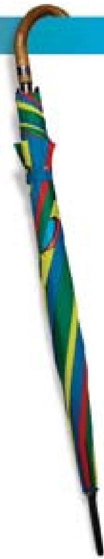
Annual Report and Accounts 2006

Balanced Growth



Legal & General

Legal & General has the expertise, growth, balance and strength to succeed as a premier financial services provider. We focus on what we do best – and we constantly seek to improve the products and services we offer.

Expertise

In-depth understanding of opportunities and risks in our chosen markets create a powerful proposition for customers and shareholders.

p11

Growth

We move and adapt with economic, demographic and market changes, and are positioned to grow in a growing market.

p15

Balance

Our scale and capability across a broad, balanced product range enables us to reach an increasingly large and diverse customer base.

p19

Strength

Our business is underpinned by the strength of our finances and our human capital. This assures customers we will be there when they need us.

p23

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EEV[1] basis

	2006	2005
Operating profit before tax[2]	**£1,233m**	£1,092m
Contribution from new business[3]	**£479m**	£380m
Ordinary shareholders' equity	**£7,931m**	£6,970m
Dividend cover[4]	**2.4**	2.3

IFRS[5] basis

	2006	2005
Operating profit before tax[2]	**£752m**	£647m
Ordinary shareholders' equity	**£5,425m**	£4,257m
Dividend cover[4]	**1.5**	1.3

	2006	2005
Worldwide new business APE[6]	**£1,842m**	£1,296m
New institutional funds	**£20.7bn**	£17.1bn
Group funds under management	**£237bn**	£208bn

1. European Embedded Value
2. From continuing operations
3. Includes pensions managed funds
4. Dividend cover is calculated as operating profit after tax divided by the current year interim dividend plus the proposed final dividend
5. International Financial Reporting Standards
6. Annual Premium Equivalent (APE) is total new annual premiums plus 10% of single premiums

UK Life and Pensions New Business (£m APE)

Year	£m APE
2006	1,073
2005	872
2004	722
2003	592
2002	608

Dividend per share (p)

Year	p
2006	5.55
2005	5.28
2004	5.06
2003	4.90
2002	4.78

New Institutional Funds (£bn)

Year	£bn
2006	20.7
2005	17.1
2004	15.5
2003	13.1
2002	14.0

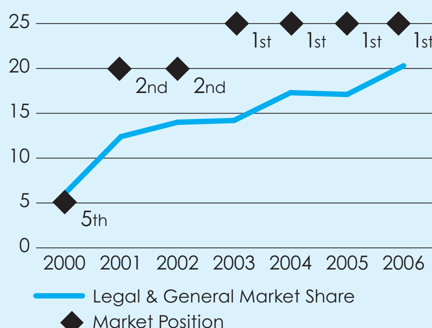
Our business at a glance

Our scale and capability across a broad, balanced product range enables us to reach an increasingly large and diverse customer base.

Protection and Annuities

Legal & General is an expert provider of risk based products, operating across a number of markets. These include life assurance and critical illness cover, individual and bulk purchase annuities, group risk and household and income protection.

Protection Retail Market Share and Rank 2000-06 (%)



Market Position

We are a major provider of life, protection and annuity products in the UK. We support the largest network of mortgage advisers in the UK who are responsible for more than £20bn of mortgage placement per annum. Our products are priced to provide value for money for our customers.

£405m

APE[1]

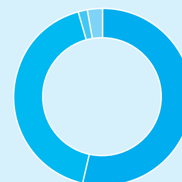
APE increased by 12%

Wealth Management

Legal & General is a leading provider of wealth management products. We distribute a wide range of individual and corporate pensions as well as investment bonds, unit trusts and ISAs through IFAs, business partners, banks, building societies and direct to customers.

Wealth Distribution Split

- IFA 53%
- Banks 42%
- Tied Agents 2%
- Direct 3%



Market Position

We are a consistent top three provider of wealth products to the IFA sector and a leading wealth product partner to banks and building societies in the UK. In 2006 we launched a range of open architecture products through our partnership with Cofunds, a leading investment platform provider in the UK.

