

# Audit Committee report



**Philip Broadley**  
Chairman of the Audit Committee

## The composition of the Committee

The Committee is composed entirely of independent non-executive directors. The table below sets out its membership during the year.

Members
Philip Broadley (Chairman)
Nilufer von Bismarck (from May 2021)
George Lewis
Toby Strauss
Henrietta Baldock (until March 2021)
Lesley Knox (until March 2021)
Julia Wilson (retired March 2021)

Other regular attendees at Committee meetings include the following:

Group Chairman; Group Chief Executive; Group Chief Financial Officer; Group Chief Risk Officer; Director of Group Finance; Group Chief Internal Auditor; Legal & General Retirement Finance Director; Group Actuary; Chief Tax Officer; Representatives of the external auditor, KPMG LLP.

## Letter from the Chairman Dear Shareholder

I am pleased to present the Audit Committee report for the year ended 31 December 2021. The report explains the work of the Committee during the year and meets the disclosure requirements set out in the 2018 UK Corporate Governance Code (the 'Code').

The Code requires that the Audit Committee must operate effectively and efficiently and that its members have a balance of skills and experience to deliver its responsibilities.

The members of the Audit Committee have a wide range of experience, including as executives in the financial services and other sectors, as non-executive directors, and as board members responsible for financial reporting. The Board considers that I meet the requirements of the Code in having recent and relevant financial experience, as do other members of the Committee. The full biographies of all Committee members can be found on pages 62 to 63. At the end of March, Julia Wilson retired from the Audit Committee and resigned from her role on the Board. I would like to take this opportunity to thank Julia for her considerable support and wise counsel during her time as both a member and former Chair of the Committee.

It is worth highlighting that all members of the Committee are also members of the Risk Committee, which ensures that there is appropriate identification and management of any issues that are relevant to both committees.

The Audit Committee meets regularly and privately with the external auditor and the Group Chief Internal Auditor. These meetings allow for regular and open dialogue of any issues relevant to the Committee's work. Audit

Committee members also meet regularly with management outside of formal Committee meetings to discuss topical issues and maintain their understanding of the group's businesses.

During 2021, the Secretary of State for Business, Energy and Industrial Strategy issued an extensive and wide-ranging consultation on "Restoring trust in audit and corporate governance." Members of the Committee reviewed the consultation and considered its implications for both the group and the Audit Committee more specifically, as well as in the wider context of ensuring that the UK remains an attractive market for shareholders, investors and broader stakeholders. We are supportive of the early establishment and empowerment of the Audit, Reporting and Governance Authority (ARGA) to ensure that reforms and associated standards are suitably embedded in relevant professional and corporate bodies, and the Committee will continue to keep a close focus on any proposed legislation, changes in corporate governance requirements and emerging best practice to ensure that the group continues to be seen as a strong advocate of high quality and transparent audit and corporate governance.

## Audit Committee focus for 2021

The Audit Committee met five times in accordance with its annual plan and additional informal meetings were arranged as necessary. In line with its purpose, the Committee's time over the course of the year was spent in consideration of:

- the resilience of operational and financial controls in a continuing hybrid working environment.
- the integrity of the company's financial statements and Solvency II disclosures, including consideration of the viability statement and going concern assessments.
- key accounting, financial reporting and actuarial areas of judgement, including the impact of Covid-19, the presentation and transparency of the group's financial disclosures, including consideration of the group's Alternative Performance Measures.
- the adequacy of climate disclosures, including consideration of the group's climate report.
- the adequacy and effectiveness of our systems of internal control, including whistleblowing.
- the effectiveness, performance and objectivity of both the internal and external audit functions including an externally facilitated review of the Group Internal Audit function.
- the group's preparations for the transition to the new accounting standard for insurance contracts, IFRS 17.

