 that its key focus areas for 2012/2013 would be:

- delivering the regulatory reform programme;
- continuing to influence the international and European policy agenda;
- delivering financial stability by maintaining ongoing supervision of firms in a period of continued fragility in markets including business model analysis, capital/liquidity assessments, recovery and resolution planning and the Significant Influence Function regime;
- delivering market confidence and credible deterrence; and
- delivering on the principal FSA initiatives to improve consumer protection – early product intervention, the Retail Distribution Review (RDR) and Mortgage Market Review (MMR).

Outside of the UK, each Aviva business is regulated by its own national regulator(s). However, overseas operations are also within the remit of the FSA to the extent that they have an interest in the systems and controls by which the Group manages its overseas businesses to mitigate the risk of financial shocks arising overseas flowing through to the UK.

The FSA monitors the strategy and performance of the Group's international businesses through its programme of regular meetings and thematic reviews.

The FSA aims to play a leading role in the development of both EU and international regulation. It is, in particular, in the vanguard of the movement towards risk-based insurance regulation.

The FSA continues to place weight on the 'Treating Customers Fairly' principle.

Intervention and enforcement

The FSA has extensive powers to investigate and intervene in the affairs of Authorised Firms and is obliged to monitor compliance with the requirements imposed by, and to enforce the provisions of, FSMA related to secondary legislation and the rules made thereunder.

The FSA's enforcement powers, which may be exercised against both Authorised Firms and Approved Persons, include public censure, imposition of unlimited fines and, in serious cases, the variation or revocation of permission to carry on regulated activities or of an Approved Person's status. The FSA may also vary or revoke an Authorised Firm's permissions to protect the interests of consumers or potential consumers if the Authorised Firm has not engaged in regulated activity for 12 months, or if it is failing to meet the threshold conditions for authorisation. The FSA has further powers to obtain injunctions against Authorised Persons and to impose or seek restitution orders where consumers have suffered loss.

In addition to applying sanctions for market abuse, the FSA has the power to prosecute criminal offences arising under FSMA and insider dealing under Part V of the Criminal Justice Act 1993, and breaches of money laundering regulations. The FSA's stated policy is to pursue criminal prosecution in all appropriate cases.

The Financial Services Compensation Scheme (FSCS)

The FSCS is intended to compensate individuals and small businesses for claims against an Authorised Firm where the Authorised Firm is unable or unlikely to be able to meet those claims (generally, when it is insolvent or has gone out of business).

The FSCS funding system, for the purposes of meeting FSCS compensation costs, has been reviewed to take into account the replacement of the FSA by the PRA and the FCA in 2013. Following this review the FSCS levy is to split into eight broad classes:

- the deposits class;
- the life and pensions provision class;
- the general insurance provision class;
- the investment provision class;
- the life and pensions intermediation class;
- the home finance intermediation class;
- the investment intermediation class; and
- the general insurance intermediation class.

The permissions held by each firm determine into which class, or classes, it falls.

Restrictions on business

FSA rules restrict an insurance company from carrying on any commercial business other than insurance business and activities directly arising from that business. Therefore, the FSA authorised insurance companies in the Group are bound by this restriction.

Long-term assets and liabilities

Where a UK insurer carries on life insurance business, its long-term business assets and liabilities – i.e. those assets and liabilities relating to life and health insurance policies – must be segregated from the assets and liabilities attributable to non-life insurance business or to shareholders. Separate accounting and other records must be maintained and a separate fund established to hold all receipts of long-term business.

The extent to which long-term fund assets may be used for purposes other than long-term business is restricted by the FSA rules. Only the 'established surplus', which is the excess of assets over liabilities in the long-term fund as determined by actuarial investigation, may be transferred so as to be available for other purposes. Restrictions also apply to the payment of dividends by the insurance company, as described below. FSA rules also require insurers to maintain sufficient assets in the separate long-term

insurance fund to cover the actuarially determined value of the insurance liabilities.

Distribution of profits and with-profits business

For UK authorised life insurers carrying on with-profits business, such as Aviva Life and Pensions UK Ltd ('AVLAP'), the FSA's rules require that where a firm decides to make a distribution of surplus from the with-profits fund it must distribute at least the required percentage (as defined in the FSA Handbook) of the total amount distributed to policyholders, with the balance of the total amount to be distributed being payable to the shareholders.

In addition, at least once a year the AVLAP Board must consider whether a distribution is required to be made from the Old WPSF inherited estate. Such a distribution will ordinarily be required if the level of the inherited estate of the OWPSF exceeds the Required Distribution Threshold as described in the Reattribution Scheme of Transfer effective from 1 October 2009 ('The Scheme') on any such annual investigation from the third such investigation after 1 October 2009. Annual investigation may also be carried out to determine if a Release to shareholders can be made from the RIEESA. Releases can only be made:

- if the Reattributed Inherited Estate exceeds the Permitted Release Threshold as defined in the Scheme;
- the AVLAP Board (based on appropriate actuarial advice including that of the With-Profits Actuary) are of the opinion that the Release will not give rise to a significant risk that the New WPSF (including the RIEESA) would be unable to meet its obligations to policyholders and its capital requirements or the Old WPSF would be unable to meet its obligations to policyholders; and
- following the sixth annual investigation after 1 October 2009 or later investigation and provided that investigation and investigations made in the previous 2 years determined that the Reattributed Inherited Estate exceeded the Permitted Release Threshold.

Reporting requirements

FSA rules require insurance companies to file their audited annual accounts, statements of financial position and life insurers' annual reports from the actuary performing the actuarial function with the regulator. There is also a requirement to report the annual solvency position of the insurance company's ultimate parent.

The FSA uses the annual return to monitor the solvency (i.e. the ability to meet current and future obligations such as claims payments to policyholders) of the insurance company. For general insurance business, the return is also used to assess retrospectively the adequacy of the company's claims provisions. The directors of an insurance company are required to sign a certificate, which includes a statement as to whether the company has maintained the required minimum margin of solvency throughout the year. The directors must also certify that the company has completed its return to the FSA properly in accordance with the FSA's instructions, and that the directors are satisfied that the company has complied in all material respects with the requirements set out in the FSA rules.

UK winding up rules

The general insolvency laws and regulations applicable to UK companies are modified in certain respects in relation to UK insurance companies where direct insurance claims will have priority over the claims of other unsecured creditors (with the exception of preferred creditors), including reinsurance creditors, on a winding up by the court or a creditors' voluntary winding up of the insurance company. Furthermore, instead of making a winding-up order when an insurance company has been proved unable to pay its debts, a UK court may reduce the amount of one or more of the insurance company's contracts on terms and subject to conditions (if any) which the court considers fit. Where an insurance company is in financial difficulties but not in

liquidation, the FSCS may take measures to secure the transfer of all or part of the business to another insurance company.

FSMA provides further protection to policyholders of insurance companies effecting or carrying out contracts of long-term insurance. Unless the court orders otherwise, a liquidator and/or administrator must carry on the insurer's business so far as it consists of carrying out the insurer's contracts of long-term insurance with a view to it being transferred as a going concern to a person who may lawfully carry out those contracts. In carrying on the business, the liquidator/administrator may agree to the variation of any contracts of insurance in existence when the winding-up order is made, but must not effect any new contracts of insurance.

United States

During 2012 we wrote life and annuity business in the United States through Aviva USA Corporation (Aviva USA), a wholly owned subsidiary formed by the merger of Aviva Life Insurance Company of America with AmerUS which it acquired in July 2006. Aviva USA is domiciled in Iowa and is the holding company for Aviva Life and Annuity Company which is licensed to conduct business in all states except New York and Washington D.C. In New York it operates a wholly owned subsidiary, Aviva Life Insurance Company of New York. Aviva plc reached agreement, in December 2012, to sell Aviva USA and, subject to regulatory approval, the sale is expected to close during 2013.

The US insurance industry is regulated primarily on a state-by-state basis. Individual states have authority to pass statutes, adopt regulation or issue directives to regulate insurance activities within their jurisdiction.

Consequently, life insurance companies are subject to regulation both in their domicile state as well as in each state in which they operate. State regulation can vary from state to state. All have laws and regulations covering the financial aspects of the insurance business, including standards of solvency, reserves, reinsurance and capital adequacy. In addition, most states have specific regulation governing licensing and the conduct of selling agents as well as the approval of products and associated product forms and literature.

Federal initiatives

While the National Association of Insurance Commissioners ('NAIC') has no statutory powers, its members are the insurance commissioners in each state and it acts as a forum to develop and propose model laws and regulations. Each state then decides whether to adopt the NAIC model laws or regulations and each state may make changes to the model laws during the adoption process. However, the models are generally widely adopted; an example being the 'Suitability in Annuity Transactions Model Regulation'.

NAIC has a commitment to modernising the state-based system of insurance regulation and is pushing forward an action plan aimed at achieving consistency of approach between states on a number of issues including risk management and the solvency regulatory framework. The American Council of Life Insurers ('ACLI') has, in the past, proposed an optional federal charter ('OFC') under which life insurers could choose to be federally regulated instead of state regulated. However, the OFC has not been adopted.

In 2010, Congress passed a law adopting significant federal regulatory reforms for the financial services industry in the US. The new law will impose stricter prudential standards on systemically significant financial companies, higher risk financial activities and introduce new mechanisms for resolving failures of significant financial companies. The law requires additional stress testing and reporting on a regular basis. In addition, a Federal Insurance Office ('FIO') has been established within the Treasury Department to monitor the insurance industry, co-ordinate federal policy and, along with the US Trade Representative, enter into international agreements on prudential insurance matters.

While the FIO will have no direct regulatory authority over the business of insurance, such international agreements could preempt inconsistent state insurance laws. The FIO is also required, among other things, to conduct a study of how to improve and modernise insurance regulation and to report to Congress. The new law does not currently have any immediate and significant impact on the Company and the FIO is still in the process of drafting its required report. We will continue to monitor the FIO and its activities.

Additionally, there is active discussion within the NAIC of moving to a principles-based valuation system for the setting of reserves and capital for life insurance companies. This could change our statutory reserve and capital requirements significantly and it is not possible to estimate the impact on our financial condition and results of operation at this time.

Risk-based capital

The NAIC has developed risk-based capital standards for life insurance companies as well as a model act for state legislatures to enact. The model act requires that life insurance companies report on a formula-based, risk-based capital standard that they calculate by applying factors to various asset, premium and reserve items. The formula takes into account the risk characteristics of a company, including asset risk, insurance risk, interest rate risk and business risk. The NAIC designed the formula as an early-warning tool to identify potentially inadequately capitalised companies for the purposes of initiating regulatory action. The model act imposes broad confidentiality requirements on those engaged in the insurance business (including insurers, agents, brokers and others) and on state insurance departments as to the use and publication of risk-based capital data.

Any state adopting the model act gives the state insurance commissioner explicit regulatory authority to require various actions by, or take various actions against, insurance companies whose adjusted capital does not meet minimum risk-based capital standards. The Iowa Insurance Commissioner takes into account the NAIC's risk-based capital standards to determine adequate compliance with Iowa insurance law.

Effective 31 December 2005, the NAIC implemented new requirements, referred to as C-3 Phase II, for calculating risk-based capital in connection with variable annuity products with death and living benefit guarantees. These changes did not have a material effect on our US operations, and at 31 December 2012, the Company's total adjusted capital under the NAIC's definition substantially exceeded Iowa standards.

Canada

We write property and casualty business in Canada via a number of wholly owned companies.

Insurance business in Canada is regulated federally by the Office of the Superintendent of Financial Institutions (OSFI) for prudential supervision (i.e. capital adequacy, solvency, etc). OSFI derives its powers from the federal Insurance Companies Act (Canada) which governs the structure and operation of federally incorporated insurance companies.

The capital adequacy of insurance companies is monitored under the Minimum Capital Test ('MCT'), a risk-based framework allowing for capital to be assessed on the basis of an individual company's risk profile taking account of the investments held and insurance business being written. Companies have their own internal MCT target that is communicated to OSFI, which is set to ensure that they maintain capital in excess of 150% of the OSFI minimum requirement.

There are also ten individual provincial regulators each regulating predominantly conduct of business issues such as policy terms and conditions, and rates and underwriting of companies they have licensed to write business in the province.

Asia

We operate in Asia through a network of subsidiary companies either wholly owned or established as a joint venture with a local partner. Our business is predominantly long-term and savings business, with small general insurance and health operations.

There are wholly owned businesses in Singapore and Hong Kong. During 2012 Aviva also operated businesses in China, India, Malaysia, Sri Lanka, Taiwan, Korea, Indonesia and Vietnam which, depending on the nature and extent of the control exerted by Aviva, were accounted for as subsidiaries, joint ventures or associates. Aviva plc reached agreement in 2012 to sell its business in Sri Lanka, and in January 2013 also reached agreement to sell its business in Malaysia, subject to regulatory approval.

The Asia area is made up of a number of widely differing and independent markets. The markets tend to be at different stages in their development but each has its own regulatory structures and Aviva complies with the local regulation in each of the countries in which it operates.

Industry regulation typically focuses on financial stability, i.e. minimum capital and the basis for calculating solvency, reserves and policyholder liability. In many of the markets regulators have the power to revoke operating licences, regulate shareholder structures and the participation in and the payment of dividends. Asia markets are moving quickly to modernise insurance regulation with an increasing focus on governance and conduct of business.

Intellectual property

Our primary brands (the Aviva name and Logo) are registered trademarks in the UK and are registered or pending in all other countries where Aviva has operations.

Aviva has an active programme of review of marks and watching for infringements. There are no material infringements in the UK known to us as at the date of this report, either by the Group or third parties.

Risks relating to our business

You should carefully review the following risk factors together with other information contained in this Annual Report before making an investment decision relating to our ordinary shares or ADSs. Our business, financial position, results of our operations and cash flow could be materially affected by any of these risks, the trading price of our ordinary shares or ADSs could decline due to any of these risks and investors may lose part or all of their investment.

Ongoing difficult conditions in the global financial markets and the economy generally may adversely affect our business and results of operations, and these conditions may continue.

Our results of operations are materially affected by uncertainty in the worldwide financial markets and macro-economic conditions generally. A wide variety of factors, including concerns over slowing growth, high sovereign debt within, and to a lesser degree outside, the Eurozone, the stability and solvency of financial institutions, longer-term low interest rates in developed markets, inflationary threats as well as geopolitical issues in the Middle East and North Africa, have contributed to increased volatility in the financial markets and diminished expectations for the global economy going forward. Global fixed income markets continue to experience periods of both volatility and limited market liquidity, which have affected a broad range of asset classes and sectors.

Factors relating to general economic conditions, such as consumer spending, business investment, government spending, the volatility and strength of both debt and equity markets, and inflation, all affect the profitability of our business. In a sustained economic phase of low growth and high public debt, characterised by higher unemployment, lower household income, lower corporate earnings, lower business investment and lower consumer spending, the demand for our financial and insurance products could be adversely affected. In addition, we may experience an elevated incidence of claims or surrenders of policies. Any potential material adverse affect will also be dependent upon customer behaviour and confidence.

As a global business, we are exposed to various local political, regulatory and economic conditions, business risks and challenges which may affect the demand for our products and services, the value of our investment portfolios and the credit quality of local counterparties.

We offer our products and services in Europe (including the UK), North America and the Asia Pacific region through wholly owned and majority-owned subsidiaries, joint ventures, companies in which we hold non-controlling equity stakes, agents and independent contractors. Our international operations expose us to different local political, regulatory, business and financial risks and challenges which may affect the demand for our products and services, the value of our investment portfolio, the required levels of capital and surplus, and the credit quality of local counterparties. These risks include, for example, political, social or economic instability in countries in which we operate, discriminatory regulation, credit risks of our counterparties, lack of local business experience in certain markets, risks associated with exposure to insurance industry insolvencies through policyholder guarantee funds or similar mechanisms set up in markets in which we are present and, in certain cases, risks associated with the potential incompatibility with foreign partners, especially in

countries in which we are conducting business through entities we do not control. Some of our international insurance operations are, and are likely to continue to be, in emerging markets where these risks are heightened. Our overall success as a global business depends, in part, upon our ability to succeed in different economic, social, regulatory and political conditions.

Credit risks relating to Aviva's business

Market developments and government actions regarding the sovereign debt crisis in Europe, particularly in Greece, Ireland, Italy, Portugal and Spain, could have a material adverse effect on our results of operations, financial condition and liquidity.

The continued uncertainty over the outcome of various EU and international financial support programs and the possibility that other EU member states may experience similar financial pressures could further disrupt global markets. In particular, this crisis has disrupted and could further disrupt equity and fixed income markets and result in volatile bond yields on the sovereign debt of EU members.

The issues arising out of the current sovereign debt crisis may transcend Europe, cause investors to lose confidence in the safety and soundness of European financial institutions and the stability of European member economies, and likewise affect UK and US-based financial institutions, the stability of the global financial markets and any economic recovery. The Group holds investments in UK and non-UK securities. See 'Performance Review – Analysis of Investments' for more information.

If an EU member state were to default on its obligations or seek to leave the Eurozone, or if the Eurozone were broken up entirely, the impact on the financial and currency markets would be significant and could impact materially all financial institutions, including the Group. Such events could adversely affect our business and results of operations, financial condition and liquidity.

Credit spread volatility may adversely affect the net unrealised value of the investment portfolio and our results of operations.

Our exposure to credit spreads primarily relates to market price variability associated with changes in credit spreads in our investment portfolio, which is largely held to maturity. Credit spread moves may be caused by changes in the perception of the credit worthiness of the issuer, or from market factors such as the markets risk appetite and liquidity. A widening of credit spreads will generally reduce the value of fixed income securities we hold. Conversely, credit spread tightening will generally increase the value of fixed income securities we hold. It can be difficult to value certain of our securities if trading becomes less liquid. Accordingly, valuations of investments may include assumptions or estimates that may have significant period to period changes that could have a material adverse effect on our consolidated results of operations or financial condition. Downturns in the net unrealised value of our investment portfolio may also have a material adverse effect on our regulatory capital surplus based on the EU Insurance Groups Directive. Although our financial statements reflect the market value of assets, our priority remains the management of assets and liabilities over the longer term.

Losses due to defaults by counterparties, including potential sovereign debt defaults or restructurings, could adversely affect the value of our investments and reduce our profitability and shareholders' equity.

We choose to take and manage credit risk through our investment assets partly to increase returns to policy holders whose policies the assets back, and partly to optimise the return for shareholders.

We have a significant exposure to third parties that owe us money, securities or other assets who may not perform under their payment obligations. These parties include private sector and government (or government-backed) issuers whose debt securities we hold in our investment portfolios (including mortgage-backed, asset-backed, government bonds and other types of securities), borrowers under residential and commercial mortgages and other loans, re-insurers to which we have ceded insurance risks, customers, trading counterparties, and counterparties under swap and other derivative contracts. We also execute transactions with other counterparties in the financial services industry, including brokers and dealers, commercial and investment banks, hedge funds and other investment funds, insurance groups and institutions. Many of these transactions expose us to credit risk in the event of default of our counterparty.

In addition, with respect to secured transactions, our credit risk may be increased when the collateral held by us cannot be realised or is liquidated at prices insufficient to recover the full amount of the loan or other value due. Losses or impairments to the carrying value of these assets could materially and adversely affect our financial condition and results of operations.

We use reinsurance and hedging programs to hedge various risks, including certain guaranteed minimum benefits contained in many of our long-term insurance and fund management products. These programs cannot eliminate all of the risks and no assurance can be given as to the extent to which such programs will be effective in reducing such risks. Our obligations under our fund management and insurance products are not changed by our hedging activities and we are liable for our obligations even if our derivative counterparties do not pay us. Defaults by such counterparties could have a material adverse effect on our financial condition and results of operations.

We are also susceptible to an adverse financial outcome from a change in third-party credit standing. As well as having a potential impact on spreads, rating movements can trigger solvency and accounting impacts.

For additional information about our investments, see 'Performance review – Analysis of investments'.

Market risks relating to Aviva's business

Changes in interest rates may cause policyholders to surrender their contracts, reduce the value of our investment portfolio and impact our asset and liability matching, which could adversely affect our results of operation and financial condition.

Our exposure to interest rate risk relates primarily to the market price and cash flow variability of assets and liabilities associated with changes in interest rates.

Some of our products, principally traditional participating products, universal life insurance and annuities, including fixed and equity indexed annuities, expose us to the risk that changes in interest rates will reduce our 'spread', or the difference between the amounts that we are required to pay under the contracts and the rate of return we are able to earn on investments intended to support obligations under the contracts. Our spread is a key component of our net income.

As interest rates decrease or remain at low levels, we may be forced to reinvest proceeds from investments that have matured or have been prepaid or sold at lower yields, reducing our investment return. Moreover, borrowers may prepay or redeem the fixed-income securities, commercial mortgages and mortgage-backed securities in our investment portfolio with greater frequency in order to borrow at lower market rates, which increases this risk. Lowering interest crediting or policyholder bonus rates can help offset decreases in investment margins on some products. However, our ability to lower these rates could be

limited by competition or contractually guaranteed minimum rates and may not match the timing or magnitude of changes in asset yields. As a result, our spread could decrease or potentially become negative. Our expectation for future spreads is an important component in the amortisation of policy acquisition costs and significantly lower spreads may cause us to accelerate amortisation, thereby reducing net income in the affected reporting period. In addition, during periods of declining interest rates, the guarantees within existing life insurance and annuity products may be more attractive to consumers, resulting in increased premium payments on products with flexible premium features, and a higher percentage of insurance policies remaining in force from year to year, during a period when our new investments carry lower returns. Accordingly, during periods of declining interest rates, our profitability may suffer as the result of a decrease in the spread between interest rates credited to policyholders and returns on our investment portfolio.

Increases in market interest rates could also negatively affect our profitability. Surrenders of life insurance policies and fixed annuity contracts may increase as policyholders seek higher returns and higher guaranteed minimum returns. Obtaining cash to satisfy these surrenders may require us to liquidate fixed maturity investments at a time when market prices for those assets are depressed which may result in realised investment losses. Regardless of whether we realise an investment loss, these cash payments would result in a decrease in total invested assets, and may decrease our net income. Premature withdrawals may also cause us to accelerate amortisation of policy acquisition costs, which would also reduce our net income.

Our mitigation efforts with respect to interest rate risk are primarily focused on maintaining an investment portfolio with diversified maturities that has a weighted average duration approximately equal to the duration of our estimated liability cash flow profile. However, it may not be possible to hold assets that will provide cash flows to exactly match those relating to policyholder liabilities, in particular in jurisdictions with less developed bond markets and in certain markets where regulated surrender value or maturity values are set with reference to the interest rate environment prevailing at the time of policy issue. This is due to the duration and uncertainty of the liability cash flows and the lack of sufficient assets of suitable duration. This results in a residual asset/liability mismatch risk that can be managed but not eliminated. In addition, our estimate of the liability cash flow profile may be inaccurate for other reasons, such as varying mortality or general insurance claims, and we may be forced to liquidate investments prior to maturity at a loss in order to cover the liability. Such a loss could have a material adverse effect on our results of operations and financial condition. See 'Financial statements IFRS – Note 56 – Risk management'.

Changes in short or long term inflation may cause policyholders to surrender their contracts, increase the size of our claims payments and expenses and reduce the value of our investments, which could adversely affect our results of operations and financial condition.

We are subject to inflation risk through our holdings of fixed interest and other investments and as a result of the potential for the cost of claims and expenses to rise faster than anticipated in our pricing or reserving. Changes in inflation could also affect the value perceived to be offered by our policies and so adversely affect persistency levels.

Falls in equity or property prices could have an adverse impact on our investment portfolio and impact our results of operations and shareholders' equity.

We are subject to equity and property price risk due to holdings of equities and investment properties in a variety of locations worldwide. Downturns in equity markets will depress equity prices and have a negative impact on our capital position in that unrealised losses in our net investment portfolio will increase, and our defined benefit pension scheme surplus/deficit will reduce/increase as the market value of scheme assets invested in equities decreases.

Downturns and volatility in equity markets can have a material adverse effect on the revenues and returns from our unit-linked, participating and fund management business. The unit-linked and fund management business depends on fees related primarily to the value of assets under management and would therefore be reduced by declines in equity and property markets. Profits could also be reduced as a result of current investors withdrawing funds or reducing their rates of ongoing investment with our fund management companies, or switching to lower risk funds generating lower income, or as a result of our fund management companies failing to attract funds from new investors. Similarly, bonuses credited to participating policyholders will reduce, following declines in equity and property markets and this will generally also lead to reductions in transfers to shareholders.

Downturns in equity markets may also have a material adverse effect on our regulatory capital surplus as measured under the EU Insurance Groups Directive. We provide certain guarantees within some of our products that protect policyholders against significant downturns in the equity markets. In volatile or declining equity market conditions, we may need to increase liabilities for future policy benefits and policyholder account balances, negatively affecting net income. For a discussion of guarantees we have given for our insurance and investment products, see 'Financial statements IFRS – Note 41 – Financial guarantees and options'.

In our US business in particular, market downturns and volatility may discourage purchases of accumulation products, such as equity-indexed annuities and equity-indexed life insurance, that have returns linked to the performance of the equity markets and may cause some of our existing customers to withdraw cash values or reduce investments in those products. A sustained weakness in the markets will decrease revenues and earnings in these types of products.

For property investment, we are subject to counterparty, valuation and liquidity risks. These investments may be adversely affected by weakness in property markets and increased mortgage delinquencies. We are also subject to property risk indirectly in our investments in residential mortgage-backed securities (RMBS) and commercial mortgage-backed securities (CMBS). There is the risk that the underlying collateral may fall in value causing the investment in securities to fall in value. The markets for these property investments and instruments can become illiquid, and issues relating to counterparty credit ratings and other factors may increase pricing and valuation uncertainties.

Fluctuations in currency exchange rates may adversely affect our results of operations and financial condition.

We operate internationally and are exposed to foreign currency exchange risk arising from fluctuations in exchange rates of various currencies. For the year ended 31 December 2012, over half of our premium income arises in currencies other than sterling, and our net assets are denominated in a variety of currencies, of which the largest are the euro, sterling and US dollar. In managing our foreign currency exposures, we do not hedge revenues as these are substantially retained locally to support the growth of the business and meet local regulatory and market requirements. Nevertheless, the effect of exchange rate fluctuations on local operating results could lead to significant fluctuations in our consolidated financial statements upon

translation of the results into sterling. Although we take certain actions to address this risk, foreign currency exchange rate fluctuation could materially adversely affect our reported results due to unhedged positions or the failure of hedges to effectively offset the impact of the foreign currency exchange rate fluctuation. Any adverse foreign currency exchange fluctuation may also have a material adverse effect on our regulatory capital surplus based on the EU Insurance Groups Directive.

For a discussion of the impact of changes in foreign exchange rates on our results of operations, see 'Financial statements IFRS – Note 56 – Risk management'.

Market fluctuations may cause the value of options and guarantees embedded in some of our life insurance products to exceed the value of the assets backing their reserves, which could adversely affect our results of operations or financial condition.

As a normal part of their operating activities, various Group companies have given guarantees and options, including interest rate and investment return guarantees, in respect of certain long-term insurance and fund management products. In providing these guarantees and options, our capital position is sensitive to fluctuations in financial variables, including foreign currency exchange rates, interest rates, property values and equity prices.

Interest rate guaranteed returns, such as those available on guaranteed annuity options (GAOs), are sensitive to interest rates falling below the guaranteed level. Other guarantees, such as maturity value guarantees and guarantees in relation to minimum rates of return, are sensitive to fluctuations in the investment return below the level assumed when the guarantee was made.

Periods of significant and sustained downturns in equity markets, increased equity or interest rate volatility or reduced interest rates could result in an increase in the valuation of the future policy benefit or policyholder account balance liabilities associated with such products, resulting in a reduction to net income. We use reinsurance in combination with derivative instruments to mitigate some of the liability exposure and the volatility of net income associated with these liabilities, and while we believe that these and other actions mitigate the risks related to these benefits, we remain liable for the guaranteed benefits in the event that reinsurers or derivative counterparties are unable or unwilling to pay, although this may be partially mitigated by the posting of collateral by our counterparties.

We are also subject to the risk that the cost of hedging these guaranteed minimum benefits increases, resulting in a reduction to net income. In addition, we are subject to the risk that unanticipated policyholder behaviour or mortality, combined with adverse market events, produces economic losses beyond the scope of the risk management techniques employed. These, individually or collectively, may have a material adverse effect on our results of operations, financial condition or liquidity.

The determination of the amount of allowances and impairments taken on our investments is highly subjective. If our business does not perform well, we may be required to recognise an impairment of our goodwill or intangibles with indefinite and finite useful lives, which could adversely affect our results of operations or financial condition.

The determination of the amount of allowances and impairments vary by investment type and is based upon our periodic evaluation and assessment of known risks associated with the respective asset class. Such evaluations and assessments are revised as conditions change and new information becomes available and additional impairments may need to be taken or allowances provided for in the future. If the carrying value of an investment is greater than the recoverable amount, the carrying value is reduced through a charge to the income statement in the period of impairment. There can be no assurance that management has

accurately assessed the level of impairments taken and allowances reflected in our financial statements.

Goodwill represents the excess of the amounts we paid to acquire subsidiaries and other businesses over the fair value of their net assets at the date of acquisition. We test goodwill and intangible assets with indefinite useful lives at least annually for impairment or when circumstances or events indicate there may be uncertainty over this value. We test intangibles with finite lives when circumstances or events indicate there may be uncertainty over this value. For impairment testing, goodwill and intangibles have been allocated to cash-generating units by geographical reporting unit and business segment.

The fair value of the reporting unit is impacted by the performance of the business. Goodwill, negative unallocated divisible surplus and indefinite life intangibles are written down for impairment where the recoverable amount is insufficient to support its carrying value. Such write downs could have a material adverse effect on our results of operations or financial condition.

Liquidity risks relating to Aviva's business

Adverse capital and credit market conditions may affect our ability to meet liquidity needs and to access capital which could adversely affect our results of operations or financial condition.

At a Group level, we need our subsidiaries to remit dividends to the Group to meet operating expenses, taxes, interest on our debt, dividends on our capital stock and repay maturing debt. Dividends from subsidiaries can become constrained by adverse business experience, regulatory actions etc which could have a material adverse effect on our business. At an operational level we also need liquidity to meet our liabilities. Without sufficient liquidity, we could be forced to curtail our operations and our business would suffer. The principal sources of our liquidity are insurance premiums, annuity considerations, deposit funds and cash flow from our investment portfolio and assets, consisting mainly of cash or assets that are readily convertible into cash. Sources of liquidity in normal markets also include a variety of short and long-term instruments, including repurchase agreements, commercial paper, medium and long-term debt, junior subordinated debt, securities, capital securities and stockholders' equity.

We hold certain investments that may lack liquidity such as privately placed fixed-maturity securities, and unlisted equities, and other investments where the inputs used for their valuation are not directly observable in the market. These asset classes represented approximately 5.3% of the total assets held at fair value as of 31 December 2012 (6.3% excluding assets held for sale). As has been the case across the industry, even some of our higher-quality assets have been more illiquid as a result of the recent challenging market conditions.

The reported value of our relatively illiquid types of investments, our investments in the asset classes described in the paragraph above and, at times, our higher-quality, generally liquid asset classes, do not necessarily reflect the lowest current market price for each asset. If we were forced to sell certain of our assets in the current market, there can be no certainty that we would be able to sell them for the prices at which we have recorded them and we may be forced to sell them at significantly lower prices.

We may need to seek additional financing in the event internal resources are not sufficient to meet our needs. The availability of additional financing would depend on a variety of factors such as market conditions, the general availability of credit, the overall availability of credit to the financial services industry and the market's perception of our financial condition. Disruptions and uncertainty or volatility in the capital and credit markets may exert downward pressure on availability of liquidity and credit capacity for certain issuers and may limit our access to capital required to operate and grow our business. Such market conditions may limit our ability to replace, in a timely manner,

maturing debt, satisfy statutory capital requirements and generate fee income and market-related revenue to meet liquidity needs. As such, we may be forced to delay raising capital, issue shorter-term securities than we prefer, or bear an unattractive cost of capital which could decrease our profitability and reduce our financial flexibility. Our results of operations, financial condition and cash flows could be materially adversely affected.

As a holding company, we are dependent on our operating subsidiaries to cover operating expenses and dividend payments.

As a holding company, Aviva plc has no substantial operations of its own. Its principal sources of funding are dividends from subsidiaries, shareholder-backed funds and any amounts that may be raised through the issuance of debt and commercial paper. Our insurance and fund management operations are generally conducted through direct and indirect subsidiaries. Certain subsidiaries have regulatory restrictions that may limit the payment of dividends, which in some circumstances could limit our ability to pay dividends to shareholders. The inability of our subsidiaries to pay dividends in an amount sufficient to enable us to meet our cash requirements at the holding company level could have a material adverse effect on our business.

Insurance risks relating to Aviva's business

The cyclical nature of the insurance industry may cause fluctuations in our results.

Historically, the insurance industry has been cyclical and operating results of insurers have fluctuated because of volatile and sometimes unpredictable developments, many of which are beyond the direct control of any insurer. Although we have a geographically diverse group of businesses providing a wide range of products, we expect to experience the effects of this cyclical nature, including changes in sales and premium levels. The unpredictability and competitive nature of the general insurance business has contributed historically to significant quarter-to-quarter and year-to-year fluctuations in underwriting results and net earnings.

The use of inaccurate assumptions in pricing and reserving for insurance business may have an adverse effect on our business profitability.

The Group's life insurance companies are required to make a number of assumptions in relation to the business written, including the mortality and morbidity rates of our customers, the development of interest rates, lapse rates (the rates at which customers terminate existing policies prior to their maturity dates) and future levels of expenses. These assumptions may turn out to be incorrect.

When establishing their liabilities, our life insurance companies allow for changes in the assumptions made, monitor their experience against the actuarial assumptions used and assess the information gathered to refine their long-term assumptions, together with taking actual claims experience into account. However, it is not possible to determine precisely the total amounts that will ultimately be paid under the policies written by the business as amounts may vary from estimates. Changes in assumptions may also lead to changes in the level of capital required to be maintained, meaning that we may need to increase the amount of our reserves. This could have a material adverse impact on the Group's value, the results of our operations and financial condition.

Additionally, our management of the general insurance business requires the general insurance companies to make a number of assumptions in relation to the business written. These assumptions include the costs of writing the business and settling claims, and the frequency and severity of claims. The assumptions may turn out to be incorrect, thereby adversely impacting our profit. Additionally, man-made disasters, including accidents and intentional events, are particularly difficult to predict with a high

degree of accuracy. These would also have an adverse impact on our profit due to higher than expected claims.

Furthermore, outstanding claims provisions for the general insurance business are based on the best-estimate of the cost of future claim payments, plus an explicit allowance for risk and uncertainty, together with related claims handling costs.

Any provisions for re-opened claims are also included. A range of methods, including stochastic projections, may be used to determine these provisions. Underlying these methods are a number of explicit or implicit assumptions relating to the expected settlement amount and settlement pattern of claims.

If the assumptions underlying the reserving basis were to prove incorrect, we might have to increase the amount of the general insurance provisions, which would adversely impact our financial condition or results of operations.

We have a significant exposure to annuity business and a significant life insurance risk is associated with longevity.

Longevity statistics are monitored in detail and compared with emerging industry trends. The results are used to inform both the reserving and pricing of annuities within the Group. It is likely that uncertainty will remain in the development of future longevity that cannot be mitigated.

A strengthening in the longevity assumption, either to reflect changes in the underlying life expectancy of the population or of our particular portfolio used to calculate our long-term business liabilities, would result in an increase in these reserves and reduce our shareholders' equity.

See 'Financial statements IFRS – Note 56 – Risk management'.

If our business does not perform well or if actual experience versus estimates used in valuing and amortising Deferred Acquisition Costs (DAC) and Acquired value of in-force business (AVIF) vary significantly, we may be required to accelerate the amortisation and/or impair the DAC and AVIF which could adversely affect our results of operations or financial condition.

We incur significant costs in connection with acquiring new and renewal business. Those costs that vary with and are driven by the production of new and renewal business are deferred and referred to as DAC. The recovery of DAC is dependent upon the future profitability of the related business. The amount of future profit or margin is dependent principally on investment returns in excess of the amounts credited to policyholders, mortality, morbidity, persistency and expenses to administer the business. Of these factors, investment margins and general insurance underwriting profit are most likely to impact the rate of amortisation of such costs. The aforementioned factors enter into management's estimates of gross profits or margins, which generally are used to amortise such costs. If the estimates of gross profits or margins were overstated, then the amortisation of such costs would be accelerated in the period the actual amount is known and would result in a charge to income. Significant or sustained equity market declines could result in an acceleration of amortisation of the DAC related to unit-linked business, resulting in a charge to income. Such adjustments could have a material adverse effect on our results of operations or financial condition.

AVIF reflects the estimated present value of future profits that will emerge over the remaining life of certain in-force contracts in a life insurance company, acquired either directly or through the purchase of a subsidiary, and represents the portion of the purchase price that is allocated to the value of the right to receive future cash flows from the insurance and investment contracts in-force at the acquisition date. AVIF is based on actuarially determined projections. Actual experience may vary from the projections. Revisions to estimates result in changes to the amounts expensed in the reporting period in which the revisions are made and could result in impairment and a charge to income. Where AVIF is amortised, an acceleration of the amortisation of AVIF would occur if the estimates of gross profits or margins were

overstated in the period in which the actual experience is known and would result in a charge to net income. Such adjustments could have an adverse effect on our results of operations or financial condition.

Catastrophic events, which are often unpredictable by nature, could result in material losses and abruptly and significantly interrupt our business activities.

Our business is exposed to volatile natural and man-made disasters such as pandemics, hurricanes, windstorms, earthquakes, terrorism, riots, fires and explosions. Over the past several years, changing weather patterns and climatic conditions have added to the unpredictability and frequency of natural disasters in certain parts of the world and created additional uncertainty as to future trends and exposure.

Our life insurance operations are exposed to the risk of catastrophic mortality, such as a pandemic or other event that causes a large number of deaths. The effectiveness of external parties, including governmental and non-governmental organisations, in combating the spread and severity of such a pandemic could have a material impact on the losses experienced by us.

The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are restricted to small geographic areas; however, pandemics, hurricanes, earthquakes and man-made catastrophes may produce significant damage in larger areas, especially those that are heavily populated. Catastrophic events could also harm the financial condition of our reinsurers and thereby increase the probability of default on reinsurance recoveries and could also reduce our ability to write new business. Furthermore, pandemics, natural disasters, terrorism and fires could disrupt our operations and result in significant loss of property, key personnel and information about our clients and our business if our business continuity plans fail to cope with the scale or nature of the catastrophe. Such events could adversely affect our business, results or operations, corporate reputation and financial condition for a substantial period of time.

Furthermore, market conditions beyond our control determine the availability and cost of the reinsurance protection we purchase. Accordingly, we may be forced to incur additional expenses for reinsurance or may not be able to obtain sufficient reinsurance on acceptable terms, which could adversely affect our ability to write future business.

Operational risks relating to Aviva's business

All of our businesses are subject to operational risks, including the risk of direct or indirect loss resulting from inadequate or failed internal and external processes, systems and human error or from external events.

Our business is dependent on processing a large number of complex transactions across numerous and diverse products. Furthermore, the long-term nature of the majority of our business means that accurate records have to be maintained for significant periods.

We also outsource several operations, including certain servicing and IT functions and are therefore partially reliant upon the operational processing performance of our outsourcing partners.

Our systems and processes on which we are dependent to serve our customers are designed to appropriately identify and address the operational risks associated with our activities. However, they may nonetheless fail due to IT malfunctions, human error, intentional disruption or hacking of IT systems by third parties, business interruptions, non-performance by third parties or other external events. This could disrupt business operations resulting in material reputational damage and the loss of customers, and have a consequent material adverse effect on our results of operations and financial condition. Although we

have taken steps to upgrade systems and processes to reduce these operational risks, we cannot anticipate the details or timing of all possible operational and systems failures which may adversely impact our business.

We operate in several markets through arrangements with third parties. These arrangements involve certain risks that we do not face with our subsidiaries.

Our ability to exercise management control over our partnership operations, our joint ventures and our investment in them depends on the terms of the legal agreements. In particular, the relationships depend on the allocation of control among, and continued co-operation between, the participants.

We may also face financial or other exposure in the event that any of our partners fail to meet their obligations under the agreement or encounter financial difficulty. For example, a significant proportion of our product distribution, such as bancassurance, is carried out through arrangements with third parties not controlled by us and is dependent upon the continuation of these relationships. A temporary or permanent disruption to these distribution arrangements could affect our financial condition. Some of these arrangements require our third-party partners to participate in and provide capital to our joint venture, associate and subsidiary undertakings. Our partners may change their strategic priorities or encounter financial difficulties preventing them from providing the necessary capital to promote future growth.

In addition, we outsource certain customer service, technology and legacy policy administration functions to third parties and may do so increasingly in the future. If we do not effectively develop and implement our outsourcing strategy, third-party providers do not perform as anticipated or we experience technological or other problems with a transition to or between such providers, we may not realise the full extent of productivity improvements or cost efficiencies and may experience operational difficulties, increased costs and a loss of business.

The failure to attract or retain the necessary personnel could have a material adverse effect on our results and/or financial condition.

As a global financial services organisation, we rely to an extent on the quality of local management in the countries in which we operate. The success of our operations is dependent, among other things, on our ability to attract and retain highly qualified professional employees. Competition for such key employees is intense. Our ability to attract and retain key employees is dependent on a number of factors, including prevailing market conditions and compensation packages offered by companies competing for the same talent.

There are inherent funding risks associated with our participation in defined benefit staff pension schemes.

We operate both defined benefit and defined contribution staff pension schemes. The defined benefit section of the UK staff pension scheme was closed to new members from 1 April 2011, with entry into the defined contribution sections being offered to the staff members affected. Closure of the defined benefit scheme has removed the volatility associated with adding future accrual for active members.

There are inherent funding risks associated with the defined benefit schemes. Events could result in a material reduction in the funding position of such schemes and, in some cases, may result in a deficit between the pension scheme's assets and liabilities. The factors that affect the scheme's position include: poor investment performance of pension fund investments; greater life expectancy than assumed; adverse changes in interest rates or inflation; and other events occurring that increase the costs of past service benefits over the amounts predicted in the actuarial assumptions. In the short term, the funding position is inherently volatile due to movements in the market value of assets. Where

a funding deficit or surplus arises, the position will be discussed with the scheme trustees to agree appropriate actions. This may include a plan to fund the deficit over a period of years. Any surplus or deficit in the defined benefit pension scheme will affect our shareholders' equity, although the IFRS position may diverge from the scheme funding position.

The UK pension schemes are subject to statutory requirements with regards to funding and other matters relating to the administration of the schemes. Compliance with these requirements is subject to regular review. A determination that we have failed to comply with applicable regulations could have a negative impact on our results of operations or our relationship with current and potential contributors and employees and adverse publicity.

Our process for valuing investments may include methodologies, estimations and assumptions which require judgement and could result in changes to investment valuations.

We value our available for sale (AFS) and fair value (FV) securities using designated methodologies, estimation and assumptions. These securities, which are reported at fair value on the consolidated statement of financial position, represent the majority of invested assets. We have categorised the measurement basis for assets carried at fair value into a 'fair value hierarchy' in accordance with the valuation inputs and consistent with IFRS 7 Financial Instruments: Disclosures. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1); the middle priority to fair values other than quoted prices based on observable market information (Level 2); and the lowest priority to unobservable inputs that reflect the assumptions that we consider market participants would normally use (Level 3). The majority of our financial assets are valued based on quoted market information (Level 1) or observable market data (Level 2). The majority of investment property and commercial mortgages are classified as Level 2. At 31 December 2012, 5.1% of total financial investments, loans and investment properties at fair value were classified as Level 3, amounting to £13,434 million (5.8% and £12,918 million excluding assets held for sale). Where estimates were used for inputs to Level 3 fair values, these were based on a combination of independent third-party evidence and internally developed models, intended to be calibrated to market observable data where possible.

An asset or liability's classification within the fair value hierarchy is based on the lowest level of significant input to its valuation.

See 'IFRS critical accounting policies – Investments'. Any change to investment valuations may affect our results of operations and reported financial condition.

Systems errors or regulatory changes may affect the calculation of unit prices or deduction of charges for our unit-linked products which may require us to compensate customers retrospectively.

A significant proportion of our product sales are unit-linked contracts, where product benefits are linked to the prices of underlying unit funds. While comprehensive controls are in place, there is a risk of error in the calculation of the prices of these funds due to human error in data entry, IT-related issues or other causes. Additionally, it is possible that policy charges which are deducted from these contracts are taken incorrectly, or the methodology is subsequently challenged by policyholders or regulators and changed retrospectively. Any of these can give rise to compensation payments to customers. Controls are in place to mitigate these risks, but errors could give rise to future liabilities. Payments due to errors or compensation may negatively impact our profits.

Moves to simplify the operating structure and activities of the Group increases the reliance placed on core businesses and is subject to execution risk.

As part of the Group's move to a more simplified structure, a number of business disposals and operational restructures have taken place and may continue to occur in the future. This includes the removal of the regional organisational structure and the potential sale of a number of non-core businesses. These changes are expected to reduce the operational costs of the Group and allow resources to be re-deployed in more capital efficient businesses. There is no assurance that these expected benefits will be realised. These changes may reduce operating profits in the short-term and will lead to changes in the geographical and product risk profile of the Group. The execution risk including the risks relating to securing the regulatory approvals necessary to complete our planned business disposals, could result in the failure to achieve cost savings, the loss of key staff, and disruption to core business activities and governance structures which could have a material adverse effect on our business, results of operations and financial condition.

Brand and reputation risks relating to Aviva's business

We are rated by several rating agencies, and a decline in any of these ratings could affect our standing among customers, broker-dealers, agents, wholesalers and other distributors of our products and services and cause our sales and earnings to decrease.

A rating downgrade, or the perceived potential for such a downgrade, of Aviva plc or any of our rated insurance subsidiaries may, among other things, materially increase the number of policy surrenders and withdrawals by policyholders of cash values from their policies. The outcome of such activities may be cash payments requiring the sale of invested assets, including illiquid assets, at a price that may result in realised investment losses. These cash payments to policyholders would result in a decrease in total invested assets and a decrease in net income. Among other things, early withdrawals may also cause us to accelerate amortisation of policy acquisition costs, which would reduce net income. A rating downgrade may also impact sales volumes, particularly in the US where there is more focus on ratings when evaluating similar products. The ratings provided by A.M. Best are widely considered to be the most important for distribution in the US, and although we have agreed to sell such operations, a downgrade could lead to a significant loss of sales. Similarly, a rating downgrade may increase our cost of borrowing or limit our access to some forms of financing.

We are dependent on the strength of our brand, the brands of our partners and our reputation with customers and agents in the sale of our products and services.

Our results are, to a certain extent, dependent on the strength of our brand and reputation. While we as a Group are well recognised, we are vulnerable to adverse market and customer perception. We operate in an industry where integrity, customer trust and confidence are paramount. We are exposed to the risk that litigation, employee misconduct, operational failures, the outcome of regulatory investigations, press speculation and negative publicity, disclosure of confidential client information, inadequate services, amongst others, whether true or not, could impact our brand or reputation. Our brand and reputation could also be affected if products or services recommended by us (or any of our intermediaries) do not perform as expected (whether or not the expectations are founded) or in line with the customers' expectations for the product range. Such a change to our brand strength could adversely affect our results of operations and financial condition.

We may not be able to protect our intellectual property and may be subject to infringement claims by a third party.

Our primary brand (Aviva) is a registered trade mark in the UK and elsewhere. We own other registered or pending trade marks in the UK, including Community trade marks having effect in the entire EU. We rely on a combination of contractual rights, copyright and trademark laws to establish and protect our intellectual property. Although we use a broad range of measures to protect our intellectual property rights, third parties may infringe or misappropriate our intellectual property. The loss of intellectual property protection or the inability to secure or enforce the protection of our intellectual property assets could have a material adverse effect on our business and our ability to compete.

Third parties may have, or may eventually be issued, patents or other protections that could be infringed by our products, methods, processes or services or could limit our ability to offer certain product features. In recent years, there has been increasing intellectual property litigation in the financial services industry challenging, among other things, product designs and business processes. If a third party were to successfully assert an intellectual property infringement claim against us, or if we were otherwise precluded from offering certain features or designs, or utilising certain processes, it could have a material effect on our business, results of operation and financial condition.

Our businesses are conducted in highly competitive environments.

There are many factors which affect our ability to sell our products, including fiscal incentives, price and yields offered, financial strength and ratings, range of product lines and product quality, brand strength and name recognition, investment management performance and historical bonus levels. In some of our markets, the Group faces competitors that are larger, have greater financial resources or greater market share, offer a broader range of products, benefit from more advantageous tax treatments, or have higher bonus rates or claims-paying ratios. Further, heightened competition for talented and skilled employees with local experience, particularly in the emerging, high-growth markets, may limit our potential to grow our business as quickly as planned.

Our principal competitors in the life market include many of the major financial services businesses including, in particular, Axa, Allianz, Generali, Prudential and Standard Life. Our principal competitors in the general insurance market include Royal Bank of Scotland Insurance, RSA, Zurich, Axa and Allianz.

We also face competitors who specialise in many of the niche markets in which we operate. We believe that competition will intensify across all businesses in response to consumer demand, technological advances, the impact of consolidation, regulatory actions and other factors.

Our ability to generate an appropriate return depends significantly upon our capacity to anticipate and respond appropriately to these competitive pressures.

Our regulated business is subject to extensive regulatory supervision both in the UK and internationally.

We are subject to extensive laws and regulations that are administered and enforced by a number of different governmental authorities and non-governmental self-regulatory agencies, including the FSA and other regulators. In light of wider financial and economic conditions, some of these authorities are considering, or may in the future consider, enhanced or new regulatory requirements intended to prevent future crises or otherwise assure the stability of institutions under their supervision. These authorities may also seek to exercise their supervisory or enforcement authority in new or more robust ways. All of these possibilities, if they occurred, could affect the way we conduct our business and manage our capital, and may require us to satisfy increased capital requirements.

Insurance regulation in the UK is largely based on the requirements of EU directives. Inconsistent application of directives by regulators in different EU member states may place our business at a competitive disadvantage to other European financial services groups. In addition, changes in the local regulatory regimes of designated territories could affect the calculation of our solvency position.

Our insurance subsidiaries worldwide are subject to detailed and comprehensive government regulation in each of the jurisdictions in which they conduct business. Regulatory agencies have broad administrative power over many aspects of the insurance business, which may include premium rates, marketing and selling practices, advertising, licensing agents, policy forms, capital adequacy and permitted investments. Government regulators are concerned primarily with the protection of policyholders rather than our shareholders or creditors. In the UK, our business is subject to regulation by the FSA, which has broad powers under the FSMA, including the authority to grant, vary the terms of, or cancel a regulated firm's authorisation, to investigate marketing and sales practices and to require the maintenance of adequate financial resources. The FSA has the power to take a range of investigative, disciplinary or enforcement actions, including public censure, restitution, fines or sanctions and to award compensation. The FSA is being replaced by twin regulators, the Prudential Regulation Authority and the Financial Conduct Authority. This change will take effect on 1 April 2013.

The FSA may make enquiries of the companies which it regulates regarding compliance with regulations governing the operation of business and, similar to the other UK regulated financial services companies, we face the risk that the FSA could find that we have failed to comply with applicable regulations or have not undertaken corrective action as required.

Issues and disputes may arise from time to time from the way in which the insurance industry or fund management industry has sold or administered an insurance policy or other product or in the way in which they have treated policyholders or customers, either individually or collectively.

Where larger groups or matters of public policy are concerned, the FSA may intervene directly. There have been several industry-wide issues in recent years in which the FSA has intervened directly, including the sale of personal pensions, the sale of mortgage-related endowments and investments in split capital investment trusts and payment protection insurance.

Outside of the UK, our business is regulated by local regulators that often have similar powers to the FSA and could therefore have a similar negative impact on perceptions of our business or have a material adverse effect on our business.

Furthermore, various jurisdictions in which we operate, including the UK, have created investor compensation schemes that require mandatory contributions from market participants in some instances in the event of a failure of another market participant. As a major participant in the majority of our chosen markets, circumstances could arise where we, along with other companies, may be required to make such contributions.

A determination that we have failed to comply with applicable regulation could have a negative impact on our results of operations or on our relations with current and potential customers. Regulatory action against a member of the Group could result in adverse publicity for, or negative perceptions regarding, the Group, or could have a material adverse effect on our business, our results of operations and financial condition and divert management's attention from the day-to-day management of the business.

We will not always be able to predict the impact of future legislation or regulation or changes in the interpretation or operation of existing legislation or regulation on our business, results of operations and financial condition. Changes in government policy, legislation or regulatory interpretation applying to companies in the financial services and insurance

industries in any of the markets in which we operate, which may be applied retrospectively, may adversely affect our product range, distribution channels, capital requirements, dividends payable by subsidiaries and, consequently, results and financing requirements.

We may face increased compliance costs due to the need to set up additional compliance controls or the direct cost of such compliance because of changes to financial services legislation or regulation.

The Solvency II Directive ('Solvency II'), an insurance industry regulation agreed by the European Parliament in 2009, will require European domiciled insurers to move to more risk-based capital requirements. The implementation date for Solvency II has been extended to January 2014 and may be extended further. There continue to be material uncertainties around the impact of the more detailed technical requirements of Solvency II and there is a risk that this could lead to a significant increase in the capital required to support our business.

We are involved in various legal proceedings, regulatory investigations and examinations and may be involved in more in the future.

We have been named as defendants in lawsuits, including class actions and individual lawsuits. We have been subject to regulatory investigations or examinations in the various jurisdictions where we operate. These actions arise in various contexts, including in connection with our activities as an insurer, securities issuer, employer, investment adviser, investor and taxpayer. Certain of these lawsuits and investigations seek significant or unspecified amounts of damages, including punitive damages, and certain of the regulatory authorities involved in these proceedings have substantial powers over the conduct and operations of our business.

Due to the nature of certain of these lawsuits and investigations, we cannot make an estimate of loss or predict with any certainty the potential impact of these lawsuits or investigations.

In the course of conducting insurance business, we receive general insurance liability claims, and become involved in actual or threatened related litigation arising there from, including claims in respect of pollution and other environmental hazards. Given the significant delays that are experienced in the notification of these claims, the potential number of incidents that they cover and the uncertainties associated with establishing liability and the availability of reinsurance, the ultimate cost cannot be determined with certainty.

Additionally, it is possible that a regulator in one of our major markets may conduct a review of products previously sold, either as part of an industry-wide review or specific to us. The result of this review may be to compensate customers for losses they have incurred as a result of the products they were sold.

All of the above could adversely impact our results of operations or financial condition.

From time to time, changes in the interpretation of existing tax laws, amendments to existing tax rates or the introduction of new tax legislation may adversely impact our business.

We operate in numerous tax jurisdictions around the world and face risks associated with changes in tax law, interpretation of tax law, changes in tax rates and the risk of failure to comply with procedures required by tax authorities. Failure to manage tax risks could lead to an additional tax charge or a financial penalty.

If, as a result of a particular tax risk materialising, the tax costs associated with certain transactions are greater than anticipated, it could affect the profitability of those transactions.

There are also specific rules governing the taxation of policyholders. We are unable to predict accurately the impact of future changes in tax law on the taxation of life insurance and pension policies in the hands of policyholders. Amendments to existing legislation, particularly if there is the withdrawal of any

tax relief, or an increase in tax rates, or the introduction of new rules, may affect the future long-term business and the decisions of policyholders. The impact of such changes upon us might depend on the mix of business in-force at the time of such change.

The design of life insurance products by our life insurance companies takes into account a number of factors, including risks and taxation. The design of long-term insurance products is based on the tax legislation in force at that time. Changes in tax legislation or in the interpretation of tax legislation may therefore, when applied to such products, have a material adverse effect on the financial condition of the relevant long-term business fund of the company in which the business was written.

Risks related to ownership of the ADSs and ordinary shares

The trading price of our ADRs and dividends paid on our ADSs may be materially adversely affected by fluctuations in the exchange rate for converting sterling into US dollars.

An ADS is a negotiable US security representing ownership in one share. An ADR is denominated in US dollars and represents ownership of any number of ADSs. ADRs are publicly traded shares in a non-US corporation, quoted and traded in US dollars in the US securities market. Any dividends are paid to investors in US dollars. ADRs are specifically designed to facilitate the purchase, holding and sale of non-US securities by US investors. The term ADR is often used to mean both the certificates and the securities themselves.

Fluctuations in the exchange rate for converting pound sterling into US dollars may affect the value of our ADRs. Specifically, as the relative value of the pound sterling against the US dollar declines, each of the following values will also decline:

- the US dollar equivalent of the pound sterling trading price of our ordinary shares on the London Stock Exchange which may consequently cause the trading price of our ADRs in the US to also decline;
- the US dollar equivalent of the proceeds that a holder of our ADSs would receive upon the sale in the UK of any our ordinary shares withdrawn from the depository; and
- the US dollar equivalent of cash dividends paid in pound sterling on our ordinary shares represented by our ADSs.

The holders of our ADSs may not be able to exercise their voting rights due to delays in notification to, and by, the depository.

The depository for our ADSs may not receive voting materials for our ordinary shares represented by our ADSs in time to ensure that holders of our ADSs can instruct the depository to vote their shares. In addition, the depository's liability to holders of our ADSs for failing to carry out voting instructions or for the manner of carrying out voting instructions is limited by the Deposit Agreement governing our ADR facility. As a result, holders of our ADSs may not be able to exercise their right to vote and may have limited or no recourse against the depository or us, if their shares are not voted according to their request.

Holders of our ADSs will have limited recourse if we or the depository fail to meet our respective obligations under the Deposit Agreement.

The Deposit Agreement expressly limits our obligations and liability and those of the depository. Neither we nor the depository will be liable if either of us:

- are prevented from or delayed in performing any obligation by circumstances beyond our/their control;
- exercise or fail to exercise discretion under the Deposit Agreement; or
- take any action based upon the advice of, or information from, legal counsel, accountants, any person presenting ordinary shares for deposit, any person in whose name the ADSs are registered on the books of the depository, any person or entity having a beneficial interest deriving from the ownership of ADRs, or any other person believed by us or the depository in good faith to be competent to give such advice or information.

In addition, the depository has the obligation to participate in any action, suit or other proceeding with respect to our ADSs which may involve it in expense or liability only if it is indemnified. These provisions of the Deposit Agreement will limit the ability of holders of our ADSs to obtain recourse if we or the depository fail to meet our obligations under the Deposit Agreement or if they wish to involve us or the depository in a legal proceeding.

The holders of our ADRs in the US may not be able to participate in offerings of rights, warrants or similar securities to holders of our ordinary shares on the same terms and conditions as holders of our ordinary shares.

In the event that we offer rights, warrants or similar securities to the holders of our ordinary shares or distribute dividends payable, in whole or in part, in securities, the Deposit Agreement provides that the depository (after consultation with us) shall have discretion as to the procedure to be followed in making such rights or other securities available to ADR holders, including disposing of such rights or other securities and distributing the net proceeds in US dollars to ADR holders. Given the significant number of our ADR holders in the US, we generally would be required to register with the SEC any public offering of rights, warrants or other securities made to our ADR holders unless an exemption from the registration requirements of the US securities laws is available. Registering such an offering with the SEC can be a lengthy process which may be inconsistent with the timetable for a global capital raising operation. Consequently, we have in the past elected and may in the future elect not to make such an offer in the US, including to our ADR holders in the US, and rather only conduct such an offering in an 'offshore' transaction in accordance with 'Regulation S' under the US Securities Act of 1933, as amended (the 'Securities Act'). Therefore, there can be no assurance that our ADR holders will be able to participate in such an offering in the same manner as our ordinary shareholders.

The ADR and ordinary share price of Aviva has been, and may continue to be volatile.

The share price of our ADRs and ordinary shares has been volatile in the past and the share price and trading volume of our ADRs may continue to be subject to significant fluctuations due, in part, to changes in our actual or forecast operating results and the inability to fulfil the profit expectations of securities analysts, as well as to the high volatility in the securities markets generally and more particularly in shares of financial institutions. Other factors, besides our financial results, that may impact our share price include, but are not limited to:

- market expectations of the performance and capital adequacy of financial institutions in general;
- investor perceptions of the success and impact of our strategies;
- a downgrade or review of our credit ratings;
- potential litigation or regulatory action involving Aviva or sectors we have exposure to through our insurance and fund management activities;
- the operations, accounting practices or regulatory investigations, and share price performance of other companies in the insurance and fund management markets in which the Group operates; and
- conjecture about the Group's business in the press, media or investment communities.

As a 'foreign private issuer' in the US we are exempt from certain rules under the US securities laws and are permitted to file less information with the SEC than US companies.

As a 'foreign private issuer' we are exempt from certain rules under the US Securities Exchange Act of 1934, as amended (the 'Exchange Act'), that impose certain disclosure obligations and procedural requirements for proxy solicitations under Section 14 of the Exchange Act. In addition, our officers, directors and principal shareholders are exempt from the reporting and 'short-swing' profit recovery provisions of Section 16 of the Exchange Act and the rules under the Exchange Act with respect to their purchases and sales of our ordinary shares and ADRs. Moreover, we are not required to file periodic reports and financial statements with the SEC as frequently or as promptly as US companies whose securities are registered under the Exchange Act. In addition, we are not required to comply with Regulation FD, which restricts the selective disclosure of material information. Although we must comply with UK Listing Rules on insider reporting of share ownership and on protection of inside information, there may be less publicly available information concerning us than there is for US public companies.

Aviva plc is an English company and it may be difficult to enforce judgments against us or our directors and executive officers.

Aviva plc is incorporated under the laws of England and Wales and our business is based in the UK. In addition, certain of our directors and officers reside outside the US, and a substantial portion of our assets and the assets of such persons are located in jurisdictions outside the US. As such, it may be difficult or impossible to effect service of process within the US upon us or those persons or to recover against us or them on judgments of US courts, including judgments predicated upon civil liability provisions of the US federal securities laws.

Shareholder rights under English law differ from the US.

Individual shareholders of an English company (including US persons) have the right under English law to bring lawsuits on behalf of the company in which they are a shareholder, and on their own behalf against the company, in certain limited circumstances. English law does not permit class action lawsuits by shareholders, except in limited circumstances.