£664m

Retail Investments APE

Total sales more than doubled

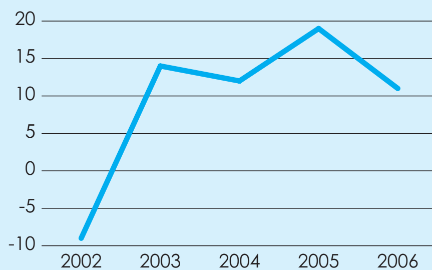
1. Annual Premium Equivalent

For more information on the Group visit www.legalandgeneralgroup.com

With-Profits

Legal & General's with-profits business includes pension and unit-linked savings products that offer a with-profits option. The business is managed separately from non profits business and is backed by a financially strong fund enabling us to take advantage of a wide range of investment opportunities.

Return on Assets Backing With-Profits Policies (%)



Market Position

In 2006 the with-profits business paid £596m in bonuses having generated a return of over 11% gross of tax and investment charges on assets backing with-profits participating policies. The five year return of 55% has exceeded the FTSE All-Share and FTSE 100 indices.

+43%

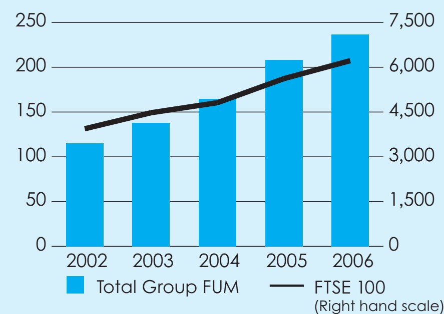
Bonus Payments

£596m bonus payments

Investment Management

Legal & General Investment Management (LGIM) is one of the largest asset managers in the UK, providing institutional investors with straightforward, value for money investment solutions. Our product range includes index funds as well as actively managed equity, fixed income, and commercial property funds.

Growth of Funds under Management (FUM) (£bn)



Market Position

LGIM is the leading provider of asset management services to UK corporate pension schemes, managing assets for over 2,800 companies including 54 of the top 100 UK listed companies. Our scale is such that we hold 3.8% of UK plc.

£20.7bn

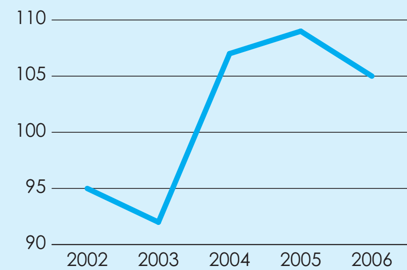
New Funds under management

New business up 21%

International

Legal & General's principal international businesses operate in the United States, France and the Netherlands. They are active in selected lines of business in individual and group protection and savings.

International New Business (£m APE)



Market Position

More than 90% of Legal & General's business is in the UK. Our international operations form a complementary portfolio of profitable, specialist businesses.

+£56m

Increase in EEV operating profit

EEV operating profits up 56%

Continued profitable growth

In 2006, Legal & General achieved both record new business and record operating profits. Our total UK market share for the year exceeded 11% for the first time. These are the achievements of a strong and successful company.

Sir Rob Margetts
Chairman

Legal & General continued to make excellent progress in 2006, achieving record new business, operating profits and market share. Your Company has performed well and achieved significant operational successes, extending its already strong franchise in the UK market.

Today, we provide financial products to over 5.7 million customers. We have a total market share of over 20% of the UK individual protection market, and with equity investments of around 3.8% of the FTSE 100 Index, we are one of the largest single investors in 'UK plc'. Our role as a financial product provider and a manager of long term savings and pension assets is underpinned by our commitment to corporate and social responsibility, and to our 9,700 employees.

Strategic Continuity

Legal & General has a clear strategy which has consistently delivered results. Customer service, value for money products, strong multi-channel distribution and excellent administration – all underscored by financial strength and integrity – drive value for customers and shareholders alike.

Our business is principally in the UK, and our long term focus on this core market has proved well-founded. In 2006, a positive economic backdrop and increasing public awareness of savings and pensions contributed to strong growth in new business, as did the continuing stimulus from the 'A-day' changes to pensions. Our main overseas businesses, in the United States, France and the Netherlands, performed steadily during the year.

We balance both production and distribution. Our product portfolio is managed to recognise the different characteristics of protection, annuity and savings businesses, and our wide product range reflects the variety of opportunity in the market and our own preferences for flexibility and spreading risk.

Our multi-channel distribution encompasses business partners, Independent Financial Advisers (IFAs) and direct sales. This reduces the risk of over-dependence on any single route to market, building flexibility and resilience into our business model. Many of our business partners are household names in

2006 Highlights

£1.2bn

EEV Operating Profit

+42%

Worldwide new business growth

+5.1%

Growth in full year dividend

UK financial services, and we are committed to the development of new distribution models and online solutions. We were delighted to be chosen as a strategic partner by the Nationwide Building Society in early 2007, and are looking forward to working closely with them, as with all of our other partners.