While the global outbreak of Covid-19 has continued to have a profound impact on society, the direct impacts on the group have lessened or been mitigated during 2021, and this has allowed the Committee to adjust its activities to look at other areas of focus. One area associated with Covid-19 where the Committee has continued to spend a proportion of its time is in respect of the move to a hybrid working model. While this is recognised more and more as a 'new normal', and brings with it many benefits from an individual employee and company perspective, it also carries a new set of risks and it is right for the Committee to focus on the resilience of the control environment in light of this changed operating model, including how it is monitored and overseen in the future.

As the implementation date of IFRS 17 draws closer, the Committee's focus on the group's preparedness has continued to increase. While the Committee has continued to monitor the implementation of the systems, processes and operating model to support the delivery of the new financial reporting requirements, time has also been spent in reviewing and approving certain methodologies, policies, assumptions and reporting metrics, supported by a number of Board technical awareness sessions held outside of the normal Committee meetings.

Finally, the Committee has spent time during 2021 in consideration of the scope, focus and quality of the various sources of assurance from which it is able to gain comfort. This has included: working with Group Internal Audit to incorporate timely and independent assurance over specific elements of the IFRS 17 programme; monitoring the continued development and embedding of the group's Model & Financial Control Framework (MFCF), including the receipt and review of regular reporting on the outcome of design and operating effectiveness testing; and a decision to require independent limited assurance over certain elements of the group's climate report.

### Effectiveness reviews

The Committee's performance was externally evaluated by Independent Board Evaluation (IBE) in December 2020. The Committee identified two actions as part of its evaluation: undertaking a review of the Committee's composition to ensure that it operated as efficiently and effectively as possible; and enhancing the Committee's engagement with both Group Internal Audit and the external auditor. In



The Audit Committee's terms of reference, which set out full details of its responsibilities, can be viewed on our website [group.legalandgeneral.com/committees](http://group.legalandgeneral.com/committees)

response to the evaluation, which suggested that the Committee would benefit from a smaller more technically focused membership, the composition of the Committee was revised on 1 May 2021 and Nilufer von Bismarck was appointed as a member of the Committee. Feedback was also provided to the Internal Audit Function to enhance communication and individual briefing sessions with external auditors were scheduled regularly.

In 2021 the Board undertook an internal evaluation, which was externally facilitated by IBE and included an effectiveness review of the Board Committees, including the Audit Committee. Committee members were satisfied with the effectiveness of the Committee and the progress that had been made on the Committee's succession plans.

I am pleased to report that the Committee continues to operate effectively. Looking ahead to the coming year, I expect the Committee to be focused on an ever-broadening range of topics. IFRS 17 will inevitably require a deeper and more concentrated focus as the group begins to produce comparative information for the year ending 31 December 2022, as KPMG undertakes more detailed audit work on those comparatives, and as the new financial reporting operating model goes through final implementation and testing in advance of go-live in 2023. At the same time, the Committee will continue to consider and review wider aspects of the group's reporting, particularly Alternative Performance Measures under the new accounting standards and the increasing stakeholder focus on non-financial metrics, as well as the continued embedding of the MFCF to support and demonstrate the robustness of the financial reporting control environment.

This will be my last report as Chairman of the Audit Committee. Tushar Morzaria will join the Board in May and will succeed me as Chairman of the Committee upon his appointment. Tushar has a wealth of recent and relevant expertise in financial services and will bring a fresh view to the work of the Committee. I will remain as a member of the Committee to provide continuity of experience.

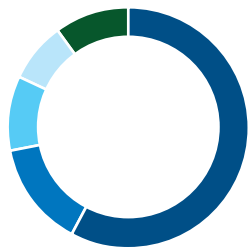
The information on the following pages sets out in detail the activities of the Committee during the year. I hope that you will find this report useful in understanding our work and I welcome any comments from shareholders on my report.

