Legal and General Assurance Society

Solvency and Financial Condition Report

31.12.2016

Contents

Summary

This document

This Solvency and Financial Condition Report (SFCR) for Legal and General Assurance Society (the Company) is a regulatory document required under Solvency II[1]. All values are (unless otherwise stated) as at 31 December 2016.

Who we are

We are a wholly owned subsidiary of Legal & General Group Plc (the Group). We are a principal operating subsidiary of the Group and the regulated entity through which the vast majority of the Group's individual and group insurance, pensions, and annuities business is executed.

What we do

We enable our customers, who range from some of the world's largest companies and funds to millions of individuals and families, to manage their financial futures whether by protecting against unforeseen events, helping to save for and support retirement or investing money to deliver growth over time. We deploy our strong balance sheet, our ability to understand and pool risk, our market insight and our capacity to create good value customer propositions for every customer, large or small. Our strong social purpose means that we strive at all times to do the right thing not just for our customers and shareholders, but for the broader economy and society at large.

Our businesses

The business divisions that operate through the Company are Legal & General Retirement; Legal & General Investment Management; Legal & General Insurance; Legal & General Capital; General Insurance; and Savings. The with-profits fund is managed as a ring-fenced fund within the Company within the Savings division.

Our performance

We consider IFRS operating profit on the insurance and savings business to be a good measure of the business's underwriting performance. This is the key measure used to manage our business.

Operating profit measures the pre-tax result excluding the impact of short-term economic variances and exceptional items which arise outside the normal course of business in the period. Operating profit reflects longer-term economic assumptions and changes in insurance risks.

The key measures in our financial statements for the year ending 31 December 2016 were:

- IFRS Operating profit £756m
- IFRS Profit before tax £1,283m
- IFRS Profit for the period £884m
- Solvency II surplus of £4.4bn on a shareholder basis
- Solvency II coverage ratio of 162% on a shareholder basis
- Solvency II surplus of £4.1bn on a SFCR regulatory basis
- Solvency II coverage ratio of 154% on a SFCR regulatory basis

[1] Required by the Reporting and Group Supervision parts of the PRA Rulebook for Solvency II firms and Directive 2009/138/EC of the European Parliament (Solvency II Directive) Articles 51 and 256.

The Solvency II coverage ratio is the eligible Own Funds divided by the Solvency Capital Requirement (SCR).

In line with market practice, the shareholder basis excludes the contribution to SCR of the with-profits fund from both the Own Funds and SCR. These exclusions have no impact on the Solvency II surplus only the reported ratio.

The shareholder basis as disclosed in the full-year results in March 2017 incorporates the estimated impacts of a recalculation of the transitional measures for technical provisions (Estimated TMTP) based on 31 December 2016 economic conditions and changes during 2016 to the Internal Model and Matching Adjustment (MA). The Estimated TMTP was amortised to 31 December 2016. This is considered to be a more consistent and more appropriate disclosure for shareholders to judge the financial position and performance of the Company.

The conditions for the PRA to allow a formal recalculation of the Company's TMTP were not met as at 31 December 2016. The TMTP is designed to be recalculated every two years unless there are significant market movements or significant changes to a company's risk profile. In line with PRA guidance, we expect to undertake a formal recalculation of the TMTP on or before 1 January 2018, i.e. when PRA conditions are met or two years from the date of commencement of the Solvency II regime.

The regulatory basis uses a TMTP recalculated at 30 June 2016 when it was deemed that the interest rate movements were sufficiently significant to warrant recalculation, it does not allow for recalculation of the TMTP as at 31 December 2016, or the amortisation since the last recalculation of the TMTP in June 2016.

Further details on our business and performance can be found in section A. Business and performance.

Our governance

The role of the Board of Legal & General Group Plc is to lead the Group and oversee the governance of the Group. It plays a key role in ensuring that the tone for the Group's culture and values is set from the top. The role of management is to deliver the strategy within the framework and standards set by the Group Board.

The separate Board of Legal and General Assurance Society Limited is accountable for the long-term success of the Company by setting the Company's strategic objectives, monitoring performance against those objectives and directly overseeing the business activities undertaken by the Company, whilst operating within the framework and overall strategy defined by the Group Board. The Board of the Company comprises the Group Chief Executive, Group Chief Financial Officer and two independent non-executive directors.

Risk management framework

Our risk framework is designed to enable the Company Board to draw assurance that risks are being appropriately identified and managed in line with our risk appetite.

Our framework seeks to reinforce the parameters of acceptable risk taking, allowing business managers to make decisions that are consistent with our risk appetite.

We deploy a 'three lines of defence' risk governance model, whereby business divisions are responsible for risk taking within the parameters of our risk appetite and accountable for managing risks in line with our risk policies; risk functions led by the Chief Risk Officer provide objective challenge and guidance on risk matters; with Group Internal Audit providing independent assurance on the effectiveness of business risk management and the overall operation of the risk framework. The core elements of our risk framework are set out below.

Risk appetite

The Company's risk appetite is set by the Company's Board. The Company's risk appetite is set with regards to, but not limited by, the Group Board. The Group Board's Risk Committee leads an annual review of the Group's risk appetite, assessing the continued appropriateness of our key measures and tolerances relative to the risk exposures of the Group. Additionally, as part of the annual planning cycle, assessment is made of the level of risk taking proposed in the plan and the capacity for risk taking within the overall appetite framework.

We cascade the parameters of our risk appetite to our business managers through 'Risk and Capital Mandates', empowering managers to make decisions that are consistent with our appetite for risk.

The Company Board oversees the business objectives of the Company within the risk appetite.

Risk policies

We set formal policies for the management of market, insurance, credit, liquidity and operational risks. The policies specify our overall strategies for ensuring each risk type is managed in line with our risk appetite and the minimum control standards that should be applied in managing our significant risk exposures.

Risk identification and assessment

Review process

We operate a risk identification and assessment process under which all our businesses regularly consider changes in the profile of existing and emerging risks. The assessment process evaluates the risks that are inherent in our products as well as those that are presented from changes in the environments that we operate in.

Scenario planning

We undertake scenario analysis of emerging and uncertain future events to assess possible outcomes and to develop proactive management responses.

Own risk and solvency assessment (ORSA)

Our risk identification and assessment process forms part of our broader 'own risk and solvency assessment' process, our ongoing assessment of the risks to which the Company is exposed and an evaluation of the sufficiency of resources to sustain the business strategy over the horizon of the Company's plan.

Risk management information

Our risk management information framework is structured to report and support the review of ongoing and emerging risks and assess actual risk positions relative to the risk limits and targets that we set.

Risk oversight

The Group Chief Risk Officer (who is also the Chief Risk Officer of the Company) and his team, who are independent of the business line, support the Group Board and its Risk Committee as well as the Company Board in articulating acceptable risk taking and ensuring the effective operation of our risk and capital framework. This includes ongoing assessment of the Group and the Company's capital requirements to confirm that they meet regulatory solvency requirements.

The Group Chief Risk Officer also provides objective challenge and guidance on a range of risk matters to business managers, including the risks implicit in product developments, business transactions and new asset classes, and strategies for managing risks in line with the Company's overall risk appetite.

Risk committees

The Company operates within the Group's risk management framework. The Company's Board has ultimate responsibility for ensuring that the Group's risk management framework is appropriate for the Company.

The Group Board's Risk Committee supported by the Group Chief Risk Officer, serves as the focal point for risk management activities. Beneath the Group Risk Committee is a structure of formal risk oversight committees providing more focused review and challenge of specific risks to the Group and Company, and reviewing the effectiveness of frameworks in place to manage those risks.

Further details on our systems of governance can be found in section B. Systems of governance.

Our risk profile

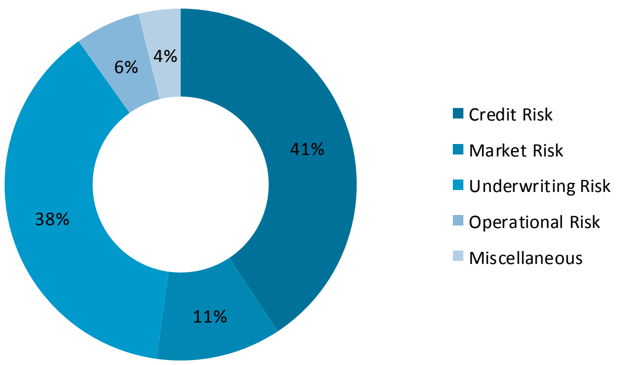
We are exposed to:

- longevity, mortality, morbidity and household insurance risks transferred to us by customers of our annuities, protection and general insurance businesses;
- investment risks, from holding portfolios of assets to meet our obligations to our customers and to deliver returns to shareholders; and
- operational risks, in respect of our business processes and IT systems, as well as broader regulatory and legislative risks that can arise in the environments in which we operate.

Our risk-based capital model

We assess on an ongoing basis the capital that we need to hold above our liabilities to meet the Company's strategic objectives and ensure continued solvency.

Our risk-based capital model seeks to provide a quantitative assessment of the Company's risk exposures. Our model forms part of the suite of tools that we use to evaluate our strategic plans, set risk appetite, allocate capital and evaluate product pricing. We also use our capital model to assess significant transactions, including large pension risk transfer deals. We calibrate our model to ensure that we hold sufficient capital to survive our assessment of a worse case 1-in-200 year event. In terms of capital requirement, credit and insurance (longevity) risks remain our most significant risks. Market risk, which includes equity, property and interest rate risks, is another material risk for which we hold capital. One of the uses of our model is to calculate our regulatory capital requirement. We have chosen to adopt a partial internal model (the Internal Model) approach to calculate the Solvency Capital Requirement (SCR) for all of the material insurance companies in the Group, including the Company. Our SCR by major risk category is shown in the chart below.



Further details on our risk profile can be found in section C. Risk profile.

Valuation for Solvency purposes

The Solvency II valuation of assets is £128bn. These are valued in line with the Solvency II definitions, and are generally consistent with the accounting fair value valuation. Assets include expected recoveries from reinsurance contracts. These are calculated consistently with the technical provisions that the Company holds to meet future policyholder liabilities. Further details can be found in Section D.1 Assets.

The Solvency II valuation for total liabilities is £116.2bn. The main component of liabilities is the technical provisions (TPs) of £103.8bn. The TPs are calculated as the sum of the best estimate liabilities (BEL) of £104.0bn and the risk margin (RM) of £5.7bn less the TMTP of £6.0bn; calculated in line with PRA approvals and allowing for the change in capital requirements from the old Solvency I regime.

The BEL represents our best estimate of future cash flows on the in-force business as at 31 December 2016. The BEL is calculated without any deductions for the amounts recoverable from reinsurance contracts. Where the PRA has granted approval for the use of a matching adjustment (MA) when calculating the BEL, this has been applied in line with the approved application. Further details can be found in Section D.2 Technical provisions.

Solvency II balance sheet

The Company is required to measure and monitor its capital resources on a regulatory basis. Following the implementation of the Solvency II regulatory regime which came into force on 1 January 2016, the Company's capital resources are managed on a Solvency II basis, as adopted by the Prudential Regulation Authority (PRA) at the balance sheet date.

Our SCR is £7.5bn. The SCR has been calculated in line with the approved Internal Model and there is no capital subject to regulatory approval. Further details can be found in Section E.2 Solvency Capital Requirement and Minimum Capital Requirement.

As at 31 December 2016 the Company held £4.1bn of Own Funds in excess of the Company's regulatory solvency requirements, a capital coverage ratio of 154%. This buffer of capital resources over the regulatory requirement ensures that we're able to still meet our insurance obligations after a 1-in-200 year event. In line with our risk management approach, we maintained an appropriate capital buffer throughout the year.

The Company's Own Funds are described below.

2016 (£m)	
Solvency II Own Funds	**11,630**
Solvency capital requirement	**(7,544)**
Solvency II surplus	**4,086**
Regulatory capital coverage ratio	**154%**
Impact of six months amortisation of TMTP to 1 January 2017	(2)%
Impact of recalculation of TMTP	6%
Impact of exclusion of the contribution to SCR of with-profits fund	4%
Shareholder basis capital coverage ratio	**162%**

Additional information on the regulatory Solvency II coverage ratio can be found in Section E. Capital management.

Any other information

The sale of Legal & General Nederland Levensversekering Maatschappij (Legal & General Netherlands) to Chesnara Plc (Chesnara) for €161 million was completed in April 2017. Legal & General Netherlands is therefore included in the figures shown in the Company's SFCR.

The sale of the Legal & General Netherlands has marginally improved the Company's coverage ratio by c.1% through a net increase to Solvency II surplus.

Directors' certificate

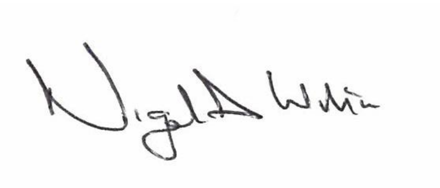
Legal & General Group – financial year ended 31 December 2016

The Directors acknowledge their responsibility for the proper preparation of the SFCR in all material respects with the PRA rules and Solvency II Regulations.

The Board is satisfied that to the best of its knowledge and belief:

(a) throughout the financial year to 31 December 2016, the firm has complied in all material respects with the requirements of the PRA rules and Solvency II Regulations as applicable to the firm; and

(b) it is reasonable to believe that in respect of the period from 31 December 2016 to the date of the publication of the SFCR, the firm has continued so to comply and that it will continue so to comply for the remainder of the financial year to 31 December 2017.



Nigel Wilson

Chief Executive Officer

18 May 2017

Auditors' report

Legal and General Assurance Society Limited – financial year ended 31 December 2016

Report of the external independent auditors to the Directors of Legal & General Assurance Society Limited ('the Company') pursuant to Rule 4.1 (2) of the External Audit Part of the PRA Rulebook applicable to Solvency II firms

Report on the Audit of the relevant elements of the Solvency and Financial Condition Report

Opinion

Except as stated below, we have audited the following documents prepared by the Company as at 31 December 2016:

- The 'Valuation for solvency purposes' and 'Capital Management' sections of the Solvency and Financial Condition Report of the Company as at 31 December 2016 ('**the Narrative Disclosures subject to audit**'); and

- Company templates S.02.01.02, S.12.01.02, S.17.01.02, S.22.01.21, S.23.01.01 and S.28.02.01 ('**the Templates subject to audit'**).

The Narrative Disclosures subject to audit and the Templates subject to audit are collectively referred to as the '**relevant elements of the Solvency and Financial Condition Report'**.

We are not required to audit, nor have we audited, and as a consequence do not express an opinion on the **Other Information** which comprises:

- Information contained within the relevant elements of the Solvency and Financial Condition Report set out above which are, or derive from the Solvency Capital Requirement, as identified in the Appendix to this report;

- The 'Summary', the 'Business and performance', 'System of governance' and 'Risk profile' elements of the Solvency and Financial Condition Report;

- Company templates S05.01.02, S05.02.01, S.19.01.21 and S.25.02.21;

- Information calculated in accordance with the previous regime used in the calculation of the transitional measure on technical provisions, and as a consequence all information relating to the transitional measure on technical provisions as set out in the Appendix to this report;

- The written acknowledgement by management of their responsibilities, including for the preparation of the Solvency and Financial Condition Report ('**the Responsibility Statement**').

To the extent the information subject to audit in the relevant elements of the Solvency and Financial Condition Report includes amounts that are totals, sub-totals or calculations derived from the Other Information, we have relied without verification on the Other Information.

In our opinion, the information subject to audit in the relevant elements of the Solvency and Financial Condition Report of the Company as at 31 December 2016 is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based, as modified by relevant supervisory modifications, and as supplemented by supervisory approvals and determinations.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & I)), International Standard on Auditing (UK) 800 and International Standard on Auditing (UK) 805, and applicable law. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report* section of our report.

Emphasis of Matter - Basis of Accounting

We draw attention to the 'Valuation for solvency purposes', 'Capital Management' and other relevant disclosures sections, such as the report summary, of the Solvency and Financial Condition Report, which describe the basis of accounting. The Solvency and Financial Condition Report is prepared in compliance with the financial reporting provisions of the PRA Rules and Solvency II regulations, and therefore in accordance with a special purpose financial reporting framework. The Solvency and Financial Condition Report is required to be published, and intended users include but are not limited to the Prudential Regulation Authority. As a result, the Solvency and Financial Condition Report may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

Responsibilities of Directors for the Solvency and Financial Condition Report

The Directors are responsible for the preparation of the Solvency and Financial Condition Report in accordance with the financial reporting provisions of the PRA rules and Solvency II regulations, which have been modified by the modifications, and supplemented by the approvals and determinations made by the PRA under section 138A of FSMA, the PRA Rules and Solvency II regulations on which they are based, as detailed below:

Approval to use a Transitional Measure on Technical Provisions

Approval to use the transitional measure on technical provisions recalculated as at 31 December 2016

Approval to use an internal model and the approval of subsequent major changes thereto

Approval to omit template NS.07 and include immaterial non-life business in NS.06

The Directors are also responsible for such internal control as they determine is necessary to enable the preparation of a Solvency and Financial Condition Report that is free from material misstatement, whether due to fraud or error.

Auditors' Responsibilities for the Audit of the relevant elements of the Solvency and Financial Condition Report

It is our responsibility to form an independent opinion, in accordance with applicable law, ISAs (UK & I) and ISAs (UK) 800 and 805 as to whether the information subject to audit in the relevant elements of the Solvency and Financial Condition Report is prepared, in all material respects, in accordance with the financial reporting provisions of the PRA Rules and Solvency II regulations on which they are based. ISAs (UK & I) require us to comply with the Auditing Practices Board's Ethical Standard for Auditors

An audit involves obtaining evidence about the amounts and disclosures in the relevant elements of the Solvency and Financial Condition Report sufficient to give reasonable assurance that the relevant elements of the Solvency and Financial Condition Report are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the relevant elements of the Solvency and Financial Condition Report. In addition, we read all the financial and non-financial information in the Solvency and Financial Condition Report to identify material inconsistencies with the audited relevant elements of the Solvency and Financial Condition Report. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

This report, including the opinion, has been prepared for the Directors of the Company to comply with their obligations under External Audit rule 2.1 of the Solvency II firms Sector of the PRA Rulebook and for no other purpose. We do not, in providing this report, accept or assume responsibility for any other purpose save where expressly agreed by our prior consent in writing.

Other Matter

The Company has authority to calculate its Solvency Capital Requirement using partial internal model (‘the Model‘) approved by the Prudential Regulation Authority in accordance with the Solvency II Regulations. In forming our opinion (and in accordance with PRA Rules), we are not required to audit the inputs to, design of, operating effectiveness of and outputs from the Model, or whether the Model is being applied in accordance with the Company's application or approval order.

Report on Other Legal and Regulatory Requirements

In accordance with Rule 4.1 (3) of the External Audit Part of the PRA Rulebook for Solvency II firms we are required to read the Other Information and consider whether it is materially inconsistent with the relevant elements of the Solvency and Financial Condition Report and our knowledge obtained in the audits of the Solvency and Financial Condition Report and of the Company’s statutory financial statements. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP

Chartered Accountants

7 More London Riverside

London

SE1 2RT

18 May 2017

- The maintenance and integrity of the Legal & General 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 Solvency and Financial Condition Report since it was initially presented on the website.
- Legislation in the United Kingdom governing the preparation and dissemination of Solvency and Financial Condition Reports may differ from legislation in other jurisdictions.

Appendix – relevant elements of the Solvency and Financial Condition Report that are not subject to audit

The relevant elements of the Solvency and Financial Condition Report that are not subject to audit comprise:

- The following elements of template S.02.01.02:
  - Row R0550: Technical provisions - non-life (excluding health) - risk margin
  - Row R0590: Technical provisions - health (similar to non-life) - risk margin
  - Row R0640: Technical provisions - health (similar to life) - risk margin
  - Row R0680: Technical provisions - life (excluding health and index-linked and unit-linked) - risk margin
  - Row R0720: Technical provisions - Index-linked and unit-linked - risk margin

- The following elements of template S.12.01.02
  - Row R0100: Technical provisions calculated as a sum of BE and RM - Risk margin
  - Rows R0110 to R0130 – Amount of transitional measure on technical provisions

- The following elements of template S.17.01.02
  - Row R0280: Technical provisions calculated as a sum of BE and RM - Risk margin
  - Rows R0290 to R0310 – Amount of transitional measure on technical provisions

- The following elements of template S.22.01.21
  - Column C0030 – Impact of transitional on technical provisions
  - Row R0010 – Technical provisions
  - Row R0090 – Solvency Capital Requirement

- The following elements of template S.23.01.01
  - Row R0580: SCR
  - Row R0740: Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds

- The following elements of Company template S.28.02.01
  - Row R0310: SCR

- Elements of the Narrative Disclosures subject to audit identified as ‘unaudited’

A. Business and performance

A.1 Business

A.1.1 Company details

This report is prepared in respect of Legal and General Assurance Society Limited (the Company) for the financial year ended 31 December 2016.

The Company	Legal and General Assurance Society Limited One Coleman Street London EC2R 5AA
The ultimate parent entity	Legal & General Group Plc One Coleman Street London EC2R 5AA
The supervisory authority responsible for financial supervision	Prudential Regulation Authority 20 Moorgate London EC2R 6DA
The external auditor	PriceWaterhouseCoopers LLP 7 More London Riverside London SE1 2RT

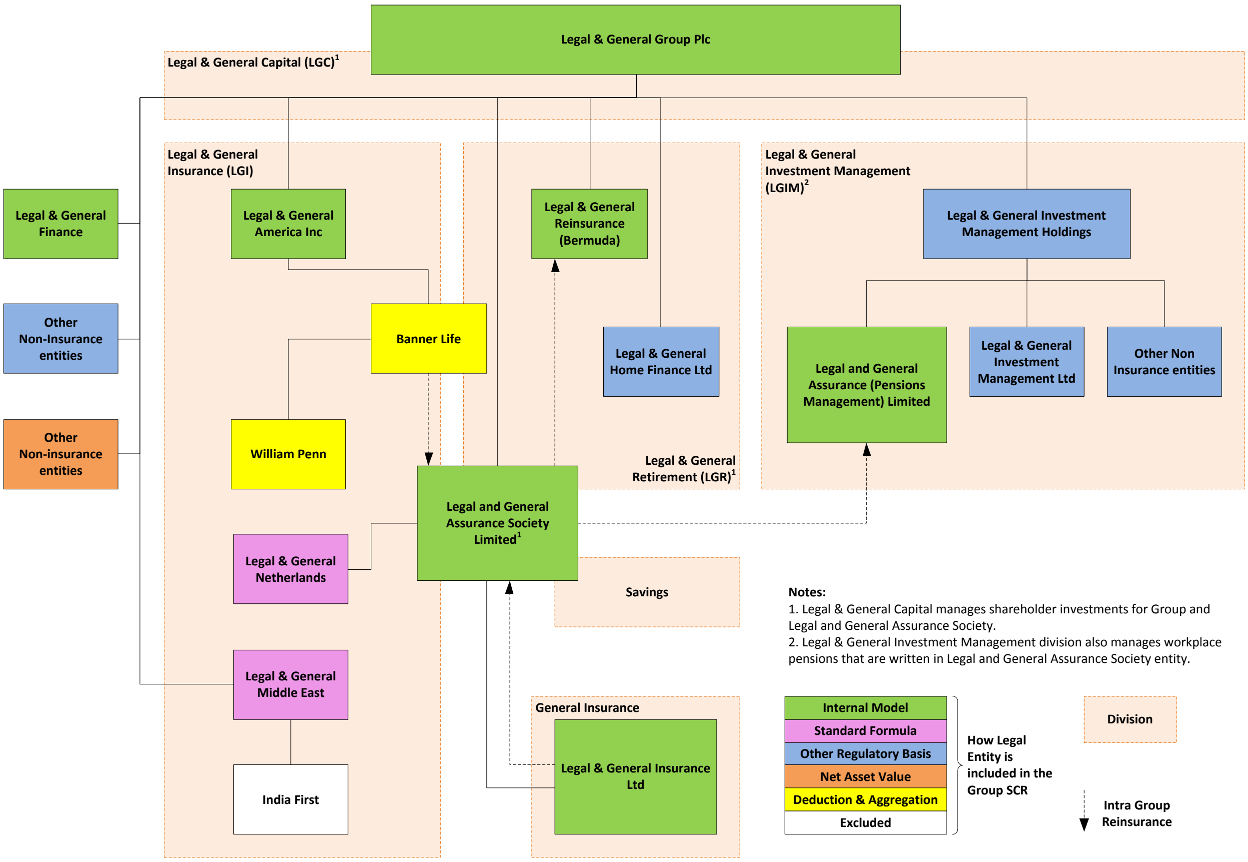
A.1.1.1 Qualified holdings

Legal and General Assurance Society Limited is wholly owned by Legal & General Group Plc (the Group).

A.1.1.2 Group structure

A simplified group structure is shown in Diagram 1 below. The chart summarises the relationship between entity and divisional responsibilities (on a forward-looking basis), further details of the principal products written by each division is provided in A.1.2 below. The Company is a principal operating subsidiary of the Group and is the regulated entity through which the vast majority of the Group's individual and group insurance, pensions and annuities business is executed.

Diagram 1: Division and entity overview



A.1.2 Material related undertakings

The particulars of the Company's subsidiaries as at 31 December 2016 are listed in Note 36 of the Company's financial statements. The material insurance undertakings are summarised below:

Company name	Country	Proportion of ownership held within the Group as at 31 December 2016
Legal & General Insurance Ltd (LGIL)	England & Wales	100%
Legal & General Nederland Levensversekering Maatschappij NV (LGN)[1]	Netherlands	100%

1. The sale of LGN to Chesnara Plc was completed on 6 April 2017. As at the reporting date LGN was held via Legal & General International holdings Limited, a wholly owned subsidiary of the Company.