Excellent administration is strategically important to your Company. Many of our customers hold long term products and rely on our service as much as on our product and investment expertise. We continue to invest significantly in new technology and our Customer Experience Programme.

Financial Highlights
Worldwide new business grew by 42% to £1,842M on an Annual Premium Equivalent (APE) basis, a new record for Legal & General. New business growth was accompanied by increases in profits. EEV Operating Profit, rose by 13% to £1,233m in 2006.

Legal & General's strong balance sheet enables us to prosper, even in difficult trading conditions. Financial strength remains a key strategic differentiator for distribution partners and customers alike.

Dividend and Shareholder Return
In 2006, Legal & General delivered a Total Shareholder Return (TSR) of 34%.

The Board remains committed to a progressive dividend policy. In July 2006 we increased the interim dividend by 5.5%. We now recommend an increase of 5.0% to the final dividend, making a full year increase of 5.1%. Our recommendation is based on a thorough review of the Company's financial strength and current investment market conditions, taking account of the capital required to support future investment and new business.

In November 2006, we announced the initial conclusions of our capital and cash flow review. These included a commitment to review our capital position on a regular basis, and have indicated that we will return excess capital to shareholders where appropriate.

Management Strength
This year was Tim Breedon's first as Group Chief Executive. The performance of the business under his leadership has fully justified the Board's confidence in appointing him. The transition has been seamless, and Tim has brought to the role his own qualities of intellectual rigour and commitment to continuous improvement.

During 2006, we implemented a realignment programme to improve focus on specific businesses and create end-to-end responsibility for product development, delivery and administration within business units. The with-profits business now has its own distinct management structure. I am proud of the way staff at all levels of the business responded to this challenge while continuing to win and execute record volumes of profitable new business. Our employees and our culture are two of our greatest assets. I would like to thank all our staff. Their commitment to teamwork and customer focus are core strengths that run through all our business.

Board Changes
Rudy Markham joined the Board as an independent non-executive director in October 2006. As Chief Financial Officer of Unilever PLC, he brings extensive business and financial experience. Barrie Morgans stepped down from the Board on 18 May 2006, having served with distinction for nine years. We thank him for his able Chairmanship of the Audit Committee and his contribution to the affairs of the Company. Beverley Hodson will stand down from the Board at the AGM, and we would also like to thank her for her contribution over the last seven years.

Shareholder Communications
Most shareholders would like a more focused, shorter, report from companies in which they invest. This year we are providing a Summary Financial Statement (SFS) as an alternative to our normal Annual Report and Accounts (ARA). Unless you have specifically requested the full ARA, you will be receiving the SFS. Both will be available on the Group's website: www.legalandgeneralgroup.com. In future, we expect to make more use of e-commerce for reporting. We will inform you of our plans later this year.

In line with new Companies Act's Narrative Reporting requirements, we now detail our financial 'Key Performance Indicators' (KPIs), on page 51, and provide a description of the principal risks and uncertainties, on page 27. These relate closely to the Company's strategy and the objectives set for executive directors.

Outlook
Your Company is well positioned for the future. We envisage continuing economic growth in the UK for the coming year, which will in turn drive business growth across our core product lines. We see a continuing A-day effect, and increased customer awareness of the need to save and invest for longer retirements. This stands to benefit both our consumer and institutional businesses. Our ongoing commitment to strong and balanced distribution will enable us to access customers increasingly effectively, while also continuing to position ourselves for technological and market evolution.

In a competitive market environment, the strategic continuity of our business model and the strength and capability of management, staff and our established culture, enable us to focus on operational delivery. We are confident we will deliver further shareholder value in 2007.

Rob Margetts

Sir Rob Margetts
Chairman

A strategy that works

Our UK-led strategy of balanced production, balanced distribution and capital strength remains the right one to build on the success of 2006 and deliver further value in 2007.

Tim Breedon
Group Chief Executive

Legal & General has a clear and consistent strategy. We operate in scale, we focus largely on the UK market, and we provide a wide range of value-for-money products backed by strong technical skills, excellent administration, multi-channel distribution and a customer service ethic.