Financial statements IFRS

In this section

Independent auditors' report	146	26 Receivables	208
Accounting policies	148	27 Deferred acquisition costs, other assets, prepayments and accrued income	208
Consolidated financial statements	160	28 Assets held to cover linked liabilities	209
Consolidated income statement	160	29 Ordinary share capital	210
Consolidated statement of comprehensive income	161	30 Group's share plans	210
Reconciliation of Group operating profit to (loss)/profit for the year	162	31 Shares held by employee trusts	214
Consolidated statement of changes in equity	164	32 Preference share capital	214
Consolidated statement of financial position	166	33 Direct capital instruments and fixed rate tier 1 notes	215
Consolidated statement of cash flows	167	34 Merger reserve	215
		35 Other reserves	216
		36 Retained earnings	216
		37 Non-controlling interests	217
		38 Contract liabilities and associated reinsurance	217
		39 Insurance liabilities	218
		40 Liability for investment contracts	228
		41 Financial guarantees and options	229
		42 Reinsurance assets	232
		43 Effect of changes in assumptions and estimates during the year	233
		44 Unallocated divisible surplus	234
		45 Tax assets and liabilities	235
		46 Provisions	236
		47 Pension obligations	237
		48 Borrowings	243
		49 Payables and other financial liabilities	246
		50 Other liabilities	246
		51 Contingent liabilities and other risk factors	246
		52 Commitments	247
		53 Group capital structure	248
		54 Statement of cash flows	249
		55 Capital statement	251
		56 Risk management	253
		57 Derivative financial instruments and hedging	264
		58 Assets under management	266
		59 Related party transactions	266
		Financial statements of the Company	267
		Statement of changes in equity	267
		Statement of financial position	268
		Statement of cash flows	269
		Notes to the Company's financial statements	270

Notes to the consolidated financial statements

1 Exchange rates	168		
2 Presentation changes	168		
3 Subsidiaries	168		
4 Segmental information	171		
5 Details of income	179		
6 Details of expenses	180		
7 Finance costs	181		
8 Long-term business economic volatility	182		
9 Longer-term investment return and economic assumption changes for non-long-term business	183		
10 Employee information	184		
11 Directors	185		
12 Auditors' remuneration	186		
13 Tax	187		
14 (Loss)/earnings per share	189		
15 Dividends and appropriations	190		
16 Goodwill	191		
17 Acquired value of in-force business (AVIF) and intangible assets	193		
18 Interests in, and loans to, joint ventures	194		
19 Interests in, and loans to, associates	196		
20 Property and equipment	197		
21 Investment property	198		
22 Fair value methodology	198		
23 Loans	201		
24 Securitised mortgages and related assets	203		
25 Financial investments	204		

Independent auditors report to the members of Aviva plc

We have audited the Group and Parent Company financial statements of Aviva plc for the year ended 31 December 2012 which comprise the Accounting policies, the Consolidated income statement, the Consolidated statement of comprehensive income, the Reconciliation of Group operating profit to (loss)/profit for the year, the Consolidated and Parent Company statements of changes in equity, the Consolidated and Parent Company statements of financial position, the Consolidated and Parent Company statements of cash flows, and the related notes 1 to 59 and A to K. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' responsibility statement set out on page 88, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the Parent Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Aviva plc Annual report and accounts to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion:

- The financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2012 and of the Group's loss and Group's and Parent Company's cash flows for the year then ended;
- The Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- The Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- The financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Separate opinion in relation to IFRSs as issued by the IASB

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

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

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

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

- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements and the part of the Directors' remuneration report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statement, set out on page 87, in relation to going concern;
- the parts of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

David Law (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors

London
6 March 2013

- 1 The maintenance and integrity of the Aviva plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- 2 Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Accounting policies

Aviva plc (the 'Company'), a public limited company incorporated and domiciled in the United Kingdom (UK), together with its subsidiaries (collectively, the 'Group' or 'Aviva') transacts life assurance and long-term savings business, fund management and most classes of general insurance and health business through its subsidiaries, associates and branches in the UK, Ireland, continental Europe, United States (US), Canada, Asia and other countries throughout the world.

Following the announcement in April 2012 relating to the restructuring of the Group, the Group's operating segments were changed to align them with the new organisational reporting structure. The Group has determined its operating segments along market reporting lines, reflecting the management structure whereby a member of the Executive Management team is accountable to the group chief executive for the operating segment for which he is responsible. Further details of the reportable segments are given in note 4.

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

(A) Basis of presentation

The consolidated financial statements and those of the Company have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU), and those parts of the Companies Act 2006 applicable to those reporting under IFRS. In addition to fulfilling their legal obligation to comply with IFRS as adopted by the EU, the Group and Company have also complied with IFRS as issued by the IASB and applicable at 31 December 2012. The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of land and buildings, available-for-sale financial assets, and financial assets and financial liabilities (including derivative instruments) at fair value through profit and loss.

In accordance with IFRS 4, Insurance Contracts, the Group has applied existing accounting practices for insurance and participating investment contracts, modified as appropriate to comply with the IFRS framework and applicable standards. Further details are given in accounting policy F.

Items included in the financial statements of each of the Group's entities are measured in the currency of the primary economic environment in which that entity operates (the functional currency). The consolidated financial statements are stated in sterling, which is the Company's functional and presentation currency. Unless otherwise noted, the amounts shown in these financial statements are in millions of pounds sterling (£m). The separate financial statements of the Company are on pages 267 to 272.

See note 2 for presentation changes to the consolidated financial statements.

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

The Group has adopted the following new amendments to standards which became effective for financial years beginning on or after 1 January 2012. Neither of these amendments has a material impact on these financial statements.

- (i) Amendment to IFRS 7, Financial Instruments – Disclosures, relating to the transfer of financial assets.
- (ii) Amendment to IAS 12, Income Taxes, relating to deferred tax.

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

The following new standards, amendments to existing standards and interpretations have been issued, are effective for accounting

periods beginning on or after the following dates and have not been adopted by the Group:

Effective for annual periods beginning on or after 1 July 2012 **Amendment to IAS 1, Financial Statement Presentation**

The amendment requires entities to group items presented in other comprehensive income according to whether they will subsequently be reclassified to profit and loss. The adoption of the amendment will change the presentation of the consolidated statement of comprehensive income in the financial statements. The amendment has been endorsed by the EU.

Effective for annual periods beginning on or after 1 January 2013

(i) **Amendment to IAS 19, Employee Benefits**

The amendment revises requirements for pensions and other post-retirement benefits, termination benefits and other employee benefits. The key changes include the revision of the calculation of the finance cost, enhanced disclosures surrounding the characteristics and risk profile of defined benefit plans, and a requirement to include all actuarial gains and losses immediately in other comprehensive income which is already in line with the Group's current policy. The amended standard will impact finance costs as the concept of expected return is removed and replaced with interest on scheme assets, which is calculated using the same interest rate that is applied for the purposes of discounting the defined benefit obligation. The difference between interest income on scheme assets and the actual return is included in other comprehensive income. If this amendment had been adopted for the year ended 31 December 2012, the net impact would have been an increase in profit before tax and a corresponding decrease in other comprehensive income of £145 million. This is the difference between the current expected return on scheme assets and the interest income on scheme assets calculated using the discount rate. The amendment has been endorsed by the EU.

(ii) **Amendment to IFRS 7, Financial Instruments – Disclosures**

The amendment includes enhanced disclosures to enable users of the financial statements to evaluate the effect or potential effect of netting arrangements in the statement of financial position. The amendments will not have a significant impact for the Group. The amendment has been endorsed by the EU.

(iii) **IFRS 10, Consolidated Financial Statements**

IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. IFRS 10 establishes a single control model that applies to all entities including special purpose entities, based on the concept of power, exposure or rights to variable returns and their linkage. This will replace the current approach which emphasises the power to govern the financial and operating policies, and exposure to risks and rewards, depending on the nature of the entity. IFRS 10 defines and prescribes how to apply the principle of control in determining which entities are required to be consolidated in the consolidated financial statements. The standard has been endorsed by the EU.

Based on our assessment to date, the Group does not expect the overall impact of the adoption of IFRS 10 on the Group's equity and profit before tax for the year to be material. The implementation of IFRS 10 is expected to mainly result in the Group consolidating some investment vehicles that were previously not consolidated.

(iv) IFRS 11, Joint Arrangements

IFRS 11 defines and establishes accounting principles for joint arrangements. It distinguishes between two types of joint arrangements – joint ventures and joint operations – based on how rights and obligations are shared by parties to the arrangements. The full impact of the changes has yet to be fully assessed but is not expected to have a significant impact on the Group's equity and profit before tax for the year. The standard has been endorsed by the EU.

(v) IFRS 12, Disclosure of Interests in Other Entities

IFRS 12 includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. The standard is expected to have a significant impact on the level of disclosure in respect of these interests. The standard has been endorsed by the EU.

(vi) IAS 27, Separate Financial Statements (2011)

IAS 27 has been revised to remove the requirements for consolidated financial statements which are superseded by the issue of IFRS 10. The standard has been endorsed by the EU.

(vii) IAS 28, Investment in Associates and Joint Ventures (2011)

IAS 28 has been revised to include joint ventures as well as associates. Joint ventures are required to be equity accounted following the issue of IFRS 11. There are no implications for the Group financial statements. The standard has been endorsed by the EU.

(viii) IFRS 13, Fair Value Measurement

IFRS 13 replaces the guidance on fair value measurement in existing IFRSs with a single standard. The standard does not include requirements regarding which items should be measured at fair value but provides guidance on how to determine fair value. The standard also includes enhanced disclosures about fair value measurement. The adoption of IFRS 13 is not expected to have a significant impact on the financial statements. The standard has been endorsed by the EU.

(ix) Improvements to IFRSs 2009-2011

Improvements to IFRSs 2009-2011 details amendments to five IFRSs, including IAS 1, Presentation of Financial Statements, IAS 32, Financial Instruments – Presentation, and IAS 34, Interim Financial Reporting. The amendments clarify existing guidance and do not give rise to a change in existing accounting practice. There are no implications for the Group's consolidated financial statements. The amendments have yet to be endorsed by the EU.

Effective for annual periods beginning on or after 1 January 2014**(i) Amendment to IAS 32, Financial Instruments – Presentation**

The amendment to IAS 32 clarifies the requirements for offsetting financial assets and financial liabilities on the statement of financial position. The impact of the adoption of the amendment has yet to be fully assessed but is not expected to have significant implications for the Group financial statements. The amendment has been endorsed by the EU.

(ii) Amendments to IFRS 10, IFRS 12 and IAS 27 (2011)

The amendments provide an exemption from consolidation of subsidiaries under IFRS 10 'Consolidated Financial Statements' for entities which meet the definition of an 'investment entity', such as certain investment funds. Instead, such entities would measure their investment in

particular subsidiaries at fair value through profit or loss in accordance with IFRS 9 'Financial Instruments' or IAS 39 'Financial Instruments: Recognition and Measurement'. There are no implications for the Group's consolidated financial statements. The amendments have yet to be endorsed by the EU.

Effective for annual periods beginning on or after 1 January 2015**IFRS 9, Financial Instruments**

IFRS 9 will replace IAS 39, Financial Instruments – Recognition and Measurement. Under IFRS 9, all recognised financial assets that are currently within the scope of IAS 39 will be measured at either amortised cost or fair value. The basis of classification will depend on the business model and the contractual cash flow characteristics of the financial asset. All equity instruments will be measured at fair value.

A debt instrument is measured at amortised cost only if it is held to collect the contractual cash flows and the cash flows represent principal and interest, otherwise it is measured at fair value through profit and loss (FVTPL). For financial liabilities designated as at FVTPL, the change in the fair value attributable to changes in the liability's credit risk is recognised in other comprehensive income unless it gives rise to an accounting mismatch in profit or loss.

We have not yet completed our assessment of the impact of the adoption of IFRS 9 on the Group which, to a large extent, will need to take into account the finalisation of the standard and the interaction of the requirements of IFRS 9 with the IASB's ongoing insurance contracts accounting project. The standard has not yet been endorsed by the EU.

(B) Operating profit

The long-term nature of much of the Group's operations means that, for management's decision-making and internal performance management, short-term realised and unrealised investment gains and losses are treated as non-operating items.

The Group focuses instead on an operating profit measure (also referred to as adjusted operating profit) that incorporates an expected return on investments supporting its long-term and non-long-term businesses. Operating profit for long-term business is based on expected investment returns on financial investments backing shareholder and policyholder funds over the reporting period, with allowance for the corresponding expected movements in liabilities. Variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are disclosed separately outside operating profit. For non-long-term business, the total investment income, including realised and unrealised gains, is analysed between that calculated using a longer-term return and short-term fluctuations from that level. Further details of this analysis and the assumptions used are given in notes 8 and 9. Operating profit also excludes impairment of goodwill, associates and joint ventures; amortisation and impairment of other intangibles; the profit or loss on disposal and remeasurement of subsidiaries, joint ventures and associates; integration and restructuring costs; and exceptional items. Exceptional items are those items that, in the Directors' view, are required to be separately disclosed by virtue of their nature or incidence to enable a full understanding of the Group's financial performance. Details of these items are provided in the relevant notes.

(C) Critical accounting policies and the use of estimates

The preparation of financial statements requires the Group to select accounting policies and make estimates and assumptions that affect items reported in the consolidated income statement,

consolidated statement of financial position, other primary statements and notes to the consolidated financial statements.

Critical accounting policies and the use of estimates

These major areas of judgement on policy application are summarised below:

Item	Critical accounting judgement estimate or assumption	Accounting policy
Consolidation	Assessment of whether the Group controls the underlying entities	D
Insurance and participating investment contract liabilities	Assessment of the significance of insurance risk passed	F
Financial investments	Classification of investments	S

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

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

Item	Accounting policy
Insurance and participating investment contract liabilities	F&K
Goodwill, AVIF and intangible assets	N
Fair values of financial investments	S
Impairment of financial investments	S
Fair value of derivative financial instruments	T
Deferred acquisition costs and other assets	W
Provisions and contingent liabilities	Z
Pension obligations	AA
Deferred income taxes	AB
Operations held for sale	AG

(D) Consolidation principles

Subsidiaries

Subsidiaries are those entities (including special purpose entities) in which the Group, directly or indirectly, has power to exercise control over financial and operating policies in order to gain economic benefits. Subsidiaries are consolidated from the date on which effective control is transferred to the Group and are excluded from consolidation from the date the Group no longer has effective control. All inter-company transactions, balances and unrealised surpluses and deficits on transactions between Group companies have been eliminated. Accounting policies of subsidiaries are aligned on acquisition to ensure consistency with the Group policies.

The Group is required to use the acquisition method of accounting for business combinations. Under this method, the cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value, and the amount of any non-controlling interest in the acquiree. For each business combination, the Group has the option to measure the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. The excess of the consideration transferred over the fair value of the net assets of the subsidiary acquired is recorded as goodwill (see accounting policy N below). Acquisition-related costs are expensed as incurred. Transactions that do not result in a loss of control are treated as equity transactions with non-controlling interests.

Merger accounting and the merger reserve

Prior to 1 January 2004, the date of first time adoption of IFRS, certain significant business combinations were accounted for using the 'pooling of interests method' (or merger accounting), which treats the merged groups as if they had been combined throughout the current and comparative accounting periods.

Merger accounting principles for these combinations gave rise to a merger reserve in the consolidated statement of financial position, being the difference between the nominal value of new shares issued by the Parent Company for the acquisition of the shares of the subsidiary and the subsidiary's own share capital and share premium account. These transactions have not been restated, as permitted by the IFRS 1 transitional arrangements.

The merger reserve is also used where more than 90% of the shares in a subsidiary are acquired and the consideration includes the issue of new shares by the Company, thereby attracting merger relief under the Companies Act 1985 and, from 1 October 2009, the Companies Act 2006.

Investment vehicles

In several countries, the Group has invested in a number of specialised investment vehicles such as Open-ended Investment Companies (OEICs) and unit trusts. These invest mainly in equities, bonds, cash and cash equivalents, and properties, and distribute most of their income. The Group's percentage ownership in these vehicles can fluctuate from day to day according to the Group's and third-party participation in them. Where Group companies are deemed to control such vehicles, with control determined based on an analysis of the guidance in IAS 27 and SIC 12, they are consolidated, with the interests of parties other than Aviva being classified as liabilities. These appear as 'Net asset value attributable to unitholders' in the consolidated statement of financial position. Where the Group does not control such vehicles, and these investments are held by its insurance or investment funds, they do not meet the definition of associates (see below) and are, instead, carried at fair value through profit and loss within financial investments in the consolidated statement of financial position, in accordance with IAS 39, Financial Instruments: Recognition and Measurement.

As part of their investment strategy, the UK and certain European long-term business policyholder funds have invested in a number of property limited partnerships (PLPs), either directly or via property unit trusts (PUTs), through a mix of capital and loans. The PLPs are managed by general partners (GPs), in which the long-term business shareholder companies hold equity stakes and which themselves hold nominal stakes in the PLPs. The PUTs are managed by a Group subsidiary.

Accounting for the PUTs and PLPs as subsidiaries, joint ventures or other financial investments depends on the shareholdings in the GPs and the terms of each partnership agreement. Where the Group exerts control over a PLP, it has been treated as a subsidiary and its results, assets and liabilities have been consolidated. Where the partnership is managed by a contractual agreement such that there is joint control between the parties, notwithstanding that the Group's partnership share in the PLP (including its indirect stake via the relevant PUT and GP) may be greater than 50%, such PUTs and PLPs have been classified as joint ventures. Where the Group holds minority stakes in PLPs, with no significant influence or control over their associated GPs, the relevant investments are carried at fair value through profit and loss within financial investments.

Associates and joint ventures

Associates are entities over which the Group has significant influence, but which it does not control. Generally, it is presumed that the Group has significant influence if it has between 20% and 50% of voting rights. Joint ventures are entities whereby the Group and other parties undertake an economic activity which is subject to joint control arising from a contractual agreement. In a number of these, the Group's share of the underlying assets and liabilities may be greater than 50% but the terms of the relevant agreements make it clear that control is not exercised. Such jointly controlled entities are referred to as joint ventures in these financial statements.

Gains on transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's

interest in the associates and joint ventures. Losses are also eliminated, unless the transaction provides evidence of an impairment of the asset transferred between entities.

Investments in associates and joint ventures are accounted for using the equity method of accounting. Under this method, the cost of the investment in a given associate or joint venture, together with the Group's share of that entity's post-acquisition changes to shareholders' funds, is included as an asset in the consolidated statement of financial position. As explained in accounting policy N, the cost includes goodwill identified on acquisition. The Group's share of their post-acquisition profits or losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves. Equity accounting is discontinued when the Group no longer has significant influence or joint control over the investment.

If the Group's share of losses in an associate or joint venture equals or exceeds its interest in the undertaking, the Group does not recognise further losses unless it has incurred obligations or made payments on behalf of the entity.

The Company's investments

In the Company statement of financial position, subsidiaries, associates and joint ventures are stated at their fair values, estimated using applicable valuation models underpinned by the Company's market capitalisation. These investments are classified as available for sale (AFS) financial assets, with changes in their fair value being recognised in other comprehensive income and recorded in a separate investment valuation reserve within equity.

(E) Foreign currency translation

Income statements and cash flows of foreign entities are translated into the Group's presentation currency at average exchange rates for the year while their statements of financial position are translated at the year-end exchange rates. Exchange differences arising from the translation of the net investment in foreign subsidiaries, associates and joint ventures, and of borrowings and other currency instruments designated as hedges of such investments, are recognised in other comprehensive income and taken to the currency translation reserve within equity. On disposal of a foreign entity, such exchange differences are transferred out of this reserve and are recognised in the income statement as part of the gain or loss on sale. The cumulative translation differences were deemed to be zero at the transition date to IFRS.

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions, and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement.

Translation differences on debt securities and other monetary financial assets measured at fair value and designated as held at fair value through profit or loss (FV) (see accounting policy S) are included in foreign exchange gains and losses in the income statement. For monetary financial assets designated as AFS, translation differences are calculated as if they were carried at amortised cost and so are recognised in the income statement, whilst foreign exchange differences arising from fair value gains and losses are recognised in other comprehensive income and included in the investment valuation reserve within equity. Translation differences on non-monetary items, such as equities which are designated as FV, are reported as part of the fair value gain or loss, whereas such differences on AFS equities are included in the investment valuation reserve.

(F) Product classification

Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause an insurer to make significant additional payments in any scenario,

excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. Contracts can be reclassified as insurance contracts after inception if insurance risk becomes significant. Any contracts not considered to be insurance contracts under IFRS are classified as investment contracts. Some insurance and investment contracts contain a discretionary participating feature, which is a contractual right to receive additional benefits as a supplement to guaranteed benefits. These are referred to as participating contracts.

As noted in accounting policy A above, insurance contracts and participating investment contracts in general continue to be measured and accounted for under existing accounting practices at the later of the date of transition to IFRS or the date of the acquisition of the entity, in accordance with IFRS 4. Accounting for insurance contracts in UK companies is determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers, the most recent version of which was issued in December 2005 and amended in December 2006. In certain businesses, the accounting policies or accounting estimates have been changed, as permitted by IFRS 4 and IAS 8 respectively, to remeasure designated insurance liabilities to reflect current market interest rates and changes to regulatory capital requirements. When accounting policies or accounting estimates have been changed, and adjustments to the measurement basis have occurred, the financial statements of that year will have disclosed the impacts accordingly. One such example is our adoption of Financial Reporting Standard 27, Life Assurance, (FRS 27) which was issued by the UK's Accounting Standards Board (ASB) in December 2004. Aviva, along with other major insurance companies and the ABI, signed a Memorandum of Understanding with the ASB, under which we voluntarily agreed to adopt in full the standard from 2005 in the Group's IFRS financial statements. FRS 27 adds to the requirements of IFRS but does not vary them in any way. The additional requirements of FRS 27 are detailed in accounting policy K below and in note 55.

(G) Premiums earned

Premiums on long-term insurance contracts and participating investment contracts are recognised as income when receivable, except for investment-linked premiums which are accounted for when the corresponding liabilities are recognised. For single premium business, this is the date from which the policy is effective. For regular premium contracts, receivables are recognised at the date when payments are due. Premiums are shown before deduction of commission and before any sales-based taxes or duties. Where policies lapse due to non-receipt of premiums, then all the related premium income accrued but not received from the date they are deemed to have lapsed is offset against premiums.

General insurance and health premiums written reflect business inception during the year, and exclude any sales-based taxes or duties. Unearned premiums are those proportions of the premiums written in a year that relate to periods of risk after the statement of financial position date. Unearned premiums are calculated on either a daily or monthly pro rata basis. Premiums collected by intermediaries, but not yet received, are assessed based on estimates from underwriting or past experience, and are included in premiums written.

Deposits collected under investment contracts without a discretionary participating feature (non-participating contracts) are not accounted for through the income statement, except for the fee income (covered in accounting policy H) and the investment income attributable to those contracts, but are accounted for directly through the statement of financial position as an adjustment to the investment contract liability.

(H) Other investment contract fee revenue

Investment contract policyholders are charged fees for policy administration, investment management, surrenders or other contract services. The fees may be for fixed amounts or vary with the amounts being managed, and will generally be charged as an adjustment to the policyholder's balance. The fees are recognised as revenue in the period in which they are collected unless they relate to services to be provided in future periods, in which case they are deferred and recognised as the service is provided.

Initiation and other 'front-end' fees (fees that are assessed against the policyholder balance as consideration for origination of the contract) are charged on some non-participating investment and investment fund management contracts. Where the investment contract is recorded at amortised cost, these fees are deferred and recognised over the expected term of the policy by an adjustment to the effective yield. Where the investment contract is measured at fair value, the front-end fees that relate to the provision of investment management services are deferred and recognised as the services are provided.

(I) Other fee and commission income

Other fee and commission income consists primarily of fund management fees, distribution fees from mutual funds, commissions on reinsurance ceded, commission revenue from the sale of mutual fund shares and transfer agent fees for shareholder record keeping. Reinsurance commissions receivable are deferred in the same way as acquisition costs, as described in accounting policy W. All other fee and commission income is recognised as the services are provided.

(J) Net investment income

Investment income consists of dividends, interest and rents receivable for the year, movements in amortised cost on debt securities, realised gains and losses, and unrealised gains and losses on FV investments (as defined in accounting policy S). Dividends on equity securities are recorded as revenue on the ex-dividend date. Interest income is recognised as it accrues, taking into account the effective yield on the investment. It includes the interest rate differential on forward foreign exchange contracts. Rental income is recognised on an accruals basis.

A gain or loss on a financial investment is only realised on disposal or transfer, and is the difference between the proceeds received, net of transaction costs, and its original cost or amortised cost, as appropriate.

Unrealised gains and losses, arising on investments which have not been derecognised as a result of disposal or transfer, represent the difference between the carrying value at the year end and the carrying value at the previous year end or purchase value during the year, less the reversal of previously recognised unrealised gains and losses in respect of disposals made during the year. Realised gains or losses on investment property represent the difference between the net disposal proceeds and the carrying amount of the property.

(K) Insurance and participating investment contract liabilities**Claims**

Long-term business claims reflect the cost of all claims arising during the year, including claims handling costs, as well as policyholder bonuses accrued in anticipation of bonus declarations.

General insurance and health claims incurred include all losses occurring during the year, whether reported or not, related handling costs, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years.

Claims handling costs include internal and external costs incurred in connection with the negotiation and settlement of claims. Internal costs include all direct expenses of the claims

department and any part of the general administrative costs directly attributable to the claims function.

Long-term business provisions

Under current IFRS requirements, insurance and participating investment contract liabilities are measured using accounting policies consistent with those adopted previously under existing accounting practices, with the exception of liabilities remeasured to reflect current market interest rates to be consistent with the value of the backing assets, and those relating to UK with-profit and non-profit contracts. For liabilities relating to UK with-profit contracts, the Group has adopted FRS 27, Life Assurance, as described in policy F above, in addition to the requirements of IFRS.

In the United States, shadow adjustments are made to the liabilities or related deferred acquisition costs and are recognised directly in other comprehensive income. This means that the measurement of these items is adjusted for unrealised gains or losses on the backing assets such as AFS financial investments (see accounting policy S), that are recognised directly in other comprehensive income, in the same way as if those gains or losses had been realised.

The long-term business provisions are calculated separately for each life operation, based either on local regulatory requirements or existing local GAAP at the later of the date of transition to IFRS or the date of the acquisition of the entity, and actuarial principles consistent with those applied in the UK. Each calculation represents a determination within a range of possible outcomes, where the assumptions used in the calculations depend on the circumstances prevailing in each life operation. The principal assumptions are disclosed in note 39(b). For liabilities of the UK with-profit funds, FRS 27 requires liabilities to be calculated as the realistic basis liabilities as set out by the UK's Financial Services Authority (FSA), adjusted to remove the shareholders' share of future bonuses. For UK non-profit insurance contracts, the Group applies the realistic regulatory basis as set out in the FSA Policy Statement 06/14, Prudential Changes for Insurers, where applicable.

Unallocated divisible surplus

In certain participating long-term insurance and investment business, the nature of the policy benefits is such that the division between shareholder reserves and policyholder liabilities is uncertain. Amounts whose allocation to either policyholders or shareholders has not been determined by the end of the financial year are held within liabilities as an unallocated divisible surplus.

If the aggregate carrying value of liabilities for a particular participating business fund is in excess of the aggregate carrying value of its assets, then the difference is held as a negative unallocated divisible surplus balance, subject to recoverability from margins in that fund's participating business. Any excess of this difference over the recoverable amount is charged to net income in the reporting period.

Embedded derivatives

Embedded derivatives that meet the definition of an insurance contract or correspond to options to surrender insurance contracts for a set amount (or based on a fixed amount and an interest rate) are not separately measured. All other embedded derivatives are separated and measured at fair value if they are not considered as closely related to the host insurance contract or do not meet the definition of an insurance contract. Fair value reflects own credit risk to the extent the embedded derivative is not fully collateralised.

Liability adequacy

At each reporting date, an assessment is made of whether the recognised long-term business provisions are adequate, using current estimates of future cash flows. If that assessment shows that the carrying amount of the liabilities (less related assets) is insufficient in light of the estimated future cash flows, the

deficiency is recognised in the income statement by setting up an additional provision in the statement of financial position.

General insurance and health provisions

Outstanding claims provisions

General insurance and health outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the statement of financial position date, whether reported or not, together with related claims handling costs. Significant delays are experienced in the notification and settlement of certain types of general insurance claims, particularly in respect of liability business, including environmental and pollution exposures, the ultimate cost of which cannot be known with certainty at the statement of financial position date. Any estimate represents a determination within a range of possible outcomes. Further details of estimation techniques are given in note 39(c).

Provisions for latent claims are discounted, using rates based on the relevant swap curve, in the relevant currency at the reporting date, having regard to the expected settlement dates of the claims. The discount rate is set at the start of the accounting period with any change in rates between the start and end of the accounting period being reflected below operating profit as an economic assumption change. The range of discount rates used is described in note 39(c). Outstanding claims provisions are valued net of an allowance for expected future recoveries. Recoveries include non-insurance assets that have been acquired by exercising rights to salvage and subrogation under the terms of insurance contracts.

Provision for unearned premiums

The proportion of written premiums, gross of commission payable to intermediaries, attributable to subsequent periods is deferred as a provision for unearned premiums. The change in this provision is taken to the income statement as recognition of revenue over the period of risk.

Liability adequacy

At each reporting date, the Group reviews its unexpired risks and carries out a liability adequacy test for any overall excess of expected claims and deferred acquisition costs over unearned premiums, using the current estimates of future cash flows under its contracts after taking account of the investment return expected to arise on assets relating to the relevant general business provisions. If these estimates show that the carrying amount of its insurance liabilities (less related deferred acquisition costs) is insufficient in light of the estimated future cash flows, the deficiency is recognised in the income statement by setting up a provision in the statement of financial position.

Other assessments and levies

The Group is subject to various periodic insurance-related assessments or guarantee fund levies. Related provisions are established where there is a present obligation (legal or constructive) as a result of a past event. Such amounts are not included in insurance liabilities but are included under 'Provisions' in the statement of financial position.

(L) Non-participating investment contract liabilities

Claims

For non-participating investment contracts with an account balance, claims reflect the excess of amounts paid over the account balance released.

Contract liabilities

Deposits collected under non-participating investment contracts are not accounted for through the income statement, except for the investment income attributable to those contracts, but are

accounted for directly through the statement of financial position as an adjustment to the investment contract liability.

The majority of the Group's contracts classified as non-participating investment contracts are unit-linked contracts and are measured at fair value. Certain liabilities for non-linked non-participating contracts are measured at amortised cost.

The fair value liability is determined in accordance with IAS 39, using a valuation technique to provide a reliable estimate of the amount for which the liability could be settled between knowledgeable willing parties in an arm's length transaction, subject to a minimum equal to the surrender value. For unit-linked contracts, the fair value liability is equal to the current unit fund value, plus additional non-unit reserves if required based on a discounted cash flow analysis. For non-linked contracts, the fair value liability is based on a discounted cash flow analysis, with allowance for risk calibrated to match the market price for risk.

Amortised cost is calculated as the fair value of consideration received at the date of initial recognition, less the net effect of payments such as transaction costs and front-end fees, plus or minus the cumulative amortisation (using the effective interest rate method) of any difference between that initial amount and the maturity value, and less any write-down for surrender payments. The effective interest rate is the one that equates the discounted cash payments to the initial amount. At each reporting date, the amortised cost liability is determined as the value of future best estimate cash flows discounted at the effective interest rate.

(M) Reinsurance

The Group assumes and cedes reinsurance in the normal course of business, with retention limits varying by line of business. Premiums on reinsurance assumed are recognised as revenue in the same manner as they would be if the reinsurance were considered direct business, taking into account the product classification of the reinsured business. The cost of reinsurance related to long-duration contracts is accounted for over the life of the underlying reinsured policies, using assumptions consistent with those used to account for these policies.

Where general insurance liabilities are discounted, any corresponding reinsurance assets are also discounted using consistent assumptions.

Gains or losses on buying retroactive reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised. Premiums ceded and claims reimbursed are presented on a gross basis in the consolidated income statement and statement of financial position as appropriate.

Reinsurance assets primarily include balances due from both insurance and reinsurance companies for ceded insurance and investment contract liabilities. This includes balances in respect of investment contracts which are legally reinsurance contracts but do not meet the definition of a reinsurance contract under IFRS. Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying contract liabilities, outstanding claims provisions or settled claims associated with the reinsured policies and in accordance with the relevant reinsurance contract.

Reinsurance of non-participating investment contracts and reinsurance contracts that principally transfer financial risk are accounted for directly through the statement of financial position. A deposit asset or liability is recognised, based on the consideration paid or received less any explicitly identified premiums or fees to be retained by the reinsured. These deposit assets or liabilities are shown within reinsurance assets in the consolidated statement of financial position.

If a reinsurance asset is impaired, the Group reduces the carrying amount accordingly and recognises that impairment loss in the income statement. A reinsurance asset is impaired if there is objective evidence, as a result of an event that occurred after initial recognition of the reinsurance asset, that the Group may not receive all amounts due to it under the terms of the contract,

and the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer.

(N) Goodwill, AVIF and intangible assets

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary, associate or joint venture at the date of acquisition. Goodwill on acquisitions prior to 1 January 2004 (the date of transition to IFRS) is carried at its book value (original cost less cumulative amortisation) on that date, less any impairment subsequently incurred. Goodwill arising before 1 January 1998 was eliminated against reserves and has not been reinstated. Goodwill arising on the Group's investments in subsidiaries since that date is shown as a separate asset, whilst that on associates and joint ventures is included within the carrying value of those investments.

Acquired value of in-force business (AVIF)

The present value of future profits on a portfolio of long-term insurance and investment contracts, acquired either directly or through the purchase of a subsidiary, is recognised as an asset. If the AVIF results from the acquisition of an investment in a joint venture or an associate, it is held within the carrying amount of that investment. In all cases, the AVIF is amortised over the useful lifetime of the related contracts in the portfolio on a systematic basis. The rate of amortisation is chosen by considering the profile of the additional value of in-force business acquired and the expected depletion in its value. The value of the acquired in-force long-term business is reviewed annually for any impairment in value and any reductions are charged as expenses in the income statement.

Intangible assets

Intangibles consist primarily of contractual relationships such as access to distribution networks and customer lists. The economic lives of these are determined by considering relevant factors such as usage of the asset, typical product life cycles, potential obsolescence, maintenance costs, the stability of the industry, competitive position and the period of control over the assets. These intangibles are amortised over their useful lives, which range from five to 30 years, using the straight-line method.

The amortisation charge for the year is included in the income statement under 'Other operating expenses'. For intangibles with finite lives, impairment charges will be recognised in the income statement where evidence of such impairment is observed. Intangibles with indefinite lives are subject to regular impairment testing, as described below.

Impairment testing

For impairment testing, goodwill and intangibles with indefinite useful lives have been allocated to cash-generating units. The carrying amount of goodwill and intangible assets with indefinite useful lives is reviewed at least annually or when circumstances or events indicate there may be uncertainty over this value. Goodwill and indefinite life intangibles are written down for impairment where the recoverable amount is insufficient to support its carrying value. Further details on goodwill allocation and impairment testing are given in note 16.

(O) Property and equipment

Owner-occupied properties are carried at their revalued amounts, which are supported by market evidence, and movements are recognised in other comprehensive income and taken to a separate reserve within equity. When such properties are sold, the accumulated revaluation surpluses are transferred from this reserve to retained earnings. These properties are depreciated down to their estimated residual values over their useful lives. All other items classed as property and equipment within the

statement of financial position are carried at historical cost less accumulated depreciation.

Investment properties under construction are included within property and equipment until completion, and are stated at cost less any provision for impairment in their values until construction is completed or fair value becomes reliably measurable.

Depreciation is calculated on the straight-line method to write-down the cost of other assets to their residual values over their estimated useful lives as follows:

■ Properties under construction	No depreciation
■ Owner-occupied properties, and related mechanical and electrical equipment	25 years
■ Motor vehicles	Three years, or lease term if longer
■ Computer equipment	Three to five years
■ Other assets	Three to five years

The assets' residual values, useful lives and method of depreciation are reviewed regularly, and at least at each financial year end, and adjusted if appropriate. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal of property and equipment are determined by reference to their carrying amount.

Borrowing costs directly attributable to the acquisition and construction of property and equipment are capitalised. All repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the most recently assessed standard of performance of the existing asset will flow to the Group and the renovation replaces an identifiable part of the asset. Major renovations are depreciated over the remaining useful life of the related asset.

(P) Investment property

Investment property is held for long-term rental yields and is not occupied by the Group. Completed investment property is stated at its fair value, which is supported by market evidence, as assessed by qualified external valuers or by local qualified staff of the Group in overseas operations. Changes in fair values are recorded in the income statement in net investment income.

As described in accounting policy O above, investment properties under construction are included within property and equipment, and are stated at cost less any impairment in their values until construction is completed or fair value becomes reliably measurable.

(Q) Impairment of non-financial assets

Property and equipment and other non-financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows. Non-financial assets except goodwill which have suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

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

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

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

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

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

(S) Financial investments

The Group classifies its investments as either financial assets at fair value through profit or loss (FV) or financial assets available for sale (AFS). The classification depends on the purpose for which the investments were acquired, and is determined by local management at initial recognition. The FV category has two subcategories – those that meet the definition as being held for trading and those the Group chooses to designate as FV (referred to in this accounting policy as 'other than trading').

In general, the other than trading category is used as, in most cases, the Group's investment or risk management strategy is to manage its financial investments on a fair value basis. Debt securities and equity securities, which the Group buys with the intention to resell in the short term, are classified as trading, as are non-hedge derivatives (see accounting policy T below). The AFS category is used where the relevant long-term business liability (including shareholders' funds) is passively managed, as well as in certain fund management and non-insurance operations.

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

Investments carried at fair value are measured using a fair value hierarchy, described in note 22, with values based on quoted bid prices or amounts derived from cash flow models. Fair values for unlisted equity securities are estimated using applicable price/earnings or price/cash flow ratios refined to reflect the specific circumstances of the issuer.

When securities classified as AFS are sold or impaired, the accumulated fair value adjustments are transferred out of the investment valuation reserve to the income statement with a corresponding movement through other comprehensive income.

Impairment

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

AFS debt securities: An AFS debt security is impaired if there is objective evidence that a loss event has occurred which has impaired the expected cash flows, i.e. where all amounts due according to the contractual terms of the security are not considered collectible. An impairment charge, measured as the difference between the security's fair value and amortised cost, is recognised when the issuer is known to be either in default or in financial difficulty. Determining when an issuer is in financial difficulty requires the use of judgement, and we consider a number of factors including industry risk factors, financial condition, liquidity position and near-term prospects of the issuer, credit rating declines and a breach of contract. A decline in fair value below amortised cost due to changes in risk-free interest rates does not necessarily represent objective evidence of a loss event.

For securities identified as being impaired, the cumulative unrealised net loss previously recognised within the investment valuation reserve is transferred to realised losses for the year, with a corresponding movement through other comprehensive income. Any subsequent increase in fair value of these impaired securities is recognised in other comprehensive income and recorded in the investment valuation reserve unless this increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement. In such an event, the reversal of the impairment loss is recognised as a gain in the income statement.

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

For securities identified as being impaired, the cumulative unrealised net loss previously recognised within the investment valuation reserve is transferred to realised losses for the year with a corresponding movement through other comprehensive income. Any subsequent increase in fair value of these impaired securities is recognised in other comprehensive income and recorded in the investment valuation reserve.

Reversals of impairments on any of these assets are only recognised where the decrease in the impairment can be objectively related to an event occurring after the write-down (such as an improvement in the debtor's credit rating), and are not recognised in respect of equity instruments.

(T) Derivative financial instruments and hedging

Derivative financial instruments include foreign exchange contracts, interest rate futures, currency and interest rate swaps, currency and interest rate options (both written and purchased) and other financial instruments that derive their value mainly from underlying interest rates, foreign exchange rates, credit indices, commodity values or equity instruments.

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

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

The notional or contractual amounts associated with derivative financial instruments are not recorded as assets or liabilities on the statement of financial position as they do not represent the fair value of these transactions. These amounts are disclosed in note 57.

The Group has collateral agreements in place between the individual Group entities and relevant counterparties. Accounting policy V below covers collateral, both received and pledged, in respect of these derivatives.

Interest rate and currency swaps

Interest rate swaps are contractual agreements between two parties to exchange periodic payments in the same currency, each of which is computed on a different interest rate basis, on a specified notional amount. Most interest rate swaps involve the net exchange of payments calculated as the difference between the fixed and floating rate interest payments. Currency swaps, in their simplest form, are contractual agreements that involve the exchange of both periodic and final amounts in two different currencies. Both types of swap contracts may include the net exchange of principal. Exposure to gain or loss on these contracts will increase or decrease over their respective lives as a function of maturity dates, interest and foreign exchange rates, and the timing of payments.

Interest rate futures, forwards and options contracts

Interest rate futures are exchange-traded instruments and represent commitments to purchase or sell a designated security or money market instrument at a specified future date and price. Interest rate forward agreements are OTC contracts in which two parties agree on an interest rate and other terms that will become a reference point in determining, in concert with an agreed notional principal amount, a net payment to be made by one party to the other, depending what rate in fact prevails at a future point in time. Interest rate options, which consist primarily of caps and floors, are interest rate protection instruments that involve

the potential obligation of the seller to pay the buyer an interest rate differential in exchange for a premium paid by the buyer. This differential represents the difference between current rate and an agreed rate applied to a notional amount. Exposure to gain or loss on all interest rate contracts will increase or decrease over their respective lives as interest rates fluctuate.

Foreign exchange contracts

Foreign exchange contracts, which include spot, forward and futures contracts, represent agreements to exchange the currency of one country for the currency of another country at an agreed price and settlement date. Foreign exchange option contracts are similar to interest rate option contracts, except that they are based on currencies, rather than interest rates.

Exposure to gain or loss on these contracts will increase or decrease over their respective lives as currency exchange and interest rates fluctuate.

Derivative instruments for hedging

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

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

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

Changes in the fair value of derivatives that are designated and qualify as net investment or cash flow hedges, and that prove to be highly effective in relation to the hedged risk, are recognised in other comprehensive income and a separate reserve within equity. Gains and losses accumulated in this reserve are included in the income statement on disposal of the relevant investment or occurrence of the cash flow as appropriate. Changes in the fair value of derivatives that are designated and qualify as fair value hedges against assets carried at amortised cost are adjusted against the carrying value of the hedged asset to the extent those changes relate to the hedged risk. This adjustment is then amortised to the income statement over the anticipated remaining life of the hedged instrument. Where the hedge is against the value of AFS securities, changes in its value are recognised in the income statement, partially or wholly offset by a transfer from the investment valuation reserve for the change in value of the hedged item.

The Group discontinues hedge accounting if the hedging instrument expires, is sold, terminated or exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation.

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

(U) Loans

Loans with fixed maturities, including policyholder loans, mortgage loans on investment property, securitised mortgages and collateral loans, are recognised when cash is advanced to

borrowers. The majority of these loans are carried at their unpaid principal balances and adjusted for amortisation of premium or discount, non-refundable loan fees and related direct costs. These amounts are deferred and amortised over the life of the loan as an adjustment to loan yield using the effective interest rate method. Loans with indefinite future lives are carried at unpaid principal balances or cost.

For certain mortgage loans, the Group has taken advantage of the fair value option under IAS 39 to present the mortgages, associated borrowings and derivative financial instruments at fair value, since they are managed as a portfolio on a fair value basis. This presentation provides more relevant information and eliminates any accounting mismatch that would otherwise arise from using different measurement bases for these three items. The fair values of mortgages classified as FV are estimated using discounted cash flow forecasts, based on a risk-adjusted discount rate which reflects the risks associated with these products, calibrated using the margins available on new lending or with reference to the rates offered by competitors. They are revalued at each period end, with movements in their fair values being taken to the income statement.

At each reporting date, we review loans carried at amortised cost for objective evidence that they are impaired and uncollectable, either at the level of an individual security or collectively within a group of loans with similar credit risk characteristics. To the extent that a loan is uncollectable, it is written down as impaired to its recoverable amount, measured as the present value of expected future cash flows discounted at the original effective interest rate of the loan, taking into account the fair value of the underlying collateral. Subsequent recoveries in excess of the loan's written-down carrying value are credited to the income statement.

(V) Collateral

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

Collateral received in the form of cash, which is not legally segregated from the Group, is recognised as an asset in the statement of financial position with a corresponding liability for the repayment in financial liabilities (note 49). However, where the Group has a currently enforceable legal right of set-off, the collateral liability and associated derivative balances are shown net, in line with market practice. Non-cash collateral received is not recognised in the statement of financial position unless the Group either (a) sells or repledges these assets in the absence of default, at which point the obligation to return this collateral is recognised as a liability; or (b) the counterparty to the arrangement defaults, at which point the collateral is seized and recognised as an asset.

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

(W) Deferred acquisition costs and other assets

Costs relating to the acquisition of new business for insurance and participating investment contracts are deferred in line with existing local accounting practices, to the extent that they are expected to be recovered out of future margins in revenues on these contracts. For participating contracts written in the UK, acquisition costs are generally not deferred as the liability for

these contracts is calculated in accordance with the FSA's realistic capital regime and FRS 27. For non-participating investment and investment fund management contracts, incremental acquisition costs and sales enhancements that are directly attributable to securing an investment management service are also deferred.

Where such business is reinsured, an appropriate proportion of the deferred acquisition costs is attributed to the reinsurer, and is treated as a separate liability.

Long-term business deferred acquisition costs are amortised systematically over a period no longer than that in which they are expected to be recoverable out of these future margins. Deferrable acquisition costs for non-participating investment and investment fund management contracts are amortised over the period in which the service is provided. General insurance and health deferred acquisition costs are amortised over the period in which the related revenues are earned. The reinsurers' share of deferred acquisition costs is amortised in the same manner as the underlying asset.

Deferred acquisition costs are reviewed by category of business at the end of each reporting period and are written-off where they are no longer considered to be recoverable.

Other assets include vehicles which are subject to repurchase agreements and inventories of vehicle parts. The former are carried at the lower of their agreed repurchase price or net realisable value, whilst the latter are carried at the lower of cost and net realisable value, where cost is arrived at on the weighted average cost formula or 'first in first out' (FIFO) basis. Provision is made against inventories which are obsolete or surplus to requirements.

(X) Statement of cash flows

Cash and cash equivalents

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

For the purposes of the statement of cash flows, cash and cash equivalents also include bank overdrafts, which are included in payables and other financial liabilities on the statement of financial position.

Operating cash flows

Purchases and sales of investment property, loans and financial investments are included within operating cash flows as the purchases are funded from cash flows associated with the origination of insurance and investment contracts, net of payments of related benefits and claims.

(Y) Leases

Leases, where a significant portion of the risks and rewards of ownership is retained by the lessor, are classified as operating leases. Where the Group is the lessee, payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the term of the relevant leases.

Where the Group is the lessor, lease income from operating leases is recognised in the income statement on a straight-line basis over the lease term.

When assets are subject to finance leases, the present value of the lease payments, together with any unguaranteed residual value, is recognised as a receivable. The Group has not entered into any material finance lease arrangements either as lessor or lessee.

(Z) Provisions and contingent liabilities

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more probable than not that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognised for future operating losses.

Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

The Group recognises a provision for onerous contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract. Contingent liabilities are disclosed if there is a possible future obligation as a result of a past event, or if there is a present obligation as a result of a past event but either a payment is not probable or the amount cannot be reasonably estimated.

(AA) Employee benefits

Annual leave and long service leave

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long service leave as a result of services rendered by employees up to the statement of financial position date.

Pension obligations

The Group operates a large number of pension schemes, whose members receive benefits on either a defined benefit basis (generally related to a member's final salary and length of service) or a defined contribution basis (generally related to the amount invested, investment return and annuity rates), the assets of which are generally held in separate trustee-administered funds. The pension plans are generally funded by payments from employees and the relevant Group companies.

For defined benefit plans, the pension costs are assessed using the projected unit credit method. Under this method, the cost of providing pensions is charged to the income statement so as to spread the regular cost over the service lives of employees. The pension obligation is measured as the present value of the estimated future cash outflows, using a discount rate based on market yields for high-quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related pension liability. The resulting pension scheme surplus or deficit appears as an asset or liability in the consolidated statement of financial position.

Costs charged to the income statement comprise the current service cost (the increase in pension obligation resulting from employees' service in the current period, together with the schemes' administration expenses), past service cost (resulting from changes to benefits with respect to previous years' service), and gains or losses on curtailment (when the employer materially reduces the number of employees covered by the scheme) or on settlements (when a scheme's obligations are transferred outside the Group). In addition, the difference between the expected return on scheme assets, less investment expenses, and the interest cost of unwinding the discount on the scheme liabilities (to reflect the benefits being one period closer to being paid out) is credited to investment income. All actuarial gains and losses, being the difference between the actual and expected returns on scheme assets, changes in assumptions underlying the liability calculations and experience gains or losses on the assumptions made at the beginning of the period, are recognised immediately in other comprehensive income.

For defined contribution plans, the Group pays contributions to publicly or privately administered pension plans. Once the contributions have been paid, the Group, as employer, has no further payment obligations. The Group's contributions are charged to the income statement in the year to which they relate and are included in staff costs.

Other post-employment obligations

Some Group companies provide post-employment healthcare or other benefits to their retirees. The entitlement to these benefits is usually based on the employee remaining in service up to retirement age and the completion of a minimum service period. Unlike the pension schemes, no assets are set aside in separate funds to provide for the future liability but none of these schemes is material to the Group. The costs of the Canadian scheme are included within those for the defined benefit pension schemes in that country. For such schemes in other countries, provisions are calculated in line with local regulations, with movements being charged to the income statement within staff costs.

Equity compensation plans

The Group offers share award and option plans over the Company's ordinary shares for certain employees, including a Save As You Earn plan (SAYE plan), details of which are given in the Directors' Remuneration Report and in note 30.

The Group accounts for options and awards under equity compensation plans, which were granted after 7 November 2002, until such time as they are fully vested, using the fair value based method of accounting (the 'fair value method'). Under this method, the cost of providing equity compensation plans is based on the fair value of the share awards or option plans at date of grant, which is recognised in the income statement over the expected vesting period of the related employees and credited to the equity compensation reserve, part of shareholders' funds. In certain jurisdictions, awards must be settled in cash instead of shares, and the credit is taken to liabilities rather than reserves. The fair value of these cash-settled awards is recalculated each year, with the income statement charge and liability being adjusted accordingly.

As described in accounting policy AD below, shares purchased by employee share trusts to fund these awards are shown as a deduction from shareholders' funds at their original cost.

When the options are exercised and new shares are issued, the proceeds received, net of any transaction costs, are credited to share capital (par value) and the balance to share premium. Where the shares are already held by employee trusts, the net proceeds are credited against the cost of these shares, with the difference between cost and proceeds being taken to retained earnings. In both cases, the relevant amount in the equity compensation reserve is then credited to retained earnings.

(AB) Income taxes

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

Provision is made for deferred tax liabilities, or credit taken for deferred tax assets, using the liability method, on all material temporary differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

The principal temporary differences arise from depreciation of property and equipment, revaluation of certain financial assets and liabilities including derivative contracts, provisions for pensions and other post-retirement benefits and tax losses carried forward; and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base. The rates enacted or substantively enacted at the statement of financial position date are used to determine the deferred tax.

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

Deferred tax is provided on temporary differences arising from investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future.

Deferred taxes are not provided in respect of temporary differences arising from the initial recognition of goodwill, or from goodwill for which amortisation is not deductible for tax purposes, or from the initial recognition of an asset or liability in a transaction which is not a business combination and affects neither accounting profit nor taxable profit or loss at the time of the transaction.

Current and deferred tax relating to items recognised in other comprehensive income and directly in equity are similarly recognised in other comprehensive income and directly in equity respectively. Deferred tax related to fair value re-measurement of available for sale investments, owner-occupied properties and other amounts charged or credited directly to other comprehensive income is recognised in the statement of financial position as a deferred tax asset or liability. Current tax on interest paid on direct capital instruments and fixed rate tier 1 notes is credited directly in equity.

In addition to paying tax on shareholders' profits, the Group's life businesses in the UK, Ireland and Singapore pay tax on policyholders' investment returns ('policyholder tax') on certain products at policyholder tax rates. Policyholder tax is accounted for as an income tax and is included in the total tax expense. The Group has decided to show separately the amounts of policyholder tax to provide a more meaningful measure of the tax the Group pays on its profits. In the pro forma reconciliations, operating profit has been calculated after charging policyholder tax.

(AC) Borrowings

Borrowings are classified as being for either core structural or operational purposes. They are recognised initially at their issue proceeds less transaction costs incurred. Subsequently, most borrowings are stated at amortised cost, and any difference between net proceeds and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest rate method. All borrowing costs are expensed as they are incurred except where they are directly attributable to the acquisition or construction of property and equipment as described in accounting policy O above.

Where loan notes have been issued in connection with certain securitised mortgage loans, the Group has taken advantage of the revised fair value option under IAS 39 to present the mortgages, associated liabilities and derivative financial instruments at fair value, since they are managed as a portfolio on a fair value basis. This presentation provides more relevant information and eliminates any accounting mismatch which would otherwise arise from using different measurement bases for these three items.

(AD) Share capital and treasury shares

Equity instruments

An equity instrument is a contract that evidences a residual interest in the assets of an entity after deducting all its liabilities. Accordingly, a financial instrument is treated as equity if:

- (i) there is no contractual obligation to deliver cash or other financial assets or to exchange financial assets or liabilities on terms that may be unfavourable; and

- (ii) the instrument is a non-derivative that contains no contractual obligation to deliver a variable number of shares or is a derivative that will be settled only by the Group exchanging a fixed amount of cash or other assets for a fixed number of the Group's own equity instruments.

Share issue costs

Incremental external costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds of the issue and disclosed where material.

Dividends

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

Treasury shares

Where the Company or its subsidiaries purchase the Company's share capital or obtain rights to purchase its share capital, the consideration paid (including any attributable transaction costs net of income taxes) is shown as a deduction from total shareholders' equity. The Group's only such holding comprises shares purchased by employee trusts to fund certain awards under the equity compensation plans described in accounting policy AA above. Gains and losses on sales of own shares are charged or credited to the treasury share account in equity.

(AE) Fiduciary activities

Assets and income arising from fiduciary activities, together with related undertakings to return such assets to customers, are excluded from these financial statements where the Group has no contractual rights in the assets and acts in a fiduciary capacity such as nominee, trustee or agent.

(AF) (Loss)/earnings per share

Basic losses/earnings per share is calculated by dividing net income available to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding the weighted average number of ordinary shares purchased by the Group and held as Treasury shares.

Earnings per share has also been calculated on the adjusted operating profit before impairment of goodwill and other adjusting items, after tax, attributable to ordinary shareholders, as the directors believe this figure provides a better indication of operating performance. Details are given in note 14.

For the diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares, such as convertible debt and share options granted to employees.

Potential or contingent share issuances are treated as dilutive when their conversion to shares would decrease net (losses) earnings per share.

(AG) Operations held for sale

Assets and liabilities held for disposal as part of operations which are held for sale are shown separately in the consolidated statement of financial position. Operations held for sale are recorded at the lower of their carrying amount and their fair value less the estimated selling costs.

Consolidated financial statements

Consolidated income statement

For the year ended 31 December 2012

	Note	2012 £m		2011 £m	
		Continuing operations	Discontinued operations ¹	Continuing operations	Discontinued Operations ¹
				Restated ²	
Income	5				
Gross written premiums		22,744	3,796	26,255	5,863
Premiums ceded to reinsurers		(1,571)	(207)	(1,548)	(200)
Premiums written net of reinsurance		21,173	3,589	24,707	5,663
Net change in provision for unearned premiums		(16)	—	(236)	(56)
Net earned premiums	G	21,157	3,589	24,471	5,607
Fee and commission income	H & I	1,273	23	1,465	111
Net investment income	J	21,106	2,241	4,341	2,086
Share of (loss)/profit after tax of joint ventures and associates		(277)	—	(123)	28
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	3b	(164)	(2,359)	565	(32)
		43,095	3,494	30,719	7,800
Expenses	6				
Claims and benefits paid, net of recoveries from reinsurers		(23,601)	(2,721)	(24,380)	(4,029)
Change in insurance liabilities, net of reinsurance		(430)	(1,566)	(2,284)	(2,523)
Change in investment contract provisions		(4,450)	(77)	1,478	(180)
Change in unallocated divisible surplus		(6,316)	—	2,721	(19)
Fee and commission expense		(4,472)	(498)	(4,326)	(420)
Other expenses		(2,845)	(1,307)	(2,779)	(809)
Finance costs	7	(735)	(21)	(776)	(284)
		(42,849)	(6,190)	(30,346)	(8,264)
Profit/(loss) before tax		246	(2,696)	373	(464)
Tax attributable to policyholders' returns	13d	(221)	—	178	—
Profit/(loss) before tax attributable to shareholders' profits		25	(2,696)	551	(464)
Tax (expense)/credit	AB & 13	(448)	(152)	44	107
Less: tax attributable to policyholders' returns	13d	221	—	(178)	—
Tax attributable to shareholders' profits		(227)	(152)	(134)	107
(Loss)/profit after tax		(202)	(2,848)	417	(357)
(Loss) from discontinued operations		(2,848)		(357)	
(Loss)/profit for the year		(3,050)		60	
Attributable to:					
Equity shareholders of Aviva plc		(3,218)		225	
Non-controlling interests	37	168		(165)	
(Loss)/profit for the year		(3,050)		60	
(Loss)/earnings per share	AF & 14				
Basic (pence per share)		(113.1)p		5.8p	
Diluted (pence per share)		(113.1)p		5.7p	
Continuing operations – Basic (pence per share)		(15.2)p		11.1p	
Continuing operations – Diluted (pence per share)		(15.2)p		10.9p	

¹ Discontinued operations in the current period represents the results of the US life and related internal asset management businesses (US Life), and in the prior period represents the results of US Life and Delta Lloyd to 6 May 2011.

² Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

Consolidated statement of comprehensive income

For the year ended 31 December 2012

	Note	2012 £m	2011 £m
(Loss)/profit for the year from continuing operations		(202)	417
(Loss) for the year from discontinued operations¹		(2,848)	(357)
Total (loss)/profit for the year		(3,050)	60
Other comprehensive income/(expense) from continuing operations:			
Investments classified as available for sale			
Fair value gains/(losses)		27	(5)
Fair value gains transferred to profit on disposals		1	1
Impairment losses on assets previously revalued through other comprehensive income now taken to the income statement		—	2
Owner-occupied properties – fair value (losses)/gains		(3)	2
Share of other comprehensive income of joint ventures and associates		14	(134)
Actuarial (losses)/gains on pension schemes	47e(iv)	(830)	996
Other pension scheme movements		—	(22)
Foreign exchange rate movements		(200)	(284)
Aggregate tax effect – shareholder tax	13b	163	(160)
Other comprehensive (expense)/income, net of tax from continuing operations		(828)	396
Other comprehensive income, net of tax from discontinued operations¹	3c(i)	68	300
Total other comprehensive income, net of tax		(760)	696
Total comprehensive (expense)/income for the year from continuing operations		(1,030)	813
Total comprehensive (expense)/income for the year from discontinued operations¹		(2,780)	(57)
Total comprehensive income for the year		(3,810)	756
Attributable to:			
Equity shareholders of Aviva plc		(3,942)	923
Non-controlling interests		132	(167)
		(3,810)	756

¹ Discontinued operations in the current period represents the results of the US life and related internal asset management businesses (US Life), and in the prior period represents the results of US Life and Delta Lloyd to 6 May 2011.

The accounting policies (identified alphabetically) on pages 148 to 159 and notes (identified numerically) on pages 168 to 266 are an integral part of these financial statements.

Reconciliation of Group operating profit to (loss)/profit for the year

For the year ended 31 December 2012

	2012 £m			2011 £m		
Note	Continuing operations	Discontinued operations ¹	Total	Continuing operations	Discontinued operations ¹	Total
Operating profit before tax attributable to shareholders' profits						
Long-term business	1,831	200	2,031	1,926	382	2,308
General insurance and health	893	—	893	935	1	936
Fund management	51	55	106	61	49	110
Other:						
Other operations	(204)	(4)	(208)	(204)	(5)	(209)
Corporate centre	(136)	—	(136)	(138)	—	(138)
Group debt costs and other interest	(659)	(12)	(671)	(648)	(13)	(661)
Operating profit before tax attributable to shareholders' profits (excluding Delta Lloyd as an associate)	1,776	239	2,015	1,932	414	2,346
Share of operating profit (before tax) of Delta Lloyd as an associate	112	—	112	157	—	157
Operating profit before tax attributable to shareholders' profits	1,888	239	2,127	2,089	414	2,503
Integration and restructuring costs	6 (461)	(7)	(468)	(261)	(7)	(268)
Operating profit before tax attributable to shareholders' profits after integration and restructuring costs	1,427	232	1,659	1,828	407	2,235
Adjusted for the following:						
Investment return variances and economic assumption changes on long-term business	8 (620)	342	(278)	(897)	(719)	(1,616)
Short-term fluctuation in return on investments on non-long-term business	9a 7	—	7	(266)	(60)	(326)
Economic assumption changes on general insurance and health business	9a (21)	—	(21)	(90)	—	(90)
Impairment of goodwill, associates and joint ventures and other amounts expensed	16a, 18, 19a (60)	(782)	(842)	(392)	—	(392)
Amortisation and impairment of intangibles	(128)	(129)	(257)	(116)	(60)	(176)
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	3b (164)	(2,359)	(2,523)	565	(32)	533
Exceptional items	6 —	—	—	(57)	—	(57)
Non-operating items before tax (excluding Delta Lloyd as an associate and integration and restructuring costs)	(986)	(2,928)	(3,914)	(1,253)	(871)	(2,124)
Share of Delta Lloyd's non-operating items (before tax) as an associate	(523)	—	(523)	10	—	10
Non-operating items before tax	(1,509)	(2,928)	(4,437)	(1,243)	(871)	(2,114)
Share of Delta Lloyd's tax expense, as an associate	107	—	107	(34)	—	(34)
Profit/(loss) before tax attributable to shareholders' profits	25	(2,696)	(2,671)	551	(464)	87
Tax on operating profit	14a(i) (465)	(78)	(543)	(487)	(163)	(650)
Tax on other activities	14a(i) 238	(74)	164	353	270	623
			(227)	(134)	107	(27)
(Loss)/profit for the year	(202)	(2,848)	(3,050)	417	(357)	60

¹ Discontinued operations in the current period represents the results of the United States and prior period represents the results of the United States and Delta Lloyd to the 6 May 2011.

The accounting policies (identified alphabetically) on pages 148 to 159 and notes (identified numerically) on pages 168 to 266 are an integral part of these financial statements.

Reconciliation of Group operating profit to (loss)/profit for the year continued

Operating profit can be further analysed into the following segments (details of segments can be found in note 4):

	Long-term business £m	General insurance and health £m	Fund manage- ment £m	Other operations £m	Total £m
Year ended 31 December 2012					
United Kingdom & Ireland	892	491	11	(54)	1,340
France	335	95	—	(8)	422
Canada	—	276	—	—	276
Italy, Spain and other	371	53	—	(10)	414
Higher Growth Markets	230	(22)	1	(7)	202
Aviva Investors	3	—	39	—	42
Other group activities	—	—	—	(125)	(125)
	1,831	893	51	(204)	2,571
Corporate centre					(136)
Group debt costs and other interest					(659)
Share of operating profit (before tax) of Delta Lloyd as an associate					112
Total – continuing operations					1,888
Total – discontinued operations					239
					2,127
Year ended 31 December 2011					
United Kingdom & Ireland	964	564	11	(30)	1,509
France	323	144	—	4	471
Canada	—	254	—	—	254
Italy, Spain and other	357	(2)	—	(21)	334
Higher Growth Markets	279	(25)	—	(25)	229
Aviva Investors	3	—	50	—	53
Other group activities	—	—	—	(132)	(132)
	1,926	935	61	(204)	2,718
Corporate centre					(138)
Group debt costs and other interest					(648)
Share of operating profit (before tax) of Delta Lloyd as an associate					157
Total – continuing operations					2,089
Total – discontinued operations					414
					2,503

The accounting policies (identified alphabetically) on pages 148 to 159 and notes (identified numerically) on pages 168 to 266 are an integral part of these financial statements.