The proportion of voting rights is the same as the ownership held for each of the entities listed above.

A.1.3 Principal products

A significant part of the Company's business involves the acceptance and management of risk.

A description of the principal products offered by the Company is outlined below. The Company seeks to manage its exposure to risk through control techniques which ensure that the residual exposures are within acceptable tolerances agreed by the Board. The Company's risk appetite framework and the methods used to monitor risk exposures can be found in sections B. Systems of governance and C. Risk profile.

Details of the risks associated with the Company's principal products and the control techniques used to manage these risks can be found in Section C. Risk profile.

A.1.3.1 Legal & General Retirement (LGR)

LGR business comprises pension risk transfers including bulk annuities and longevity insurance, and retail annuity business.

Annuities

Annuity products provide guaranteed income for a specified time, usually the life of the policyholder, in exchange for a lump sum capital payment. Immediate and deferred annuity contracts are offered. Immediate annuities provide a regular income stream to the policyholder, purchased with a lump sum investment, where the income stream starts immediately after the purchase. The income stream from a deferred annuity is delayed until a specified future date. Bulk annuities are also offered, where the Company accepts the assets and liabilities of a company pension scheme or a life fund, predominantly to UK clients, but also for US, and Irish clients. A small portfolio of immediate annuities has been written as participating business.

The Company also offers products for individuals that provide a guaranteed level of income over a chosen fixed period of time, in exchange for an initial lump sum payment from the policyholder. The products can provide a fixed lump sum at maturity and/or options to surrender on non-guaranteed terms.

The Company has written some deferred annuity contracts with guaranteed minimum pensions. These options expose the Company to interest rate and longevity risk as the cost would be expected to increase with decreasing interest rates and improved longevity.

Longevity insurance contracts

The Company also provides longevity insurance products for company pension schemes, under which regular payments are made to the scheme reflecting their actual longevity experience, while the scheme makes an agreed set of regular payments in return. Some policies contain a guaranteed surrender value. The value of these guarantees is currently immaterial.

Intragroup reinsurance arrangements

The Company accepts reinsurance from Banner Life Insurance Company, a subsidiary of Legal & General Group Plc. The reinsurance covers one pension risk transfer contract.

A.1.3.2 Legal & General Insurance (LGI)

LGI business comprises UK retail and group protection, and intragroup reinsurance.

UK Protection business (retail and group)

The Company offers protection products which provide mortality or morbidity benefits. They may include health, disability, critical illness and accident benefits; these additional benefits are commonly provided as supplements to main life policies but can also be sold separately. The benefit amounts would usually be specified in the policy terms. Some sickness benefits cover the policyholder's mortgage repayments and are linked to the prevailing mortgage interest rates. In addition to these benefits, some contracts may guarantee premium rates, provide guaranteed insurability benefits and offer policyholders conversion options.

Intragroup reinsurance arrangements

The Company accepts reinsurance from Banner Life Insurance Company and William Penn Life Insurance Company of New York, subsidiaries of Legal & General Group Plc. The reinsurance covers both individual term assurance which provides death benefits, and universal life contracts which provide savings and death benefits. In addition the Company accepts a tranche of the weather catastrophe risk reinsurance placed by Legal & General Insurance Limited.

A.1.3.3 Legal & General Investment Management (LGIM)

LGIM manages workplace pensions written in the Company.

Workplace savings

Workplace savings are a range of workplace pension solutions, focusing on the UK auto enrolment schemes. These schemes offer a wide choice of investment options, including a self-investment option.

A.1.3.4 Savings

A range of contracts are offered in a variety of different forms to meet customers' long-term savings objectives. Policyholders may choose to include a number of protection benefits within their savings contracts. The majority of the Savings products are closed to new business.

With-profits

With-profits products are only written in the with-profits fund, a ring-fenced sub fund within the Company. The with-profits fund ceased writing new business on 31 January 2015. Only increases to existing pension policies and new members to existing group Personal Pension Schemes, where allowed for in the policy terms and conditions, have been accepted after that date.

A.1.4 Significant business or other events

There were no significant business or other events over the reporting period.

A.2 Underwriting performance

We consider the IFRS operating profit on insurance and savings business to be a good measure of the business's underwriting performance. This is the key group metric used to manage our business.

Operating profit measures the pre-tax result excluding the impact of investment volatility, economic assumption changes and exceptional items and includes expected investment return. Operating profit therefore reflects longer-term economic assumptions and changes in insurance risks such as mortality and longevity for the Company's insurance business and shareholder funds.

The Company's operating profit is presented in the following sections. Information on premiums, claims and changes in technical provisions, which can be considered as key elements of underwriting performance, is presented by Solvency II line of business in QRT S.05.01 in Annex 1 of this report.

Over 90% of the business written by the Company is within the UK.

A.2.1 Operating profit by division

The table below shows the operating profit for the Company. This reflects the Company's contribution to the Group operating profit reported in the Group consolidated report and accounts. These results are on an IFRS basis.

(£m)	2016
From continuing operations	
Legal & General Retirement (LGR)	**677**
Legal & General Insurance (LGI)	**43**
General Insurance	**8**
Savings & LGIM	**28**
Operating profit from divisions	**756**

LGR achieved record operating profits of £677m driven by strong performance from our front and back books, as well as benefitting from higher levels of longevity reinsurance on new business. Longevity experience in the year was once again positive compared to our assumptions. Despite this outcome, forward-looking longevity reserves have not been materially changed.

LGI operating profit reflects a lower expected release from the UK retail protection back book, and adverse claims experience primarily in group protection. The LGI operating profit includes the impact of a number of intragroup reinsurance arrangements between the Company and the US insurance business. For 2016 these arrangements reduced the operating profit for the Company. This reduction was primarily driven by adverse experience, and treaty and modelling changes.

The Workplace Pensions business continues to grow its assets under administration from £14.7bn in 2015 to £20.7bn and its customer base from 1.8m to 2.1m.

The Company's Savings net outflows improved year-on-year due to improved retention of the non-profit book and in the with-profits business, due to reducing maturity profiles, particularly on endowments.

A.3 Investment performance

The Company earns an investment return from holdings in financial instruments and property investments, held to back insurance and investment contracts on behalf of policyholders and as shareholder funds.

The total investment return for the Company over 2016 was £12,944m as reported in the Company's financial statements.

Investment return represents the Company's overall investment performance for both policyholders and shareholders. Policyholder assets are invested in line with the fund choices made by unit-linked policyholders and the investment risk is borne by the policyholder. The Company's shareholder exposure to these assets arises from the fact that some of the income received is a proportion of the assets under management.

Investment return as identified in the IFRS accounts is as follows:

	2016 £m
Financial investment return	**12,833**
Property investment return	**111**
Investment return	**12,944**

The total investment return includes the expected investment return included in the IFRS operating profit and the variance between the actual and expected investment performance. As such, there is some element of duplication with the underwriting performance reported in A.2 Underwriting performance, above.

Financial investment return includes fair value gains and losses, dividends and interest. Net gains/(losses) (excluding interest and dividend income) of £10,414m arose on financial investments designated as fair value through profit or loss and £(426)m arose on derivative contracts classified as held for trading. Investment income of £4m arose on loans and receivables.

Property investment return includes £103m of rental income excluding investment income from property partnerships.

Investment return relating to funds withheld payable to the other Group companies is recognised as an expense and reported within Finance Costs. Total finance costs over 2016 were £738m.

A.3.1 Investment income and expenses

The table below presents the actual investment income and expenses split by Solvency II asset class and the component of such income and expenses.

(£m)	**Rent**	**Interest**	**Dividends**	**Gains and losses**	**Total**
Bonds	-	1,654	-	5,370	**7,024**
Cash	-	78	-	(90)	**(12)**
Collateralised securities	-	50	-	765	**815**
Collectives	35	1	(87)	(323)	**(374)**
Deposits to cedants	-	145	-	180	**325**
Derivatives	-	(1,777)	-	1,376	**(401)**
Equity	-	-	480	1,477	**1,957**
Mortgages and loans	-	(0)	-	24	**24**
Property	10	-	-	26	**36**
Other assets	-	-	-	(12)	**(12)**
Assets held for index-linked and unit-linked contracts	83	141	522	2,816	**3,562**
Total	**128**	**292**	**915**	**11,609**	**12,944**

All investment gains and losses are recognised in the income statement. There are no amounts recognised directly in equity.

A.3.2 Investments in securitisation

The Company holds securitisations with a market value of £2.0bn as at 31 December 2016, of which £32m is held for index-linked and unit-linked contracts.

A.4 Performance of other activities

A.4.1 Operational income

Operational income of £57m comprises of rebates of unit trust management fees received from Legal and General Investment Management Limited.

A.4.2 Other expenses

Other expenses of £712m comprise administrative expenses, management fees payable, corporate expenses and other charges. Other costs are accounted for as they arise.

A.5 Any other information

This is the first annual report since the Solvency II regime took effect, and as such no comparative information at this level of detail is provided relating to performance during the previous solvency regime.

The sale of Legal & General Nederland Levensversekering Maatschappij (Legal & General Netherlands) to Chesnara Plc (Chesnara) was completed on 6 April 2017. Legal & General Netherlands is therefore included in the figures shown in the Company's SFCR.

The sale of the Legal & General Netherlands has marginally improved the Company's coverage ratio, by c.1% through a net increase to Solvency II surplus.

B. System of governance

B.1 General information on the system of governance

B.1.1 The structure of the Board

The Company's Board is accountable for the long-term success of the Company by setting the Company's strategic objectives within the overall strategy defined by the Group Board and monitoring performance against those objectives. The Board is led by the Group Chief Executive as the Board's Chairman, and as at 31 December comprised two Executive Directors (the Group Chief Executive and the Group Chief Financial Officer) and two Non-Executive Directors. The day-to-day management of the Company is led by the Group Chief Executive. The Group Chief Risk Officer, who is also the Company's Chief Risk Officer and the Company's Chief Actuary are standing attendees.

The Company's Board meets formally on a regular basis. At each Board meeting the Group Chief Financial Officer provides the Board with an update on the underlying business performance of each of the business divisions as part of the presentation of the monthly board management information report. Each of the Divisional Managing Directors/CEOs is invited on a periodic basis to give the Company's Board a more in-depth presentation on their Division's underlying performance. On a regular basis the Board receives formal reports from the Group Chief Risk Officer and Group Internal Audit on Risk and Compliance issues impacting the Company.

The Company operates within a clearly defined delegated authority framework. The delegated authority framework ensures that there is an appropriate level of Board contribution to and oversight of key decisions and that the day-to-day business is managed effectively.

The Company is managed across divisions rather than legal entities. The Company's business divisions are Legal & General Retirement; Legal & General Insurance; Legal & General Investment Management; Savings; General Insurance; and Legal & General Capital manages the shareholder funds of the Company. Group business functions deliver a number of centralised activities.

B.1.2 Delegated authorities

The Board delegated authority framework consists of a clearly defined schedule of matters reserved for the Company's Board. The types of matters reserved for the Board include, amongst others, matters relating to the Company's strategic plan, risk appetite, and systems of internal control and corporate governance policies. Those matters which are not reserved are delegated by the Board to the Group Chief Executive, who then onward delegates decision making to the Group Capital Committee and his direct reports. The Board is supported on matters relating to audit, risk and remuneration by the Group level committees.

The Delegated Authorities have been reviewed and approved by both the Group Capital Committee and the Company's Board.

Matters delegated to Group level Committees (Committees of the Group Board) are as follows:

- **Group Audit Committee** The primary responsibility of the Committee is to assist the Board in discharging its responsibilities with regards to monitoring the integrity of the Company's financial statements, the effectiveness of internal control and the independence and objectivity of the internal and external auditors.
- **Group Risk Committee** The purpose of the Committee is to assist the Board in fulfilling its responsibilities in relation to the oversight of risk within the Company and to provide advice in relation to current and potential future risk exposures of the Company. This includes

reviewing the Group's risk appetite and risk profile and assessing the effectiveness of the Group's risk management framework.
- **Group Remuneration Committee** Responsible for determining and approving the framework of the remuneration policy for the Group and its subsidiaries and specifically to manage executive director remuneration and the remuneration of other designated senior managers, including those undertaking business activities on behalf of the Company.

The Group Chief Executive delegates day-to-day operations and decision making in the following way:

- to the Group Capital Committee which has a group-wide remit and joint decision-making responsibility in relation to certain capital allocations for new product lines, large transactions and capital investments, M&A transactions and other material group-wide capital management and allocation matters that may arise; and
- to individuals, being the Group CEO's direct reports and heads of the Group's business divisions.

Each of the heads of the Group's business divisions then onward delegate to their direct reports the matters for which they have decision-making responsibility in relation to their area.

Each individual's schedule of delegated authorities operates in conjunction with their job description and relevant Risk and Capital Mandate. The Risk and Capital Mandates set the parameters of acceptable risk-taking as regards the Company's core product lines and investment risk.

The Company's Board has four committees to assist the Board in the management of the Company's with-profits, Savings and Workplace Pensions businesses:

- **Independent Governance Committee (IGC):** The IGC is chaired by an Independent Chairman and is comprised of a majority of independent members, who have been appointed because of their significant pension's industry experience. The IGC provides oversight of the Workplace Pension products (managed within LGIM and Savings) specifically to assess the ongoing value for money for relevant policyholders delivered by these Registered Pension Schemes.
  The IGC meets six times per annum. The IGC produces an annual report to the Company Board which is presented by the IGC's Chairman. The minutes of the IGC together with a summary of the key points discussed at the meeting are provided to the Board.
- **Unit-Linked Management Committee (ULMC):** The ULMC meets quarterly and is chaired by the Mature Savings Commercial Director. The ULMC provides oversight of the management of the Company's unit-linked funds. The Chief Actuary is a member. The Chief Risk Officer and the Head of Internal Client Services (LGIM) are both standing attendees. The minutes of the ULMC are provided to the board.
- **With-Profits Management Committee (WPMC):** The WMPC meets monthly, is chaired by the Savings Managing Director and is responsible for the oversight of the management of the with-profit fund. The Managing Director Savings, Finance Director Mature Savings, Commercial Director Mature Savings, Chief Operating Officer Mature Savings, and the LGAS Chief Actuary are all members. The With-Profit Actuary, Chief Risk Officer, Mature Savings and the Group Legal Manager are all standing attendees. The Company Board considers throughout the year a number of with-profit specific items including the Annual Bonus Declaration and compliance with the Principles and Practices of Financial Management (PPFM).
- **With-Profits Committee (WPC):** The WPC is chaired by an Independent Chairman and is comprised of a majority of independent members. It meets on a bi-monthly basis and is responsible for providing independent oversight of the management of the with-profit fund from a policyholder perspective. The Managing Director Mature Savings is a standing attendee along with the With-profit Actuary, Finance Director Mature Savings and the Chief Risk Officer Mature Savings. The Company Board considers reports, which take the form of

minutes from the WPC meetings and a report highlighting issues discussed, from the WPC at each Board meeting. At certain points during the year the Company Board considers specific with-profit items such as the annual bonus declaration and compliance with the PPFM all of which have been reviewed from a policyholder perspective by the WPC. On an annual basis the Chairman of the WPC makes a formal presentation to the Company Board on the activities of the WPC. The Chairman of the WPC also has access to the Chairman of the Company Board.

To provide the Company Board with the appropriate assurances that the Committees are discharging their responsibilities effectively as delegated to them by the Board, the Board receives the minutes of meetings of these Committees in the Board papers for noting.

The Company's business divisions are supported by the Group Risk, Legal, Finance, HR, IT and Procurement and Internal Audit Functions.

The diagram in Annex 2 illustrates the Company's governance framework.

B.1.3 Insurance company subsidiary governance

The Company, which is a principal operating subsidiary of the Group, is the regulated entity through which the vast majority of the Group's individual and group insurance, pensions and annuities business is executed. The Board of the Company reports in to the Group Board and the minutes of the Company Board meetings are submitted to the Group Board following each meeting.

Legal & General Insurance Limited is a direct subsidiary of the Company. The Board of Legal & General Insurance Limited reports in to the Company's Board via the submission of minutes for noting following each meeting. To the extent material issues arise in relation to the business of Legal & General Insurance Limited, the Group Board has line of sight of these through the Company.

Each entity delegates responsibility for delivering strategy and day-to-day operational matters to the Group CEO subject to the authority delegated to the Group CEO by the Group Board. The Group CEO onwards delegates to the heads of the Group's business divisions.

Oversight of risk management, audit and remuneration responsibilities for these entities is provided by the Group Board committees, being the Group Risk Committee, Group Remuneration Committee and the Audit Committee.

Details of the Company's governance framework are provided in Annex 2.

B.1.4 Remuneration policy and practices

B.1.4.1 Principles of the remuneration policy

The Group's remuneration policy is consistent across the Group including the Company and, in line with our remuneration principles, it is designed to reward, motivate and retain high performers in line with the risk appetite of the Group.

A summary of the remuneration structure for employees is shown below.

Base salary

The Group aims to attract and retain key employees by paying salaries which deliver competitive total remuneration. Factors taken into account when determining salaries include:

- The nature, size and scope of the role
- The knowledge, skills and experience of the individual
- Individual and overall business performance
- Pay and conditions elsewhere in the Group

	• Appropriate external market data Salary levels for all employees are reviewed on an annual basis taking into account the above factors. However, this does not mean a flat increase annually for all employees.
Annual bonus	The majority of employees participate in a discretionary bonus plan, unless an alternative plan applies based on role. An employee will be considered for a discretionary bonus award based on achievement against objectives, conduct and behaviours, the role performed during that year and internal relativities. Variable pay awards are set to ensure an appropriate balance between fixed and variable pay, and are designed to reward performance at the individual, business division, and overall Group levels. When making individual variable pay awards, both financial and non-financial performance in support of our business strategy is considered against specific, measurable targets, which are set at the beginning of the year. The Group operates bespoke bonus plans where business appropriate. However, the Remuneration Committee has ultimate discretion over all bonus plans. Bonuses above a certain threshold are subject to deferral with the deferral amount increasing with the size of the bonus. Deferred awards are normally held in shares for three years. The Group reserves the right to adjust deferral levels for Code Staff[1] as deemed appropriate.
Performance Share Plan (PSP)	Participation in the PSP is offered to a small number of senior executives each year in recognition of the strategic and influential role that they hold in terms of driving group performance, as well as their individual contribution. Participation in the plan for one year does not guarantee participation in future years. Where appropriate, grants under the PSP may also be made for new employees who join the Company during the year in key roles.
Other share plans and long-term incentives	The Group operates a Share Bonus Plan (SBP) which provides the vehicle for deferral of annual bonuses in the majority of cases and also allows for a limited number of awards of shares to high-potential individuals and those with critical skills. In addition, the Group operates a cash based long-term incentive plan for LGIM (LGIM LTIP) based on the financial performance of the division. Participation in the LGIM LTIP is limited to senior managers within the division.
Pension	All employees are given the opportunity to participate in a group pension scheme.
Shareholding requirements	The CEO is asked to build up a shareholding for 300% of salary and other Executive Directors are asked to build up a shareholding of 200% of salary. Other members of the leadership group are asked to build up a voluntary shareholding of 50% of base salary.

1 Code Staff is a category of role defined under various applicable European Directives (CRDIII & IV, AIFMD, UCITS V, and Solvency II). The name is taken from the FCA's Remuneration Code that interprets and applies these Directives for the UK. Broadly, Code Staff includes roles that are considered to have the authority to take risks that could directly, or indirectly, affect one or more firms within the Group and its investors.

Further details on the remuneration policy can be found in the Directors' Remuneration Report.

B.1.4.2 Performance criteria for remuneration

Annual incentives are designed to reward financial and non-financial performance that supports the business strategy, taking into account the Group's risk appetite and personal contribution in the business context that it was delivered. Targets are specific, measurable, set at the beginning of the year and communicated to employees.

For Code Staff in the control functions (Internal Audit, Regulatory Compliance and Risk), separate performance measures have been designed which exclude any direct linkage to financial performance.

Individual performance assessment is supported by a structured performance management framework. In reviewing an individual's performance against their objectives, the individual's approach to risk management (including environmental, social or governance risks) is considered when determining the overall level of bonus pay out. The bonus policy allows for zero bonus payments to be made when appropriate.

Deferred bonus

Under the group-wide deferral arrangements a significant proportion of the annual bonus for senior employees is deferred into group shares over a three-year period. The purpose of the deferral plan is to promote the sustainable long-term performance of the Group and to align the interests of our senior management with our shareholders.

Deferred awards for senior employees may be subject to forfeiture if the performance which led to a bonus being paid is found to be incorrect or in the event of personal misconduct. From 2015 onwards, annual incentive awards (including any deferred element) are subject to malus and clawback for material risk takers.

Long-term incentives

The Group provides long-term incentives which link reward with the long-term success and growth in value of Legal & General. Long-term incentive awards for most group staff are conditional on the satisfaction of total shareholder return (TSR), dividends per share, earnings per share and return on equity performance conditions which clearly aligns reward to the interests of shareholders and provides a degree of risk management (TSR reflects both underlying financial performance and the market's assessment of the quality and sustainability of those earnings).

The Remuneration Committee may exercise its discretion to scale back the vesting of awards if it was felt that the Group's financial performance did not justify the level of vesting (the Committee may not increase the award). The parameters which the Committee uses in making this assessment include market share, partnerships entered into and maintained, cost constraint, capital management, risk and shareholder perception.

Awards under the Group long-term incentive plan are subject to malus and clawback provisions.

B.1.4.3 Supplementary pension or early retirement schemes

All employees in the UK have the opportunity to participate in a defined contribution pension plan, or receive a cash allowance in lieu of pension, or receive a combination thereof.

There are no supplementary or early retirement schemes.

B.1.5 Material transactions

There were no material transactions between key management personnel and the Legal & General group of companies during the period. All transactions between the Group and its key management personnel are on commercial terms which are no more favourable than those available to employees in general. Contributions to the post-employment defined benefit plans were £75m (2015: £93m) for all employees.

At 31 December 2016 there were no loans outstanding to officers of the Company.

B.1.6 Solvency II Key functions

The Solvency II key functions within the Group's overall system of governance are the Risk-Management and Compliance functions led by the Group Chief Risk Officer; the Internal Audit function led by the Group Chief Internal Auditor; and the Actuarial function, led by the Chief Actuary. The functions operate independently from the business line with the activities of the Risk-Management and Compliance function being mandated by the Group Risk Committee and the Group Audit Committee establishing the role of the Group Internal Audit function through a formal Audit Charter. The Chief Actuary has the authority of the Board to report on those matters defined by legislation and regulation. The overall resourcing and effectiveness of the Risk-Management and Compliance functions, and the Actuarial function are assessed through a combination of internal audit review activity and by the governance forums to which the functions report. The effectiveness of the Internal Audit function is considered by the Group Board Audit Committee which may periodically seek independent external assurance.

Risk management

The Group Chief Risk Officer (Group CRO) leads the risk management function, including the Solvency II compliance function. The Group CRO reports functionally to the Chair of the Group Risk Committee. Administratively, the CRO reports to the Group Chief Financial Officer. The risk management function is aligned to the divisional structure, with LGIM, LGR, LGI, Savings and General Insurance having risk management functions. The Group CRO has been appointed as the Chief Risk Officer for the Company.

The CRO role is:

- Independent of the business line
- A provider of objective advice and guidance, oversight and challenge for all of Legal & General's risks
- Involved, where appropriate, in all material decisions to influence and provide objective challenge (e.g. products, pricing, projects, strategy, etc)

The Group CRO has a right to be heard in the setting of business strategy, product approval and capital planning activities, and may request revision to business proposals that may otherwise result in the Group operating outside agreed risk appetite. The Group CRO has authority to set and further refine risk limits within the parameters of the risk appetite agreed by the Group Risk Committee. The Group CRO has the right of escalation to the Group Risk Committee on any appropriate matters as they see fit.

Internal audit

The Group Chief Internal Auditor (GCIA), a senior position within the Group, reports functionally to the Chair of the Group Audit Committee. Administratively, the GCIA reports to the Group Chief Executive. The Group Audit Committee approves the performance evaluation, appointment, or removal of the GCIA and reviews his/her annual remuneration each year. There is regular communication between the Group Audit Committee Chair and the GCIA. In addition, the GCIA will also engage in day-to-day communication with Executive Management. The GCIA has right of attendance at all or part of any of the Group's governance and risk forums or any other forum in the execution of the Group Internal Audit remit.

Group Internal Audit act across the Group including providing independent audit for the Company.

Actuarial function

The actuarial function is split along legal entity lines, with Legal and General Assurance Society Limited, PMC, LGN, Legal & General Insurance Ltd and Legal & General Reinsurance having actuarial functions. Each legal entity has a Chief Actuary who fulfils the role of Head of Actuarial Function as required under the Prudential Regulation Authority's (PRA) senior insurance managers regime. Additionally there is a Group Chief Actuary responsible for the Group actuarial function. The actuarial activities are split between those involved in delivery of actuarial results and analysis and independent oversight and validation. The Chief Actuary role:

- Coordinates the calculation of technical provisions
- Ensures models are appropriate
- Assesses sufficiency and quality of data used in technical provisions
- Compares best estimates against experience
- Assesses the level of uncertainty in the assumptions
- Informs the Board of the reliability and adequacy of the calculation of technical provisions
- Oversees the calculation of technical provisions where insufficient data of appropriate quality requires approximations in the calculation of the best estimate
- Expresses an opinion on the overall underwriting policy
- Expresses an opinion on the adequacy of reinsurance arrangements
- Contributes to the effective implementation of the risk management systems

The Chief Actuary has a right to be heard in the setting of business strategy, product approval and capital planning activities, and may request revision to business proposals that may otherwise conflict with the overall underwriting policy or the adequacy of reinsurance arrangements. The Group Chief Actuary has the right of escalation to the Group Risk Committee on any appropriate matters as he or she sees fit.