**Philip Broadley**  
Chairman of the Audit Committee

# Audit Committee report

## continued

### Percentage of time allocated to specific agenda items



- 58% Actuarial, accounting and financial reporting, including areas of judgement and reporting developments
- 14% External audit
- 10% Internal audit
- 8% Internal controls
- 10% Other (including governance)

### How the Audit Committee spent its time in 2021

The Audit Committee is a Board Committee with governance responsibilities that include the oversight of financial disclosures and corporate reporting. The Board has delegated to the Audit Committee the principal responsibilities to assist the Board in discharging its responsibilities with regard to monitoring the integrity of the group's financial statements, monitoring the effectiveness of the internal control (including financial internal control) framework and overseeing the independence and objectivity of the internal and external auditors. The Audit Committee is also responsible for advising the Board on whether the annual report and accounts, taken as a whole, are fair, balanced and understandable and for reviewing the basis on which the Board provides the viability statement and going concern assessment.

The Audit Committee has an annual work plan aligned with the financial reporting cycle of the Company. The Audit Committee's activities fall into three principal areas:

- accounting and financial reporting.
- internal and external audit.
- internal control.

#### Accounting and financial reporting

The Audit Committee reviews the appropriateness of the half year and annual financial statements, which it carries out with both management and the external auditors. This review includes ensuring that the annual report and accounts, taken as a whole, are fair, balanced and understandable, as well as covering compliance with disclosure requirements and the material areas in which significant judgements have been applied.

In collaboration with the Risk Committee, the Audit Committee also reviews the disclosures to be made in relation to internal control and risk management, as well as the principal risks and uncertainties the group faces.

The Committee can confirm that the key judgements and significant issues considered in relation to the 2021 financial statements are consistent with the disclosures of key estimation uncertainties and critical judgements as detailed in Note 1 on page 139.

Robust year-end governance processes are in place to support the Audit Committee's considerations which include:

- ensuring that all of those involved in the preparation of the Company's annual report have been appropriately trained and fully briefed on the 'fair, balanced and understandable' requirements.
- internal legal verification of all factual statements, and descriptions used within the narrative.
- regular engagement with and feedback from senior management on proposed content and changes.
- feedback from external advisors (corporate reporting specialists, remuneration and strategic reporting advisors, external auditor) to enhance the quality of our reporting.
- early opportunity for review and feedback on our annual report by Audit Committee members.

During the year, the Audit Committee has continued to keep abreast of significant and emerging accounting and reporting developments, including consideration of changes in disclosures arising from best practice application and Financial Reporting Council (FRC) publications on aspects of UK reporting.

Significant accounting and reporting judgements considered during 2021 are shown below:

Issue	Committee's response
<p><b>Valuation of non-participating insurance contract liabilities – retirement:</b></p> <p>The non-participating insurance liabilities for retirement products are significant in size and their estimation is inherently judgemental.</p>	<p>The Committee evaluated the significant judgements that have an impact on the valuation of non-participating insurance liabilities for retirement products. This included considering:</p> <p>Valuation interest rates – which are used to discount the liabilities. These are sensitive to judgements made, for example, on credit default of the backing assets, as well as the investment data used to calculate the internal rate of return. The Committee focused on management's proposed changes to reserving assumptions, other modelling changes, and the determination of the credit default assumption. This included analysis of internal historic data and external market experience.</p> <p>Longevity assumptions – which estimate how long policyholders receiving annuity payments will live. The challenge around the setting of longevity assumptions was a particularly significant area for review as the judgements made could be expected to have a material impact on the group's results. The Committee considered the effectiveness of the controls over the accuracy and completeness of the data used in determining the longevity assumption and the validity of independent industry data supporting those assumptions. The Committee also reviewed available data illustrating recent trends in mortality experience in the UK population and the mortality experience on different blocks of our business, taking account of the uncertainty in more recent data as a result of Covid-19.</p> <p>The Committee concluded that the retirement insurance contract liabilities are appropriate for including in the financial statements, reflecting the asset risks and the available data on policy holder longevity.</p>
<p><b>Valuation of complex investments:</b></p> <p>Mark to model investments can involve significant judgement and can produce valuation challenges for investments in new classes.</p> <p>Mark to model valuations inherently include assumptions that lead to the existence of a range of plausible valuations for financial instruments (known as valuation uncertainty). Certain assets are subject to a higher degree of valuation uncertainty, particularly where valuations are modelled using no market inputs or the valuations are affected by other factors such as the illiquidity of the asset.</p>	<p>The group balance sheet carries exposure to complex investments (typically classified as Level 3 in the fair value hierarchy), in line with the group's strategy and risk appetite. The valuation of these investments, including property assets, lifetime mortgages, and private credit, requires the use of complex models and management judgement. The Committee seeks to ensure that the valuation process for these investments is robust.</p> <p>While 2020 saw increased volatility within asset markets as a result of Covid-19, we have experienced a market recovery and greater stability during 2021, further supported by the diversity of our asset portfolio. These harder to value assets remain a key areas of focus, however, and the Committee has continued to review the processes and controls over investment valuations, and in particular the valuation uncertainty policies and governance which include management's assessment of valuation uncertainty by asset type. While we do not currently see any material impact on the valuation of our asset portfolio arising from climate change, we expect this to be an increasing area of judgement (and therefore disclosure) in future years, and it will form a key area of focus in the Committee's review of this area.</p> <p>The Committee concluded that there are appropriate controls surrounding the valuation of complex assets and that they are valued appropriately for inclusion in the financial statements.</p>
<p><b>Valuation of non-participating insurance liabilities – insurance:</b></p> <p>The non-participating insurance liabilities for protection contracts are an important driver of the profitability for this line of business and require judgements to be made regarding the assumed rates of mortality and persistency. The Company makes extensive use of reinsurance to reduce mortality risk.</p>	<p>The Committee has reviewed the methodology for calculating reserves including the allowance made for payments to and from reinsurance counterparties. The assumptions for the rate of future mortality and morbidity (how many customers will die or become ill during the policy term) and persistency (how many customers will discontinue cover) are based on the Company's internal experience and use judgement about how experience may vary in the future. During 2021, the Committee has continued to spend time reviewing the findings and judgements in respect of the mortality experience of our UK and US books as a result of Covid-19.</p> <p>During 2021 the Committee reviewed the rationale and assumptions used to support the change in valuation interest rate methodology for UK protection liabilities to incorporate an illiquidity premium as a reflection of available assets to back later duration cash flows yielding more than the risk-free rate.</p> <p>The Committee reviewed the assumptions and the expected level of prudence taking into account market benchmarking, internal experience studies and the reinsurance structures. The Committee considered the effectiveness of controls in place over valuation models.</p> <p>The Committee concluded that the insurance liabilities of the Insurance division are appropriate for inclusion in the financial statements.</p>