Consolidated statement of changes in equity

For the year ended 31 December 2012

	Ordinary share capital £m	Preference share capital £m	Share premium £m	Merger reserve £m	Shares held by employee trusts £m	Currency translation reserve £m	Owner-occupied properties reserve £m	Investment valuation reserve £m	Hedging instruments reserve £m	Equity compensation reserve £m	Retained earnings £m	Equity attributable to shareholders of Aviva plc £m	DCI and Fixed rate tier 1 notes £m	Non controlling interests £m	Total equity £m
Balance at 1 January	726	200	1,173	3,271	(43)	1,530	79	530	(663)	86	5,954	12,843	990	1,530	15,363
(Loss)/profit for the year	—	—	—	—	—	—	—	—	—	—	(3,218)	(3,218)	—	168	(3,050)
Other comprehensive (expense)/income	—	—	—	—	—	(349)	(2)	229	74	—	(676)	(724)	—	(36)	(760)
Total comprehensive (expense)/income for the year	—	—	—	—	—	(349)	(2)	229	74	—	(3,894)	(3,942)	—	132	(3,810)
Dividends and appropriations	—	—	—	—	—	—	—	—	—	—	(847)	(847)	—	—	(847)
Shares issued in lieu of dividends	9	—	(9)	—	—	—	—	—	—	—	127	127	—	—	127
Capital contributions from non-controlling interests	—	—	—	—	—	—	—	—	—	—	—	—	—	20	20
Non-controlling interests share of dividends declared in the year	—	—	—	—	—	—	—	—	—	—	—	—	—	(102)	(102)
Transfer to profit on disposal of subsidiaries, joint ventures and associates	—	—	—	—	—	91	—	96	—	—	—	187	—	—	187
Changes in non-controlling interests in existing subsidiaries	—	—	—	—	—	—	—	—	—	—	—	—	—	(6)	(6)
Shares acquired by employee trusts	—	—	—	—	(33)	—	—	—	—	—	—	(33)	—	—	(33)
Shares distributed by employee trusts	—	—	—	—	44	—	—	—	—	—	(36)	8	—	—	8
Reserves credit for equity compensation plans	—	—	—	—	—	—	—	—	—	42	—	42	—	—	42
Shares issued under equity compensation plans	1	—	1	—	—	—	—	—	—	(68)	67	1	—	—	1
Aggregate tax effect – shareholder tax	—	—	—	—	—	—	—	—	—	—	18	18	—	—	18
Issue of fixed rate tier 1 notes	—	—	—	—	—	—	—	—	—	—	—	—	392	—	392
Balance at 31 December	736	200	1,165	3,271	(32)	1,272	77	855	(589)	60	1,389	8,404	1,382	1,574	11,360

The accounting policies (identified alphabetically) on pages 148 to 159 and notes (identified numerically) on pages 168 to 266 are an integral part of these financial statements.

Consolidated statement of changes in equity continued

For the year ended 31 December 2011

	Ordinary share capital £m	Preference share capital £m	Share premium £m	Merger reserve £m	Shares held by employee trusts £m	Currency translation reserve £m	Owner-occupied properties reserve £m	Investment valuation reserve £m	Hedging instruments reserve £m	Equity compensation reserve £m	Retained earnings £m	Equity attributable to shareholders of Aviva plc £m	DCI and Fixed rate tier 1 notes £m	Non controlling interests £m	Total equity £m
Balance at 1 January	705	200	1,194	3,271	(32)	2,183	83	573	(693)	99	5,411	12,994	990	3,741	17,725
Profit/(loss) for the year	—	—	—	—	—	—	—	—	—	—	225	225	—	(165)	60
Other comprehensive (expense)/income	—	—	—	—	—	(165)	4	72	30	—	757	698	—	(2)	696
Total comprehensive (expense)/income for the year	—	—	—	—	—	(165)	4	72	30	—	982	923	—	(167)	756
Owner-occupied properties fair value gains transferred to retained earnings on disposals	—	—	—	—	—	—	(6)	—	—	—	6	—	—	—	—
Dividends and appropriations	—	—	—	—	—	—	—	—	—	—	(813)	(813)	—	—	(813)
Shares issued in lieu of dividends	21	—	(21)	—	—	—	—	—	—	—	307	307	—	—	307
Capital contributions from non-controlling	—	—	—	—	—	—	—	—	—	—	—	—	—	68	68
Effect of deconsolidation of Delta Lloyd	—	—	—	—	—	(485)	(2)	(115)	—	—	2	(600)	—	(1,770)	(2,370)
Non-controlling interests share of dividends declared in the year	—	—	—	—	—	—	—	—	—	—	—	—	—	(126)	(126)
Transfer to profit on disposal of subsidiaries, joint ventures and associates	—	—	—	—	—	(3)	—	—	—	—	—	(3)	—	—	(3)
Changes in non-controlling interests in existing subsidiaries	—	—	—	—	—	—	—	—	—	—	—	—	—	(11)	(11)
Shares acquired by employee trusts	—	—	—	—	(29)	—	—	—	—	—	—	(29)	—	—	(29)
Shares distributed by employee trusts	—	—	—	—	18	—	—	—	—	—	(18)	—	—	—	—
Reserves credit for equity compensation plans	—	—	—	—	—	—	—	—	—	48	—	48	—	—	48
Shares issued under equity compensation plans	—	—	—	—	—	—	—	—	—	(61)	61	—	—	—	—
Reclassification to financial liabilities	—	—	—	—	—	—	—	—	—	—	—	—	—	(205)	(205)
Aggregate tax effect – shareholder tax	—	—	—	—	—	—	—	—	—	—	16	16	—	—	16
Balance at 31 December	726	200	1,173	3,271	(43)	1,530	79	530	(663)	86	5,954	12,843	990	1,530	15,363

The accounting policies (identified alphabetically) on pages 148 to 159 and notes (identified numerically) on pages 168 to 266 are an integral part of these financial statements.

Consolidated statement of financial position

As at 31 December 2012

	Note	2012 £m	Restated ¹ 2011 £m
Assets			
Goodwill	N & 16	1,520	2,640
Acquired value of in-force business and intangible assets	N & 17	1,084	2,021
Interests in, and loans to, joint ventures	D & 18	1,493	1,700
Interests in, and loans to, associates	D & 19	215	1,118
Property and equipment	O & 20	391	510
Investment property	P & 21	10,815	11,638
Loans	U & 23	24,537	28,116
Financial investments	R, S & 25	189,078	216,058
Reinsurance assets	M & 42	6,684	7,112
Deferred tax assets	AB	188	238
Current tax assets		67	140
Receivables	26	7,617	7,937
Deferred acquisition costs and other assets	W & 27	3,799	6,444
Prepayments and accrued income		2,701	3,235
Cash and cash equivalents	X & 54d	22,897	23,043
Assets of operations classified as held for sale	AG & 3c	42,603	426
Total assets		315,689	312,376
Equity			
Capital	AD		
Ordinary share capital	29	736	726
Preference Share Capital	32	200	200
		936	926
Capital reserves			
Share premium	29b	1,165	1,173
Merger reserve	D & 34	3,271	3,271
		4,436	4,444
Shares held by employee trusts	31	(32)	(43)
Other reserves	35	1,675	1,562
Retained earnings	36	1,389	5,954
Equity attributable to shareholders of Aviva plc		8,404	12,843
Direct capital instruments and fixed rate tier 1 notes	33	1,382	990
Non-controlling interests	37	1,574	1,530
Total equity		11,360	15,363
Liabilities			
Gross insurance liabilities	K & 39	113,091	147,379
Gross liabilities for investment contracts	L & 40	110,494	113,366
Unallocated divisible surplus	K & 44	6,931	650
Net asset value attributable to unitholders	D	11,146	10,352
Provisions	Z, AA & 46	1,119	992
Deferred tax liabilities	AB	547	1,171
Current tax liabilities		112	232
Borrowings	AC & 48	8,194	8,450
Payables and other financial liabilities	R & 49	9,441	11,230
Other liabilities	50	1,843	2,828
Liabilities of operations classified as held for sale	AG & 3c	41,411	363
Total liabilities		304,329	297,013
Total equity and liabilities		315,689	312,376

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

Approved by the Board on 6 March 2013.

Patrick Regan
Chief financial officer

Consolidated statement of cash flows

For the year ended 31 December 2012

The cash flows presented in this statement cover all the Group's activities and include flows from both policyholder and shareholder activities. All cash and cash equivalents are available for use by the Group.

	Notes	2012 £m	2011 £m
Cash flows from operating activities			
Cash generated from continuing operations	54a	2,676	111
Tax paid		(428)	(425)
Net cash from/(used in) operating activities – continuing operations		2,248	(314)
Net cash from/(used in) operating activities – discontinued operations		46	(28)
Total net cash from/(used in) operating activities		2,294	(342)
Cash flows from investing activities			
Acquisition of, and additions to subsidiaries, joint ventures and associates, net of cash acquired	54b	(129)	(114)
Disposals of subsidiaries, joint ventures and associates, net of cash transferred	54c	421	877
New loans to joint ventures	18a	(4)	(18)
Repayment of loans to joint ventures		12	17
Net new loans to joint ventures		8	(1)
Purchases of property and equipment	20	(220)	(86)
Proceeds on sale of property and equipment		43	40
Purchases of intangible assets	17	(128)	(109)
Net cash (used in)/from investing activities – continuing operations		(5)	607
Net cash (used in) investing activities – discontinued operations		(10)	(529)
Total net cash (used in)/from investing activities		(15)	78
Cash flows from financing activities			
Proceeds from issue of ordinary shares and fixed rate tier 1 notes, net of transaction costs		392	—
Treasury shares purchased for employee trusts		(33)	(29)
New borrowings drawn down, net of expenses		2,529	3,423
Repayment of borrowings		(2,513)	(3,359)
Net drawdown of borrowings		16	64
Interest paid on borrowings		(665)	(686)
Preference dividends paid	15	(17)	(17)
Ordinary dividends paid		(630)	(431)
Coupon payments on direct capital instruments and fixed rate tier 1 notes	15	(73)	(58)
Capital contributions from non-controlling interests	37	20	68
Dividends paid to non-controlling interests of subsidiaries		(102)	(126)
Net cash (used in) financing activities – continuing operations		(1,092)	(1,215)
Net cash (used in) financing activities – discontinued operations		(27)	(558)
Total net cash (used in) financing activities		(1,119)	(1,773)
Total net increase/(decrease) in cash and cash equivalents		1,160	(2,037)
Cash and cash equivalents at 1 January		22,401	24,695
Effect of exchange rate changes on cash and cash equivalents		(313)	(257)
Cash and cash equivalents at 31 December	54d	23,248	22,401

The accounting policies (identified alphabetically) on pages 148 to 159 and notes (identified numerically) on pages 168 to 266 are an integral part of these financial statements.

1 – Exchange rates

The Group's principal overseas operations during the year were located within the Eurozone and the United States. The results and cash flows of these operations have been translated into sterling at the average rates for the year and the assets and liabilities have been translated at the year end rates as follows:

	2012	2011
Eurozone		
– Average rate (€1 equals)	£0.81	£0.87
– Period end rate (€1 equals)	£0.81	£0.84
United States		
– Average rate (\$US1 equals)	£0.63	£0.63
– Period end rate (\$US1 equals)	£0.62	£0.65

Total foreign currency translations from continuing operations amounted to a gain of £128 million (2011: £35 million loss) in the income statement. These result from the settlement of transactions and translations of assets and liabilities denominated in foreign currencies.

2 – Presentation changes

(a) Discontinued operations

As described in note 3c, the Group's US life and annuity business and associated investment management operations (together 'US Life'), have been classified as held for sale. As the Group will exit from a major geographical area of operations, previously presented as 'United States' in the segmental reporting note, the results of US Life for the year, as well as those for preceding years, have been classified as discontinued operations.

The results presented as discontinued operations for 2011 and preceding years also include the results of Delta Lloyd N.V. as a subsidiary, which was deconsolidated during 2011.

(b) Change to operating segments

Following the announcement in April 2012 relating to the restructuring of the Group, the Group's operating segments were changed to align them with the revised organisational reporting structure. The Group has determined its operating segments along market reporting lines, reflecting the management structure whereby a member of the Executive Management team is accountable to the group chief executive for the operating segment for which he is responsible. Further details of the reportable segments are given in note 4.

(c) Restatement of prior period figures

Following a review of the classification of contracts issued by the Group's Italian long-term business certain portfolios have been reclassified from participating insurance contracts to participating investment contracts. As a result there has been a reallocation from gross insurance liabilities at 31 December 2011 to gross liabilities for investment contracts of £2,722 million. The change in insurance liabilities net of reinsurance recognised in the income statement for the year to 31 December 2011 has decreased by £168 million, and the change in investment contract provisions has increased by an equal amount. There is no impact on profit for the year or equity reported for the year ended 31 December 2011.

3 – Subsidiaries

This note provides details of the acquisitions and disposals of subsidiaries that the Group has made during the year, together with details of businesses held for sale at the year end. The principal Group subsidiaries are listed in the performance review section.

(a) Acquisitions

There have been no material acquisitions during 2012.

(b) Disposal and remeasurement of subsidiaries, joint ventures and associates

The (loss)/profit on the disposal and remeasurement of subsidiaries, joint ventures and associates comprises:

	2012 £m	2011 £m
Continuing operations		
United Kingdom – RAC Limited (see (i) below)	(21)	532
Delta Lloyd associate (see (iii) below)	(129)	—
Australia	—	23
Sri Lanka (see (iv) below)	12	—
Czech Republic, Hungary and Romania (see (ii) below)	7	—
Other small operations	(33)	10
(Loss)/profit on disposal and remeasurement from continuing operations	(164)	565
Loss on disposal and remeasurement from discontinued operations (see note 3c(i) below)	(2,359)	(32)
Total (loss)/profit on disposal and remeasurement	(2,523)	533

No tax arises on the profits and losses on these disposals.

3 – Subsidiaries continued

(i) RAC Limited

The loss in respect of RAC Limited in 2012 arises from residual costs related to the sale of that company in September 2011.

(ii) Czech Republic, Hungary and Romania life business

On 31 July 2012, the Group sold its operations in the Czech Republic and Hungary and its Romania life assurance business to MetLife, Inc, for £37 million. Net assets disposed of were £32 million, comprising gross assets of £379 million and liabilities of £347 million, giving a profit on disposal of £3 million after transaction costs. Recycling currency translation reserves of £4 million to the income statement resulted in an overall profit on disposal of £7 million. The sale of our Romania pensions business is still subject to regulatory approval and is expected to complete in the next 12 months, so it has been classified as held for sale (see note 3c(v)).

(iii) Delta Lloyd associate

On 5 July 2012, the Group sold 37.2 million shares in Delta Lloyd for £313 million (net of transaction costs), reducing our holding at that date to 19.8% of Delta Lloyd's ordinary share capital, representing 18.6% of shareholder voting rights. As the Group no longer had significant influence over Delta Lloyd, the Group ceased to account for that company as an associate from 5 July 2012. From that date, our holding was classified as a financial investment, held at fair value through profit and loss.

The loss on disposal is calculated as follows:

	2012 £m
Cash consideration, net of transaction costs	313
Fair value of financial investment holding at 5 July 2012	315
Net Consideration	628
Interest in associate	(595)
Currency translation and investment valuation reserves recycled to income statement	(162)
Loss on disposal	(129)

On 8 January 2013 the Group announced the sale of its remaining shareholding in Delta Lloyd, resulting in gross cash proceeds of £353 million.

(iv) Sri Lanka

On 4 December 2012, the Group sold its controlling 58.4% interest in Aviva NDB Holdings Lanka (Private) Limited ("Aviva NDB"), to AIA Group Limited for consideration of £31 million. Net assets of the business were £16 million (comprising gross assets of £205 million and liabilities of £189 million). After recycling of currency translation reserves of £3 million the profit on disposal amounted to £12 million.

(c) Assets and liabilities of operations classified as held for sale

The assets and liabilities of operations classified as held for sale as at 31 December 2012 are as follows:

			2012	2011
	US Life ¹ £m	Other £m	Total £m	Total £m
Assets				
Goodwill	—	183	183	—
Acquired value of in-force and intangible assets	408	83	491	1
Interests in, and loans to, joint ventures and associates	—	126	126	12
Property and equipment	—	2	2	1
Investment Property	6	12	18	—
Loans	3,397	—	3,397	—
Financial investments	31,212	5,203	36,415	347
Reinsurance assets	644	239	883	1
Deferred acquisition costs	1,468	70	1,538	23
Other assets	769	97	866	15
Cash and cash equivalents	544	373	917	26
	38,448	6,388	44,836	426
Additional impairment to write down the disposal group to fair value less costs to sell	(2,233)	—	(2,233)	—
Total assets	36,215	6,388	42,603	426
Liabilities				
Gross insurance liabilities	(31,153)	(3,294)	(34,447)	(344)
Gross liabilities for investment contracts	(2,197)	(1,857)	(4,054)	—
Unallocated divisible surplus	—	(55)	(55)	—
Provisions	(184)	(3)	(187)	(4)
Deferred tax liabilities	(672)	(8)	(680)	—
Borrowings	(145)	—	(145)	—
Other liabilities	(1,497)	(346)	(1,843)	(15)
Total liabilities	(35,848)	(5,563)	(41,411)	(363)
Net assets	367	825	1,192	63

¹ US Life comprises US long term business previously reported under the heading "United States" and associated internal asset management operations previously reported under "Aviva Investors" in note 4 – segmental information.

3 – Subsidiaries continued

The businesses classified as held for sale comprise:

(i) US long term business

On 8 November 2012 the Group confirmed it was in discussions with external parties with respect to its US life operations, consisting of Aviva Life and Annuity Company and the associated internal asset management operations of Aviva Investors North America, Inc (“US Life”) and these have been classified as held for sale. On 21 December 2012 the Group announced that it had agreed to sell US Life to Athene Holding Ltd for consideration of £1.0 billion including the shareholder loan (£1.1 billion including repayment of an external loan). There is uncertainty in the ultimate consideration, which depends on the development of statutory surplus between the announcement of sale and ultimate completion date. The transaction is expected to complete in 2013.

Following classification as held for sale, US Life has been re-measured to fair value less costs to sell resulting in an impairment loss of £2,359 million, recognised within “Loss on the disposal and re-measurement of subsidiaries and associates” in the income statement, as a component of the result of discontinued operations.

An impairment of £126 million has reduced the carrying value of property and equipment, investments in associates and prepayments within US Life to nil. The remaining impairment of £2,233 million reduces the value of the US Life disposal group so that the carrying value of this business is equal to its fair value less costs to sell of £367 million.

As described in Note 2a, the results of US Life for the year, as well as those for preceding years, have been classified as discontinued operations in the income statement.

Other comprehensive income, net of tax from discontinued operations of £68 million includes £528 million fair value gains on available for sale financial investments, £(235) million fair value gains on available for sale financial investments transferred to the income statement on disposal, £(130) million foreign exchange losses, £12 million of impairment losses transferred to the income statement, and £(107) million aggregate shareholder tax effect.

On completion of the disposal the currency translation reserves and investment valuation reserves relating to the US Life operations, currently recognised within equity, will be recycled to the income statement.

(ii) Irish long-term business – Ark Life

Irish long-term business is carried out through a subsidiary, Aviva Life Holdings Ireland Limited (“ALHI”), which is 75% owned by Aviva and 25% owned by Allied Irish Bank (“AIB”). ALHI holds four subsidiaries, one of which is Ark Life Assurance Company Limited (“Ark Life”) which carries out bancassurance business via a distribution agreement with AIB. The original distribution agreement was renewable in 2011 but, on 15 December 2011, AIB notified the Group that they did not wish to renew it and the existing shareholders’ agreement governing ALHI was terminated. The termination of this agreement triggered the ability for both parties to exercise put and call options that will result in the unwind of the original structure such that the Ark Life business returns 100% to AIB and the Group will purchase the 25% minority stake in ALHI. The formal exercise of these options was approved on 17 January 2012 and, as a result, the Ark Life business became held for sale on that date. Completion of the transaction is subject to agreement of terms with AIB and regulatory approval. Completion is expected in the next 12 months.

Management’s current best estimate of the disposal proceeds for the Ark Life business is £232 million net of transaction costs, which is lower than its carrying value following impairments charged in 2011. A further charge to profit of £111 million has been recognised during 2012 reflecting revised expected disposal proceeds.

The exercise of the put options in January 2012 over AIB’s non-controlling interest in ALHI led to our reclassifying this non-controlling interest from equity to financial liabilities as at 31 December 2011. Our current estimate of the liability as at 31 December 2012 is £122 million. A credit to the income statement of £76 million has been recognised in 2012 reflecting the revised expected purchase liability.

The net impact of these two movements is a charge to profit of £35 million, before exchange movements, recognised within net investment income. Finalisation of the exit value for Ark Life and the purchase value for the minority share in ALHI is subject to the conclusion of discussions with AIB.

(iii) Spanish long-term business – Aseval

On 18 December 2012 Aviva reached a settlement with Bankia S.A. (“Bankia”) to transfer the Group’s entire holding in Aseval Aseguradora Valenciana, Sociedad Anónima de Seguros y Reaseguros (“Aseval”), a Spanish life assurance company, to Bankia. Aseval was classified as held for sale at this date. The transfer is expected to complete on or before 30 April 2013 with proceeds of £494 million. Aseval is included within the ‘Italy, Spain and Other’ operating segment at its carrying value.

(iv) Russian long-term business

During the year the Group entered into negotiations to dispose of Aviva Russia. On 27 February 2013 the Group announced the sale of the business to Blagosostoyanie for consideration of €35 million. The transaction is expected to complete in the first half of 2013. The business is included in the statement of financial position at its carrying value.

(v) Other

Other businesses classified as held for sale comprise joint ventures in Taiwan and Malaysia, details of which are given in note 18(a), and the Group’s pensions business subsidiary in Romania.

4 – Segmental information

The Group's results can be segmented, either by activity or by geography. Our primary reporting format is on market reporting lines, with supplementary information being given by business activity. This note provides segmental information on the consolidated income statement and consolidated statement of financial position.

(a) Operating segments

Following the announcement in April 2012 relating to the restructuring of the Group, the Group's operating segments were changed to align them with the new management structure. The revised segments are set out below. Results for prior years have been restated to facilitate comparison with this new structure.

United Kingdom & Ireland

The United Kingdom and Ireland comprises two operating segments – Life and General Insurance. The principal activities of our UK and Ireland Life operations are life insurance, long-term health and accident insurance, savings, pensions and annuity business and Health in the UK, whilst UK and Ireland General Insurance provides insurance cover to individuals and businesses, for risks associated mainly with motor vehicles, property and liability (such as employers' liability and professional indemnity liability) and medical expenses. UK & Ireland General Insurance business also includes the results of Ireland Health. For the period to its disposal on 30 September 2011, UK and Ireland General Insurance also included the RAC motor recovery business.

France

The principal activities of our French operations are long-term business and general insurance. The long-term business offers a range of long-term insurance and savings products, primarily for individuals, with a focus on the unit-linked market. The general insurance business predominantly sells personal and small commercial lines insurance products through agents and a direct insurer.

Canada

The principal activity of the Canadian operation is general insurance. In particular it provides personal and commercial lines insurance products through a range of distribution partners.

Italy, Spain and Other

These countries are not individually significant at a Group level, so have been aggregated into a single reporting segment in line with IFRS8. This segment includes our operations in Italy and Spain (including Aseval which is held for sale as at 31 December 2012). The principal activities of our Italian operations are long-term business and general insurance. The life business offers a range of long-term insurance and savings products, and the general insurance business provides motor and home insurance products to individuals, as well as small commercial risk insurance to businesses. The principal activity of the Spanish operation is the sale of long-term business, accident and health insurance and a selection of savings products. This segment also includes the results of our Czech, Hungarian and Romanian life businesses up until the date of their sale in July 2012 as well as our Reinsurance and Run Off businesses.

Higher growth markets

Activities reported in the higher growth markets operating segment include our businesses in Asia, Poland, Turkey and Russia. Our activities in Asia principally comprise our long-term business operations in China, India, Singapore, Hong Kong, South Korea, Vietnam and Indonesia as well as our life operations in Taiwan and Malaysia which are held for sale as at the balance sheet date and the results of Sri Lanka up until the date of disposal in December 2012. Higher growth also includes general insurance operations in Singapore, Indonesia, Poland and Turkey and long-term business in Poland, Turkey and Russia (which is held for sale at the year-end).

Aviva Investors

Aviva Investors operates in most of the markets in which the Group operates, in particular the UK, France and Canada and other international businesses, managing policyholders' and shareholders' invested funds, providing investment management services for institutional pension fund mandates and managing a range of retail investment products, including investment funds, unit trusts, OEICs and ISAs. The internal asset management operations of Aviva Investors North America are being sold with the Group's US life operations and are classified as held for sale and as a discontinued operation in these financial statements.

Other Group activities

Investment return on centrally held assets and head office expenses, such as Group treasury and finance functions, together with certain taxes and financing costs arising on central borrowings are included in 'Other Group activities', along with central core structural borrowings and certain tax balances in the segmental statement of financial position. Also included here are consolidation and elimination adjustments and the Group's interest in Delta Lloyd, as an associate to 5 July 2012, and as a financial investment after that date.

Discontinued operations

In December 2012 the Group announced it had agreed to sell its US life operations (including the related internal asset management operations of Aviva Investors) and therefore it has been classified as a discontinued operation for presentation in the income statement and held for sale in the statement of financial position.

On 6 May 2011 the Group ceased to hold a majority of the shareholder voting rights in Delta Lloyd and therefore the results of Delta Lloyd up to 6 May 2011 are presented as discontinued operations for 2011 and prior years. After this date, the Group ceased to consolidate Delta Lloyd.

Measurement basis

The accounting policies of the segments are the same as those for the Group as a whole. Any transactions between the business segments are on normal commercial terms and market conditions. The Group evaluates performance of operating segments on the basis of:

- (i) profit or loss from operations before tax attributable to shareholders
- (ii) profit or loss from operations before tax attributable to shareholders, adjusted for non-operating items outside the segment management's control, including investment market performance and fiscal policy changes

4 – Segmental information continued

a (i) Segmental income statement for the year ended 31 December 2012

	Developed Markets										Total £m
	United Kingdom & Ireland			Canada £m	Italy, Spain and Other £m	Higher growth markets £m	Aviva Investors ³ £m	Other Group activities ⁴ £m	Continuing operations £m	Discontinued Operations ² £m	
Gross written premiums	6,363	4,951	4,763	2,248	3,033	1,386	—	—	22,744	3,796	26,540
Premiums ceded to reinsurers	(740)	(450)	(55)	(63)	(127)	(136)	—	—	(1,571)	(207)	(1,778)
Internal reinsurance revenue	—	(11)	(6)	(9)	36	(10)	—	—	—	—	—
Net written premiums	5,623	4,490	4,702	2,176	2,942	1,240	—	—	21,173	3,589	24,762
Net change in provision for unearned premiums	(15)	63	(28)	(31)	3	(8)	—	—	(16)	—	(16)
Net earned premiums	5,608	4,553	4,674	2,145	2,945	1,232	—	—	21,157	3,589	24,746
Fee and commission income	448	188	121	42	125	70	279	—	1,273	23	1,296
	6,056	4,741	4,795	2,187	3,070	1,302	279	—	22,430	3,612	26,042
Net investment income/(expense)	8,639	523	8,042	140	3,140	697	(8)	(67)	21,106	2,241	23,347
Inter-segment revenue	—	—	—	—	—	—	134	—	134	75	209
Share of (loss)/profit of joint ventures and associates	(37)	—	8	—	—	1	7	(256)	(277)	—	(277)
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	(2)	(21)	—	—	7	12	—	(160)	(164)	(2,359)	(2,523)
Segmental income	14,656	5,243	12,845	2,327	6,217	2,012	412	(483)	43,229	3,569	46,798
Claims and benefits paid, net of recoveries from reinsurers	(9,224)	(2,908)	(5,272)	(1,268)	(3,916)	(1,013)	—	—	(23,601)	(2,721)	(26,322)
Change in insurance liabilities, net of reinsurance	404	(22)	(880)	(40)	400	(292)	—	—	(430)	(1,566)	(1,996)
Change in investment contract provisions	(3,151)	—	(983)	—	(295)	18	(39)	—	(4,450)	(77)	(4,527)
Change in unallocated divisible surplus	(347)	—	(4,359)	—	(1,491)	(119)	—	—	(6,316)	—	(6,316)
Amortisation of acquired value of in-force business	(13)	—	(18)	—	(9)	(3)	—	—	(43)	(183)	(226)
Impairment of goodwill and other intangibles, depreciation and other amortisation expense	(107)	(59)	(3)	(17)	(129)	(7)	(9)	(5)	(336)	(916)	(1,252)
Other operating expenses	(1,505)	(1,944)	(845)	(745)	(432)	(352)	(357)	(678)	(6,858)	(691)	(7,549)
Impairment losses on AVIF and tangible assets ¹	(34)	(43)	(1)	—	(3)	1	—	—	(80)	(15)	(95)
Inter-segment expenses	(122)	(3)	—	(4)	—	(5)	—	—	(134)	(75)	(209)
Finance costs	(261)	(58)	(2)	(9)	(2)	—	(5)	(398)	(735)	(21)	(756)
Segmental expenses	(14,360)	(5,037)	(12,363)	(2,083)	(5,877)	(1,772)	(410)	(1,081)	(42,983)	(6,265)	(49,248)
Profit/(loss) before tax	296	206	482	244	340	240	2	(1,564)	246	(2,696)	(2,450)
Tax attributable to policyholders' returns	(198)	—	—	—	—	(23)	—	—	(221)	—	(221)
Profit/(loss) before tax attributable to shareholders	98	206	482	244	340	217	2	(1,564)	25	(2,696)	(2,671)
Adjusted for non-operating items:											
Reclassification of corporate costs and unallocated interest	7	(1)	25	—	3	—	1	(35)	—	—	—
Investment return variances and economic assumption changes on long-term business	663	—	(28)	—	—	(15)	—	—	620	(342)	278
Short-term fluctuation in return on investments backing non-long- term business	—	(36)	(68)	10	(56)	(1)	—	144	(7)	—	(7)
Economic assumption changes on general insurance and health business	—	20	—	—	1	—	—	—	21	—	21
Impairment of goodwill, associates and joint ventures	(1)	—	—	—	108	—	—	(47)	60	782	842
Amortisation and impairment of intangibles	54	40	—	11	13	4	6	—	128	129	257
(Profit)/loss on the disposal of subsidiaries and associates	2	21	—	—	(7)	(12)	—	160	164	2,359	2,523
Integration and restructuring costs	87	154	11	11	12	9	33	144	461	7	468
Exceptional items	—	—	—	—	—	—	—	—	—	—	—
Share of Delta Lloyd's non-operating items (before tax), as an associate	—	—	—	—	—	—	—	523	523	—	523
Share of Delta Lloyd's tax expense, as an associate	—	—	—	—	—	—	—	(107)	(107)	—	(107)
Operating profit/(loss) before tax attributable to shareholders	910	404	422	276	414	202	42	(782)	1,888	239	2,127

1 Impairment losses, and reversal of such losses, recognised directly in other comprehensive income were £nil million and £nil million respectively.

2 Discontinued operations represent the operations of the United States Life business and related internal asset management activities.

3 Aviva Investors operating profit includes £3 million profit relating to the Aviva Investors Pooled Pension business.

4 Other group activities include Delta Lloyd as an associate up until 5 July 2012 and as a financial investment thereafter.

4 – Segmental information continued

a (ii) Segmental income statement for the year ended 31 December 2011

	Developed Markets											
	United Kingdom & Ireland											Total £m
	Life £m	GI £m	France £m	Canada £m	Restated ⁴ Italy, Spain and Other £m	Higher growth markets £m	Aviva Investors ³ £m	Other Group activities ⁵ £m	Restated ⁴ Continuing operations £m	Discontinued Operations ² £m		
Gross written premiums	7,639	5,227	5,305	2,164	4,586	1,334	—	—	26,255	5,863	32,118	
Premiums ceded to reinsurers	(816)	(375)	(66)	(70)	(108)	(115)	—	—	(1,550)	(198)	(1,748)	
Internal reinsurance revenue	—	(11)	(6)	(11)	34	(4)	—	—	2	(2)	—	
Net written premiums	6,823	4,841	5,233	2,083	4,512	1,215	—	—	24,707	5,663	30,370	
Net change in provision for unearned premiums	(39)	(78)	(22)	(46)	(25)	(26)	—	—	(236)	(56)	(292)	
Net earned premiums	6,784	4,763	5,211	2,037	4,487	1,189	—	—	24,471	5,607	30,078	
Fee and commission income	462	240	147	38	174	80	324	—	1,465	111	1,576	
Net investment income/(expense)	7,246	5,003	5,358	2,075	4,661	1,269	324	—	25,936	5,718	31,654	
Inter-segment revenue	5,495	451	(896)	236	(747)	(158)	79	(119)	4,341	2,086	6,427	
Share of (loss)/profit of joint ventures and associates	—	—	—	—	—	—	148	—	148	71	219	
Profit/(loss) on the disposal and remeasurement of subsidiaries and associates	(41)	—	9	—	(12)	1	4	(84)	(123)	28	(95)	
Segmental income	12,700	5,982	4,508	2,311	3,902	1,112	578	(226)	30,867	7,871	38,738	
Claims and benefits paid, net of recoveries from reinsurers	(9,589)	(3,217)	(5,366)	(1,308)	(4,118)	(782)	—	—	(24,380)	(4,029)	(28,409)	
Change in insurance liabilities, net of reinsurance	(2,373)	89	62	(1)	(283)	222	—	—	(2,284)	(2,523)	(4,807)	
Change in investment contract provisions	949	—	583	—	37	46	(137)	—	1,478	(180)	1,298	
Change in unallocated divisible surplus	358	—	1,334	—	1,053	(24)	—	—	2,721	(19)	2,702	
Amortisation of acquired value of in-force business	(35)	—	(19)	—	(11)	(5)	—	—	(70)	(200)	(270)	
Impairment of goodwill and other intangibles, depreciation and other amortisation expense	(260)	(36)	(7)	(18)	(28)	(8)	(17)	(2)	(376)	(64)	(440)	
Other operating expenses	(1,375)	(1,894)	(806)	(673)	(567)	(369)	(384)	(495)	(6,563)	(932)	(7,495)	
Impairment losses on AVIF and tangible assets ¹	—	(60)	(4)	—	(31)	—	(1)	—	(96)	(33)	(129)	
Inter-segment expenses	(133)	(6)	—	(3)	—	(6)	—	—	(148)	(71)	(219)	
Finance costs	(277)	(52)	(18)	(11)	(2)	—	(3)	(413)	(776)	(284)	(1,060)	
Segmental expenses	(12,735)	(5,176)	(4,241)	(2,014)	(3,950)	(926)	(542)	(910)	(30,494)	(8,335)	(38,829)	
(Loss)/profit before tax	(35)	806	267	297	(48)	186	36	(1,136)	373	(464)	(91)	
Tax attributable to policyholders' returns	186	—	—	—	—	(8)	—	—	178	—	178	
Profit/(loss) before tax attributable to shareholders	151	806	267	297	(48)	178	36	(1,136)	551	(464)	87	
Adjusted for non-operating items:												
Reclassification of corporate costs and unallocated interest	—	2	20	—	2	—	1	(25)	—	—	—	
Investment return variances and economic assumption changes	543	—	47	—	285	22	—	—	897	719	1,616	
Short term fluctuation in return on investments backing non-long-term business	—	54	140	(64)	62	—	—	74	266	60	326	
Economic assumption changes on general insurance and health business	—	86	—	4	—	—	—	—	90	—	90	
Impairment of goodwill, associates and joint ventures	149	—	—	—	11	15	—	217	392	—	392	
Amortisation and impairment of intangibles	66	9	4	11	12	5	9	—	116	60	176	
(Profit)/loss on the disposal of subsidiaries and associates	—	(528)	(37)	—	—	—	(23)	23	(565)	32	(533)	
Integration and restructuring costs	46	37	30	6	10	9	30	93	261	7	268	
Exceptional items	22	35	—	—	—	—	—	—	57	—	57	
Share of Delta Lloyd's non-operating items (before tax), as an associate	—	—	—	—	—	—	—	(10)	(10)	—	(10)	
Share of Delta Lloyd's tax expense, as an associate	—	—	—	—	—	—	—	34	34	—	34	
Operating profit/(loss) before tax attributable to shareholders	977	501	471	254	334	229	53	(730)	2,089	414	2,503	

1 Impairment losses, and reversal of such losses, recognised directly in other comprehensive income were £2 million and £nil respectively.

2 Discontinued operations represent the operations of the United States Life assurance and related asset management activities, and the results of Delta Lloyd up until its deconsolidation in May 2011.

3 Aviva Investors operating profit includes £3 million profit relating to the Aviva Investors Pooled Pension business.

4 Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

5 Other group activities include Delta Lloyd as an associate.

4 – Segmental information continued**a (iii) Segmental statement of financial position as at 31 December 2012**

	Developed Markets									
	United Kingdom & Ireland			United States £m	Canada £m	Italy, Spain and Other £m	Higher growth markets £m	Aviva Investors £m	Other Group activities £m	Total £m
Life £m	GI £m	France £m								
Goodwill	—	1,037	—	—	50	342	64	27	—	1,520
Acquired value of in-force business and intangible assets	140	58	133	—	49	633	15	56	—	1,084
Interests in, and loans to, joint ventures and associates	1,185	—	148	—	—	—	371	4	—	1,708
Property and equipment	91	34	220	—	21	5	11	5	4	391
Investment property	7,650	8	1,342	—	—	2	—	1,093	720	10,815
Loans	23,193	299	848	—	83	14	30	—	70	24,537
Financial investments	90,064	3,127	60,001	—	3,766	21,900	5,761	759	3,700	189,078
Deferred acquisition costs	1,422	519	211	—	275	106	35	—	—	2,568
Other assets	16,883	4,122	11,304	—	1,053	2,828	699	436	4,060	41,385
Assets of operations classified as held for sale	3,490	—	—	36,187	—	2,631	267	28	—	42,603
Total assets	144,118	9,204	74,207	36,187	5,297	28,461	7,253	2,408	8,554	315,689
Insurance liabilities										
Long term business and outstanding claims provisions	71,282	5,789	14,194	—	2,494	9,730	4,913	—	—	108,402
Unearned premiums	238	2,274	369	—	1,127	280	153	—	—	4,441
Other insurance liabilities	—	86	61	—	98	2	1	—	—	248
Liability for investment contracts	49,719	—	46,952	—	—	11,893	47	1,883	—	110,494
Unallocated divisible surplus	2,055	—	4,591	—	—	38	247	—	—	6,931
Net asset value attributable to unitholders	1,375	—	3,383	—	—	205	—	—	6,183	11,146
External borrowings	2,949	3	—	—	—	101	—	—	5,141	8,194
Other liabilities, including inter-segment liabilities	7,114	(2,545)	2,562	—	467	931	346	255	3,932	13,062
Liabilities of operations classified as held for sale	3,257	—	—	35,835	—	2,188	118	13	—	41,411
Total liabilities	137,989	5,607	72,112	35,835	4,186	25,368	5,825	2,151	15,256	304,329
Total equity										11,360
Total equity and liabilities										315,689
Capital expenditure (excluding business combinations)	63	42	176	29	21	15	7	24	—	377

External borrowings by holding companies within the Group which are not allocated to operating companies are included in 'Other Group activities'.

4 – Segmental information continued

a (iv) Segmental statement of financial position as at 31 December 2011

	United Kingdom & Ireland				Developed Markets					
	Life £m	GI £m	France £m	United States £m	Canada £m	Restated ² Italy, Spain and Other £m	Higher growth markets £m	Aviva Investors £m	Other Group activities ¹ £m	Restated ² Total £m
Goodwill	—	1,040	—	800	50	650	71	29	—	2,640
Acquired value of in-force business and intangible assets	326	67	155	681	47	678	23	44	—	2,021
Interests in, and loans to, joint ventures and associates	1,274	—	152	1	—	—	600	15	776	2,818
Property and equipment	228	45	50	113	19	18	13	16	8	510
Investment property	8,431	20	1,246	6	—	2	—	1,133	800	11,638
Loans	23,440	524	949	3,067	80	16	40	—	—	28,116
Financial investments	90,165	3,268	55,074	30,613	3,683	23,895	5,398	884	3,078	216,058
Deferred acquisition costs	1,594	566	207	1,950	274	129	35	—	—	4,755
Other assets	16,864	3,828	11,856	1,752	1,183	2,366	507	579	4,459	43,394
Assets of operations classified as held for sale	—	—	—	—	—	414	12	—	—	426
Total assets	142,322	9,358	69,689	38,983	5,336	28,168	6,699	2,700	9,121	312,376
Insurance liabilities										
Long term business and outstanding claims provisions	72,513	6,048	13,679	30,697	2,538	12,408	4,732	—	—	142,615
Unearned premiums	350	2,209	353	—	1,122	296	153	—	—	4,483
Other insurance liabilities	—	95	85	—	100	1	—	—	—	281
Liability for investment contracts	48,456	—	47,346	2,833	—	12,543	51	2,137	—	113,366
Unallocated divisible surplus	1,712	—	249	—	—	(1,435)	124	—	—	650
Net asset value attributable to unitholders	1,279	—	3,362	—	—	18	—	—	5,693	10,352
External borrowings	2,945	2	—	159	—	89	—	—	5,255	8,450
Other liabilities, including inter-segment liabilities	8,829	(3,280)	2,538	2,188	456	1,059	232	309	4,122	16,453
Liabilities of operations classified as held for sale	—	—	—	—	—	363	—	—	—	363
Total liabilities	136,084	5,074	67,612	35,877	4,216	25,342	5,292	2,446	15,070	297,013
Total equity										15,363
Total equity and liabilities										312,376
Capital expenditure (excluding business combinations)	55	79	5	21	8	17	9	20	—	214

1 Other group activities include Delta Lloyd as an associate.

2 Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

(b) Further analysis by products and services

The Group's results can be further analysed by products and services which comprise long-term business, general insurance and health, fund management and other activities.

Long-term business

Our long-term business comprises life insurance, long-term health and accident insurance, savings, pensions and annuity business written by our life insurance subsidiaries, including managed pension fund business and our share of the other life and related business written in our associates and joint ventures, as well as lifetime mortgage business written in the UK.

General insurance and health

Our general insurance and health business provides insurance cover to individuals and to small and medium sized businesses, for risks associated mainly with motor vehicles, property and liability, such as employers' liability and professional indemnity liability, and medical expenses.

Fund management

Our fund management business invests policyholders' and shareholders' funds, provides investment management services for institutional pension fund mandates and manages a range of retail investment products, including investment funds, unit trusts, OEICs and ISAs. Clients include Aviva Group businesses and third-party financial institutions, pension funds, public sector organisations, investment professionals and private investors.

Other

Other includes the RAC non-insurance operations (up to the disposal date of 30 September 2011), service companies, head office expenses, such as Group treasury and finance functions, and certain financing costs and taxes not allocated to business segments.

Discontinued operations and Delta Lloyd

In the products and services analysis, the results of US Life (including the related internal asset management business) for all periods presented and Delta Lloyd up to 6 May 2011 are presented as discontinued operations. Between 6 May 2011 and 5 July 2012, the Group's share of the results of its interest in Delta Lloyd as an associate and, from 5 July 2012 to the year-end, as a financial investment, are shown only within other activities within continuing operations.

4 – Segmental information continued

b (i) Segmental income statement – products and services for the year ended 31 December 2012

	Long-term business £m	General insurance and health ² £m	Fund management £m	Other ³ £m	Total £m
Gross written premiums ¹	13,209	9,535	—	—	22,744
Premiums ceded to reinsurers	(930)	(641)	—	—	(1,571)
Net written premiums	12,279	8,894	—	—	21,173
Net change in provision for unearned premiums	—	(16)	—	—	(16)
Net earned premiums	12,279	8,878	—	—	21,157
Fee and commission income	632	65	331	245	1,273
	12,911	8,943	331	245	22,430
Net investment income/(expense)	20,295	823	6	(18)	21,106
Inter-segment revenue	—	—	127	—	127
Share of (loss)/profit of joint ventures and associates	(27)	1	3	(254)	(277)
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	(6)	(21)	—	(137)	(164)
Segmental income	33,173	9,746	467	(164)	43,222
Claims and benefits paid, net of recoveries from reinsurers	(17,839)	(5,762)	—	—	(23,601)
Change in insurance liabilities, net of reinsurance	(359)	(71)	—	—	(430)
Change in investment contract provisions	(4,450)	—	—	—	(4,450)
Change in unallocated divisible surplus	(6,316)	—	—	—	(6,316)
Amortisation of acquired value of in-force business	(43)	—	—	—	(43)
Impairment of goodwill and other intangibles, depreciation and other amortisation expense	(236)	(25)	(10)	(65)	(336)
Other operating expenses	(2,477)	(3,170)	(390)	(821)	(6,858)
Impairment losses on AVIF and tangible assets	(37)	(43)	—	—	(80)
Inter-segment expenses	(116)	(11)	—	—	(127)
Finance costs	(215)	(29)	(56)	(435)	(735)
Segmental expenses	(32,088)	(9,111)	(456)	(1,321)	(42,976)
Profit/(loss) before tax from continuing operations	1,085	635	11	(1,485)	246
Tax attributable to policyholder returns	(221)	—	—	—	(221)
Profit/(loss) before tax attributable to shareholders	864	635	11	(1,485)	25
Adjusted for:					
Non-operating items from continuing operations (excluding Delta Lloyd as an associate)	967	258	40	182	1,447
Share of Delta Lloyd's non-operating items (before tax), as an associate	—	—	—	523	523
Share of Delta Lloyd's tax expense, as an associate	—	—	—	(107)	(107)
Operating profit/(loss) before tax attributable to shareholders' profits from continuing operations	1,831	893	51	(887)	1,888
Operating profit/(loss) before tax attributable to shareholders' profits from discontinued operations⁴	200	—	55	(16)	239
Operating profit/(loss) before tax attributable to shareholders' profits	2,031	893	106	(903)	2,127

¹ Gross written premiums includes inward reinsurance premiums assumed from other companies amounting to £370 million, of which £130 million relates to property and liability insurance and £240 million relates to long-term business.

² General insurance and health business segment includes gross written premiums of £1,164 million relating to health business. The remaining business relates to property and liability insurance.

³ Other includes Delta Lloyd as an associate to 5 July 2012, head office expenses such as group treasury and finance functions, and certain financing costs and taxes not allocated to business segments.

⁴ Discontinued operations represent the operations of the United States Life business and related internal asset management activities.

4 – Segmental information continued

b (ii) Segmental income statement – products and services for the year ended 31 December 2011

	Restated ⁵ Long-term Business £m	General insurance and health ² £m	Fund management £m	Other ³ £m	Restated ⁵ Total £m
Gross written premiums ¹	16,505	9,750	—	—	26,255
Premiums ceded to reinsurers	(960)	(588)	—	—	(1,548)
Net written premiums	15,545	9,162	—	—	24,707
Net change in provision for unearned premiums	—	(236)	—	—	(236)
Net earned premiums	15,545	8,926	—	—	24,471
Fee and commission income	705	54	373	333	1,465
	16,250	8,980	373	333	25,936
Net investment income/(expense)	3,811	725	4	(199)	4,341
Inter-segment revenue	—	—	156	—	156
Share of (loss)/profit of joint venture and associates	(10)	—	(2)	(111)	(123)
(Loss)/profit on the disposal and remeasurement of subsidiaries and associates	—	(28)	24	569	565
Segmental income	20,051	9,677	555	592	30,875
Claims and benefits paid, net of recoveries from reinsurers	(18,435)	(5,945)	—	—	(24,380)
Change in insurance liabilities, net of reinsurance	(2,281)	(3)	—	—	(2,284)
Change in investment contract provisions	1,478	—	—	—	1,478
Change in unallocated divisible surplus	2,721	—	—	—	2,721
Amortisation of acquired value of in-force business on insurance contracts	(70)	—	—	—	(70)
Impairment of goodwill and other intangibles, depreciation and other amortisation expense	(277)	(19)	(16)	(64)	(376)
Other operating expenses	(2,293)	(2,994)	(443)	(833)	(6,563)
Impairment losses on AVIF and tangible assets	(17)	(60)	—	(19)	(96)
Inter-segment expenses	(145)	(11)	—	—	(156)
Finance costs	(205)	(36)	(51)	(484)	(776)
Segmental expenses	(19,524)	(9,068)	(510)	(1,400)	(30,502)
Profit/(loss) before tax from continuing operations	527	609	45	(808)	373
Tax attributable to policyholder returns	178	—	—	—	178
Profit/(loss) before tax attributable to shareholders from continuing operations	705	609	45	(808)	551
Adjusted for:					
Non-operating items from continuing operations (excluding Delta Lloyd as an associate)	1,221	326	16	(49)	1,514
Share of Delta Lloyd's non-operating items (before tax), as an associate	—	—	—	(10)	(10)
Share of Delta Lloyd's tax expense, as an associate	—	—	—	34	34
Operating profit/(loss) before tax attributable to shareholders' profits from continuing operations	1,926	935	61	(833)	2,089
Operating profit/(loss) before tax attributable to shareholders' profits from discontinued operations⁴	382	1	49	(18)	414
Operating profit/(loss) before tax attributable to shareholders' profits	2,308	936	110	(851)	2,503

1 Gross written premiums includes inward reinsurance premiums assumed from other companies amounting to £226 million, of which £110 million relates to property and liability insurance and £116 million relates to long-term business.

2 General insurance and health business segment includes gross written premiums of £1,107 million relating to health business. The remaining business relates to property and liability insurance.

3 Other includes the RAC, up to the date of disposal, Delta Lloyd as an associate from 6 May 2011, head office expenses, such as group treasury and finance functions, and certain financing costs and taxes not allocated to business segments.

4 Discontinued operations represent the operations of the United States Life business and related internal asset management activities and the results of Delta Lloyd up until its deconsolidation in May 2011.

5 Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

4 – Segmental information continued

b (iii) Segmental statement of financial position – products and services as at 31 December 2012

	Long-term business £m	General insurance and health £m	Fund management £m	Other £m	Total £m
Goodwill	361	1,060	27	72	1,520
Acquired value of in-force business and intangible assets	799	146	56	83	1,084
Interests in, and loans to, joint ventures and associates	1,699	5	4	—	1,708
Property and equipment	253	94	5	39	391
Investment property	9,956	139	—	720	10,815
Loans	24,085	433	—	19	24,537
Financial investments	175,846	9,266	39	3,927	189,078
Deferred acquisition costs	1,615	939	14	—	2,568
Other assets	29,307	7,237	453	4,388	41,385
Assets of operations classified as held for sale	42,564	11	28	—	42,603
Total assets	286,485	19,330	626	9,248	315,689
Gross insurance liabilities	98,086	15,005	—	—	113,091
Gross liabilities for investment contracts	110,494	—	—	—	110,494
Unallocated divisible surplus	6,931	—	—	—	6,931
Net asset value attributable to unitholders	4,963	—	—	6,183	11,146
External borrowings	3,034	—	—	5,160	8,194
Other liabilities, including inter-segment liabilities	8,778	(2,661)	334	6,611	13,062
Liabilities of operations classified as held for sale	41,237	2	13	159	41,411
Total liabilities	273,523	12,346	347	18,113	304,329
Total equity					11,360
Total equity and liabilities					315,689

b (iv) Segmental statement of financial position – products and services as at 31 December 2011

	Restated ² Long-term Business £m	General insurance and health £m	Fund management £m	Other ¹ £m	Restated ² Total £m
Goodwill	1,466	1,067	29	78	2,640
Acquired value of in-force business and intangible assets	1,742	145	44	90	2,021
Interests in, and loans to, joint ventures and associates	2,035	5	—	778	2,818
Property and equipment	395	34	16	65	510
Investment property	10,686	152	—	800	11,638
Loans	27,511	605	—	—	28,116
Financial investments	203,247	9,391	43	3,377	216,058
Deferred acquisition costs	3,755	986	14	—	4,755
Other assets	31,023	6,717	495	5,159	43,394
Assets of operations classified as held for sale	426	—	—	—	426
Total assets	282,286	19,102	641	10,347	312,376
Gross insurance liabilities	132,138	15,241	—	—	147,379
Gross liabilities for investment contracts	113,366	—	—	—	113,366
Unallocated divisible surplus	650	—	—	—	650
Net asset value attributable to unitholders	4,659	—	—	5,693	10,352
External borrowings	3,016	—	—	5,434	8,450
Other liabilities, including inter-segment liabilities	12,430	(3,170)	374	6,819	16,453
Liabilities of operations classified as held for sale	363	—	—	—	363
Total liabilities	266,622	12,071	374	17,946	297,013
Total equity					15,363
Total equity and liabilities					312,376

1 "Other" includes Delta Lloyd as an associate.

2 Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

5 – Details of income

This note gives further detail on the items appearing in the income section of the consolidated income statement.

Continuing operations	2012 £m	Restated ¹ 2011 £m
Gross written premiums (note 4a and 4b)		
Long-term:		
Insurance contracts	9,683	11,671
Participating investment contracts	3,526	4,834
General insurance and health	9,535	9,750
	22,744	26,255
Less: Premiums ceded to reinsurers (note 4a and 4b)	(1,571)	(1,548)
Gross change in provision for unearned premiums (note 39e)	(21)	(189)
Reinsurers' share of change in provision for unearned premiums (note 42ciii)	5	(47)
Net change in provision for unearned premiums	(16)	(236)
Net earned premiums	21,157	24,471
Fee and commission income		
Fee income from investment contract business	461	519
Fund management fee income	330	368
Other fee income	304	445
Reinsurance commissions receivable	92	71
Other commission income	41	33
Net change in deferred revenue	45	29
	1,273	1,465
Total revenue	22,430	25,936
Net investment income		
Interest and similar income		
From financial instruments designated as trading and other than trading	5,737	6,088
From AFS investments and financial instruments at amortised cost	83	83
	5,820	6,171
Dividend income	1,652	1,627
Other income from investments designated as trading		
Realised (losses)/gains on disposals	(667)	(388)
Unrealised gains and losses (policy J)		
(Losses)/gains arising in the year	(697)	(319)
Losses/(gains) recognised in prior periods and now realised	667	388
	(30)	69
	(697)	(319)
Other income from investments designated as other than trading		
Realised gains on disposals	1,844	1,729
Unrealised gains and losses (see policy J)		
Gains/(losses) arising in the year	14,239	(3,827)
(Gains) recognised in prior periods and now realised	(1,844)	(1,729)
	12,395	(5,556)
	14,239	(3,827)
Realised gains and losses on AFS investments		
Gains recognised in prior periods as unrealised in equity	(1)	(1)
Net income from investment properties		
Rent	648	690
Expenses relating to these properties	(57)	(39)
Realised gains on disposal	7	8
Fair value (losses)/gains on investment properties	(492)	148
	106	807
Realised (losses)/gains on loans	(9)	—
Foreign exchange gains and losses on investments other than trading	132	(12)
Other investment (expenses)	(136)	(105)
Net investment income	21,106	4,341
Share of (loss) after tax of joint ventures	(38)	(38)
Share of (loss) after tax of associates	(239)	(85)
Share of (loss) after tax of joint ventures and associates	(277)	(123)
(Loss)/profit on disposal of subsidiaries and associates (note 3b)	(164)	565
Income from continuing operations	43,095	30,719
Income from discontinued operations	3,494	7,800
Total income	46,589	38,519

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

6 – Details of expenses

This note gives further detail on the items appearing in the expenses section of the consolidated income statement.

Continuing operations	2012 £m	Restated ¹ 2011 £m
Claims and benefits paid		
Claims and benefits paid to policyholders on long-term business		
Insurance contracts	12,382	12,250
Participating investment contracts	6,500	6,835
Non-participating investment contracts	33	38
Claims and benefits paid to policyholders on general insurance and health business	6,050	6,264
	24,965	25,387
Less: Claim recoveries from reinsurers		
Insurance contracts	(1,197)	(832)
Participating investment contracts	(167)	(175)
Claims and benefits paid, net of recoveries from reinsurers	23,601	24,380
Change in insurance liabilities		
Change in insurance liabilities	663	2,583
Change in reinsurance asset for insurance provisions	(233)	(299)
Change in insurance liabilities, net of reinsurance	430	2,284
Change in investment contract provisions		
Investment income allocated to investment contracts	3,178	(363)
Other changes in provisions		
Participating investment contracts (note 40)	759	(944)
Non-participating investment contracts	525	(174)
Change in reinsurance asset for investment contract provisions	(12)	3
Change in investment contract provisions	4,450	(1,478)
Change in unallocated divisible surplus (note 44)	6,316	(2,721)
Fee and commission expense		
Acquisition costs		
Commission expenses for insurance and participating investment contracts	2,393	2,476
Change in deferred acquisition costs for insurance and participating investment contracts	131	(2)
Deferrable costs for non-participating investment contracts	126	66
Other acquisition costs	970	1,113
Change in deferred acquisition costs for non-participating investment contracts	85	46
Investment income attributable to unitholders	456	252
Reinsurance commissions and other fee and commission expense	311	375
	4,472	4,326
Other expenses		
Other operating expenses		
Staff costs (note 10b)	1,122	1,160
Central costs and sharesave schemes	136	138
Depreciation (note 20)	42	54
Impairment of goodwill on subsidiaries (note 16)	109	160
Amortisation of acquired value of in-force business on insurance contracts (note 17)	43	70
Amortisation of intangible assets (note 17)	96	111
Impairment of acquired value of in-force business (note 17)	73	—
Impairment of intangible assets (note 17)	49	49
Integration and restructuring costs (see below)	461	261
Exceptional items (see below)	—	—
Other expenses	664	657
	2,795	2,660
Impairments		
Net impairment on loans	43	62
Net impairment on financial investments	—	2
Net impairment on receivables and other financial assets	3	31
Net impairment on non-financial assets	—	1
	46	96
Other net foreign exchange (gains)/losses	4	23
Finance costs (note 7)	735	776
Expenses from continuing operations	42,849	30,346
Expenses from discontinued operations	6,190	8,264
Total expenses	49,039	38,610

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this reclassification.

6 – Details of expenses continued

Integration and restructuring costs

Integration and restructuring costs from continuing operations are £461 million (2011: £261 million). This includes restructuring and transformation activity that has been taken to align our business operations with our strategy, including the Group's Simplify programme (£165 million), Ireland transformation (£130 million) including the merger of our UK and Ireland businesses, £24 million in relation to the transformation of Aviva Investors and £25 million in respect of other restructuring activities. This also includes a cost of £117 million relating to preparing the business for the implementation of Solvency II.

Exceptional items

Exceptional items relating to continuing operations totalled £nil million (2011: £57 million net credit) in the year.

For the year ended 31 December 2011, this comprised:

- £22 million provision for compensation scheme costs for the leveraged property fund in Ireland; and
- £35 million expense for the discounted cost of strengthening latent claims provisions in the UK.

The table below sets out the lines of the income statement in which the exceptional items have been included:

	2012 £m	2011 £m
Change in insurance liabilities, net of reinsurance (note 39)	—	(57)
Other expenses (as above)	—	—
Total continuing operations	—	(57)
Total discontinued operations	—	—
	—	(57)

7 – Finance costs

This note analyses the interest costs on our borrowings (which are described in note 48) and similar charges.

Finance costs comprise:

	2012 £m	2011 £m
Continuing operations		
Interest expense on core structural borrowings		
Subordinated debt	294	302
Long term senior debt	19	19
Commercial paper	4	3
	317	324
Interest expense on operational borrowings		
Amounts owed to financial institutions	111	125
Securitised mortgage loan notes at fair value	90	88
	201	213
Interest on collateral received	27	33
Net finance charge on pension schemes (note 47e(iv))	82	87
Unwind of discount on GI reserves	21	24
Other similar charges	87	95
Total finance costs from continuing operations	735	776
Total finance costs from discontinued operations	21	284
Total finance costs	756	1,060

8 – Long-term business economic volatility

The long-term nature of much of the Group's operations means that, for management's decision-making and internal performance management, the effects of short-term economic volatility are treated as non-operating items. The Group focuses instead on an operating profit measure that incorporates an expected return on investments supporting its long-term business, as described below.

(a) Definitions

Operating profit for long-term business is based on expected investment returns on financial investments backing shareholder and policyholder funds over the reporting period, with consistent allowance for the corresponding expected movements in liabilities. Operating profit includes the effect of variance in experience for non-economic items, such as mortality, persistency and expenses, and the effect of changes in non-economic assumptions, where not treated as exceptional. Changes due to economic items, such as market value movements and interest rate changes, which give rise to variances between actual and expected investment returns, and the impact of changes in economic assumptions on liabilities, are disclosed separately outside operating profit.

(b) Economic volatility

The investment variances and economic assumption changes excluded from the long-term business operating profit are as follows:

	2012 £m	2011 £m
Long-term business		
Investment variances and economic assumptions – continuing operations	(620)	(897)
Investment variances and economic assumptions – discontinued operations	342	(719)
Investment variances and economic assumptions	(278)	(1,616)

For continuing operations, negative investment variances of £620 million (2011: £897 million negative) mainly relate to the UK. The total for the UK includes increasing the allowance for credit defaults on UK commercial mortgages together with some adverse current year experience on this portfolio, and the cost of de-risking activity. Elsewhere, positive variances in Spain and France were offset by a negative variance in Italy. In the prior period, the negative variance resulted from market falls and increased volatility in asset values in all major markets.

The positive variance of £342 million for discontinued operations relates to the US, driven by reductions in interest rates and credit spreads and the impact of favourable equity market performance on embedded derivatives. The prior period negative variance (2011: £719 million negative) also includes the result for Delta Lloyd up to the partial disposal on 6 May 2011 of £820 million. Liabilities in Delta Lloyd are discounted using a yield curve based on a fully collateralised AAA bond portfolio. Over the period up to the partial disposal, the AAA collateralised bond credit spread narrowed by about 80bps as a result of changes in the underlying bond index, which was the main driver of the negative variance.

(c) Methodology

The expected investment returns and corresponding expected movements in long-term business liabilities are calculated separately for each principal long-term business unit.

The expected return on investments for both policyholders' and shareholders' funds is based on opening economic assumptions applied to the expected funds under management over the reporting period. Expected investment return assumptions are derived actively, based on market yields on risk-free fixed interest assets at the end of each financial year. The same margins are applied on a consistent basis across the Group to gross risk-free yields, to obtain investment return assumptions for equities and properties. Expected funds under management are equal to the opening value of funds under management, adjusted for sales and purchases during the period arising from expected operating experience.

The actual investment return is affected by differences between the actual and expected funds under management and changes in asset mix, as well as movements in interest rates. To the extent that these differences arise from the operating experience of the long-term business, or management decisions to change asset mix, the effect is included in the operating profit. The residual difference between actual and expected investment return is included in investment variances, outside operating profit but included in profit before tax.

The movement in liabilities included in operating profit reflects both the change in liabilities due to the expected return on investments and the impact of experience variances and assumption changes for non-economic items.

The effect of differences between actual and expected economic experience on liabilities, and changes to economic assumptions used to value liabilities, are taken outside operating profit. For many types of long-term business, including unit-linked and with-profits funds, movements in asset values are offset by corresponding changes in liabilities, limiting the net impact on profit. For other long-term business the profit impact of economic volatility depends on the degree of matching of assets and liabilities, and exposure to financial options and guarantees.

(d) Assumptions

The expected rate of investment return is determined using consistent assumptions between operations, having regard to local economic and market forecasts of investment return and asset classification under IFRS.