B.2 Fit and proper requirements

B.2.1 Application of the policy

Legal & General has in place a fit and proper policy, the purpose of which is to set out the procedures required by regulated firms within the Legal & General Group to assess the fitness and propriety of individuals who run these undertakings or who hold other key functions in them.

B.2.2 Key requirements

In summary the policy requires that each insurance regulated entity shall establish, implement and maintain documented policies and adequate procedures to ensure that all persons who are responsible for running the entity or are responsible for other key functions are at all times fit and proper.

The assessment of fitness and propriety covers the following factors:

- Honesty, integrity and reputation
- Competence and capability
- Financial soundness

B.2.2.1 Legal & General assessment procedures

In support of the Group policy, defined processes are in place to ensure that the fitness and propriety of applicants is carefully considered before an application to the regulators to grant approval is submitted. An assessment will also be made before a notification is made to the regulators in relation to the appointment of a key function holder.

Legal & General will not support an application for approval or a notification if it is believed that the candidate fails to meet any element of the fit and proper test.

Each application will be looked at on its own merits, on a case-by-case basis, but the following principle generally applies to all applications:

- Has the candidate been open and honest with Legal & General and disclosed all relevant matters

If the candidate has disclosed any incidents pertaining to their fitness and propriety, the following will be considered:

- The seriousness of the issue and the relevance to the specific role applied for
- The passage of time since the incident occurred
- Whether the issue relates to an isolated incident or whether there is a pattern of adverse behaviour

Fit and proper assessment criteria have been developed and each application will be considered against these criteria, regardless of the current approved status of the individual.

Legal & General's assessment of an individual's competence and capability will be based around the following factors:

- knowledge – does the individual have generic knowledge of the industry sector and specific knowledge of the firm;
- qualifications – does the individual have prerequisite or supporting relevant qualifications;
- skills – does the individual demonstrate the appropriate level of business and interpersonal skills;
- behaviour – does the individual demonstrate the appropriate attitudes and standards of ethical behaviour; and
- expertise – does the individual achieve positive and fair outcomes and meet performance standards expected of the post.

The assessment criteria for each of the three key factors are also relevant in assessing the continuing fitness and propriety of approved persons.

B.2.2.2 Maintaining fitness and propriety

From time to time, individuals will be required to certify that there has been no change to the information provided at the point of approval and consequently, the fitness and propriety status is unchanged.

Legal & General's Group Policies and Procedures place an obligation on approved persons to notify the Group Conduct Risk and HR Director in the event of any pending or actual criminal, civil or other disciplinary charges, judgements, petitions for bankruptcy, or other actions or disciplinary measures whatsoever, against them or any entity, body or other entity with which he/she is, or has been associated.

Should such a notification occur, Legal & General will assess the information to decide whether the individual remains fit and proper. If the assessment ultimately concludes that the individual can no longer remain as an approved person, a notification will be made to the regulators in line with the regulatory requirements.

Legal & General's performance management process is the primary mechanism for tracking ongoing competency. Legal & General will take appropriate steps to monitor an individual's financial soundness on an ongoing basis.

B.3 Risk management system including the own risk and solvency assessment (ORSA)

B.3.1 Risk management system

Legal & General deploys a ‘three lines of defence’ risk governance model, whereby:

- business divisions are responsible for risk taking within the parameters of our risk appetite and accountable for managing risks in line with our risk policies;
- risk functions led by the Group Chief Risk Officer (Group CRO) provide objective challenge and guidance on risk matters; with
- Group Internal Audit providing independent assurance on the effectiveness of business risk management and the overall operation of the risk framework.

B.3.1.1 Risk appetite

The Company’s risk appetite statement sets out our overall attitude to risk, and the ranges and limits of acceptable risk taking. The Group Risk Committee leads an annual review of the Group’s risk appetite, assessing the continued appropriateness of our key measures and tolerances relative to the risk exposures of the Group. Additionally, as part of the annual planning cycle, assessment is made of the level of risk-taking proposed in the Group plan and the capacity for risk-taking within the overall appetite framework.

The Company’s risk appetite is approved by the Company’s Board. The Company’s risk appetite is set with regard to, but not limited by, the Group Board. The regular management information received by Group Board and Group Risk Committee includes our risk appetite dashboard setting out actual positions relative to the key targets and limits set in our risk appetite.

B.3.1.2 Risk taking authorities

The parameters of acceptable risk taking defined within the Company’s risk appetite are cascaded to business managers through ‘Risk and Capital Mandates’, empowering managers to make decisions that are consistent with appetite for risk.

Mandates articulate the product types and features that may be written; the asset classes that may be held; the target capital positions and ranges of earnings volatility within which the overall profile of risks should be managed; and tolerances for specific risk exposures. Activities that would result in a business operating outside agreed parameters require formal approval.

In conjunction with the Divisional Chief Risk Officers and the Group Chief Risk Officer, the Managing Directors have developed, and the Company Board has approved, the risk appetite for the Retirement, Insurance, Savings and LGIM businesses within the overall Group risk appetite and specifically the risk appetite for the Company. The Company Board approves the risk appetite for LGC’s management of the Company’s shareholder funds. This is contained within the relevant Risk and Capital Mandate.

B.3.1.3 Risk policies

Risk control

We set formal policies for the management of market, insurance, credit, liquidity and operational risks. The policies specify our overall strategies for ensuring each risk type is managed in line with our risk appetite and the minimum control standards that should be applied in managing our significant risk exposures.

Risk mitigation

We deploy a range of risk management techniques to manage and mitigate risks, so as to control risk exposures in line with our risk limits. For example, we use derivative instruments to hedge unrewarded risks as part of our asset liability management activity; and reinsurance programmes to transfer significant aggregations and concentrations of insurance risk exposures. Our framework of controls includes documented underwriting policies and structured delegated pricing and underwriting authorities. It also includes investment policies which take into account the nature of our liabilities, guarantees and other embedded options given to policyholders.

B.3.1.4 Risk identification and assessment

Review process

We operate a risk identification and assessment process under which all our businesses regularly consider changes in the profile of existing and emerging risks. The assessment process evaluates the risks that are inherent in our products as well as those that are presented from changes in the environments that we operate in.

Own risk and solvency assessment (ORSA)

Our risk identification and assessment process forms part of our broader 'own risk and solvency assessment'[2] (ORSA) process, our ongoing assessment of the risks to which the Company is exposed and an evaluation of the sufficiency of resources to sustain the business strategy over the horizon of the Group plan.

B.3.1.5 Risk management information

Our risk management information framework is structured to report and support the review of ongoing and emerging risks and assess actual risk positions relative to the risk limits and targets that we set.

B.3.1.6 Risk oversight

The Group CRO, who is independent of the business line, supports the Group Board and its Risk Committee in articulating acceptable risk taking and ensuring the effective operation of our risk and capital framework. This includes ongoing assessment of the Company's capital requirements to confirm that they meet regulatory solvency requirements.

The Group CRO also provides objective challenge and guidance on a range of risk matters to business managers, including the risks implicit in product developments, business transactions and new asset classes, and strategies for managing risks in line with the Company's overall risk appetite.

B.3.1.7 Risk committees

The Company operates within the Group's risk management framework. The Company's Board has ultimate responsibility for ensuring that the Group's risk management framework is appropriate for the Company. The Group Board's Risk Committee supported by the Group CRO, serves as the focal point for risk management activities. Details of the operation of the Group Risk Committee are set out in the full 2016 annual report.

Beneath the Group Risk Committee is a structure of formal risk oversight committees providing more focused review and challenge of specific risks to the Group, and reviewing the effectiveness of frameworks in place to manage those risks.

The Company's Board:

- Owns the overall Risk Management System
- Owns the Company's risk appetite statements

[2] Also known as the forward-looking assessment of own risks.

- Is the ultimate owner of the regulatory responsibilities

The Group Risk Committee ensures the effectiveness of the overall risk management system and recommends to the Group Board material changes in risk appetite.

The Executive Directors are accountable for:

- The implementation and operation of the risk management system
- Identifying, measuring, managing, monitoring and reporting risks within the business
- Ensuring all business decisions are informed by risk-based measures by reference to the agreed risk appetite statements wherever appropriate
- Ensuring appropriate risk taking and risk assurance resources are in place

The Group CRO leads the risk management function which provides the second line of defence across the Group.

Group Internal Audit provides the third line of defence across the Group. It provides assurance to the Group Audit Committee, Executive Directors and risk management function that the design and operation of the risk management system is appropriate for all risk types.

B.3.2 Own risk and solvency assessment (ORSA)

The purposes of the annual own risk and solvency assessment (ORSA) are to assess our risks and to evaluate whether we have sufficient financial resources to sustain the business strategy over the plan horizon. In line with PRA approval, a single group and Legal and General Assurance Society Limited ORSA assessment and report is undertaken. The Company's Board remains responsible for ensuring that the Company's ORSA is an integral part of the Company's business strategy and is taken into account on an ongoing basis in its strategic decisions. The Company's Board has approved the final report as suitable for the Company's ORSA.

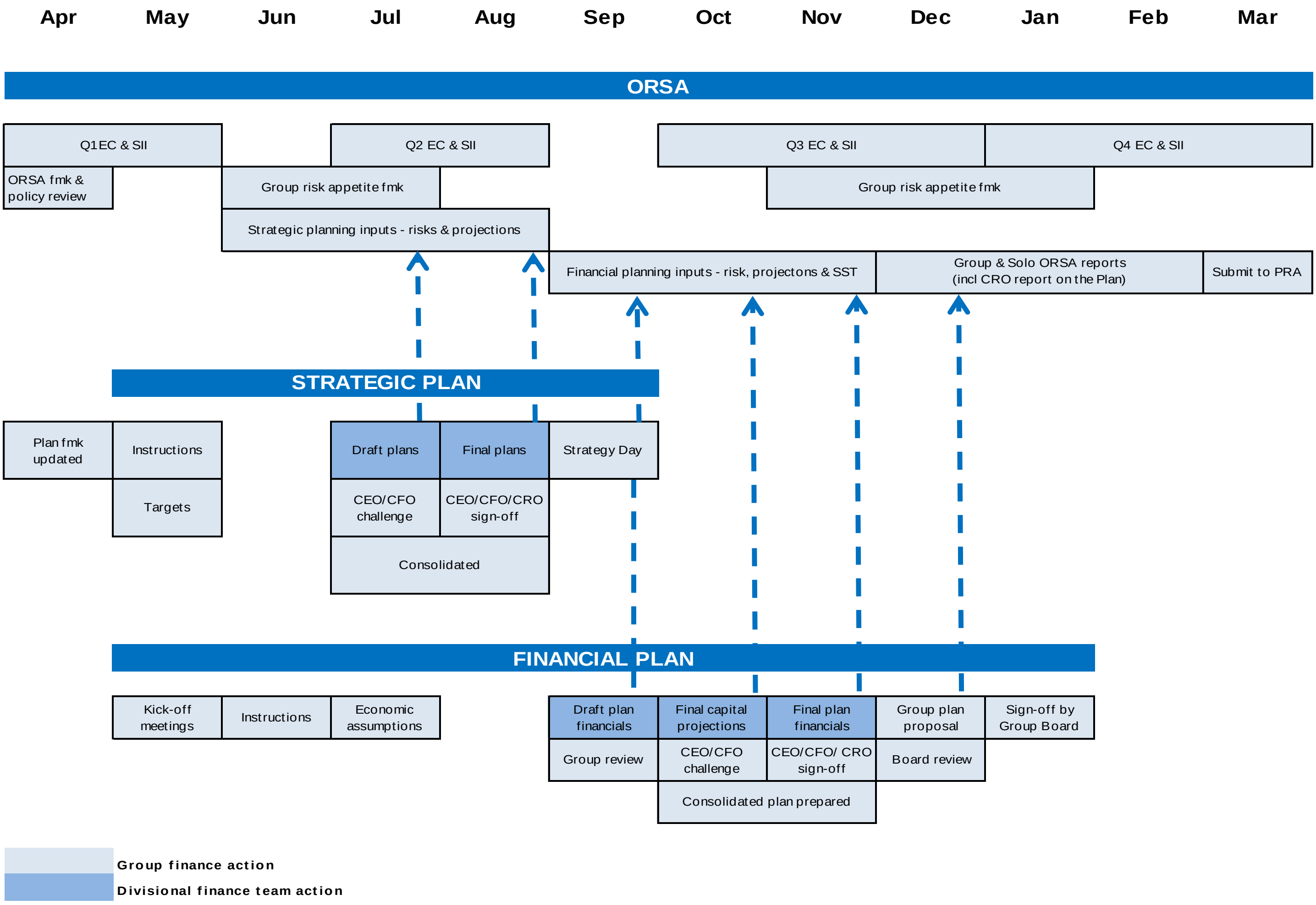
The ORSA process brings together the underlying risk and capital management processes by which we assess, monitor and measure our risks, review our business against risk appetite and tolerances and project the solvency position over the business plan. We have continued to integrate the ORSA with business as usual risk and capital management. The ORSA cycle is aligned with the strategic and business planning process so that the key elements can interact and inform forward looking decision-making. This is set out in diagram B3.1 below.

The ORSA policy was last reviewed by the Group Board (delegated to Group Risk Committee) in July 2016 and the Company Board in September 2016.

Integration of group and subsidiary ORSA processes

Legal & General is managed on a divisional basis. As such, ORSA (i.e. risk and capital management) responsibilities follow the Group's divisional management structure. Regular ORSA processes are aligned with the strategic and business planning process, with divisions providing key ORSA inputs in line with the plan timetable and various Group functions coordinating and/or aggregating. A single Group and Legal and General Assurance Society ORSA report is produced.

Diagram B3.1: ORSA/Plan timeline



The Company's Board is very active in the ORSA and risk and capital management processes during the year. Their key involvement is summarised below:

ORSA processes	LGAS Board
Framework review	Review of policy and framework (Jul/Sep)
Risk appetite	Updated LGAS risk appetite, specifically with regard to SCR coverage (Sep) Risk appetite reporting in quarterly CRO report to Board
Risk identification	Approve risk landscape and emerging & strategic risks (Sep)
Capital and solvency calculation	SII YE15, Q116, HY16, Q316, YE16F (May, May, Sep, Dec, Monthly) EC YE15, Q116, HY16, Q316 (May, June, Sep, Nov)
Projections of solvency	Dividend paper and ORSA projection results (Jan 2017)
Stress and scenario testing (SST)	Review SST proposals including LGAS specific stresses/scenarios (Jul/Sep) SST results (Dec, Jan 2017, Feb 2017)
Risk management review	Approve risk review documents (Sep)
ORSA reports	2016 Group & LGAS ORSA report (Feb 2016)

Throughout the year, the Company monitors its performance against the current plan as well as monitoring risk and capital management information (MI).

B.3.3 Governance of the Internal Model

The Group Board is ultimately responsible for ensuring the continuous appropriateness of the design and operation of the Group's partial internal model (the Internal Model). This responsibility is discharged through the Group Risk Committee, whilst the Group Internal Model Committee (GIMC) oversees Internal Model activities. The Company's Board is responsible for ensuring the continuous appropriateness of the design and operation of the Internal Model for the Company

The overall appropriateness and effectiveness of the Internal Model depends upon the effective operation of the Group's established internal control system.

First line business management are responsible for implementing adequate and effective controls over the Internal Model as well as the Group's material product risk exposures, with the ongoing application and effectiveness of these overseen by second line Group and divisional risk teams and by Group Internal Audit in the third line of defence. Material concerns are escalated to operational and senior management for resolution. The status of remediation activity is monitored by Group and divisional risk teams, with significant issues escalated to the GIMC and where necessary to the Group Risk Committee. Group Internal Audit provide independent oversight of the effectiveness of the internal control system.

This approach has ensured the implementation of adequate controls to ensure the ongoing appropriateness of the design and operation of the Internal Model, and these controls are subject to effective governance and oversight.

The Group Internal Model Governance Policy sets out the governance framework in place for Legal & General's partial internal model designed to mitigate model risk. This complements the Group's existing system of governance, highlighting specific requirements in respect of the Internal Model to ensure that it operates properly on a continuous basis, including ensuring that controls relating to the Internal Model are implemented in accordance with the Group Internal Control Policy and are adequate and effective at all times.

The Internal Model governance framework is outlined in the table below:

Board/Committee	Responsibilities
Group Board	Ensuring the ongoing appropriateness of the design and operation of the Internal Model. This responsibility is discharged through the Group Risk Committee, subject to certain matters being reserved for its direct attention.
Legal entity boards	Ensuring the ongoing appropriateness of the design and operation of their parts of the Internal Model; discharged by use and challenge of the model in decision-making; ensuring that the model's scope remains appropriate; and ensuring that appropriate validation is performed.
Group Risk Committee (GRC)	Monitoring the performance and appropriateness of the Internal Model, including ensuring that related controls are adequate, effective, and implemented in line with the Group's Internal Control Policy. Primarily, the Group Risk Committee discharges these responsibilities through acting on the receipt of recommendations, analysis and reports from the Group CRO team and the GIMC
Group Internal Model Committee (GIMC)	Overseeing the design, development and operation of the Internal Model to ensure that it operates as expected on a continuous basis to meet the Group's regulatory and economic requirements for risk-based capital management. This includes reviewing the effectiveness of internal controls as they relate to the Internal Model through the receipt of relevant reports and management information (MI).

B.3.3.1 Internal Model controls

First line business divisions are responsible for operating a robust control framework and appropriate controls to manage exposures and mitigate unacceptable outcomes (per the Group's risk appetite). Business management are responsible for implementing robust controls to mitigate key risks associated with processes they are responsible for, and to ensure that these are regularly reviewed and remain fit for purpose. Day-to-day responsibility for ensuring that robust internal controls are in place and are operating effectively over Internal Model related processes is delegated to Internal Model Controllers (IMCs). IMCs provide first line management coverage of the Internal Model across all relevant legal entities and business divisions. Key responsibilities include ensuring compliance of their area with the requirements of the Group Internal Model Governance Policy and Group Internal Control Policy.

Oversight of the internal control system is provided by the Group Risk and divisional risk teams.

B.3.3.1.1 Changes over the reporting period

Solvency II regulations necessitated the implementation of additional financial reporting and governance processes, and 2016 was the first year of full live operation of these processes. There has been close scrutiny by our second line actuarial and risk teams and Group Internal Audit in the third line of defence to ensure that the processes are fully embedded in the Group's governance and that they are being operated robustly and effectively. The Company has responded to supervisory requirements to provide greater levels of evidence in areas such as model change and validation.

B.3.3.1.2 Internal Model validation

The Group Validation Policy and associated standards define the Group's validation framework, and capture the requirements of the PRA Rulebook and relevant EU regulations. The framework requires an annual validation cycle for the Group's partial internal model (the Internal Model). This has been performed as part of the production of the SCR as at 31 December 2016. The objective is to produce a robust, proportionate and demonstrably complete approach to validation overseen by the Group Chief Risk Officer.

There is an annual assessment of which aspects of the Internal Model must be independently validated. Independent validation is carried out mainly by the second line, sometimes by a first line team from a different business division, or sometimes by an external party. Independent validators must demonstrate how independence is met and state any limitations on independence.

Requirements for each annual cycle are specified in the Validation Terms of Reference. Respective validators outline approach, activities, tools and aspects of the model in Validation Work Programmes. The results, conclusions and consequences including remediation are detailed in independent validation reports or validation reports prepared by the first line. These are presented to GIMC for approval.

B.3.3.1.3 Validation activity

Internal Model validation activity for the reporting period covered the whole of the Internal Model. The level of validation undertaken was consistent with the level of risk incurred. Independent validation was performed on those areas identified as most material to the Internal Model's operation and results. The outputs are validation reports, highlighting key findings, strengths, weaknesses, limitations and remediation actions.

B.4 Internal control system

The Group internal control policy requires that each division's internal control system shall at least include administrative and accounting procedures, an internal control framework, appropriate reporting arrangements at all levels of the undertaking, and a compliance function.

The Group's internal control framework seeks to ensure that:

- An organisational structure is defined, with clarity of roles, responsibilities and reporting lines;
- Appropriate management information and reporting processes are defined
- Frameworks for decision making (including the delegation of authority) are articulated
- Clear segregation of duties is in place
- Conflicts of interest are managed
- Administrative and accounting procedures are aligned with Group requirements
- Personnel have sufficient skills, knowledge and expertise to discharge their responsibilities (including those relating to the regulatory environment)
- Adequate and orderly records of business are maintained
- The security of customer data and other internal records is ensured
- Business procedures combat financial crime
- Processes are in place to deal with policyholder claims and complaints
- The integrity of manual and computerised business systems is ensured
- Processes ensure assessment of the possible impact of any changes in the legal environment

The Group's main operating boards and the Group Audit Committee oversee the adequacy and effectiveness of the internal control framework, primarily through the receipt of assurances in support of the UK Corporate Governance Code, and reports from Group Internal Audit, external auditors, and risk teams in the second line of defence.

B.4.1 Solvency II Compliance function

Legal & General has defined the Solvency II Compliance function as being responsible for:

- advising the Company Board and its sub committees on compliance with the requirements of the Solvency II Directive[3] and its associated laws, regulations and administrative provisions;
- advising the Company Board on the possible impact of any changes in the legal environment on operations of the undertaking concerned and the identification and assessment of compliance risk;

[3] Directive 2009/138/EC of the European Parliament.

- developing and managing the Group's Solvency II Compliance Policy, which inter alia sets out the responsibilities, competencies and reporting duties of the (Solvency II) compliance function; and
- establishing and operating the Group's Solvency II Compliance Plan that details the activities the function will undertake in relation to compliance risk.

Legal & General has defined the Group Chief Risk Officer role as the functional head of Solvency II Compliance at the Group level, with the Risk, Actuarial, Group Finance and HR functions delivering activities in support of the Solvency II Group Level Compliance Function.

Legal & General's Solvency II Compliance Plan is defined as the review activities performed by the Compliance function to support it in advising the Company Board on compliance in relation to Solvency II matters.

B.5 Internal audit function

Group Internal Audit carries out:

- independent reviews and audits of the controls mitigating the key risks in all areas of the business, prioritised according to the relative risk of each assignment as determined by the Group Chief Internal Auditor in conjunction with senior management;
- reviews of major Business Change Initiatives; and
- reviews of the risk management and internal control processes.

Internal control objectives considered by Group Internal Audit include:

- consistency of operations or programmes with the Group's established risk appetite, objectives and goals;
- effectiveness and efficiency of operations, and use of resources;
- compliance with policies, plans, procedures, laws and regulations;
- reliability and integrity of management and financial information processes, including the means to identify, measure, classify, and report such information; and
- safeguarding of assets.

The Group Chief Internal Auditor reports functionally to the Chair of the Group Audit Committee and administratively to the Group Chief Executive Officer.

The internal audit activity remains free from interference by anyone within Legal & General. This includes the choice of business areas to audit, procedures, frequency, timing, or the content of the Group Internal Audit reports. This ensures that the Group Internal Audit can maintain a necessary independent and objective perspective.

Internal auditors have no direct operational responsibility or authority over any of the activities audited. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair internal auditors' judgement.

Internal auditors will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors will make a balanced assessment of all the relevant circumstances and will not lose their objectivity when forming judgements.

The GCIA confirms to the Group Audit Committee, at least annually, the organisational independence of internal audit activity.

B.6 Actuarial function

The actuarial function is split along legal entity lines, with the Legal and General Assurance Society Limited, PMC, LGN, LGIL and group having actuarial functions. Legal & General America (LGA) and Legal & General Reinsurance (LG Re) have their own Actuarial team but are not EEA insurers. They are therefore supported by the Group Actuarial Function Team for their Solvency II reporting. The Company's Chief Actuary reports functionally to the Group Risk Officer.

The Prudential Regulatory Authority (PRA) have specified that firms should appoint a Chief Actuary who should fulfil the role of Head of Actuarial Function (a role that is not required by the Directive) and hold the Chief Actuary role as set out under the Prudential Regulation Authority's (PRA) senior insurance managers regime. For Legal & General, actuarial functions (and Chief Actuaries) are required for the Legal and General Assurance Society Limited, PMC and LGIL. Additionally a Group Chief Actuary is required for the Group Actuarial Function.

The Company's Chief Actuary presents an annual report to the Board summarising the activities of the actuarial function that:

- Supported compliance with the requirements on the calculation of the technical provisions (TPs)
- Provided the opinions on the underwriting and reinsurance arrangements
- Contributed to the effectiveness of the risk management systems more widely

These reports are shared with the Group Chief Actuary.

The requirements covering TP calculations were addressed through various activities, including, in particular, actuarial function review of divisional and entity level calculations and the membership of oversight committees. A number of reports during the year were provided to the Board on the data, models, methodologies, assumptions and results of the Solvency II TP calculations.

Oversight of underwriting and reassurance by the Actuarial Function were provided substantially through the membership of Divisional Pricing and Capital Committees. Business division reports were produced on underwriting and reassurance and actuarial function reports providing an actuarial opinion on these areas for the Company were provided to the Board during the year.