Our underlying businesses again performed strongly in 2006. The 46% increase in our UK new business was achieved against a favourable economic backdrop and demographic changes that encourage long term saving and financial planning. Ultimately our success is due to having the right mix of well-designed competitively-priced products, sold through the most effective distribution channels.

Balanced Production

Legal & General's broad product range differentiates us from other companies in the UK life and pensions sector. We maintain a wide product set, giving us flexibility to adjust to consumer preferences.

Our combination of protection, annuity, insurance and savings – including pensions – gives us a product range that can meet a customer's needs at every stage of their life. Financial protection for individuals and their families often coincides with changes to mortgage arrangements. Flexible saving through unitised products or ISAs can be part of a series of long term saving vehicles, perhaps including employer or personal pension schemes. Ultimately, accumulated savings can be consolidated in the most efficient way, and a lifetime income purchased by way of an annuity.

Legal & General is active in all these retail markets, as well as providing group schemes, bulk purchase annuities and institutional fund management for employers and pension funds. In addition our Investment Management business has established itself as a leading provider of index tracking funds and other investment products.

Balanced Distribution

Balance and flexibility also underpin our distribution strategy.

We continue to expand distribution through new bank and building society partnerships, most recently with Nationwide, which with 11 million customers, is the country's largest building society. Each partnership is different, but collectively our business partners have over 40 million personal finance customer accounts in the UK, and a powerful High Street presence. Some 60% of our retail sales are through IFAs. We constantly evolve our product and service offering to the advised sector. This includes developing multi-manager and platform solutions which widen choice and add to administrative convenience for IFAs. They make it easier for customers, with their advisers, to make asset allocation decisions. They also administer a portfolio of long term savings and investments managed by a variety of asset managers but held on a single online platform. Cofunds, the fund supermarket with which we have formed a strategic alliance and which now has over £11bn of funds under management, is an example of leadership in its sector.

In addition, our direct distribution capability serves our customers and enhances our offering to business partners.

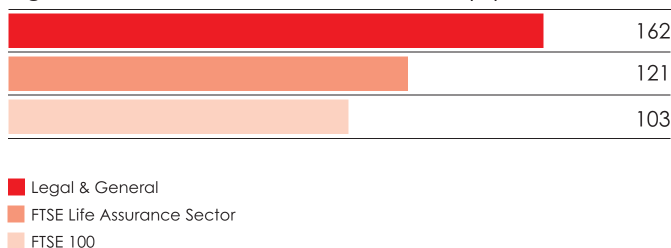
Flexibility in profitable distribution will remain important to growth. In the future consumer purchasing patterns, and regulation of sales, may change – for example as a result of the Financial Service Authority's upcoming Distribution Review. This will place a premium on those financial product providers best-adapted to an increasingly multi-channel distribution network.

Growth and Profitability

It is axiomatic to our strategy that growth should not be at the expense of profitability. We monitor margins closely across the product range and aim to adjust our business mix accordingly.

Occasionally where necessary, we make changes to our portfolio of business.

Fig 1. Ten Year Total Shareholder Return (%)



>90%

of new business generated in the UK

For example, in April 2006 we launched a new Self-Invested Personal Pension (SIPP) product, and in General Insurance, we withdrew from the motor and subsequently the healthcare sectors.

Over 90% of new business is generated in the UK. Our strategy is strongly focused on our domestic market, though our overseas businesses – principally in the United States, France and the Netherlands – are valuable assets and solid performers. Strategically, we are open to new opportunities in different markets, but only where they satisfy our rigorous internal investment criteria.

Capital Strength

Capital strength enables us to take the strain of growing the business and provides security for long term customers and policyholders. It is a further strategic differentiator and is reflected in our AA+ financial strength rating from Standard & Poor's. Excellence in the management of our capital is a key skill for a life company. Our previous capital structure has served us well for a decade, enabling us to deliver growth across a stock market cycle. The current capital review will ensure we balance capital strength, growth and shareholder return in the most efficient way. The Board currently intends to initiate a programme of returning capital to shareholders from the second half of 2007 where it is clear that there is excess.

This capital review is taking place against a changing regulatory and fiscal background. Our challenge is to have the right amount of capital, the right type of capital, and to deploy our capital in the right places. In late 2006 we took the first steps by establishing a new reinsurance company to assume our own pension and annuity liabilities. Further actions, which will provide long term benefits to our business, are planned in 2007.