The principal assumptions underlying the calculation of the expected investment return for equities and properties are:

	Equities		Properties	
	2012 %	2011 %	2012 %	2011 %
United Kingdom	5.8	7.2	4.3	5.7
Eurozone	5.9	6.9	4.4	5.4

The expected return on equities and properties is calculated by reference to the 10-year swap rate in the relevant currency plus an appropriate risk margin. These are the same assumptions as are used under MCEV principles to calculate the longer-term investment return for the Group's long-term business.

For fixed interest securities classified as fair value, the expected investment returns are based on average prospective yields for the actual assets held less an adjustment for credit risks. Where such securities are classified as AFS, such as in the US, the expected investment return comprises the expected interest or dividend payments and amortisation of the premium or discount at purchase.

9 – Longer-term investment return and economic assumption changes for non-long-term business

For non-long-term business, the total investment income, including realised and unrealised gains, is split between a calculated longer-term return, which is included in operating profit, and short-term fluctuations from this, which are disclosed outside operating profit but are included in profit before tax. This note gives details of the longer-term return calculation and the relevant assumptions, as well as the economic assumption changes on our general insurance and health business.

(a) The short-term fluctuations in investment return and economic assumption changes attributable to the non-long-term business result and reported outside operating profit were as follows:

Non-long-term business	2012 £m	2011 £m
Short-term fluctuations in investment return (see (b) below) – continuing operations	7	(266)
Economic assumption changes – continuing operations (see (g) below)	(21)	(90)
	(14)	(356)
Short-term fluctuation in investment return – discontinued operations	—	(60)
	(14)	(416)

(b) The longer-term investment return and short-term fluctuation for continuing operations are as follows:

Non-long-term business – Continuing operations	2012 £m	2011 £m
Net investment income	827	602
Foreign exchange on unrealised gains/losses and other charges	(97)	(99)
	730	503
Analysed between:		
Longer-term investment return, reported within operating profit	723	769
Short-term fluctuation in investment return, reported outside operating profit		
General insurance and health	18	(124)
Other operations ¹	(11)	(142)
	7	(266)
	730	503

¹ Represents assets backing non-long-term business held by the France holding company.

(c) The longer-term investment return is calculated separately for each principal non-long-term business unit. In respect of equities and properties, the return is calculated by multiplying the opening market value of the investments, adjusted for sales and purchases during the year, by the longer-term rate of investment return.

The longer-term rate of investment return is determined using consistent assumptions between operations, having regard to local economic and market forecasts of investment return. The allocated longer-term return for other investments is the actual income receivable for the year. Actual income and longer-term investment return both contain the amortisation of the discounts/premium arising on the acquisition of fixed income securities. For other operations, the longer-term return reflects assets backing non-long-term business held in the France holding company.

(d) The total assets supporting the general insurance and health business, which contribute towards the longer-term return, are:

	2012 £m	Restated 2011 £m
Debt securities	9,297	9,371
Equity securities	774	551
Properties	139	152
Cash and cash equivalents	2,535	2,315
Other	5,997	6,476
Assets supporting general insurance and health business	18,742	18,865
Assets supporting other non-long-term business ¹	206	268
Total assets supporting non-long-term business	18,948	19,133

Figures for 2011 have been restated to include loan balances supporting general insurance and health business, which contribute to the longer-term investment return

¹ Represents assets in France holding company backing non-long-term business.

The principal assumptions underlying the calculation of the longer-term investment return are:

	Longer-term rates of return Equities		Longer-term rates of return Properties	
	2012 %	2011 %	2012 %	2011 %
United Kingdom	5.8	7.2	4.3	5.7
France	5.9	6.9	4.4	5.4
Ireland	5.9	6.9	4.4	5.4
Canada	5.8	7.0	4.3	5.5
Netherlands – Discontinued	—	6.9	—	5.4

The Group has applied the same economic assumptions for equities and properties as are used under MCEV principles to calculate the longer-term investment return for its non-long-term business in 2011 and 2012.

9 – Longer-term investment return and economic assumption changes for non-long-term business continued

(e) The table below compares the actual return on investments attributable to the non-long-term business, after deducting investment management expenses and charges, with the aggregate longer-term return over a five-year period.

	2008-2012 £m	2007-2011 £m
Continuing operations		
Actual return attributable to shareholders	3,095	3,175
Longer-term return credited to operating results	(3,902)	(4,114)
Excess of longer-term returns over actual returns	(807)	(939)

(f) The table below shows the sensitivity of the Group's non-long-term business operating profit for continuing operations before tax to changes in the longer-term rates of return:

Movement in investment return for	By	Change in	2012 £m	2011 £m
Equities	1% higher/lower	Group operating profit before tax	6	4
Properties	1% higher/lower	Group operating profit before tax	2	1

(g) The economic assumption changes mainly arise from movements in the rate used to discount latent claims.

As explained in accounting policy K, provisions for latent claims are discounted, using rates based on the relevant swap curve, in the relevant currency at the reporting date, having regard to the duration of the expected settlement of the claims. The discount rate is set at the start of the accounting period, with any change in rates between the start and end of the accounting period being reflected below operating profit as an economic assumption change. The range of discount rates used is disclosed in note 39.

10 – Employee information

This note shows where our staff are employed throughout the world, excluding staff employed by our joint ventures and associates, and analyses the total staff costs.

(a) Employee numbers

The number of persons employed by the Group, including directors under a service contract, was:

	At 31 December		Average for the year	
	2012 Number	2011 Number	2012 Number	2011 Number
Continuing operations				
United Kingdom & Ireland	17,580	19,176	18,695	21,835
France	4,272	4,347	4,261	4,380
Spain	570	578	570	580
Italy	641	618	641	606
Canada	3,758	3,599	3,729	3,552
Other	24	422	217	503
Developed markets	26,845	28,740	28,113	31,456
Higher Growth markets	2,669	3,607	3,509	3,516
Aviva Investors	1,056	1,152	1,134	1,179
Group other	641	1,109	833	887
Employees in continuing operations	31,211	34,608	33,639	37,038
Employees in discontinued operations	1,911	1,954	1,941	3,802
Total employee numbers	33,122	36,562	35,580	40,840

10 – Employee information continued

(b) Staff costs

	2012 £m	2011 £m
Continuing operations		
Wages and salaries	1,324	1,421
Social security costs	205	219
Post-retirement obligations		
Defined benefit schemes (note 47d)	19	58
Defined contribution schemes (note 47d)	102	86
Profit sharing and incentive plans	112	126
Equity compensation plans (note 30d)	47	58
Termination benefits	41	21
Staff costs from continuing operations	1,850	1,989
Staff costs from discontinued operations	145	343
Total staff costs	1,995	2,332

Staff costs are charged within:

	2012 £m	2011 £m
Continuing operations		
Acquisition costs	522	597
Claims handling expenses	158	222
Central costs and sharesave schemes	48	10
Other operating expenses	1,122	1,160
Staff costs from continuing operations	1,850	1,989
Staff costs from discontinued operations	145	343
Total staff costs	1,995	2,332

11 – Directors

Information concerning individual directors' emoluments, interests and transactions is given in the Directors' Remuneration Report on pages 104 to 120 in the 'Corporate governance' section of this report. For the purposes of the disclosure required by Schedule 5 to the Companies Act 2006, the total aggregate emoluments of the directors in respect of 2012 was £6.3 million (2011: £7.7 million). Employer contributions to pensions for executive directors for qualifying periods were £179,200 (2011: £71,900). The aggregate net value of share awards granted to the directors in the period was £8.9 million (2011: £12.1 million). The net value has been calculated by reference to the closing middle market price of an ordinary share at the date of grant. During the year, no share options were exercised by directors (2011: nil).

12 – Auditors' remuneration

This note shows the total remuneration payable by the Group to our auditors. PricewaterhouseCoopers LLP (PwC) replaced Ernst & Young LLP (E&Y) as the Group's principal auditor for the 2012 financial year.

The total remuneration payable by the Group, excluding VAT and any overseas equivalent thereof, to its principal auditors and their associates is shown below.

	2012 £m
Continuing operations	
Fees payable to PwC LLP and its associates for the statutory audit of the Aviva Group and Company financial statements	2.2
Fees payable to PwC LLP and its associates for other services: Audit of Group subsidiaries	9.6
Total audit fees	11.8
Audit related assurance	2.3
Other assurance services	7.2
Total audit and assurance fees	21.3
Tax compliance services	0.4
Tax advisory services	0.1
Services relating to corporate finance transactions	0.3
Other non-audit services not covered above	7.7
Fees payable to PwC LLP and its associates for services to Group companies classified as continuing operations	29.8
Discontinued operations	
Fees payable to PwC LLP and its associates for Audit of Group subsidiaries	1.7
Fees payable to PwC LLP and its associates for other non-audit services to Group subsidiaries	0.3
Total fees payable to PwC LLP and its associates for services to Group companies	31.8
	2011 £m
Continuing operations	
Fees payable to E&Y LLP and its associates for the statutory audit of the Aviva Group and Company financial statements	2.5
Fees payable to E&Y LLP and its associates for other services: Audit of Group subsidiaries	10.3
Additional fees related to the prior year audit of Group subsidiaries	0.9
Total audit fees	13.7
Audit related assurance	2.7
Other assurance services	5.6
Total audit and assurance fees	22.0
Tax compliance services	0.2
Other non audit services not covered above	2.0
Fees payable to E&Y LLP and its associates for services to Group companies classified as continuing operations	24.2
Discontinued operations	
Fees payable to E&Y LLP and its associates for audit of Group subsidiaries	3.6
Fees payable to E&Y LLP and its associates for other assurance services to Group subsidiaries	0.5
Fees payable to E&Y LLP and its associates for other non-audit services to Group subsidiaries	0.2
Total fees payable to E&Y LLP and its associates for services to Group companies	28.5

The tables above reflect the disclosure requirements of SI2011/2198 – The Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) (Amendment) Regulations 2011. Comparatives for 2011 have been adjusted accordingly.

In addition to the fees for 2012 shown above, during 2012 the Group paid PwC £0.2 million in relation to the audit of Group occupational pension schemes and paid E&Y £1.0 million in relation to the 2011 audit of group subsidiaries.

Fees payable for the audit of the Group's subsidiaries include fees for the statutory audit of the subsidiaries, both inside and outside the UK, and for the work performed by the principal auditors in respect of the subsidiaries for the purpose of the consolidated financial statements of the Group.

Audit related assurance comprises services in relation to statutory and regulatory filings. These include audit services for the audit of FSA returns in the UK and review of interim financial information under the Listing Rules of the UK Listing Authority.

Fees for other assurance services comprise non statutory assurance work which is customarily performed by the external auditor, including the audit of the Group's MCEV reporting. Although embedded value is a primary management reporting basis and our disclosures require a full audit, the relevant fees are not classified as being for statutory audit.

As noted above PwC replaced E&Y as the group's principal auditor for the 2012 year. Prior to 2012, PwC was a significant provider of consulting services to the Group. The level of 2012 fees for non-audit services therefore includes fees billed in the year relating to projects that commenced prior to PwC's appointment as auditor. All of these services are in compliance with applicable UK, US and IFAC independence rules. We do not expect PwC's non-audit fees to continue at this level in the future.

Other assurance services in 2012 includes fees relating to the audit of the Group's MCEV reporting of £1.3 million, £1.8 million for examination of the Group Individual Capital Assessment and Economic Capital, and £3.4 million associated with assurance services to prepare the businesses for Solvency II implementation.

The 2012 fees for other non-audit services for continuing operations of £7.7 million includes advice to our European businesses in relation to the risk management aspects of Solvency II (£1.9 million), £1.9 million relating to four regulatory advice engagements, £0.7 million relating to restructuring at Aviva Investors, £0.3 million for risk training, £0.3 million supporting an industry-wide competition review, £0.3 million for an additional claims reserves review and £2.3 million for other services. The 2012 fees for tax compliance services of £0.4 million includes fees for one engagement in Higher Growth markets of £0.3 million, and fees for corporate finance transactions of £0.3 million relates to an engagement for an Aviva Investors property fund.

Details of the Group's process for safeguarding and supporting the independence and objectivity of the external auditors are given in the Audit Committee report.

13 – Tax

This note analyses the tax charge/(credit) for the year and explains the factors that affect it.

(a) Tax charged/(credited) to the income statement

(i) The total tax charge/(credit) comprises:

	2012 £m	2011 £m
Current tax		
For this year	516	535
Prior year adjustments	(47)	(10)
Total current tax from continuing operations	469	525
Deferred tax		
Origination and reversal of temporary differences	(52)	(599)
Changes in tax rates or tax laws	(12)	(28)
Write-down of deferred tax assets	43	58
Total deferred tax from continuing operations	(21)	(569)
Total tax charged/(credited) to income statement from continuing operations	448	(44)
Total tax charged/(credited) to income statement from discontinued operations	152	(107)
Total tax charged/(credited) to income statement	600	(151)

(ii) The Group, as a proxy for policyholders in the UK, Ireland and Singapore, is required to record taxes on investment income and gains each year. Accordingly, the tax benefit or expense attributable to UK, Irish and Singapore life insurance policyholder returns is included in the tax charge/(credit). The tax charge attributable to policyholders' returns included in the charge above is £221 million (2011: £178 million credit).

(iii) The tax charge/(credit) can be analysed as follows:

	2012 £m	2011 £m
UK tax	(34)	(304)
Overseas tax	634	153
	600	(151)

(iv) Unrecognised tax losses and temporary differences of previous years were used to reduce the current tax expense and deferred tax expense by £7 million and £11 million (2011: £25 million and £108 million), respectively.

(v) Deferred tax charged/(credited) to the income statement represents movements on the following items:

	2012 £m	2011 £m
Long-term business technical provisions and other insurance items	(1,868)	916
Deferred acquisition costs	254	(3)
Unrealised gains/(losses) on investments	2,312	(1,265)
Pensions and other post-retirement obligations	(7)	6
Unused losses and tax credits	(30)	22
Subsidiaries, associates and joint ventures	—	1
Intangibles and additional value of in-force long-term business	(12)	(10)
Provisions and other temporary differences	(670)	(236)
Deferred tax credited to income statement from continuing operations	(21)	(569)
Deferred tax charged to income statement from discontinued operations	143	56
Total deferred tax charged/(credited) to income statement	122	(513)

(b) Tax (credited)/charged to other comprehensive income

(i) The total tax (credit)/charge comprises:

	2012 £m	2011 £m
Current tax from continuing operations		
In respect of pensions and other post-retirement obligations	(14)	(88)
In respect of foreign exchange movements	(17)	(8)
	(31)	(96)
Deferred tax from continuing operations		
In respect of pensions and other post-retirement obligations	(140)	260
In respect of fair value gains on owner-occupied properties	(1)	(1)
In respect of unrealised gains on investments	9	(3)
	(132)	256
Tax (credited)/charged to other comprehensive income arising from continuing operations	(163)	160
Tax charged to other comprehensive income arising from discontinued operations	107	98
Total tax (credited)/charged to other comprehensive income	(56)	258

13 – Tax continued

(ii) The tax charge attributable to policyholders' returns included above is £nil (2011: £nil).

(c) Tax credited to equity

Tax credited directly to equity in the year amounted to £18 million (2011: £16 million), and is wholly in respect of coupon payments on the direct capital instruments and fixed rate tier 1 notes.

(d) Tax reconciliation

The tax on the Group's (loss)/profit before tax differs from the theoretical amount that would arise using the tax rate of the home country of the Company as follows:

	2012			2011		
	Shareholder £m	Policyholder £m	Total £m	Shareholder £m	Policyholder £m	Total £m
Total (loss)/profit before tax	(2,671)	221	(2,450)	87	(178)	(91)
Tax calculated at standard UK corporation tax rate of 24.5% (2011: 26.5%)	(654)	54	(600)	23	(47)	(24)
Reconciling items						
Different basis of tax – policyholders	—	170	170	—	(129)	(129)
Adjustment to tax charge in respect of prior years	(20)	—	(20)	(25)	—	(25)
Non-assessable income	(86)	—	(86)	(60)	—	(60)
Non-taxable loss/(profit) on sale of subsidiaries and associates	872	—	872	(135)	—	(135)
Disallowable expenses	418	—	418	215	—	215
Different local basis of tax on overseas profits	(141)	(3)	(144)	84	(2)	82
Change in future local statutory tax rates	(12)	—	(12)	(32)	—	(32)
Movement in deferred tax not recognised	(69)	—	(69)	(5)	—	(5)
Tax effect of loss/(profit) from associates and joint ventures	75	—	75	(41)	—	(41)
Other	(4)	—	(4)	3	—	3
Total tax charged/(credited) to income statement	379	221	600	27	(178)	(151)

The tax charge/(credit) attributable to policyholders' returns is removed from the Group's total loss before tax in arriving at the Group's (loss)/profit before tax attributable to shareholders' profits. As the net of tax profits attributable to with-profit and unit-linked policyholders is zero, the Group's pre-tax profit/(loss) attributable to policyholders is an amount equal and opposite to the tax charge/(credit) attributable to policyholders included in the total tax charge/(credit). The difference between the policyholder tax charge/(credit) and the impact of this item in the tax reconciliation can be explained as follows:

	2012 £m	2011 £m
Tax attributable to policyholder returns	221	(178)
UK corporation tax at a rate of 24.5% (2011: 26.5%) in respect of the policyholder tax deduction	(54)	47
Different local basis of tax of overseas profits	3	2
Different basis of tax – policyholders per tax reconciliation	170	(129)

The UK corporation tax rate reduced to 24% from 1 April 2012. A subsequent reduction in the UK corporation tax rate to 23% was substantively enacted on 3 July 2012 and will apply from 1 April 2013. The substantively enacted rate of 23% has been used in the calculation of the UK's deferred tax assets and liabilities.

As announced in the 2012 Autumn Statement, the rate is expected to reduce further to 21% from 1 April 2014. The aggregate impact of the reduction in rate from 23% to 21% would reduce the deferred tax assets and liabilities and increase IFRS net assets by approximately £31 million and will be recognised when the legislation is substantively enacted.

Finance Act 2012 included initial legislation introducing considerable changes to the regime for taxing UK life insurance companies applicable from 1 January 2013. The impact of the legislation has been included in the results of the Group for the year ended 31 December 2012 but has not had a material impact.

14 – (Loss)/earnings per share

This note shows how we calculate (loss)/earnings per share, based both on the present shares in issue (the basic (loss)/earnings per share) and the potential future shares in issue, including conversion of share options granted to employees (the diluted earnings per share). We have also shown the same calculations based on our operating profit as we believe this gives a better indication of operating performance.

(a) Basic (loss)/earnings per share

(i) The (loss)/profit attributable to ordinary shareholders is:

	2012			2011		
	Operating profit £m	Non-operating items £m	Total £m	Operating profit £m	Non-operating items £m	Total £m
Continuing operations						
Profit/(loss) before tax attributable to shareholders' profits	1,888	(1,970)	(82)	2,089	(1,504)	585
Share of Delta Lloyd's tax expense as an associate	(28)	135	107	(39)	5	(34)
Profit/(loss) before tax	1,860	(1,835)	25	2,050	(1,499)	551
Tax attributable to shareholders' profit/(loss)	(465)	238	(227)	(487)	353	(134)
Profit/(loss) for the year	1,395	(1,597)	(202)	1,563	(1,146)	417
Amount attributable to non-controlling interests	(184)	16	(168)	(150)	109	(41)
Cumulative preference dividends for the year	(17)	—	(17)	(17)	—	(17)
Coupon payments in respect of direct capital instruments (DCI) and fixed rate tier 1 notes (net of tax)	(55)	—	(55)	(43)	—	(43)
Profit/(loss) attributable to ordinary shareholders from continuing operations	1,139	(1,581)	(442)	1,353	(1,037)	316
Profit/(loss) attributable to ordinary shareholders from discontinued operations	161	(3,009)	(2,848)	178	(329)	(151)
Profit/(loss) attributable to ordinary shareholders	1,300	(4,590)	(3,290)	1,531	(1,366)	165

(ii) Basic (loss)/earnings per share is calculated as follows:

	2012			2011		
	Before tax £m	Net of tax, non-controlling interests, preference dividends and DCI ¹ £m	Per share p	Before tax £m	Net of tax, non-controlling interests, preference dividends and DCI £m	Per share p
Continuing operations						
Operating profit attributable to ordinary shareholders	1,888	1,139	39.2	2,089	1,353	47.6
Non-operating items:						
Investment return variances and economic assumption changes on long-term business	(620)	(499)	(17.2)	(897)	(599)	(21.1)
Short-term fluctuation in return on investments backing non-long-term business	7	9	0.3	(266)	(198)	(7.0)
Economic assumption changes on general insurance and health business	(21)	(16)	(0.6)	(90)	(67)	(2.3)
Impairment of goodwill, associates and joint ventures	(60)	(60)	(2.1)	(392)	(359)	(12.6)
Amortisation and net impairment of intangibles	(128)	(84)	(2.9)	(116)	(141)	(5.1)
(Loss)/profit on disposal of subsidiaries and associates	(164)	(164)	(5.6)	565	552	19.5
Integration and restructuring costs and exceptional items	(461)	(379)	(13.0)	(318)	(240)	(8.4)
Share of Delta Lloyd's non-operating items (before tax) as an associate	(523)	(388)	(13.3)	10	15	0.5
Share of Delta Lloyd's tax expense, as an associate	107	—	—	(34)	—	—
(Loss)/profit attributable to ordinary shareholders from continuing operations	25	(442)	(15.2)	551	316	11.1
(Loss)/profit attributable to ordinary shareholders from discontinued operations	(2,696)	(2,848)	(97.9)	(464)	(151)	(5.3)
(Loss)/profit attributable to ordinary shareholders	(2,671)	(3,290)	(113.1)	87	165	5.8

¹ DCI includes direct capital instruments and fixed rate tier 1 notes

(iii) The calculation of basic (loss)/earnings per share uses a weighted average of 2,910 million (2011: 2,845 million) ordinary shares in issue, after deducting shares owned by the employee share trusts. The actual number of shares in issue at 31 December 2012 was 2,946 million (2011: 2,906 million) and 2,936 million (2011: 2,892 million) excluding shares owned by the employee share trusts.

14 – (Loss)/earnings per share continued**(b) Diluted earnings per share**

(i) Diluted earnings per share is calculated as follows:

	2012			2011		
	Total £m	Weighted average number of shares million	Per share p	Total £m	Weighted average number of shares million	Per share p
(Loss)/profit attributable to ordinary shareholders	(442)	2,910	(15.2)	316	2,845	11.1
Dilutive effect of share awards and options	—	44	—	—	50	(0.2)
Diluted (loss)/earnings per share from continuing operations¹	(442)	2,954	(15.2)	316	2,895	10.9
(Loss)/profit attributable to ordinary shareholders	(2,848)	2,910	(97.9)	(151)	2,845	(5.3)
Dilutive effect of share awards and options	—	44	—	—	50	—
Diluted (loss)/earnings per share from discontinued operations¹	(2,848)	2,954	(97.9)	(151)	2,895	(5.3)
Diluted (loss)/earnings per share¹	(3,290)	2,954	(113.1)	165	2,895	5.7

¹ Losses have an anti-dilutive effect. Therefore the basic and diluted earnings for 2012 and the diluted earnings for 2011, have remained the same.

(ii) Diluted earnings per share on operating profit attributable to ordinary shareholders is calculated as follows:

	2012			2011		
	Total £m	Weighted average number of shares million	Per share p	Total £m	Weighted average number of shares million	Per share p
Operating profit attributable to ordinary shareholders	1,139	2,910	39.2	1,353	2,845	47.5
Dilutive effect of share awards and options	—	44	(0.6)	—	50	(0.8)
Diluted operating profit per share from continuing operations	1,139	2,954	38.6	1,353	2,895	46.7
Operating profit attributable to ordinary shareholders	161	2,910	5.5	178	2,845	6.3
Dilutive effect of share awards and options	—	44	(0.1)	—	50	(0.1)
Diluted operating profit per share from discontinued operations	161	2,954	5.4	178	2,895	6.2
Diluted operating profit per share	1,300	2,954	44.0	1,531	2,895	52.9

15 – Dividends and appropriations

This note analyses the total dividends and other appropriations we paid during the year. The table below does not include the final dividend proposed after the year end because it is not accrued in these financial statements. The impact of shares issued in lieu of dividends is shown separately in note 36.

	2012 £m	2011 £m
Ordinary dividends declared and charged to equity in the year		
Final 2011 – 16.00 pence per share, paid on 17 May 2012	465	—
Final 2010 – 16.00 pence per share, paid on 17 May 2011	—	451
Interim 2012 – 10.00 pence per share, paid on 16 November 2012	292	—
Interim 2011 – 10.00 pence per share, paid on 17 November 2011	—	287
	757	738
Preference dividends declared and charged to equity in the year	17	17
Coupon payments on direct capital instruments and fixed rate tier 1 notes	73	58
	847	813

Subsequent to 31 December 2012, the directors proposed a final dividend for 2012 of 9.0 pence per ordinary share (2011: 16.0 pence), amounting to £265 million (2011: £465 million) in total. Subject to approval by shareholders at the AGM, the dividend will be paid on 17 May 2013 and will be accounted for as an appropriation of retained earnings in the year ending 31 December 2013.

Interest payments on the direct capital instruments issued in November 2004 and the fixed rate tier 1 notes issued in May 2012 are treated as an appropriation of retained profits and, accordingly, are accounted for when paid. Tax relief is obtained at a rate of 24.5% (2011: 26.5%).

16 – Goodwill

This note analyses the changes to the carrying amount of goodwill during the year, and details the results of our impairment testing on both goodwill and intangible assets with indefinite lives.

(a) Carrying amount

	2012 £m	2011 £m
Gross amount		
At 1 January	2,850	3,671
Acquisitions and additions	1	13
Disposals	(13)	(284)
Deconsolidation of Delta Lloyd	—	(542)
Foreign exchange rate movements	(64)	(8)
At 31 December	2,774	2,850
Accumulated impairment		
At 1 January	(210)	(280)
Impairment losses charged to expenses	(891)	(160)
Disposals	10	—
Deconsolidation of Delta Lloyd	—	226
Foreign exchange rate movements	20	4
At 31 December	(1,071)	(210)
Carrying amount at 1 January	2,640	3,391
Carrying amount at 31 December	1,703	2,640
Less: Assets classified as held for sale	(183)	—
Carrying amount at 31 December	1,520	2,640

Goodwill on acquisitions and additions arose on the acquisition of a small long-term insurance business in Spain and a small general insurance business in Canada.

Goodwill impairment charges of £891 million have been recognised as expenses. Together with impairment charges of £9 million recognised in respect of goodwill within interests in joint ventures (note 18), and impairment charges of £147 million recognised in respect of goodwill within interests in associates (note 19) the goodwill write down for the year was £1,047 million. After a reversal of a previously recognised impairment of the Delta Lloyd associate of £205 million (note 19) the total charge for impairment of goodwill, joint ventures and associates for the year was £842 million.

Goodwill disposed of during the year relates to the Group's Sri Lanka subsidiary (see note 3(b)).

Goodwill classified as held for sale consists of £180 million relating to Aseval, a Spanish long-term business, and £3 million relating to the Russian long-term business (see note 3(c)).

(b) Goodwill allocation and impairment testing

A summary of the goodwill and intangibles with indefinite useful lives allocated to cash-generating units is presented below.

	Carrying amount of goodwill		Carrying amount of intangibles with indefinite useful lives (detailed in note 17)		Total	
	2012 £m	2011 £m	2012 £m	2011 £m	2012 £m	2011 £m
United Kingdom – general insurance and health	924	924	—	—	924	924
Ireland – general insurance and health	112	116	—	—	112	116
France – long-term business	—	—	51	52	51	52
Italy						
Long-term business	35	64	—	—	35	64
General insurance and health	37	44	—	—	37	44
Spain – long-term business	450	542	—	—	450	542
United States						
Long-term business	—	800	—	—	—	800
Fund management	27	29	—	—	27	29
Canada	50	50	—	—	50	50
Other developed markets	—	—	—	—	—	—
Higher growth markets	68	71	—	—	68	71
	1,703	2,640	51	52	1,754	2,692

Goodwill in all business units is tested for impairment by comparing the carrying value of the cash generating unit to which the goodwill relates to the recoverable value of that cash generating unit. The recoverable amount is the value in use of the cash generating unit unless otherwise stated.

Long-term business

Value in use is calculated as an actuarially determined appraisal value, based on the embedded value of the business calculated in accordance with market consistent embedded value ('MCEV') principles, together with the present value of expected profits from future new business. If the embedded value of the business tested is sufficient to demonstrate goodwill recoverability on its own, then it is not necessary to estimate the present value of expected profits from future new business.

If required, the present value of expected profits arising from future new business written over a given period is calculated on an MCEV basis, using profit projections based on the most recent three year business plans approved by management. These plans reflect management's best estimate of future profits based on both historical experience and expected growth rates for the relevant cash

16 – Goodwill continued

generating unit. The underlying assumptions of these projections include market share, customer numbers, mortality, morbidity and persistency.

Future new business profits for the remainder of the given period beyond the initial three years are extrapolated using a steady growth rate. Growth rates and expected future profits are set with regards to management estimates, past experience and relevant available market statistics.

Expected profits from future new business are discounted using a risk adjusted discount rate. The discount rate is a combination of a risk-free rate and a risk margin to make prudent allowance for the risk that experience in future years for new business may differ from that assumed.

See results of impairment testing for US long-term cash generating unit. For other businesses classified as held for sale the recoverable amount was assessed based on the fair value less costs to sell of the business, based on the expected net disposal proceeds of the businesses.

Key Assumptions

	Embedded value basis		Future new business profits growth rate		Future new business profits discount rate	
	2012	2011	2012 %	2011 %	2012 %	2011 %
Italy long-term business	MCEV	MCEV	2.0	3.0	10.6	10.8
Spain long-term business	MCEV	MCEV	0.0	3.0	7.9	5.3

General insurance, health, fund management and other businesses

Value in use is calculated as the discounted value of expected future profits of each business. The calculation uses cash flow projections based on business plans approved by management covering a three-year period. These plans reflect management's best estimate of future profits based on both historical experience and expected growth rates for the relevant cash generating unit. The underlying assumptions of these projections include market share, customer numbers, premium rate and fee income changes, claims inflation and commission rates.

Cash flows beyond that three-year period are extrapolated using a steady growth rate. Growth rates and expected future profits are set with regards to past experience and relevant available market statistics.

Future profits are discounted using a risk adjusted discount rate.

Key assumptions

	Extrapolated future profits growth rate		Future profits discount rate	
	2012 %	2011 %	2012 %	2011 %
United Kingdom general insurance and health	1.3	1.3	8.0	8.2
Ireland general insurance and health	2.0	2.0	10.6	13.7
Italy general insurance and health	2.0 – 3.0	2.0 – 3.0	9.0 – 11.4	9.2 – 10.3
United States (fund management)	3.0	3.0	17.0	17.0

France – indefinite life intangible asset

The recoverable amount of the indefinite life intangible asset has been assessed based on the fair value less costs to sell of the cash-generating unit to which it relates. The fair value less costs to sell was determined based on the quoted market value of the share of interest in the subsidiary to which it relates.

Results of impairment testing

Following the impairment business review conducted during the year the US long-term cash generating unit was tested for impairment and the Directors concluded that the goodwill associated with this cash generating unit was no longer recoverable. As a result, an impairment of £782 million was recognised during the period, reducing the carrying value of goodwill to £nil. Subsequently, the US business was classified as held for sale and recorded at its fair value less costs to sell (see Note 3).

Management concluded that the goodwill associated with the Spanish long-term cash generating unit, excluding Aseval which is held for sale, is no longer fully recoverable. An impairment of £76 million has been recognised reducing the carrying value of this cash generating unit to its recoverable amount as a result of a reduction to management's estimates for future profitability due to current economic circumstances.

Similarly, as a result of the test of the Italian long-term and general businesses, impairments of £27 million and £6 million respectively have been recognised.

Other than the CGUs noted above, the recoverable amount exceeds the carrying value of the cash generating units including goodwill.

17 – Acquired value of in-force business (AVIF) and intangible assets

This note shows the movements in cost and amortisation of the in-force business and intangible assets acquired when we have purchased subsidiaries.

	AVIF on insurance contracts ¹ £m	AVIF on investment contracts ² £m	Other intangible assets with finite useful lives £m	Intangible assets with indefinite useful lives (a) £m	Total £m
Gross amount					
At 1 January 2011	2,724	308	1,842	323	5,197
Additions	—	—	151	—	151
Acquisition of subsidiaries	—	—	3	—	3
Disposals	—	—	(63)	(204)	(267)
Movement in shadow adjustment	(123)	—	—	—	(123)
Deconsolidation of Delta Lloyd	(126)	—	(158)	—	(284)
Foreign exchange rate movements	(11)	(9)	(10)	(2)	(32)
At 31 December 2011	2,464	299	1,765	117	4,645
Additions	—	—	143	—	143
Acquisition of subsidiaries	—	—	2	—	2
Disposals	(160)	(5)	(134)	—	(299)
Movement in shadow adjustment	45	—	—	—	45
Transfers from property and equipment	—	—	3	—	3
Foreign exchange rate movements	(88)	(6)	(42)	(3)	(139)
At 31 December 2012	2,261	288	1,737	114	4,400
Accumulated amortisation					
At 1 January 2011	(1,362)	(113)	(663)	—	(2,138)
Amortisation for the year	(271)	(45)	(125)	—	(441)
Disposals	—	—	25	—	25
Deconsolidation of Delta Lloyd	98	—	117	—	215
Foreign exchange rate movements	—	3	(4)	—	(1)
At 31 December 2011	(1,535)	(155)	(650)	—	(2,340)
Amortisation for the year	(226)	(20)	(107)	—	(353)
Disposals	154	5	59	—	218
Foreign exchange rate movements	60	5	16	—	81
At 31 December 2012	(1,547)	(165)	(682)	—	(2,394)
Accumulated Impairment					
At 1 January 2011	(108)	—	(76)	(69)	(253)
Impairment losses charged to expenses (note 6)	(7)	—	(50)	—	(57)
Reversal of impairment losses	—	—	2	—	2
Disposals	2	—	9	3	14
Deconsolidation of Delta Lloyd	—	—	10	—	10
Foreign exchange rate movements	(1)	—	—	1	—
At 31 December 2011	(114)	—	(105)	(65)	(284)
Impairment losses charged to expenses (note 6)	(34)	(39)	(152)	—	(225)
Disposals	3	—	70	—	73
Foreign exchange rate movements	1	—	2	2	5
At 31 December 2012	(144)	(39)	(185)	(63)	(431)
Carrying amount					
At 1 January 2011	1,254	195	1,103	254	2,806
At 31 December 2011	815	144	1,010	52	2,021
At 31 December 2012	570	84	870	51	1,575
Less: Assets classified as held for sale	(443)	(39)	(9)	—	(491)
	127	45	861	51	1,084

1 On insurance and participating investment contracts.

2 On non-participating investment contracts.

- (a) Intangible assets with indefinite useful lives comprise the value of the Union Financière de France Banque distribution channel, where the existing lives of the assets and their competitive position in, and the stability of, their respective markets support this classification. Impairment testing of these intangibles is covered in note 16(b).
- (b) Other intangible assets with finite useful lives consist primarily of the value of bancassurance and other distribution agreements. Acquisitions of intangible assets with finite lives relate to Canadian broker businesses.

Disposals include the derecognition of exhausted assets which are fully amortised or impaired with nil carrying value.

Impairment losses on intangible assets with finite lives of £152 million arise from impairments of capitalised software in US long-term operations, UK long-term operations and UK general insurance operations of £102 million, £25 million and £22 million respectively, and £3 million in relation to other businesses. Impairment tests were conducted as described in note 16(b).

Excluding assets classified as held for sale, AVIF on insurance and investment contracts is generally recoverable in more than one year. Of the total AVIF of £172 million (£127 million on insurance contracts, £45 million on investment contracts), £131 million (2011: £713 million) is expected to be recovered more than one year after the statement of financial position date.

18 – Interests in, and loans to, joint ventures

In several business units, Group companies and other parties jointly control certain entities. This note analyses these interests and describes the principal joint ventures in which we are involved.

(a) Carrying amount

(i) The movements in the carrying amount comprised:

	2012				2011			
	Goodwill and intangibles £m	Equity interests £m	Loans £m	Total £m	Goodwill and intangibles £m	Equity interests £m	Loans £m	Total £m
At 1 January	147	1,465	100	1,712	187	1,446	375	2,008
Share of results before tax	—	(19)	—	(19)	—	(14)	—	(14)
Share of tax	—	(4)	—	(4)	—	(3)	—	(3)
Share of results after tax	—	(23)	—	(23)	—	(17)	—	(17)
Impairment of goodwill	(9)	—	—	(9)	(15)	—	—	(15)
Amortisation of intangibles ¹	(6)	—	—	(6)	(6)	—	—	(6)
Share of profit/loss after tax	(15)	(23)	—	(38)	(21)	(17)	—	(38)
Acquisitions	—	—	—	—	—	12	—	12
Additions	—	89	4	93	—	59	18	77
Reclassification to subsidiary	—	(107)	—	(107)	—	—	(282)	(282)
Reduction in Group interest	—	—	—	—	—	(1)	—	(1)
Disposals	—	(41)	—	(41)	—	(37)	—	(37)
Share of gains taken to other comprehensive income	—	21	—	21	—	7	—	7
Loans repaid	—	—	(12)	(12)	—	—	(17)	(17)
Dividend received	—	(5)	—	(5)	—	—	—	—
Foreign exchange rate movements	—	(4)	—	(4)	(19)	(4)	6	(17)
At 31 December	132	1,395	92	1,619	147	1,465	100	1,712
Less: Amounts classified as held for sale	(54)	(72)	—	(126)	—	(12)	—	(12)
	78	1,323	92	1,493	147	1,453	100	1,700

¹ Comprises amortisation of AVIF on insurance contracts of £3 million (2011: £3 million) and other intangibles of £3 million (2011: £3 million).

During 2010, the Group's Taiwan joint venture, First-Aviva Life Insurance Co., Ltd., was classified as held for sale following the decision of management to seek to dispose of the business. A sale of this business was not completed in 2012 and management have reviewed its classification as held for sale and determined that the classification remains appropriate. The disposal is expected to be completed within 12 months of the balance sheet date.

During 2012, the Group's Malaysian joint ventures, CIMB Aviva Assurance Berhad and CIMB Aviva Takaful Berhad, were classified as held for sale following the decision of management to seek to dispose of the businesses. On 17 January 2013 agreement was reached to sell Aviva's interests in these businesses to Sun Life Assurance Company of Canada. Upon receipt of regulatory approval the parties will work to close the proposed transaction during the first half of 2013. The expected proceeds of this transaction are £152 million. These businesses have been included in the statement of financial position at their carrying value.

Additions and disposals relate to the increase and reduction of investments in property management undertakings. The Group's principal interests in property management joint ventures are listed below.

(ii) The balances at 31 December comprised:

	2012				2011			
	Goodwill and intangibles £m	Equity interests £m	Loans £m	Total £m	Goodwill and intangibles £m	Equity interests £m	Loans £m	Total £m
Property management undertakings	—	1,050	92	1,142	—	1,145	100	1,245
Long-term business undertakings	132	339	—	471	147	315	—	462
General insurance undertakings	—	6	—	6	—	5	—	5
Total	132	1,395	92	1,619	147	1,465	100	1,712

The loans are not secured and no guarantees were received in respect thereof. They are interest-bearing and are repayable on termination of the relevant partnership.

(b) Property management undertakings

The principal joint ventures are as follows:

Company	GP proportion held	PLP proportion held
Airport Property Partnership	50.00%	50.00%
The Ashtenne Industrial Fund Limited Partnership	67.70%	43.66%
The Mall Limited Partnership	50.00%	50.52%
Paddington Central IV Unit Trust	50.00%	50.00%
Queensgate Limited Partnership	50.00%	50.00%
Quercus Healthcare Property Partnership Limited	50.00%	29.33%
The Southgate Limited Partnership	50.00%	50.00%

All the above entities perform property ownership and management activities, and are incorporated and operate in the UK. All these investments are held by subsidiary entities.

18 – Interests in, and loans to, joint ventures continued**(c) Long-term business undertakings**

The principal joint ventures are as follows:

Company	Proportion held	Country of incorporation and operation
Aviva-COFCO Life Insurance Co. Limited	50.00%	China
AvivaSA Emeklilik ve Hayat A.S.	49.83%	Turkey
CIMB Aviva Assurance Berhad	49.00%	Malaysia
CIMB Aviva Takaful Berhad	49.00%	Malaysia
First-Aviva Life Insurance Co., Ltd.	49.00%	Taiwan
Vietinbank Aviva Life Insurance Limited	49.99%	Vietnam
Woori Aviva Life insurance Co. Ltd	47.31%	Korea

All investments in the above companies are unlisted and are held by subsidiaries, except for the shares in Aviva-COFCO Life Insurance Co. Limited which are held by the Company. The Group's share of net assets of that company is £141 million (2011: £150 million) which have a fair value of £141 million (2011: £150 million).

(d) Impairment testing

Joint ventures are tested for impairment by comparing the carrying value of the cash generating unit to which the goodwill relates to the recoverable value of that cash generating unit.

The recoverable amount of long-term business undertakings is the value in use of the joint venture. This is calculated according to the methodology for the calculation of the value in use of long-term business cash generating units for the impairment testing of goodwill, as set out in note 16(b).

The recoverable amount for joint ventures classified as held for sale (CIMB Aviva Assurance Berhad, CIMB Aviva Takaful Berhad & First-Aviva Life Insurance Co., Ltd.) is the fair value less costs to sell for each entity, based on the expected net disposal proceeds. The recoverable amount of property management undertakings is the fair value less costs to sell of the joint venture, measured in accordance with the Groups accounting policy for Investment Property (See: Accounting Policy P).

Key Assumptions for the calculation of value in use for long-term business undertakings

All interests in joint ventures have been tested for impairment but only the material items are detailed below.

	Embedded value basis		Future new business profits growth rate		Future new business profits discount rate	
	2012	2011	2012 %	2011 %	2012 %	2011 %
Aviva-COFCO Life Insurance Co. Limited	MCEV	MCEV	n/a¹	n/a ¹	n/a¹	n/a ¹
AvivaSA Emeklilik ve Hayat A.S.	MCEV	MCEV	9.2	4.0	18.0	12.8
Woori Aviva Life insurance Co. Ltd	MCEV	MCEV	4.0	4.0	13.1	13.6

¹ Projection of future new business not required as MCEV exceeds carrying value.

Results of impairment testing

Following the impairment test of Woori Aviva Life Insurance Co. Ltd an impairment of £9 million has been recognised fully impairing the goodwill to £nil, reflecting local economic conditions.

(e) Additional information

Summarised aggregate financial information on the Group's interests in its joint ventures is as follows:

	2012 £m	2011 £m
Income, including unrealised gains/(losses) on investments	808	763
Expenses	(827)	(777)
Share of results before tax	(19)	(14)
Long-term assets	2,731	1,831
Current assets	1,676	2,534
Share of total assets	4,407	4,365
Long-term liabilities	(1,778)	(1,634)
Current liabilities	(1,234)	(1,266)
Share of total liabilities	(3,012)	(2,900)
Share of net assets	1,395	1,465

The joint ventures have no significant contingent liabilities to which the Group is exposed. The Group has capital commitments to property management joint ventures of £157 million (2011: £258 million).

19 – Interests in, and loans to, associates

This note analyses our interests in entities which we do not control but where we have significant influence.

(a) Carrying amount

	2012			2011		
	Goodwill and intangibles £m	Equity interests £m	Total £m	Goodwill and intangibles £m	Equity interests £m	Total £m
At 1 January	115	1,003	1,118	80	563	643
Share of results before tax	—	(295)	(295)	—	196	196
Share of tax	—	(2)	(2)	—	(36)	(36)
Share of results after tax	—	(297)	(297)	—	160	160
Impairment – see notes (i) and (ii) below	(147)	205	58	—	(217)	(217)
Share of loss after tax	(147)	(92)	(239)	—	(57)	(57)
Acquisitions	—	—	—	—	1,116	1,116
Additions – see note (iii) below	32	—	32	35	—	35
Reduction in Group interest	—	(601)	(601)	—	(3)	(3)
Share of losses taken to other comprehensive income	—	(7)	(7)	—	(143)	(143)
Dividends received	—	(43)	(43)	—	(71)	(71)
Deconsolidation of Delta Lloyd	—	—	—	—	(359)	(359)
Foreign exchange rate movements	—	(45)	(45)	—	(43)	(43)
Movements in carrying amount	(115)	(788)	(903)	35	440	475
At 31 December	—	215	215	115	1,003	1,118

The Group had no loans to associates as at 31 December 2012 (2011: *£nil*).

(i) Disposal of Delta Lloyd

On 5 July 2012, the Group sold 37.2 million shares in Delta Lloyd for £313 million (net of costs), reducing the Group's holding to 19.8% of Delta Lloyd's ordinary share capital, representing 18.6% of shareholder voting rights. As the Group no longer has significant influence over Delta Lloyd, the Group ceased to account for that company as an associate from 5 July 2012. From that date, our holding was classified as a financial investment, held at fair value through profit and loss.

Prior to sale, the Group's share of Delta Lloyd's net asset value declined to a value below its quoted market value and therefore the impairment recognised in 2011 to reduce the carrying value of the associate to the quoted market value was redundant and no longer required. The amount previously recognised as an impairment of £205 million has therefore been reversed during the current period, through the Group's share of loss after tax of associates, after exchange movements on the opening balance of £12 million.

(ii) Impairment testing

Following the business review, management have determined that the goodwill in Aviva Life Insurance Company India Limited is fully impaired. An impairment of £147 million has been recognised in respect of this associate, reducing its goodwill to nil.

The recoverable amount of property management undertakings is the fair value less costs to sell of the joint venture, measured in accordance with the Groups accounting policy for Investment Property (See: Accounting Policy P).

(iii) Additions

Additions in 2012 relate to Aviva Life Insurance Company India Limited.

(b) Principal associates

The Group's principal associates are as follows:

Company	Type of business	Proportion held	Country of incorporation and operation
Aviva Life Insurance Company India Limited	Insurance	26.00%	India
SCPI Logipierre 1	Property management	44.46%	France
SCPI Selectipierre 2	Property management	22.16%	France
SCPI Ufifrance Immobilier	Property management	20.40%	France

All investments in principal associates are held by subsidiaries.

(c) Additional information

Summarised aggregate financial information on the Group's interests in its associates is as follows:

	2012 Total £m	2011 Total £m
Share of revenues	1,990	2,244
Share of results before tax	(295)	196
Share of assets	458	25,957
Share of liabilities	(243)	(24,954)
Share of net assets	215	1,003

The Group's share of associated companies' contingent liabilities amounted to £nil million at 31 December 2012 (2011: *£173 million*).

20 – Property and equipment

This note analyses our property and equipment, which are primarily properties occupied by Group companies, properties under construction and computer equipment.

	Properties under construction £m	Owner-occupied properties £m	Motor vehicles £m	Computer equipment £m	Other assets £m	Total £m
Cost or valuation						
At 1 January 2011	126	440	9	723	409	1,707
Additions	45	—	1	38	20	104
Disposals	—	(44)	(3)	(66)	(51)	(164)
Transfers from/(to) investment property (note 21)	—	(1)	—	—	—	(1)
Fair value gains	32	—	—	—	—	32
Deconsolidation of Delta Lloyd	(29)	(184)	—	(63)	(128)	(404)
Foreign exchange rate movements	1	4	—	(2)	(3)	—
At 31 December 2011	175	215	7	630	247	1,274
Additions	16	171	—	27	20	234
Disposals	—	(13)	(4)	(46)	(41)	(104)
Transfers (to) investment property (note 21)	(111)	(32)	—	—	—	(143)
Fair value gains	(6)	(3)	—	—	—	(9)
Transfer to intangible assets (note 17)	—	—	—	(3)	—	(3)
Foreign exchange rate movements	—	(1)	—	—	(7)	(8)
At 31 December 2012	74	337	3	608	219	1,241
Depreciation and impairment						
At 1 January 2011	—	—	(7)	(640)	(310)	(957)
Charge for the year	—	—	(1)	(36)	(24)	(61)
Disposals	—	—	2	52	35	89
Deconsolidation of Delta Lloyd	—	—	—	54	108	162
Impairment losses charged to restructuring costs	—	—	—	—	—	—
Foreign exchange rate movements	—	—	1	3	(1)	3
At 31 December 2011	—	—	(5)	(567)	(192)	(764)
Charge for the year	—	—	1	(28)	(19)	(46)
Disposals	—	—	2	38	20	60
Impairment charge (see below)	—	(91)	—	(5)	(10)	(106)
Foreign exchange rate movements	—	(1)	—	3	6	8
At 31 December 2012	—	(92)	(2)	(559)	(195)	(848)
Carrying amount						
At 31 December 2011	175	215	2	63	55	510
At 31 December 2012	74	245	1	49	24	393
Less: Assets classified as held for sale	—	(2)	—	—	—	(2)
	74	243	1	49	24	391

Fair value losses of £3 million (2011: £2 million gains) have been charged to other comprehensive income, with the net reversal of losses previously charged to the income statement now being credited there.

Owner-occupied properties are stated at their revalued amounts, as assessed by qualified external valuers. These values are assessed in accordance with the relevant parts of the current RICS Appraisal and Valuation Standards in the UK, and with current local valuation practices in other countries. This assessment, on the basis of Existing Use Value and in accordance with UK Valuations Standards ("Red book"), is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction, after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion, assuming that the buyer is granted vacant possession of all parts of the property required by the business and disregarding potential alternative uses. The valuation assessment adopts market-based evidence and is in line with guidance from the International Valuation Standards Committee and the requirements of IAS 16, *Property, Plant and Equipment*.

Similar considerations apply to properties under construction, where an estimate is made of valuation when complete, adjusted for anticipated costs to completion, profit and risk, reflecting market conditions at the valuation date.

The £106 million impairment loss charged to the income statement mainly relates to Aviva USA's property and equipment, the carrying value of which has been reduced to nil as set out in note 3c(i).

If owner-occupied properties were stated on a historical cost basis, the carrying amount would be £275 million (2011: £189 million).

The Group has no material finance leases for property and equipment.

21 – Investment property

This note gives details of the properties we hold for long-term rental yields or capital appreciation.

	2012			2011		
	Freehold £m	Leasehold £m	Total £m	Freehold £m	Leasehold £m	Total £m
Carrying value						
At 1 January	9,848	1,790	11,638	11,241	1,823	13,064
Additions	536	194	730	1,107	85	1,192
Capitalised expenditure on existing properties	103	8	111	52	9	61
Fair value (losses) / gains	(416)	(76)	(492)	92	6	98
Disposals	(940)	(207)	(1,147)	(694)	(17)	(711)
Transfers (to)/from property and equipment (note 20)	89	54	143	1	—	1
Deconsolidation of Delta Lloyd	—	—	—	(2,015)	(116)	(2,131)
Foreign exchange rate movements	(145)	(5)	(150)	64	—	64
At 31 December	9,075	1,758	10,833	9,848	1,790	11,638
Less: Assets classified as held for sale	(18)	—	(18)	—	—	—
	9,057	1,758	10,815	9,848	1,790	11,638

Investment property in the UK is valued at least annually by external chartered surveyors at open market values in accordance with the guidance issued by The Royal Institution of Chartered Surveyors or using internal valuations and estimates during the intervening period. Outside the UK, valuations are produced by local qualified staff of the Group or external qualified professional valuers in the countries concerned. In the event of a material change in market conditions between the valuation date and balance sheet date, adjustments are made to reflect any material changes in fair value. Values are calculated using a discounted cash flow approach and are based on current rental income plus anticipated uplifts at the next rent review, lease expiry, or break option taking into consideration lease incentives and assuming no future growth in the estimated rental value of the property. This uplift and the discount rate are derived from rates implied by recent market transactions on similar properties.

The fair value of investment properties leased to third parties under operating leases at 31 December 2012 was £10,822 million (2011: £11,552 million). Future contractual aggregate minimum lease rentals receivable under the non-cancellable portion of these leases are given in note 52(b)(i).

22 – Fair value methodology

This note explains the methodology for valuing our financial assets and liabilities carried at fair value, and provides an analysis of these according to a 'fair value hierarchy', determined by the market observability of valuation inputs.

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

For financial assets and liabilities carried at fair value, we have categorised the measurement basis into a 'fair value hierarchy' as follows:

Quoted market prices in active markets – ('Level 1')

Inputs to Level 1 fair values are quoted prices (unadjusted) in active markets for identical assets and liabilities. An active market is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis. Examples are listed equities in active markets, listed debt securities in active markets and quoted unit trusts in active markets.

Modelled with significant observable market inputs – ('Level 2')

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

- Quoted prices for similar (i.e. not identical) assets and liabilities in active markets.
- Quoted prices for identical or similar assets and liabilities in markets that are not active, the prices are not current, or price quotations vary substantially either over time or among market makers, or in which little information is released publicly.
- Inputs other than quoted prices that are observable for the asset or liability (for example, interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment spreads, loss severities, credit risks, current property values and default rates).
- Inputs that are derived principally from, or corroborated by, observable market data by correlation or other means (market-corroborated inputs).

Examples of these are securities measured using discounted cash flow models based on market observable swap yields, and listed debt or equity securities in a market that is inactive. Valuations, whether sourced from internal models or third parties include credit risk by adjusting the spread above the yield curve for government treasury securities for the appropriate amount of credit risk for each issuer, based on observed market transactions. To the extent observed market spreads are either not used in valuing a security, or do not fully reflect liquidity risk, our valuation methodology, whether sourced from internal models or third parties, reflects a liquidity premium.

Where we use broker quotes and no information as to the observability of inputs is provided by the broker, we generally validate the price quoted by the broker by using internal models with observable inputs. When the price obtained from the broker and internal model are similar, we look to the inputs used in our internal model to understand the observability of the inputs used by the broker. In circumstances where internal models are not used to validate broker prices, and the observability of inputs used by brokers is unavailable, the investment is classified as Level 3. Broker quotes are usually non-binding.

22 – Fair value methodology continued

Modelled with significant unobservable market inputs – ('Level 3')

Inputs to Level 3 fair values are unobservable inputs for the asset or liability. Unobservable inputs may have been used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date (or market information for the inputs to any valuation models). As such, unobservable inputs reflect the assumptions the business unit considers that market participants would use in pricing the asset or liability. Examples are certain private equity investments and private placements.

The majority of the Group's financial assets and certain financial liabilities are valued based on quoted market information or observable market data. A small percentage (5.5%) of total financial assets recorded at fair value are based on estimates and recorded as Level 3 investments. Where estimates are used, these are based on a combination of independent third-party evidence and internally developed models, calibrated to market observable data where possible.

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

(b) Fair value hierarchy analysis

An analysis of financial assets and liabilities according to fair value hierarchy is given below:

	Fair value hierarchy				Amortised cost £m	Less: Assets of operations classified as held for sale £m	Statement of financial position Total £m
	Level 1 £m	Level 2 £m	Level 3 £m	Sub-total fair value £m			
2012							
Financial investments and loans (notes 23 & 25)							
Loans	—	18,973	—	18,973	8,961	(3,397)	24,537
Fixed maturity securities	107,953	43,588	10,082	161,623	—	(33,617)	128,006
Equity securities	33,074	230	473	33,777	—	(1,248)	32,529
Other investments (including derivatives)	21,704	5,510	2,879	30,093	—	(1,550)	28,543
Total	162,731	68,301	13,434	244,466	8,961	(39,812)	213,615
Financial Liabilities							
Non-participating investment contracts	45,032	825	442	46,299	1,400	(3,958)	43,741
Borrowings (note 48)	—	1,332	—	1,332	7,007	(145)	8,194
Derivative liabilities (note 49)	132	1,570	59	1,761	—	(108)	1,653
Total	45,164	3,727	501	49,392	8,407	(4,211)	53,588

Discussion on the valuation techniques applied to value financial liabilities carried at fair value is included in the relevant footnote disclosure for the financial liability.

For the year to 31 December 2012, transfers of financial assets from fair value hierarchy Level 1 to Level 2 amounted to £1.3 billion (2011: £2.2 billion), and £0.3 billion (2011: £9 million) from Level 2 to Level 1. The transfers from Level 1 to Level 2 arose primarily in France (£1.0 billion) and the UK (£0.3 billion) as a result of changes in the level of activity and environment in the markets from which prices are sourced.

For the year to 31 December 2012, there were no transfers of financial liabilities between fair value hierarchy levels (2011: no transfers).

	Fair value hierarchy				Amortised cost £m	Less: Assets of operations classified as held for sale £m	Statement of financial position Total £m
	Level 1 £m	Level 2 £m	Level 3 £m	Sub-total fair value £m			
2011							
Financial investments and loans (notes 23 & 25)							
Loans	—	18,486	—	18,486	9,630	—	28,116
Fixed maturity securities	103,183	42,222	7,940	153,345	—	(93)	153,252
Equity securities	31,556	644	483	32,683	—	(37)	32,646
Other investments (including derivatives)	21,902	5,530	2,945	30,377	—	(217)	30,160
Total	156,641	66,882	11,368	234,891	9,630	(347)	244,174
Financial Liabilities							
Non-participating investment contracts (note 40)	42,523	1,219	248	43,990	1,669	—	45,659
Borrowings (note 48)	—	1,306	—	1,306	7,144	—	8,450
Derivative liabilities (note 49)	446	1,360	44	1,850	—	—	1,850
Total	42,969	3,885	292	47,146	8,813	—	55,959

22 – Fair value methodology continued

(c) Further information on Level 3 financial instruments

(i) The table below shows movements in the Level 3 financial assets and liabilities measured at fair value.

	2012					2011				
	Fixed maturity securities £m	Equity securities £m	Other investments £m	Financial Investments Total £m	Financial liabilities Total £m	Fixed maturity securities £m	Equity securities £m	Other investments £m	Financial Investments Total £m	Financial liabilities Total £m
Total funds										
Balance at 1 January	7,940	483	2,945	11,368	292	8,709	972	2,668	12,349	208
Total net (losses)/gains recognised in the income statement	934	7	18	959	(4)	(466)	(35)	114	(387)	5
Total net gains/(losses) recognised in other comprehensive income	113	—	17	130	—	33	—	(10)	23	—
Purchases	1,826	27	646	2,499	18	876	85	680	1,641	30
Issuances	—	—	1	1	23	—	—	1	1	46
Disposals	(767)	(29)	(755)	(1,551)	—	(960)	(12)	(582)	(1,554)	—
Transfers into Level 3	443	2	56	501	184	167	6	119	292	—
Transfers out of Level 3	(149)	(3)	(12)	(164)	—	(234)	(3)	(24)	(261)	—
Deconsolidation of Delta Lloyd	—	—	—	—	—	(1)	(518)	—	(519)	—
Foreign exchange rate movements	(258)	(14)	(37)	(309)	(12)	(184)	(12)	(21)	(217)	3
Balance at 31 December	10,082	473	2,879	13,434	501	7,940	483	2,945	11,368	292
Less: Amounts classified as held for sale	(120)	—	(396)	(516)	—	—	—	—	—	—
	9,962	473	2,483	12,918	501	7,940	483	2,945	11,368	292

Total net gains recognised in the income statement in the year in respect of Level 3 financial investments amounted to £959 million (2011: £387 million net losses). Included in this balance are £1,030 million net gains (2011: £354 million net losses) attributable to assets still held at the end of the year.

The Group assesses the fair value hierarchy of its financial investments biannually at 30 June and 31 December. Transfers between fair value hierarchy levels are deemed to have occurred at the assessment date.

Transfers into and out of Level 3 for the year arose for the following reasons:

- Changes in the market observability of valuation inputs.
- Changes in the market observability of inputs used to validate valuations.
- Significant differences between third-party prices used for valuations and validation prices either sourced from third parties or internal models.

The transfers into and out of Level 3 in 2012 were predominantly in our business in France and related principally to changes in the market liquidity of certain debt securities resulting in changes to the availability of observable market inputs.

Of the £959 million net gains (2011: £387 million net losses) recognised in the income statement during the year, a £968 million gain (2011: £390 million losses) is recognised in net investment income and £9 million losses (2011: £3 million gains) relates to impairments and is included in other expenses.

(ii) The principal investments classified as Level 3, and the valuation techniques applied to them, are:

- Structured bond-type products held by our business in France amounting to £8.6 billion (2011: £6.1 billion), for which there is no active market. These bonds are valued either using third-party counterparty or broker quotes. These bonds are validated against internal or third-party models. These bonds have been classified as Level 3 because either (i) the third-party models included a significant unobservable liquidity adjustment or (ii) differences between the valuation provided by the counterparty and broker quotes and the validation model were sufficiently significant to result in a Level 3 classification. At 31 December 2012, the values reported in respect of these products were the lower of counterparty and broker quotes and modelled valuations.
- Notes issued by loan partnerships held by our UK Life business amounting to £1.0 billion (2011: £1.2 billion), for which there is no active market. These are valued using counterparty quotes which are corroborated against index information obtained for similar asset classes, taking into further consideration the quality of the underlying loan portfolio, leverage structure, credit rating, illiquidity margins, market spreads and duration.
- Private equity investment funds amounting to £1.3 billion (2011: £1.5 billion), of which £1.1 billion (2011: £0.9 billion) is held by our UK business. In valuing our interest in these funds, we rely on investment valuation reports received from the fund manager, making adjustments for items such as subsequent draw-downs and distributions between the date of the report and the balance sheet date and the fund manager's carried interest. In addition, an indexation adjustment is made to reflect changes in appropriate equity market indices between the valuation report date and balance sheet date.
- External hedge funds held principally by businesses in the UK, the US and France amounting to £1.3 billion (2011: £1.3 billion). Valuations received from fund managers are based on net asset values. However, insufficient information is provided on the underlying fund assets to support a classification other than Level 3.
- Certain strategic interests in banking partners held by our Italian business amounting to £0.3 billion (2011: £0.3 billion). Valuations are based on third-party independent appraisals, or where internally modelled, transactions in similar entities, discounted cash flow techniques and valuation multiples, using public and internal management information.
- Other Level 3 investments amount to £0.9 billion (2011: £1.0 billion) and relate to a diverse range of different types of securities held by a number of businesses throughout the Group.

22 – Fair value methodology continued

(iii) Where possible, the Group tests the sensitivity of the fair values of Level 3 investments to changes in unobservable inputs to reasonable alternatives. 99% (2011: 99%) of valuations for Level 3 investments are sourced from independent third parties and, where appropriate, validated against internally-modelled valuations, third-party models or broker quotes. Where third-party pricing sources are unwilling to provide a sensitivity analysis for their valuations, the Group undertakes, where feasible, sensitivity analysis on the following basis:

- For third-party valuations validated against internally-modelled valuations using significant unobservable inputs, the sensitivity of the internally modelled valuation to changes in unobservable inputs to a reasonable alternative is determined.
- For third-party valuations either not validated or validated against a third-party model or broker quote, the third-party valuation in its entirety is considered an unobservable input. Sensitivities are determined by flexing to a reasonable alternative the yield, NAV multiple, IRR or other suitable valuation multiples of the financial instrument implied by the third-party valuation. For example, for a fixed income security the implied yield would be the rate of return which discounts the security's contractual cash flows to equal the third-party valuation.

On the basis of the methodology outlined above, the Group is able to perform sensitivity analysis for £12.3 billion of the Group's Level 3 investments. For these Level 3 investments, changing unobservable valuation inputs to a reasonable alternative would result in a change in fair value in the range of £558 million positive impact and £623 million adverse impact.