The actuarial function contributes to the effective implementation of the risk management system through various activities and the membership of a number of key divisional, entity and Group Committees with risk and financial reporting responsibilities. Areas of focus, both within the responsibility of the risk function and more generally, with significant levels of actuarial function involvement include: the Internal Model and SCR; the ORSA; identifying, measuring and monitoring risks; Asset Liability Modelling (including matching adjustment and liquidity management); product pricing; financial reporting; business plans; and Part VII transfers.

B.7 Outsourcing

The Group's Outsourcing and Essential Supplier Services Policy sets out the framework and minimum standards of control and governance that Legal & General expects to be applied in the management of risks associated with outsourced supplier service arrangements. The policy specifies that an activity should not be outsourced where it would materially impair the quality of the Group's system of governance; unduly increase the Group's exposure to operational risk; impair the ability of supervisory authorities to monitor the Group's compliance with its obligations; or undermine continuous and satisfactory service to the Group's policyholders.

The policy requires that for all outsourced arrangements a rigorous evaluation and supplier selection process is undertaken having regard for the financial stability, expertise, ability and capacity of the supplier to deliver the required service. The policy also specifies that a written contract must be in place which must include:- a service level agreement; the conditions under which the arrangement may be terminated; provision for the orderly transition of services to another provider or Legal & General if the contract is terminated; a defined mechanism to resolve disputes arising out of/ or relating to the contract; appropriate contingency plans should the supplier be unable to provide the required service; and provision for the continued availability of any software upon which Legal & General is reliant. Contracts must also ensure access to the providers premises, business management and any data relating to the outsourced activity, by Legal & General's Internal Audit, Risk and Compliance functions, its external auditors and Supervisory Authorities; and appropriate warranties that Legal & General and client data is adequately protected against unauthorised access at all times. All outsourced arrangements must be managed under the direction of a named Legal & General relationship manager. The risk function maintains oversight of the management of outsourcing arrangements established by the first line business operations.

Below is a schedule of outsourcers used by the Company either directly or through relationships established by the broader Legal & General Group:

Service Providers	**Entity**	**Goods/services**	**Jurisdiction**
Sungard Availability Services (UK) Limited	LGAS, LGI	Disaster recovery warm site	UK
IBM United Kingdom Limited	LGAS, LGI	IT infrastructure and operations	UK
RR Donnelley Global Document Solutions Group Limited	LGAS, LGI	Document printing and mailing	UK
Tata Consultancy Services Limited	LGAS, LGI	IT application development	UK
Vodafone Ltd	LGAS, LGI	Telephony and data connectivity services	UK
State Street Bank And Trust Company	LGAS	Fund pricing and valuations	UK

Insourcing is the use by one Legal & General Group company of another company within the Group for the supply of business facilities or services. The Company's core insourced relationships are as follows:

- Investment management services provided by Legal & General Investment Management Limited LGIM;
- Treasury services by Legal & General Finance Plc; and
- The provision of employees and procurement services by Legal & General Resources Limited.

Legal & General Resources Limited is the main employment company for the UK Group as the contracts of employment for all staff, other than main board directors and staff employed by LGIM, are held with this company. Legal & General Resources Limited is also the company through which group-wide contracts for the supply of goods and services for Legal & General UK businesses are placed.

The Group's Shared Services IT (SSIT) provides IT services for Legal & General Assurance Society, LGIL and Group entities. By virtue of all IT personnel, and many of BIS's contracts, being in the name of Legal & General Resources, from a corporate entity perspective these services are effectively provided to these companies by Legal & General Resources.

B.8 Any other information

B.8.1 Adequacy of the system of governance

The Company operates within the Group's risk management framework. The Group Executive Risk Committee (a sub-committee of the Group Risk Committee) undertakes an annual review of the Group's risk management framework and broader system of governance to confirm its adequacy given the nature, scale and complexity of the risks inherent in its business. The most recent review was in February 2017, where the Committee concluded that the Group's risk framework aligns with the Group's key risk exposures, and operated effectively during 2016 in identifying material risk exposures. The conclusion was noted by the Group Audit Committee.

B.8.2 Any other information

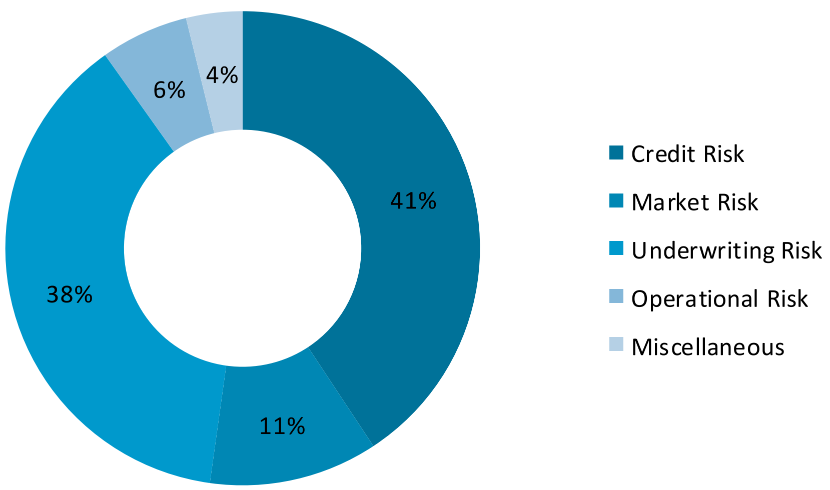
To enhance the governance at the subsidiary level two non-executive directors were appointed to the Company Board in 2016. In addition the Independent Reviewer was replaced by the With-Profits Committee chaired by an Independent Chairman and comprised of a majority of independent members.

C. Risk profile

Measures used to assess risks

Our risk-based capital model (the Internal Model) seeks to provide a quantitative assessment of the Company's risk exposures. It forms part of the suite of tools that we use to evaluate our strategic plans, set risk appetite, allocate capital and evaluate product pricing. We also use our capital model to assess significant transactions, including large pension risk transfer deals. The key output from our capital model is the generation of capital requirements. We calibrate our model to a 99.5% value at risk confidence level over one year, equivalent to ensuring that we hold sufficient capital to survive our assessment of a worse case 1-in-200 year event. In terms of capital requirement, credit and insurance (longevity) risks remain our most significant risks. Market risk, which includes equity, property and interest rate risks, are also more material risks for which we hold capital.

Below is the breakdown of the Company's diversified Solvency Capital Requirements by major risk categories:



The financial risks associated with LGIM's businesses are directly borne by the investors in its funds. Therefore detailed risk disclosures have not been presented.

Prudent Person Principle

All investments held by insurance and reinsurance undertakings should be managed in accordance with the 'Prudent Person Principle'. The Prudent Person Principle requires companies to only invest in assets and instruments:

- whose risks can be properly identified, measured, monitored, managed, controlled and reported;
- that ensure the security, quality, liquidity and profitability of the portfolio as a whole;
- that are appropriate to the nature and duration of insurance and reinsurance liabilities; and
- are in the best interest of policyholders and beneficiaries.

The Group and Company's risk appetite for credit and market risk is set in accordance with the Prudent Person Principle.

Group Credit Risk, Market Risk and Asset Liability Matching policies define the Group's policy for the management of assets and the framework that supports its practical application, and have been defined in line with the Group risk appetite and the Prudent Person Principle. The policies are applicable to all entities in the Legal & General Group and any exemptions from the policy must be authorised by the Group CRO.

All divisions are required to invest their assets in line with the Group policies. Compliance with the Group policies is monitored through the Group's risk framework described in Section B. System of Governance above. The following processes support the Group in ensuring it meets the Prudent Person Principle:

- Risk & Capital Mandates set out the parameters of acceptable risk taking; including the approach taken to ensuring investment decisions are made in accordance with the Prudent Person Principles;
- it is the responsibility of the business to ensure that the adherence to the Risk and Capital Mandates are appropriately monitored with any exceptions escalated to the divisional risk committees and relevant Group committees; and
- the Group's Investment Management Risk Committee oversees the effectiveness of overall framework for managing the compliance of Prudent Person Principles.

C.1 Underwriting risk

C.1.1 Risk exposure and controls

The Company is exposed to underwriting (also known as insurance) risk as a consequence of offering the principal products outlined in Section A.1.2. Underwriting risk is the exposure to loss arising from experience being different to that anticipated. Detailed below are the risks associated with each of the Company's divisions and the associated controls operated.

Principal risk	Division	Risk mitigations
Longevity, mortality and morbidity risks		
For contracts providing death benefits, higher mortality rates would lead to an increase in claims costs. The cost of health related claims depends on both the incidence of policyholders becoming ill and the duration over which they remain ill. Higher than expected incidence or duration would increase costs over the level currently assumed in the calculation of liabilities.	LGI	The pricing of protection business is based on assumptions as to future trends in mortality and morbidity having regard to past experience. Underwriting criteria are defined setting out the risks that are unacceptable and the terms for non-standard risks presented by the lives to be insured. Extensive use of reinsurance is made within the UK retail protection business, placing a proportion of all risks meeting prescribed criteria. Mortality and morbidity experience is compared to that assumed within the pricing basis with variances subject to actuarial investigation.
For savings contracts providing minimum assured death benefits, higher mortality rates may result in an increase in claims costs.	Savings	The pricing basis for contracts providing minimum assured death benefits include provision for future trends in mortality based on past experience. The level of mortality risk accepted within each contract is not sufficiently material to warrant formal underwriting at an individual policy level.

Principal risk	Division	Risk mitigations
Older contracts containing a basic guaranteed benefit expressed as an amount of pension payable or a guaranteed annuity option expose the Company to interest rate and longevity risk. The cost of guarantees increases during periods when interest rates are low or when annuitant mortality improves faster than expected.	Savings	The ultimate cost of basic guarantees provided on older contracts will depend on the take up rate of any option and the final form of annuity selected by the policyholder. The Company has limited ability to control the take up of these options. However, the book of business itself is diminishing in size.
For annuity contracts, the Company is exposed to the risk that mortality experience is lower than assumed. Lower than expected mortality would require payments to be made for longer and increase the cost of benefits provided. Lifetime mortgage business also explicitly has some exposure to the life expectancy of borrowers.	LGR	Annuity business is priced having regard to trends in improvements in future mortality. Enhanced annuities, which are priced taking account of impairments to life expectancy, are subject to specific underwriting criteria. Certain annuitant mortality risks, including enhanced annuities, are placed with reinsurers. The Company regularly reviews its mortality experience and industry projections of longevity and adjusts the pricing and valuation assumptions accordingly. In pricing lifetime mortgage business, account is taken of trends in mortality rates in setting the amounts that are advanced to borrowers relative to the value of the property on which the loan is secured.
Persistency risk		
In the early years of a policy, lapses may result in a loss to the Company, as the acquisition costs associated with the contract would not have been recovered from product margins.	LGI and Savings	The pricing basis for protection business includes provision for policy lapses. The persistency assumption for protection business allows for the expected pattern of persistency. Actual trends in policy lapse rates are monitored with adverse trends being subject to actuarial investigation. For insured contracts, terms and conditions typically include surrender deductions to mitigate the risk. In later periods, once the acquisition costs have been recouped, the effect of lapses and surrenders depends upon the relationship between the exit benefit, if any, and the liability for that contract. Exit benefits are not generally guaranteed and the Company has some discretion in determining the amount of the payment. As a result, the effect on profit in later periods is expected to be broadly neutral.
Expense risk		
In pricing long-term insurance business, assumptions are made as to the future cost of product servicing. A significant adverse divergence in actual expenses experience could reduce product profitability.	LGR, LGI and Savings	In determining pricing assumptions, account is taken of changes in price indices and the costs of employment, with stress testing used to evaluate the effect of significant deviations. Actual product servicing costs are monitored relative to the costs assumed with the product pricing basis, with variances investigated.

Principal risk	Division	Risk mitigations
Concentration (catastrophe) risk		
Insurance risk may be concentrated in geographic regions, altering the risk profile of the Company. The most significant exposure of this type arises for group protection business, where a single event could result in a large number of related claims.	LGI	Group protection business contracts include an ‘event limit’ capping the total liability under the policy from a single event. Excess of loss reinsurance further mitigates loss from the exposure. For general insurance business, the risk acceptance policy, terms and premiums reflect expected claims and cost associated with a location and avoids adverse selection. Additionally, exposure by location is monitored to ensure there is a geographic spread of risk. Catastrophe reinsurance cover also mitigates loss from concentrations of risk.
The Company accepts a tranche of catastrophe cover issued by its subsidiary company Legal & General Insurance Ltd (LGIL). Should a significant event occur, triggering LGIL’s catastrophe cover, the Company will be required to meet its share of its subsidiary’s claims payments.	LGI	The Company accepts a share of the catastrophe reinsurance in line with market rates. When calculating the extent of the catastrophe cover required for the Group, the exposure is assessed on a group basis as well as for LGIL on a standalone basis.
Insurance risk may be concentrated in geographic regions, altering the risk profile of the Company. The most significant exposure of this type arises for group protection business, where a single event could result in a large number of related claims.	LGI	Group protection business contracts include an ‘event limit’ capping the total liability under the policy from a single event. Excess of loss reinsurance further mitigates loss from the exposure. For general insurance business, the risk acceptance policy, terms and premiums reflect expected claims and cost associated with a location and avoids adverse selection. Additionally, exposure by location is monitored to ensure there is a geographic spread of risk. Catastrophe reinsurance cover also mitigates loss from concentrations of risk.
Epidemic (catastrophe) risk		
The spread of an epidemic could cause large aggregate claims across the Company’s portfolio of protection businesses.	LGI	The pricing basis for protection business includes an assessment of potential claims as a result of epidemic risks. Quota share and excess of loss reinsurance contracts are used by individual and group protection, respectively, to further mitigate the risk. Depending on the nature of an epidemic, mortality experience may lead to a reduction in the cost of claims for annuity business.

C.1.2 Insurance Special Purpose Vehicles (SPVs)

The Company has no SPVs authorised under Article 211 of the Solvency II Directive.

C.1.3 Risk concentration

There is limited potential for single incidents to give rise to a large number of claims across the different contract types written by the Company. In particular, there is little significant overlap between the long-term and short-term insurance business written by the Company. However, there are potentially material correlations of insurance risk with other types of risk exposure. The Company’s capital model seeks to measure risk correlations particularly those that would tend to be more acute as the underlying risk scenarios become more extreme. An example of the accumulation of risk is the correlation between reinsurer counterparty risk with mortality and morbidity exposures.

While exposure to concentration risk is an inherent aspect of writing insurance business, we have limited appetite for the scale or frequency of events anticipated in product pricing materially diverging from expectations as a consequence of significant accumulations of exposure to a single event or counterparty. Where required, we will set limits on the aggregate values for individual lives that we will insure, and the minimum geographic spread of insurance business that we will accept. Reinsurance arrangements are also used to mitigate our risk.

Concentrations of risk are reported as part of the Group's risk monitoring and reporting framework. The risk management reports presented at divisional and group risk committees provide both qualitative and quantitative information on concentration risks, as well as on material risk drivers and mitigating actions taken where exposures are outside acceptable tolerances.

C.2 Market risk

C.2.1 Risk exposure and controls

The Company is exposed to market risk as a consequence of offering the principal products outlined in section A.1.2. Market risk is the exposure to loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets.

Principal risk	Division	Risk mitigations
Investment performance risk The Company is exposed to the risk that the income from, and value of, assets held to back insurance liabilities do not perform in line with investment and product pricing assumptions leading to a potential financial loss.	LGR and LGI	Stochastic models are used to assess the impact of a range of future return scenarios on investment values and associated liabilities in order to determine optimum portfolios of invested assets. For immediate annuities, which are sensitive to interest rate risk, analysis of the liabilities is undertaken to create a portfolio of securities, the value of which changes in line with the value of liabilities when interest rates change.

Principal risk	Division	Risk mitigations
The financial risk exposure for participating contracts is different from that for non-participating business. Greater emphasis is placed on investing to maximise future investment returns rather than matching assets to liabilities. This results in holding significant equity and property investments. Lower investment returns increase the costs associated with maturity and investment guarantees provided on these contracts.	Savings	These risks are managed by maintaining capital sufficient to cover the consequences of mismatch under a number of adverse scenarios. In addition, different investment strategies are followed for assets backing policyholder asset shares and assets backing other participating liabilities and surplus. The former include significant equity and property holdings, whilst the latter are invested largely in fixed interest securities. The assets held are managed so as to provide a partial hedge to movements in fixed interest yields and equity markets. The methodology used to calculate the liabilities for participating contracts makes allowance for the possibility of adverse changes in investment markets on a basis consistent with the market cost of hedging the guarantees provided. The methodology also makes allowance for the cost of future discretionary benefits, guarantees and options. The value of future discretionary benefits depends on the return achieved on assets backing these contracts. The asset mix varies with investment conditions reflecting the Company's investment policy, which aims to optimise returns to policyholders over time whilst limiting capital requirements for this business.
For unit-linked contracts, there is a risk of volatility in asset management fee income due to the impact of interest rate and market price movements on the fair value of the assets held in the linked funds, on which investment management fees are based. There is also the risk of expense over-runs should the market depress the level of charges which could be imposed.	LGI and Savings	The performance of linked investment funds relative to their investment objectives is subject to regular monitoring. Periodic assessment is also made of the long-term profitability to the Company of these funds. For some contracts the Company has discretion over the level of management charges levied.
Property risk		
Lifetime Mortgages include a no-negative equity guarantee which transfers an exposure to loss to the Company as a result of low house price inflation and an exposure on specific properties which may underperform the general house price inflation for whatever reason.	LGR	To mitigate the risk, maximum loan to value ratios are set for all lending with further underwriting criteria setting out acceptable properties for lending purposes. Policy terms also require properties to be fully insured and maintained, including the right of inspection. Diversification of lending by property type and geographic region seek to control exposures to specific aspects of the property market.

Principal risk	Division	Risk mitigations
Currency risk To diversify credit risk within the annuities business corporate bond portfolio, investments are held in corporate bonds denominated in non-Sterling currencies. Fluctuations in the value of, or income from, these assets relative to liabilities denominated in Sterling could result in unforeseen loss.	LGR	To mitigate the risk of loss from currency fluctuations, currency swaps and forwards are used to hedge exposures to corporate bonds denominated in currencies other than Sterling. Hedging arrangements are placed with strongly rated counterparties with collateral requirements being subject to regular review and reconciliation with the counterparties. In all cases, it is not possible to perfectly hedge currency risk, leaving some residual risk.
The liabilities of the intragroup reinsurance arrangements are revalued from US Dollars into Sterling potentially resulting in a loss to equity.	LGI	Balance sheet foreign exchange currency translation exposure in respect of the Group's international subsidiaries is managed in accordance with a policy, agreed by the Group Board, which allows net foreign currency assets to be hedged through the use of derivatives. In all cases, it is not possible to perfectly hedge currency risk, leaving some residual risk.
Inflation risk Inflation risk is the potential for loss as a result of relative or absolute changes in inflation rates. Annuity contracts may provide for future benefits to be paid taking account of changes in the level of inflation. Annuity contracts in payment may include an annual adjustment for movements in price indices.	LGR	The investment strategy for annuities business takes explicit account of the effect of movements in price indices on contracted liabilities. Significant exposures that may adversely impact profitability are hedged using inflation swaps. Annuity contracts also typically provide for a cap on the annual increase in inflation linked benefits in payment. It is not possible to perfectly hedge inflation risk linked with contracted liabilities, leaving some residual risk.
Interest rate risk Interest rate risk is the risk that the Company is exposed to lower returns or loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets and liabilities arising from changes in underlying interest rates.	LGR	To mitigate the risk that guarantees and commitments are not met, financial instruments are purchased, which broadly match the expected non-participating policy benefits payable, by their nature and term. The composition of the investment portfolio is governed by the nature of the insurance or savings liabilities, the expected rate of return applicable on each class of asset and the capital available to meet the price fluctuations for each asset class, relative to the liabilities they support.
The Company is exposed to interest rate risk on the investment portfolio it maintains to meet the obligations and commitments under its non-linked insurance and investment contracts, in that the proceeds from the assets may not be sufficient to meet the Company's obligations to policyholders.	LGR, LGI and Savings	Asset liability matching significantly reduces the Company's exposure to interest rate risk. IFRS sensitivity to interest rate changes is included in our analysis and disclosed in our financial statements.

C.2.2 Risk concentration

The Company holds a significant portfolio of investment assets to meet our obligations to policyholders. Investment classes include equities, bonds, properties and cash. Some exposure to concentration risk is an inherent aspect of operating significant portfolios of investment assets. However, we have limited appetite for the scale or frequency of events anticipated in investment management strategies materially diverging from expectations as a consequence of significant accumulations of exposure to a single event or counterparty. Where required, we will set limits on the maximum aggregate exposures to investment, banking and reassurance counterparties, sectors and geographies.

Concentrations of risk are reported as part of the Group's risk monitoring and reporting framework. The risk management reports presented at divisional and group risk committees provide both qualitative and quantitative information on concentration risks, as well as on material risk drivers and mitigating actions taken where exposures are outside acceptable tolerances.

C.3 Credit risk

C.3.1 Risk exposure and controls

The Company is exposed to credit risk as a consequence of offering the principal products outlined in section A.1.2. Credit risk is the exposure to loss if another party fails to perform its financial obligations to the Company.

Principle risk	Division	Risk mitigations
Bond default risk A significant portfolio of corporate bonds and commercial loans are held to back the liabilities arising from writing annuities and general insurance business. Whilst the portfolio is diversified, the asset class is inherently exposed to the risk of issuer default, with financial loss.	LGR	Portfolio level and specific issuer limits are set by financial strength rating, sector and geographic region so as to limit exposure from a default event. Issuer limits are regularly reviewed to take account of changes in market conditions, sector performance and the re-assessment of financial strength by rating agencies and the Group's own internal analysts. Exposures are monitored relative to limits. Financial instruments are also used to mitigate the impact of rating downgrades and defaults. If appropriate, actions are taken to trade out investments at risk of default.

Principle risk	Division	Risk mitigations
Reinsurance counterparty risk Exposure to insurance risk is mitigated by ceding part of the risks assumed to the reinsurance market. Default of a reinsurer would require the business to be re-brokered potentially on less advantageous terms, or for the risks to be borne directly resulting in an increased exposure to insurance risk. Credit risk syndication also exposes the Company to counterparty default risks with the Company being required to carry an element of associated credit risk capital requirement on its balance sheet should the business not be re-brokered on the same terms.	LGR, LGI and General Insurance	When selecting new reinsurance partners for its protection business, the Group considers only companies which have a minimum credit rating equivalent to A- from Standard & Poor's. For each reinsurer, exposure limits are determined based on credit ratings and projected exposure over the term of the treaty. Actual exposures are regularly monitored relative to these limits. Similarly, for longevity and credit risk syndication transactions, the Group targets the use of strongly rated counterparties and seeks to ensure that positions are fully collateralised. The adequacy and quality of collateral is subject to ongoing monitoring.
Property lending counterparty risk As part of our asset diversification strategy, we hold property lending and sale and leaseback investments. We are inherently exposed to the risk of default by a borrower or tenant.	LGR and LGC	Each property lending and sale and leaseback investment transaction is subject to a due diligence process to assess the credit risks implicit in the transaction and confirm that any risk of default has been appropriately mitigated. We also protect our interests through taking security over the underlying property associated with the investment transaction.

C.3.2 Risk concentration

A significant portfolio of corporate bonds is held to back the liabilities arising from writing annuities and general insurance business. The Company can be exposed to concentrations of credit risk within the portfolio from events impacting a specific sector or geography or through concentrations of exposure to an individual counterparty. Accumulations of exposures to credit risk in relation to individual counterparties can also arise through holdings in cash, equities, bonds and property and through reinsurance and as a result of delegated premium collection arrangements.

The Company manages the credit concentration risk by setting quantitative limits on maximum exposures to counterparties. The Group Credit Risk Committee (GCRC) is responsible for reviewing the aggregate exposures for the Group and the credit portfolios backing the Company's annuity liabilities and the extent to which specific limits are required for concentrations by counterparty, sector and geographic areas. Where exposures are identified as being outside acceptable ranges adjudicated by the Group Credit Risk Committee, it will initiate action with the relevant business firm(s) to manage the exposure.

C.4 Liquidity risk

C.4.1 Risk exposure

Liquidity and collateral risk is the risk that the Company, though solvent, either does not have sufficient financial resources available to enable it to meet its obligations as they fall due, or can secure them only at excessive cost. For Legal & General this means an amalgamation of:

The Company's exposure to liquidity risk primarily arises from contingent events including pandemic mortality, weather events and timing difference of cash flows, such as claims due to policyholders and other operational cash flows. The Company is also exposed to 'collateral risk' under its derivatives contracts which could require the firm to post assets eligible as collateral at short notice.