A skilled workforce

During 2006 we realigned management responsibilities to create a clearer structure in our Protection and Annuities, Wealth Management and With-Profits businesses. These changes will deliver increased focus, end-to-end product and profit responsibility and improved efficiency. This will help us make the most of the very considerable skill base of our workforce.

Achievements and Outlook

2006 was a year of significant milestones for Legal & General. We are an established scale player in the UK market. Our bulk annuities business passed the £1bn single premium mark in new business during the year; despite the arrival of new competitors. Our wealth management business achieved significant sales growth, with over £11bn of new UK savings premiums. Our institutional fund management business added almost £21bn of new funds under management, taking us to £233bn in total.

Looking ahead, Legal & General's scale gives us the opportunity to invest in the people and skills to make further gains in our markets. Our focus on core skills and products, and our balance sheet strength, position us well in markets which continue to provide growth opportunities. Our flexibility across product and distribution lines will enable us to adjust our business mix to concentrate on delivering growth and doing so profitably.

The UK's underlying economic strength, combined with later retirement and improving longevity mean continuing growth in saving through long term financial products. Corporate activity to tackle pension fund deficits is positive for our institutional fund management and bulk annuities businesses. The mortgage market remains active which generates business flow for protection and general insurance businesses.

We remain of the view that our UK-led strategy of balanced production, balanced distribution and capital strength remains the right one to build on the success of 2006 and deliver further progress in 2007.

Tim Breedon
Group Chief Executive

A well balanced business

Legal & General reports its financial results within three main business segments: Life and Pensions, Investment Management and General Insurance. The Life and Pensions segment comprises the Protection and Annuities, Wealth Management and With-Profits businesses in the UK and the international businesses.

Overview of Results

Legal & General's 2006 results demonstrate the continued strength of our core business and also reflect the first benefits of our wide-ranging capital review, as outlined in a presentation to analysts on Capital and Cash Flow in November 2006 and available on our website: www.legalandgeneralgroup.com.

Our worldwide operating profit on an EEV basis grew by 13% to £1,233m (2005: £1,092m). Contribution from new life and pensions business increased by 26% to £418m (2005: £331m) and total experience and operating assumption changes were positive at £82m. UK life and pensions Operating profit grew by 9% to £874m (2005: £801m), reflecting increased new business contribution. Operating profit from our international business grew by 56% to £156m.

On an IFRS basis, worldwide operating profit increased by 16% to £752m (2005: £647m), owing to higher contributions from both the UK non profit and With-Profits businesses.

With a record £21bn in new institutional funds under management in 2006 and a highly scalable platform, our investment management business grew operating profits by 29% to £133m (2005: £103m). Profit after tax on an EEV basis increased by 18% to £1,446m and by 59% to £1,631m on an IFRS basis.

Significant Events

During 2006, the following events had a significant effect on the Group's results, both on an EEV and IFRS basis. The financial impacts of these events are shown in Figure 2.

Corporate restructure – creation of pensions and annuity company

On 31 December 2006, the non profit pensions and annuity business of Legal & General Assurance Society Limited (Society) was ceded to a new wholly owned reinsurance subsidiary – Legal & General Pensions Limited (LGP). We believe this will provide greater capital transparency and flexibility, enhance Legal & General's ability to compete in the annuity markets and ensure that both our non profit life and pensions businesses are taxed appropriately.
Legal & General Investment Management (LGIM) provides investment services to LGP on a market-related fee basis.

Implementation of changes to FSA reporting

In 2006, the FSA introduced a more realistic reserving framework for certain non profit businesses, as detailed in their Policy Statement 06/14.

Review of annuity investment policy

During 2006, Legal & General undertook a review of its asset liability matching strategy for annuity business. As a result of falling yields, property assets backing annuity liabilities were replaced with corporate bonds. We entered into inflation swaps to better mitigate negative inflation risk. As a result of these actions, a closer match between assets and liabilities was achieved, together with a lower capital requirement and a higher valuation discount rate, reflecting the higher yield. Additionally, the margin within the reserves to cover an interest rate mismatch was reviewed and reduced.

Fig 2. Summary of financial impacts arising from significant events

	Corporate Restructuring	Changes to FSA reporting and capital rules	Annuity investment policy
IFRS			
Increase in SRC	£502m[1]	£496m	£422m
Profit after tax	£171m	£496m	£422m
EEV			
Operating profit	–	£97m	£18m
Profit before tax	(£216m)	£97m	(£9m)
Profit after tax	£171m	£68m	(£6m)
Capital[2]			
IGD surplus capital	(£0.5bn)	–	–
Society surplus capital	(£0.5bn)	£0.1bn	£0.4bn

Note: more detail of the impacts is set out in Note 2 of the Financial Statements and Note 14 of the Supplementary Financial Statements.