Of the £1.1 billion Level 3 investments for which sensitivity analysis is not provided, £0.8 billion relates to investments held in unit-linked and participating funds mainly in France where investment risk is predominantly borne by policyholders and therefore shareholder profit before tax is insensitive to reasonable changes in fair value of these investments. The remaining £0.3 billion of Level 3 investments are held to back non-linked shareholder business and it is estimated that a 10% change in valuation of these investments would reduce shareholder profit before tax by £30 million.

23 – Loans

This note analyses the loans our Group companies have made, the majority of which are mortgage loans.

(a) Carrying amounts

The carrying amounts of loans at 31 December 2012 and 2011 were as follows:

	2012			2011		
	At fair value through profit or loss other than trading £m	At amortised cost £m	Total £m	At fair value through profit or loss other than trading £m	At amortised cost £m	Total £m
Policy loans	2	1,309	1,311	3	1,465	1,468
Loans to banks	—	4,250	4,250	—	4,988	4,988
UK securitised mortgage loans (see note 24)	2,218	—	2,218	2,154	—	2,154
Non-securitised mortgage loans	16,753	3,211	19,964	16,329	2,905	19,234
Loans to brokers and other intermediaries	—	89	89	—	96	96
Other loans	—	102	102	—	176	176
Total	18,973	8,961	27,934	18,486	9,630	28,116
Less: Amounts classified as held for sale	(56)	(3,341)	(3,397)	—	—	—
	18,917	5,620	24,537	18,486	9,630	28,116

Loans to banks include cash collateral received under stock lending arrangements (see note 25(d)). The obligation to repay this collateral is included in payables and other financial liabilities (note 49).

Of the above loans, £19,179 million (2011: £21,626 million) are due to be recovered in more than one year after the statement of financial position date.

Loans at fair value

Fair values have been calculated by discounting the future cash flows using appropriate current interest rates for each portfolio of mortgages. Further details of the fair value methodology are given in note 22.

The change in fair value of these loans during the year, attributable to a change in credit risk, was £491 million loss (2011: £555 million loss). The cumulative change attributable to changes in credit risk to 31 December 2012 was £2,665 million loss (2011: £2,174 million loss).

Non-securitised mortgage loans include £4.1 billion (2011: £3.7 billion) relating to UK primary healthcare and PFI businesses which are secured against General Practitioner premises, other primary health-related premises or other emergency services related premises. For all such loans, government support is provided through either direct funding or reimbursement of rental payments to the tenants to meet income service and provide for the debt to be reduced substantially over the term of the loan. Although the loan principal is not government-guaranteed, the nature of these businesses and premises provides considerable comfort of an ongoing business model and low risk of default.

23 – Loans continued

Loans at amortised cost

The fair value of these loans at 31 December 2012 was £8,735 million (2011: £9,532 million).

(b) Analysis of loans carried at amortised cost

	2012			2011		
	Amortised Cost £m	Impairment £m	Carrying Value £m	Amortised Cost £m	Impairment £m	Carrying Value £m
Policy loans	1,309	—	1,309	1,465	—	1,465
Loans to banks	4,250	—	4,250	4,988	—	4,988
Non-securitised mortgage loans	3,335	(124)	3,211	2,995	(90)	2,905
Loans to brokers and other intermediaries	89	—	89	96	—	96
Other loans	106	(4)	102	180	(4)	176
Total	9,089	(128)	8,961	9,724	(94)	9,630

The movements in the impairment provisions on these loans for the years ended 31 December 2011 and 2012 were as follows:

	2012 £m	2011 £m
At 1 January	(94)	(141)
Increase during the year	(45)	(66)
Write back following sale or reimbursement	2	2
Write back following recovery in value	9	39
Deconsolidation of Delta Lloyd	—	72
Foreign exchange rate movements	—	—
At 31 December	(128)	(94)

(c) Collateral

The Group holds collateral in respect of loans where it is considered appropriate in order to reduce the risk of non-recovery. This collateral generally takes the form of liens or charges over properties and, in the case of policy loans, the underlying policy for the majority of the loan balances above. In all other situations, the collateral must be in a readily realisable form, such as listed securities, and is held in segregated accounts. Transfer of title for the collateral received always occurs in such cases, although no market risk or benefit is taken. In the event of a default, the Group is able to sell or repledge the collateral.

The amount of collateral received with respect to loans which the Group is permitted to sell or repledge in the absence of default was £4,560 million (2011: £4,601 million). No collateral was actually sold or repledged in the absence of default during the year (2011: *Nil*).

24 – Securitised mortgages and related assets

The Group, in our UK Life business has loans receivable, secured by mortgages, which have then been securitised through non-recourse borrowings. This note gives details of the relevant transactions.

(a) Description of current arrangements

In a UK long-term business subsidiary, Aviva Equity Release UK Limited (AER), the beneficial interest in certain portfolios of lifetime mortgages has been transferred to five special purpose securitisation companies (the ERF companies), in return for initial consideration and, at later dates, deferred consideration. The deferred consideration represents receipts accrued within the ERF companies after meeting all their obligations to the note holders, loan providers and other third parties in the priority of payments. The purchases of the mortgages were funded by the issue of fixed and floating rate notes by the ERF companies.

All the shares in the ERF companies are held by independent companies, whose shares are held on trust. Although AER does not own, directly or indirectly, any of the share capital of the ERF companies or their parent companies, it retains control of the majority of the residual or ownership risks and rewards related to the assets of the securitisation companies, and they have therefore been treated as subsidiaries in the consolidated financial statements. AER has no right to repurchase the benefit of any of the securitised mortgage loans, other than in certain circumstances where AER is in breach of warranty or loans are substituted in order to effect a further advance.

AER has purchased subordinated notes and granted subordinated loans to some of the ERF companies. In addition, Group companies have invested in loan notes issued by the ERF companies. These have been eliminated on consolidation through offset against the borrowings of the ERF companies in the consolidated statement of financial position.

In all of the above transactions, the Company and its subsidiaries are not obliged to support any losses that may be suffered by the note holders and do not intend to provide such support. Additionally, the notes were issued on the basis that note holders are only entitled to obtain payment, of both principal and interest, to the extent that the available resources of the respective special purpose securitisation companies, including funds due from customers in respect of the securitised loans, are sufficient and that note holders have no recourse whatsoever to other companies in the Aviva Group.

(b) Carrying values

The following table summarises the securitisation arrangements:

	2012		2011	
	Securitized assets £m	Securitized borrowings £m	Securitized assets £m	Securitized borrowings £m
Securitized mortgage loans				
At fair value (note 23)	2,218	(1,515)	2,154	(1,486)
Other securitisation assets/(liabilities)	351	(1,054)	191	(859)
	2,569	(2,569)	2,345	(2,345)

Loan notes held by third parties are as follows:

	2012 £m	2011 £m
Total loan notes issued, as above	1,515	1,486
Less: Loan notes held by Group companies	(183)	(180)
Loan notes held by third parties (note 48(c)(i))	1,332	1,306

25 – Financial investments

This note analyses our financial investments by type and shows their cost and fair value. These will change from one period to the next as a result of new business written, claims paid and market movements.

(a) Carrying amount

Financial investments comprise:

	2012				2011			
	At fair value through profit or loss			Total £m	At fair value through profit or loss			Total £m
	Trading £m	Other than trading £m	Available for sale £m		Trading £m	Other than trading £m	Available for sale £m	
Fixed maturity securities								
Debt securities								
UK government	—	18,348	—	18,348	115	18,129	—	18,244
UK local authorities	—	18	—	18	—	18	—	18
Non-UK government (note 25e)	—	44,118	2,258	46,376	—	39,686	1,888	41,574
Corporate bonds								
Public utilities	—	6,259	2,881	9,140	—	6,064	2,951	9,015
Other corporate	—	54,942	21,449	76,391	—	54,602	19,991	74,593
Convertibles and bonds with warrants attached	—	465	6	471	—	418	17	435
Other	—	5,528	3,301	8,829	—	3,371	4,168	7,539
	—	129,678	29,895	159,573	115	122,288	29,015	151,418
Certificates of deposit	—	2,047	3	2,050	100	1,822	—	1,922
Redeemable preference shares	—	—	—	—	—	—	5	5
	—	131,725	29,898	161,623	215	124,110	29,020	153,345
Equity securities								
Ordinary shares								
Public utilities	—	3,684	—	3,684	—	4,133	—	4,133
Banks, trusts and insurance companies	—	7,196	62	7,258	—	6,184	81	6,265
Industrial, miscellaneous and all other	—	22,397	1	22,398	—	21,857	1	21,858
	—	33,277	63	33,340	—	32,174	82	32,256
Non-redeemable preference shares	—	437	—	437	—	426	1	427
	—	33,714	63	33,777	—	32,600	83	32,683
Other investments								
Unit trusts and other investment vehicles	—	26,315	441	26,756	—	26,775	485	27,260
Derivative financial instruments (note 57)	1,590	—	—	1,590	1,498	—	—	1,498
Deposits with credit institutions	—	739	—	739	—	427	—	427
Minority holdings in property management undertakings	—	584	—	584	—	617	—	617
Other investments – long-term	—	370	54	424	—	515	60	575
Other investments – short-term	—	—	—	—	—	—	—	—
	1,590	28,008	495	30,093	1,498	28,334	545	30,377
Total financial investments	1,590	193,447	30,456	225,493	1,713	185,044	29,648	216,405
Less assets classified as held for sale								
Fixed maturity securities	—	(4,236)	(29,381)	(33,617)	—	(93)	—	(93)
Equity securities	—	(1,187)	(61)	(1,248)	—	(37)	—	(37)
Other investments	—	(1,072)	(478)	(1,550)	—	(217)	—	(217)
	—	(6,495)	(29,920)	(36,415)	—	(347)	—	(347)
	1,590	186,952	536	189,078	1,713	184,697	29,648	216,058

Of the above total, £129,448 million (2011: £154,116 million) is due to be recovered in more than one year after the statement of financial position date.

Other debt securities of £8,829 million (2011: £7,539 million) primarily include residential and commercial mortgage-backed securities, as well as other structured credit securities.

25 – Financial investments continued

(b) Cost, unrealised gains and fair value

The following is a summary of the cost/amortised cost, gross unrealised gains and losses and fair value of financial investments:

	2012				2011			
	Cost/ amortised cost £m	Unrealised gains £m	Unrealised losses and impairments £m	Fair value £m	Cost/ amortised cost £m	Unrealised gains £m	Unrealised losses and impairments £m	Fair value £m
Fixed maturity securities	147,220	16,433	(2,030)	161,623	147,537	12,395	(6,587)	153,345
Equity securities	30,898	5,043	(2,164)	33,777	33,055	3,637	(4,009)	32,683
Other investments								
Unit trusts and specialised investment vehicles	25,966	1,647	(857)	26,756	27,416	74	(230)	27,260
Derivatives financial instruments	1,201	518	(129)	1,590	1,228	336	(66)	1,498
Deposits with credit institutions	739	—	—	739	427	—	—	427
Minority holdings in property management undertakings	599	123	(138)	584	639	124	(146)	617
Other long-term investments	434	20	(30)	424	652	19	(96)	575
	207,057	23,784	(5,348)	225,493	210,954	16,585	(11,134)	216,405
These are further analysed as follows:								
At fair value through profit or loss	180,006	20,202	(5,171)	195,037	183,959	13,555	(10,757)	186,757
Available for sale	27,051	3,582	(177)	30,456	26,995	3,030	(377)	29,648
	207,057	23,784	(5,348)	225,493	210,954	16,585	(11,134)	216,405

All unrealised gains and losses and impairments on financial investments classified as fair value through profit or loss have been recognised in the income statement.

Gains and losses on financial investments from continuing operations classified as at fair value through profit or loss recognised in the income statement in the year were a net gain of £12,365 million (2011: £5,487 million net loss). Of this, £30 million net loss (2011: £69 million net gain) related to financial investments designated as trading and £12,395 million net gain (2011: £5,556 million net loss) related to investments designated as other than trading.

The movement in the unrealised gain/loss position reported in the statement of financial position during the year, shown in the table above, includes foreign exchange movements on the translation of unrealised gains and losses on financial investments held by foreign subsidiaries, which are recognised in other comprehensive income, as well as transfers due to the realisation of gains and losses on disposal and the recognition of impairment losses.

Total impairments of financial investments classified as AFS in the income statement in the year were £14 million (2011: £21 million). The total accumulated impairment provision for financial investments classified as available-for-sale included in the table above within unrealised losses and impairments was £97 million (2011: £138 million). Movements in this AFS provision are shown in section (c) below.

(c) Impairment of financial investments

The movements in impairment provisions on available-for-sale financial investments for the years ended 31 December 2011 and 2012 were as follows:

	2012				2011			
	Fixed maturity securities £m	Equity securities £m	Other Investments £m	Total £m	Fixed maturity securities £m	Equity securities £m	Other Investments £m	Total £m
At 1 January	(126)	(5)	(7)	(138)	(151)	(825)	(7)	(983)
Charge for the year taken to the income statement	(12)	—	(2)	(14)	(19)	(2)	—	(21)
Write back following sale or reimbursement	49	—	—	49	28	—	—	28
Write back following recovery in value	—	1	—	1	—	—	—	—
Deconsolidation of Delta Lloyd	—	—	—	—	16	822	—	838
Foreign exchange rate movements	5	—	—	5	—	—	—	—
At 31 December	(84)	(4)	(9)	(97)	(126)	(5)	(7)	(138)

(d) Financial investment arrangements

(i) Stock lending arrangements

The Group has entered into stock lending arrangements in the UK and overseas in accordance with established market conventions. The majority of the Group's stock lending transactions occur in the UK, where investments are lent to EEA-regulated, locally domiciled counterparties and governed by agreements written under English law.

Non-cash collateral received

The Group receives collateral in order to reduce the credit risk of these arrangements. Collateral must be in a readily realisable form, such as listed securities, and is held in segregated accounts. Transfer of title always occurs for collateral received, although no market risk or economic benefit is taken. The level of collateral held is monitored regularly, with further collateral obtained where this is considered necessary to manage the Group's risk exposure.

In certain markets, the Group or the Group's appointed stock lending managers obtain legal ownership of the collateral received and can re-pledge it as collateral elsewhere or sell outright in the absence of default. The carrying amount of financial assets received

25 – Financial investments continued

in this manner at 31 December 2012 was £16,043 million (2011: £20,053 million). The value of collateral that was actually sold in the absence of default was £nil (2011: £150 million).

Cash collateral received

In addition to the above, the Group has received cash collateral under stock lending arrangements that has been recognised in the statement of financial position with a corresponding obligation for its return. The latter balance is included in note 49.

(ii) Other arrangements

In carrying on its bulk purchase annuity business, the Group's UK Life operation is required to place certain investments in trust on behalf of the policyholders. Amounts become payable from the trust funds to the trustees if the Group were to be in breach of its payment obligations in respect of policyholder benefits. At 31 December 2012 £1,208 million (2011: £1,044 million) of financial investments were restricted in this way.

Certain financial investments are also required to be deposited under local laws in various overseas countries as security for the holders of policies issued in those countries. Other investments are pledged as security collateral for bank letters of credit.

(e) Non UK Government Debt Securities (gross of non-controlling interests)

The following is a summary of non UK government debt by issuer as at 31 December 2012 analysed by policyholder, participating and shareholder funds.

	Policyholder		Participating		Shareholder		Total	
	2012 £m	2011 £m	2012 £m	2011 £m	2012 £m	2011 £m	2012 £m	2011 £m
Non UK Government Debt Securities								
Austria	14	28	634	512	123	58	771	598
Belgium	45	30	1,342	1,029	172	176	1,559	1,235
France	189	215	9,072	7,529	1,944	1,634	11,205	9,378
Germany	217	239	2,389	1,751	957	792	3,563	2,782
Greece	—	—	—	46	—	2	—	48
Ireland	34	33	363	378	26	216	423	627
Italy	263	273	8,517	9,670	617	1,056	9,397	10,999
Netherlands	65	63	1,193	1,284	228	136	1,486	1,483
Poland	672	509	1,012	720	445	329	2,129	1,558
Portugal	—	—	257	204	—	8	257	212
Spain	36	46	1,317	1,046	854	639	2,207	1,731
European Supranational debt	136	114	2,928	2,376	1,470	856	4,534	3,346
Other European countries	235	125	634	410	421	91	1,290	626
Europe	1,906	1,675	29,658	26,955	7,257	5,993	38,821	34,623
Canada	18	18	195	195	2,517	2,342	2,730	2,555
United States	131	129	40	66	1,665	1,631	1,836	1,826
North America	149	147	235	261	4,182	3,973	4,566	4,381
Singapore	7	8	453	309	276	211	736	528
Sri Lanka	2	21	2	2	—	139	4	162
Other	604	391	1,252	1,262	393	227	2,249	1,880
Asia Pacific and other	613	420	1,707	1,573	669	577	2,989	2,570
Total	2,668	2,242	31,600	28,789	12,108	10,543	46,376	41,574
Less: assets of operations classified as held for sale	197	34	556	9	2,274	19	3,027	62
Total (excluding assets held for sale)	2,471	2,208	31,044	28,780	9,834	10,524	43,349	41,512

At 31 December 2012, the Group's total government (non-UK) debt securities stood at £46.4 billion (2011: £41.6 billion), an increase of £4.8 billion. The significant majority of these holdings are within our participating funds where the risk to our shareholders is governed by the nature and extent of our participation within those funds.

Our direct shareholder asset exposure to government (non-UK) debt securities amounts to £12.1 billion (2011: £10.5 billion). The primary exposures, relative to total shareholder (non-UK) government debt exposure, are to French (16%), German (8%), Spanish (7%) and Italian (5%) (non-UK) government debt securities.

The participating funds exposure to (non-UK) government debt amounts to £31.6 billion (2011: £28.8 billion), an increase of £2.8 billion. The primary exposures, relative to total (non-UK) government debt exposures included within our participating funds, are to the (non-UK) government debt securities of France (29%), Italy (27%), Germany (8%), Belgium (4%), Spain (4%), Netherlands (4%) and Poland (3%).

25 – Financial investments continued

(f) Exposure to worldwide banks – debt securities

Direct shareholder and participating fund assets exposures to worldwide bank debt securities (net of non-controlling interests, excluding policyholder assets)

2012	Shareholder assets			Participating fund assets		
	Total senior debt £bn	Total subordinated debt £bn	Total debt £bn	Total senior debt £bn	Total subordinated debt £bn	Total debt £bn
Austria	—	—	—	0.3	—	0.3
France	0.1	—	0.1	3.5	0.8	4.3
Germany	0.1	0.1	0.2	0.5	0.5	1.0
Ireland	—	0.1	0.1	—	—	—
Italy	0.1	0.1	0.2	0.3	0.1	0.4
Netherlands	0.4	0.2	0.6	1.9	0.3	2.2
Portugal	—	—	—	0.1	—	0.1
Spain	0.8	0.1	0.9	1.1	0.1	1.2
United Kingdom	0.8	0.5	1.3	1.0	1.2	2.2
United States	1.3	0.8	2.1	1.0	0.1	1.1
Other	0.6	0.4	1.0	2.0	0.8	2.8
Total	4.2	2.3	6.5	11.7	3.9	15.6
Less: assets of operations classified as held for sale	1.3	1.0	2.3	0.1	0.1	0.2
Total (excluding assets held for sale)	2.9	1.3	4.2	11.6	3.8	15.4
2011 Total	3.7	2.2	5.9	10.6	3.6	14.2

Net of non-controlling interests, our direct shareholder assets exposure to worldwide bank debt securities is £6.5 billion. The majority of our holding (65%) is in senior debt. The primary exposures are to US (32%) and UK (20%) banks. Net of non-controlling interests, our direct shareholder asset exposure to worldwide bank equity securities is £0.2 billion. Our holdings include strategic holdings in Italian banks of £148 million.

Net of non-controlling interests, the participating fund exposures to worldwide bank debt securities, where the risk to our shareholders is governed by the nature and extent of our participation within those funds, is £15.6 billion. The majority of the exposure (75%) is in senior debt. Participating funds are the most exposed to French (28%), UK (14%) and Dutch (14%) banks.

Direct shareholder and participating fund assets exposures to worldwide bank debt securities (gross of non-controlling interests, excluding policyholder assets)

2012	Shareholder assets			Participating fund assets		
	Total senior debt £bn	Total subordinated debt £bn	Total debt £bn	Total senior debt £bn	Total subordinated debt £bn	Total debt £bn
Austria	—	—	—	0.3	—	0.3
France	0.1	—	0.1	4.0	0.9	4.9
Germany	0.1	0.1	0.2	0.5	0.5	1.0
Ireland	—	0.1	0.1	—	—	—
Italy	0.2	0.1	0.3	0.5	0.2	0.7
Netherlands	0.4	0.2	0.6	2.0	0.3	2.3
Portugal	—	—	—	0.1	—	0.1
Spain	1.2	0.1	1.3	1.5	0.2	1.7
United Kingdom	0.8	0.6	1.4	1.1	1.3	2.4
United States	1.4	0.8	2.2	1.1	0.1	1.2
Other	0.7	0.4	1.1	2.2	0.9	3.1
Total	4.9	2.4	7.3	13.3	4.4	17.7
Less: assets of operations classified as held for sale	1.4	1.1	2.5	0.2	0.1	0.3
Total (excluding assets held for sale)	3.5	1.3	4.8	13.1	4.3	17.4
2011 Total	4.3	2.3	6.6	12.0	3.9	15.9

Gross of non-controlling interests, our direct shareholder assets exposure to worldwide bank debt securities is £7.3 billion. The majority of our holding (67%) is in senior debt. The primary exposures are to US (30%) and UK (19%) banks. Gross of non-controlling interests, our direct shareholder asset exposure to worldwide bank equity securities is £0.4 billion. Our holdings include strategic holdings in Italian banks of £289 million.

Gross of non-controlling interests, the participating fund exposures to worldwide bank debt securities, where the risk to our shareholders is governed by the nature and extent of our participation within those funds, is £17.7 billion. The majority of the exposure (75%) is in senior debt. Participating funds are the most exposed to French (28%), UK (14%) and Dutch (13%) banks.

26 – Receivables

This note analyses our total receivables.

	2012 £m	2011 £m
Amounts owed by contract holders	1,693	1,838
Amounts owed by intermediaries	1,398	1,139
Deposits with ceding undertakings	1,395	1,426
Amounts due from reinsurers	367	339
Amounts due from brokers for investment sales	444	270
Amounts receivable for cash collateral pledged	241	26
Amounts due from government, social security and taxes	521	467
Corporate owned life insurance	162	156
Dividends receivable	6	109
Finance lease receivables	141	200
Other receivables	1,662	1,978
Total	8,030	7,948
Less: Amounts classified as held for sale	(413)	(11)
	7,617	7,937
Expected to be recovered in less than one year	7,525	7,713
Expected to be recovered in more than one year	92	224
	7,617	7,937

Concentrations of credit risk with respect to receivables are limited due to the size and spread of the Group's trading base. No further credit risk provision is therefore required in excess of the normal provision for doubtful receivables.

27 – Deferred acquisition costs, other assets, prepayments and accrued income

(a) Deferred acquisition costs and other assets – carrying amount

The carrying amount comprises:

	2012 £m	2011 £m
Deferred acquisition costs in respect of:		
Insurance contracts – Long-term business	2,122	2,733
Insurance contracts – General insurance and health business	939	986
Participating investment contracts – Long-term business	30	21
Non-participating investment contracts – Long-term business	936	1,024
Retail fund management business	14	14
Total deferred acquisition costs	4,041	4,778
Surpluses in the staff pension schemes (note 47 (e) (vii))	1,257	1,670
Other assets	56	19
Total	5,354	6,467
Less: Amounts classified as held for sale	(1,555)	(23)
	3,799	6,444

Deferrable acquisition costs (DAC) on long-term business are generally recoverable in more than one year whereas such costs on general insurance and health business are generally recoverable within one year. Of the above total, £1,351 million (2011: £3,148 million) is expected to be recovered more than one year after the statement of financial position date; the reduction in this amount reflects that the DAC balance for the US is included in amounts classified as held for sale at 31 December 2012. For long-term business where amortisation of the DAC balance depends on projected profits, the amount expected to be recovered is estimated and actual experience will differ.

Surpluses in the staff pension schemes are recoverable more than one year after the statement of financial position date.

27 – Deferred acquisition costs, other assets, prepayments and accrued income continued**(b) Deferred acquisition costs – movements in the year**

The movements in deferred acquisition costs (DAC) during the year were:

	2012				2011			
	Long-term business £m	General insurance and health business £m	Retail fund management business £m	Total £m	Long-term business £m	General insurance and health business £m	Retail fund management business £m	Total £m
Carrying amount at 1 January	3,778	986	14	4,778	4,261	1,141	14	5,416
Acquisition costs deferred during the year	841	2,221	4	3,066	1,012	2,414	5	3,431
Amortisation	(804)	(2,257)	(4)	(3,065)	(735)	(2,467)	(5)	(3,207)
Impact of assumption changes	(201)	—	—	(201)	(48)	—	—	(48)
Effect of portfolio transfers, acquisitions and disposals	(15)	(1)	—	(16)	—	(18)	—	(18)
Foreign exchange rate movements	(89)	(10)	—	(99)	(3)	(5)	—	(8)
Shadow adjustment	(422)	—	—	(422)	(593)	—	—	(593)
Deconsolidation of Delta Lloyd	—	—	—	—	(116)	(79)	—	(195)
Carrying amount at 31 December	3,088	939	14	4,041	3,778	986	14	4,778
Less: Amounts classified as held for sale	(1,538)	—	—	(1,538)	(23)	—	—	(23)
	1,550	939	14	2,503	3,755	986	14	4,755

The balance of deferred acquisition costs for long-term business decreased by £0.7 billion in 2012, reflecting the impact of assumption changes and shadow adjustment in the US.

Where amortisation of the DAC balance depends on projected profits, changes to economic conditions may lead to a movement in the DAC balance and a corresponding impact on profit. It is estimated that the movement in the DAC balance would reduce profit by £30 million (2011: £145 million) if market yields on fixed income investments were to increase by 1% and increase profit by £50 million (2011: £170 million) if yields were to reduce by 1%. The reduction in sensitivities for 2012 reflects that the US business is held for sale and carried at fair value less cost to sell.

The shadow adjustments relate to deferred acquisition costs on business in the US backed by investments classified as AFS. As explained in accounting policy K, unrealised gains and losses on the AFS investments and the shadow adjustments above are both recognised directly in other comprehensive income.

(c) Other assets

Other assets include £3 million (2011: £6 million) that is expected to be recovered more than one year after the statement of financial position date.

(d) Prepayments and accrued income

Prepayments and accrued income of £3,104 million including assets classified as held for sale (2011: £3,235 million), includes £108 million (2011: £90 million) that is expected to be recovered more than one year after the statement of financial position date.

28 – Assets held to cover linked liabilities

Certain unit-linked products have been classified as investment contracts, while some are included within the definition of an insurance contract. The assets backing these unit-linked liabilities are included within the relevant balances in the consolidated statement of financial position, while the liabilities are included within insurance and investment contract provisions. This note analyses the carrying values of assets backing these liabilities.

	2012 £m	2011 £m
Loans	605	917
Debt securities	16,472	15,295
Equity securities	22,500	20,602
Reinsurance assets	1,576	1,454
Cash and cash equivalents	4,305	3,980
Other	28,512	28,119
	73,970	70,367
Less: Assets classified as held for sale	(3,048)	—
	70,922	70,367

29 – Ordinary share capital

This note gives details of Aviva plc's ordinary share capital and shows the movements during the year.

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

	2012 £m	2011 £m
The allotted, called up and fully paid share capital of the Company at 31 December 2012 was: 2,945,972,261 (2011: 2,905,712,938) ordinary shares of 25 pence each	736	726

(b) During 2012, a total of 40,259,323 ordinary shares of 25 pence each were allotted and issued by the Company as follows:

	2012			2011		
	Number of shares	Share Capital £m	Share Premium £m	Number of shares	Share Capital £m	Share Premium £m
At 1 January 2012	2,905,712,938	726	1,173	2,820,148,642	705	1,194
Shares issued under the Group's Employee and Executive Share Option Schemes	3,335,566	1	1	1,574,706	—	—
Shares issued in lieu of dividends	36,923,757	9	(9)	83,989,590	21	(21)
At 31 December 2012	2,945,972,261	736	1,165	2,905,712,938	726	1,173

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

The issue of shares in lieu of cash dividends is considered a bonus issue under the terms of the Companies Act 2006 and the nominal value of the shares is charged to the share premium account.

30 – Group's share plans

This note describes the Group's various equity compensation plans, and shows how the Group values the options and awards of shares in the Company.

(a) Description of the plans

The Group maintains a number of active share option and award plans and schemes (the Group's Share Plans). These are as follows:

(i) Savings-related options

These are options granted under the HMRC-approved Save As You Earn (SAYE) share option schemes in the UK and Irish Revenue-approved SAYE share option scheme in Ireland. Options are normally exercisable during the six-month period following either the third, fifth or seventh anniversary of the start of the relevant savings contract. Options granted in 2012 are normally exercisable following the third or fifth anniversary.

(ii) Executive share options

These are options granted on various dates until 2004 under the Aviva Executive Share Option Plan and in 2010, under the Aviva Executive Share Option Plan 2005. Options granted between 2001 and 2004 were subject to the satisfaction of conditions relating to both the Company's Return on Equity (ROE) and its relative Total Shareholder Return (TSR). The performance was measured over a three-year performance period and the options are normally exercisable between the third and tenth anniversary of their grant. The options granted in 2010 are described in the Directors' Remuneration Report.

(iii) Long-term incentive plan awards

These awards have been made under the Aviva Long Term Incentive Plan 2005 and Aviva Long Term Incentive Plan 2011, and are described in section (b) below and in the Directors' Remuneration Report.

(iv) Annual bonus plan awards

These awards have been made under the Aviva Annual Bonus Plan 2005 and Aviva Annual Bonus Plan 2011, and are described in section (b) below and in the Directors' Remuneration Report.

(v) One Aviva, twice the value bonus plan awards

These are conditional awards granted under the Aviva Annual Bonus Plan 2005 between 2008 and 2010, and are described in section (b) below and in the Directors' Remuneration Report.

(vi) Recruitment and retention share award plan awards

These are conditional awards granted under the Aviva Recruitment and Retention Share Award Plan in relation to the recruitment or retention of senior managers excluding Executive Directors. The awards vest in tranches on various dates and vesting is conditional upon the participant being employed by the Group on the vesting date and not having served notice of resignation. If a participant's employment is terminated due to resignation or dismissal, any tranche of the award which has vested within the 12 months prior to the termination date will be subject to clawback and any unvested tranches of the award will lapse in full. No new Aviva plc ordinary shares will be issued or transferred from treasury to satisfy vested awards under this plan.

30 – Group's share plans continued**(vii) CFO recruitment share awards plan awards**

The following awards were granted to Patrick Regan under the CFO Recruitment Share Awards Plan following his recruitment in 2010: the Replacement Restricted Share Award (RRSA), the Bonus Replacement Deferred Share Award (BRDSA) and the One Aviva Twice the Value (OATTV) Award. The RRSA was awarded to compensate Mr Regan for the loss of share awards granted by his previous employer and the BRDSA was awarded to compensate Mr Regan for the loss of bonus from his previous employer. The awards are described in section (b) below and in the Directors' Remuneration Report. No further awards will be made under this plan.

(viii) Conditional share award granted to Trevor Matthews

A conditional share award was awarded to Trevor Matthews as compensation for the loss of share awards granted by his previous employer. The awards are described in section (b) below and in the Directors' Remuneration Report.

(b) Outstanding options and awards**(i) Share options**

At 31 December 2012, options to subscribe for ordinary shares of 25 pence each in the Company were outstanding as follows:

Aviva Savings Related Share Option Scheme	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	491	13,228	2012	316	2,337,854	2012, 2014 or 2016
	593	39,615	2013	310	2,421,083	2013, 2015 or 2017
	563	139,960	2012 or 2014	268	10,302,920	2014, 2016 or 2018
	410	502,299	2013 or 2015	266	5,892,828	2015 or 2017

Aviva Ireland Savings Related Share Option Scheme (in euros)	Option price c	Number of shares	Normally exercisable	Option price c	Number of shares	Normally exercisable
	830	32,130	2012	374	140,085	2013 or 2015
	509	49,387	2013	304	507,254	2014 or 2016
	360	362,066	2012 or 2014	336	268,003	2015 or 2017

Aviva Executive Share Option Plan	Option price p	Number of shares	Normally exercisable
	512	533,707	2006 to 2013
	526	361,010	2007 to 2014
	386	1,308,781	2013

The following table summarises information about options outstanding at 31 December 2012:

Range of exercise prices	Outstanding options Number	Weighted average remaining contractual life Years	Weighted average exercise price p
£2.66 – £4.29	24,092,560	3	287.77
£4.30 – £5.89	1,080,035	1	524.55
£5.90 – £10.35	39,615	1	593.00

The comparative figures as at 31 December 2011 were:

Range of exercise prices	Outstanding options Number	Weighted average remaining contractual life Years	Weighted average exercise price p
£2.68 – £4.29	27,743,093	3	303.84
£4.30 – £5.89	2,052,537	2	524.03
£5.90 – £10.35	278,354	1	593.00

30 – Group's share plans continued**(ii) Share awards**

At 31 December 2012, awards issued under the Company's executive incentive plans over ordinary shares of 25 pence each in the Company were outstanding as follows:

Aviva Long Term Incentive Plan 2005		Number of shares	Vesting period
		5,458,500	2010 to 2012
Aviva Long Term Incentive Plan 2011		Number of shares	Vesting period
		7,391,026	2011 to 2013
		11,321,800	2012 to 2014
One Aviva, twice the value bonus plan		Number of shares	Vesting period
		1,422,544	2010 to 2012
Aviva Annual Bonus Plan 2005		Number of shares	Vesting period
		2,762,731	2010 to 2012
Aviva Annual Bonus Plan 2011		Number of shares	Vesting period
		2,496,279	2011 to 2013
		4,476,090	2012 to 2014
CFO Recruitment Share Awards Plan	Award type	Number of shares	Vesting period
	RRSA	85,197	2013
	BRDSA	43,231	2010 to 2012
	OATTV	55,051	2010 to 2012
Conditional Share Award granted to Trevor Matthews		Number of shares	Vesting period
		435,814	2013 and 2014
Recruitment and Retention Share Award Plan		Number of shares	Vesting period
		19,481	2013
		166,921	2013 and 2014
		39,122	2013, 2014 and 2015
		78,167	2015

The vesting of awards under the Aviva Long Term Incentive Plan 2005, the Aviva Long Term Incentive Plan 2011, the OATTV bonus plan and the OATTV Award under the CFO Recruitment Share Awards Plan is subject to the attainment of performance conditions as described in the Directors' Remuneration Report. Shares which do not vest will lapse.

(iii) Shares to satisfy awards and options

Since July 2008, it has been the Company's practice to satisfy all awards and options using shares purchased in the market and held by employee trusts except where local regulations make it necessary to issue new shares. Further details are given in note 31.

(c) Movements in the year

A summary of the status of the option plans as at 31 December 2011 and 2012, and changes during the years ended on those dates, is shown below.

	2012		2011	
	Number of options	Weighted average exercise price p	Number of options	Weighted average exercise price p
Outstanding at 1 January	30,073,984	321.55	27,256,640	367.51
Granted during the year	6,236,944	269.02	13,486,990	268.00
Exercised during the year	(2,862,952)	315.24	(182,907)	353.26
Forfeited during the year	(2,187,371)	337.96	(1,089,738)	347.58
Cancelled during the year	(3,282,095)	300.34	(7,142,132)	320.36
Expired during the year	(2,766,300)	432.85	(2,254,869)	539.48
Outstanding at 31 December	25,212,210	298.40	30,073,984	321.55
Exercisable at 31 December	1,943,130	424.99	3,460,979	471.26

30 – Group's share plans continued

(d) Expense charged to the income statement

The total expense recognised for the year arising from equity compensation plans was as follows:

	2012 £m	2011 £m
Equity-settled expense	42	48
Cash-settled expense	5	10
Total (note 10b)	47	58

(e) Fair value of options and awards granted after 7 November 2002

The weighted average fair values of options and awards granted during the year, estimated by using the Binomial option pricing model, were £0.70 and £2.61 (2011: £0.99 and £4.20) respectively.

(i) Share options

The fair value of the options was estimated on the date of grant, based on the following weighted average assumptions:

Weighted average assumption	2012	2011
Share price	326p	312p
Exercise price	266p	268p
Expected volatility	41%	58%
Expected life	3.71 years	3.64 years
Expected dividend yield	7.98%	6.40%
Risk-free interest rate	0.37%	0.89%

The expected volatility used was based on the historical volatility of the share price over a period equivalent to the expected life of the option prior to its date of grant. The risk-free interest rate was based on the yields available on UK government bonds as at the date of grant. The bonds chosen were those with a similar remaining term to the expected life of the options. 2,862,952 options granted after 7 November 2002 were exercised during the year (2011: 182,907).

(ii) Share awards

The fair value of the awards was estimated on the date of grant based on the following weighted average assumptions:

Weighted average assumption	2012	2011
Share price	331.54p	435.70p
Expected volatility ¹	37%	66%
Expected volatility of comparator companies' share price ¹	38%	65%
Correlation between Aviva and competitors' share price ¹	63%	57%
Expected life	3.00 years	3.00 years
Expected dividend yield ²	n/a	n/a
Risk-free interest rate ¹	0.42%	1.79%

¹ For awards with market-based performance conditions.

² The long term incentive plan awards granted in 2011 and 2012 include additional shares being provided to employees equal to dividend rights before vesting. As a result, no dividend yield assumption is required for these awards.

The expected volatility used was based on the historical volatility of the share price over a period equivalent to the expected life of the share award prior to its date of grant. The risk-free interest rate was based on the yields available on UK government bonds as at the date of grant. The bonds chosen were those with a similar remaining term to the expected life of the share awards.

31 – Shares held by employee trusts

We satisfy awards and options granted under the Group's share plans primarily through shares purchased in the market and held by employee share trusts. This note gives details of the shares held in these trusts. Movements in the carrying value of shares held by employee trusts comprise:

	2012		2011	
	Number	£m	Number	£m
Cost debited to shareholders' funds				
At 1 January	13,284,476	43	8,415,487	32
Acquired in the year	10,269,904	33	9,396,602	29
Distributed in the year	(13,500,865)	(44)	(4,527,613)	(18)
Balance at 31 December	10,053,515	32	13,284,476	43

The shares are owned by employee share trusts with an undertaking to satisfy awards of shares in the Company under the Company's share plans and schemes. Details of the features of the plans can be found in the Directors' Remuneration Report and in note 30.

These shares were purchased in the market and are carried at cost. At 31 December 2012, they had an aggregate nominal value of £2,513,379 (2011: £3,321,119) and a market value of £37,499,611 (2011: £39,959,704). The trustees have waived their rights to dividends on the shares held in the trusts.

32 – Preference share capital

This note gives details of Aviva plc's preference share capital.

The preference share capital of the Company at 31 December 2012 was:

	2012 £m	2011 £m
Issued and paid up		
100,000,000 8.375% cumulative irredeemable preference shares of £1 each	100	100
100,000,000 8.75% cumulative irredeemable preference shares of £1 each	100	100
	200	200

Under its articles of association, the Company may issue and allot Sterling New Preference Shares and Euro New Preference Shares, which, if issued and allotted, would rank, as to payment of a dividend and capital, ahead of the Company's ordinary share capital but behind the cumulative irredeemable preference shares currently in issue. The issued preference shares are non-voting except where their dividends are in arrears, on a winding up or where their rights are altered.

On a winding up, they carry a preferential right of return of capital ahead of the ordinary shares. The Company does not have a contractual obligation to deliver cash or other financial assets to the preference shareholders and therefore the directors may make dividend payments at their discretion.

33 – Direct capital instruments and fixed rate tier 1 notes

Notional amount	2012 £m	2011 £m
5.9021% £500 million direct capital instrument	500	500
4.7291% €700 million direct capital instrument	490	490
	990	990
Issued May 2012		
8.25% US \$650 million fixed rate tier 1 notes	392	—
	1,382	990

The euro and sterling direct capital instruments (the DCIs) were issued on 25 November 2004 and qualify as Innovative Tier 1 capital, as defined by the Financial Services Authority in GENPRU Annex 1 'Capital Resources'. They have no fixed redemption date but the Company may, at its sole option, redeem all (but not part) of the euro and sterling DCIs at their principal amounts on 28 November 2014 and 27 July 2020 respectively, at which dates the interest rates change to variable rates, or on any respective coupon payment date thereafter. In the case of the sterling DCI this variable rate will be the six month sterling deposit rate plus margin while the euro DCI variable rate will be the three month euro deposit rate plus margin.

The fixed rate tier 1 notes (the FxdRNs) were issued on 3 May 2012 and also qualify as Innovative Tier 1 capital. The FxdRNs are perpetual but are subject to a mandatory exchange into non-cumulative preference shares in the Company after 99 years. The Company may, at its sole option, redeem all (but not part) of the FxdRNs at their principal amounts on 3 November 2017, or on any respective coupon payment date thereafter.

On the occurrence of a Capital Disqualification Event as defined in the terms and conditions of the issue for both the DCIs and FxdRNs, the Company may at its sole option substitute at any time not less than all of the DCIs or FxdRNs for, or vary the terms of the DCIs so that they become, Qualifying Tier 1 Securities or Qualifying Upper Tier 2 Securities.

In addition, on the occurrence of a Substitution Event as defined in the terms and conditions of the issue for the DCIs, the Company may at its sole option substitute not less than all of the DCIs for fully paid non-cumulative preference shares in the Company. These preference shares can only be redeemed on 28 November 2014 in the case of the euro DCIs and on 27 July 2020 in the case of the sterling DCIs, or in each case on any dividend payment date thereafter. For the FxdRNs, having given the required notice, the Company has the right to substitute not less than all of the notes for fully paid non-cumulative preference shares at any time. These preference shares can only be redeemed on 3 November 2017, or on any dividend payment date thereafter. The Company has the right to choose whether or not to pay any dividend on the new shares, and any such dividend payment will be non-cumulative.

The Company has the option to defer coupon payments on the DCIs or FxdRNs on any relevant payment date.

In relation to the DCIs, deferred coupons shall be satisfied only in the following circumstances, all of which occur at the sole option of the Company:

- Redemption; or
- Substitution by, or variation so they become, alternative Qualifying Tier 1 Securities or Qualifying Upper Tier 2 Securities; or
- Substitution by preference shares.

In relation to the FxdRNs, deferred coupons may be satisfied at any time, at the sole option of the Company. The Company is required to satisfy deferred coupons on the FxdRNs only in the following circumstances:

- Redemption; or
- Substitution by preference shares.

No interest will accrue on any deferred coupon. Deferred coupons will be satisfied by the issue and sale of ordinary shares in the Company at their prevailing market value, to a sum as near as practicable to (and at least equal to) the relevant deferred coupons. In the event of any coupon deferral, the Company will not declare or pay any dividend on its ordinary or preference share capital.

These instruments have been treated as equity. Please refer to accounting policy AD.

34 – Merger reserve

This note describes the use of the merger reserve.

Prior to 1 January 2004, certain significant business combinations were accounted for using the 'pooling of interests method' (or merger accounting), which treats the merged groups as if they had been combined throughout the current and comparative accounting periods. Merger accounting principles for these combinations gave rise to a merger reserve in the consolidated statement of financial position, being the difference between the nominal value of new shares issued by the Parent Company for the acquisition of the shares of the subsidiary and the subsidiary's own share capital and share premium account.

The merger reserve is also used where more than 90% of the shares in a subsidiary are acquired and the consideration includes the issue of new shares by the Company, thereby attracting merger relief under the Companies Act 1985 and, from 1 October 2009, the Companies Act 2006.

The balance on the reserve of £3,271 million (2011: £3,271 million) has arisen through the mergers of Commercial Union, General Accident and Norwich Union companies, forming Aviva plc in 2000, together with the acquisition of RAC plc ("RAC") in 2005. Because RAC ownership was immediately transferred from Aviva plc to a subsidiary company, this reserve is unaffected by the disposal of RAC in 2011.

35 – Other reserves

This note gives details of the various reserves forming part of the Group's consolidated equity and shows the movements during the year net of non-controlling interests:

	Currency translation reserve (see accounting policy E) £m	Owner occupied properties reserve (see accounting policy O) £m	Investment valuation reserve (see accounting policy S) £m	Hedging instruments reserve (see accounting policy T) £m	Equity compensation reserve (see accounting policy AA) £m	Total £m
Balance at 1 January 2011	2,183	83	573	(693)	99	2,245
Arising in the year:						
Fair value gains	—	2	424	—	—	426
Fair value gains transferred to profit on disposals	—	—	(189)	—	—	(189)
Transfer to profit on disposal of subsidiary	(3)	—	—	—	—	(3)
Fair value gains transferred to retained earnings on disposals (note 36)	—	(6)	—	—	—	(6)
Share of fair value changes in joint ventures and associates taken to other comprehensive income (note 18a & 19a)	—	1	(86)	—	—	(85)
Impairment losses on assets previously revalued directly through other comprehensive income now taken to income statement	—	—	21	—	—	21
Reserves credit for equity compensation plans	—	—	—	—	48	48
Shares issued under equity compensation plans (note 36)	—	—	—	—	(61)	(61)
Transfer to profit on deconsolidation of Delta Lloyd	(485)	—	(115)	—	—	(600)
Transfer to retained earnings on deconsolidation of Delta Lloyd	—	(2)	—	—	—	(2)
Foreign exchange rate movements	(174)	—	—	30	—	(144)
Aggregate tax effect – shareholders' tax	9	1	(98)	—	—	(88)
Balance at 31 December 2011	1,530	79	530	(663)	86	1,562
Arising in the year:						
Fair value gains	—	(3)	554	—	—	551
Fair value gains transferred to profit on disposals	—	—	(234)	—	—	(234)
Transfer to profit on disposal of subsidiaries, joint ventures and associates	91	—	96	—	—	187
Share of fair value changes in joint ventures and associates taken to other comprehensive income (note 18a & 19a)	—	—	14	—	—	14
Impairment losses on assets previously revalued directly through other comprehensive income now taken to income statement	—	—	12	—	—	12
Reserves credit for equity compensation plans	—	—	—	—	42	42
Shares issued under equity compensation plans (note 36)	—	—	—	—	(68)	(68)
Foreign exchange rate movements	(367)	—	—	74	—	(293)
Aggregate tax effect – shareholders' tax	18	1	(117)	—	—	(98)
Balance at 31 December 2012	1,272	77	855	(589)	60	1,675

Included in the above are £1.0 billion of currency translation and investment valuation reserves at 31 December 2012 relating to discontinued operations.

36 – Retained earnings

This note analyses the movements in the consolidated retained earnings during the year.

	2012 £m	2011 £m
Balance at 1 January	5,954	5,411
(Loss)/profit for the year attributable to equity shareholders	(3,218)	225
Actuarial (losses)/gains on pension schemes (note 47 (e) (iv))	(830)	1,002
Other pension scheme movements	—	(22)
Dividends and appropriations (note 15)	(847)	(813)
Shares issued in lieu of dividends	127	307
Shares issued under equity compensation plans (note 35)	67	61
Shares distributed by employee trusts (note 31)	(36)	(18)
Fair value gains realised from reserves (note 35)	—	6
Effect of deconsolidation of Delta Lloyd	—	2
Share of other comprehensive income of joint ventures and associates	—	(51)
Aggregate tax effect	172	(156)
Balance at 31 December	1,389	5,954

The shares issued in lieu of dividends are in respect of the transfer to retained earnings from the ordinary dividend account, arising from the treatment of these shares explained in note 29(b).

The Group's regulated subsidiaries are required to hold sufficient capital to meet acceptable solvency levels based on applicable local regulations. Their ability to transfer retained earnings to the UK parent companies is therefore restricted to the extent these earnings form part of local regulatory capital.

37 – Non-controlling interests

This note gives details of the Group's non-controlling interests and shows the movements during the year.

Non-controlling interests at 31 December comprised:

	2012 £m	2011 £m
Equity shares in subsidiaries	424	480
Share of earnings	643	501
Share of other reserves	257	299
	1,324	1,280
Preference shares in General Accident plc	250	250
Total	1,574	1,530

Movements in the year comprised:

	2012 £m	2011 £m
Balance at 1 January	1,530	3,741
(Loss)/profit for the year attributable to non-controlling interests	168	(165)
Non-controlling interests share of movements in other reserves	1	(16)
Foreign exchange rate movements	(37)	14
Total comprehensive income attributable to non-controlling interests	132	(167)
Capital contributions from non-controlling interests	20	68
Non-controlling interests share of dividends declared in the year	(102)	(126)
Changes in non-controlling interests in existing subsidiaries	(6)	(11)
Reclassification to financial liabilities (see below)	—	(205)
Effect of deconsolidation of Delta Lloyd	—	(1,770)
Balance at 31 December	1,574	1,530

As explained in note 3, the minority shareholder in an Irish subsidiary has an option requiring the Group to purchase its shares. As a result of this obligation, the Group has reclassified this non-controlling interest to financial liabilities in the consolidated statement of financial position. This option was exercised on 17 January 2012, with completion expected in 2013.

38 – Contract liabilities and associated reinsurance

The following notes explain how the Group calculates its liabilities to policyholders for insurance and investment products it has sold to them. Notes 39 and 40 cover these liabilities, and note 41 details the financial guarantees and options given for some of these products. Note 42 details the reinsurance recoverables on these liabilities while note 43 shows the effects of changes in the assumptions.

The following is a summary of the contract provisions and related reinsurance assets as at 31 December.

	2012			2011		
	Gross provisions £m	Reinsurance assets £m	Net £m	Restated ¹ Gross provisions £m	Reinsurance assets £m	Restated ¹ Net £m
Long-term business						
Insurance contracts	(131,190)	4,291	(126,899)	(131,171)	3,747	(127,424)
Participating investment contracts	(66,849)	3	(66,846)	(67,707)	—	(67,707)
Non-participating investment contracts	(47,699)	1,678	(46,021)	(45,659)	1,626	(44,033)
	(245,738)	5,972	(239,766)	(244,537)	5,373	(239,164)
Outstanding claims provisions						
Long-term business	(1,342)	93	(1,249)	(1,311)	126	(1,185)
General insurance and health	(7,711)	900	(6,811)	(8,099)	974	(7,125)
	(9,053)	993	(8,060)	(9,410)	1,100	(8,310)
Provisions for claims incurred but not reported	(2,843)	354	(2,489)	(2,646)	395	(2,251)
	(257,634)	7,319	(250,315)	(256,593)	6,868	(249,725)
Provision for unearned premiums	(4,441)	248	(4,193)	(4,483)	245	(4,238)
Provision arising from liability adequacy tests	(11)	—	(11)	(13)	—	(13)
Totals	(262,086)	7,567	(254,519)	(261,089)	7,113	(253,976)
Less: Amounts classified as held for sale	38,501	(883)	37,618	344	(1)	343
	(223,585)	6,684	(216,901)	(260,745)	7,112	(253,633)

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, there has been a reallocation from participating insurance liabilities at 31 December 2011 to participating investment contract liabilities of £2,722 million.

39 – Insurance liabilities

This note analyses the Group insurance contract liabilities by type of product and describes how the Group calculates these liabilities and the assumptions the Group used.

(a) Carrying amount

Insurance liabilities at 31 December comprise:

	2012			2011		
	Long-term business £m	General insurance and health £m	Total £m	Restated ¹ Long-term business £m	General insurance and health £m	Restated ¹ Total £m
Long-term business provisions						
Participating	49,473	—	49,473	52,872	—	52,872
Unit-linked non-participating	9,936	—	9,936	10,168	—	10,168
Other non-participating	71,781	—	71,781	68,131	—	68,131
	131,190	—	131,190	131,171	—	131,171
Outstanding claims provisions	1,342	7,711	9,053	1,311	8,099	9,410
Provision for claims incurred but not reported	—	2,843	2,843	—	2,646	2,646
	1,342	10,554	11,896	1,311	10,745	12,056
Provision for unearned premiums	—	4,441	4,441	—	4,483	4,483
Provision arising from liability adequacy tests	—	11	11	—	13	13
Other technical provisions	—	—	—	—	—	—
Total	132,532	15,006	147,538	132,482	15,241	147,723
Less: Amounts classified as held for sale	(34,446)	(1)	(34,447)	(344)	—	(344)
	98,086	15,005	113,091	132,138	15,241	147,379

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, there has been a reallocation from participating insurance liabilities at 31 December 2011 to participating investment contract liabilities of £2,722 million.

(b) Long-term business liabilities

(i) Business description

The Group underwrites long-term business in a number of countries as follows:

- In the UK mainly in:
 - New With-Profits sub-fund (NWPSF) of Aviva Life & Pensions UK (UKLAP), where the with-profit policyholders are entitled to at least 90% of the distributed profits, the shareholders receiving the balance. Any surplus or deficit emerging in NWPSF that is not distributed as bonus will be transferred from this sub-fund to the Reattributed Inherited Estate External Support Account (RIEESA) (see below).
 - Old With-Profits sub-fund (OWPSF), With-Profits sub-fund (WPSF) and Provident Mutual sub-fund (PMSF) of UKLAP, where the with-profit policyholders are entitled to at least 90% of the distributed profits, the shareholders receiving the balance.
 - 'Non-profit' funds of Aviva Annuity UK and UKLAP, where shareholders are entitled to 100% of the distributed profits. Shareholder profits on unitised with-profit business written by WPSF and on stakeholder unitised with-profit business are derived from management fees and policy charges, and emerge in the non-profit funds.
 - The RIEESA of UKLAP, which is a non-profit fund where shareholders are entitled to 100% of the distributed profits, but these cannot be distributed until the 'lock-in' criteria set by the Reattribution Scheme have been met. RIEESA will be used to write non-profit business and also to provide capital support to NWPSF.
- In France, where the majority of policyholders' benefits are determined by investment performance, subject to certain guarantees, and shareholders' profits are derived largely from management fees. In addition, a substantial number of policies participate in investment returns, with the balance being attributable to shareholders.
- In the US, there are two main types of business – protection products and accumulation products. Protection products include interest-sensitive whole life, term life, universal life and indexed life insurance policies. The accumulation product segment includes traditional fixed and indexed deferred annuities for individuals and funding agreements for business customers. In addition, there are two closed blocks of participating contracts arising from demutualisations of subsidiary companies. All products are classified as insurance contracts except for the funding agreements and term certain immediate annuities, which are classified as non-participating investment contracts.
- In other operations in Europe and Asia, a range of long-term insurance and savings products are written.

39 – Insurance liabilities continued

(ii) Group practice

The long-term business provision is calculated separately for each of the Group's life operations. The provisions for overseas subsidiaries have generally been included on the basis of local regulatory requirements, modified where necessary to reflect the requirements of the Companies Act 2006.

Material judgement is required in calculating the provisions and is exercised particularly through the choice of assumptions where discretion is permitted. In turn, the assumptions used depend on the circumstances prevailing in each of the life operations. Provisions are most sensitive to assumptions regarding discount rates and mortality/morbidity rates. Where discount rate assumptions are based on current market yields on fixed interest securities, allowance is made for default risk implicit in the yields on the underlying assets.

In 2010, a test case was taken to the European Court of Justice to rule on the current law and practice whereby insurers may take into account a person's gender in the assessment of risk and consequently the pricing of insurance products. The ruling was issued on 1 March 2011 and required gender equality for pricing from 21 December 2012. The impact of the ruling on existing long-term business provisions in our UK and European businesses is not considered to be material.

Bonuses paid during the year are reflected in claims paid, whereas those allocated as part of the bonus declaration are included in the movements in the long-term business provision.

For UK with-profit life funds falling within the scope of the FSA realistic capital regime, and hence FRS 27, an amount may be recognised for the present value of future profits (PVFP) on non-participating business written in a with-profit fund where the determination of the realistic value of liabilities in that with-profit fund takes account, directly or indirectly, of this value. For our UK with-profit funds, no adjustment for this value is made to the participating insurance and investment contract liabilities or the unallocated divisible surplus.

(iii) Methodology and assumptions

There are two main methods of actuarial valuation of liabilities arising under long-term insurance contracts – the net premium method and the gross premium method – both of which involve the discounting of projected premiums and claims.

Under the net premium method, the premium taken into account in calculating the provision is determined actuarially, based on the valuation assumptions regarding discount rates, mortality and disability. The difference between this premium and the actual premium payable provides a margin for expenses. This method does not allow for voluntary early termination of the contract by the policyholder, and so no assumption is required for persistency.

The gross premium method uses the amount of contractual premiums payable and includes explicit assumptions for interest and discount rates, mortality and morbidity, persistency and future expenses. These assumptions can vary by contract type and reflect current and expected future experience.

(a) UK

With-profit business

The valuation of with-profit business uses the methodology developed for the Realistic Balance Sheet, adjusted to remove the shareholders' share of future bonuses. The key elements of the Realistic Balance Sheet methodology are the with-profit benefit reserve (WPBR) and the present value of the expected cost of any payments in excess of the WPBR (referred to as the cost of future policy-related liabilities). The realistic liability for any contract is equal to the sum of the WPBR and the cost of future policy-related liabilities. The WPBR for an individual contract is generally calculated on a retrospective basis, and represents the accumulation of the premiums paid on the contract, allowing for investment return, taxation, expenses and any other charges levied on the contract.

For a small proportion of business, a prospective valuation approach is used, including allowance for anticipated future regular and final bonuses.

The items included in the cost of future policy-related liabilities include:

- Maturity Guarantees;
- Guaranteed Annuity Options;
- GMP underpin on Section 32 transfers; and
- Expected payments under Mortgage Endowment Promise.

In the Provident Mutual and With-Profits sub-funds in UKLAP, this is offset by the expected cost of charges to WPBR to be made in respect of guarantees.

The cost of future policy-related liabilities is determined using a market-consistent approach and, in the main, this is based on a stochastic model calibrated to market conditions at the end of the reporting period. Non-market-related assumptions (for example, persistency, mortality and expenses) are based on experience, adjusted to take into account future trends.

The principal assumptions underlying the cost of future policy-related liabilities are as follows:

39 – Insurance liabilities continued

Future investment return

A 'risk-free' rate equal to the spot yield on UK swaps was used. This replaced the use of a spot yield on UK government securities plus a margin of 0.1%, which was used at 31 December 2011. The rates vary according to the outstanding term of the policy, with a typical rate as at 31 December 2012 of 1.92% (2011: 2.20%) for a policy with ten years outstanding.

Volatility of investment return

Volatility assumptions are set with reference to implied volatility data on traded market instruments, where available, or on a best estimate basis where not.

Volatility	2012	2011
Equity returns	26.3%	26.4%
Property returns	15.0%	15.0%
Fixed interest yields	17.1%	18.0%

The equity volatility used depends on term, money-ness and region. The figure shown is for a sample UK equity, at the money, with a ten-year term. Fixed interest yield volatility is also dependent on term and money-ness. The figure shown is for a ten-year swap option with ten-year term, currently at the money.

Future regular bonuses

Annual bonus assumptions for 2012 have been set consistently with the year-end 2011 declaration. Future annual bonus rates reflect the principles and practices of the fund. In particular, the level is set with regard to the projected margin for final bonus and the change from one year to the next is limited to a level consistent with past practice.

Mortality

Mortality assumptions for with-profit business are set with regard to recent Company experience and general industry trends. The mortality tables used in the valuation are summarised below:

Mortality table used	2012	2011
Assurances, pure endowments and deferred annuities before vesting	Nil or Axx00 adjusted	Nil or Axx00 adjusted
Pensions business after vesting and pensions annuities in payment	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement

Non-profit business

The valuation of non-profit business is based on regulatory requirements, adjusted to remove certain regulatory reserves and margins in assumptions, notably for annuity business. Conventional non-profit contracts, including those written in the with-profit funds, are valued using gross premium methods which discount projected future cash flows. The cash flows are calculated using the amount of contractual premiums payable, together with explicit assumptions for investment returns, inflation, discount rates, mortality, morbidity, persistency and future expenses. These assumptions vary by contract type and reflect current and expected future experience.

For unit-linked and some unitised with-profit business, the provisions are valued by adding a prospective non-unit reserve to the bid value of units. The prospective non-unit reserve is calculated by projecting the future non-unit cash flows on the assumption that future premiums cease, unless it is more onerous to assume that they continue. Where appropriate, allowance for persistency is based on actual experience.

Valuation discount rate assumptions are set with regard to yields on the supporting assets and the general level of long-term interest rates as measured by gilt yields. An explicit allowance for risk is included by restricting the yields for equities and properties with reference to a margin over long-term interest rates or by making an explicit deduction from the yields on corporate bonds, mortgages and deposits, based on historical default experience of each asset class. A further margin for risk is then deducted for all asset classes.

39 – Insurance liabilities continued

The provisions held in respect of guaranteed annuity options are a prudent assessment of the additional liability incurred under the option on a basis and method consistent with that used to value basic policy liabilities, and includes a prudent assessment of the proportion of policyholders who will choose to exercise the option.

Valuation discount rates for business in the non-profit funds are as follows:

Valuation discount rates	2012	2011
Assurances		
Life conventional non-profit	1.8%	1.8% to 1.9%
Pensions conventional non-profit	2.2%	2.6%
Annuities		
Conventional immediate and deferred annuities	2.6% to 4.1%	2.2% to 4.3%
Non-unit reserves on Unit Linked business		
Life	2.1%	1.8% to 2.2%
Pensions	2.5%	2.2% to 2.7%
Income Protection		
Active lives	2.2%	2.4%
Claims in payment – level	3.1%	3.6%
Claims in payment – index linked	(0.7)%	(1.0)%

The above valuation discount rates are after reduction for investment expenses and credit risk. For conventional immediate annuity business the allowance for credit risk comprises long-term assumptions for default and downgrades, which vary by the credit ratings for bonds and mortgages, and short-term supplementary allowances for higher expected defaults during the current economic conditions. The credit risk allowance made for corporate bonds and commercial mortgages, including healthcare mortgages, held by Aviva Annuity UK Limited equated to 56 bps and 89 bps respectively at 31 December 2012 (2011: 60 bps and 69 bps respectively). For corporate bonds, the allowance represented 30% of the average credit spread for the portfolio (2011: 26%). The total valuation allowance held by Aviva Annuity UK Limited in respect of corporate bonds and mortgages, including healthcare mortgages, was £1.8 billion (2011: £1.6 billion) over the remaining term of the UK Life corporate bond and commercial mortgage portfolio. Total liabilities for annuity business were £30 billion at 31 December 2012 (2011: £27 billion).

Mortality assumptions for non-profit business are set with regard to recent Company experience and general industry trends. The mortality tables used in the valuation are summarised below:

Mortality tables used	2012	2011
Assurances		
Non-profit	AM00/AF00 or TM00/TF00 adjusted for smoker status and age/sex specific factors	AM00/AF00 or TM00/TF00 adjusted for smoker status and age/sex specific factors
Pure endowments and deferred annuities before vesting	AM00/AF00 adjusted	AM00/AF00 adjusted
Annuities in payment		
Pensions business	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement
General annuity business	IML00/IFL00 adjusted plus allowance for future mortality improvement	IML00/IFL00 adjusted plus allowance for future mortality improvement

For pensions annuity business in 2012, the underlying mortality assumptions for Males are 100.5% of PCMA00 with base year 2000, improvements based on CMI_2011 with a long-term improvement rate of 1.5% and an addition of 0.5% to all future annual improvements; for Females the underlying mortality assumptions are 95.5% of PCFA00 with base year 2000, improvements based on CMI_2011 with a long-term improvement rate of 1.0% and an addition of 0.5% to all future annual improvements. Year-specific adjustments are made to allow for selection effects due to the development of the Enhanced Annuity market.