C.4.2 Liquidity risk

Principal risk	Division	Risk mitigations
Contingent event risk Events that result in liquidity risk may include a flu pandemic or natural disaster leading to significantly higher levels of claims than would normally be expected, or extreme events impacting the timing of cash flows or the ability to realise investments at a given value within a specified timeframe.	LGI	The Company seeks to ensure that it meets its obligations as they fall due and avoids incurring material losses on forced asset sales in order to meet those obligations. A limited level of contingent liquidity risk is however an accepted element of writing contracts of insurance. It is furthermore a consequence of the markets in which the Company operates and the executions of investment management strategies. However, the Group's insurance businesses seek to maintain sufficient liquid assets and standby facilities to meet a prudent estimate of the cash outflows that may arise from contingent events. The level of required liquidity is identified using techniques including stress tests for shock events, with the profile of actual liquid assets being regularly compared to the required profile. The Group's treasury function provides formal facilities to the rest of the Group to cover contingent liquidity requirements arising from more extreme events and where investment assets may not be readily realisable.
Collateral risk Within the annuities businesses, the use of financial instruments to hedge default, interest rate, currency and inflation risks can require the posting of collateral with counterparties, and as such an appropriate pool of the asset types specified by counterparties must either be held or readily available.	LGR	Liquidity requirements to meet potential collateral calls are actively managed. Typically within the overall fund of investment assets held to meet the long-term liabilities arising from annuity business, £600m is held in cash and other highly liquid investment types for general liquidity purposes. As at 31 December 2016 eligible assets worth five times the outstanding collateral were held (using the most representative definition of collateral contained within the Company's different collateral agreements).

Other risks	Division	Risk mitigations
Investment liquidity risk Within the with-profits fund, exposure to liquidity risk may arise if the profile of investment assets held to meet obligations to policyholders is not aligned with the maturity profile of policies, or the profile does not adequately take account of the rights of policyholders to exercise options or guarantees to specified early surrender terms or minimum rates of return.	Savings	Liquidity risk is managed ensuring that an appropriate proportion of the fund is held in cash or other readily realisable assets to meet each tranche of maturities and anticipated early withdrawals as they fall due. Where policyholders have discretion to require early payment of policy proceeds, contractual safeguards are in place to ensure that the fund and remaining policyholders are not disadvantaged should a material number of policyholders exercise this discretion.
Non-participating savings contracts are exposed to liquidity risk in that certain asset classes in which underlying funds invest, such as property, may not be readily realisable in certain market conditions, or are realisable at a diminution of value.	Savings	Liquidity risks associated with non-participating savings contracts are documented and communicated to customers within product terms and conditions. The terms also highlight that for certain asset classes such as property, the Group retains the right to defer the processing of fund withdrawal requests for up to six months, should underlying assets need to be realised to meet payment requests.
Direct lending, sales and leaseback investments and lifetime mortgage business are inherently illiquid forms of investment, with limited secondary markets to realise the value of assets outside agreed redemption terms.	LGR	Given the illiquid nature of the annuity and other liabilities, the Company is able and willing to take advantage of the premium offered by illiquid assets. The Company, however, sets limits on the overall exposure to illiquid investment types taking account of the nature and type of liabilities that the assets are held to meet.

C.4.3 Liquidity risk management

The Company does not seek exposure to liquidity risk as a part of its business model, but accepts that exposure to liquidity risk can arise as a consequence of the markets in which it operates, the products that it writes and through the execution of investment management strategies.

Overall, the Company maintains sufficient funds for business as usual purposes. Furthermore, it seeks to ensure that exposures to liquidity risk which arise across the Group are effectively managed so that the Company is able to meet payment and collateral obligations under unlikely but plausible, extreme liquidity scenarios.

It is the Group's policy that business divisions remain self-sufficient from a liquidity perspective by maintaining sufficient liquid assets and assessing the appropriateness of the composition of the assets in terms of their nature, duration and liquidity to meet obligations as they fall due. The business divisions also need to maintain sufficient eligible assets to meet collateral requirements that arise from their normal business conduct and under the two defined stressed scenarios. To the extent that a business division is not self-sufficient it is required to have a committed credit facility (standby facility) with the Group Treasury function to cover the risk exposure.

The primary sources of liquidity across the Company are cash and gilts. In addition the Group has a committed revolving syndicated facility.

C.4.4 Liquidity stress testing

The exposure to liquidity risk is measured by a liquidity coverage ratio (LCR) under the two prescribed liquidity stress scenarios. The main purpose of the model is to measure the compliance to the approved risk appetite defined in the Group Liquidity Risk Policy. As a group standard the liquidity stress testing is performed monthly or more frequently if needed.

LCR is defined as total sources of liquidity divided by total liquidity requirements and is calculated separately for each business division, entity, and Group Treasury.

The Group Treasury function works with the business divisions to ensure that, at a local and entity level, businesses have developed and implemented their own liquidity risk framework and models, based on the assumptions and processes set out by Group Treasury. The framework and assumptions are reviewed and reaffirmed annually.

C.4.5 Expected profit in future premiums

The total amount of the expected profit included in future premiums (EPIFP) as calculated in accordance with Article 260(2) of the Solvency II Delegated Regulation[4] was £2,728m as at 31 December 2016 as seen in Column C0010, Row R0790 of the Own Funds QRT S.23 in Annex 1.

C.5 Operational risk

C.5.1 Risk exposure and management

Operational risk is defined as loss arising from inadequate or failed internal processes, people, systems or external events. Potential for exposure to operational risk extends to all the Group's businesses. The Group has constructed a framework of internal controls to minimise material loss from operational risk events recognising that no system of internal control can completely eliminate the risk of error, financial loss, fraudulent action, or reputational damage.

Mitigation techniques are deployed via the Group's internal control framework, which comprises the systems, processes and procedures that ensure business operations are conducted so as to meet our obligations to all stakeholders, comply with regulation and legislation, and minimise the risk of material error or fraud. We aim to implement effective controls (both preventative and detective) to reduce operational risk exposures, except where the costs of such controls exceed the expected benefits. We accept that no system of control will eliminate the risk of financial loss or reputational damage, and we expect all employees to report weaknesses and deficiencies as soon as they are identified.

A variety of sensitivity tests have been undertaken within the calibration of the operational risk SCR, including: using alternative distribution shapes for operational risk scenarios; applying different techniques to combine scenarios; and varying correlation assumptions. The sensitivity tests employed have identified no material concerns with the results of the standard calibration.

We have not identified any material risk concentrations for operational risk.

C.6 Other material risks

Other material risks, such as conduct risk, have been included in the above assessment of the Company's risk profile.

[4] Commission Delegated Regulation (EU) 2015/35.

C.7 Any other information

C.7.1 Sensitivities

As part of the ORSA process a range of stress tests are carried out. The following sensitivities are provided to give an indication of how the Group's Solvency II surplus as at 31 December 2016 would have changed in a variety of events. These are all independent stresses to a single risk. In practice the balance sheet is impacted by combinations of stresses and the combined impact can be different from adding together the impacts of the same stresses in isolation. It is expected that, particularly for market risks, adverse stresses will happen together.

Risk	Description	Impact on net of tax capital surplus 2016 £bn	Impact on Solvency II coverage ratio 2016 (%)
CREDIT	Credit spreads widen by 100bps assuming a level addition to all ratings[1]	0.2	6
	Credit spreads widen by 100bps assuming an escalating addition to ratings[1,2]	0.2	5
	Credit spreads narrow by 100bps assuming a level addition to all ratings[1]	(0.42)	(5)
	Credit spreads narrow by 100bps assuming an escalating addition to ratings[1,2]	(0.2)	(4)
	Credit migration[3]	(0.5)	(7)
MARKET	20% fall in equity markets	(0.3)	(4)
	40% fall in equity markets	(0.6)	(7)
	20% rise in equity markets	0.3	4
	15% fall in property markets	(0.1)	(1)
	15% rise in property markets	0.1	1
	100bps increase in risk free rates	0.7	16
	50bps fall in risk free rates[4]	(0.4)	(8)

Risk	Description	Impact on net of tax capital surplus 2016 £bn	Impact on Solvency II coverage ratio 2016 (%)
UNDERWRITING	1% reduction in annuitant base mortality	(0.1)	(2)
	1% increase in annuitant base mortality	0.1	2
	Substantially reduced risk margin[5]	0.1	1

1. The spread sensitivity applies to the Company's corporate bond (and similar) holdings, with no change in the Company's long-term default expectations.
2. The stress for AA bonds is twice that for AAA bonds, for A bonds it is three times, for BBB four times and so on, such that the weighted average spread stress for the portfolio is 100bps.
3. Credit migration stress covers the cost of an immediate big letter downgrade on c.20% of annuity portfolio bonds, or three-times level expected in the next 12 months.
4. In the 'interest rate down' stress negative rates are allowed, i.e. there is no floor at zero.
5. This represents a reduction of two-thirds in risk margin (RM) and subsequent recalculation of the TMTP.

In the sensitivity for credit spreads, corporate bond yields have increased by 100bps, gilt and approved security yields are unchanged, and there has been no adjustment to the default assumptions.

The annuitant mortality stress is a 1% change in the mortality rates for immediate and deferred annuitants with no change to the mortality improvement rates.

The above sensitivity analysis does not reflect management actions which could be taken to reduce the impacts. In practice, the Group manages its asset and liability positions to respond to market movements. The above table does allow for the recalculation of the TMTP in line with management's view of the underlying risks.

The impacts of these stresses are not linear therefore these results should not be used to extrapolate the impact of a smaller or larger stress. The results of these tests are indicative of the market conditions prevailing at the balance sheet date. The results could be different if performed at an alternative reporting date.

In addition to the sensitivities in the table above, the Group also considers extreme likelihood stresses. As the Company participates in the general insurance catastrophe reinsurance programme, the 1-in-250 windstorm and coastal flood stress would result in a loss to the Company of £258m. The total loss to Legal & General as a group would be £354m as a result of such an event. It should be highlighted that it is more likely for multiple events to occur and produce a gross loss of £565m rather one single event causing this amount of loss, which would not impact on the Company.

C.7.2 Material changes to the risk profile over the reporting period

As part of the ORSA the Company has reviewed all material risks; credit and market risks and longevity improvements remain our key risk exposures. These risk exposures are expected to remain relatively stable. Over the reporting period longevity exposure has increased due to the reduction in interest rates.

D. Valuation for Solvency purposes

D.1 Assets

The Company's assets as at 31 December 2016 are as below:

Assets (£m)	Reference	Solvency II	IFRS	Variance
Deferred acquisition costs	D1.1.1		559	(559)
Intangible assets	D1.1.1		19	(19)
Deferred tax assets	D1.1.2		5	(5)
Property, plant and equipment held for own use	D1.1.3	8	8	-
Investments (other than assets held for index-linked and unit-linked contracts)		72,380	72,131	249
Property (other than for own use)	*D1.1.4*	*409*	*409*	-
Holdings in related undertakings, including participations	*D1.1.5*	*1,325*	*1,076*	*249*
Equities	*D1.1.6*	*3,687*	*3,687*	-
Bonds	*D1.1.7*	*56,425*	*56,425*	-
Collective investments undertakings	*D1.1.8*	*6,639*	*6,639*	-
Derivatives	*D1.1.9*	*3,684*	*3,684*	-
Deposits other than cash equivalents	*D1.1.10*	*211*	*211*	-
Assets held for index-linked and unit-linked contracts	D1.1.11	27,387	27,387	-
Loans and mortgages	D1.1.12	1,581	1,581	-
Reinsurance recoverables	D1.1.13	22,878	24,780	(1,902)
Deposits to cedants	D1.1.14	906	906	-
Insurance and intermediaries receivables	D1.1.15	79	79	-
Reinsurance receivables	D1.1.16	170	170	-
Receivables (trade, not insurance)	D1.1.17	1,725	1,725	-
Cash and cash equivalents	D1.1.18	671	671	-
Total Assets		127,785	130,021	(2,236)

Note: Assets held for index-linked and unit-linked contracts include linked derivative liabilities of £41.3m in line with Solvency II presentational requirements. There is an equal and opposite difference in total assets and liabilities between the IFRS values above and the IFRS values within the statutory accounts.

D.1.1 Solvency II valuation basis

Unless otherwise stated, assets and liabilities have been recognised in conformity with International Financial Reporting Standards (IFRS), as adopted by the EU.

Individual assets and liabilities have been valued separately and can offset each other, where permitted, in accordance with IFRS accounting principles.

Assets and liabilities (other than deferred tax) have been valued:

- on a going concern basis;
- in accordance with Article 75 of the Solvency II Directive or where specifically provided for by Delegated Acts:

- where IFRS valuation is consistent with Article 75 this shall be adopted, therefore Solvency II economic value is equal to IFRS fair value in line with IFRS unless otherwise stated;
- where more than one valuation method is prescribed by IFRS, only valuation methods that are consistent with Article 75 shall be applied.

D.1.1.1 Deferred acquisition costs (DAC) and intangibles

Intangible assets are valued at zero unless:

- the intangible asset can be sold separately; and
- it can be demonstrated that there is a value for the same or similar assets (i.e. that a value has been derived from quoted prices in active markets).

As at December 31 2016 none of the intangible assets (including DAC) that the Company held met these criteria and therefore are valued at zero on the Solvency II balance sheet. This results in a £559m valuation difference arising on DAC and an £19m valuation difference arising on other intangibles between the Solvency II and IFRS valuations.

D.1.1.2 Deferred tax assets

The valuation of deferred tax assets is consistent with the deferred tax liability methodology. Further details of this methodology are provided in section D.3.4 below.

D.1.1.3 Property, plant and equipment (PPE)

Property plant and equipment is valued in accordance with their treatment under IFRS, and there is no valuation difference under Solvency II.

D.1.1.4 Property (other than for own use)

The valuation of the Company's property assets are provided by external valuation experts on a regular basis which are calibrated to recent similar transactions. The external valuations are performed in line with professional standards.

Property is carried at fair value and in the UK is valued quarterly by independent valuers on the basis of open market value as defined in the appraisal and valuation manual of the Royal Institute of Chartered Surveyors. Valuation techniques may include discounted cash flow calculations using net current rent, and estimated and terminal values. They may also include yield methodology calculations using market rental values capitalised with a market capitalisation rate. Both of these are then further validated against actual market transactions to produce a final valuation.

D.1.1.5 Holdings in related undertakings, including participations

The Company has participations that are not quoted in active markets. Under Solvency II, these are valued using an adjusted equity method where the value of the investment is determined as the Company's share of the subsidiary's net assets valued in accordance with the Solvency II valuation rules. The valuation rules under Solvency II, and in particular the rules around the valuation of technical provisions of the insurance subsidiaries, are different from IFRS. The application of these rules has led to a difference of £249m between IFRS and Solvency II.

D.1.1.6 Equities

Equity investments are measured at fair value in accordance with IFRS. The fair values of quoted financial investments are based on bid prices. If the market for a financial investment is not active, the Group establishes fair value using valuation techniques such as recent arm's length transactions, consensus market pricing, reference to similar listed investments, discounted cash flow models or option pricing models (see section D.4 Alternative methods for valuation below for further information on valuation techniques).

Private equity investments are valued in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which represent current best practice. The techniques used for determining fair value include earnings multiples, the price of a recent investment or a net asset basis. There is no valuation difference from IFRS.

D.1.1.7 Bonds

Bond investments are measured at fair value in accordance with IFRS. Where available, valuations are based on quoted market prices. Where quoted prices are not available, fair value estimates are made at a point in time, based on relevant market data, as well as the best information about the individual financial investment (see section D.4 Alternative methods for valuation below for further information on valuation techniques). There is no valuation difference from IFRS.

D.1.1.8 Collective investment undertakings

Collective Investment Undertakings are measured at fair value in accordance with IFRS. Where available, valuations are based on quoted market prices. Where quoted prices are not available, fair value estimates are made at a point in time, based on relevant market data, as well as the best information about the individual financial investment (see section D.4 Alternative methods for valuation below for further information on valuation techniques). There is no valuation difference from IFRS.

D.1.1.9 Derivatives

Derivatives are measured at fair value in accordance with IFRS. Where available, valuations are based on quoted market prices. Where quoted prices are not available, fair value estimates are made at a point in time, based on relevant market data, as well as the best information about the individual financial investment. There is no valuation difference from IFRS.

D.1.1.10 Deposits other than cash equivalents

Deposits other than cash equivalents are measured at fair value, and there is no valuation difference between Solvency II and IFRS.

D.1.1.11 Assets held for index-linked and unit-linked funds

Investment assets held for index-linked and unit-linked contracts are measured at the fair value of the underlying assets and liabilities (other than technical provisions) held within such funds. There is no valuation difference from IFRS.

D.1.1.12 Loans and mortgages

The Company has recognised Lifetime Mortgage business in this asset class.

Policy loans are valued using the amortised cost basis under IFRS. This approach is deemed to be prudent and appropriate for use in the Solvency II balance sheet, where the amount of policy loans is not material to the reporting entity balance sheet, as is the case for the Company.

D.1.1.13 Reinsurance recoverables

The reinsurance recoverables and gross liabilities are calculated consistently with the best estimate liability in all cases, save that there is an allowance for the probability weighted best estimate of external reinsurer default. The reinsurance recoverables have reduced by £1.9bn under Solvency II. This difference is primarily driven by different underlying assumptions used in calculating the provisions.

D.1.1.14 Deposits to cedants

Deposits to cedants are valued at fair value, in accordance with their treatment in IFRS.

D.1.1.15 Insurance and intermediaries receivables

Insurance and intermediaries receivables are valued at fair value, in accordance with their treatment in IFRS.

D.1.1.16 Reinsurance receivables

Reinsurance receivables have been valued in accordance with their treatment in IFRS.

D.1.1.17 Receivables (trade not insurance)

Trade receivables are short term in nature and are valued in line with IFRS on a cost basis on materiality grounds.

D.1.1.18 Cash and cash equivalents

Cash and cash equivalents are valued at fair value in accordance with IFRS.

D.1.2 Valuation uncertainty

The Company values its assets in accordance with Article 10 of the Solvency II Delegated Regulation. Valuations of assets are underpinned by a system of processes and controls to ensure that the Company complies with Article 267 of the Solvency II Delegated Regulation. Included within these processes is an assessment of valuation uncertainty and the extent to which asset valuations are appropriate in light of uncertainties that exist. This processes focus on, although is not limited to, assets that are valued using alternative valuation techniques. The Company has concluded that its assets are valued appropriately in accordance with Article 10 of the Solvency II Delegated Regulation and appropriately reflect consideration of valuation uncertainty.

D.2 Technical provisions

A summary of the Company's technical provisions is set out below:

Technical provisions (£m)	With-profit participation	Index-linked and unit-linked insurance	Other life insurance	Accepted reinsurance	Health insurance	Non-life non-proportional property reinsurance	Total
Best estimate liability	10,636	41,558	48,366	3,039	449	(0)	**104,048**
Risk margin	122	60	5,167	376	2	2	**5,729**
Transitional measure on technical provisions	(85)	(32)	(5,553)	(330)	-	-	**(6,000)**
Technical provisions total	**10,673**	**41,586**	**47,980**	**3,085**	**451**	**2**	**103,777**

Note: The non-life general liability insurance is negligible (<0.5m) and is not split out in the table above.

The table above provides an overview of the Company's technical provisions split by Solvency II LoB. As the Legal & General Group is managed across divisions rather than legal entities, the technical provisions are shown below by Solvency II LoB and Division.

Total technical provisions (£m)	With-profit participation	Index-linked and unit-linked insurance	Other life insurance	Accepted reinsurance	Health Insurance	Non-life non-proportional property reinsurance	Total
LGR	-	-	46,501	3,501	-	-	**50,002**
Insurance	-	-	1,221	(416)	451	2	**1,258**
Savings	10,673	41,586	184	-	-	-	**52,443**
Other	-	-	74	-	-	-	**74**
Technical provisions total	**10,673**	**41,586**	**47,980**	**3,085**	**451**	**2**	**103,777**

The majority of the Company's risk margin (RM) is attributed to business divisions apart from an Operational Risk RM element (£74m) which is held at the entity level to cover risks such as tax, mis-selling and balance sheet mis-statement.

D.2.1 Solvency II valuation basis

D.2.1.1 Methodology

The technical provisions (TPs) are calculated as the sum of the best estimate liabilities (BEL) of £104,048m and the risk margin (RM) of £5,729m less the transitional measure on technical provisions (TMTP) of £6,000m, calculated in line with PRA approvals and allowing for the change in capital requirements from the old Solvency I regime.

The BEL reflects the probability-weighted average of future cash flows, taking into account the time value of money (expected present value of future cash flows) using the relevant risk-free interest rate term structure (including the matching adjustment where relevant). Deterministic and stochastic valuation techniques are used to calculate the BEL.

The main cash flows cover premiums, future financial obligations of policyholder benefits, and expenses of running the business (including investment expense and commission payments). Future management actions are allowed for, where these are deemed to be objective, realistic and verifiable. The management actions used in the calculation of the TPs consider the time delays and costs applicable to their implementation.

The BEL is calculated gross, without deduction of the amounts recoverable from reinsurance contracts and special purpose vehicles, but includes expenses in respect of these arrangements. The BEL is calculated at a level deemed appropriate for homogeneous risk groupings, at a minimum by line of business segmented according to Chapter 10 of the TPs part of the Prudential Regulation Authority (PRA) Rulebook for Solvency II firms. The BEL is based on exposures as at 31 December 2016.

Future premiums are only considered for the period up to where the policyholder or the Company has the option to establish, renew, extend, increase or resume the insurance contract. . Except for LGA business ceded to the Company, where the contract boundary is the maximum age in the contract, typically age 95 for Term assurance business.

Business not included in the full cash flow projections on materiality grounds is explicitly allowed for in the BEL through manual adjustments. The most material un-modelled business reflects the non-participating Conventional Pensions business within the with-profits BEL. This reflects less than 0.5% of the gross BEL. There are two instances where BEL modelling simplifications are used, namely the allowance for catastrophe risk (e.g. epidemic and event risks) and mass lapse risk where data is limited and the probability weighted mean is not allowed for in the BEL. For these risks there is a corresponding SCR overstatement offsetting this on the Solvency II balance sheet.

The RM is the cost that would be incurred in holding eligible Own Funds (as defined in the Own Funds part of the PRA Rulebook for Solvency II firms) to cover the SCR necessary to support the insurance and reinsurance obligations over their lifetime, determined using a cost of capital rate. The RM is calculated separately from the BEL. The RM is the present value of the cost of capital required, to cover the SCR for certain defined risks (referred to here as the RM capital requirement), to meet adverse deviations on the underlying best estimate cash flows over the full run-off of the business. The RM capital requirement covers underwriting risk, credit risk associated with reinsurance contracts and operational risk. Future new business is not allowed for in the RM capital requirement. No allowance is made for the loss-absorbing capacity of deferred taxes as referred to in Article 108 of Directive 2009/138/EC.

The RM is calculated for the Company as a whole, allowing for diversification between the risks within the entity. The discount rate used in the cost of capital calculation is the relevant basic risk-free rate (excluding matching adjustment). The cost of capital rate is set to 6% as prescribed in Article 39 of the Delegated Regulation.

Where investment management agreements are in place with Legal and General Investment Management Limited, the TPs are calculated using investment expenses on a fees (rather than costs) basis.

The calculation of the TPs is dependent on the quality of the data underlying the calculations. The data has been assessed in line with Article 48 of Directive 2009/138/EC. This assessment has concluded that the quality and sufficiency of data used in the preparation of the above TPs is such as to enable a reliable and adequate calculation of the technical provisions.

Further information on material elements of the technical provisions by division is set out below:

D.2.1.1.1 Legal & General Retirement (LGR)

Best estimate liabilities (BEL)

Deterministic actuarial projection models are used, in line with the methodology described above.

In addition, Insurance undertakings are permitted to apply a matching adjustment (MA) to the relevant risk-free interest rate term structure when calculating the best estimate of a portfolio of life insurance obligations, subject to prior approval by the supervisory authorities. Legal & General has been approved by the PRA to use a MA when calculating the BEL for the majority of annuity business held within the Company. This has been applied in line with the approved application.

Risk margin (RM)

The RM capital requirement is projected forward for each future year over the run-off of the business.

Longevity is the most material component of the RM capital requirement. Consequently, the RM calculation allows for more accuracy in calculating this component. Best estimate and stressed future cash flows are projected to capture the capital requirement at future points in time and the discounted cost of capital is applied. The capital requirement for other risk sub-groups are projected using a proxy approach i.e. the projected capital requirements are estimated using appropriate carrier variables.

The Matching Adjustment Portfolio in LGR is not assumed to be ring-fenced for the purpose of the risk margin calculation.

D.2.1.1.2 Legal & General Insurance (LGI)

Best estimate liabilities (BEL)

Deterministic actuarial projection models are used, in line with the methodology described above.

Risk margin (RM)

The RM capital requirement is projected for each future year over the run-off of the business by risk sub-group. The RM capital requirement is estimated, using appropriate proxy carrier variables e.g. percentage of BEL.

For reinsurance accepted from Legal & General America (LGA), the RM capital requirement is projected over the run-off of the business, with run-off factors determined by projecting the in-force business with real world best estimate assumptions to discrete points in the future. The capital requirement in intermediate years is calculated using linear interpolation. Stresses are applied to the individual non-hedgeable risk types. The RM capital requirement as at the valuation date is projected forward using these run-off factors.

D.2.1.1.3 Savings including Workplace Savings

Best estimate liabilities (BEL)

Deterministic and stochastic valuation techniques are used, in line with the methodology described above.

Stochastic valuation techniques are used where the cash flows exhibit the presence of material financial options and guarantees and management actions that are employed in the management of the with-profits fund. Deterministic actuarial projection models are used for all other BEL calculations.

For unit-linked business, the total BEL is split by unit and non-unit components. The unit BEL is the actuarially funded value of current units, including guaranteed additional units.

The with-profits fund has the ability to employ a range of management actions in the management of its business, as set out in the Company’s Principles and Practices of Fund Management (PPFM). In accordance with Article 225 of the Delegated Regulation, future management actions have been allowed for in the BEL, provided that they are objective, realistic and verifiable. The impact of changes in policyholder behaviour has also been reflected in the BEL.