[1]There was an offsetting negative in LGP.

[2]Management estimates based on draft regulatory returns.

Fig 3. Worldwide Operating Profit[1] – IFRS Basis

Year ended 31 December	2006 £m	2005 £m
UK life and pensions		
– Distribution relating to non profit and shareholder net worth	**388**	312
– Subordinated debt interest	**34**	37
– With-profits business	**95**	66
	517	415
International life and pensions	**75**	74
Investment management	**133**	103
General insurance	**9**	14
Other operating income	**18**	41
Operating Profit	**752**	647

[1]Operating profit before tax.

Industry and Markets

Regulatory and Political Environment

The majority of Legal & General's business is conducted in the UK. Both our principal operating company, Legal & General Assurance Society Limited (Society), and our investment company, Legal & General Investment Management Limited (LGIM) are regulated by the Financial Services Authority (FSA). Amongst other things, FSA regulation covers sales of products and levels of risk and capital. Our business is also subject to fiscal risk in particular relating to tax treatment of savings products.

Legal & General's principal overseas businesses are also supervised by the relevant local financial regulators. Aspects of the financial services industry, financial products and sales are also subject to European Commission directives.

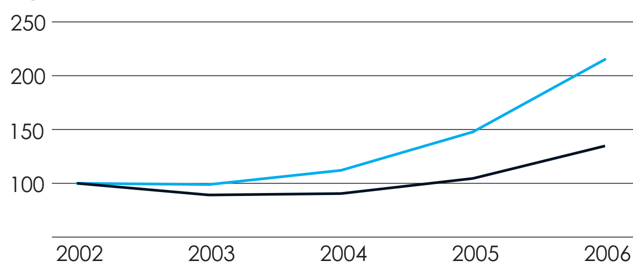
The main regulatory and fiscal impact on our business in 2006 was the simplification of UK pensions regulation – the "A-Day" reforms – which encouraged greater flexibility in pension saving. During the year, the Government announced it would extend the existing Individual Savings Account (ISA) regime and encourage switching from cash to equity ISAs, which we regard as positive. On a negative note, the Government and Her Majesty's Revenue & Customs (HMRC) decision to withdraw favourable tax treatment for stand-alone Pension Term Assurance, months after introduction, closed down the product to new customers, resulting in uncertainty for customers and sunk costs for providers including Legal & General.

Outlook

The Government's proposals to establish 'Personal Account' pensions following the Turner Report are now being progressed through legislation. In common with the industry, we support the principle of extending access to additional pension products to a broader market, but we have reservations about some detailed aspects of the proposals. In particular, we are concerned that Personal Accounts should remain targeted at the currently unprovided market for which we believe they are suitable, and that they do not undermine the existing levels of corporate and private pension provision. We are engaged in dialogue with Government, both directly and through our membership of the Association of British Insurers (ABI), on this subject.

During 2007, the FSA intends to review distribution of financial products, but has signalled that proposals for change should be led by the industry. Legal & General, as a company utilising a broad variety of channels to market, is actively involved in providing input to this process.

Fig 4. UK Total Market Growth[1]



1. Based on new business APE rebased 2002 = 100

Business Environment

Market Overview

The UK financial services industry has grown strongly over the last decade. Value erosion in state pensions and the phasing out of employer defined benefit provision has led to a greater onus on individuals to plan for their long term financial future. Greater awareness of the need to increase retirement provision as a result of increasing longevity, as well as robust economic growth and a strong housing market, have helped the savings, protection and investment market deliver compound annual growth of over 9%pa over the last ten years.

ABI market statistics show that Legal & General has succeeded in growing total UK market share from 4% in 1995 to the current level of above 11% of life, pensions and investment business. We believe this success is a result of our product quality, distribution strength and strategic consistency.

The institutional fund management sector has similarly grown strongly, with an estimated £3 trillion funds now managed in the UK. LGIM manages institutional and retail funds. The majority of funds under management are derived from external institutions, in particular pension funds. Historically, LGIM has specialised in index-tracking and other passive investment strategies, but in line with market developments it is also offering specialist active strategies including liability-driven investment and Structured Solutions.