(b) France

The majority of reserves arise from single premium savings products and are based on the accumulated fund values, adjusted to maintain consistency with the value of the assets backing the policyholder liabilities. For traditional business the net premium method is used for prospective valuations, in accordance with local regulation, where the valuation assumptions depend on the date of issue of the contract. The valuation discount rate also depends on the original duration of the contract and mortality rates are based on industry tables.

	Valuation discount rates	Mortality tables used
	2012 and 2011	2012 and 2011
Life assurances	0% to 4.5%	TD73-77, TD88-90, TH00-02, TF00-02
Annuities	0% to 4.5%	TGF05/TGH05

39 – Insurance liabilities continued

(c) United States

For the major part of our US business, insurance liabilities are measured in accordance with US GAAP as at the date of acquisition.

The liability for future policy benefits for traditional life insurance is computed using the net level method, based on guaranteed interest and mortality rates as used in calculating cash surrender values. Reserve interest assumptions ranged from 2.00% to 7.50% in 2012 (2011: 2.00% to 7.50%). The weighted average interest rate for all traditional life policy reserves in 2012 was 4.50% (2011: 4.50%).

Future policy benefit reserves for universal life insurance, deferred annuity products and funding agreements are computed under a retrospective deposit method and represent policy account balances before applicable surrender charges. For the indexed products, the liability held is calculated based on the option budget method and is equal to the host contract and the calculated value of the derivative. The value of the derivative is based on the present value of the difference between the projected fund value and the underlying fund guarantee. The range of interest crediting rates for deferred annuity products, the largest component of the US business, excluding sales inducement payouts, was 1.00% to 5.20% in 2012 (2011: 1.00% to 5.20%). An additional liability is established for universal life contracts with death or other insurance benefit features, which is determined using an equally weighted range of scenarios with respect to investment returns, policyholder lapses, benefit election rates, premium payout patterns and mortality. The additional liability represents the present value of future expected benefits based on current product assumptions.

The indexed life and annuity products guarantee the return of principal to the customer, and credit interest based on certain indices. A portion of the premium from each customer is invested in fixed income securities and is intended to cover the minimum guaranteed value. A further portion of the premium is used to purchase derivatives to hedge the growth in interest credited to the customer as a direct result of increases in the related indices. Both the derivatives and the options embedded in the policy are valued at their fair value.

Deferred income reserves are established for fees charged for insurance benefit features which are assessed in a manner that is expected to result in higher profits in earlier years, followed by lower profits or losses in subsequent years. The excess charges are deferred and amortised using the same assumptions and factors used to amortise deferred acquisition costs. Deferred income reserves of £85 million in respect of insurance contracts in the United States are included under Other liabilities – Deferred income in note 50. Shadow adjustments may be made to deferred acquisition costs, acquired value of in-force business, deferred income reserves and contract liabilities. The shadow adjustments are recognised directly in other comprehensive income so that unrealised gains or losses on investments that are recognised directly in other comprehensive income affect the measurement of the liability, or related assets, in the same way as realised gains or losses.

(d) Other countries

In all other countries, local generally accepted interest rates and published standard mortality tables are used for different categories of business as appropriate. The tables are based on relevant experience and show mortality rates, by age, for specific groupings of people.

(iv) Movements

The following movements have occurred in the long-term business provisions during the year:

	2012 £m	Restated ¹ 2011 £m
Carrying amount at 1 January	131,171	157,988
Provisions in respect of new business	8,631	10,894
Expected change in existing business provisions	(8,362)	(8,541)
Variance between actual and expected experience	943	(2,279)
Impact of other operating assumption changes	(718)	(61)
Impact of economic assumption changes	1,726	5,663
Other movements	(109)	(623)
Change in liability recognised as an expense	2,111	5,053
Effect of portfolio transfers, acquisitions and disposals	(214)	(6)
Deconsolidation of Delta Lloyd	—	(32,159)
Foreign exchange rate movements	(1,878)	295
Carrying amount at 31 December	131,190	131,171

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, there has been a reallocation from participating insurance liabilities at 31 December 2011 to participating investment contract liabilities of £2,722 million.

The variance between actual and expected experience of £0.9 billion in 2012 was primarily due to the impact of favourable investment returns on liabilities for unit-linked insurance contracts. For many types of long-term business, including unit-linked and participating funds, movements in asset values are offset by corresponding changes in liabilities, limiting the net impact on profit. Minor variances arise from differences between actual and expected experience for persistency, mortality and other demographic factors.

The impact of assumption changes in the above analysis shows the resulting movement in the carrying value of insurance liabilities. The £1.7 billion impact of economic assumption changes reflects reductions in valuation interest rates, primarily in respect of immediate annuity and participating insurance contracts in the UK. The £0.7 billion impact of operating assumption changes mainly relates to mortality assumption in the UK, with the net impact reduced by movements in corresponding reinsurance assets. For participating business, a movement in liabilities is generally offset by a corresponding adjustment to the unallocated divisible surplus and does not impact on profit. Where assumption changes do impact on profit, these are included in the effect of changes in assumptions and estimates during the year shown in note 43, together with the impact of movements in related non-financial assets.

39 – Insurance liabilities continued

(c) General insurance and health liabilities

(i) Provisions for outstanding claims

Delays occur in the notification and settlement of claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the statement of financial position date. The reserves for general insurance and health business are based on information currently available. However, it is inherent in the nature of the business written that the ultimate liabilities may vary as a result of subsequent developments.

Provisions for outstanding claims are established to cover the outstanding expected ultimate liability for losses and loss adjustment expenses (LAE) in respect of all claims that have already occurred. The provisions established cover reported claims and associated LAE, as well as claims incurred but not yet reported and associated LAE.

The Group only establishes loss reserves for losses that have already occurred. The Group therefore does not establish catastrophe equalisation reserves that defer a share of income in respect of certain lines of business from years in which a catastrophe does not occur to future periods in which catastrophes may occur. When calculating reserves, the Group takes into account estimated future recoveries from salvage and subrogation, and a separate asset is recorded for expected future recoveries from reinsurers after considering their collectability.

The table below shows the split of total general insurance and health outstanding claim provisions and IBNR provisions, gross of reinsurance, by major line of business.

	As at 31 December 2012			As at 31 December 2011		
	Outstanding claim provisions £m	IBNR provisions £m	Total claim provisions £m	Outstanding claim provisions £m	IBNR provisions £m	Total claim provisions £m
Motor	3,737	1,051	4,788	3,960	995	4,955
Property	1,408	212	1,620	1,392	155	1,547
Liability	2,003	1,394	3,397	2,206	1,321	3,527
Creditor	54	13	67	59	19	78
Other	509	173	682	482	156	638
	7,711	2,843	10,554	8,099	2,646	10,745

(ii) Discounting

Outstanding claims provisions are based on undiscounted estimates of future claim payments, except for the following classes of business for which discounted provisions are held:

Class	Rate		Mean term of liabilities	
	2012	2011	2012	2011
Reinsured London Market business	2.0%	2.20%	11 years	13 years
Latent claims	0.33% to 3.35%	0.75% to 3.25%	6 to 15 years	7 to 16 years
Structured settlements	2.60%	2.70%	33 years	31 years

The gross outstanding claims provision before discounting was £11,004 million (2011: £11,420 million). The period of time which will elapse before the liabilities are settled has been estimated by modelling the settlement patterns of the underlying claims.

The discount rate that has been applied to latent claims reserves is based on the relevant swap curve in the relevant currency having regard to the expected settlement dates of the claims. The range of discount rates used depends on the duration of the claims and is given in the table above. The duration of the claims span over 35 years, with the average duration being between 6 and 15 years depending on the geographical region. Any change in discount rates between the start and the end of the accounting period is reflected below operating profit as an economic assumption change.

During 2012, the Group has seen a levelling off in the number of new bodily injury claims settled by periodic payment orders (PPOs) or structured settlements, which are reserved for on a discounted basis.

(iii) Assumptions

Outstanding claims provisions are estimated based on known facts at the date of estimation. Case estimates are set by skilled claims technicians and established case setting procedures. Claim technicians apply their experience and knowledge to the circumstances of individual claims. They take into account all available information and correspondence regarding the circumstances of the claim, such as medical reports, investigations and inspections. Claims technicians set case estimates according to documented claims department policies and specialise in setting estimates for certain lines of business or types of claim. Claims above certain limits are referred to senior claims handlers for authorisation.

No adjustments are made to the claims technicians' case estimates included in booked claim provisions, except for rare occasions when the estimated ultimate cost of individual large or unusual claims may be adjusted, subject to internal reserve committee approval, to allow for uncertainty regarding, for example, the outcome of a court case. The ultimate cost of outstanding claims is then estimated by using a range of standard actuarial claims projection techniques, such as the Chain Ladder and Bornhuetter-Ferguson methods. The main assumption underlying these techniques is that a company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios. Historical claims development is mainly analysed by accident period, although underwriting or notification period is also used where this is considered appropriate.

Claim development is separately analysed for each geographic area, as well as by each line of business. Certain lines of business are also further analysed by claim type or type of coverage. In addition, large claims are usually separately addressed, either by being reserved at the face value of loss adjuster estimates or separately projected in order to reflect their future development.

39 – Insurance liabilities continued

The assumptions used in most non-life actuarial projection techniques, including future rates of claims inflation or loss ratio assumptions, are implicit in the historical claims development data on which the projections are based. Additional qualitative judgement is used to assess the extent to which past trends may not apply in the future, for example, to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy conditions and claims handling procedures in order to arrive at a point estimate for the ultimate cost of claims that represents the likely outcome, from a range of possible outcomes, taking account of all the uncertainties involved. The range of possible outcomes does not, however, result in the quantification of a reserve range.

As noted in section in section (b)(ii) – Group Practice, an area of judgement is the impact of a European Court of Justice ruling in March 2011 on gender equality for the pricing of insurance products. At 31 December 2012, the impact of the ruling on existing general business provisions was not considered to be material.

The following explicit assumptions are made which could materially impact the level of booked net reserves:

UK mesothelioma claims

The level of uncertainty associated with latent claims is considerable due to the relatively small number of claims and the long-tail nature of the liabilities. UK mesothelioma claims account for a large proportion of the Group's latent claims. The key assumptions underlying the estimation of these claims include claim numbers, the base average cost per claim, future inflation in the average cost of claims and legal fees.

The best estimate of the liabilities reflects the latest available market information and studies. Many different scenarios can be derived by flexing these key assumptions and applying different combinations of the different assumptions. An upper and lower scenario can be derived by making reasonably likely changes to these assumptions, resulting in an estimate £240 million greater than the best estimate, or £65 million lower than the best estimate. These scenarios do not, however, constitute an upper or lower bound on these liabilities.

Interest rates used to discount latent claim liabilities

The discount rates used in determining our latent claim liabilities are based on the relevant swap curve in the relevant currency at the reporting date, having regard to the duration of the expected settlement of latent claims. The range of discount rates used is shown in section (ii) above and depends on the duration of the claim and the reporting date. At 31 December 2012, it is estimated that a 1% fall in the discount rates used would increase net claim reserves by approximately £95 million, excluding the offsetting effect on asset values as assets are not hypothecated across classes of business. The impact of a 1% fall in interest rates across all assets and liabilities of our general insurance and health businesses is shown in note 56.

Allowance for risk and uncertainty

The uncertainties involved in estimating loss reserves are allowed for in the reserving process and by the estimation of explicit reserve uncertainty distributions. The reserve estimation basis for non-life claims requires all non-life businesses to calculate booked claim provisions as the best estimate of the cost of future claim payments, plus an explicit allowance for risk and uncertainty. The allowance for risk and uncertainty is calculated by each business unit in accordance with the requirements of the Group non-life reserving policy, taking into account the risks and uncertainties specific to each line of business and type of claim in that territory. The requirements of the Group non-life reserving policy also seek to ensure that the allowance for risk and uncertainty is set consistently across both business units and reporting periods.

Changes to claims development patterns can materially impact the results of actuarial projection techniques. However, allowance for the inherent uncertainty in the assumptions underlying reserving projections is automatically allowed for in the explicit allowance for risk and uncertainty included when setting booked reserves.

Lump sum payments in settlement of bodily injury claims decided by the UK courts are calculated in accordance with the Ogden Tables. The Ogden Tables contain a discount rate that is set by the Lord Chancellor and that is applied when calculating the present value of loss of earnings for claims settlement purposes. The process for setting this discount rate is currently under review.

The timing of the conclusion of this review is unclear and it is still uncertain whether or by how much the rate will change. However an allowance has been included in provisions for a reduction in the Ogden discount rates. A reduction in the Ogden discount rates will increase lump sum payments to UK bodily injury claimants.

39 – Insurance liabilities continued**(iv) Movements**

The following changes have occurred in the general insurance and health claims provisions during the year:

	2012 £m	2011 £m
Carrying amount at 1 January	10,745	12,263
Impact of changes in assumptions	61	149
Claim losses and expenses incurred in the current year	6,291	6,520
Decrease in estimated claim losses and expenses incurred in prior years	(199)	(140)
Exceptional strengthening of general insurance latent claims provisions	—	45
Included claims losses and expenses	6,153	6,574
Less:		
Payments made on claims incurred in the current year	(3,243)	(3,393)
Payments made on claims incurred in prior years	(3,104)	(3,514)
Recoveries on claim payments	297	313
Claims payments made in the year, net of recoveries	(6,050)	(6,594)
Unwind of discounting	35	47
Other movements in the claims provisions	2	(12)
Changes in claims reserve recognised as an expense	140	15
Effect of portfolio transfers, acquisitions and disposals	(171)	—
Deconsolidation of Delta Lloyd	—	(1,445)
Foreign exchange rate movements	(158)	(87)
Other movements	(2)	(1)
Carrying amount at 31 December	10,554	10,745

The effect of changes in the main assumptions is given in note 43 and the economic assumption changes are explained in note 9.

(d) Loss development tables**(i) Description of tables**

The tables that follow present the development of claim payments and the estimated ultimate cost of claims for the accident years 2003 to 2012. The upper half of the tables shows the cumulative amounts paid during successive years related to each accident year. For example, with respect to the accident year 2003, by the end of 2012 £5,727 million had actually been paid in settlement of claims. In addition, as reflected in the lower section of the table, the original estimated ultimate cost of claims of £6,385 million was re-estimated to be £5,791 million at 31 December 2012.

The original estimates will be increased or decreased, as more information becomes known about the individual claims and overall claim frequency and severity.

The Group aims to maintain strong reserves in respect of its general insurance and health business in order to protect against adverse future claims experience and development. As claims develop and the ultimate cost of claims become more certain, the absence of adverse claims experience will result in a release of reserves from earlier accident years, as shown in the loss development tables and movements table (c)(iv) above. However, in order to maintain overall reserve adequacy, the Group establishes strong reserves in respect of the current accident year (2012) where the development of claims is less mature and there is much greater uncertainty attaching to the ultimate cost of claims. Releases from prior accident year reserves are also due to an improvement in the estimated cost of claims.

Key elements of the movement in prior accident year general insurance and health net provisions during 2012 were:

- £47 million release from UK & Ireland, including Group reinsurance business, due to favourable development in Group reinsurance, health and across a number of lines of business in Ireland.
- £51 million release from Europe mainly due to favourable development of personal motor and commercial property claims in France.
- £122 million release from Canada mainly due to continued favourable experience on motor, following the legislative changes in Ontario.

Key elements of the release from prior accident year general insurance and health net provisions during 2011 were:

- £42 million strengthening from UK & Ireland, including Group reinsurance business, mainly due to unfavourable development on commercial motor, commercial liability and December 2010 freeze claims in the UK offset by favourable development of personal and commercial motor claims in Ireland.
- £6 million release from Europe mainly due to favourable development of personal and commercial motor claims in France offset by adverse development in Italy and Delta Lloyd.
- £92 million release from Canada mainly due to favourable experience on motor, following the legislative changes in Ontario, and commercial liability.

39 – Insurance liabilities continued**(ii) Gross figures**

Before the effect of reinsurance, the loss development table is:

Accident year	All prior years £m	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m	2011 £m	2012 £m	Total £m
Gross cumulative claim payments												
At end of accident year		(2,819)	(2,971)	(3,345)	(3,653)	(4,393)	(4,915)	(3,780)	(3,502)	(3,420)	(3,055)	
One year later		(4,190)	(4,561)	(5,011)	(5,525)	(6,676)	(7,350)	(5,464)	(5,466)	(4,765)		
Two years later		(4,613)	(4,981)	(5,449)	(5,971)	(7,191)	(7,828)	(6,102)	(5,875)			
Three years later		(4,972)	(5,263)	(5,784)	(6,272)	(7,513)	(8,304)	(6,393)				
Four years later		(5,258)	(5,448)	(6,001)	(6,531)	(7,836)	(8,607)					
Five years later		(5,409)	(5,617)	(6,156)	(6,736)	(8,050)						
Six years later		(5,527)	(5,725)	(6,311)	(6,936)							
Seven years later		(5,594)	(5,792)	(6,467)								
Eight years later		(5,660)	(5,826)									
Nine years later		(5,727)										
Estimate of gross ultimate claims												
At end of accident year		6,385	6,891	7,106	7,533	8,530	9,508	7,364	6,911	6,428	6,201	
One year later		6,172	6,557	6,938	7,318	8,468	9,322	7,297	7,006	6,330		
Two years later		6,124	6,371	6,813	7,243	8,430	9,277	7,281	6,950			
Three years later		6,036	6,178	6,679	7,130	8,438	9,272	7,215				
Four years later		5,932	6,008	6,603	7,149	8,409	9,235					
Five years later		5,853	6,003	6,605	7,167	8,446						
Six years later		5,813	5,953	6,591	7,167							
Seven years later		5,792	5,933	6,596								
Eight years later		5,798	5,926									
Nine years later		5,791										
Estimate of gross ultimate claims		5,791	5,926	6,596	7,167	8,446	9,235	7,215	6,950	6,330	6,201	
Cumulative payments		(5,727)	(5,826)	(6,467)	(6,936)	(8,050)	(8,607)	(6,393)	(5,875)	(4,765)	(3,055)	
	2,798	64	100	129	231	396	628	822	1,075	1,565	3,146	10,954
Effect of discounting	(479)	(4)	—	18	8	5	2	—	—	—	—	(450)
Present value	2,319	60	100	147	239	401	630	822	1,075	1,565	3,146	10,504
Cumulative effect of foreign exchange movements	—	14	18	24	39	37	(19)	(14)	(34)	(22)	—	43
Effect of acquisitions	—	1	1	1	4	—	—	—	—	—	—	7
Present value recognised in the statement of financial position	2,319	75	119	172	282	438	611	808	1,041	1,543	3,146	10,554

39 – Insurance liabilities continued**(iii) Net of reinsurance**

After the effect of reinsurance, the loss development table is:

Accident year	All prior years £m	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m	2011 £m	2012 £m	Total £m
Net cumulative claim payments												
At end of accident year		(2,819)	(2,870)	(3,281)	(3,612)	(4,317)	(4,808)	(3,650)	(3,386)	(3,300)	(2,925)	
One year later		(4,158)	(4,378)	(4,925)	(5,442)	(6,542)	(7,165)	(5,286)	(5,242)	(4,578)		
Two years later		(4,565)	(4,712)	(5,344)	(5,881)	(7,052)	(7,638)	(5,885)	(5,637)			
Three years later		(4,924)	(4,986)	(5,671)	(6,181)	(7,356)	(8,094)	(6,177)				
Four years later		(5,180)	(5,163)	(5,892)	(6,434)	(7,664)	(8,356)					
Five years later		(5,325)	(5,327)	(6,039)	(6,625)	(7,852)						
Six years later		(5,442)	(5,430)	(6,188)	(6,724)							
Seven years later		(5,502)	(5,491)	(6,245)								
Eight years later		(5,567)	(5,524)									
Nine years later		(5,592)										
Estimate of net ultimate claims												
At end of accident year		6,218	6,602	6,982	7,430	8,363	9,262	7,115	6,650	6,202	5,941	
One year later		6,093	6,266	6,818	7,197	8,302	9,104	7,067	6,751	6,103		
Two years later		6,037	6,082	6,688	7,104	8,244	9,028	7,036	6,685			
Three years later		5,942	5,882	6,544	6,996	8,249	9,007	6,978				
Four years later		5,851	5,709	6,476	6,980	8,210	8,962					
Five years later		5,772	5,699	6,448	6,992	8,221						
Six years later		5,683	5,639	6,397	6,939							
Seven years later		5,663	5,624	6,372								
Eight years later		5,667	5,613									
Nine years later		5,649										
Estimate of net ultimate claims		5,649	5,613	6,372	6,939	8,221	8,962	6,978	6,685	6,103	5,941	
Cumulative payments		(5,592)	(5,524)	(6,245)	(6,724)	(7,852)	(8,356)	(6,177)	(5,637)	(4,578)	(2,925)	
	1,695	57	89	127	215	369	606	801	1,048	1,525	3,016	9,548
Effect of discounting	(330)	1	—	19	9	5	3	—	—	—	—	(293)
Present value	1,365	58	89	146	224	374	609	801	1,048	1,525	3,016	9,255
Cumulative effect of foreign exchange movements	—	12	16	21	37	35	(19)	(12)	(32)	(20)	—	38
Effect of acquisitions	—	1	1	1	4	—	—	—	—	—	—	7
Present value recognised in the statement of financial position	1,365	71	106	168	265	409	590	789	1,016	1,505	3,016	9,300

In the loss development tables shown above, the cumulative claim payments and estimates of cumulative claims for each accident year are translated into sterling at the exchange rates that applied at the end of that accident year. The impact of using varying exchange rates is shown at the bottom of each table. Disposals are dealt with by treating all outstanding and IBNR claims of the disposed entity as 'paid' at the date of disposal.

The loss development tables above include information on asbestos and environmental pollution claims provisions from business written before 2003. The undiscounted claim provisions for continuing operations, net of reinsurance, in respect of this business at 31 December 2012 were £1,003 million (2011: £929 million). The movement in the year reflects strengthening of provisions by £8 million in the UK (2011: exceptional strengthening of £35 million), other increases in undiscounted provisions of £51 million (2011: £23 million), reclassification of commercial liability provisions of £55 million, claim payments, reinsurance recoveries and foreign exchange rate movements.

(e) Provision for unearned premiums**Movements**

The following changes have occurred in the provision for unearned premiums (UPR) during the year:

	2012 £m	2011 £m
Carrying amount at 1 January	4,483	4,855
Premiums written during the year	9,535	10,364
Less: Premiums earned during the year	(9,514)	(10,099)
Change in UPR recognised as income	21	265
Gross portfolio transfers and acquisitions	(6)	(161)
Deconsolidation of Delta Lloyd	—	(424)
Foreign exchange rate movements	(57)	(52)
Carrying amount at 31 December	4,441	4,483

40 – Liability for investment contracts

This note analyses our investment contract liabilities by type of product and describes how the Group calculates these liabilities and the assumptions used.

(a) Carrying amount

The liability for investment contracts at 31 December comprised:

	2012 £m	Restated ¹ 2011 £m
Long-term business		
Participating contracts	66,849	67,707
Non-participating contracts at fair value	46,299	43,990
Non-participating contracts at amortised cost	1,400	1,669
	47,699	45,659
Total	114,548	113,366
Less: Amounts classified as held for sale	(4,054)	—
	110,494	113,366

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, there has been a reallocation from participating insurance liabilities at 31 December 2011 to participating investment contract liabilities of £2,722 million.

(b) Long-term business investment liabilities

Investment contracts are those that do not transfer significant insurance risk from the contract holder to the issuer, and are therefore treated as financial instruments under IFRS.

Many investment contracts contain a discretionary participation feature in which the contract holder has a contractual right to receive additional benefits as a supplement to guaranteed benefits. These are referred to as participating contracts and are measured according to the methodology and Group practice for long-term business liabilities as described in note 39. They are not measured at fair value as there is currently no agreed definition of fair valuation for discretionary participation features under IFRS. In the absence of such a definition, it is not possible to provide a range of estimates within which a fair value is likely to fall. The IASB has deferred consideration of participating contracts to Phase II of its insurance contracts project.

For participating business, the discretionary participation feature is recognised separately from the guaranteed element and is classified as a liability, referred to as unallocated divisible surplus. Guarantees on long-term investment products are discussed in note 41.

Investment contracts that do not contain a discretionary participation feature are referred to as non-participating contracts and the liability is measured at either fair value or amortised cost.

Of the non-participating investment contracts measured at fair value, £45,087 million in 2012 are unit linked in structure and the fair value liability is equal to the unit reserve plus additional non-unit reserves, if required, on a fair value basis. These contracts are generally classified as 'Level 1' in the fair value hierarchy, as the unit reserve is calculated as the publicly quoted unit price multiplied by the number units in issue, and any non-unit reserve is insignificant.

For unit-linked business, a deferred acquisition cost asset and deferred income reserve liability are recognised in respect of transaction costs and front-end fees respectively, that relate to the provision of investment management services, and which are amortised on a systematic basis over the contract term. The amount of the related deferred acquisition cost asset is shown in note 27 and the deferred income liability is shown in note 50.

In the US, funding agreements consist of one to ten year fixed rate contracts. These contracts may not be cancelled by the holders unless there is a default under the agreement, but may, subject to a call premium, be terminated by Aviva at any time. Aviva issued no new funding agreements in 2012. The weighted average interest rates for fixed-rate and floating-rate funding agreements as at 31 December 2012 were 4.688% and 0.305% respectively. Funding agreements issued before 2008 are measured at fair value equal to the present value of contractual cash flows and, for business issued since 2008, are measured at amortised cost. Most funding agreements are fully collateralised and therefore their fair values are not adjusted for own credit risk. Funding agreements carried at fair value total £0.6 billion and are classified as 'Level 2' in the fair value hierarchy.

There is a small volume of annuity certain business for which the liability is measured at amortised cost using the effective interest method.

The fair value of contract liabilities measured at amortised cost is not materially different from the amortised cost liability.

(c) Movements in the year

The following movements have occurred in the year:

(i) Participating investment contracts

	2012 £m	Restated ¹ 2011 £m
Carrying amount at 1 January	67,707	72,440
Provisions in respect of new business	2,695	3,688
Expected change in existing business provisions	(2,039)	(2,618)
Variance between actual and expected experience	102	(2,708)
Impact of operating assumption changes	9	(72)
Impact of economic assumption changes	74	631
Other movements	(82)	211
Change in liability recognised as an expense	759	(868)
Foreign exchange rate movements	(1,610)	(1,352)
Deconsolidation of Delta Lloyd	—	(2,523)
Other movements	(7)	10
Carrying amount at 31 December	66,849	67,707

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, there has been a reallocation from participating insurance liabilities at 31 December 2011 to participating investment contract liabilities of £2,722 million.

40 – Liability for investment contracts continued

For many types of long-term business, including unit-linked and participating funds, movements in asset values are offset by corresponding changes in liabilities, limiting the net impact on profit. Minor variances arise from differences between actual and expected experience for persistency, mortality and other demographic factors.

The impact of assumption changes in the above analysis shows the resulting movement in the carrying value of participating investment contract liabilities. For participating business, a movement in liabilities is generally offset by a corresponding adjustment to the unallocated divisible surplus and does not impact on profit. Where assumption changes do impact on profit, these are included in the effect of changes in assumptions and estimates during the year shown in note 43, together with the impact of movements in related non-financial assets.

(ii) Non-participating investment contracts

	2012 £m	2011 £m
Carrying amount at 1 January	45,659	48,305
Provisions in respect of new business	3,851	3,863
Expected change in existing business provisions	(2,531)	(2,558)
Variance between actual and expected experience	982	(2,796)
Impact of operating assumption changes	14	1
Impact of economic assumption changes	4	7
Other movements	104	(123)
Change in liability	2,424	(1,606)
Effect of portfolio transfers, acquisitions and disposals	25	—
Deconsolidation of Delta Lloyd	—	(832)
Foreign exchange rate movements	(404)	(206)
Other movements	(5)	(2)
Carrying amount at 31 December	47,699	45,659

The variance between actual and expected experience of £1.0 billion was primarily driven by favourable movements in investment markets in 2012. The rise in investment markets increased the value of unit linked contracts, which comprise the vast majority of the non-participating investment contract liabilities. For unit-linked investment contracts, movements in asset values are offset by corresponding changes in liabilities, limiting the net impact on profit. Minor variances arise from differences between actual and expected experience for persistency, mortality and other demographic factors.

The impact of assumption changes in the above analysis shows the resulting movement in the carrying value of non-participating investment contract liabilities. The impact of assumption changes on profit are included in the effect of changes in assumptions and estimates during the year shown in note 43, which combines participating and non-participating investment contracts together with the impact of movements in related non-financial assets.

41 – Financial guarantees and options

This note details the financial guarantees and options that the Group has given for some of our insurance and investment products.

As a normal part of their operating activities, various Group companies have given guarantees and options, including investment return guarantees, in respect of certain long-term insurance and fund management products. Further information on assumptions is given in notes 39 and 40.

(a) UK Life with-profit business

In the UK, life insurers are required to comply with the FSA's realistic reporting regime for their with-profit funds for the calculation of FSA liabilities. Under the FSA's rules, provision for guarantees and options within realistic liabilities must be measured at fair value, using market-consistent stochastic models. A stochastic approach includes measuring the time value of guarantees and options, which represents the additional cost arising from uncertainty surrounding future economic conditions.

The material guarantees and options to which this provision relates are:

(i) Maturity value guarantees

Substantially all of the conventional with-profit business and a significant proportion of unitised with-profit business have minimum maturity values reflecting the sums assured plus declared annual bonus. In addition, the guarantee fund has offered maturity value guarantees on certain unit-linked products. For some unitised with-profit life contracts the amount paid after the fifth policy anniversary is guaranteed to be at least as high as the premium paid increased in line with the rise in RPI/CPI.

(ii) No market valuation reduction (MVR) guarantees

For unitised business, there are a number of circumstances where a 'no MVR' guarantee is applied, for example on certain policy anniversaries, guaranteeing that no market value reduction will be applied to reflect the difference between the accumulated value of units and the market value of the underlying assets.

41 – Financial guarantees and options continued

(iii) Guaranteed annuity options

The Group's UK with-profit funds have written individual and group pension contracts which contain guaranteed annuity rate options (GAOs), where the policyholder has the option to take the benefits from a policy in the form of an annuity based on guaranteed conversion rates. The Group also has exposure to GAOs and similar options on deferred annuities.

Realistic liabilities for GAOs in the UK with-profit funds were £1,156 million at 31 December 2012 (2011: £1,170 million). With the exception of the New With-Profits Sub Fund (NWPSF), movements in the realistic liabilities in the with-profit funds are offset by a corresponding movement in the unallocated divisible surplus, with no net impact on IFRS profit. Realistic liabilities for GAOs in the NWPSF were £180 million at 31 December 2012 (2011: £193 million).

(iv) Guaranteed minimum pension

The Group's UK with-profit funds also have certain policies that contain a guaranteed minimum level of pensions as part of the condition of the original transfer from state benefits to the policy.

In addition, the with-profit fund companies have made promises to certain policyholders in relation to their with-profit mortgage endowments. Top-up payments will be made on these policies at maturity to meet the mortgage value up to a maximum of the 31 December 1999 illustrated shortfall. For UKLAP WP policyholders, these payments are subject to certain conditions.

(b) UK Life non-profit business

The Group's UK non-profit funds are evaluated by reference to statutory reserving rules, including changes introduced in 2006 under FSA Policy Statement 06/14, *Prudential Changes for Insurers*.

(i) Guaranteed annuity options

Similar options to those written in the with-profit fund have been written in relation to non-profit products. Provision for these guarantees does not materially differ from a provision based on a market-consistent stochastic model, and amounts to £35 million at 31 December 2012 (2011: £35 million).

(ii) Guaranteed unit price on certain products

Certain unit-linked pension products linked to long-term life insurance funds provide policyholders with guaranteed benefits at retirement or death. No additional provision is made for this guarantee as the investment management strategy for these funds is designed to ensure that the guarantee can be met from the fund, mitigating the impact of large falls in investment values and interest rates.

(c) Overseas life businesses

In addition to guarantees written in the Group's UK life businesses, our overseas businesses have also written contracts containing guarantees and options. Details of the significant guarantees and options provided by overseas life businesses are set out below.

(i) France

Guaranteed surrender value and guaranteed minimum bonuses

Aviva France has written a number of contracts with such guarantees. The guaranteed surrender value is the accumulated value of the contract including accrued bonuses. Bonuses are based on accounting income from amortised bond portfolios, where the duration of bond portfolios is set in relation to the expected duration of the policies, plus income and releases from realised gains on equity-type investments. Policy reserves are equal to guaranteed surrender values. Local statutory accounting envisages the establishment of a reserve, 'Provision pour Aléas Financiers' (PAF), when accounting income is less than 125% of guaranteed minimum credited returns. No PAF was established at the end of 2012.

The most significant of these contracts is the AFER Eurofund which has total liabilities of £33 billion at 31 December 2012 (2011: £33 billion). The guaranteed minimum bonus is agreed between Aviva France and the AFER association at the end of each year, in respect of the following year. The bonus was 3.45% for 2012 (2011: 3.43%) compared with an accounting income from the fund of 3.94% (2011: 3.92%).

Non-AFER contracts with guaranteed surrender values had liabilities of £14 billion at 31 December 2012 (2011: £14 billion) and all guaranteed annual bonus rates are between 0% and 4.5%.

Guaranteed death and maturity benefits

In France, the Group has also sold unit-linked policies where the death and/or maturity benefit is guaranteed to be at least equal to the premiums paid. The reserve held in the Group's consolidated statement of financial position at the end of 2012 for this guarantee is £101 million (2011: £130 million). The reserve is calculated on a prudent basis and is in excess of the economic liability. At the end of 2012, total sums at risk for these contracts were £223 million (2011: £631 million) out of total unit-linked funds of £12 billion (2011: £12 billion). The average age of policyholders was approximately 54. It is estimated that this liability would increase by £88 million (2011: £96 million) if yields were to decrease by 1% per annum and by £21 million (2011: £26 million) if equity markets were to decline by 10% from year end 2012 levels. These figures do not reflect our ability to review the tariff for this option.

(ii) Ireland

Guaranteed annuity options

Products with similar GAOs to those offered in the UK have been issued in Ireland. The current net of reinsurance provision for such options is £256 million (2011: £271 million). This has been calculated on a deterministic basis, making conservative assumptions for the factors which influence the cost of the guarantee, principally annuitant mortality option take-up and long-term interest rates.

These GAOs are 'in the money' at current interest rates but the exposure to interest rates under these contracts has been hedged through the use of reinsurance, using derivatives (swaptions). The swaptions effectively guarantee that an interest rate of 5% will be available at the vesting date of these benefits so there is reduced exposure to a further decrease in interest rates.

41 – Financial guarantees and options continued

'No MVR' guarantees

Certain unitised with-profit policies containing 'no MVR' guarantees, similar to those in the UK, have been sold in Ireland.

These guarantees are currently 'in-the-money' by £0.4 million (2011: £5.5 million). This has been calculated on a deterministic basis as the excess of the current policy surrender value over the discounted value (excluding terminal bonus) of the guarantees. The value of these guarantees is usually sensitive to the performance of investments held in the with-profit fund. Amounts payable under these guarantees are determined by the bonuses declared on these policies. There is no sensitivity to either interest rates or equity markets since there is no longer any exposure to equity in these funds and a matching strategy has been implemented for bonds.

Return of premium guarantee

Until 2005, Aviva Life and Pensions Ireland wrote two tranches of linked bonds with a return of premium guarantee, or a price floor guarantee, after five or six years. The first tranche expired before the end of the previous financial reporting period. The second tranche expired during the last quarter of the current reporting period. As a result there is no provision held for this business (2011: £7 million).

(iii) Spain and Italy

Guaranteed investment returns and guaranteed surrender values

The Group has also written contracts containing guaranteed investment returns and guaranteed surrender values in both Spain and Italy. Traditional profit-sharing products receive an appropriate share of the investment return, assessed on a book value basis, subject to a guaranteed minimum annual return of up to 6% in Spain and 4% in Italy on existing business, while on new business the maximum guaranteed rate is lower. Liabilities are generally taken as the face value of the contract plus, if required, an explicit provision for guarantees calculated in accordance with local regulations. At 31 December 2012, total liabilities for the Spanish business were £3 billion (2011: £3 billion) with a further reserve of £0.1 million (2011: £5.1 million) for guarantees. Total liabilities for the Italian business were £10 billion (2011: £11 billion), with a further provision of £45 million (2011: £43 million) for guarantees. Liabilities are most sensitive to changes in the level of interest rates. It is estimated that provisions for guarantees would need to increase by £5 million (2011: £18 million) in Spain and £1 million (2011: £5 million) in Italy if interest rates fell by 1% from end 2012 values. Under this sensitivity test, the guarantee provision in Spain is calculated conservatively, assuming a long-term market interest rate of 1.89% and no lapses or premium discontinuances.

(iv) United States

Indexed and total return strategy products

In the United States, the Group writes indexed life and deferred annuity products. These products guarantee the return of principal to the policyholder and credit interest based on certain indices, primarily the Standard & Poor's 500 Composite Stock Price Index. A portion of each premium is used to purchase derivatives to hedge the growth in interest credited to the policyholder. The derivatives held by the Group and the options embedded in the policy are both carried at fair value.

The US Treasury swap curve plus a risk adjustment of 1.06% (2011: 2.48%) for indexed life and 1.57% (2011: 2.51%) for indexed deferred annuities is used as the discount rate to calculate the fair value of the embedded options.

The risk adjustment calculation is based on market spreads on senior long-term unsecured Aviva plc debt with a reduction to reflect policyholder priority over other creditors in case of default. The amount of change in the fair value of these embedded options resulting from the risk adjustment in 2012 is an increase of £269 million (2011: £453 million), and is principally attributable to market factors rather than instrument specific credit risk. At 31 December 2012, the total liabilities for indexed products were £23 billion (2011: £22 billion), including liabilities for the embedded option of £2.7 billion (2011: £2.6 billion). If interest rates were to increase by 1%, the provision for embedded options would decrease by £151 million (2011: £152 million) and, if interest rates were to decrease by 1%, the provision would increase by £167 million (2011: £167 million).

The Group has certain products that credit interest based on a total return strategy, whereby policyholders are allowed to allocate their premium payments to different asset classes within the general account. The Group guarantees a minimum return of premium plus approximately 3% interest over the term of the contracts. The linked general account assets are fixed maturity securities, and both the securities and the contract liabilities are carried at fair value. At 31 December 2012, the liabilities for total return strategy products were £0.8 billion (2011: £0.9 billion).

The Group offers an optional lifetime guaranteed income benefit focused on the retirement income segment of the deferred annuity marketplace to help customers manage income during both the accumulation stage and the distribution stage of their financial life. At 31 December 2012, a total of £11.0 billion (2011: £10.1 billion) in indexed deferred annuities have elected this benefit, taking steps to guarantee retirement income.

(d) Sensitivity

In providing these guarantees and options, the Group's capital position is sensitive to fluctuations in financial variables including foreign currency exchange rates, interest rates, real estate prices and equity prices. Interest rate guaranteed returns, such as those available on GAOs, are sensitive to interest rates falling below the guaranteed level. Other guarantees, such as maturity value guarantees and guarantees in relation to minimum rates of return, are sensitive to fluctuations in the investment return below the level assumed when the guarantee was made.

42 – Reinsurance assets

This note details the reinsurance recoverables on our insurance and investment contract liabilities.

(a) Carrying amounts

The reinsurance assets at 31 December comprised:

	2012 £m	2011 £m
Long-term business		
Insurance contracts	4,291	3,747
Participating investment contracts	3	—
Non-participating investment contracts ¹	1,678	1,626
	5,972	5,373
Outstanding claims provisions	93	126
	6,065	5,499
General insurance and health		
Outstanding claims provisions	900	974
Provisions for claims incurred but not reported	354	395
	1,254	1,369
Provisions for unearned premiums	248	245
	1,502	1,614
	7,567	7,113
Less: Amounts classified as held for sale	(883)	(1)
Total	6,684	7,112

¹ Balances in respect of all reinsurance treaties are included under reinsurance assets, regardless of whether they transfer significant insurance risk.

Of the above total, £5,251 million (2011: £5,086 million) is expected to be recovered more than one year after the statement of financial position date.

(b) Assumptions

The assumptions, including discount rates, used for reinsurance contracts follow those used for insurance contracts. Reinsurance assets are valued net of an allowance for their recoverability.

(c) Movements

The following movements have occurred in the reinsurance asset during the year:

(i) In respect of long-term business provisions

	2012 £m	2011 £m
Carrying amount at 1 January	5,373	5,115
Asset in respect of new business	387	187
Expected change in existing business asset	166	7
Variance between actual and expected experience	197	290
Impact of operating assumption changes	(306)	(9)
Impact of economic assumption changes	143	433
Other movements	(137)	(260)
Change in asset	450	648
Effect of portfolio transfers, acquisitions and disposals	197	(2)
Deconsolidation of Delta Lloyd	—	(375)
Foreign exchange rate movements	(48)	(13)
Carrying amount at 31 December	5,972	5,373

The impact of assumption changes in the above analysis shows the resulting movement in the carrying value of reinsurance assets. The changes to the reinsurance asset from assumption changes mainly relates to business in the UK and Ireland, with corresponding movements in gross insurance contract liabilities. For participating businesses, a movement in reinsurance assets is generally offset by a corresponding adjustment to the unallocated divisible surplus and does not impact on profit. Where assumption changes do impact profit, these are included in the effect of changes in assumptions and estimates during the year shown in note 43, together with the impact of movements in related liabilities and other non-financial assets.

42 – Reinsurance assets continued**(ii) In respect of general insurance and health outstanding claims provisions and IBNR**

	2012 £m	2011 £m
Carrying amount at 1 January	1,369	1,558
Impact of changes in assumptions	22	87
Reinsurers' share of claim losses and expenses		
Incurred in current year	286	247
Incurred in prior years	13	(84)
Exceptional strengthening of general insurance latent claims provisions	—	10
Reinsurers' share of incurred claim losses and expenses	299	173
Less:		
Reinsurance recoveries received on claims		
Incurred in current year	(138)	(138)
Incurred in prior years	(150)	(196)
Reinsurance recoveries received in the year	(288)	(334)
Unwind of discounting	13	19
Other movements	—	(1)
Change in reinsurance asset recognised as income	46	(56)
Effect of portfolio transfers, acquisitions and disposals	(136)	28
Deconsolidation of Delta Lloyd	—	(153)
Foreign exchange rate movements	(26)	(2)
Other movements	1	(6)
Carrying amount at 31 December	1,254	1,369

(iii) Reinsurers' share of the provision for UPR

	2012 £m	2011 £m
Carrying amount at 1 January	245	307
Premiums ceded to reinsurers in the year	641	650
Less: Reinsurers' share of premiums earned during the year	(636)	(678)
Change in reinsurance asset recognised as income	5	(28)
Reinsurers' share of portfolio transfers and acquisitions	3	—
Deconsolidation of Delta Lloyd	—	(30)
Foreign exchange rate movements	(5)	(4)
Other movements	—	—
Carrying amount at 31 December	248	245

43 – Effect of changes in assumptions and estimates during the year

Certain estimates and assumptions used in determining our liabilities for insurance and investment contract business were changed from 2011 to 2012, affecting the profit recognised for the year with an equivalent effect on liabilities. This note analyses the effect of the changes. This note only allows for the impact on liabilities and related assets, such as unallocated divisible surplus, reinsurance, deferred acquisition costs and AVIF, and does not allow for offsetting movements in the value of backing financial assets.

	Effect on profit 2012 £m	Effect on profit 2011 £m
Assumptions		
Long-term insurance business		
Interest rates	(515)	(2,403)
Expenses	11	5
Persistency rates	—	(4)
Mortality for assurance contracts	—	35
Mortality for annuity contracts	241	(21)
Tax and other assumptions	(207)	99
Investment contracts		
Interest rates	(2)	(82)
Expenses	(1)	—
Persistency rates	—	—
Tax and other assumptions	—	28
General insurance and health business		
Change in loss ratio assumptions	—	5
Change in discount rate assumptions	(21)	(90)
Change in expense ratio and other assumptions	(21)	22
Total	(515)	(2,406)

The impact of interest rates for long-term business relates primarily to the UK and Ireland driven by the reduction in valuation interest rates. This had the effect of increasing liabilities and hence a negative impact on profit. The overall impact on profit also depends on movements in the value of assets backing the liabilities, which is not included in this disclosure. The impact of tax and other assumptions relates mainly to strengthening of credit default assumptions for commercial mortgages backing UK annuity business.

44 – Unallocated divisible surplus

An unallocated divisible surplus (UDS) is established where the nature of policy benefits is such that the division between shareholder reserves and policyholder liabilities is uncertain at the reporting date. Therefore the expected duration for settlement of the UDS is not defined.

The following movements have occurred in the year:

	2012 £m	2011 £m
Carrying amount at 1 January	650	3,428
Change in participating contract assets	6,140	(3,016)
Change in participating contract liabilities	253	244
Other movements	(77)	70
Change in liability recognised as an expense	6,316	(2,702)
Effect of portfolio transfers, acquisitions and disposal	1	—
Deconsolidation of Delta Lloyd	—	(144)
Foreign exchange rate movements	24	60
Other movements	(5)	8
Carrying amount at 31 December	6,986	650
Less: Amounts classified as held for sale	(55)	—
	6,931	650

In Italy, the UDS balance was £2 million negative at 31 December 2012 (2011: £1,449 million negative). In Spain, certain participating funds had negative UDS balances at 31 December 2012, although in aggregate the UDS balance was £95 million positive (2011: £13 million positive).

Negative UDS balances result from an accounting mismatch between participating assets carried at market value and participating liabilities measured using local practice. The negative balances were tested for recoverability using embedded value methodology and in line with local accounting practice. Testing is conducted at a participating fund-level within each life entity. The negative balances are considered to be recoverable from margins in the existing participating business liabilities.

In Italy, there was a loss of £9 million for negative UDS considered irrecoverable (2011: £17 million loss), and in Spain a reversal of £33 million of previous losses (2011: £49 million loss).

In Italy the estimation of the recoverable negative UDS balance uses a real-world embedded value method, with a risk-discount rate of 6.25%. (2011: 7.05%). The embedded value method includes implicit allowance for the time value of options and guarantees. If the risk discount rate were increased by 1% it is estimated that the recoverable negative UDS balance would be unchanged.

In Spain, the estimation of the recoverable negative UDS balance uses a market-consistent embedded value method.

45 – Tax assets and liabilities

This note analyses the tax assets and liabilities that appear in the statement of financial position and explains the movements in these balances in the year.

(a) Current tax

Current tax assets recoverable and liabilities payable in more than one year are £37 million and £8 million (2011: £29 million and £48 million), respectively.

(b) Deferred tax

(i) The balances at 31 December comprise:

	2012 £m	2011 £m
Deferred tax assets	220	238
Deferred tax liabilities	(1,227)	(1,171)
Net deferred tax liability	(1,007)	(933)
Less: Amounts classified as held for sale	648	—
	(359)	(933)

Amounts classified as held for sale include £32 million of deferred tax assets (2011: £nil) and £680 million of deferred tax liabilities (2011: £nil).

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

	2012 £m	2011 £m
Long-term business technical provisions and other insurance items	2,067	455
Deferred acquisition costs	(681)	(598)
Unrealised gains on investments	(2,869)	(347)
Pensions and other post-retirement obligations	(135)	(245)
Unused losses and tax credits	535	462
Subsidiaries, associates and joint ventures	(10)	(10)
Intangibles and additional value of in-force long-term business	(363)	(445)
Provisions and other temporary differences	449	(205)
Net deferred tax liability	(1,007)	(933)
Less: Amounts classified as held for sale	648	—
	(359)	(933)

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

	2012 £m	2011 £m
Net liability at 1 January	(933)	(1,470)
Acquisition and disposal of subsidiaries	—	53
Amounts (charged)/credited to income statement (note 13a)	(122)	513
Amounts credited/(charged) to other comprehensive income (note 13b)	24	(354)
Deconsolidation of Delta Lloyd	—	326
Foreign exchange rate movements	27	(6)
Other movements	(3)	5
Net liability at 31 December	(1,007)	(933)

Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised. In countries where there is a history of tax losses, deferred tax assets are only recognised in excess of deferred tax liabilities if there is convincing evidence that future profits will be available. Where this is the case, the directors have relied on business plans supporting future profits.

The Group has unrecognised tax losses and other temporary differences of £1,005 million (2011: £910 million) to carry forward against future taxable income of the necessary category in the companies concerned. Of these, trading losses of £278 million will expire within the next 20 years. The remaining losses have no expiry date.

In addition, the Group has unrecognised capital losses of £652 million (2011: £418 million). These have no expiry date.

There are no temporary differences in respect of unremitted overseas retained earnings for which deferred tax liabilities have not been recognised at 31 December 2012 (2011: £nil).

46 – Provisions

This note details the non-insurance provisions that the Group holds, and shows the movements in these during the year.

(a) Carrying amounts

	2012 £m	2011 £m
Total IAS 19 obligations to main staff pension schemes (note 47(e)(vii))	651	406
Deficits in other staff pension schemes	88	86
Total IAS 19 obligations to staff pension schemes	739	492
Restructuring provisions	144	106
Other provisions	423	398
Total provisions	1,306	996
Less: Amounts classified as held for sale	(187)	(4)
	1,119	992

Other provisions comprise many small provisions throughout the Group for obligations such as costs of compensation, litigation, staff entitlements and reorganisation.

Of the total, £901 million (2011: £605 million) is expected to be settled more than one year after the statement of financial position date.

(b) Movements on restructuring and other provisions

	2012			2011		
	Restructuring provisions £m	Other provisions £m	Total £m	Restructuring provisions £m	Other provisions £m	Total £m
At 1 January	106	398	504	152	690	842
Additional provisions	236	120	356	82	69	151
Unused amounts reversed	—	(30)	(30)	(5)	(40)	(45)
Change in the discounted amount arising from passage of time	—	5	5	—	3	3
Charge to income statement	236	95	331	77	32	109
Utilised during the year	(197)	(53)	(250)	(50)	(124)	(174)
Disposal of subsidiaries	—	(3)	(3)	—	(6)	(6)
Effect of deconsolidation of Delta Lloyd	—	—	—	(55)	(177)	(232)
Foreign exchange rate movements	(1)	(14)	(15)	(18)	(17)	(35)
At 31 December	144	423	567	106	398	504

47 – Pension obligations

(a) Introduction

The Group operates a large number of defined benefit and defined contribution pension schemes. The material defined benefit schemes are in the UK, Canada and Ireland with the main UK scheme being the largest. This note gives full IAS 19 disclosures for these schemes. The smaller ones, while still measured under IAS 19, are included as one total within Provisions (see note 46). Similarly, while the charges to the income statement for the main schemes are shown in section (e)(iv) below, the total charges for all pension schemes are disclosed in section (d) below.

The assets of the UK, Irish and Canadian schemes are held in separate trustee-administered funds to meet long-term pension liabilities to past and present employees. In all schemes, the appointment of trustees of the funds is determined by their trust documentation, and they are required to act in the best interests of the schemes' beneficiaries. The long-term investment objectives of the trustees and the employers are to limit the risk of the assets failing to meet the liabilities of the schemes over the long term, and to maximise returns consistent with an acceptable level of risk so as to control the long-term costs of these schemes.

A full actuarial valuation of each of the defined benefit schemes is carried out at least every three years for the benefit of scheme trustees and members. Actuarial reports have been submitted for each scheme within this period, using appropriate methods for the respective countries on local funding bases.

(b) Membership

The number of scheme members was as follows:

	United Kingdom		Ireland		Canada	
	2012 Number	2011 Number	2012 Number	2011 Number	2012 Number	2011 Number
Active members	—	—	791	1,063	—	—
Deferred members	56,825	57,328	1,246	998	1,022	1,213
Pensioners	30,647	30,447	723	707	1,344	1,284
Total members	87,472	87,775	2,760	2,768	2,366	2,497

As noted below, the final salary sections of both the UK schemes were closed to future accrual with effect from 1 April 2011. The Canadian scheme closed to future accrual on 31 December 2011.

(c) UK schemes

In the UK, the Group operates two main pension schemes, the Aviva Staff Pension Scheme (ASPS) and the smaller RAC (2003) Pension Scheme which was retained after the sale of RAC Limited in September 2011.

The Group confirmed its decision to close the final salary sections of both UK schemes with effect from 1 April 2011, with entry into the defined contribution sections being offered to the staff members affected. New entrants join the defined contribution section of the ASPS. Closure of the schemes has removed the volatility associated with adding future accrual for active members, and has also led to lower service costs and their cash funding since April 2011.

(i) Defined benefit section of the ASPS

This scheme is operated by a trustee company, with 11 trustee directors, comprising representatives of the employers, staff, pensioners and an independent trustee (referred to as the trustees). The Company works closely with the trustees who are required to consult it on the funding of the scheme and its investment strategy. Following each actuarial valuation, the Company and the trustees agree the level of contributions needed and funding levels are then monitored on an annual basis.

At 31 March 2009, the date of the last actuarial valuation, this section of the scheme had an excess of obligations over available assets, on a funding basis, which uses more prudent assumptions than are required for reporting under IAS 19, of £3.0 billion. As a result of that valuation, the Company and the trustees have agreed a long-term funding plan where contributions, together with anticipated growth in scheme investments, are expected to eliminate the funding deficit over time. Under this agreement, deficit funding payments of £378 million were made in 2010, £178 million in 2011 and £128 million in 2012. Further funding payments of £144 million are expected in 2013. Funding payments along with the rise in gilt yields and return on invested scheme assets have resulted in a reduced deficit which is estimated to have fallen by £1.3 billion to £1.0 billion at 31 December 2012. The Company is currently undergoing a triennial actuarial valuation as at 31 March 2012, which is expected to be finalised by 30 June 2013.

(ii) Defined contribution (money purchase) section of the ASPS

The trustees have responsibility for selecting a range of suitable funds in which the members can choose to invest and for monitoring the performance of the available investment funds. Members are responsible for reviewing the level of contributions they pay and the choice of investment fund to ensure these are appropriate to their attitude to risk and their retirement plans. Members of this section contribute at least 2% of their pensionable salaries and, depending on the percentage chosen, the Company contributes up to a maximum 14%, together with the cost of the death-in-service benefits. These contribution rates are unchanged for 2013.

47 – Pension obligations continued

(d) Charge to staff costs in the income statement

The total pension charge to staff costs of all the Group's defined benefit and defined contribution schemes were:

	2012 £m	2011 £m
Continuing operations		
UK defined benefit schemes	12	36
Overseas defined benefit schemes	7	22
Total defined benefit schemes (note 10b)	19	58
UK defined contribution schemes	91	75
Overseas defined contribution schemes	11	11
Total defined contribution schemes (note 10b)	102	86
Total charge from continuing operations	121	144
Total charge from discontinued operations	5	16
Total charge for pension schemes	126	160

There were no significant contributions outstanding or prepaid as at either 31 December 2012 or 2011.

(e) IAS 19 disclosures

Disclosures under IAS 19 for the material defined benefit schemes in the UK, Ireland and Canada, are given below. Where schemes provide both defined benefit and defined contribution pensions, the assets and liabilities shown exclude those relating to defined contribution pensions. Total employer contributions for these schemes in 2013, including the ASPS deficit funding, are currently expected to be £230 million.

(i) Assumptions on scheme liabilities

The projected unit credit method

The inherent uncertainties affecting the measurement of scheme liabilities require these to be measured on an actuarial basis. This involves discounting the best estimate of future cash flows to be paid out by the scheme using the projected unit credit method. This is an accrued benefits valuation method which calculates the past service liability to members and makes allowance for their projected future earnings. It is based on a number of actuarial assumptions, which vary according to the economic conditions of the countries in which the relevant businesses are situated, and changes in these assumptions can materially affect the measurement of the pension obligations.

Alternative measurement methods

There are alternative methods of measuring liabilities, for example by calculating an accumulated benefit obligation (the present value of benefits for service already rendered but with no allowance for future salary increases) or on a solvency basis, using the cost of securing the benefits at a particular date with an insurance company or one of the growing market of alternative buy-out providers. This could take the form of a buy-out, in which the entire liability will be settled in one payment with all obligations transferred to an insurance company or buy-out provider, or a buy-in, in which annuities or other insurance products are purchased to cover a part or all of the liability. A valuation of the liabilities in either of these cases will almost always result in a higher estimate of the pension deficit than under an on-going approach, as they assume that the sponsor immediately transfers the majority, if not all, of the risk to another provider who would be seeking to make a profit on the transaction. However there is no active market of organisations that would be able to offer a full buy-out option for schemes of the size of our main UK scheme.

There is a small buy-out market in Ireland, largely restricted to pensions currently in payment and it is not clear whether current capacity would enable an immediate buy-out of our Irish pension liabilities at present. The Canadian defined benefit plan's liabilities represent the likely limit on what the Canadian group annuity market could absorb at normal competitive group annuity prices if the entire plan were subject to a buy-out valuation. There is in fact a reasonably high chance that only a portion of the plan's liabilities could be absorbed in one tranche.

IAS 19 requires us to use the projected unit credit method to measure our pension scheme liabilities. Neither of the alternative methods is considered appropriate in presenting fairly the Group's obligations to the members of its pension schemes on an ongoing basis, so they are not considered further.

Valuations and assumptions

The valuations used for accounting under IAS 19 have been based on the most recent full actuarial valuations, updated to take account of that standard's requirements in order to assess the liabilities of the material schemes at 31 December 2012. Scheme assets are stated at their fair values at 31 December 2012.

47 – Pension obligations continued

The main actuarial assumptions used to calculate scheme liabilities under IAS 19 are:

	UK		Ireland		Canada	
	2012	2011	2012	2011	2012	2011
Inflation rate	3.0%	3.1%	2.0%	2.0%	2.5%	2.5%
General salary increases	4.8%	4.9%	3.5%	3.5%	3.0%	3.75%
Pension increases	3.0%	3.1%	2.0%	2.0%	1.25%	1.25%
Deferred pension increases	3.0%	3.1%	2.0%	2.0%	—	—
Discount rate	4.5%	4.9%	3.5%	5.7%	3.75%	4.5%
Basis of discount rate	AA-rated corporate bonds		AA-rated corporate bonds		AA-rated corporate bonds	

The discount rate and pension increase rate are the two assumptions that have the largest impact on the value of the liabilities, with the difference between them being known as the net discount rate. For each country, the discount rate is based on current average yields of high-quality debt instruments taking account of the maturities of the defined benefit obligations. A 1% increase in this rate (and therefore the net discount rate) would reduce the liabilities by £2.0 billion and the service cost for the year by £2 million. It would also increase the interest cost on the liabilities by £1 million.

Mortality assumptions

Mortality assumptions are significant in measuring the Group's obligations under its defined benefit schemes, particularly given the maturity of these obligations in the material schemes. The assumptions used are summarised in the table below and have been selected to reflect the characteristics and experience of the membership of these schemes.

The mortality tables, average life expectancy and pension duration used at 31 December 2012 for scheme members are as follows:

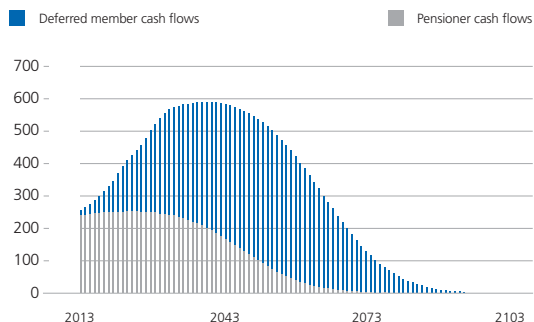
Mortality table	Normal retirement age (NRA)	Life expectancy/(pension duration) at NRA of a male		Life expectancy/(pension duration) at NRA of a female	
		Currently aged NRA	20 years younger than NRA	Currently aged NRA	20 years younger than NRA
UK – ASPS Club Vita pooled experience, including an allowance for future improvements	60	90.1 (30.1)	93.3 (33.3)	90.1 (30.1)	92.2 (32.2)
– RAC SAPS series 1, including allowances for future improvement	65	87.9 (22.9)	90.9 (25.9)	89.9 (24.9)	91.9 (26.9)
Ireland 94% PNA00 with allowance for future improvements	61	87.0 (26.0)	90.2 (29.2)	89.9 (28.9)	93.0 (32.0)
Canada UP1994, with Projection Scale AA applied on a generational basis	65	84.7 (19.7)	86.2 (21.2)	87.1 (22.1)	87.9 (22.9)

The assumptions above are based on commonly used mortality tables and, in the UK, are those used by both schemes' trustees in the most recently completed full actuarial valuations. The tables make allowance for observed variations in such factors as age, gender, pension amount, salary and postcode-based lifestyle group, and have been adjusted to reflect recent research into mortality experience. However, the extent of future improvements in longevity is subject to considerable uncertainty and judgement is required in setting this assumption. In the UK schemes, which are the most material to the Group, the assumptions include an allowance for future mortality improvement, based on the actuarial profession's long and medium cohort projection tables (for the ASPS and RAC schemes respectively) and incorporating underpins to the rate of future improvement equal to 1.5% pa for males and 1.0% pa for females. The effect of assuming all members were one year younger would increase the liabilities in all the schemes by £293 million and would not significantly impact the service cost for the year.

The discounted scheme liabilities have an average duration of 20 years in the main UK scheme, 21 years in the RAC scheme, 22 years in the Irish scheme and 13 years in the Canadian scheme. The undiscounted benefits payable from the main UK defined benefit scheme are expected to be as shown in the chart below:

47 – Pension obligations continued

Undiscounted benefit payments £m



(ii) Assumptions on scheme assets

The expected rates of return on the schemes' assets are:

	UK		Ireland		Canada	
	2012	2011	2012	2011	2012	2011
Equities	5.8%	7.2%	5.9%	6.9%	5.8%	7.0%
Bonds	3.4%	4.4%	3.2%	2.7%	3.2%	3.2%
Property	4.3%	5.7%	4.4%	5.4%	n/a	n/a
Cash	0.7%	0.6%	0.9%	2.7%	0.8%	1.0%

The expected rates of return on the schemes' assets presented above are as at the beginning of the year. The overall rates of return are based on the expected returns within each asset category and on current asset allocations. The expected returns for equities and properties are aligned with the rates used for the Group's longer-term investment return assumptions. The figures for the total expected return on scheme assets in the following section are stated after deducting investment expenses and, in Ireland, the government levy on pension fund assets. The amended IAS 19, *Employee Benefits*, which is effective from 1 January 2013, will replace the concept of expected return on scheme assets with interest on scheme assets, which will be calculated using the same interest rate as applied for the purpose of discounting the defined benefit obligation.

(iii) Investments in Group-managed funds and insurance policies

Plan assets include investments in Group-managed funds in the consolidated statement of financial position of £62 million (2011: £112 million) and insurance policies with other Group companies of £179 million (2011: £163 million) in the main UK scheme.

(iv) Pension expense

The total pension expense comprises:

Recognised in the income statement

	2012 £m	2011 £m
Continuing operations		
Current service cost	(19)	(51)
Gains on curtailments	15	—
Total pension cost from continuing operations	(4)	(51)
Total pension cost from discontinued operations	—	(7)
Total pension cost charged to net operating expenses	(4)	(58)
Expected return on scheme assets	427	452
Interest charge on scheme liabilities	(509)	(539)
Charge to finance costs from continuing operations	(82)	(87)
Charge to finance costs from discontinued operations	—	(26)
Total charge to finance costs	(82)	(113)
Total charge to income arising from continuing operations	(86)	(138)
Total charge to income arising from discontinued operations	—	(33)
Total charge to income	(86)	(171)

The gains on curtailments in 2012 arose from restructuring activities in Ireland.