The surplus funds in respect of with-profits business refer to accumulated profits which have not been made available for distribution to participating policyholders at the valuation date. The surplus funds reflect the Own Funds, excluding the effect of the RM, the transitional measure on technical provisions allocated to the with-profits fund and excluding the present value of future shareholder transfers defined in relation to future discretionary benefits. Surplus funds are shown in Annex 1 QRT S.23 Own funds in R0070. Permanent enhancements to benefits resulting from the previous distribution of surplus assets are allowed for in the appropriate BEL.

Risk margin (RM)

The RM capital requirement is projected forward for each future year over the run-off of the business. The RM capital requirement is estimated using appropriate proxy carrier variables e.g. percentage of BEL.

D.2.1.1.4 General insurance

The general insurance catastrophe reinsurance BEL is comprised of the claims and premium provision.

D.2.1.2 Main assumptions

This section covers the assumptions used in the calculation of the BEL for the Company's long-term insurance business.

Cash flow projections are determined using best estimate assumptions for each component of cash flow and for each policy group. The assumptions used in the valuation of the BEL are the same best estimate assumptions as the basis for calculating IFRS assumptions, excluding the margin for prudence included within the IFRS assumptions. In some cases where the class of business is immaterial the BEL uses the same assumptions as used in the IFRS reserves.

The best estimate assumptions are derived by reference to the most recent experience and any relevant market data (e.g. future mortality improvement factors issued by the Continuous Mortality Investigation Bureau).

Assumptions are set by following an established methodology which has been discussed with the Board.

Assumptions are set for homogeneous risk groups to avoid introducing distortions that might arise from combining business with different characteristics. At a minimum, these groupings are by line of business segmentation stipulated by the European Insurance and Occupational Pensions Authority (EIOPA).

D.2.1.2.1 Economic assumptions

The economic assumptions have been set such that they reflect the economic conditions at the valuation date.

Risk free yield curve

The valuation interest rate is based on a risk-free yield curve. The risk-free rate used is calculated based on the methodology specified by EIOPA, which is applied to construct zero coupon base rates from the underlying swap rates. The Company uses a continuously compounding version of this rate.

The Company has received approval from the PRA to apply a matching adjustment, which allows for an increase to be applied to the risk-free yield curve for the MA portfolios. No other adjustments have been made to the risk-free rate.

Inflation

Expense and unit cost inflation rates have been set by reference to external indicators as at the valuation date. Claims inflation, such as RPI-linked annuities, is set using an assessment of inflation implied by UK government bond yields or inflation swap curves.

Unit growth

For the calculation of the non-unit BEL on linked contracts, an assumption regarding the rate of future unit growth is required. The assumption made is that the growth rate before charges is the same as the risk free discount rate.

Participating business

The stochastic model is based on a large number of market consistent economic scenarios derived from assumptions consistent with the deterministic assumptions. The model is calibrated using market data from a variety of sources. This enables assumptions to be determined for the term structure of risk-free interest rates, and for property and equity volatility.

Risk-free interest rates are determined as described above. Property volatility is set with reference to historic variations in property prices. Equity volatility is set so that the model reproduces observed market prices of traded equity derivatives. Correlations between asset classes are based on historic data.

Each investment scenario contains a consistent set of assumptions for investment returns and inflation.

D.2.1.2.2 Non economic assumptions

Expenses

The cash flow projection used to calculate the BEL takes into account administrative, investment, claims and acquisition expenses, allowing for future expense inflation. The assumptions for long-term maintenance unit costs are set based on the forecast expenses, suitably adjusted where necessary, and include overhead expenses in line with the approved methodology.

Mortality and morbidity

Regular investigations of mortality and morbidity experience against appropriate base tables are conducted, with the portfolio segmented by groups of contracts that are expected to exhibit similar mortality and/or morbidity trends. An investigation is normally carried out from time to time (typically every three years) to review the fit of the experience to an appropriate base mortality table. In other years, assumptions are compared to the results of the most recent experience investigations and revised where the experience implies a shift that is likely to be due to more than random fluctuation. The best estimate assumption allows for claims incurred but not reported by the investigation date.

The assumption for annuitant mortality is set as a combination of a base table (i.e. the rate of mortality currently experienced by annuitants) plus future improvements (i.e. how the rates of mortality will change over time).

The mortality basis for retail protection business is set as a base table plus an allowance for deterioration in respect of contracts with critical illness cover benefits. Future mortality improvement assumptions are made for whole of life products.

For some classes where the reserves are insensitive to the chosen level of mortality, no investigation is carried out but an assumption that is demonstrably prudent is used.

Persistency

Persistency experience can include lapses, take-up rates for guaranteed annuity options, partial withdrawals and early retirement, where relevant. Persistency rates are reviewed annually for most products to determine the best estimate. This investigation generally uses three years of data with a six month delay, to allow for lapses that the Company has not been notified of at the date of the investigation, to generate weighted average (by premium) lapse rates. The long-term persistency assumptions are set using these lapse rates. Alternative approaches are used if it is considered that the exposure is insufficient for the experience to be credible, observed lapse rates are excessively volatile or it is expected that the lapse experience will change in future.

Participating business

Participating business requires additional assumptions on future management and policyholder actions.

Future bonuses

Future reversionary and terminal bonuses are consistent with the bonus policies set out in the Company's Principles and Practices of Financial Management (PPFM).

Guaranteed annuity options

The guarantees are valued on a market consistent basis. The valuation methodology allows for the correlation between interest rates and the proportion of the policyholders who take up the option.

Guaranteed cash options

The liability is determined assuming that policyholders choose the most valuable alternative between the annuity and cash available at retirement.

Further details of the main assumptions are provided in Annex 2 of this report.

D.2.1.3 Material changes in assumptions compared to the previous reporting period

This is the first annual report since the Solvency II regime took effect, and as such no comparative assumptions are provided relating to the position during the previous solvency regime.

D.2.1.4 Transitional measures

The Company does not apply the transitional risk-free interest rate-term structure.

The Company applies the transitional measure to the technical provisions (TMTP). As at 31 December 2016 the impact of not applying the transitional measure is provided in the table below:

(£m)	Regulatory basis	Impact	Adjusted balance
Technical provisions	103,777	6,000	109,777
SCR	7,544	977	8,521
MCR	1,886	244	2,130
Basic Own Funds	11,630	(4,964)	6,666
Eligible Own Funds for SCR	11,630	(4,964)	6,666
Eligible Own Funds for MCR	11,630	(4,964)	6,666
Capital coverage ratio	154%	(76)%	78%
MCR coverage ratio	617%	(304)%	313%

The TMTP has been calculated in line with PRA approvals. The TMTP of £6,000m is broadly equivalent to the impact of the risk margin of £5,729m.

D.2.1.5 Volatility adjustment

The Company does not apply a volatility adjustment.

D.2.1.6 Matching adjustment (MA)

In common with other UK annuity providers, the Company has received approval from the PRA to apply a matching adjustment, in line with Article 77b of Directive 2009/138/EC.

As at 31 December 2016 the impact of change to zero of the MA is provided in the table below:

(£m)	Regulatory basis	Impact	Adjusted balance
Technical provisions	103,777	7,506	111,283
SCR	7,544	8,378	15,922
MCR	1,886	2,095	3,981
Basic Own Funds	11,630	(6,230)	5,400
Eligible Own Funds for SCR	11,630	(6,230)	5,400
Eligible Own Funds for MCR	11,630	(6,230)	5,400
Capital coverage ratio	154%	(120)%	34%
MCR coverage ratio	617%	(481)%	136%

1. The impact is measured as the change due to setting the MA to zero. The impact has been calculated assuming no further recalculation of the TMTP.

The MA is applied as an addition to the risk-free interest rate term structure and applies to individual annuities and certain bulk purchase annuity schemes that meet the approved eligibility criteria. The assets contained within the matching adjustment portfolios are predominantly corporate bonds, but also long-term direct investments held in MA-eligible structures, such as infrastructure investments and lifetime mortgages.

Losing MA approval is a remote risk for the business; however Article 296(2d) of the Solvency II Delegated Regulation requires the disclosure of the impact of a change to zero of the matching adjustment. We have an extensive controls framework to ensure our on-going MA compliance and we have a regular dialogue with the PRA about our MA strategy.

D.2.2 Reconciliation between IFRS and Solvency II valuation of gross BEL

The table below bridges the BEL under Solvency II to the IFRS liabilities.

YE 2016 (£m)	Insurance	LGR	Savings	Total
Closing gross IFRS liabilities *	**4,397**	**53,768**	**54,097**	**112,262**
Data changes	-	(96)	(1)	**(97)**
Model changes	(27)	-	-	**(27)**
Non-economic assumptions	(2,599)	(3,868)	-	**(6,467)**
Economic assumptions	253	2,049	-	**2,302**
Methodology changes	(958)	(1,247)	(1,720)	**(3,925)**
Closing Solvency II Gross BEL	**1,066**	**50,606**	**52,376**	**104,048**

* The gross IFRS liabilities in the table above are consistent with the insurance and investment contract liabilities in the year ended 2016 Legal and General Assurance Society Limited Statutory Accounts excluding outstanding claims liability of c.£369m, but allowing for with-profit unallocated distributable surplus of c.£699m and the value of in-force non-participating business in the with-profit fund of c.£169m.

The reduction in liabilities from non-economic assumptions differences primarily relates to the removal of margins for adverse deviation allowed for in the IFRS liabilities. The BEL is calculated using best estimate assumptions excluding these prudent margins.

The increase in liabilities from economic assumption differences primarily relates to the move from discounting the cash flows at a prudent valuation interest rate (VIR) under IFRS to using the risk free interest rate term structure plus matching adjustment (MA) for eligible liabilities under Solvency II. Implicit within this step is the allowance for investment expenses, which changes from an implicit allowance within the IFRS VIR to being an explicit cash flow under Solvency II. The same assumption applies under IFRS and under Solvency II; the only difference is in how it is allowed for, which should have very little impact.

£0.6bn of the methodology difference for Insurance is related to additional prudence within the IFRS calculation. A further £0.4bn difference relates to exchange rate impacts, reinsurance accepted new business and treaty changes.

For LGR, the £1.2bn methodology difference is made up of the difference between floating and fixed legs on longevity swaps (£0.5bn) as the floating legs include the prudent margins on the IFRS basis; a release of additional provisions for default risk and exchange rates that are held as IFRS liabilities, but under Solvency II are held within the Capital requirement (£0.6bn); and a difference arising from surplus asset hypothecation (£0.1bn).

The £1.7bn methodology difference for Savings includes £0.7bn of unallocated distributable surplus for with-profits business, which is not applicable under Solvency II. The remaining £1.0bn is mainly due to the difference in accounting treatment for negative non-unit liabilities where under IFRS a negative non-unit liability for investment business is not allowed while this is allowed under Solvency II.

Solvency II Line of business

The table below shows a comparison of Solvency II technical provisions and IFRS liabilities, split by Solvency II line of business.

YE 2016 (£m)	Solvency II	IFRS	Difference
Participating business	10,636	11,336	700
Index and unit-linked	41,558	42,453	895
Other life insurance	48,367	53,306	4,939
Reinsurance accepted (Life)	3,039	4,471	1,432
Health insurance	449	689	240
Health reinsurance accepted			
Non-life	(1)	7	8
Total liabilities	104,048	112,262	8,214
Risk margin	5,729		(5,729)
Transitional measure on technical provisions	(6,000)		6,000
Technical provisions	103,777	112,262	8,485

LGR business from the above table is predominantly included within the ‘other life insurance’ line above. Savings business is mostly included within ‘Index and unit-linked’ and Insurance is included within ‘Other life insurance’ and ‘Health insurance’.

D.2.3 Reinsurance recoverables

The calculation of the reinsurance recoverable asset is consistent with the calculation of the gross BEL described above, except that where a matching adjustment is applied to the gross BEL on eligible business, the equivalent reinsurance recoverable asset will be discounted at the risk-free interest rate term structure, excluding matching adjustment. The reinsurance recoverable asset is adjusted for the best estimate probability of reinsurer default, and includes an allowance for the timing difference between recoveries and reinsurance payments.

(£m)	With-profit participation	Index-linked and unit-linked insurance	Other life insurance	Accepted reinsurance	Health insurance	Non-life non-proportional property reinsurance	Total
Gross technical provisions	**10,673**	**41,586**	**47,980**	**3,085**	**451**	**2**	**103,777**
Reinsurance recoverables	0	14,847	7,592	350	88	0	**22,878**
Net technical provisions	**10,673**	**26,739**	**40,388**	**2,735**	**363**	**2**	**80,899**

Reinsurance recoverables are described in section D.1.1.13 above. The Company has no SPVs authorised under Article 211 of the Solvency II Directive.

D.2.4 Level of uncertainty associated with the value of technical provisions (TPs)

A framework to assess the confidence in the methodology and assumptions used to calculate the TPs has been established by the Group Audit Committee. The framework allocates a status to the confidence in each of the assumptions or methodologies, based on a mixture of qualitative and quantitative criteria. The criteria set out in the framework, and the initial assessments, have been challenged and validated by experienced actuaries and accountants throughout the business.

The assumptions underpinning the technical provision calculations are the best estimate view of the Company. As one of the UK's largest life companies, the Company has a significant amount of data regarding its own historic experience. Experience investigations using this data are undertaken regularly and the results used to inform the choice of best estimate assumptions. This is augmented by expert judgement, in particular where past experience is not considered to be an appropriate reflection of future expectations. Where there is a high level of expert judgement required, this has been highlighted in the confidence assessment. Confidence in the base annuitant mortality is good, but due to limited data, the longevity trend assumption has been highlighted as an area of future uncertainty. Overall the Company has a high degree of confidence in the assumptions underpinning technical provisions and hence the level of uncertainty in the technical provisions is low.

D.3 Other liabilities

As at 31 December 2016 the Company had other liabilities as follows:

Other liabilities	Reference	Solvency II (£m)	IFRS (£m)	Variance
Provisions other than technical provisions	D3.1	67	67	-
Pension benefit obligations	D3.2	161	-	161
Deposits from reinsurers	D3.3	5,258	5,258	-
Deferred tax liabilities	D3.4	1,207	370	837
Derivatives	D3.5	1,965	1,965	-
Debts owed to credit institutions		-	-	-
Insurance and intermediaries payables	D3.6	411	411	-
Reinsurance payables	D3.7	9	9	-
Payables (trade, not insurance)	D3.8	3,300	3,478	(178)
Any other liabilities, not elsewhere shown	D3.9	-	61	(61)
Total		**12,378**	**11,619**	**759**

Note: Assets held for index-linked and unit-linked contracts include linked derivative liabilities of £41.3m in line with Solvency II presentational requirements. There is an equal and opposite difference in total assets and liabilities between the IFRS values above and the IFRS values within the statutory accounts.

The following sections provide a quantitative and qualitative analysis of the differences in valuation between IFRS and Solvency II, as well as a description of the valuation methods used for each material class of other liability.

D.3.1 Provisions other than technical provisions

Provisions are valued in accordance with IFRS, at an amount representing best estimate of the expenditure required to settle the obligation or to transfer it to a third party at the balance sheet date.

D.3.2 Pension benefit obligations

In the Company's Solvency II balance sheet the with-profits fund's share of the surplus/deficit of the Group's defined benefit pension schemes is reported within Pension benefit obligations and technical provisions (TPs), as shown in the following table:

(£m)	2016
LGAS WP Pension benefit obligations (net of tax)	161
Loss absorbing capacity of technical provisions (LACoTP, included in technical provisions)	-47
Total LGAS WP Pension scheme deficit (net of LACoTP and tax)	**114**

Under Solvency II regulations no pension scheme deficit is required to be held on the solo balance sheets of legal entities. However, the Company's with-profits fund Pension scheme deficit is recognised on its solo balance sheet.

The Company's WP Pension benefit obligations relate to the following defined benefit schemes of the Group:

- Legal & General Group UK Senior Pension Scheme
- Legal & General Group UK Pension & Assurance Fund
- For Solvency II, the Group's defined benefit pension schemes are valued under the IAS19 basis, which uses a prescribed methodology also used in IFRS reporting.
- The Solvency II surplus/deficit is calculated as the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, provided any surplus in the fund is not restricted.

Under IFRS the Pension scheme deficit is reported in full at the Group level, the amount reported in the Company is zero.

D.3.3 Deposits from reinsurers

Deposits from reinsurers are valued at fair value in line with IFRS and there is no valuation difference between the two bases.

D.3.4 Deferred tax liabilities

Deferred tax assets and liabilities are recognised and valued in accordance with IFRS (IAS12), except that deferred tax assets and liabilities in respect of temporary differences are valued based upon the differences between the value of assets and liabilities in the Solvency II balance sheet and their value for tax purposes.

The Company has a total deferred tax liability on the balance sheet of £1.2bn, comprised of the following material components:

(£m)	Solvency II	IFRS
Realised and unrealised gains/(losses) on investments	375	375
Excess of depreciation over capital allowances	(13)	(13)
Spread acquisition expenses	(49)	(3)
Other	(6)	6
Difference between tax and accounting value of insurance contracts	900	
Total deferred tax (asset)/liability	**1,207**	**365**

None of the above deferred tax assets or liabilities have an expiration date.

The Company has the following tax losses for which no deferred tax asset has been recognised:

(£m)	Gross	Net
Tax losses in respect of equity and property assets	73	15
Trade losses in respect of business transferred in	12	2

D.3.5 Derivatives

All derivative contracts are measured at fair value in accordance with IFRS by reference to market transactions or using valuation models incorporating market based assumptions. There is no valuation difference between IFRS and Solvency II.

D.3.6 Insurance and intermediaries payables

All insurance payables are measured at fair value in line with IFRS.

D.3.7 Reinsurance payables

Reinsurance payables are valued at fair value in line with IFRS. There is no valuation difference to IFRS.

D.3.8 Payables (trade, not insurance)

There is a £178m valuation difference within payables (trade, not insurance) which relates to trail commission which is inadmissible under Solvency II as it is deemed to be intangible (in line with deferred acquisition costs and deferred income liability).

All other payables within this line item are valued at fair value in line with IFRS.

D.3.9 Any other liabilities, not elsewhere shown

Under IFRS there are £61m of other liabilities that are not shown elsewhere. On the IFRS balance sheet this is classified as the deferred income liability which is intangible and therefore inadmissible under Solvency II. Therefore this liability is removed from the Solvency II balance sheet.

D.4 Alternative methods for valuation

Legal & General has in place a group-wide valuation policy, which sets out the policy to ensure that for all assets across the Group, valued using alternative valuation methods, are governed, controlled and valued in a manner that is appropriate and consistent with the requirements of Article 263 of the Delegated Regulation. These policies include a requirement for ensuring models are reviewed on a timely basis and that independent review of the models and outputs is obtained on a regular basis.

A Group Asset Valuation Committee monitors the application of the processes and compliance with the Group policy. This includes setting the policies to ensure appropriate documentation, including documentation of the models, significant assumptions, sensitivities and an assessment of the resulting valuations.

The Group committee reviews all asset valuation submission from the Company. Whilst the committee will review all asset valuations, the committee's main focus is on assets or liabilities where alternative methods for valuation have been used. These assets include:

- **Commercial real estate loans** These are illiquid private assets and valuations are derived by using a discounted future cash flow approach with yields based on selected comparator bonds with similar durations and investment grades, combined with an assumption on the initial spread of the investment. Valuation uncertainty values calculated by adjusting the initial spread to calculate a plausible range of valuation scenarios to ensure that a fair value is reflected.
- **Income strips** These are property investment assets with lease durations typically in excess of 30 years. This asset class is valued using a discounted future cash flow approach based on comparator bond durations and investment grades, combined with assumptions on initial spread and future inflation factors. The valuation uncertainty element has been assessed by comparing the valuation against independent valuations performed by Royal Institute of Chartered Surveyors approved external valuers as a reasonableness check.
- **Lifetime Mortgages loans** There is no market-observable value for Lifetime Mortgage assets. However, the amount paid to acquire the assets at outset is objective, and is assumed to be the market value of the loan at the start date.
  Each Lifetime Mortgage loan is valued by projecting the expected proceeds and discounting at an appropriate discount rate. The main component of the spread is an estimate of the expected spread if the loan were issued on terms currently offered on new loans (with comparable LTVs). This spread will change over time, and aims to capture movements in the illiquidity premium available from investing in such Lifetime Mortgage assets.
  To project the expected proceeds, we make assumptions about: expected future property prices, volatility of property price growth, costs of selling the properties, decrement rates (mortality, morbidity and prepayment, as well as timing lags), running expenses.
  The asset valuation has been subjected to a variety of sensitivity tests covering reasonable ranges.
  The Lifetime mortgage portfolio is immature, and credible experience is yet to emerge.
- **Investment property** Due to the non-heterogeneity of the property portfolio, the valuation of the Group's property assets are provided by external valuation experts on a quarterly basis which are calibrated to recent precedent transactions in the market place. The external

valuations are performed in line with professional valuation standards as prescribed by the Royal Institute of Chartered Surveyors.

- **Sale and Leaseback arrangements** These are in relation to investment property and are valued as property.
- **Any non traded or illiquid bonds and equities** For illiquid Fixed Income we will consume a price from the counterparty broker to the deal where possible, or we will utilise the purchase price or issue price. For illiquid equities, our valuations are made, in line with the IPEV guidelines, by establishing a valuation with reference to relevant market, income and cost factors. These valuations are subject to internal review through independent asset valuation committees. Valuations are reviewed by independent expert valuation companies.

The Group Valuation Uncertainty Committee receives management information from each significant entity on their assessments of valuation uncertainty and provides oversight and challenge to these.

Following the completion of these processes the Company has concluded that its assets are valued appropriately in accordance with Article 10 of the Solvency II Delegated Regulation and appropriately reflect consideration of valuation uncertainty.

D.5 Any other information

The transitional measure on technical provisions (TMTP) is assumed to be amortised as at 1 January 2017. The additional six months of amortisation reduces the TMTP by £183m and results in a reduction to the regulatory solvency coverage ratio of 2%.

E. Capital management

E.1 Own Funds

E.1.1 Objectives for managing Own Funds

The Company's Board has established risk appetite statements to set the Company's overall objective for capital; the Company aims to maintain an appropriate buffer of capital resources over the minimum regulatory and economic capital requirements. The Company's Board sets a quantitative risk appetite for the Solvency II and Economic Capital coverage ratios and these are used to monitor the position relative to the Risk Appetite.

The Group Capital Committee considers and approves matters such as capital allocation, new product lines, large transactions and capital investments, mergers and acquisitions transactions, direct investment and other material matters that may arise under delegated authority from the Board and Chief Executive Officer.

Each year the Company prepares a five-year Capital Plan, consistent with the Company's strategic Plan and Business Plan, to forecast how the capital position is expected to develop over the Company's business planning period and consider the impact of the Company's strategy on the capital position. Performance against the capital plan is monitored on a regular basis and is used to inform decisions on the Company's capital structure and dividend policy.

E.1.2 Quantitative explanation of Own Funds

The components of the IFRS equity and the Solvency II Own Funds as at 31 December 2016 are as follows:

(£m)	IFRS equity	Solvency II Own Funds
Ordinary shares	651	651
Share premium	1,049	1,049
Retained earnings	4,441	-
Surplus funds	-	224
Reconciliation reserve	-	9,706
Total	**6,141**	**11,630**

This is the first annual report since the Solvency II regime took effect, and as such no comparative figures are provided relating to the position during the previous solvency regime.

E.1.3 Structure, amount, and quality of basic Own Funds

All of the Company's Own Funds have been assessed as basic Own Funds. There are no ancillary Own Fund items included in total Own Funds. Material basic Own Funds have been assessed against Article 71 of the Delegated Regulation and have accordingly been categorised as Tier 1 assets.

There are no items of Own Funds subject to transitional arrangements for the Company.

The structure and quality of the Company's Own Funds as at 31 December 2016 is as follows:

The structure and quality of the Group's Own Funds as at 31 December 2016 is as follows:

(£m)	Total	Tier 1 Unrestricted	Tier 1 Restricted	Tier 2	Tier 3
Ordinary share capital (gross of own shares)	651	651	-	-	-
Share premium account related to ordinary share capital	1,049	1,049	-	-	-
Surplus funds	224	224			
Reconciliation reserve	9,705	9,706	-	-	-
Total basic Own Funds	11,630	11,630	-	-	-
Total eligible Own Funds to cover the SCR	11,630	11,630	-	-	-
Total eligible Own Funds to cover the MCR	11,630	11,630	-	-	-

(£m)	Total
Solvency Capital Requirement	7,544
Solvency Surplus	4,086
Ratio of eligible Own Funds to SCR	**1.54**
Minimum Capital Requirement	1,886
Minimum Capital Surplus	9,744
Ratio of eligible Own Funds to MCR	**6.17**

All available Own Funds are perpetual with no maturity date.

E.1.4 Restrictions on Own Funds

As at 31 December 2016 there were no restrictions on the Own Funds for any of the Matching Adjustment Portfolios (MAPs) or the ring-fenced funds (RFF) within the Company.