# Audit Committee report

## continued

Issue	Committee's response
<p><b>Alternative Performance Measures (APMs):</b></p> <p>APMs offer investors and stakeholders additional information on the Company's performance and the financial effect of 'one-off' events, and the group uses a range of these metrics to enhance understanding of the group's performance.</p>	<p>As part of its consideration of whether the annual report is fair, balanced and understandable, the Committee has paid particular attention to the use of APMs in reporting the group's performance. In this regard the Committee has reviewed the group's use of APMs in light of the FRC's thematic review in October 2021.</p> <p>The Committee has reviewed the application of adjusted operating profit, and specifically the inclusion of certain items either as part of adjusted operating profit or investment variances, to ensure that they are aligned to both the group's disclosed policies on these APMs, and the underlying principles of fair and consistent reporting. Where appropriate the Committee has reviewed additional disclosures provided to enhance transparency in respect of the group's APMs.</p> <p>The Committee concluded that the use and disclosure of APMs, including the clarity of labelling the prominence of APMs versus statutory measures, are appropriate for inclusion in the annual report.</p>
<p><b>IFRS 17:</b></p> <p>IFRS 17 is a new accounting standard for insurance contracts due to take effect on 1 January 2023. IFRS 17 is expected to have a significant impact on the reporting of the group's financial performance.</p>	<p>As well as continuing to monitor the preparedness of the group to implement IFRS 17, the Committee has reviewed a number of papers during 2021, covering various areas of policy, methodology and assumptions, such as the application of the General Measurement Model.</p> <p>In particular, the Committee has reviewed the methodology and assumptions to support the transition to IFRS 17, including the decision to apply the fair value approach to calculate the contractual service margin on transition for annuities issued prior to 2016.</p> <p>The Committee has further reviewed certain demographic assumptions which will be applied as part of the transition, as well as broader additions to the group's Accounting Policy Manual in respect of IFRS 17.</p> <p>The Committee concluded that the disclosures in respect of IFRS 17 included in Note 1 Basis of Preparation are appropriate for inclusion in the annual report.</p>

The Audit Committee, having completed its review, recommended to the Board that, when taken as a whole, the 2021 annual report is fair, balanced and understandable, and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy and the business risks that it faces. The Audit Committee, together with the Risk Committee, reviewed the key assumptions and methodologies of the risk-based capital model as well as related Solvency II disclosures. The statement is underpinned by the Committee's belief that all important information has been disclosed and that the descriptions and reviews of the group's business and performance as set out in the Strategic Report are consistent with the financial reporting in the group's financial statements.

### Internal control

The Board has delegated responsibility for reviewing the effectiveness of the group's systems of internal control to the Audit Committee.

The Audit Committee has the primary responsibility for the oversight of the group's system of internal controls including controls over financial reporting and the work of the

internal audit function. The Audit Committee, in collaboration with the Risk Committee, seeks to ensure that the group operates within a framework of prudent and effective controls that allow risk to be identified, assessed and managed.

The Audit Committee has completed its review of the effectiveness of the group's system of internal control policies and procedures, during the year and up to the date this report was approved, in accordance with the requirements of the Guidance on Risk Management, Internal Control and related Financial and Business Reporting published by the FRC. During this review, the Audit Committee did not identify any weaknesses which were determined to be significant to the preparation of the financial statements. Where areas for improvement were identified, processes are in place to ensure that the necessary actions are taken and progress is monitored by the Audit Committee.

### Internal Audit

The Audit Committee monitored and reviewed the scope, extent and effectiveness of the activity of the Group Internal Audit function. In particular, the Audit Committee evaluates the alignment of the internal audit plan with the group's key risks and strategy.

The Group Chief Internal Auditor has a standing agenda item at each Audit Committee meeting to update the Audit Committee on audit activities, progress of the audit plans, the results of any unsatisfactory audits and the action plans to address these areas. The group has adapted quickly to the adoption of a hybrid working model, and Internal Audit were able to undertake all the audits within their Internal Audit Plan, including some additional reviews to test the continued effectiveness of the overall control environment as remote working continued during the year, as approved by the Committee, completing 115 audits in 2021. There was a particular focus on key themes including: the effectiveness of the control framework in a remote working environment; cyber/data management and governance; financial control framework; digital business and regulatory change; conduct risk; financial management and control; model and end user computer risk; outsourcing/vendor management and economic and political volatility.

The Audit Committee meets with the Group Chief Internal Auditor in private throughout the year. The Committee, in line with the Chartered Institute of Internal Auditors Financial Services Code of Practice, conducted an assessment of, and were able to confirm, the independence of the Group Chief Internal Auditor.

### The external auditor

The Audit Committee has the primary responsibility for overseeing the relationship with, and performance of, the external auditor. This includes making recommendations for their appointment, re-appointment, removal and remuneration.