47 – Pension obligations continued**Recognised in the statement of comprehensive income**

	2012 £m	2011 £m
Continuing operations		
Expected return on scheme assets	(427)	(452)
Actual return on these assets	611	1,815
Actuarial gains on scheme assets	184	1,363
Experience losses arising on scheme liabilities	(100)	(46)
Changes in assumptions underlying the present value of the scheme liabilities	(914)	(321)
Actuarial (losses)/gains from continuing operations	(830)	996
Actuarial gains from discontinued operations	—	11
Total actuarial (losses)/gains recognised in other comprehensive income	(830)	1,007
Attributable to equity shareholders of Aviva plc	(830)	1,002
Attributable to non-controlling interests	—	5
	(830)	1,007

The loss arising from changes in assumptions in 2012 primarily reflects the impact of lower discount rates for liabilities.

The cumulative amount of actuarial gains and losses on the pension schemes recognised in other comprehensive income since 1 January 2004 (the date of transition to IFRS) is a loss of £1,054 million at 31 December 2012 (2011: cumulative loss of £224 million).

(v) Experience gains and losses

The following disclosures of experience gains and losses give a five-year history. Scheme assets exclude insurance policies with Group companies and income on the assets underlying them.

	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Fair value of scheme assets at the end of the year	12,281	11,791	9,971	8,754	7,936
Present value of scheme liabilities at the end of the year	(11,675)	(10,527)	(11,419)	(11,812)	(9,951)
Net surplus/(deficits) in the schemes	606	1,264	(1,448)	(3,058)	(2,015)
Difference between the expected and actual return on scheme assets					
Amount of gains/(losses)	184	1,363	547 ¹	561 ¹	(1,893) ¹
Percentage of the scheme assets at the end of the year	1.5%	11.6%	5.5%	6.4%	23.8%
Experience (losses)/gains on scheme liabilities (excluding changes in assumptions)					
Amount of (losses)/gains	(100)	(46)	450 ¹	77 ¹	105 ¹
Percentage of the present value of scheme liabilities	0.9%	0.4%	3.9%	0.7%	1.1%

¹ Including gains and losses from discontinued operations.

(vi) Risk management and asset allocation strategy

As noted above, the long-term investment objectives of the trustees and the employers are to limit the risk of the assets failing to meet the liabilities of the schemes over the long term, and to maximise returns consistent with an acceptable level of risk so as to control the long-term costs of these schemes. To meet these objectives, each scheme's assets are invested in a diversified portfolio, consisting primarily of debt securities, equity securities and property.

Main UK scheme

Both the Group and the trustees regularly review the asset/liability management of the main UK scheme. It is fully understood that, whilst the current asset mix is designed to produce appropriate long-term returns, this introduces a material risk of volatility in the scheme's surplus or deficit of assets compared with its liabilities.

The principal risks to which the scheme is exposed are interest rate, inflation and equity markets. These are actively mitigated for example, by using inflation and interest rate swaps. Additionally, the exposure to equities has been reduced over time. There is also an exposure to currency risk where assets are not denominated in the same currency as the liabilities. The majority of this exposure has been removed by the use of hedging instruments.

Other schemes

The other schemes are considerably less material but their risks are managed in a similar way to those in the main UK scheme.

47 – Pension obligations continued**(vii) Recognition in the statement of financial position**

The assets and liabilities of the schemes attributable to defined benefit members at 31 December 2012 were:

	2012				2011			
	UK £m	Ireland £m	Canada £m	Total £m	UK £m	Ireland £m	Canada £m	Total £m
Equities	909	87	92	1,088	735	46	76	857
Bonds	8,867	260	121	9,248	8,663	233	129	9,025
Property	914	12	—	926	657	13	—	670
Other	957	47	15	1,019	1,135	90	14	1,239
Total fair value of assets	11,647	406	228	12,281	11,190	382	219	11,791
Present value of scheme liabilities	(10,501)	(777)	(397)	(11,675)	(9,606)	(539)	(382)	(10,527)
Net surplus/(deficits) in the schemes	1,146	(371)	(169)	606	1,584	(157)	(163)	1,264
Surplus included in other assets (note 27)	1,257	—	—	1,257	1,670	—	—	1,670
Deficits included in provisions (note 46)	(111)	(371)	(169)	(651)	(86)	(157)	(163)	(406)
	1,146	(371)	(169)	606	1,584	(157)	(163)	1,264

Other assets comprise cash at bank, derivative financial instruments, receivables and payables.

Plan assets in the table above include investments in Group-managed funds and insurance policies, as described in section (iii) above. Where the investment and insurance policies are in segregated funds with specific asset allocations, they are included in the appropriate line in the table above, otherwise they appear in 'Other'.

The present value of unfunded post-retirement benefit obligations included in the table above is £127 million at 31 December 2012 (2011: £116 million).

(viii) Movements in the scheme deficits and surpluses

Movements in the pension schemes' surpluses and deficits comprise:

	Scheme assets £m	Scheme liabilities £m	Pension scheme net surplus/ (deficit) £m	Adjust for Group insurance policies £m	IAS 19 pensions net surplus/ (deficit) £m
2012					
Net surplus in the schemes at 1 January	11,791	(10,527)	1,264	—	1,264
Employer contributions	250	—	250	—	250
Employee contributions	2	(2)	—	—	—
Benefits paid	(357)	357	—	—	—
Current and past service cost (see (iv) above)	—	(19)	(19)	—	(19)
Gain on curtailments and settlements (see (iv) above)	—	15	15	—	15
Credit/(charge) to finance costs (see (iv) above)	427	(509)	(82)	—	(82)
Actuarial gains/(losses) (see (iv) above)	184	(1,014)	(830)	—	(830)
Exchange rate movements on foreign plans	(16)	24	8	—	8
Net surplus in the schemes at 31 December	12,281	(11,675)	606	—	606
2011					
Net deficits in the schemes at 1 January	11,416	(11,419)	(3)	(1,445)	(1,448)
Employer contributions	452	—	452	(66)	386
Employee contributions	12	(12)	—	(9)	(9)
Benefits paid	(356)	356	—	15	15
Current and past service cost (see (iv) above)	—	(58)	(58)	—	(58)
Credit/(charge) to finance costs (see (iv) above)	465	(565)	(100)	(13)	(113)
Actuarial gains/(losses) (see (iv) above)	1,347	(356)	991	16	1,007
Disposals	(23)	30	7	—	7
Deconsolidation of Delta Lloyd	(1,589)	1,558	(31)	1,582	1,551
Exchange rate movements on foreign plans	67	(61)	6	(80)	(74)
Net surplus in the schemes at 31 December	11,791	(10,527)	1,264	—	1,264

2 Relates to non-transferrable insurance policies treated as other obligations to staff pension schemes in the Delta Lloyd subsidiary, which was deconsolidated in 2011.

The fall in the pension schemes' net surplus during 2012 is mainly attributable to losses arising from changes in actuarial assumptions, which primarily reflect the impact of lower discount rates for liabilities.

48 – Borrowings

Our borrowings are either core structural borrowings or operational borrowings. This note shows the carrying values and contractual maturity amounts of each type, and explains their main features and movements during the year.

(a) Analysis of total borrowings

Total borrowings comprise:

	2012 £m	2011 £m
Core structural borrowings, at amortised cost	5,139	5,255
Operational borrowings, at amortised cost	1,868	1,889
Operational borrowings, at fair value	1,332	1,306
	3,200	3,195
	8,339	8,450
Less: Amounts classified as held for sale	(145)	—
	8,194	8,450

(b) Core structural borrowings

(i) The carrying amounts of these borrowings are:

	2012				2011			
	Upper Tier 2 £m	Lower Tier 2 £m	Senior £m	Total £m	Upper Tier 2 £m	Lower Tier 2 £m	Senior £m	Total £m
Subordinated debt								
6.125% £700 million subordinated notes 2036	—	691	—	691	—	690	—	690
5.250% €650 million subordinated notes 2023	—	527	—	527	—	510	—	510
5.700% €500 million undated subordinated notes	404	—	—	404	416	—	—	416
6.125% £800 million undated subordinated notes	792	—	—	792	792	—	—	792
Floating rate US\$300 million subordinated notes 2017	—	—	—	—	—	193	—	193
6.875% £400 million subordinated notes 2058	—	395	—	395	—	398	—	398
6.875% £200 million subordinated notes 2058	—	199	—	199	—	199	—	199
6.875% €500 million subordinated notes 2018	—	404	—	404	—	416	—	416
10.6726% £200 million subordinated notes 2019	—	200	—	200	—	200	—	200
10.464% €50m subordinated notes 2019	—	40	—	40	—	42	—	42
8.25% \$400 million subordinated notes 2041	—	239	—	239	—	248	—	248
6.625% £450 million subordinated notes 2041	—	446	—	446	—	446	—	446
	1,196	3,141	—	4,337	1,208	3,342	—	4,550
Debenture Loans								
9.5% guaranteed bonds 2016	—	—	199	199	—	—	199	199
	—	—	199	199	—	—	199	199
Commercial paper	—	—	603	603	—	—	506	506
Total	1,196	3,141	802	5,139	1,208	3,342	705	5,255

The classifications between Upper Tier 2, Lower Tier 2 and Senior debt shown above are as defined by the FSA in GENPRU Annex 1 'Capital Resources'.

Subordinated debt is stated net of notes held by Group companies which were £nil (2011: £32 million). All the above borrowings are stated at amortised cost.

As described in note 57, the Group has designated a portion of its euro and US dollar denominated debt as a hedge of the net investment in its European and American subsidiaries. The carrying value of the debt, included in the table above, at 31 December 2012 was £1,741 million (2011: £1,815 million).

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

	2012			2011		
	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m
Within one year	603	307	910	506	312	818
1 to 5 years	200	1,197	1,397	200	1,237	1,437
5 to 10 years	241	1,342	1,583	435	1,395	1,830
10 to 15 years	527	1,192	1,719	510	1,236	1,746
Over 15 years	3,608	2,610	6,218	3,643	2,859	6,502
Total contractual undiscounted cash flows	5,179	6,648	11,827	5,294	7,039	12,333

Borrowings are considered current if the contractual maturity dates are within a year. Where subordinated debt is undated or loan notes are perpetual, the interest payments have not been included beyond 15 years. Annual interest payments for these borrowings are £72 million (2011: £73 million).

48 – Borrowings continued

Contractual undiscounted interest payments are calculated based on underlying fixed interest rates or prevailing market floating rates as applicable. Year-end exchange rates have been used for interest projections on loans in foreign currencies.

(c) Operational borrowings

(i) The carrying amounts of these borrowings are:

	2012 £m	2011 £m
Amounts owed to financial institutions		
Loans	1,868	1,889
Securitised mortgage loan notes		
UK lifetime mortgage business	1,332	1,306
Total	3,200	3,195

All the above borrowings are stated at amortised cost, except for the loan notes issued in connection with the UK lifetime mortgage business of £1,332 million (2011: £1,306 million). These loan notes are carried at fair value, their values are modelled on risk-adjusted cash flows for defaults discounted at a risk-free rate plus a market-determined liquidity premium, and are therefore classified as 'Level 2' in the fair value hierarchy. These have been designated at fair value through profit and loss in order to present the relevant mortgages, borrowings and derivative financial instruments at fair value, since they are managed as a portfolio on a fair value basis. This presentation provides more relevant information and eliminates any accounting mismatch.

The securitised mortgage loan notes are at various fixed, floating and index-linked rates. Further details about these notes are given in note 24.

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

	2012			2011		
	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m
Within one year	725	64	789	677	39	716
1 to 5 years	951	259	1,210	995	124	1,119
5 to 10 years	399	364	763	247	82	329
10 to 15 years	611	284	895	510	64	574
Over 15 years	940	291	1,231	1,008	439	1,447
Total contractual undiscounted cash flows	3,626	1,262	4,888	3,437	748	4,185

Contractual undiscounted interest payments are calculated based on underlying fixed interest rates or prevailing market floating rates as applicable. Year-end exchange rates have been used for interest projections on loans in foreign currencies.

(d) Description and features

(i) Subordinated debt

A description of each of the subordinated notes is set out in the table below:

Notional amount	Issue date	Redemption date	Callable at par at option of the Company from	In the event the Company does not call the notes, the coupon will reset at each applicable reset date to
£700 million	14 Nov 2001	14 Nov 2036	16 Nov 2026	5 year Benchmark Gilt + 2.85%
€650 million	29 Sep 2003	02 Oct 2023	02 Oct 2013	3 month Euribor + 2.08%
€500 million	29 Sep 2003	Undated	29 Sep 2015	3 month Euribor + 2.35%
£800 million	29 Sep 2003	Undated	29 Sep 2022	5 year Benchmark Gilt + 2.40%
£400 million	20 May 2008	20 May 2058	20 May 2038	3 month LIBOR + 3.26%
£200 million	8 Aug 2008	20 May 2058	20 May 2038	3 month LIBOR + 3.26%
€500 million	20 May 2008	22 May 2038	22 May 2018	3 month Euribor + 3.35%
£200 million	1 Apr 2009	1 Apr 2019	1 Apr 2014	3 month LIBOR + 8.10%
€50 million	30 Apr 2009	30 Apr 2019	30 Apr 2014	3 month Euribor + 8.25%
£450 million	26 May 2011	3 June 2041	3 June 2021	6 Month LIBOR + 4.136%
\$400 million	22 November 2011	1 December 2041	1 December 2016	8.25%(fixed)

Subordinated notes issued by the Company rank below its senior obligations and ahead of its preference shares and ordinary share capital. The dated subordinated notes rank ahead of the undated subordinated notes. The fair value of these notes at 31 December 2012 was £4,435 million (2011: £3,814 million), calculated with reference to quoted prices.

(ii) Debenture loans

The 9.5% guaranteed bonds were issued by the Company at a discount of £1.1 million. This discount and the issue expenses are being amortised over the full term of the bonds. Although these bonds were issued in sterling, the loans have effectively been converted into euro liabilities through the use of financial instruments in a subsidiary.

All these borrowings are at fixed rates and their fair value at 31 December 2012 was £246 million (2011: £246 million), calculated with reference to quoted prices.

(iii) Commercial paper

The commercial paper consists of £603 million issued by the Company (2011: £506 million) and is considered core structural funding.

All commercial paper is repayable within one year and is issued in a number of different currencies, primarily sterling, euros and US dollars. Its fair value is considered to be the same as its carrying value.

48 – Borrowings continued**(iv) Loans**

Loans comprise:

	2012 £m	2011 £m
Non-recourse		
Loans to property partnerships (see (a) below)	1,004	1,128
Loans to Irish investment funds (see (b) below)	20	33
UK Life reinsurance (see (c) below)	257	254
Other non-recourse loans (d)	336	224
	1,617	1,639
Other loans (see (e) below)	251	250
	1,868	1,889

(a) As explained in accounting policy D, the UK long-term business policyholder funds have invested in a number of property limited partnerships (PLPs). The PLPs have raised external debt, secured on their respective property portfolios, and the lenders are only entitled to obtain payment of both interest and principal to the extent there are sufficient resources in the respective PLPs. The lenders have no recourse whatsoever to the policyholder or shareholders' funds of any companies in the Group. Loans of £1,004 million (2011: £1,128 million) included in the table relate to those PLPs which have been consolidated as subsidiaries.

(b) Certain Irish policyholder investment funds and unit trusts, which have been fully consolidated in accordance with accounting policy D, have raised borrowings with external credit institutions. The borrowings are secured on the funds, with the only recourse on default being the underlying investments in these funds and unit trusts. The lenders have no recourse whatsoever to the shareholders' funds of any companies in the Aviva Group. These loans run for a period of five years, with interest rates fixed monthly and based on a fixed margin above the euro inter-bank rate.

(c) The UK long-term business entered into a financial reinsurance agreement with Swiss Re in 2008, under which up-front payments are received from Swiss Re in return for 90% of future surpluses arising. The loan will be repaid as profits emerge on the business. The UK long-term business entered into an additional financial reinsurance agreement with BNP Paribas in 2012 in return for 100% of future surpluses arising. The loan will be repaid as profits emerge on the business.

(d) Other non-recourse loans include external debt raised by special purpose vehicles in the UK long-term business. The lenders have no recourse whatsoever to the shareholders' funds of any companies in the Group. It also includes an operational loan from Delta Lloyd to the UK Life Belgian branch.

(e) Other loans include external debt raised by overseas long-term businesses to fund operations, which includes £145 million (2011: £158 million) of external debt held by the Group's US business.

(v) Securitised mortgage loan notes

Loan notes have been issued by special purpose securitisation companies in the UK. Details are given in note 24.

(e) Movements during the year

Movements in borrowings during the year were:

	2012			2011		
	Core Structural £m	Operational £m	Total £m	Core Structural £m	Operational £m	Total £m
New borrowings drawn down, including commercial paper, net of expenses	2,200	452	2,652	3,853	1,042	4,895
Repayment of borrowings, including commercial paper	(2,295)	(347)	(2,642)	(3,848)	(1,283)	(5,131)
Net cash outflow/(inflow)	(95)	105	10	5	(241)	(236)
Foreign exchange rate movements	(54)	(130)	(184)	9	193	202
Borrowings acquired for non-cash consideration	—	—	—	—	34	34
Fair value movements	—	43	43	—	8	8
Amortisation of discounts and other non-cash items	1	(13)	(12)	3	—	3
Deconsolidation of Delta Lloyd	—	—	—	(816)	(5,683)	(6,499)
Movements in debt held by Group companies ¹	32	—	32	(12)	1	(11)
Movements in the year	(116)	5	(111)	(811)	(5,688)	(6,499)
Balance at 1 January	5,255	3,195	8,450	6,066	8,883	14,949
Balance at 31 December	5,139	3,200	8,339	5,255	3,195	8,450

¹ Certain subsidiary companies have purchased issued subordinated notes and securitised loan notes as part of their investment portfolios. In the consolidated statement of financial position, borrowings are shown net of these holdings but movements in such holdings over the year are reflected in the tables above.

All movements in fair value in 2011 and 2012 on securitised mortgage loan notes designated as fair value through profit or loss were attributable to changes in market conditions.

(f) Undrawn borrowings

The Group and Company have the following undrawn committed central borrowing facilities available to them, of which £750 million (2011: £750 million) is used to support the commercial paper programme:

	2012 £m	2011 £m
Expiring within one year	420	955
Expiring beyond one year	1,725	1,160
	2,145	2,115

49 – Payables and other financial liabilities

This note analyses our payables and other financial liabilities at the end of the year.

	2012 £m	2011 £m
Payables arising out of direct insurance	1,234	1,098
Payables arising out of reinsurance operations	426	360
Deposits and advances received from reinsurers	318	346
Bank overdrafts	566	668
Derivative liabilities	1,761	1,850
Amounts due to brokers for investment purchases	135	60
Obligations for repayment of cash collateral received (notes 25d(i) & 57c)	4,460	5,229
Other financial liabilities	1,649	1,628
Total	10,549	11,239
Less: Amounts classified as held for sale	(1,108)	(9)
	9,441	11,230
Expected to be settled within one year	8,613	10,253
Expected to be settled in more than one year	828	977
	9,441	11,230

Bank overdrafts arise substantially from un-presented cheques and amount to £194 million (2011: £211 million) in long-term business operations and £372 million (2011: £457 million) in general business and other operations.

All payables and other financial liabilities are carried at cost, which approximates to fair value, except for derivative liabilities, which are carried at their fair values.

50 – Other liabilities

This note analyses our other liabilities at the end of the year.

	2012 £m	2011 £m
Deferred income	319	359
Reinsurers' share of deferred acquisition costs	11	12
Accruals	1,138	1,336
Other liabilities	1,110	1,128
Total	2,578	2,835
Less: Amounts classified as held for sale	(735)	(7)
	1,843	2,828
Expected to be settled within one year	1,458	2,195
Expected to be settled in more than one year	385	633
	1,843	2,828

51 – Contingent liabilities and other risk factors

This note sets out the main areas of uncertainty over the calculation of our liabilities.

(a) Uncertainty over claims provisions

Note 39 gives details of the estimation techniques used by the Group to determine the general business outstanding claims provisions and of the methodology and assumptions used in determining the long-term business provisions. These approaches are designed to allow for the appropriate cost of policy-related liabilities, with a degree of prudence, to give a result within the normal range of outcomes. To the extent that the ultimate cost falls outside this range, for example where experience is worse than that assumed, or future general business claims inflation differs from that expected, there is uncertainty in respect of these liabilities.

(b) Asbestos, pollution and social environmental hazards

In the course of conducting insurance business, various companies within the Group receive general insurance liability claims, and become involved in actual or threatened related litigation arising there from, including claims in respect of pollution and other environmental hazards. Amongst these are claims in respect of asbestos production and handling in various jurisdictions, including Europe, Canada and Australia. Given the significant delays that are experienced in the notification of these claims, the potential number of incidents which they cover and the uncertainties associated with establishing liability and the availability of reinsurance, the ultimate cost cannot be determined with certainty. However, on the basis of current information having regard to the level of provisions made for general insurance claims, the directors consider that any additional costs arising are not likely to have a material impact on the financial position of the Group.

51 – Contingent liabilities and other risk factors continued

(c) Guarantees on long-term savings products

As a normal part of their operating activities, various Group companies have given guarantees and options, including interest rate guarantees, in respect of certain long-term insurance and fund management products. Note 41 gives details of these guarantees and options. In providing these guarantees and options, the Group's capital position is sensitive to fluctuations in financial variables including foreign currency exchange rates, interest rates, property values and equity prices. Interest rate guaranteed returns, such as those available on GAOs, are sensitive to interest rates falling below the guaranteed level. Other guarantees, such as maturity value guarantees and guarantees in relation to minimum rates of return, are sensitive to fluctuations in the investment return below the level assumed when the guarantee was made. The directors continue to believe that the existing provisions for such guarantees and options are sufficient.

(d) Regulatory compliance

The Group's insurance and investment business is subject to local regulation in each of the countries in which it operates. The FSA regulates the Group's UK business (from 1 April 2013, the FSA will split into two new regulatory bodies: the Prudential Regulation Authority (PRA), which will be a subsidiary of the Bank of England, and the Financial Conduct Authority (FCA)) and will monitor the financial resources and organisation of the Group as a whole. The FSA has broad powers including the authority to grant, vary the terms of, or cancel a regulated firm's authorisation; to investigate marketing and sales practices; and to require the maintenance of adequate financial resources. The Group's regulators outside the UK typically have similar powers, but in some cases they also operate a system of 'prior product approval'.

The Group's regulated businesses have compliance resources to respond to regulatory enquiries in a constructive way, and take corrective action when warranted. However, all regulated financial services companies face the risk that their regulator could find that they have failed to comply with applicable regulations or have not undertaken corrective action as required.

The impact of any such finding (whether in the UK or overseas) could have a negative impact on the Group's reported results or on its relations with current and potential customers. Regulatory action against a member of the Group could result in adverse publicity for, or negative perceptions regarding, the Group, or could have a material adverse effect on the business of the Group, its results of operations and/or financial condition and divert management's attention from the day-to-day management of the business.

(e) Payment protection insurance (PPI) mis-selling

In September 2009, the FSA launched an investigation into sales practices for payment protection insurance (PPI). On 10 August 2010, the FSA announced that mis-selling of PPI policies had been widespread and that consumers who could prove mis-selling would be entitled to financial redress from distributors of the policies. The directors do not consider that the Group is liable for mis-selling in its role as underwriter and so no provision is currently necessary.

(f) Structured settlements

The Company has purchased annuities from licensed Canadian life insurers to provide for fixed and recurring payments to claimants. As a result of these arrangements, the Company is exposed to credit risk to the extent that any of the life insurers fail to fulfil their obligations. The Company's maximum exposure to credit risk for these types of arrangements is approximately \$1,145 million as at 31 December 2012 (2011: \$1,085 million, 2010: \$1,063 million). Credit risk is managed by acquiring annuities from a diverse portfolio of life insurers with proven financial stability. This risk is reduced to the extent of coverage provided by Assuris, the life insurance industry compensation plan. As at 31 December 2012, no information has come to the Company's attention that would suggest any weakness or failure in life insurers from which it has purchased annuities and consequently no provision for credit risk is required.

(g) Other

In the course of conducting insurance and investment business, various Group companies receive liability claims, and become involved in actual or threatened related litigation. In the opinion of the directors, adequate provisions have been established for such claims and no material loss will arise in this respect.

At 31 December 2012, the Company and several of its subsidiaries have guaranteed the overdrafts and borrowings of certain other Group companies. At 31 December 2012, the Group and Company had no exposure (2011: *£nil and £334 million respectively*).

In addition, in line with standard business practice, various Group companies have given guarantees, indemnities and warranties in connection with disposals in recent years of subsidiaries and associates to parties outside the Aviva Group. In the opinion of the directors, no material loss will arise in respect of these guarantees, indemnities and warranties.

There are a number of charges registered over the assets of Group companies in favour of other Group companies or third parties. In addition, certain of the Company's assets are charged in favour of certain of its subsidiaries as security for intra Group loans.

The Group's insurance subsidiaries pay contributions to levy schemes in several countries in which we operate. Given the economic environment, there is a heightened risk that the levy contributions will need to be increased to protect policyholders if an insurance company falls into financial difficulties. The directors continue to monitor the situation but are not aware of any need to increase provisions at the statement of financial position date.

52 – Commitments

This note gives details of our commitments to capital expenditure and under operating leases.

(a) Capital commitments

Contractual commitments for acquisitions or capital expenditures of investment property and property and equipment, which have not been recognised in the financial statements, are as follows:

	2012 £m	2011 £m
Investment property	6	23
Property and equipment	36	36
	42	59

52 – Commitments continued

Contractual obligations for future repairs and maintenance on investment properties are £nil (2011: £nil).

The Group has capital commitments to its joint ventures of £157 million (2011: £258 million) and to other investment vehicles of £nil (2011: £nil).

(b) Operating lease commitments

(i) Future contractual aggregate minimum lease rentals receivable under non-cancellable operating leases are as follows:

	2012 £m	2011 £m
Within 1 year	269	313
Later than 1 year and not later than 5 years	832	562
Later than 5 years	1,570	1,738
	2,671	2,613

(ii) Future contractual aggregate minimum lease payments under non-cancellable operating leases are as follows:

	2012 £m	2011 £m
Within 1 year	136	120
Later than 1 year and not later than 5 years	421	400
Later than 5 years	587	667
	1,144	1,187
Total future minimum sub-lease payments expected to be received under non-cancellable sub-leases	53	56

53 – Group capital structure

The Group maintains an efficient capital structure from a combination of equity shareholders' funds, preference capital, subordinated debt and borrowings, consistent with our overall risk profile and the regulatory and market requirements of our business. This note shows where this capital is employed.

Accounting basis and capital employed by segment

The table below shows how our capital, on an MCEV³ basis, is deployed by segment and how that capital is funded.

	2012 £m	2011 £m
Long-term savings	16,337	14,148
General insurance and health	6,089	5,875
Fund management	225	184
Other business	(1,059)	(1,102)
Corporate ¹	(588)	508
Delta Lloyd	—	776
United States	365	361
Total capital employed	21,369	20,750
Financed by		
Equity shareholders' funds	12,434	12,829
Non-controlling interests	2,214	1,476
Direct capital instruments and fixed rate tier 1 notes	1,382	990
Preference shares	200	200
Subordinated debt	4,337	4,550
External debt	802	705
Total capital employed	21,369	20,750

¹ 'Corporate' includes centrally held tangible net assets, the staff pension scheme surplus and also reflects internal lending arrangements. These internal lending arrangements, which net out on consolidation, arise in relation to the following:
– Aviva Insurance Limited (AI) acts as both a UK general insurer and as the primary holding company for our foreign subsidiaries. Internal capital management mechanisms in place allocate a portion of the total capital of the company to the UK general insurance operations, giving rise to notional lending between the general insurance and holding company activities. These mechanisms also allow for some of the assets of the general insurance business to be made available for use across the Group.

² – Subsequent to the year end, the Group has taken action to improve its access to dividends from the Group's insurance and asset management business by undertaking a corporate restructure. This will see the Group's interest in the majority of its overseas businesses move to Aviva Group Holdings Limited from Aviva Insurance Limited.

– Certain subsidiaries, subject to continuing to satisfy stand-alone capital and liquidity requirements, loan funds to corporate and holding entities. These loans satisfy arm's length criteria and all interest payments are made when due.

³ – In preparing the MCEV information, the directors have done so in accordance with the MCEV Principles with the exception of stating held for sale operations at their expected fair value, as represented by expected sale proceeds, less cost to sell.

Total capital employed is financed by a combination of equity shareholders' funds, preference capital, subordinated debt and borrowings.

At the end of 2012 we had £21.4 billion (2011: £20.8 billion) of total capital employed in our trading operations measured on an MCEV³ basis.

In May 2012 we issued US\$650 million of Fixed Rate Tier 1 Notes. The Notes are perpetual and may be called from November 2017. The Notes qualify as Innovative Tier 1 capital under current regulatory rules and are expected to be treated as Fixed Rate Tier 1 capital under Solvency II transitional rules. The transaction had a positive impact on Group IGD solvency and Economic Capital measures.

In June 2012 US\$300 million of Lower Tier 2 floating rate notes were redeemed at first call.

Financial leverage, the ratio of external senior and subordinated debt to MCEV³ capital and reserves, was 35.1% (2011: 36.7%). Fixed charge cover, which measures the extent to which external interest costs, including subordinated debt interest and preference dividends, are covered by MCEV³ operating profit was 5.1 times (2011: 8.9 times). The impact of the agreement to sell Aviva USA has meant that financial leverage under IFRS is higher at 52.6% (FY11: 37.1%).

53 – Group capital structure continued

At the end of 2012 the market value of our external debt, subordinated debt, preference shares (including both Aviva plc preference shares of £200 million and General Accident plc preference shares, within non-controlling interests, of £250 million), and direct capital instruments and fixed rate tier 1 notes was £7,260 million (2011: £5,782 million), with a weighted average cost, post tax, of 4.4% (2011: 6.6%). The Group Weighted Average Cost of Capital (WACC) is 6.3% (2011: 7.1%) and has been calculated by reference to the cost of equity and the cost of debt at the relevant date. The cost of equity at 2012 was 7.5% (2011: 7.4%) based on a risk free rate of 1.9% (2011: 2.0%), an equity risk premium of 4.0% (2011: 4.0%) and a market beta of 1.4 (2011: 1.3).

54 – Statement of cash flows

This note gives further detail behind the figures in the statement of cash flows.

(a) The reconciliation of profit before tax to the net cash inflow from operating activities is:

	2012 £m	2011 £m
Profit before tax from continuing operations	246	373
Adjustments for:		
Share of loss of joint ventures and associates	277	123
Dividends received from joint ventures and associates	48	71
(Profit)/loss on sale of:		
Investment property	(7)	(8)
Property and equipment	—	(4)
Subsidiaries, joint ventures and associates	164	(565)
Investments	(1,167)	(1,340)
	(1,010)	(1,917)
Fair value (gains)/losses on:		
Investment property	492	(148)
Investments	(12,402)	5,488
Borrowings	43	1
	(11,867)	5,341
Depreciation of property and equipment	42	54
Equity compensation plans, equity settled expense	42	48
Impairment and expensing of:		
Goodwill on subsidiaries	109	160
Financial Investments, loans and other assets	46	95
Acquired value of in-force business and intangibles	122	49
Non-financial assets	—	1
	277	305
Amortisation of:		
Premium or discount on debt securities	105	82
Premium or discount on borrowings	(12)	3
Premium or discount on non-participating investment contracts	20	45
Financial instruments	64	7
Acquired value of in-force business and intangibles	121	137
	298	274
Change in unallocated divisible surplus	6,316	(2,721)
Interest expense on borrowings	653	689
Net finance charge on pension schemes	82	87
Foreign currency exchange (gains)/losses	(128)	35
Changes in working capital		
(Increase)/decrease in reinsurance assets	(416)	(611)
Decrease in deferred acquisition costs	216	45
Increase in insurance liabilities and investment contracts	4,325	550
Increase in other assets and liabilities	1,742	1,123
	5,867	1,107
Net purchases of operating assets		
Purchases of investment property	(839)	(1,211)
Proceeds on sale of investment property	1,141	717
Net purchases/(sales) of financial investments	1,231	(3,264)
	1,533	(3,758)
Cash generated from operating activities – continuing operations	2,676	111
Cash generated from operating activities – discontinued operations	46	27
Total cash generated from operating activities	2,722	138

Operating cash flows reflect the movement in both policyholder and shareholder controlled cash and cash equivalent balances. Around two thirds of the Group's balances relate to unit-linked or participating policyholder funds. As such, the asset mix and the level of cash held by these funds are determined from a policyholder perspective and can move significantly from one year to another. Shareholder cash at 31 December 2012 is at £9.0 billion (2011: £8.6 billion).

Purchases and sales of operating assets, including financial investments, are included within operating cash flows as the purchases are funded from cash flows associated with the origination of insurance and investment contracts, net of payments of related benefits and claims. During the year, the net operating cash inflow reflects a number of factors, including changes in the investment strategy of funds to hold a lower weighting of cash and higher levels of financial investments, the level of premium income and the timing of receipts of premiums and the payment of creditors, claims and surrenders. It also includes changes in the size and value of consolidated cash investment funds and changes in the Group participation in these funds.

54 – Statement of cash flows continued**(b) Cash flows in respect of, and additions to, the acquisition of subsidiaries, joint ventures and associates comprised:**

	2012 £m	2011 £m
Cash consideration for subsidiaries, joint ventures and associates acquired and additions	136	114
Less: Cash and cash equivalents acquired with subsidiaries	(7)	—
Cash flows on acquisitions and additions – continuing operations	129	114
Cash flows on acquisitions and additions – discontinued operations	—	—
Cash flows on acquisitions and additions	129	114

(c) Cash flows in respect of the disposal of subsidiaries, joint ventures and associates comprised:

	2012 £m	2011 £m
Cash proceeds from disposal of subsidiaries, joint ventures and associates	442	988
Less: Net cash and cash equivalents divested with subsidiaries	(21)	(111)
Cash flows on disposals – continuing operations	421	877
Cash flows on disposals – discontinued operations	—	(502)
Cash flows on disposals	421	375

The above figures form part of cash flows from investing activities.

(d) Cash and cash equivalents in the statement of cash flows at 31 December comprised:

	2012 £m	2011 £m
Cash at bank and in hand	13,020	8,854
Cash equivalents	10,794	14,215
	23,814	23,069
Bank overdrafts	(566)	(668)
	23,248	22,401

Cash and cash equivalents reconciles to the statement of financial position as follows:

	2012 £m	2011 £m
Cash and cash equivalents (excluding bank overdrafts)	23,814	23,069
Less: Assets classified as held for sale	(917)	(26)
	22,897	23,043

55 – Capital statement

This statement sets out the financial strength of our Group entities and provides an analysis of the disposition and constraints over the availability of capital to meet risks and regulatory requirements. The capital statement also provides a reconciliation of shareholders' funds to regulatory capital.

The analysis below sets out the Group's available capital resources, which includes available capital resources of subsidiaries classified as held for sale in the Group IFRS statement of financial position still included in the Group's available capital resources at 31 December 2012.

Available capital resources

	Old with-profit sub-fund £m	New with-profit sub-fund £m	With-profit sub-fund ⁵ £m	Total UK life with-profit funds £m	Other UK life operations £m	Total UK life operations £m	Overseas life operations £m	Total life operations £m	Other operations ⁶ £m	2012 Total £m	Restated 2011 Total £m
Total shareholders' funds	3	(310)	31	(276)	5,170	4,894	7,449	12,343	(983)	11,360	15,363
Other sources of capital ¹	—	—	—	—	200	200	43	243	4,137	4,380	4,824
Unallocated divisible surplus ²	263	—	1,693	1,956	18	1,974	5,012	6,986	—	6,986	650
Adjustments onto a regulatory basis:											
Shareholders' share of accrued bonus	(23)	(95)	(186)	(304)	—	(304)	—	(304)	—	(304)	(351)
Goodwill and other intangibles ³	—	—	—	—	(136)	(136)	(1,759)	(1,895)	(1,515)	(3,410)	(4,923)
Regulatory valuation and admissibility restrictions ⁴	48	1,312	298	1,658	(2,564)	(906)	1,615	709	(686)	23	(3,279)
Total available capital resources	291	907	1,836	3,034	2,688	5,722	12,360	18,082	953	19,035	12,284
Analysis of liabilities:											
Participating insurance liabilities ⁷	1,909	14,078	11,228	27,215	8	27,223	22,250	49,473	—	49,473	52,872
Unit-linked liabilities	—	—	—	—	3,693	3,693	6,243	9,936	—	9,936	10,168
Other non-participating life insurance	359	2,758	483	3,600	33,889	37,489	35,634	73,123	—	73,123	69,442
Amounts classified as held for sale	—	—	—	—	—	—	(34,446)	(34,446)	—	(34,446)	(344)
Total insurance liabilities	2,268	16,836	11,711	30,815	37,590	68,405	29,681	98,086	—	98,086	132,138
Participating investment liabilities ⁷	651	3,097	5,967	9,715	2,453	12,168	54,681	66,849	—	66,849	67,707
Non-participating investment liabilities	(3)	(24)	—	(27)	33,851	33,824	13,875	47,699	—	47,699	45,659
Amounts classified as held for sale	—	—	—	—	—	—	(4,054)	(4,054)	—	(4,054)	—
Total investment liabilities	648	3,073	5,967	9,688	36,304	45,992	64,502	110,494	—	110,494	113,366
Total liabilities	2,916	19,909	17,678	40,503	73,894	114,397	94,183	208,580	—	208,580	245,504

1 Other sources of capital include Subordinated debt of £4,337 million issued by Aviva and £43 million of other qualifying capital issued by Italian and Spanish subsidiary and associate undertakings.

2 Unallocated divisible surplus for overseas life operations is included gross of minority interest and amounts disclosed include balances classified as held for sale. 2012 includes a negative balance of £2 million in Italy (2011: £1,449 million negative).

3 Goodwill and other intangibles includes goodwill of £132 million in joint ventures and associates including amounts classified as held for sale.

4 Includes an adjustment for minorities (except for other sources of capital that are reflected net of minority interest).

5 Includes the Provident Mutual with-profit fund.

6 Other operations include general insurance and fund management business.

7 Following review of the classification of contracts issued by the Group's Italian business, there has been a reallocation from participating insurance liabilities at 31 December 2011 to participating investment contract liabilities of £2,722 million.

Analysis of movements in capital of long-term businesses

For the year ended 31 December 2012

	Old with-profit sub-fund £m	New with-profit sub-fund £m	With-profit sub-fund £m	Total UK life with-profit funds £m	Other UK life operations £m	Total UK life operations £m	Overseas life operations £m	Total life operations £m
Available capital resources at 1 January	240	1,159	1,629	3,028	2,779	5,807	3,745	9,552
Effect of new business	—	(194)	(12)	(206)	107	(99)	(398)	(497)
Expected change in available capital resources	18	196	235	449	283	732	1,343	2,075
Variance between actual and expected experience ¹	58	(20)	50	88	(20)	68	7,596	7,664
Effect of operating assumption changes	2	(13)	21	10	26	36	—	36
Effect of economic assumption changes	(19)	(103)	(69)	(191)	—	(191)	79	(112)
Effect of changes in management policy	—	—	(23)	(23)	—	(23)	7	(16)
Effect of changes in regulatory requirements	—	—	—	—	—	—	(10)	(10)
Transfers, acquisitions and disposals	—	—	—	—	—	—	(43)	(43)
Foreign exchange movements	—	—	—	—	—	—	(127)	(127)
Other movements	(8)	(118)	5	(121)	(487)	(608)	168	(440)
Available capital resources at 31 December	291	907	1,836	3,034	2,688	5,722	12,360	18,082

1 The positive variance between actual and expected experience is driven by increases in the market value of assets backing participating funds in continental Europe, and consequential increases in unallocated divisible surplus.

Further analysis of the movement in the liabilities of the long-term business can be found in notes 39 and 40.

The analysis of movements in capital provides an explanation of the movement in available capital of the Group's life business for the year. This analysis is intended to give an understanding of the underlying causes of changes in the available capital of the Group's life business, and provides a distinction between some of the key factors affecting the available capital.

The negative shareholders' funds balance within the UK with-profit funds arises in NWPSF as a result of regulatory valuation and admissibility differences in the reattributed estate which is valued on a realistic regulatory basis compared to the disclosure on an IFRS basis.

NWPSF is fully supported by the reattributed estate of £748 million (this is known as RIEESA) at 31 December 2012 (31 December 2011: £1,113 million) held within NPSF1 (a non-profit fund within UKLAP included within other UK life operations) in the form of a capital support arrangement. This support arrangement will provide capital to NWPSF to ensure that the value of assets of NWPSF are at least equal to the value of liabilities calculated on a realistic regulatory basis, therefore it forms part of the NWPSF available capital resources.

55 – Capital statement continued

The with-profit funds and the RIEESA use internal hedging to limit the impacts of equity market volatility.

In aggregate, the Group has at its disposal total available capital of £19.0 billion (2011: £12.3 billion), representing the aggregation of the solvency capital of all of our businesses.

This capital is available to meet risks and regulatory requirements set by reference to local guidance and EU directives.

After effecting the year-end transfers to shareholders, the UK with-profit funds have available capital of £3.0 billion (2011: £3.0 billion) (including amounts held in RIEESA). Subject to certain conditions, the RIEESA capital can be used to write new non-profit business, but the primary purpose of this capital is to provide support for the UK with-profit business. The capital is comfortably in excess of the required capital margin, and therefore the shareholders are not required to provide further support.

For the remaining life and general insurance operations, the total available capital amounting to £16.0 billion (2011: £9.3 billion) is higher than the minimum requirements established by regulators and, in principle, the excess is available to shareholders. In practice, management will hold higher levels of capital within each business operation to provide appropriate cover for risk.

The total available capital of £19.0 billion is arrived at on the basis of local regulatory guidance, which evaluates assets and liabilities prudently and includes the Group's unallocated divisible surplus of overseas life operations. This is a limitation of the Group Capital Statement which, to be more meaningful, needs to evaluate available capital on an economic basis and compare it with the risk capital required for each individual operation, after allowing for the considerable diversification benefits that exist in our Group.

Within the Aviva Group there exist intra-group arrangements to provide capital to particular business units. Included in these arrangements is a subordinated loan of £200 million from Aviva Life Holdings UK Limited to Aviva Annuity Limited to provide capital to support the writing of new business.

The available capital of the Group's with-profit funds is determined in accordance with the 'Realistic balance sheet' regime prescribed by the FSA's regulations, under which liabilities to policyholders include both declared bonuses and the constructive obligation for future bonuses not yet declared. The available capital resources include an estimate of the value of their respective estates, included as part of the unallocated divisible surplus. The estate represents the surplus in the fund that is in excess of any constructive obligation to policyholders. It represents capital resources of the individual with-profit fund to which it relates and is available to meet regulatory and other solvency requirements of the fund and, in certain circumstances, additional liabilities may arise.

The liabilities included in the balance sheet for the with-profit funds do not include the amount representing the shareholders' portion of future bonuses. However, the shareholders' portion is treated as a deduction from capital that is available to meet regulatory requirements and is therefore shown as a separate adjustment in the capital statement.

In accordance with the FSA's regulatory rules under its realistic capital regime, the Group is required to hold sufficient capital in its UK life with-profit funds to meet the FSA capital requirements, based on the risk capital margin (RCM). The determination of the RCM depends on various actuarial and other assumptions about potential changes in market prices, and the actions management would take in the event of particular adverse changes in market conditions.

	31 December 2012					31 December 2011
	Estimated realistic assets £bn	Estimated realistic liabilities ¹ £bn	Estimated realistic inherited estate ² £bn	Capital support arrangement ³ £bn	Estimated risk capital margin £bn	Estimated excess available capital £bn
NWPSF	17.3	(17.3)	—	0.7	(0.4)	0.3
OWPSF	2.9	(2.6)	0.3	—	(0.1)	0.2
WPSF ⁴	18.3	(16.5)	1.8	—	(0.5)	1.3
Aggregate	38.5	(36.4)	2.1	0.7	(1.0)	1.9

¹ These realistic liabilities include the shareholders' share of future bonuses of £0.3 billion (31 December 2011: £0.3 billion). Realistic liabilities adjusted to eliminate the shareholders' share of future bonuses are £36.0 billion (31 December 2011: £38.8 billion). These realistic liabilities make provision for guarantees, options and promises on a market consistent stochastic basis. The value of the provision included within realistic liabilities is £1.8 billion, £0.3 billion and £3.5 billion for NWPSF, OWPSF and WPSF respectively (31 December 2011: £1.9 billion, £0.3 billion and £3.1 billion for NWPSF, OWPSF and WPSF respectively).

² Estimated realistic inherited estate at 31 December 2011 was £nil, £0.3 billion and £1.6 billion for NWPSF, OWPSF and WPSF respectively.

³ This represents the reattributed estate of £0.7 billion at 31 December 2012 (31 December 2011: £1.1 billion) held within NPSF1 (a non-profit fund within UKLAP included within other UK life operations).

⁴ The WPSF fund includes the Provident Mutual (PM) fund, which has realistic assets and liabilities of £1.7 billion and therefore does not impact the realistic inherited estate.

Under the FSA regulatory regime, UK life with-profits business is required to hold capital equivalent to the greater of their regulatory requirement based on EU directives (regulatory peak) and the FSA realistic bases (realistic peak) described above.

For UK non-participating business, the relevant capital requirement is the minimum solvency requirement determined in accordance with FSA regulations. The available capital reflects the excess of regulatory basis assets over liabilities before deduction of capital resources requirement.

For UK general insurance businesses, the relevant capital requirement is the minimum solvency requirement determined in accordance with the FSA requirements.

For overseas businesses in the European Economic Area (EEA), US, Canada, Hong Kong and Singapore, the available capital and the minimum requirement are calculated under the locally applicable regulatory regimes. The businesses outside these territories are subject to the FSA rules for the purposes of calculation of available capital and capital resource requirement.

For fund management and other businesses, the relevant capital requirement is the minimum solvency requirement determined in accordance with the local regulator's requirements for the specific class of business.

55 – Capital statement continued

The available capital resources in each regulated entity are generally subject to restrictions as to their availability to meet requirements that may arise elsewhere in the Group. The principal restrictions are:

- **(i) UK with-profits fund – (NWPSF, OWPSF and WPSF)** – any available surplus held in each fund can be used to meet the requirements of the fund itself, be distributed to policyholders and shareholders or in the case of NWPSF and OWPSF, transferred via the capital support arrangement explained above (for OWPSF only to the extent support has been provided in the past). In most cases, with-profit policyholders are entitled to at least 90% of the distributed profits while the shareholders receive the balance. The latter distribution would be subject to a tax charge, which is met by the fund.
- **(ii) UK non-participating funds** – any available surplus held in these is attributable to shareholders. Capital in the non-profit funds may be made available to meet requirements elsewhere in the Group subject to meeting the regulatory requirements of the fund. Any transfer of the surplus may give rise to a tax charge subject to availability of tax relief elsewhere in the Group.
- **(iii) Overseas life operations** – the capital requirements and corresponding regulatory capital held by overseas businesses are calculated using the locally applicable regulatory regime. The available capital resources in all these businesses are subject to local regulatory restrictions which may constrain management's ability to utilise these in other parts of the Group. In several business units, Group companies and other parties jointly control certain entities; these joint venture operations may constrain management's ability to utilise the capital in other parts of the Group. Any transfer of available capital may give rise to a tax charge subject to availability of tax relief elsewhere in the Group.
- **(iv) General insurance operations** – the capital requirements and corresponding regulatory capital held by overseas businesses are calculated using the locally applicable regulatory regime. The available capital resources in all these businesses are subject to local regulatory restrictions which may constrain management's ability to utilise these in other parts of the Group. Any transfer of available capital may give rise to a tax charge, subject to availability of tax relief elsewhere in the Group.

56 – Risk management

This note sets out the major risks our businesses and its shareholders face and describes the Group's approach to managing these. It also gives sensitivity analyses around the major economic and non-economic assumptions that can cause volatility in the Group's earnings and capital position.

(a) Risk management framework

The risk management framework (RMF) in Aviva forms an integral part of the management and Board processes and decision-making framework across the Group. The key elements of our risk management framework comprise risk appetite; risk governance, including risk policies and business standards, risk oversight committees and roles and responsibilities; and the processes we use to identify, measure, manage, monitor and report (IMMMR) risks, including the use of our risk models and stress and scenario testing.

For the purposes of risk identification and measurement, and aligned to Aviva's risk policies, risks are usually grouped by risk type: credit, market, liquidity, life insurance, general insurance, asset management and operational risk. Risks falling within these types may affect a number of metrics including those relating to balance sheet strength, liquidity and profit. They may also affect the performance of the products we deliver to our customers and the service to our customers and distributors, which can be categorised as risks to our brand and reputation.

To promote a consistent and rigorous approach to risk management across all businesses we have a set of risk policies and business standards which set out the risk strategy, appetite, framework and minimum requirements for the Group's worldwide operations. On a semi-annual basis the business chief executive officers and chief risk officers sign-off compliance with these policies and standards, providing assurance to the relevant oversight committees that there is a consistent framework for managing our business and the associated risks.

A regular top-town key risk identification and assessment process is carried out by the risk function. This includes the consideration of emerging risks and is supported by deeper thematic reviews. This process is replicated at the business unit level. The risk assessment processes are used to generate risk reports which are shared with the relevant risk committees.

Risk models are an important tool in our measurement of risks and are used to support the monitoring and reporting of the risk profile and in the consideration of the risk management actions available. We carry out a range of stress (where one risk factor, such as equity returns, is assumed to vary) and scenario (where combinations of risk factors are assumed to vary) tests to evaluate their impact on the business and the management actions available to respond to the conditions envisaged.

Roles and responsibilities for risk management in Aviva are based around the 'three lines of defence model' where ownership for risk is taken at all levels in the Group. Line management in the business is accountable for risk management, including the implementation of the risk management framework and embedding of the risk culture. The risk function is accountable for quantitative and qualitative oversight and challenge of the IMMMR process and for developing the risk management framework. Internal Audit provides an independent assessment of the risk framework and internal control processes.

Board oversight of risk and risk management across the Group is maintained on a regular basis through its Risk Committee. The Board has overall responsibility for determining risk appetite, which is an expression of the risk the business is willing to take. Risk appetites are set relative to capital, liquidity and franchise value at Group and in the business units. Economic capital risk appetites are also set for each risk type. The Group's position against risk appetite is monitored and reported to the Board on a regular basis. The oversight of risk and risk management at the Group level is supported by the Asset Liability Committee (ALCO), which focuses on business and financial risks, and the Operational Risk Reputation Committee (ORRC) which focuses on operational and reputational risks. Similar committee structures with equivalent terms of reference exist in the business units.

56 – Risk management continued

Further information on the types and management of specific risk types is given in sections (b) - (j) below.

The risk management framework of a small number of our joint ventures and strategic equity holdings differs from the Aviva framework outlined in this note. We work with these entities to understand how risks are managed and to align them, where possible, with Aviva's framework.

(b) Credit risk

Credit risk is the risk of financial loss as a result of the default or failure of third parties to meet their payment obligations to Aviva, or variations in market values as a result of changes in expectations related to these risks. Credit risk is an area where we can provide the returns required to satisfy policyholder liabilities and to generate returns for our shareholders. In general we prefer to take credit risk over equity and property risks, due to the better expected risk adjusted return, our credit risk analysis capability and the structural investment advantages conferred to insurers with long-dated, relatively illiquid liabilities.

Our approach to managing credit risk recognises that there is a risk of adverse financial impact resulting from fluctuations in credit quality of third parties including default, rating transition and credit spread movements. Our credit risks arise principally through exposures to debt security investments, structured asset investments, bank deposits, derivative counterparties, mortgage lending and reinsurance counterparties.

The Group manages its credit risk at business unit and Group level. All business units are required to implement credit risk management processes (including limits frameworks), operate specific risk management committees, and ensure detailed reporting and monitoring of their exposures against pre-established risk criteria. At Group level, we manage and monitor all exposures across our business units on a consolidated basis, and operate a Group limit framework that must be adhered to by all.

A detailed breakdown of the Group's current credit exposure by credit quality is shown below.

(i) Financial exposures by credit ratings

Financial assets are graded according to current external credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. Financial assets which fall outside this range are classified as sub-investment grade. The following table provides information regarding the aggregated credit risk exposure of the Group for financial assets with external credit ratings, excluding assets 'held for sale'. 'Not rated' assets capture assets not rated by external ratings agencies.

As at 31 December 2012	AAA	AA	A	BBB	Speculative grade	Not rated	Carrying value including held for sale	Less assets classified as held for sale	Carrying value £m
Debt securities	24.4%	16.9%	23.8%	25.4%	4.2%	5.3%	161,623	(33,617)	128,006
Reinsurance assets	0.4%	63.4%	30.1%	0.7%	0.1%	5.3%	7,567	(883)	6,684
Other investments	0.1%	0.2%	2.3%	2.0%	1.5%	93.9%	30,093	(1,550)	28,543
Loans	5.8%	8.2%	1.2%	0.1%	0.7%	84.0%	27,934	(3,397)	24,537
Total							227,217	(39,447)	187,770

As at 31 December 2011	AAA	AA	A	BBB	Speculative grade	Not rated	Carrying value including held for sale	Less assets classified as held for sale	Carrying value £m
Debt securities	32.3%	13.2%	29.9%	16.3%	2.8%	5.4%	153,345	(93)	153,252
Reinsurance assets	0.0%	70.1%	23.2%	0.0%	0.4%	6.3%	7,113	(1)	7,112
Other investments	0.2%	0.8%	1.4%	2.3%	0.4%	94.9%	30,377	(217)	30,160
Loans	0.9%	1.3%	1.2%	0.2%	0.8%	95.6%	28,116	—	28,116
Total							218,951	(311)	218,640

The carrying amount of assets included in the statement of financial position represents the maximum credit exposure.

The impact of collateral held on the net credit exposure is shown below.

At 31 December 2012	2012			Restated 2011		
	Carrying value in the statement of financial position £m	Collateral held £m	Net credit exposure £m	Carrying value in the statement of financial position £m	Collateral held £m	Net credit exposure £m
Debt securities	161,623	(33)	161,590	153,345	(31)	153,314
Reinsurance assets	7,567	(21)	7,546	7,113	(443)	6,670
Other investments	30,093	(1,224)	28,869	30,377	(465)	29,912
Loans	27,934	(26,893)	1,041	28,116	(26,957)	1,159
Total	227,217	(28,171)	199,046	218,951	(27,896)	191,055
Less: Assets classified as held for sale	(39,447)	3,958	(35,489)	(311)	—	(311)
Total (excluding held for sale)	187,770	(24,213)	163,557	218,640	(27,896)	190,744

Following a review of the collateral reported, the total net credit exposure (excluding assets classified as held for sale) at 31 December 2011 has decreased by £1,045 million.

Additional information in respect to collateral is provided in notes 23(c) and notes 25(d)(i).

To the extent that collateral held is greater than the amount receivable that it is securing, the table above shows only an amount equal to the latter. In the event of default, any over-collateralised security would be returned to the relevant counterparty.

56 – Risk management continued

(ii) Financial exposures to peripheral European countries

Included in our debt securities and other financial assets, are exposures to peripheral European countries. Gross of non-controlling interests, our direct shareholder assets exposure to the governments (and local authorities and agencies) of Greece, Ireland, Portugal, Italy and Spain has reduced since 2011 and is detailed in 25 (e). We continue to monitor closely the situation in the eurozone and have had additional restrictions on further investment in place since late 2009 as well as taking actions to reduce exposure to higher risk assets.

(iii) Other investments

Other investments (including assets of operations classified as held for sale) include unit trusts and other investment vehicles; derivative financial instruments, representing positions to mitigate the impact of adverse market movements; and other assets includes deposits with credit institutions and minority holdings in property management undertakings.

The credit quality of the underlying debt securities within investment vehicles is managed by the safeguards built into the investment mandates for these funds which determine the funds' risk profiles. At the Group level, we also monitor the asset quality of unit trusts and other investment vehicles against Group set limits.

A proportion of the assets underlying these investments are represented by equities and so credit ratings are not generally applicable. Equity exposures are managed against agreed benchmarks that are set with reference to overall appetite for market risk.

(iv) Loans

The Group loan portfolio principally comprises:

- Policy loans which are generally collateralised by a lien or charge over the underlying policy;
- Loans and advances to banks which primarily relate to loans of cash collateral received in stock lending transactions. These loans are fully collateralised by other securities; and
- Mortgage loans collateralised by property assets.

We use loan to value; interest and debt service cover; and diversity and quality of the tenant base metrics to internally monitor our exposures to mortgage loans. We use credit quality, based on dynamic market measures, and collateralisation rules to manage our stock lending activities. Policy loans are loans and advances made to policyholders, and are collateralised by the underlying policies.

(v) Credit concentration risk

The long-term and general insurance businesses are generally not individually exposed to significant concentrations of credit risk due to the regulations applicable in most markets and the Group credit policy and limits framework, which limit investments in individual assets and asset classes. Credit concentrations are monitored as part of the regular credit monitoring process and are reported to Group ALCO. With the exception of government bonds the largest aggregated counterparty exposure within shareholder assets is approximately 1.5% of the total shareholder assets (gross of 'held for sale').

(vi) Reinsurance credit exposures

The Group is exposed to concentrations of risk with individual reinsurers due to the nature of the reinsurance market and the restricted range of reinsurers that have acceptable credit ratings. The Group operates a policy to manage its reinsurance counterparty exposures, by limiting the reinsurers that may be used and applying strict limits to each reinsurer. Reinsurance exposures are aggregated with other exposures to ensure that the overall risk is within appetite. The Group risk function has an active monitoring role with escalation to the Chief Financial Officer (CFO), Group ALCO and the Board Risk Committee as appropriate.

The Group's largest reinsurance counterparty is Swiss Reinsurance Company Ltd (including subsidiaries). At 31 December 2012, the reinsurance asset recoverable, including debtor balances, from Swiss Reinsurance Company Ltd was £1,717 million.

(vii) Securities finance

The Group has significant securities financing operations within the UK and smaller operations in some other businesses. The risks within this activity are mitigated by over-collateralisation and minimum counterparty credit quality requirements which are designed to minimise residual risk. The Group operates strict standards around counterparty quality, collateral management, margin calls and controls.

(viii) Derivative credit exposures

The Group is exposed to counterparty credit risk through derivative trades. This risk is mitigated through collateralising almost all trades (the exception being certain foreign exchange trades where it has historically been the market norm not to collateralise). Residual exposures are captured within the Group's credit management framework.

(ix) Unit-linked business

In unit-linked business the policyholder bears the direct market risk and credit risk on investment assets in the unit funds and the shareholders' exposure to credit risk is limited to the extent of the income arising from asset management charges based on the value of assets in the fund.

56 – Risk management continued**(x) Impairment of financial assets**

In assessing whether financial assets are impaired, due consideration is given to the factors outlined in accounting policy (S). The following table provides information regarding the carrying value of financial assets that have been impaired and the ageing of financial assets that are past due but not impaired. The table excludes assets 'held for sale'.

	Financial assets that are past due but not impaired					Financial assets that have been impaired £m	Carrying value £m
	Neither past due nor impaired £m	0-3 months £m	3-6 months £m	6 months-1 year £m	Greater than 1 year £m		
At 31 December 2012							
Debt securities	128,006	—	—	—	—	—	128,006
Reinsurance assets	6,684	—	—	—	—	—	6,684
Other investments	28,535	—	—	—	—	8	28,543
Loans	23,770	85	—	—	—	682	24,537
Receivables and other financial assets	7,518	46	13	14	26	—	7,617

	Financial assets that are past due but not impaired					Financial assets that have been impaired £m	Carrying value £m
	Neither past due nor impaired £m	0-3 months £m	3-6 months £m	6 months-1 year £m	Greater than 1 year £m		
At 31 December 2011							
Debt securities	152,988	—	—	—	—	264	153,252
Reinsurance assets	7,112	—	—	—	—	—	7,112
Other investments	30,152	—	—	—	—	8	30,160
Loans	27,582	6	—	—	—	528	28,116
Receivables and other financial assets	7,650	134	148	2	3	—	7,937

Where assets have been classed as 'past due and impaired', an analysis is made of the risk of default and a decision is made whether to seek to mitigate the risk. There were no material financial assets that would have been past due or impaired had the terms not been renegotiated.

(c) Market risk

Market risk is the risk of adverse financial impact resulting, directly or indirectly from fluctuations in interest rates, foreign currency exchange rates, equity and property prices. Market risk arises in business units due to fluctuations in both the value of liabilities and the value of investments held. At Group level, it also arises in relation to the overall portfolio of international businesses and in the value of investment assets owned directly by the shareholders. We actively seek some market risks as part of our investment and product strategy however have limited appetite for interest rate risk as we do not believe it is adequately rewarded.

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

In addition, where the Group's long-term savings businesses have written insurance and investment products where the majority of investment risks are borne by its policyholders, these risks are managed in line with local regulations and marketing literature, in order to satisfy the policyholders' risk and reward objectives. The Group writes unit-linked business in a number of its operations. The shareholders' exposure to market risk on this business is limited to the extent that income arising from asset management charges is based on the value of assets in the fund.

The most material types of market risk that the Group is exposed to are described below.

(i) Equity price risk

The Group is subject to equity price risk arising from changes in the market values of its equity securities portfolio.

We continue to limit our direct equity exposure in line with our risk preferences. The reduction of the shareholding in Delta Lloyd has decreased the Group's equity price risk and, in particular, has led to a fall in equity exposures. Our equity hedging programme during 2012 has further reduced our equity exposures. At a business unit level, investment limits and local asset admissibility regulations require that business units hold diversified portfolios of assets thereby reducing exposure to individual equities. The Group does not have material holdings of unquoted equity securities.

Equity risk is also managed using a variety of derivative instruments, including futures and options. Businesses actively model the performance of equities through the use of risk models, in particular to understand the impact of equity performance on guarantees, options and bonus rates. At 31 December 2012 the Group's shareholder funds held £3 billion notional of equity hedges, with up to 12 months to maturity with an average strike of 88% of the prevailing market levels on 31 December 2012.

Sensitivity to changes in equity prices is given in section '(j) risk and capital management' below.

(ii) Property price risk

The Group is subject to property price risk directly due to holdings of investment properties in a variety of locations worldwide and indirectly through investments in mortgages and mortgage backed securities. Investment in property is managed at business unit level, and is subject to local regulations on asset admissibility, liquidity requirements and the expectations of policyholders.

As at 31 December 2012, no material derivative contracts had been entered into to mitigate the effects of changes in property prices.

Sensitivity to changes in property prices is given in section '(j) risk and capital management' below.

56 – Risk management continued

(iii) Interest rate risk

Interest rate risk arises primarily from the Group's investments in long-term debt and fixed income securities and their movement relative to the value placed on the insurance liabilities. A number of policyholder product features have an influence on the Group's interest rate risk. The major features include guaranteed surrender values, guaranteed annuity options, and minimum surrender and maturity values. Details of material guarantees and options are given in note 41.

Exposure to interest rate risk is monitored through several measures that include duration, economic capital modelling, sensitivity testing and stress and scenario testing. The impact of exposure to sustained low interest rates is considered within our scenario testing.