E.1.5 Reconciliation between IFRS Equity and excess assets over liabilities

An explanation of the movement in each of the component parts of the Solvency II Excess of assets over liabilities is presented in Section D – Valuation for Solvency purposes, including a qualitative explanation for all valuation adjustments. The movement is shown below:

(£m)	2016	
IFRS Shareholders' equity	6,141	
Solvency II Excess of assets over liabilities	11,630	
Difference	**5,489**	
Explained by:		
Difference in the valuation of assets	(2,236)	Section D1
Difference in the valuation of technical provisions	8,485	Section D2
Difference in the valuation of other liabilities	(760)	Section D3
Total	**5,489**	

E.1.6 Reconciliation reserve

The reconciliation reserve, which is a core component of basic Own Funds, is made up of the excess of assets over liabilities seen on the Balance Sheet QRT S.02.01.02 (shown in Annex 1 of this report), adjusted for ordinary share capital, surplus funds and the share premium account, which are presented as separate components of Own Funds.

The calculation of the reconciliation reserve is as follows:

(£m)	
Excess of assets over liabilities	11,630
Own shares (held directly and indirectly)	-
Foreseeable dividends, distributions and charges	-
Less other basic Own Fund items	(1,924)
Less adjustment for restricted Own Fund items in respect of Matching Adjustment portfolios and ring-fenced funds	-
Reconciliation reserve	9,706

E.2 Solvency Capital Requirement and Minimum Capital Requirement

E.2.1 Solvency Capital Requirement (SCR)

The total SCR for the Company as at 31 December 2016 was £7,544m. This was calculated using the Group's approved partial internal model. No element of the SCR is subject to supervisory assessment.

Further information on the SCR by risk categories is provided in the QRT S.25 in Annex 1 of this report.

E.2.2 Minimum Capital Requirement (MCR)

The MCR for the Company is calculated in accordance with the Solvency II Directive and Delegated regulation. The total MCR for the Company as at 31 December 2016 was £1,886m.

Details on the inputs used to calculate the MCR are provided in the QRT S.28 in Annex 1 of this report.

E.3 Use of the duration-based equity risk sub-module in the calculation of the Solvency Capital Requirement

Duration-based equity risk sub module is not used in the calculation of the Solvency Capital Requirement.

E.4 Differences between the Standard Formula and any Internal Model used

E.4.1 Internal Model

The Group use a group partial internal model (referred to as the Internal Model), as approved by the Prudential Regulation Authority (PRA). The Group's Internal Model is used to calculate the capital requirements for the Company. The following sections describe the Group Internal Model used by the Company to assess its solo solvency requirements.

E.4.1.1 Use of the Internal Model

The Internal Model is a key tool within the risk management system. It plays a central role in the measurement of risks, as the internal model translates identified risk exposures into risk-based capital requirements. The Internal Model models the material and quantifiable risks that are identified as part of the Group's risk identification and review process.

The Internal Model's primary calculation engine, Algorithmics (Algo), has been designed to generate output at the level at which it will be used, i.e. at both a business unit and entity level, and by risk sub-category. This is important in ensuring its use and also helps to improve understanding and decision-making. In addition to being the Internal Model's calculation engine, Algo is also employed by the Group for operational Asset-Liability Management purposes.

Output from the Internal Model is used to formulate risk tolerances for the following group level risk appetite statements which are reviewed annually:

- The measure of return on risk-based capital
- The appropriate additional capital resources to be held over the minimum regulatory capital requirements.
- Management of volatility of earnings

Output from the Internal Model is essential for effectively monitoring risk exposures across the Group. Effective management information (MI) informs and supports the decision-making, oversight and risk assessment responsibilities of the Group's risk and capital management committees.

The Group level approach also serves as a model for the MI required for lower-level (i.e. divisional, entity and business unit) committees.

In an Internal Model context, risk and capital MI assists Legal & General to monitor risk exposures in relation to appetite and limits.

E.4.1.2 Scope of the Internal Model

We have chosen to adopt an Internal Model approach to calculate the Solvency Capital Requirement (SCR) for material insurance companies in the Group. The Internal Model covers all of the Group's material and quantifiable risk exposures, which are identified as falling into the following categories:

- Insurance
- Market
- Counterparty credit
- Liquidity
- Operational
- Group

The following subsidiaries are within the scope of the Group's partial internal model and are 'major business units':

Firms regulated on a solo basis

Entity	Model Type	Description
Legal and General Assurance Society Limited (LGAS)	Partial internal model (The model includes entities on a Standard Formula basis)	LGAS is a European Economic Area (EEA) composite insurer. LGAS currently operates primarily as a life and pensions business in the UK.
Legal & General Insurance Limited (LGIL)	Internal Model	LGIL is an EEA general insurer. A wholly owned subsidiary of LGAS, LGIL operates as a stand-alone business unit.
Legal & General Assurance (Pensions Management) Limited (PMC)	Internal Model	PMC is an EEA long-term insurer. PMC provides unit-linked pension policies and segregated Investment management services primarily to occupational pension scheme trustees.

Other firms included in the Group SCR

Entity	Model Type	Description
Legal & General Group Plc	Partial internal model	The Group level insurance holding company.
Legal & General Reinsurance Ltd (LG Re)	Internal Model	LG Re is a non-EEA reinsurer that started writing business during 2014, initially accepting primarily annuity related risks.
Banner Life Insurance Company William Penn Life Insurance Company of New York	Included in the model using the Deduction and Aggregation method based on the local statutory requirements	Banner and William Penn sell primarily individual protection policies in the US and are subsidiaries of the non-EEA holding company Legal & General America Inc.
Legal & General Finance Plc	Internal Model	Legal & General Finance is an ancillary firm whose principal activity is to provide funding to other Legal & General insured entities.

In line with the regulations Legal & General Finance Plc has been classified as a ‘major business unit’. As an 'ancillary services undertaking' as defined in the Solvency II Delegated Regulation (January 2015), its activities are highly integrated with other insured entities within the Group.

To support the management of the Group, the business is also run on a divisional basis. The divisions have business in the ‘major business units’ as follows:

Division	Major business units with division business
Legal & General Retirement (LGR)	LGAS, LG Re, Banner Life
Legal & General Insurance (LGI)	LGAS, Banner Life, William Penn
Legal & General Capital (LGC)	LGAS, Legal & General Finance
Legal & General Investment Management (LGIM)	PMC, LGAS
Savings	LGAS
General Insurance	LGIL

Our Internal Model is integrated into our risk management and governance systems. The material risks identified through the risk framework are also those covered by the Internal Model and vice versa. Actual risk exposures relative to Internal Model derived risk limits are monitored and reported.

The output of the Internal Model is used:

- to measure and rank the relative profile of the Group's core risk exposures;
- in determining the Group's strategies, risk limits and tolerances for managing different types of risk exposure relative to risk appetite;
- in the own risk and solvency assessment (ORSA) for the Group and for relevant solo firms;
- as a key factor in decisions such as those covering capital allocations, product pricing and asset class selection; and
- in the assessment of significant transactions.

The Board is assured of the adequacy and effectiveness of the integration and use of the Internal Model through regular reporting to the Group Risk Committee, both as part of the formal management information received by the Committee and through briefings on the operation and development of the Internal Model.

The Company will use alternative Method 1 defined in the Solvency II Delegated Regulation. This method involves simple addition of various sources of SCR without allowing for diversification between them (but allowing for full diversification within each of the Internal Model and standard formula SCRs). The sources of SCR are as follows:

- Internal Model SCR for the Company
- SCR in relation to subsidiary companies, without diversification

Our approach also includes the addition of pension scheme required capital allowing for some diversification with the Internal Model assessment, which is considered a part of the Internal Model rather than a separate source of SCR.

E.4.1.3 Methods used in the Internal Model

The approach used generates 500,000 simulations of 'risk drivers' such as equity returns and interest rates. The simulations are constructed in such a way that each risk driver follows a predefined distribution and that the relationship between any two risk drivers follows a predefined correlation assumption. The simulations can be looked at as a sample generated from a multidimensional distribution. This distribution is sometimes referred to as a 'marginal distribution'.

The multidimensional distribution is built from the risk driver distributions, correlation assumptions and a t-copula function which represents the dependency structure between the risks.

Each scenario is fed into an asset valuation module, which is capable of revaluing the Company's assets for each of these scenarios. The output is the total asset value under each scenario. This module covers the vast majority of assets required for capital calculation purposes.

Similarly, the scenarios are fed into a liability valuation module (and for certain situations the results from the asset valuation are also fed into the liability valuation module). Due to run time constraints, the liability valuation module is a simplified model (referred to as a 'proxy model').

The results of the liability valuation and the asset valuation module are combined for each scenario to give the resulting net asset position and the change in net asset value compared to the starting position. These results cover existing business, as well as the new business expected to be written over the following 12 months.

The risk measure used for the purpose of the Internal Model is a 'value-at-risk' measure (VaR); the VaR is defined as the estimated loss for a given probability over a one-year period.

By ordering the results (i.e. changes in net assets) the empirical aggregated loss distribution can be constructed. If the number of simulations is too small then the estimate of the percentile can be volatile and methods (such as smoothing) are required to stabilise results.

Whilst capital calculations are based upon a one-year VaR approach, the stresses applied in Algo are effectively carried out assuming that the event occurs exactly at the valuation date. An adjustment is made to allow for the investment return that would be earned over the year on the eligible Own Funds (EOF). For prudence it is assumed that the assets earn a risk free rate of return from the balance sheet date. At the point of the SCR event the EOFs will reduce by the size of the SCR and will then only yield a return at the post stress risk free rate. The 1-in-200 event could occur at any point over the year; however, to simplify the calculation of the adjustment, only month-ends are considered.

A simple average of the possible returns (each relating to the event occurring at the end of a different month) gives the expected return, on the assumption that the probability of the event occurring is uniformly distributed across the year.

E.4.2 The risk measure and time period used in the Internal Model

In line with Article 101 of the Solvency II Directive the Internal Model SCR is the 1-in-200 value-at-risk (VaR) of Own Funds over a one-year period.

E.4.3 Main differences against the Standard Formula approach

As described above, the Internal Model calibration standard is the same as for the Standard Formula. However, the detailed calculations differ in their sophistication and the extent to which they have been tailored to Legal & General's own risk profile. As part of the review of the Internal Model an annual exercise is carried out to assess the Group Standard Formula result.

Standard Formula is not the Company's regulatory basis. The production of a group Standard Formula result is not carried out as part of the year-end valuation cycle, and has been carried out on a proportionate basis and is not subject to the level of rigour as the Internal Model result validation.

The most significant (pre-diversification between risks) differences, based on the year end 2015 Standard Formula calculation, are as follows:

- the Standard Formula SCR includes segregation of the Matching Adjustment Portfolio, which results in a loss of diversification between annuities and the remaining business units;
- the capital arising from spread risk (net of matching adjustment) is higher for the Standard Formula than for the Internal Model, primarily due to the treatment of the assets held in Special Purpose Vehicles (SPVs). The Internal Model spread risk calibration is significantly stronger than the Standard Formula, but the stronger calibration is offset by an assumed correlation of less than 100% between the various Internal Model spread risk drivers. Different treatment of asset types in the internal model to the Standard Formula approach make a direct comparison difficult;
- property risk capital is lower for Standard Formula than Internal Model because, under Standard Formula, the rental element of sale and leaseback assets is treated as an unrated structured product and hence receives a credit stress. There are also some investments which are modelled using property risk factors in the Internal Model but in the Standard Formula they are modelled as 'strategic equity' and included in the equity risk family. Otherwise investments are treated consistently;
- Standard Formula has no inflation risk capital, whereas the Internal Model has a non-zero amount;

- Standard Formula has no non-market risk capital on the pension scheme, whereas the Internal Model has a non-zero amount;
- longevity risk capital is lower for Standard Formula than for Internal Model primarily because the Internal Model calibration (which targets base mortality as well as trend) is stronger than the Standard Formula;
- mortality risk capital is higher for Standard Formula than for Internal Model, primarily because the Internal Model calibration for retail protection business is lower than the Standard Formula;
- lapse risk capital is higher for Standard Formula than for Internal Model, primarily because the Internal Model mass lapse calibration for PMC and retail protection business is lower than the Standard Formula; where the Group's Standard Formula biting lapse shock is the mass lapse scenario;
- there is less diversification benefit between both market and insurance risks under Standard Formula than under Internal Model. This is primarily because the risks from annuities included within the Matching Adjustment Portfolio are assumed to diversify against the other insurance risks on other products within the Internal Model but this is not permitted under the Standard Formula;
- there is generally less diversification between market, insurance, operational and counterparty risks under Standard Formula than under Internal Model; and
- The Internal Model uses a copula approach to aggregate the components rather than the matrix multiplication specified in the Standard Formula. This enables the Internal Model to more accurately allow for interactions between risks and non-normal risk distribution shapes and results in different diversification benefit under the Internal Model.

E.4.4 Internal Model data

In order to calculate our Solvency Capital Requirement our Internal Model is provided with data about our assets, liabilities and the risks associated with each of these. The majority of assets are modelled on an individual asset terms and conditions basis, providing readily validated valuations and granular modelling of how assets respond under different scenarios. Insurance liabilities are provided by our proven process for the calculation of best estimate liabilities; the same process provides figures for our IFRS reporting and calculation of technical provisions.

In order to assess the risks associated with our assets and liabilities a wide range of economic, market and insurance data and operational risk experience is used. Internal and external historical and experience data are used to project possible future scenarios, and external forecasts are used for example in life longevity, causes of death, epidemic risks and event catastrophe risks.

Data are used to assess:

- the likelihood and scale of individual risks; and
- how these risks are correlated, i.e. the extent to which a change in one risk is likely to coincide with a change in another risk

Our Solvency II data governance has been designed to instil best practice in managing data risk and improving data quality to add robustness to model processes and outputs. The Solvency II Data Management Policy sets out the Group's requirements for managing data risk on data used to develop, populate, operate and validate the Internal Model. The data management control framework provides the conditions for business areas to ensure that all Internal Model data are recorded and that associated data risks and quality are managed effectively. The framework includes regular assessments of data quality and controls effectiveness.

The appropriateness of all internal and external data is considered and justified by the experts in each area of risk; these justifications are independently validated.

E.5 Non-compliance with the Minimum Capital Requirement and non-compliance with the Solvency Capital Requirement

There have been no instances of non-compliance with either the MCR or SCR for the Company over the reporting period.

E.6 Any other information

Post the year-end the Company declared a dividend payment of £402m to be paid to Legal & General Group Plc. The impact of this dividend payment as at 31 December 2016 would have been to reduce the regulatory solvency coverage ratio by 5%.

Annex 1 – Quantitative Reporting Templates (QRTs)

LEGAL AND GENERAL ASSURANCE SOCIETY LIMITED - SOLVENCY and FINANCIAL CONDITION REPORT 31 DECEMBER 2016
Values are shown in £'000

S.02.01.02
Balance sheet

		Solvency II value
	Assets	C0010
R0030	Intangible assets	
R0040	Deferred tax assets	
R0050	Pension benefit surplus	
R0060	Property, plant & equipment held for own use	7,547
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	72,379,993
R0080	*Property (other than for own use)*	409,052
R0090	*Holdings in related undertakings, including participations*	1,325,122
R0100	*Equities*	3,687,326
R0110	*Equities - listed*	3,573,382
R0120	*Equities - unlisted*	113,944
R0130	*Bonds*	56,425,139
R0140	*Government Bonds*	13,305,466
R0150	*Corporate Bonds*	41,106,456
R0160	*Structured notes*	
R0170	*Collateralised securities*	2,013,217
R0180	*Collective Investments Undertakings*	6,638,552
R0190	*Derivatives*	3,684,233
R0200	*Deposits other than cash equivalents*	210,568
R0210	*Other investments*	
R0220	Assets held for index-linked and unit-linked contracts	27,386,921
R0230	Loans and mortgages	1,580,915
R0240	*Loans on policies*	72
R0250	*Loans and mortgages to individuals*	869,833
R0260	*Other loans and mortgages*	711,010
R0270	Reinsurance recoverables from:	22,878,138
R0280	*Non-life and health similar to non-life*	
R0290	*Non-life excluding health*	
R0300	*Health similar to non-life*	
R0310	*Life and health similar to life, excluding index-linked and unit-linked*	8,030,904
R0320	*Health similar to life*	88,005
R0330	*Life excluding health and index-linked and unit-linked*	7,942,899
R0340	*Life index-linked and unit-linked*	14,847,234
R0350	Deposits to cedants	905,929
R0360	Insurance and intermediaries receivables	78,823
R0370	Reinsurance receivables	169,749
R0380	Receivables (trade, not insurance)	1,725,869
R0390	Own shares (held directly)	
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	
R0410	Cash and cash equivalents	671,202
R0420	Any other assets, not elsewhere shown	
R0500	**Total assets**	127,785,086

	Liabilities	Solvency II value	
		C0010	
R0510	Technical provisions - non-life	1,431	
R0520	*Technical provisions - non-life (excluding health)*	1,431	
R0530	*TP calculated as a whole*		
R0540	*Best Estimate*	(293)	note 1
R0550	*Risk margin*	1,724	note 2
R0560	*Technical provisions - health (similar to non-life)*		
R0570	*TP calculated as a whole*		
R0580	*Best Estimate*		note 1
R0590	*Risk margin*		note 2
R0600	Technical provisions - life (excluding index-linked and unit-linked)	62,177,753	
R0610	*Technical provisions - health (similar to life)*	451,248	
R0620	*TP calculated as a whole*		
R0630	*Best Estimate*	448,776	note 1
R0640	*Risk margin*	2,472	note 2
R0650	*Technical provisions - life (excluding health and index-linked and unit-linked)*	61,726,505	
R0660	*TP calculated as a whole*		
R0670	*Best Estimate*	61,578,193	note 1
R0680	*Risk margin*	148,312	note 2
R0690	Technical provisions - index-linked and unit-linked	41,597,851	
R0700	*TP calculated as a whole*		
R0710	*Best Estimate*	41,569,622	note 1
R0720	*Risk margin*	28,229	note 2
R0740	Contingent liabilities		
R0750	Provisions other than technical provisions	67,236	
R0760	Pension benefit obligations	160,922	
R0770	Deposits from reinsurers	5,256,092	
R0780	Deferred tax liabilities	1,207,474	
R0790	Derivatives	1,965,484	
R0800	Debts owed to credit institutions	308	
R0810	Financial liabilities other than debts owed to credit institutions		
R0820	Insurance & intermediaries payables	411,120	
R0830	Reinsurance payables	9,235	
R0840	Payables (trade, not insurance)	3,300,459	
R0850	Subordinated liabilities		
R0860	*Subordinated liabilities not in BOF*		
R0870	*Subordinated liabilities in BOF*		
R0880	Any other liabilities, not elsewhere shown		
R0900	**Total liabilities**	116,155,365	
R1000	**Excess of assets over liabilities**	11,629,721	

Note 1
BELs are shown net of Transitional Measure on Technical Provisions (TMTP) applied.
The total BELs above sum to £103,596,298k. The total unadjusted BELs of £104,047,533k can be seen in section D.2.1 on page 58 of the report.

Note 2
Risk Margin is shown net of TMTPs applied. The total risk margin above sums to £180,738k. The total unadjusted risk margin of £5,729,488k can be seen in section D.2.1 on page 58 of the report.

In total, TMTP of £5,999,985k was applied, and can be seen in section D.2.1.4 on page 63 of the report.

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Premiums, claims and expenses by line of business

Non-life

		Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)						Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)						Line of business for: accepted non-proportional reinsurance				Total
		Medical expense insurance	Income protection insurance	Workers' compensation insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Credit and suretyship insurance	Legal expenses insurance	Assistance	Misc. financial loss	Health	Casualty	Marine, aviation and transport	Property	
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110	C0120	C0130	C0140	C0150	C0160	C0200
	Premiums written																	
R0110	*Gross - Direct Business*																	
R0120	*Gross - Proportional reinsurance accepted*																	
R0130	*Gross - Non-proportional reinsurance accepted*																12,822	12,822
R0140	*Reinsurers' share*																	
R0200	*Net*																12,822	12,822
	Premiums earned																	
R0210	*Gross - Direct Business*																	
R0220	*Gross - Proportional reinsurance accepted*																	
R0230	*Gross - Non-proportional reinsurance accepted*																12,367	12,367
R0240	*Reinsurers' share*																	
R0300	*Net*																12,367	12,367
	Claims incurred																	
R0310	*Gross - Direct Business*						71											71
R0320	*Gross - Proportional reinsurance accepted*																	
R0330	*Gross - Non-proportional reinsurance accepted*																	
R0340	*Reinsurers' share*																	
R0400	*Net*						71											71
	Changes in other technical provisions																	
R0410	*Gross - Direct Business*																	
R0420	*Gross - Proportional reinsurance accepted*																	
R0430	*Gross - Non-proportional reinsurance accepted*																	
R0440	*Reinsurers' share*																	
R0500	*Net*																	
R0550	**Expenses incurred**						33		63								1,854	1,950
R1200	**Other expenses**																	
R1300	**Total expenses**																	1,950

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Premiums, claims and expenses by line of business
Life

		Line of Business for: life insurance obligations						Life reinsurance obligations		Total
		Health insurance	Insurance with profit participation	Index-linked and unit-linked insurance	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	Health reinsurance	Life reinsurance	
		C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0300
	Premiums written									
R1410	*Gross*	116,387	43,806		5,478,119				3,452,894	9,091,206
R1420	*Reinsurers' share*	30,008	1,311		1,703,201				294,462	2,028,982
R1500	*Net*	86,379	42,495		3,774,918				3,158,432	7,062,224
	Premiums earned									
R1510	*Gross*	116,387	43,806		5,478,119				3,452,894	9,091,206
R1520	*Reinsurers' share*	30,008	1,311		1,703,201				294,462	2,028,982
R1600	*Net*	86,379	42,495		3,774,918				3,158,432	7,062,224
	Claims incurred									
R1610	*Gross*	88,020	810,843		3,647,472				422,030	4,968,365
R1620	*Reinsurers' share*	17,720	869		1,447,846				14,843	1,481,278
R1700	*Net*	70,300	809,974		2,199,626				407,187	3,487,087
	Changes in other technical provisions									
R1710	*Gross*	54,134	271,339	5,676,242	8,776,389				3,201,416	17,979,520
R1720	*Reinsurers' share*	4,029	10	2,205,556	2,106,031				285,189	4,600,815
R1800	*Net*	50,105	271,329	3,470,686	6,670,358				2,916,227	13,378,705
R1900	**Expenses incurred**	13,808	67,475	258,121	558,364				2,708	900,476
R2500	**Other expenses**									277,844
R2600	**Total expenses**									1,178,320

S.12.01.02
Life and Health SLT Technical Provisions

		Insurance with profit participation	Index-linked and unit-linked insurance			Other life insurance			Annuities stemming from non-life insurance contracts and relating to insurance obligation other than health insurance obligations	Accepted reinsurance	Total (Life other than health insurance, including Unit-Linked)
				Contracts without options and guarantees	Contracts with options or guarantees		Contracts without options and guarantees	Contracts with options or guarantees			
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0150
R0010	**Technical provisions calculated as a whole**										
R0020	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole										
	Technical provisions calculated as a sum of BE and RM										
	Best estimate										
R0030	**Gross Best Estimate**	10,635,550			41,557,968		24,581,613	23,784,862		3,039,057	103,599,050
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default				14,847,234		4,802,254	2,790,170		350,476	22,790,133
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re	10,635,550			26,710,734		19,779,359	20,994,692		2,688,581	80,808,916
R0100	**Risk margin**	122,152	60,368			5,166,536				376,236	5,725,292
	Amount of the transitional on Technical Provisions										
R0110	Technical Provisions calculated as a whole										
R0120	Best estimate						(239,259)	(204,123)		(7,853)	(451,235)
R0130	Risk margin	(85,323)	(32,139)			(5,109,180)				(322,109)	(5,548,751)
R0200	**Technical provisions - total**	10,672,379	41,586,197			47,980,449				3,085,331	103,324,356

S.12.01.02

Life and Health SLT Technical Provisions

		Health insurance (direct business)			Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Health reinsurance (reinsurance accepted)	Total (Health similar to life insurance)
			Contracts without options and guarantees	Contracts with options or guarantees			
		C0160	C0170	C0180	C0190	C0200	C0210
R0010	**Technical provisions calculated as a whole**						
R0020	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole						
	Technical provisions calculated as a sum of BE and RM						
	Best estimate						
R0030	**Gross Best Estimate**		215,064	233,711			448,775
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default		71,023	16,982			88,005
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re		144,041	216,730			360,771
R0100	**Risk margin**	2,473					2,473
	Amount of the transitional on Technical Provisions						
R0110	Technical Provisions calculated as a whole						
R0120	Best estimate						
R0130	Risk margin						
R0200	**Technical provisions - total**	451,248					451,248

S.17.01.02

Non-Life Technical Provisions

		Direct business and accepted proportional reinsurance				Accepted non-proportional reinsurance				Total Non-Life obligation
		Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Non-proportional health reinsurance	Non-proportional casualty reinsurance	Non-proportional marine, aviation and transport reinsurance	Non-proportional property reinsurance	
		C0060	C0070	C0080	C0090	C0140	C0150	C0160	C0170	C0180
R0010	**Technical provisions calculated as a whole**									
R0050	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP calculated as a whole									
	Technical provisions calculated as a sum of BE and RM									
	Best estimate									
	Premium provisions									
R0060	Gross								(674)	(674)
R0140	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default									
R0150	**Net Best Estimate of Premium Provisions**								(674)	(674)
	Claims provisions									
R0160	Gross		110	1	270					381
R0240	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default									
R0250	**Net Best Estimate of Claims Provisions**		110	1	270					381
R0260	**Total best estimate - gross**		110	1	270				(674)	(293)
R0270	**Total best estimate - net**		110	1	270				(674)	(293)
R0280	**Risk margin**								1,724	1,724
	Amount of the transitional on Technical Provisions									
R0290	Technical Provisions calculated as a whole									
R0300	Best estimate									
R0310	Risk margin									
R0320	**Technical provisions - total**		110	1	270				1,050	1,431
R0330	**Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total**									
R0340	**Technical provisions minus recoverables from reinsurance/SPV and Finite Re - total**		110	1	270				1,050	1,431

S.22.01.21

Impact of long term guarantees measures and transitionals

		Amount with Long Term Guarantee measures and transitionals	Impact of transitional on technical provisions	Impact of transitional on interest rate	Impact of volatility adjustment set to zero	Impact of matching adjustment set to zero
		C0010	C0030	C0050	C0070	C0090
R0010	**Technical provisions**	103,777,036	5,999,985	-	-	7,506,108
R0020	**Basic own funds**	11,629,720	(4,964,132)	-	-	(6,230,070)
R0050	**Eligible own funds to meet Solvency Capital Requirement**	11,629,720	(4,964,132)	-	-	(6,230,070)
R0090	**Solvency Capital Requirement**	7,544,254	977,135	-	-	8,378,342
R0100	**Eligible own funds to meet Minimum Capital Requirement**	11,629,720	(4,964,132)	-	-	(6,230,070)
R0110	**Minimum Capital Requirement**	1,886,063	244,284	-	-	2,094,586

Note

The information disclosed in this template is as defined in Annex I of Commission Implementing Regulation (EU) 2015/2542, and is at 31 December 2016.