### Appointment

The Audit Committee is cognisant of the requirements governing the appointment of an external auditor, notably the requirements of the Statutory Audit Services for Large Companies Market Investigation (Mandatory Uses of Competitive Tender Process and Audit Committee Responsibilities) Order 2014, including requirements for mandatory audit firm rotation. The Company confirms that it has complied with such requirements for the financial year under review.

Following a competitive tender carried out in 2016, KPMG was appointed as the group's external auditors with effect from the financial year ended 31 December 2018. In May 2021, KPMG was reappointed as the group's external auditor for the financial year ended 31 December 2021, which is their fourth year as the group's external auditor. Rees Aronson, who has been the lead audit partner for KPMG since appointment, continued in that role for the year ended 31 December 2021. Mr Aronson will retire from KPMG during the course of 2022. The Committee accepted KPMG's proposal that Salim Tharani succeeds Mr Aronson as lead audit partner for 2022. Mr Tharani has been involved as a partner on the audit for the past four years.

### Performance

The Audit Committee assesses the effectiveness of the external auditor against the following criteria:

- provision of timely and accurate industry-specific and technical knowledge.
- maintaining a professional and open dialogue with the Audit Committee Chair and members at all times.
- delivery of an efficient and effective audit and the ability to meet objectives within the agreed timeframes.
- the quality of its judgements and audit findings, management's response and stakeholder feedback.

The Audit Committee receives regular reports from the external auditor on audit findings, significant accounting and actuarial issues, and internal control matters. During 2021, there has been an increase in reporting relating to IFRS 17,

including work on key judgement areas, accounting policies, actuarial assumptions and the impact of the transition to IFRS 17 on audit approach and planning.

The Audit Committee meets the external auditor in private throughout the year.

As in the prior year, as a result of Covid-19 much of KPMG's audit work has been undertaken remotely. The Audit Committee has sought to understand whether this has impacted KPMG's audit plan or their ability to undertake their work effectively. KPMG's regular reporting throughout the year has demonstrated no significant or adverse impact from remote working, and the Committee is comfortable that there has been no undue impact on their effectiveness.

The Audit Committee reviews and approves the terms of engagement of the external auditor and monitors its independence. This includes maintaining the policy for overseeing the engagement of the external auditor for pre-approved audit services, audit-related services and other non-audit work. The non-audit services policy includes a 'whitelist' of permitted audit and audit-related services along with a list of prohibited services. The policy, the purpose of which is to ensure that the independence of the external auditor is not impaired, is approved by the Audit Committee and meets the requirements of the FRC Ethical Standard.

Our practice is to approach other firms for significant non-audit work. The group's policy requires that all services with an anticipated cost in excess of a specified amount are subject to a full competitive tender involving at least one other alternate party in addition to the external auditor. If the external auditor is selected following the tender process, the Audit Committee is responsible for approving the external auditors' fees on the engagement.

For services with an anticipated cost below the specified amount, the Group Chief Financial Officer has authority to approve the engagement. The external auditor and management are required to report regularly to the Audit Committee on the nature and fees relating to non-audit services provided under this authority.

KPMG annually reports on whether and why it deems itself to be independent. The Audit Committee remains satisfied that KPMG continues to be independent.

### Remuneration

In 2021, the group spent £1.3 million on non-audit services provided by KPMG. It spent £1.3 million on audit-related services required by legislation, which is excluded from any calculation of the ratio of non-audit to audit fees in accordance with the UK FRC Revised Ethical Standard for Auditors (2019). Further details can be found in Note 31 to the consolidated financial statements. The non-audit fee represents 11% of the total audit fee for 2021.

### Analysis of current and prior-year spend on audit, other assurance and non-assurance services

	2021	2020	2019
Audit	9.3	10.1	7.1
Audit-related required by legislation	1.3	1.4	0.8
Other audit-related	1.2	0.6	1.1
Other assurance	0.1	0.6	0.3
Non-assurance	–	–	0.2
Total	11.9	12.7	9.5