The Group typically manages interest rate risk by investing in fixed interest securities which closely match the interest rate sensitivity of the liabilities where this is available. Interest rate risk is also managed in some business units using a variety of derivative instruments, including futures, options, swaps, caps and floors.

Sensitivity to changes in interest rates is given in section '(j) risk and capital management' below. Further information on borrowings is included in note 48.

(iv) Inflation risk

Inflation risk arises primarily from the Group's exposure to general insurance claims inflation, to inflation linked benefits within the defined benefit staff pension schemes and within the UK annuity portfolio and to expense inflation. Increases in long-term inflation expectations are closely linked to long-term interest rates and so are frequently considered with interest rate risk. Exposure to inflation risk is monitored through economic capital modelling, sensitivity testing and stress and scenario testing. The Group typically manages inflation risk through its investment strategy and, in particular, by investing in inflation linked securities and through a variety of derivative instruments, including inflation linked swaps.

(v) Currency risk

The Group has minimal exposure to currency risk from financial instruments held by business units in currencies other than their functional currencies, as nearly all such holdings are backing either by unit-linked or with-profit contract liabilities or hedging.

The Group operates internationally and as a result is exposed to foreign currency exchange risk arising from fluctuations in exchange rates of various currencies. Approximately half of the Group's premium income arises in currencies other than sterling and the Group's net assets are denominated in a variety of currencies, of which the largest are euro, sterling and US dollars. The Group does not hedge foreign currency revenues as these are substantially retained locally to support the growth of the Group's business and meet local regulatory and market requirements.

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

At 31 December 2012 and 2011, the Group's total equity deployment by currency including assets 'held for sale' was:

	Sterling £m	Euro £m	US\$ £m	Other £m	Total £m
Capital 31 December 2012	4,445	4,648	(51)	2,318	11,360
Capital 31 December 2011	3,427	6,442	3,237	2,257	15,363

A 10% change in sterling to euro/US\$ foreign exchange rates would have had the following impact on total equity.

	10% increase in sterling/ euro rate £m	10% decrease in sterling/ euro rate £m	10% increase in sterling/ US\$ rate £m	10% decrease in sterling/ US\$ rate £m
Net assets at 31 December 2012	(386)	411	34	(5)
Net assets at 31 December 2011	(524)	632	(323)	323

A 10% change in sterling to euro/US\$ foreign exchange rates would have had the following impact on profit before tax, excluding 'discontinued operations'.

	10% increase in sterling/ euro rate £m	10% decrease in sterling/ euro rate £m	10% increase in sterling/ US\$ rate £m	10% decrease in sterling/ US\$ rate £m
Impact on profit before tax 31 December 2012	(32)	32	1	(1)
Impact on profit before tax 31 December 2011	(84)	11	(4)	17

The balance sheet changes arise from retranslation of business unit statements of financial position from their functional currencies into sterling, with above movements being taken through the currency translation reserve. These balance sheet movements in exchange rates therefore have no impact on profit. Net asset and profit before tax figures are stated after taking account of the effect of currency hedging activities.

56 – Risk management continued

(vi) Derivatives risk

Derivatives are used by a number of the businesses. Activity is overseen by the Group risk function, who monitors exposure levels and approves large or complex transactions. Derivatives are primarily used for efficient investment management, risk hedging purposes, or to structure specific retail savings products.

The Group applies strict requirements to the administration and valuation processes it uses, and has a control framework that is consistent with market and industry practice for the activity that is undertaken.

(vii) Correlation risk

The Group recognises that lapse behaviour and potential increases in consumer expectations are sensitive to and interdependent with market movements and interest rates. These interdependencies are taken into consideration in the internal economic capital model and in scenario analysis.

(d) Liquidity risk

Liquidity risk is the risk of not being able to make payments as they become due because there are insufficient assets in cash form. The relatively illiquid nature of insurance liabilities is a potential source of additional investment return by allowing us to invest in higher yielding, but less liquid assets such as commercial mortgages. The Group seeks to ensure that it maintains sufficient financial resources to meet its obligations as they fall due through the application of a Group liquidity risk policy and business standard. At Group and business unit level, there is a liquidity risk appetite which requires that sufficient liquid resources be maintained to cover net outflows in a stress scenario. The Company's main sources of liquidity are liquid assets held within the Company and Aviva Group Holdings Limited (AGH), and dividends received from the Group's insurance and asset management businesses. Sources of liquidity in normal markets also includes a variety of short and long-term instruments including commercial papers and medium and long-term debt. For 2012 and prior years, the Company's main sources of liquidity also included intercompany loans from Aviva Insurance Limited and Aviva International Insurance Limited, subject to regulatory constraints. In addition to the existing liquid resources and expected inflows, the Group and Company maintain significant undrawn committed borrowing facilities (£2.1 billion) from a range of leading international banks to further mitigate this risk.

Maturity analyses

The following tables show the maturities of our insurance and investment contract liabilities, and of the financial and reinsurance assets to meet them. A maturity analysis of the contractual amounts payable for borrowings and derivatives is given in notes 48 and 57, respectively. Contractual obligations under operating leases and capital commitments are given in note 52.

(i) Analysis of maturity of insurance and investment contract liabilities

For non-linked insurance business, the following table shows the gross liability at 31 December 2012 and 2011 analysed by remaining duration. The total liability is split by remaining duration in proportion to the cash-flows expected to arise during that period, as permitted under IFRS 4, *Insurance Contracts*.

Almost all linked business and non-linked investment contracts may be surrendered or transferred on demand. For such contracts, the earliest contractual maturity date is therefore the current statement of financial position date, for a surrender amount approximately equal to the current statement of financial position liability. We expect surrenders, transfers and maturities to occur over many years, and the tables reflect the expected cash flows for these contracts. However, contractually, the total liability for linked business and non-linked investment contracts would be shown in the 'within 1 year' column below, and previously the total liability for linked business was shown in the 'within 1 year' column. Changes in durations between 2011 and 2012 reflect evolution of the portfolio, and changes to the models for projecting cash-flows.

At 31 December 2012	Total £m	On demand or within 1 year £m	1-5 years £m	5-15 years £m	Over 15 years £m
Long-term business					
Insurance contracts – non-linked	117,602	8,303	31,894	44,455	32,950
Investment contracts – non-linked	59,788	2,491	12,390	16,679	28,228
Linked business	69,690	5,667	18,203	21,590	24,230
General insurance and health	15,006	6,166	5,763	2,456	621
Total contract liabilities	262,086	22,627	68,250	85,180	86,029

At 31 December 2011	Total £m	On demand or within 1 year £m	1-5 years £m	5-15 years £m	Over 15 years £m
Long-term business					
Insurance contracts – non-linked (restated) ¹	117,442	9,693	35,403	45,829	26,517
Investment contracts – non-linked (restated) ¹	62,412	6,240	20,208	26,252	9,712
Linked business (restated) ²	65,994	7,297	20,614	24,324	13,759
General insurance and health	15,241	5,645	5,967	2,913	716
Total contract liabilities	261,089	28,875	82,192	99,318	50,704

¹ Following a review of the classification of contracts issued by the Group's Italian long-term business, certain portfolios have been reclassified from participating insurance to participating investment contracts for all years presented. There is no impact on the result for any year presented as a result of this classification.

² Linked business maturity profile has been restated to reflect an expected rather than contractual basis. Contractually, the total liability for linked business would be shown in the 'within 1 year column'.

56 – Risk management continued

(ii) Analysis of maturity of financial assets

The following table provides an analysis, by maturity date of the principal, of the carrying value of financial assets which are available to fund the repayment of liabilities as they crystallise. This table excludes assets held for sale.

	Total £m	On demand or within 1 year £m	1-5 years £m	Over 5 years £m	No fixed term (perpetual) £m
At 31 December 2012					
Debt securities	128,006	16,796	36,009	75,198	3
Equity securities	32,529	—	—	—	32,529
Other investments	28,543	12,638	866	12,508	2,531
Loans	24,537	5,358	1,780	17,329	70
Cash and cash equivalents	22,897	22,897	—	—	—
	236,512	57,689	38,655	105,035	35,133
At 31 December 2011					
Debt securities	153,252	18,698	39,079	95,460	15
Equity securities	32,646	—	—	—	32,646
Other investments	30,160	21,007	1,192	1,016	6,945
Loans	28,116	6,490	2,800	18,825	1
Cash and cash equivalents	23,043	23,043	—	—	—
	267,217	69,238	43,071	115,301	39,607

The assets above are analysed in accordance with the earliest possible redemption date of the instrument at the initiation of the Group. Where an instrument is transferable back to the issuer on demand, such as most unit trusts or similar types of investment vehicle, it is included in the 'On demand or within 1 year' column. Debt securities with no fixed contractual maturity date are generally callable at the option of the issuer at the date the coupon rate is reset under the contractual terms of the instrument. The terms for resetting the coupon are such that we expect the securities to be redeemed at this date, as it would be uneconomic for the issuer not to do so, and for liquidity management purposes we manage these securities on this basis. The first repricing and call date is normally ten years or more after the date of issuance. Most of the Group's investments in equity securities and fixed maturity securities are market traded and therefore, if required, can be liquidated for cash at short notice.

(e) Life insurance risk

Life insurance risk in the Group arises through its exposure to mortality and morbidity risks and exposure to worse than anticipated operating experience on factors such as persistency levels and management and administration expenses. The Group chooses to take measured amounts of life insurance risk provided that the relevant business has the appropriate core skills to assess and price the risk and adequate returns are available.

The underlying risk profile of our life insurance risks, primarily persistency, longevity, mortality and expense risk, has remained stable during 2012, although the current low levels of interest rates have increased our sensitivity to longevity shocks. Persistency risk remains significant and continues to have a volatile outlook with underlying performance linked to some degree to economic conditions. However, businesses across the Group have continued to make progress with a range of customer retention activities. The Group has continued to write strong volumes of life protection business, and to utilise reinsurance to reduce exposure to potential losses. More generally, life insurance risks are believed to benefit from a significant diversification against other risks in the portfolio. Life insurance risks are modelled within the internal economic capital model and subject to sensitivity and stress and scenario testing. The assumption and management of life insurance risks is governed by the group-wide business standards covering underwriting, pricing, product design and management, in-force management, claims handling, and reinsurance. The individual life insurance risks are managed as follows:

- Mortality and morbidity risks are mitigated by use of reinsurance. The Group allows businesses to select reinsurers, from those approved by the Group, based on local factors, but retains oversight of the overall exposures and monitor that the aggregation of risk ceded is within credit risk appetite.
- Longevity risk and internal experience analysis are monitored against the latest external industry data and emerging trends. Whilst individual businesses are responsible for reserving and pricing for annuity business, the Group monitors the exposure to this risk and any associated capital implications. The Group has used reinsurance solutions to reduce the risks from longevity and continually monitors and evaluates emerging market solutions to mitigate this risk further.
- Persistency risk is managed at a business unit level through frequent monitoring of company experience, and benchmarked against local market information. Generally, persistency risk arises from customers lapsing their policies earlier than has been assumed. Where possible the financial impact of lapses is reduced through appropriate product design. Businesses also implement specific initiatives to improve retention of policies which may otherwise lapse. The Group has developed guidelines on persistency management.
- Expense risk is primarily managed by the business units through the assessment of business unit profitability and frequent monitoring of expense levels.

Embedded derivatives

The Group has exposure to a variety of embedded derivatives in its long-term savings business due to product features offering varying degrees of guaranteed benefits at maturity or on early surrender, along with options to convert their benefits into different products on pre-agreed terms. The extent of the impact of these embedded derivatives differs considerably between business units and exposes Aviva to changes in policyholder behaviour in the exercise of options as well as market risk.

56 – Risk management continued

Examples of each type of embedded derivative affecting the Group are:

- Options: call, put, surrender and maturity options, guaranteed annuity options, options to cease premium payment, options for withdrawals free of market value adjustment, annuity options, and guaranteed insurability options.
- Guarantees: embedded floor (guaranteed return), maturity guarantee, guaranteed death benefit, and guaranteed minimum rate of annuity payment.
- Other: indexed interest or principal payments, maturity value, loyalty bonus.

The impact of these is reflected in the economic capital model and MCEV reporting and managed as part of the asset liability framework.

(f) General insurance risk

Types of risk

General insurance risk in the Group arises from:

- Fluctuations in the timing, frequency and severity of claims and claim settlements relative to expectations;
- Unexpected claims arising from a single source or cause;
- Inaccurate pricing of risks or inappropriate underwriting of risks when underwritten; and
- Inadequate reinsurance protection or other risk transfer techniques.

Aviva has a preference for general insurance risk in measured amounts for explicit reward, in line with our core skills in underwriting and pricing. The majority of the general insurance business underwritten by the Group continues to be short tail in nature such as motor, household and commercial property insurances. The Group's underwriting strategy and appetite is communicated via specific policy statements, related business standards and guidelines. General insurance risk is managed primarily at business unit level with oversight at the Group level. Claims reserving is undertaken by local actuaries in the various general insurance businesses and is also subject to periodic external reviews. Reserving processes are further detailed in note 39 'insurance liabilities'.

The vast majority of the Group's general insurance business is managed and priced in the same country as the domicile of the customer.

Management of general insurance risks

Significant insurance risks will be reported under the risk management framework. Additionally, the economic capital model is used to assess the risks that each general insurance business unit, and the Group as a whole, is exposed to, quantifying their impact and calculating appropriate capital requirements.

Business units have developed mechanisms that identify, quantify and manage accumulated exposures to contain them within the limits of the appetite of the Group. The business units are assisted by a Business Capability team who provide technical input for major decisions which fall outside individual delegated limits or escalations outside group risk preferences, group risk accumulation, concentration and profitability limits.

Reinsurance strategy

Significant reinsurance purchases are reviewed annually at both business unit and Group level to verify that the levels of protection being bought reflect any developments in exposure and the risk appetite of the Group. The basis of these purchases is underpinned by analysis of economic capital, economic gain, earnings volatility, liquidity, retained risk exposure profile and the Group's franchise value.

Detailed actuarial analysis is used to calculate the Group's extreme risk profile and then design cost and capital efficient reinsurance programmes to mitigate these risks to within agreed appetites. For businesses writing general insurance we analyse the natural catastrophe exposure using external probabilistic catastrophe models widely used by the rest of the (re)insurance industry.

The Group cedes much of its worldwide catastrophe risk to third-party reinsurers but retains a pooled element for its own account gaining diversification benefit. The total Group potential loss from its most concentrated catastrophe exposure zone (Northern Europe) is approximately £260 million, for a one in ten year annual loss scenario, compared to approximately £460 million when measured on a one in a hundred year annual loss scenario.

In our 2011 Annual Report & Accounts we reported our participation in a share of Hiscox's US property catastrophe portfolio. This arrangement expired on the 31 December 2012 and remaining exposure will run off during 2013.

(g) Asset management risk

Asset Management risk arises through exposure to negative investment performance, fund liquidity, and factors that influence franchise value such as product development appropriateness and capability, and client retention. The Group's exposure to asset management risk is informed through regular assessment of the investment management capabilities and proven track record of the investment funds.

Aviva is directly exposed to the risks associated with operating an asset management business through its ownership of Aviva Investors. The underlying risk profile of our asset management risk is derived from investment performance, specialist investment professionals and leadership, product development capabilities, fund liquidity, margin, client retention, regulatory developments, fiduciary and contractual responsibilities. Investment performance has remained strong over 2012 despite some positions being impacted by the volatility of global markets.

56 – Risk management continued

Action has been taken during the year to improve the operational infrastructure and enhance the quality of the customer experience including; progressing towards the implementation of the Blackrock Aladdin platform to support our investment process; review of our Business Development capability; and a continued drive to work closely with clients.

(h) Operational risk

Operational risk is the risk of direct or indirect loss, arising from inadequate or failed internal processes, people and systems, or external events including changes in the regulatory environment. We have limited appetite for operational risk and aim to reduce these risks as far as is commercially sensible.

Our business units are primarily responsible for identifying and managing operational risks within their businesses, within the group-wide operational risk framework including the risk and control self-assessment process. Businesses must be satisfied that all material risks falling outside our risk tolerances are being mitigated, monitored and reported to an appropriate level. Any risks with a high potential impact are monitored centrally on a regular basis. Businesses use key indicator data to help monitor the status of the risk and control environment. They also identify and capture loss events, taking appropriate action to address actual control breakdowns and promote internal learning.

(i) Brand and reputation risk

We are exposed to the risk that litigation, employee misconduct, operational failures, the outcome of regulatory investigations, media speculation and negative publicity, disclosure of confidential client information, inadequate services, whether or not founded, could impact our brands or reputation. Any of our brands or our reputation could also be affected if products or services recommended by us (or any of our intermediaries) do not perform as expected (whether or not the expectations are founded) or the customer's expectations for the product change. We seek to reduce this risk to as low a level as commercially sensible.

The FSA regularly considers whether we are meeting the requirement to treat our customers fairly and we make use of various metrics to assess our own performance, including customer advocacy, retention and complaints. Failure to meet these requirements could also impact our brands or reputation.

If we do not manage the perception of our brands and reputation successfully, it could cause existing customers or agents to withdraw from our business and potential customers or agents to choose not to do business with us.

(j) Risk and capital management

(i) Sensitivity test analysis

The Group uses a number of sensitivity tests to understand the volatility of earnings, the volatility of its capital requirements, and to manage its capital more efficiently. Sensitivities to economic and operating experience are regularly produced on the Group's key financial performance metrics to inform the Group's decision making and planning processes, and as part of the framework for identifying and quantifying the risks to which each of its business units, and the Group as a whole, are exposed.

For long-term business in particular, sensitivities of market consistent performance indicators to changes in both economic and non-economic experience are continually used to manage the business and to inform the decision making process.

(ii) Life insurance and investment contracts

The nature of long-term business is such that a number of assumptions are made in compiling these financial statements. Assumptions are made about investment returns, expenses, mortality rates and persistency in connection with the in-force policies for each business unit. Assumptions are best estimates based on historic and expected experience of the business. A number of the key assumptions for the Group's central scenario are disclosed elsewhere in these statements for both IFRS reporting and reporting under MCEV methodology.

(iii) General insurance and health business

General insurance and health claim liabilities are estimated by using standard actuarial claims projection techniques. These methods extrapolate the claims development for each accident year based on the observed development of earlier years. In most cases, no explicit assumptions are made as projections are based on assumptions implicit in the historic claims.

(iv) Sensitivity test results

Illustrative results of sensitivity testing for long-term business, general insurance and health business and the fund management and non-insurance business are set out below. For each sensitivity test the impact of a reasonably possible change in a single factor is shown, with other assumptions left unchanged.

56 – Risk management continued

Sensitivity factor	Description of sensitivity factor applied
Interest rate and investment return	The impact of a change in market interest rates by a 1% increase or decrease. The test allows consistently for similar changes to investment returns and movements in the market value of backing fixed interest securities.
Credit spreads	The impact of a 0.5% increase in credit spreads over risk-free interest rates on corporate bonds and other non-sovereign credit assets. The test allows for any consequential impact on liability valuations
Equity/property market values	The impact of a change in equity/property market values by \pm 10%.
Expenses	The impact of an increase in maintenance expenses by 10%.
Assurance mortality/morbidity (life insurance only)	The impact of an increase in mortality/morbidity rates for assurance contracts by 5%.
Annuitant mortality (life insurance only)	The impact of a reduction in mortality rates for annuity contracts by 5%.
Gross loss ratios (non-life insurance only)	The impact of an increase in gross loss ratios for general insurance and health business by 5%.

Long-term business

Sensitivities as at 31 December 2012

2012 Impact on profit before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality -5%
Insurance Participating	(45)	(15)	(110)	60	(95)	(25)	(5)	(50)
Insurance non-participating	(160)	130	(430)	—	—	(75)	(45)	(470)
Investment participating	(55)	45	—	5	(10)	(10)	—	—
Investment non-participating	(40)	35	(5)	10	(15)	(20)	—	—
Assets backing life shareholders' funds	10	(15)	(40)	45	(45)	—	—	—
Total excluding Delta Lloyd and United States	(290)	180	(585)	120	(165)	(130)	(50)	(520)
United States	880	(640)	495	—	—	—	—	—
Total excluding Delta Lloyd	590	(460)	(90)	120	(165)	(130)	(50)	(520)

2012 Impact on shareholders' equity before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality -5%
Insurance Participating	(45)	(15)	(110)	60	(95)	(25)	(5)	(50)
Insurance non-participating	(165)	125	(430)	—	—	(75)	(45)	(470)
Investment participating	(55)	45	—	5	(10)	(10)	—	—
Investment non-participating	(45)	40	—	10	(15)	(20)	—	—
Assets backing life shareholders' funds	(5)	—	(45)	50	(50)	—	—	—
Total excluding Delta Lloyd and United States	(315)	195	(585)	125	(170)	(130)	(50)	(520)
United States	—	—	—	—	—	—	—	—
Total excluding Delta Lloyd	(315)	195	(585)	125	(170)	(130)	(50)	(520)

Sensitivities as at 31 December 2011

2011 Impact on profit before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality -5%
Insurance Participating	(45)	(155)	(20)	5	(95)	(45)	(10)	(50)
Insurance non-participating	(180)	130	(385)	30	(35)	(65)	(45)	(470)
Investment participating	(35)	40	(30)	50	(75)	(10)	—	—
Investment non-participating	(15)	20	(5)	15	(15)	(20)	—	—
Assets backing life shareholders' funds	135	(15)	(10)	10	(10)	—	—	—
Total excluding Delta Lloyd and United States	(140)	20	(450)	110	(230)	(140)	(55)	(520)
United States	45	(50)	10	50	(35)	(10)	(15)	—
Total excluding Delta Lloyd	(95)	(30)	(440)	160	(265)	(150)	(70)	(520)

2011 Impact on shareholders' equity before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality -5%
Insurance Participating	(45)	(155)	(25)	5	(95)	(45)	(10)	(50)
Insurance non-participating	(180)	130	(385)	30	(35)	(65)	(45)	(470)
Investment participating	(35)	40	(30)	50	(75)	(10)	—	—
Investment non-participating	(15)	20	(5)	15	(15)	(20)	—	—
Assets backing life shareholders' funds	125	—	(15)	15	(15)	—	—	—
Total excluding Delta Lloyd and United States	(150)	35	(460)	115	(235)	(140)	(55)	(520)
United States	(540)	455	(350)	50	(35)	(10)	(15)	—
Total excluding Delta Lloyd	(690)	490	(810)	165	(270)	(150)	(70)	(520)

56 – Risk management continued

Changes in sensitivities between 2012 and 2011 reflect movements in market interest rates, portfolio growth, changes to asset mix and the relative durations of assets and liabilities and asset liability management actions.

The sensitivities to economic movements (excluding the United States) relate mainly to business in the UK. In general, a fall in market interest rates has a beneficial impact on non-participating business, due to the increase in market value of fixed interest securities and the relative durations of assets and liabilities; similarly a rise in interest rates has a negative impact. The mortality sensitivities also relate primarily to the UK.

In the United States, most debt securities are classified as AFS for which movements in unrealised gains or losses are taken directly to shareholders' equity. This limited the overall sensitivity of IFRS profit to interest rate and credit spread movements. Following the classification of the business as held for sale in 2012 it was remeasured to fair value less costs to sell. It has been assumed that economic movements would not materially impact the fair value less costs to sell and the impact on shareholders' equity is therefore reported as £nil. As a result, were economic movements to occur, the corresponding movements in AFS assets which would be taken directly to shareholders' equity, are reversed out through profit before tax in order to maintain the remeasurement value of the US at fair value less costs to sell.

General insurance and health business sensitivities as at 31 December 2012

2012 Impact on profit before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance excluding Delta Lloyd	(260)	235	(125)	45	(50)	(120)	(300)
Net of reinsurance excluding Delta Lloyd	(300)	285	(125)	45	(50)	(120)	(285)

2012 Impact on shareholders' equity before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance excluding Delta Lloyd	(260)	235	(125)	50	(50)	(25)	(300)
Net of reinsurance excluding Delta Lloyd	(300)	285	(125)	50	(50)	(25)	(285)

Sensitivities as at 31 December 2011

2011 Impact on profit before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance excluding Delta Lloyd	(205)	180	(125)	50	(55)	(130)	(300)
Net of reinsurance excluding Delta Lloyd	(275)	275	(125)	50	(55)	(130)	(290)

2011 Impact on shareholders' equity before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance excluding Delta Lloyd	(205)	180	(125)	50	(55)	(30)	(300)
Net of reinsurance excluding Delta Lloyd	(275)	275	(125)	50	(55)	(30)	(290)

For general insurance, the impact of the expense sensitivity on profit also includes the increase in ongoing administration expenses, in addition to the increase in the claims handling expense provision.

Fund management and non-insurance business sensitivities as at 31 December 2012

2012 Impact on profit before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%
Total excluding Delta Lloyd	(5)	—	30	(90)	10

2012 Impact on shareholders' equity before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%
Total excluding Delta Lloyd	(5)	—	30	(90)	10

56 – Risk management continued

Sensitivities as at 31 December 2011

2011 Impact on profit before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%
Total excluding Delta Lloyd	(10)	10	—	(40)	75

2011 Impact on shareholders' equity before tax £m	Interest rates +1%	Interest rates -1%	Credit spreads +0.5%	Equity/ property +10%	Equity/ property -10%
Total excluding Delta Lloyd	(10)	10	—	(40)	75

Limitations of sensitivity analysis

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs. For example, the Group's financial risk management strategy aims to manage the exposure to market fluctuations.

As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation, adjusting bonuses credited to policyholders, and taking other protective action.

A number of the business units use passive assumptions to calculate their long-term business liabilities. Consequently, a change in the underlying assumptions may not have any impact on the liabilities, whereas assets held at market value in the statement of financial position will be affected. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity. Similarly, for general insurance liabilities, the interest rate sensitivities only affect profit and equity where explicit assumptions are made regarding interest (discount) rates or future inflation.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Group's view of possible near-term market changes that cannot be predicted with any certainty, and the assumption that all interest rates move in an identical fashion.

57 – Derivative financial instruments and hedging

This note gives details of the various instruments we use to mitigate risk.

The Group uses a variety of derivative financial instruments, including both exchange traded and over-the-counter instruments, in line with our overall risk management strategy. The objectives include managing exposure to price, foreign currency and / or interest rate risk on existing assets or liabilities, as well as planned or anticipated investment purchases.

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

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

(a) Instruments qualifying for hedge accounting

The Group has formally assessed and documented the effectiveness of its instruments qualifying for hedge accounting in accordance with IAS 39, *Financial Instruments: Recognition and Measurement*. To aid discussion and analysis, these instruments are analysed into cash flow, fair value and net investment hedges, as detailed below.

(i) Cash flow hedges

At the end of 2012 the Group entered into two cash flow hedges, using foreign exchange forward and option contracts, to hedge the currency exposure on expected proceeds in 2013 of businesses held for sale as at 31 December 2012. The fair value of the cash flow hedges as of 31 December 2012 was a £5 million derivative asset. No amounts in respect of the cash flow hedges have been recognised in the income statement for the year. All cash flows being hedged upon transaction completion are expected to occur and movements in the fair value will be recycled to the income statement in 2013. These hedges were fully effective in the year.

(ii) Fair value hedges

The Group entered into a number of interest rate swaps in order to hedge fluctuations in the fair value part of its portfolio of mortgage loans and debt securities in the US. The notional value of these swaps was £765 million at 31 December 2012 (2011: £844 million) and their fair value was £54 million liability (2011: £77 million liability). During 2012, there were hedging relationships that became ineffective. The amount of ineffectiveness included in the income statement as a result was £14 million. The related hedges were re-designated and are expected to be effective in future periods.

57 – Derivative financial instruments and hedging continued

(iii) Net investment hedges

To reduce its exposure to foreign currency risk, the Group has entered into the following net investment hedges:

The Group has designated a portion of its euro and US dollar denominated debt as a hedge of the net investment in its European and American subsidiaries. The carrying value of the debt at 31 December 2012 was £1,741 million (2011: £1,815 million) and its fair value at that date was £1,785 million (2011: £1,694 million).

The foreign exchange gain of £74 million (2011: gain of £30 million) on translation of the debt to sterling at the statement of financial position date has been recognised in the hedging instruments reserve in shareholders' equity. This hedge was fully effective throughout the current and prior years.

(b) Derivatives not qualifying for hedge accounting

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

(i) The Group's non-hedge derivative activity at 31 December 2012 and 2011 was as follows:

	2012			Restated 2011		
	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m
Foreign exchange contracts						
OTC						
Forwards	8,123	71	(7)	6,727	41	(38)
Interest rate and currency swaps	611	64	(21)	502	83	(3)
Options	4,600	6	(5)	4,600	33	(9)
Total	13,334	141	(33)	11,829	157	(50)
Interest rate contracts						
OTC						
Swaps	25,889	135	(925)	13,931	247	(986)
Options	32,656	272	(4)	2,604	208	(2)
Exchange traded						
Futures	3,725	58	(14)	2,794	46	(25)
Total	62,270	465	(943)	19,329	501	(1,013)
Equity/Index contracts						
OTC						
Options	2,765	650	(10)	2,864	531	(5)
Exchange traded						
Futures	5,468	45	(123)	3,805	52	(452)
Options	11,880	228	(139)	7,405	242	(161)
Total	20,113	923	(272)	14,074	825	(618)
Credit contracts	6,277	41	(53)	5,478	2	(17)
Other	3,163	15	(406)	3,309	13	(75)
Totals at 31 December	105,157	1,585	(1,707)	54,019	1,498	(1,773)
Less: Amounts classified as held for sale	(4,403)	(679)	54	—	—	—
	100,754	906	(1,653)	54,019	1,498	(1,773)

The 2011 figures have been restated in respect of the notional values of the exchange traded equity option contracts. £5,478 million notional of credit derivatives (and their related fair values) have been reclassified out of the 'other' and 'interest rate swap' categories to the 'credit' contracts category. Additionally £3,156 million notional of inflation linked swaps have been reclassified out of the 'interest rate swap' category to the 'other' category.

Fair value assets are recognised as 'Derivative financial instruments' in note 25(a), while fair value liabilities are recognised as 'Derivative liabilities' in note 49. Fair value assets in note 25(a) of £1,590 million represent non-hedge derivative assets of £1,585 million per the table above plus £5 million of cash flow hedges. Fair value liabilities in note 49 of £1,761 million represent non-hedge derivative liabilities of £1,707 million per the table above plus £54 million of fair value hedges.

The Group's derivative risk management policies are outlined in note 56.

(ii) The contractual undiscounted cash flows in relation to non-hedge derivative liabilities have the following maturities:

	2012 £m	2011 £m
Within 1 year	534	226
Between 1 and 2 years	434	144
Between 2 and 3 years	158	135
Between 3 and 4 years	387	123
Between 4 and 5 years	113	355
After 5 years	1,787	1,911
	3,413	2,894

(c) Collateral

Certain derivative contracts, primarily interest rate and currency swaps, involve the receipt or pledging of cash and non-cash collateral. The amounts of cash collateral receivable or repayable are included in notes 26 and 49 respectively.

58 – Assets under management

In addition to the assets included in the consolidated statement of financial position, the Group manages funds for third parties. This note details the total assets under management.

	2012 £m	2011 £m
Total IFRS assets included in the consolidated statement of financial position	315,689	312,376
Less: Third-party funds included within consolidated IFRS assets	(13,525)	(11,814)
Third-party funds under management	302,164	300,562
	73,114	67,557
Non-managed assets	375,278	368,119
	(26,137)	(31,558)
Funds under management	349,141	336,561
Discontinued operations	(38,148)	(37,110)
Funds under management (excluding discontinued operations)	310,993	299,451
Managed by:		
Aviva Investors	274,484	262,506
Other Aviva and external managers	74,657	74,055
	349,141	336,561

59 – Related party transactions

This note gives details of the transactions between Group companies and related parties which comprise our joint ventures, associates and staff pension schemes.

The Group undertakes transactions with related parties in the normal course of business. Loans to related parties are made on normal arm's-length commercial terms.

Services provided to, and by related parties

	2012				2011			
	Income earned in period £m	Expenses incurred in period £m	Payable at period end £m	Receivable at period end £m	Income earned in period £m	Expenses incurred in period £m	Payable at period end £m	Receivable at period end £m
Associates	—	(4)	—	—	—	(3)	(49)	—
Joint ventures	23	(1)	—	103	23	—	—	125
Employee pension schemes	12	—	—	6	13	—	—	9
	35	(5)	—	109	36	(3)	(49)	134

Transactions with joint ventures in the UK relate to the property management undertakings, the most material of which are listed in note 18(b). Our interest in these joint ventures comprises a mix of equity and loans, together with the provision of administration services and financial management to many of them. Our UK life insurance companies earn interest on loans advanced to these entities, movements in which may be found in note 18(a).

Our fund management companies also charge fees to these joint ventures for administration services and for arranging external finance.

Our UK fund management companies manage most of the assets held by the Group's main UK staff pension scheme, for which they charge fees based on the level of funds under management. The main UK scheme holds investments in Group-managed funds and insurance policies with other Group companies, as explained in note 47(e)(iii).

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms. Details of guarantees, indemnities and warranties provided on behalf of related parties are given in note 51(g).

Key management compensation

The total compensation to those employees classified as key management, being those having authority and responsibility for planning, directing and controlling the activities of the Group, including the executive and non-executive directors is as follows:

	2012 £m	2011 £m
Salary and other short-term benefits ¹	4.7	6.7
Other long-term benefits	0.4	2.8
Post-employment benefits ¹	1.9	1.7
Equity compensation plans ¹	4.8	5.9
Termination benefits ¹	1.5	0.7
Total	13.3	17.8

¹ Following a review of the composition of key management in the current year, comparative amounts have been restated from the amounts previously reported. The total key management compensation reported in 2011 was £65 million.

Information concerning individual directors' emoluments, interests and transactions is given in the Directors' Remuneration Report.

Financial statements of the Company

Statement of changes in equity

For the year ended 31 December 2012

Note	Ordinary share capital £m	Preference share capital £m	Share premium £m	Merger reserve £m	Investment valuation reserve £m	Equity compensation reserve £m	Retained earnings £m	Equity £m	DCI and fixed rate tier 1 notes £m	Total equity £m
Balance at 1 January Restated	726	200	1,173	735	4,414	86	3,116	10,450	990	11,440
Profit for the year	—	—	—	—	—	—	616	616	—	616
Other comprehensive income	—	—	—	—	2,380	—	—	2,380	—	2,380
Total comprehensive income for the year	—	—	—	—	2,380	—	616	2,996	—	2,996
Dividends and appropriations	15	—	—	—	—	—	(847)	(847)	—	(847)
Shares issued in lieu of dividends	29 & 36	9	—	(9)	—	—	127	127	—	127
Employee trust shares distributed in the year	31	—	—	—	—	—	(44)	(44)	—	(44)
Reserves credit for equity compensation plans	—	—	—	—	—	42	—	42	—	42
Shares issued under equity compensation plans	—	1	—	1	—	(68)	74	8	—	8
Issue of fixed rate tier 1 notes	—	—	—	—	—	—	—	—	392	392
Aggregate tax effect	—	—	—	—	—	—	18	18	—	18
Balance at 31 December	736	200	1,165	735	6,794	60	3,060	12,750	1,382	14,132

For the year ended 31 December 2011

Note	Ordinary share capital £m	Preference share capital £m	Share premium £m	Merger reserve £m	Investment valuation reserve £m	Equity compensation reserve £m	Retained earnings £m	Equity £m	Direct capital instrument £m	Total equity £m
Balance at 1 January Restated	705	200	1,194	735	6,803	99	3,331	13,067	990	14,057
Profit for the year	—	—	—	—	—	—	231	231	—	231
Other comprehensive income	—	—	—	—	(2,389)	—	1	(2,388)	—	(2,388)
Total comprehensive income for the year	—	—	—	—	(2,389)	—	232	(2,157)	—	(2,157)
Dividends and appropriations	15	—	—	—	—	—	(813)	(813)	—	(813)
Shares issued in lieu of dividends	29 & 36	21	—	(21)	—	—	307	307	—	307
Employee trust shares distributed in the year	31	—	—	—	—	—	(18)	(18)	—	(18)
Reserves credit for equity compensation plans	—	—	—	—	—	48	—	48	—	48
Shares issued under equity compensation plans	—	—	—	—	—	(61)	61	—	—	—
Aggregate tax effect	—	—	—	—	—	—	16	16	—	16
Balance at 31 December Restated	726	200	1,173	735	4,414	86	3,116	10,450	990	11,440

Where applicable, the accounting policies of the Company are the same as those of the Group on pages 148 to 159. The notes identified alphabetically on pages 270 to 272 are an integral part of these separate financial statements. Where the same items appear in the Group financial statements, reference is made to the notes (identified numerically) on pages 168 to 266.

Statement of financial position

At 31 December 2012 and 2011 and 2010

	Note	2012 £m	Restated 2011 £m	Restated 2010 £m
Assets				
Non-current assets				
Investments in subsidiaries	B	31,023	28,889	31,284
Investment in joint venture	18c	141	150	115
Loans owed by subsidiaries	H	1,054	2,375	2,411
Deferred tax assets	C	180	—	—
Current tax assets	C	50	261	388
		32,448	31,675	34,198
Current assets				
Loans owed by subsidiaries	H	1,240	—	691
Other amounts owed by subsidiaries	H	3,019	2,280	2,334
Other assets		49	61	74
Cash and cash equivalents		152	17	1
Total assets		36,908	34,033	37,298
Equity				
Ordinary share capital	29	736	726	705
Preference share capital	32	200	200	200
Called up capital		936	926	905
Share premium account	29b	1,165	1,173	1,194
Merger reserve	D	735	735	735
Investment valuation reserve	D	6,794	4,414	6,803
Equity compensation reserve	D	60	86	99
Retained earnings	D	3,060	3,116	3,331
Direct capital instruments and fixed rate tier 1 notes	33	1,382	990	990
Total equity		14,132	11,440	14,057
Liabilities				
Non-current liabilities				
Borrowings	E	4,536	4,781	4,805
Loans owed to subsidiaries	H	13,153	13,306	14,067
Provisions		36	35	46
		17,725	18,122	18,918
Current liabilities				
Borrowings	E	603	506	504
Loans owed to subsidiaries	H	794	502	514
Other amounts owed to subsidiaries	H	3,569	3,366	3,184
Other creditors		85	97	121
Total liabilities		22,776	22,593	23,241
Total equity and liabilities		36,908	34,033	37,298

Approved by the Board on 6 March 2013.

Patrick Regan
Chief Financial Officer

Statement of cash flows

For the years ended 31 December 2012 and 2011

All the Company's operating and investing cash requirements are met by subsidiary companies and settled through intercompany loan accounts. As the direct method of presentation has been adopted for these activities, no further disclosure is required. In respect of financing activities, the following items pass through the Company's own bank accounts.

	2012 £m	2011 £m
Cash flows from financing activities		
Funding provided by subsidiaries	868	847
New borrowings, net of expenses	2,200	3,319
Repayment of borrowings	(2,295)	(3,326)
Net repayment of borrowings	(95)	(7)
Proceeds from issue of fixed rate tier 1 notes, net of expenses	392	—
Preference dividends paid	(17)	(17)
Ordinary dividends paid	(630)	(431)
Interest paid on borrowings	(383)	(376)
Net cash from financing activities	135	16
Net increase in cash and cash equivalents	135	16
Cash and cash equivalents at 1 January	17	1
Cash and cash equivalents at 31 December	152	17

Where applicable, the accounting policies of the Company are the same as those of the Group on pages 148 to 159. The notes identified alphabetically on pages 270 to 272 are an integral part of these separate financial statements. Where the same items appear in the Group financial statements, reference is made to the notes (identified numerically) on pages 168 to 266.

Notes to the Company's financial statements

A – Presentation changes

During 2012, the Company reviewed the presentation of its investment in its subsidiary General Accident plc ('GA') which was previously shown net of an intercompany liability in the statement of financial position and determined that the investment should be presented gross of the intercompany liability. The result of this has been to increase the value of investments in subsidiaries at 31 December 2011 by £13,659 million, intercompany loan liabilities by £13,919 million, and the investment valuation reserve by £260 million. The value of investments in subsidiaries at 31 December 2010 has been restated by £13,661 million, intercompany loan liabilities by £13,919 million, and the investment valuation reserve by £258 million.

B – Investments in subsidiaries

(i) Movements in the Company's investments in its subsidiaries are as follows:

	2012 £m	Restated 2011 £m	Restated 2010 £m
Fair value as at 1 January	28,889	31,284	30,897
Movement in fair value	2,134	(2,395)	387
At 31 December	31,023	28,889	31,284

Fair values are estimated using applicable valuation models underpinned by the Company's market capitalisation, and are classified as Level 2 in the fair value hierarchy described in note 22 to the Group consolidated financial statements.

(ii) At 31 December 2012, the Company has two wholly owned subsidiaries, both incorporated in the UK. These are General Accident plc and Aviva Group Holdings Limited. Aviva Group Holdings Limited is an intermediate holding company, whilst General Accident plc no longer carries out this function. The principal subsidiaries of the Aviva Group at 31 December 2012 are listed on pages 48 and 49.

C – Tax

(i) Tax credited to equity

Tax credited to equity comprises £18 million (2011: £16 million) in respect of coupon payments on the direct capital instruments and fixed rate tier 1 notes.

(ii) Deferred tax

A deferred tax asset of £180 million has been recognised in the Company at 31 December 2012 at 23% (2011: £nil). As announced in the 2012 Autumn Statement, the rate is expected to reduce further to 21% from 1 April 2014 and this would reduce the deferred tax asset to £164 million. The Company has gross unrecognised tax losses of £nil (2011: £296 million) and other temporary differences of £50 million (2011: £245 million).

(iii) Current tax assets

Amounts due in respect of current tax assets are expected to be recovered in more than 12 months.

D – Reserves

	Merger reserve £m	Investment valuation reserve £m	Equity compen- sation reserve £m	Retained earnings £m
Balance at 1 January 2011 Restated	735	6,803	99	3,331
Arising in the year:				
Profit for the year	—	—	—	231
Fair value losses on investments in subsidiaries and joint ventures	—	(2,389)	—	—
Actuarial gains on pension provisions	—	—	—	1
Dividends and appropriations	—	—	—	(813)
Reserves credit for equity compensation plans	—	—	48	—
Shares issued in lieu of dividends	—	—	—	307
Trust shares distributed in the year	—	—	—	(18)
Issue of share capital under equity compensation scheme	—	—	(61)	61
Aggregate tax effect	—	—	—	16
Balance at 31 December 2011 Restated	735	4,414	86	3,116
Arising in the year:				
Profit for the year	—	—	—	616
Fair value gains on investments in subsidiaries and joint ventures	—	2,126	—	—
Impairment losses on assets previously revalued through other comprehensive income now taken to the income statement	—	254	—	—
Dividends and appropriations	—	—	—	(847)
Reserves credit for equity compensation plans	—	—	42	—
Shares issued in lieu of dividends	—	—	—	127
Trust shares distributed in the year	—	—	—	(44)
Issue of share capital under equity compensation scheme	—	—	(68)	74
Aggregate tax effect	—	—	—	18
Balance at 31 December 2012	735	6,794	60	3,060

Tax of £18 million (2011: £16 million) is deductible in respect of coupon payments of £73 million (2011: £58 million) on the direct capital instruments and fixed rate tier 1 notes.

E – Borrowings

The Company's borrowings comprise:

	2012 £m	2011 £m
Subordinated debt	4,337	4,582
9.5% guaranteed bonds 2016	199	199
Commercial paper	603	506
Total	5,139	5,287

Maturity analysis of contractual undiscounted cash flows:

	2012			2011		
	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m
Within 1 year	603	307	910	506	314	820
1 to 5 years	200	1,197	1,397	200	1,244	1,444
5 to 10 years	241	1,342	1,583	435	1,404	1,839
10 to 15 years	527	1,192	1,719	543	1,240	1,783
Over 15 years	3,608	2,610	6,218	3,643	2,859	6,502
Total contractual undiscounted cash flows	5,179	6,648	11,827	5,327	7,061	12,388

Where subordinated debt is undated, the interest payments have not been included beyond 15 years. Annual interest payments for these borrowings are £72 million (2011: £73 million).

The fair value of the subordinated debt at 31 December 2012 was £4,435 million (2011: £3,814 million). The fair value of the 9.5% guaranteed bonds 2016 at 31 December 2012 was £246 million (2011: £246 million). The fair value of the commercial paper is considered to be the same as its carrying value.

Further details of these borrowings and undrawn committed facilities can be found in the Group consolidated financial statements, note 48.

F – Contingent liabilities

Details of the Company's contingent liabilities are given in the Group consolidated financial statements, note 51(g).

G – Risk management

Risk management in the context of the Group is considered in the Group consolidated financial statements, note 56.

The business of the Company is managing its investments in subsidiary and joint venture operations. Its risks are considered to be the same as those in the operations themselves and full details of the major risks and the Group's approach to managing these are given in the Group consolidated financial statements, note 56. Such investments are held by the Company at fair value in accordance with accounting policy D.

The fair values of the subsidiaries and joint venture are estimated using applicable valuation models, underpinned by the Company's market capitalisation. This uses the Company's closing share price at year end. Given that the key input into the valuation model is based on an observable current share price, and therefore sensitive to movements in that price, the valuation process is not sensitive to non-observable market assumptions.

Financial assets, other than investments in subsidiaries and the joint venture, largely consist of amounts due from subsidiaries. As at the balance sheet date, these receivable amounts were neither past due nor impaired.

Financial liabilities owed by the Company as at the balance sheet date are largely in respect of borrowings (details of which are provided in note E and the Group consolidated financial statements, note 48) and loans owed to subsidiaries. Loans owed to subsidiaries were within agreed credit terms as at the balance sheet date.

Interest rate risk

Loans to and from subsidiaries are at either fixed or floating rates of interest, with the latter being exposed to fluctuations in these rates. The choice of rates is designed to match the characteristics of financial investments (which are also exposed to interest rate fluctuations) held in both the Company and the relevant subsidiary, to mitigate as far as possible each company's net exposure.

The majority of the Company's external borrowings are at fixed rates of interest and are therefore not exposed to changes in these rates. However, for those borrowings that are at floating rates, the Company is affected by changes in these rates. Further details of the Company's borrowings are provided in note E and the Group consolidated financial statements, note 48.

Currency risk

The Company's direct subsidiaries are exposed to foreign currency risk arising from fluctuations in exchange rates during the course of providing insurance and asset management services around the world. The exposure of the subsidiaries to currency risk is considered from a Group perspective in the Group consolidated financial statements, note 56.

The Company faces exposure to foreign currency risk through some of its borrowings which are denominated in Euros and US dollars. However, most of these borrowings have been on-lent to a subsidiary which holds investments in these currencies, generating the net investment hedge described in the Group consolidated financial statements, note 57(a)(iii).

H – Related party transactions

The Company receives dividend and interest income from subsidiaries and pays interest and fee expense to those subsidiaries in the normal course of business. These activities are reflected in the table below.

Loans to and from subsidiaries are made on normal arm's-length commercial terms. The maturity analysis of the related party loans is as follows:

Loans owed by subsidiaries

Maturity analysis	2012 £m	2011 £m
Within 1 year	1,240	—
1 to 5 years	446	1,749
Over 5 years	608	626
Total	2,294	2,375

Loans owed to subsidiaries

Maturity analysis of contractual undiscounted cash flows	2012			Restated 2011			Restated 2010		
	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m
Within 1 year	794	336	1,130	502	365	867	514	424	938
1 to 5 years	11,333	506	11,839	11,564	810	12,374	12,325	362	12,687
Over 5 years	1,820	83	1,903	1,742	128	1,870	1,742	180	1,922
Total	13,947	925	14,872	13,808	1,303	15,111	14,581	966	15,547

Other related party balances comprise dividends and interest receivable and payable, as well as inter-company balances for fees and other transactions in the normal course of business.

Dividends, loans, interest

Services provided to related parties

	2012		2011		2010	
	Income earned in year £m	Receivable at year end £m	Income earned in year £m	Receivable at year end £m	Income earned in year £m	Receivable at year end £m
Subsidiaries	1,692	5,313	1,211	4,655	1,260	5,436

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms. Details of guarantees, indemnities and warranties given by the Company on behalf of related parties are given in note 51(g).

Services provided by related parties

	2012		Restated 2011		Restated 2010	
	Expense incurred in year £m	Payable at year end £m	Expense incurred in year £m	Payable at year end £m	Expense incurred in year £m	Payable at year end £m
Subsidiaries	402	17,516	460	17,174	458	17,765

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

The directors and key management of the Company are considered to be the same as for the Group. Information on both the Company and Group key management compensation can be found in note 59.

I – Parent company income statement

The Company has not presented its own income statement as permitted by Section 408 of the Companies Act 2006. The profit for the year attributable to equity shareholders was £616 million (2011: £231 million), which included £1,585 million (2011: £1,068 million) dividend income from subsidiary companies.

J – Equity compensation plans

All transactions in the Group's equity compensation plans involve options and awards for ordinary shares of the Company. Full disclosure of these plans is given in the Group consolidated financial statements, note 30. The cost of such options and awards is borne by all participating businesses and, where relevant, the Company bears an appropriate charge. As the majority of the charge to the Company relates to directors' options and awards, for which full disclosure is made in the Directors' Remuneration Report, no further disclosure is given here on the grounds of materiality.

K – Subsequent event

On 21 January 2013 the Company provided a guarantee to its subsidiary, Aviva Group Holdings Limited, on a short term external borrowing of £200 million which will be repaid from disposal proceeds.

Other information

In this section

Glossary	274
Shareholder services	276

Product definitions

Annuities

A type of policy that pays out regular amounts of benefit, either immediately and for the remainder of a person's lifetime, or deferred to commence from a future date. Immediate annuities may be purchased for an individual and his or her dependants or on a bulk purchase basis for groups of people. Deferred annuities are accumulation contracts, which may be used to provide benefits in retirement, and may be guaranteed, unit-linked or index-linked.

Bonds and savings

These are accumulation products with single or regular premiums and unit-linked or guaranteed investment returns.

Critical illness cover

Pays out a lump sum if the insured person is diagnosed with a serious illness that meets the plan definition.

Deferred annuities

An annuity (or pension) due to be paid from a future date or when the policyholder reaches a specified age. A deferred annuity may be funded by a policyholder by payment of a series of regular contributions or by a capital sum.

Group pensions

A pension plan that covers a group of people, which is typically purchased by a company and offered to their employees.

Guaranteed annuities

A policy that pays out a fixed regular amount of benefit for a defined period.

Income drawdown

The policyholder can transfer money from any pension fund to an income drawdown plan from which they receive an income. The remainder of the pension fund continues to be invested, giving it the potential for growth.

Investment sales

Comprise retail sales of mutual fund-type products such as unit trusts, individual savings accounts (ISAs) and open ended investment companies (OEICs).

ISAs

Individual savings accounts – Tax-efficient plans for investing in stocks and shares, cash deposits or life insurance investment funds, subject to certain limits.

Mortgage endowment

An insurance contract combining savings and protection elements which is designed to repay the principal of a loan or mortgage.

Mortgage life insurance

A protection contract designed to pay off the outstanding amount of a mortgage or loan in the event of death of the insured.

OEIC (Open ended investment company)

An collective investment fund structured as a limited company in which investors can buy and sell shares.

Pensions

A means of providing income in retirement for an individual and possibly his/her dependants.

Personal pensions

A pension plan tailored to the individual policyholder, which includes the options to stop, start or change their payments.

Protection

An insurance contract that protects the policyholder or his/her dependants against financial loss on death or ill-health.

Regular premium

A series of payments are made by the policyholder, typically monthly or annually, for part of or all of the duration of the contract.

SICAVs

This is an open-ended investment fund, structured as a legally independent joint stock company, whose units are issued in the form of shares.

Single premium

A single lump sum is paid by the policyholder at commencement of the contract.

Stakeholder pensions

Low cost and flexible pension plans available in the UK, governed by specific regulations.

Term assurance

A simple form of life insurance, offering cover over a fixed number of years during which a lump sum will be paid out if the life insured dies.

Unit trusts

A form of open ended collective investment constituted under a trust deed, in which investors can buy and sell units.

Unit-linked annuities

A type of deferred annuity which is invested in units of investment funds, whose value depends directly on the market value of assets in those funds.

Whole life

A protection policy that remains in force for the insured's whole life. Traditional whole life contracts have fixed premium payments that typically cannot be missed without lapsing the policy. Flexible whole life contracts allow the policyholder to vary the premium and/or amount of life cover, within certain limits.

With-profits

A type of long-term savings and insurance product sold in the UK under with profits policies premiums are paid into a separate fund. Policyholders receive a return on their policies through bonuses, which "smooth" the investment return from the assets which premiums are invested in. Bonuses are declared on an annual and terminal basis. Shareholders have a participating interest in the with-profit funds and any declared bonuses. Generally, policyholder and shareholder participation in with-profit funds in the UK is split 90:10.

General terms**Available for sale (AFS)**

Securities that have been acquired neither for short-term sale nor to be held to maturity. These are shown at fair value on the statement of financial position and changes in value are taken straight to equity instead of the income statement.

Association of British Insurers (ABI)

A major trade association for UK insurance companies, established in July 1985.

Acquired value of in force (AVIF)

The present value of future profits on a portfolio of long-term insurance and investment contracts, acquired either directly or through the purchase of a subsidiary.

Bancassurance

An arrangement whereby banks and building societies sell insurance and investment products to their customers on behalf of other financial providers.

UK Corporate Governance Code

The code sets out guidance in the form of principles and provisions on how companies should be directed and controlled to follow good governance practice.

Deferred acquisition costs (DAC)

The costs directly attributable to the acquisition of new business for insurance and investment contracts may be deferred to the extent that they are expected to be recoverable out of future margins in revenue on these contracts.

Fair value

The amount for which an asset can be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

FSA

The UK's Financial Services Authority – Main regulatory body appointed by the government to oversee financial services industry in the UK. Since December 2001 it has been the single statutory regulator responsible for savings, insurance and investment business. From 1 April 2013, the FSA will split into two new regulatory bodies: the Prudential Regulation Authority (PRA), which will be a subsidiary of the Bank of England, and the Financial Conduct Authority (FCA).

Funds under management

Represents all assets actively managed or administered by or on behalf of the Group including those funds managed by third parties.

Funds under management by Aviva

Represents all assets actively managed or administered by the fund management operations of the Group.

General insurance

Also known as non-life or property and casualty insurance. Property insurance covers loss or damage through fire, theft, flood, storms and other specified risks. Casualty insurance primarily covers losses arising from accidents that cause injury to other people or damage the property of others.

Gross written premiums

The total earnings or revenue generated by sales of insurance products, before any reinsurance is taken into account. Not all premiums written will necessarily be treated as income in the current financial year, because some of them could relate to insurance cover for a subsequent period.

Independent Financial Advisers (IFAs)

A person or organisation authorised to give advice on financial matters and to sell the products of all financial service providers.

IFRS

International Financial Reporting Standards. These are accounting regulations designed to ensure comparable statement of financial position preparation and disclosure, and are the standards that all publicly listed companies in the European Union are required to use.

Operating profit

From continuing operations based on expected investment returns, stated before tax attributable to shareholders' profits and before non-operating items including, impairment of goodwill, exceptional and other items. This is also referred to as adjusted operating profit.

Inherited estate

In the UK, the assets of the long-term with-profit funds less the realistic reserves for non-profit policies written within the with-profit funds, less asset shares aggregated across the with-profit policies and any additional amounts expected at the valuation date to be paid to in-force policyholders in the future in respect of smoothing costs and guarantees.

Long-term and savings business

Collective term for life insurance, pensions, savings, investments and related business.

Net written premiums

Total gross written premiums for the given period, minus premiums paid over or 'ceded' to reinsurers.

Net asset value per ordinary share

Net asset value divided by the number of ordinary shares in issue. Net asset value is based on equity shareholders' funds.

Present value of new business (PVNBP)

Present value of new regular premiums plus 100% of single premiums, calculated using assumptions consistent with those used to determine the value of new business under Market Consistent Embedded Value (MCEV) principles published by the CFO Forum.

Turnbull Guidance on Internal Control

The Turnbull Guidance sets out best practice on internal controls for UK listed companies, and provides additional guidance in applying certain sections of the UK Corporate Governance Code.

Shareholder profile as at 31 December 2012

By category of shareholder	Number of shareholders	%*	Number of shares	%*
Individual	571,901	96.89	278,168,612	9.44
Banks and nominee companies	15,334	2.60	2,614,092,081	88.73
Pension fund managers and insurance companies	239	0.04	2,788,904	0.09
Other corporate bodies	2,771	0.47	50,922,664	1.73
Total	590,245	100	2,945,972,261	100

By size of shareholding	Number of shareholders	%*	Number of shares	%*
1–1,000	532,678	90.25	148,707,650	5.05
1,001–5,000	51,069	8.65	97,672,281	3.32
5,001–10,000	3,605	0.61	25,063,113	0.85
10,001–250,000	2,304	0.39	97,703,037	3.32
250,001–500,000	162	0.03	58,338,929	1.98
500,001 and above	426	0.07	2,498,907,051	84.82
American Depository Receipts (ADRs)	1	0.00	19,580,200*	0.66
Total	590,245	100	2,945,972,261	100

*The number of registered ordinary shares represented by ADRs. Please note that each Aviva ADR represents two (2) ordinary shares.

*Percentages do not necessarily add up due to rounding.

2013 financial calendar

Annual General Meeting	9 May 2013
Announcement of first quarter Interim Management Statement	16 May 2013
Announcement of unaudited half-year results	8 August 2013
Announcement of third quarter Interim Management Statement	7 November 2013

2012 final dividend dates – ordinary shares

Ex-dividend date	20 March 2013
Record date	22 March 2013
Dividend payment date*	17 May 2013

*Please note that the ADR local payment date will be approximately five business days after the proposed dividend date for ordinary shares.

Annual General Meeting (AGM)

- The 2013 AGM will be held at The Barbican Centre, Silk Street, London EC2Y 8DS on Thursday, 9 May 2013 at 11am.
- Details of each resolution to be considered at the meeting are provided in the Notice of AGM, which is available on the Company's website at www.aviva.com/agm.
- Shareholders can vote electronically at www.investorcentre.co.uk/eproxy, in person by attending the meeting, or by completing and returning the relevant voting card(s) by post.
- The voting results for the 2013 AGM will be accessible on the Company's website at www.aviva.com/agm shortly after the meeting.
- If you are unable to attend the AGM but would like to ask the directors a question in connection with the business of the meeting, you can do so by sending a question to the group company secretary by email to aviva.shareholders@aviva.com. We will endeavour to provide you with a response as soon as possible.

AGM voting instructions

- Completed proxy instructions must be submitted to the Company's Registrar, Computershare Investor Services PLC (Computershare), as soon as possible, but in any event to arrive by no later than:
 - 11am on Tuesday, 7 May 2013 for ordinary shareholders; and
 - 11am on Friday, 3 May 2013 for members of the Aviva Share Account and participants in the Aviva All Employee Share Ownership Plan.

Dividends

- Dividends on ordinary shares are normally paid in May and November - please see the table above for the key dates in respect of the 2012 final dividend.
- Dividends on preference shares are normally paid in March, June, September and December - please visit www.aviva.com/preferenceshares for the latest dividend payment dates.
- Holders of ordinary and preference shares will receive any dividends payable in sterling and holders of ADRs will receive any dividends payable in US dollars.

Direct credit of dividend payments

- If you would like to have your cash dividends paid directly into your bank or building society account, please visit www.aviva.com/dividendmandate for more information or contact Computershare using the contact details overleaf.

Overseas global dividend service

- The Global Payments Service provided by Computershare enables shareholders living overseas to elect to receive their dividends in a choice of over 65 international currencies. For further details and fees for this service please visit www.investorcentre.co.uk/faq and select the Dividends and Payments tab, followed by Global Payment Service.

Manage your holdings online

You can view and manage your shareholding online by visiting www.aviva.com/ecomms. To log in you will require your 11 digit Shareholder Reference Number (SRN), which you will find on your proxy or voting card, latest dividend stationery, or any share certificate issued since 4 July 2011.

Shareholders can also elect to receive electronic communications by registering their email address online, or by contacting Computershare directly. Making this election will save on printing and distribution costs and has environmental benefits.

Useful links for shareholders**Online Shareholder Services Centre**

www.aviva.com/shareholderservices

Dividend information for ordinary shares

www.aviva.com/dividends

Annual General Meeting information and Electronic Voting

www.aviva.com/agm

www.investorcentre.co.uk/eproxy

Aviva share price

www.aviva.com/shareprice

ADR holders

www.aviva.com/adr

Aviva preference shareholders

www.aviva.com/preferenceshares

Aviva preference share price

www.londonstockexchange.com

Aviva Annual Review

In response to shareholder feedback, we have reintroduced the Annual Review as an alternative to the full Annual Report and Accounts. The Annual Review provides a summary of Aviva's businesses and performance in an easier to read format, which many of our shareholders found useful in the past. You can find further information and view the Annual Review at www.aviva.com/reports. If you prefer to receive hard copy documents and would like to elect to receive a copy of the Annual Review instead of the full Annual Report and Accounts, please contact Computershare.

Contact details**Ordinary and preference shares – Computershare**

For any queries regarding your shareholding, or to advise of changes to your personal details, please contact our Registrar, Computershare:



By telephone: 0871 495 0105

Lines are open from 8.30am to 5pm (UK time), Monday to Friday (excluding public holidays).

Please call +44 117 378 8361 if calling from outside the UK.



By email: avivaSHARES@computershare.co.uk



In writing: Computershare Investor Services PLC

The Pavilions, Bridgwater Road, Bristol BS99 6ZZ

American Depositary Receipts (ADRs) – Citibank

For any queries regarding Aviva ADRs, please contact Citibank Shareholder Services (Citibank):



By telephone: 1 877 248 4237 (1 877-CITI-ADR), or

+1 781 575 4555 if you are calling from outside the US.

(Lines are open from 8.30am to 6.00pm, Monday to Friday US Eastern Standard Time).



By email: citibank@shareholders-online.com



In writing: Citibank Shareholder Services,

PO Box 43077, Providence, Rhode Island 02940-3077 USA

Please visit www.citi.com/dr for further information about Aviva's ADR programme.

Group Company Secretary

Shareholders may contact the group company secretary as follows:



By email: aviva.shareholders@aviva.com



In writing: Kirstine Cooper, Group Company Secretary

St Helen's, 1 Undershaft, London EC3P 3DQ



By telephone: +44 (0)20 7283 2000

Form 20-F

Aviva is a foreign private issuer in the United States of America and is subject to certain reporting requirements of the Securities Exchange Commission (SEC). Aviva files its Form 20-F with the SEC, copies of which can be found at www.aviva.com/reports.

Be on your guard – beware of fraudsters!

Shareholders are advised to be very wary of any unsolicited telephone calls or correspondence offering to buy shares at a discount or offering free financial advice or company reports. Boiler rooms use increasingly sophisticated means to approach investors and often leave their victims out of pocket. The Financial Services Authority (FSA) has found most share fraud victims are experienced investors who lose an average of £20,000. The FSA has provided tips on how to protect your savings which you can find at www.fsa.gov.uk/scams.

- Remember: if it sounds too good to be true, it probably is!
- Keep in mind that genuine companies are very unlikely to call you with an offer to buy or sell shares.
- If the caller persists, hang up.

For more information please visit the warning to shareholders page at: www.aviva.com/shareholderservices.

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www.aviva.com

Registered in England
Number 2468686