Values in this table alone do not provide sufficient information to gain a fair and transparent understanding of the Company's solvency position.

Additional information on the transitional measure on technical provisions and the matching adjustment can be found in section D2 of the report.

S.23.01.01
Own Funds

	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35	Total	Tier 1 unrestricted	Tier 1 restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
R0010	Ordinary share capital (gross of own shares)	651,430	651,430			
R0030	Share premium account related to ordinary share capital	1,048,914	1,048,914			
R0040	Initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings					
R0050	Subordinated mutual member accounts					
R0070	Surplus funds	224,654	224,654			
R0090	Preference shares					
R0110	Share premium account related to preference shares					
R0130	Reconciliation reserve	9,704,722	9,704,722			
R0140	Subordinated liabilities					
R0160	An amount equal to the value of net deferred tax assets					
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above					
	Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds					
R0220	Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds					
	Deductions					
R0230	Deductions for participations in financial and credit institutions					
R0290	**Total basic own funds after deductions**	11,629,720	11,629,720			
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand					
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand					
R0320	Unpaid and uncalled preference shares callable on demand					
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand					
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC					
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC					
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC					
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC					
R0390	Other ancillary own funds					
R0400	**Total ancillary own funds**					
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	11,629,720	11,629,720			
R0510	Total available own funds to meet the MCR	11,629,720	11,629,720			
R0540	Total eligible own funds to meet the SCR	11,629,720	11,629,720			
R0550	Total eligible own funds to meet the MCR	11,629,720	11,629,720			
R0580	**SCR**	7,544,254				
R0600	**MCR**	1,886,063				
R0620	**Ratio of Eligible own funds to SCR**	154.15%				
R0640	**Ratio of Eligible own funds to MCR**	616.61%				

	Reconcilliation reserve	C0060
R0700	Excess of assets over liabilities	11,629,720
R0710	Own shares (held directly and indirectly)	
R0720	Foreseeable dividends, distributions and charges	
R0730	Other basic own fund items	1,924,998
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	
R0760	**Reconciliation reserve**	9,704,722
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) - Life business	2,727,768
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	
R0790	**Total Expected profits included in future premiums (EPIFP)**	2,727,768

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S.25.02.21

Solvency Capital Requirement - for undertakings using the standard formula and partial internal model

Row	Unique number of component	Component description	Calculation of the Solvency Capital Requirement	Amount modelled	
	C0010	C0020	C0030	C0070	
1	10300I	Interest rate risk (other than pension scheme)	763,924	763,924	
2	10400I	Equity risk (other than pension scheme)	809,134	809,134	
3	10600I	Property risk (other than pension scheme)	766,817	766,817	
4	10700I	Spread risk (other than pension scheme)	4,381,644	4,381,644	
5	10800I	Concentration risk (other than pension scheme)	-	-	
6	10900I	Currency risk (other than pension scheme)	507,159	507,159	
7	11000I	Other market risk (other than pension scheme)	294,838	294,838	
8	10300P	Interest rate risk (pension scheme)	60,362	60,362	
9	10400P	Equity risk (pension scheme)	91,343	91,343	
10	10600P	Property risk (pension scheme)	7,814	7,814	
11	10700P	Spread risk (pension scheme)	142,936	142,936	
12	10800P	Concentration risk (pension scheme)	-	-	
13	10900P	Currency risk (pension scheme)	-	-	
14	11000P	Other market risk (pension scheme)	120,121	120,121	
15	19900I	Diversification within market risk (including pension scheme)	(1,454,819)	(1,454,819)	note 1
16	20100I	Type 1 counterparty risk	164,492	164,492	
17	20200I	Type 2 counterparty risk	5,084	5,084	
18	29900I	Diversification within counterparty risk	-	-	
19	30100I	Mortality risk	470,003	470,003	
20	30200I	Longevity risk (other than pension scheme)	5,426,625	5,426,625	
21	30200P	Longevity risk (pension scheme)	167,840	167,840	
22	30400I	Mass lapse	418,416	418,416	
23	30500I	Other lapse risk	486,779	486,779	
24	30600I	Expense risk	580,027	580,027	
25	30800I	Life catastrophe risk	725,465	725,465	
26	30900I	Other life underwriting risk	-	-	
27	39900I	Diversification within life underwriting risk	(2,480,568)	(2,480,568)	note 1
28	41600I	Other health underwriting risk	115,211	115,211	
29	50100I	Premium risk	-	-	
30	50200I	Reserve risk	-	-	
31	50150I	Premium risk if premium risk covers premium provision and business planned to be written in coming 12 months combined	98,790	98,790	
32	50210I	Reserving risk if claims provision and premium provision combined	25,192	25,192	
33	50300I	Non-life catastrophe risk	419,925	419,925	
34	59900I	Diversification within non-life underwriting risk	(88,165)	(88,165)	note 1
35	70100I	Operational risk	932,038	932,038	
36	80100I	Other risks	-	-	
37	80200I	Loss-absorbing capacity of technical provisions	-	-	
38	80300I	Loss-absorbing capacity of deferred tax	(1,399,622)	(1,399,622)	
39	80400I	Other adjustments	(107,659)	(107,659)	

	Calculation of Solvency Capital Requirement	C0100	
R0110	Total undiversified components	12,451,146	Sum of components above
R0060	Diversification	(4,906,892)	note 2
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC		
R0200	**Solvency capital requirement excluding capital add-on**	7,544,254	
R0210	Capital add-ons already set		
R0220	**Solvency capital requirement**	7,544,254	total plus diversification (a)

	Other information on SCR- FOR INFORMATION ONLY, EMBEDDED IN COMPONENTS ABOVE	
R0300	Amount/estimate of the overall loss-absorbing capacity of technical provisions	(1,108,440)
R0310	Amount/estimate of the overall loss-absorbing capacity ot deferred taxes	(1,399,622)
R0400	Capital requirement for duration-based equity risk sub-module	
R0410	Total amount of Notional Solvency Capital Requirements for remaining part	2,887,166
R0420	Total amount of Notional Solvency Capital Requirement for ring fenced funds	484,227
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	5,305,741
R0440	Diversification effects due to RFF nSCR aggregation for article 304	

note 1

These items represent diversification within individual risk categories. The total diversification within categories is £4,023,553k

note 2

This item represents diversification between risk categories. The total diversification within and between risk categories is £8,930,445k

S.28.02.01

Minimum Capital Requirement - Both life and non-life insurance activity

		Non-life activitie	Life activities
		$MCR_{(NL,NL)}$ Result	$MCR_{(NL,L)}$ Result
		C0010	C0020
R0010	**Linear formula component for non-life insurance and reinsurance obligations**	2,078	0

		Non-life activities		Life activities	
		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0030	C0040	C0050	C0060
R0020	Medical expense insurance and proportional reinsurance				
R0030	Income protection insurance and proportional reinsurance				
R0040	Workers' compensation insurance and proportional reinsurance				
R0050	Motor vehicle liability insurance and proportional reinsurance				
R0060	Other motor insurance and proportional reinsurance				
R0070	Marine, aviation and transport insurance and proportional reinsurance	110			
R0080	Fire and other damage to property insurance and proportional reinsurance	1			
R0090	General liability insurance and proportional reinsurance	271			
R0100	Credit and suretyship insurance and proportional reinsurance				
R0110	Legal expenses insurance and proportional reinsurance				
R0120	Assistance and proportional reinsurance				
R0130	Miscellaneous financial loss insurance and proportional reinsurance				
R0140	Non-proportional health reinsurance				
R0150	Non-proportional casualty reinsurance				
R0160	Non-proportional marine, aviation and transport reinsurance				
R0170	Non-proportional property reinsurance		12,822		

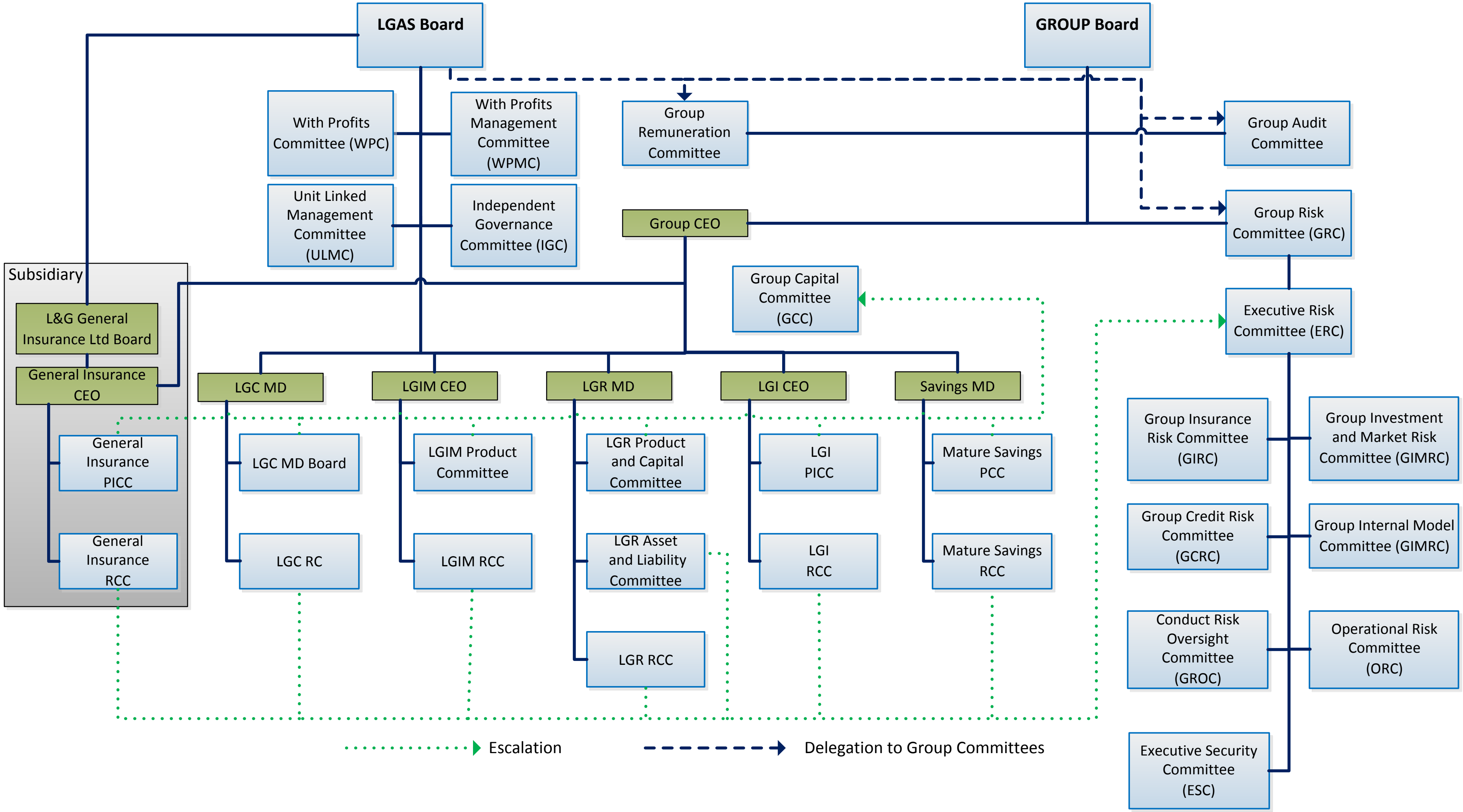
		$MCR_{(L,NL)}$ Result	$MCR_{(L,L)}$ Result
		C0070	C0080
R0200	**Linear formula component for life insurance and reinsurance obligations**	0	1,618,666

		Non-life activities		Life activities	
		Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance/SPV) total capital at risk
		C0090	C0100	C0110	C0120
R0210	Obligations with profit participation - guaranteed benefits			6,797,512	
R0220	Obligations with profit participation - future discretionary benefits			3,838,038	
R0230	Index-linked and unit-linked insurance obligations			26,722,389	
R0240	Other life (re)insurance and health (re)insurance obligations			43,360,515	
R0250	Total capital at risk for all life (re)insurance obligations				670,155,286

	Overall MCR calculation	C0130
R0300	Linear MCR	1,620,744
R0310	SCR	7,544,254
R0320	MCR cap	3,394,914
R0330	MCR floor	1,886,063
R0340	Combined MCR	1,886,063
R0350	Absolute floor of the MCR	5,583
R0400	**Minimum Capital Requirement**	1,886,063

	Notional non-life and life MCR calculation	C0140	C0150
R0500	Notional linear MCR	2,078	1,618,666
R0510	Notional SCR excluding add-on (annual or la	9,672	7,534,582
R0520	Notional MCR cap	4,352	3,390,562
R0530	Notional MCR floor	2,418	1,883,645
R0540	Notional combined MCR	2,418	1,883,645
R0550	Absolute floor of the notional MCR	2,251	3,332
R0560	**Notional MCR**	2,418	1,883,645

Annex 2 – Entity governance oversight structure



Annex 3 – Main assumptions underlying technical provisions

Non-linked individual term assurances	
Smokers	76% TMS00/TFS00 Sel 5
Non-smokers	73% TMN00/TFN00 Sel 5
Non-linked individual term assurances with terminal illness[1]	
Smokers	56% - 71% TMS00/TFS00 Sel 5
Non-smokers	54% - 72% TMN00/TFN00 Sel 5
Non-linked individual term assurances with critical illness (Sold until 31/12/2012) [2]	
Smokers	97% - 116% ACMS04/ACFS04
Non-smokers	102% - 134% ACMN04/ACFN04
Non-linked individual term assurances with critical illness (Sold from 01/01/2013) [2]	
Smokers	99% - 117% ACMS04/ACFS04
Non-smokers	105% - 137% ACMN04/ACFN04
Whole of Life[3]	
Smokers	Bespoke tables based on TMS00/TFS00, AM92/AF92 and UK death registrations
Non-smokers	Bespoke tables based on TMN00/TFN00, AM92/AF92 and UK death registrations
Annuities	
Annuities in deferment[4]	87.4%% - 88.7% PNMA00/PNFA00
Bulk purchase annuities in payment[5]	87.4% - 88.7% PCMA00/PCFA00
Other annuities[5]	67.4% - 143.4% PCMA00/PCFA00

1. The percentage of the table varies with the duration that the policy has been in-force for the first five years.

2. The percentage of the table varies with the duration that the policy has been in-force for the first two years. For term assurance with critical illness, morbidity rates are assumed to deteriorate at a rate of 0.50% p.a. for males and 0.75% p.a. for females. There is an additive loading of 1% for guaranteed term contracts post policy duration 5.

3. The percentage of the TM00/TF00 tables varies with the duration that the policy has been in-force for the first five years. Thereafter, a bespoke mortality table constructed based on TM00/TF00 tables, AM92/AF92 tables and UK death registrations. Mortality rates are assumed to reduce whilst business is ceded to reinsurer (after which any reduction is maintained but no further reduction is applied) based on CMI2014 model with a long term annual improvement rate of 1.5% p.a. for males and 1.0% p.a. for females.

4. Table created by blending PCXA00 with PNXA00 tables. The base table to be used for bulk purchase annuity policies in deferment is PNMA00 up to and including age 55 and PCMA00 for age 65 and above for males. The identical method is applied to females using PNFA00 and PCFA00.

5. For vested annuities, mortality rates are assumed to reduce according to an adjusted version of CMIB's mortality improvement model; CMI 2014 with the following parameters:

Males: Long Term Rate of 1.50% p.a. up to age 85 tapering to 0% at 120
Females: Long Term Rate of 1. 0% p.a. up to age 85 tapering to 0% at 120
Different business classes have different effective dates for applying improvers.

For certain annuities, a further allowance is made for the effect of initial selection.

The basis above is applicable up to age 90. After age 90 the basis is blended towards a bespoke table from age 105 onwards

Lapse Rates

	Years 1-5	Years 6-10	Years 11+
Level Term	6.6%-13.5%	4.5%-7.8%	3.0%-4.5%
Decreasing Term	7.4%-10.9%	6.8%-9.8%	6.2%-7.6%
Investment Bond	1.9%-4.1%	3.5%-11.4%	5.25%-7.08%

Glossary

A

ALM
Asset liability management.

Annuity
A regular payment from an insurance company made for an agreed period of time (usually up to the death of the recipient) in return for either a cash lump sum or a series of premiums which the policyholder has paid to the insurance company during their working lifetime.

B

Basic Own Funds
The surplus of assets over liabilities and subordinated liabilities.

Best estimate liability (BEL)
The probability-weighted average of best estimate future cash flows, discounted using risk-free term structure of interest rates (adjusted for a matching adjustment where appropriate).

C

Capital coverage ratio
Also known as the solvency coverage ratio. The eligible Own Funds on a regulatory basis divided by the Group Solvency Capital Requirement. This represents the number of times the SCR is covered by eligible Own Funds.

CEO
Chief Executive Officer.

Code Staff
A category of role defined under various applicable European Directives (CRDIII & IV, AIFMD, UCITS V, and Solvency II). The name is taken from the FCA's Remuneration Code that interprets and applies these Directives for the UK. Broadly, Code Staff includes roles that are considered to have the authority to take risks that could directly, or indirectly, affect one or more firms within the Group and its investors.

CRO
Chief Risk Officer.

D

DAC
Deferred acquisition costs.

E

EEA
European economic area.

EIOPA
European Insurance and Occupational Pensions Authority.

Eligible Own Funds (EOF)
The amount of Own Funds available to meet the SCR and MCR. This includes any adjustments for eligibility requirements as defined by the Solvency II regulations.

EPIFP
Expected profit included in future premiums.

G

GIMC
Group Internal Model Committee.

I

IFRS operating profit
Operating profit measures the pre-tax result excluding the impact of investment volatility, economic assumption changes and exceptional items. Operating profit therefore reflects longer-term economic assumptions and changes in insurance risks such as mortality and longevity for the Group's insurance business and shareholder funds, except for LGA which excludes unrealised investment returns to align with the liability measurement under US GAAP. Variances between actual and smoothed assumptions are reported below operating profit. Exceptional income and expenses which arise outside the normal course of business in the period, such as merger and acquisition and start-up costs are excluded from operating profit.

Internal Model
A solvency calculation model tailored to the individual risk profile of a specific firm.

International financial reporting standards (IFRS)
These are accounting guidelines and rules that companies and organisations follow when completing financial statements. They are designed to enable comparable reporting between companies, and they are the standards that all publicly listed groups in the European Union (EU) are required to use.

L

LGA
Legal & General America.

LGAS
Legal and General Assurance Society Limited.

LG Re
Legal & General Reinsurance Limited.

LGC
Legal & General Capital division.

LGI
Legal & General Insurance division.

LGIL
Legal & General Insurance Limited.

LGIM
Legal & General Investment Management.

LGR
Legal & General Retirement division.

Liability driven investment (LDI)
A form of investing in which the main goal is to gain sufficient assets to meet all liabilities, both current and future. This form of investing is most prominent in final salary pension plans, whose liabilities can often reach into billions of pounds for the largest of plans.

Lifetime Mortgages
An equity release product aimed at people aged 60 years and over. It is a mortgage loan secured against the customer's house. Customers do not make any monthly payments and continue to own and live in their house until they move into long-term care or on death. A no negative equity guarantee exists such that if the house value on repayment is insufficient to cover the outstanding loan, any shortfall is borne by the lender.

Liquidity coverage ratio (LCR)
The measure of exposure to liquidity risk. The LCR is defined as total sources of liquidity divided by total liquidity requirements.

Longevity
Risk associated with increasing life expectancy trends among policyholders and pensioners.

M

Matching adjustment (MA)
An adjustment to the risk-free interest rate term structure used to calculate the best estimate of a portfolio of eligible insurance obligations. Its use is subject to prior supervisory approval where certain eligibility criteria are met.

MAP
Matching Adjustment Portfolio.
A portfolio of assets created to back a certain set of liabilities, which is then eligible for a matching adjustment.

MCR
Minimum Capital Requirement is calculated using a prescribed formula and which is the minimum level of capital below which the amount of financial resources should not fall.

MI
Management information.

Mortality rate
Rate of death, influenced by age, gender and health, used in pricing and calculating liabilities for future policyholders of life and annuity products, which contain mortality risks.

N

Notional Solvency Capital Requirement
A Notional Solvency Capital requirement is calculated for a specific group of business, such as the with-profits fund, on a standalone basis.

O

ORSA
Own risk and solvency assessment, also known as the forward-looking assessment of own risks.

Own Funds
The amount of capital available to cover a firm's SCR.

P

Pension risk transfer (PRT)
PRT represents bulk annuities bought by entities that run final salary pension schemes to reduce their responsibilities by closing the schemes to new members and passing the assets and obligations to insurance providers.

PIM
Partial internal model.

PMC
Legal and General (Pensions Management) Limited.

PPE
Property, plant and equipment.

PPFM
The principles and practices of financial management (PPFM) used to manage the with-profits business.

PRA
Prudential Regulation Authority was created as a part of the Bank of England by the Financial Services Act (2012) and is responsible for the prudential regulation and supervision of insurance companies in the UK.

Purchased interest in long-term business (PILTB)
An estimate of the future profits that will emerge over the remaining term of life and pensions policies that have been acquired via a business combination.

Q

QRTs
Quantitative reporting templates.
Templates defined by EIOPA for the regular reporting of financial information.

R

Reconciliation reserve
A basic Own Funds item, comprising the excess of assets over liabilities, adjusted for other basic Own Funds items comprising of own shares, foreseeable dividends, restricted Own Fund items, and other non-available Own Funds.

Ring-fenced funds (RFF)
Own Funds that can only be used to cover a particular segment of liabilities or particular risks and cannot be made available to cover liabilities or risks outside the ring-fenced fund.

Risk appetite
The aggregate level and types of risk a company is willing to assume in its exposures and business activities in order to achieve its business objectives.

Risk margin (RM)
The cost of providing funds to cover the Solvency Capital requirements over the lifetime of the associated insurance policies. The approach for calculating the risk margin is prescribed in Solvency II regulations.

S

SBP
Share bonus plan.

SCR
Solvency Capital Requirement is the amount of capital that insurance and reinsurance undertakings are required to hold and is calibrated to ensure that all quantifiable risks are taken into account in a 1-in-200 year risk event.

SFCR
Solvency and Financial Condition Report.

Solvency coverage ratio
Also known as the capital coverage ratio. The eligible Own Funds on a regulatory basis divided by the Group Solvency Capital Requirement. This represents the number of times the SCR is covered by eligible own funds.

Solvency II
Taking effect from 1 January 2016, the Solvency II regulatory regime is a harmonised

prudential framework for insurance firms in the EEA. This single market approach is based on economic principles that measure assets and liabilities to appropriately align insurers' risk with the capital they hold to safeguard policyholders.

Solvency II Delegated Regulation
Commission Delegated Regulation (EU) 2015/35 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II).

Solvency II Directive
Directive 2009/138/EC of the European Parliament (Solvency II Directive).

SPV
Special purpose vehicle.

Standard Formula (SF)
A standardised solvency calculation method, not tailored to the individual risk profile of a specific firm. It aims to capture the material quantifiable risks to which most undertakings are exposed.

Surplus
The excess of eligible Own Funds on a regulatory basis over the Solvency Capital Requirement. This represents the amount of capital available to the company in excess of that required to sustain it in a 1-in-200 year risk event.

T

Technical provisions (TP)
The sum of the best estimate liabilities and the risk margin.

TMTP
Transitional measure on technical provisions.

Total shareholder return (TSR)
TSR is a measure used to compare the performance of different companies' stocks and shares over time. It combines the share price appreciation and dividends paid to show the total return to the shareholder.

U

ULMC
Unit-Linked Management Committee.

V

Value-at-risk (VaR)
The estimated loss for a given probability over a one-year period.

W

With-profits fund
Individually identifiable portfolios where policyholders have a contractual right to receive additional benefits based on factors such as the performance of a pool of assets held within the fund, as a supplement to any guaranteed benefits. An insurer may either have discretion as to the timing of the allocation of those benefits to participating policyholders or may have discretion as to the timing and the amount of the additional benefits.

WPMC
With-Profits Management Committee.

Y

Yield
A measure of the income received from an investment compared to the market value of the investment. It is usually expressed as a percentage.