Outlook

We envisage economic and demographic fundamentals continuing to provide a favourable backdrop to growth in the UK financial services sector. We expect economic growth to continue at or around trend in 2007. We expect to benefit as rising prosperity, later and longer retirements combine to increase investment in long term financial savings and investment products. We expect housing

Expertise

In-depth understanding of opportunities and risks in our chosen markets create a powerful proposition for customers and shareholders.

John Pollock
Group Executive Director (Protection and Annuities)

...that really s

Topping the tables

Last year, Legal & General was recognised in the media as the leading protection provider in the UK.

In January, Legal & General was awarded Best Life Assurance Provider by Professional Adviser magazine, and Best Service Provider at the Lifesearch Protection awards in February.

April heralded the Financial Adviser Life & Pensions Awards where we won Life Assurance Provider of the Year, Protection Provider of the Year and Term Assurance Provider of the Year. On to September and the Moneyfacts Investment, Life & Pensions Awards, where Legal & General won awards for Best Protection Service and Most Competitive Term Assurance IFA Provider.

In October, Legal & General won Protection Provider of the Year from Bankhall Financial Services and in November Best Mortgage Related Insurance Provider from "Your Mortgage". The final awards of the year were first place for Term Assurance and first place for Critical Illness at the Financial Adviser Service Awards.

Best

Life Assurance Adviser

sets us apart

Fast track underwriting academy

Legal & General's medical underwriting team is the largest in Europe, and is continuing to expand and develop through the Company's partnership with Cardiff University. The University now offers an Underwriting Academy tailored to meet the needs of the company. This has allowed Legal & General to create a fast track course to train new underwriters and expand the skills and knowledge of its existing underwriters and medical claims specialists. Courses were designed with input from Professor Mansel Aylward CB, Chief Medical Adviser, Medical Director and Chief Scientist to the Department for Work and Pensions, and enable Legal & General specialists to interface with teams of eminent clinicians and academics.

3m

Annuitant years of experience

Annuities – mortality data

Legal & General's expertise in pricing annuities is driven by our in-depth understanding of mortality trends and rates. We have over 3,000,000 annuitant years of experience, and arrive at a highly informed understanding of mortality based on analysis of over twenty variables.

The result is accurate, differential pricing of annuities which reflects street-by-street differences in life expectancy. Proof of our dedication to detail.

market activity, which has relevance to our protection business, to remain robust though interest rate changes may lead to some caution. Given that it is estimated only 11% of the private sector workforce is now covered by employer defined-benefit pension schemes, we see further capacity for growth in personal long term saving and pension provision.

In the annuities sector, we have seen some increased competition in bulk annuities from new entrants. We expect this trend to continue, especially for larger transactions, but we note that the potentially very large Bulk Purchase Annuity (BPA) market for open schemes remains untapped. Increasing longevity, in our opinion, creates a competitive advantage for companies like ourselves with a strong administrative and risk management skillset.

As in 2006, we believe distribution and in particular platform technologies will continue to be an important factor in our markets, and we are strengthening our position in these areas. The overall strength of the long term savings market, and further efforts by companies to reduce pension fund deficits, have the capacity to drive further growth in the institutional fund management sector. While the market will remain competitive, the flexibility inherent in our product and distribution mix enables us to pursue growth profitably.

Protection and Annuities

Protection
Protection and annuities represents 23% of Legal & General's UK new business APE – we are market leaders in individual protection with over 20% market share. This is a business built on protecting individuals and their families. Around a quarter of our total protection business comes from corporate clients who seek protection for their employees.

Key strengths
Our scale in this market supports clear competitive advantages:

Underwriting expertise
Legal & General has the largest team of life underwriters in Europe. Their expertise is at the core of our success – providing confidence in our pricing decisions. In 2006 we invested further in our capability, by opening a dedicated underwriting office in Edinburgh – attracting a high-calibre team of specialists from the local market.

The power of numbers
Legal & General underwrote over 50,000 policies each month last year. We have a database of over 12m customer years of experience. Every time we write a policy, this volume of data means that we can do so quickly, efficiently and with confidence in the price that we set for each individual.

Administrative focus
Each time a customer or intermediary comes to Legal & General for protection, we believe it is essential to make sure their experience is a good one. This means making sure our systems are robust, that our processes are efficient. We have invested significantly in technology and believe we remain market leading.

Distribution
Our distribution reach in protection is another great strength. We work with a range of high quality bank, building society and other tied agency brands – delivering a strong and dependable flow of new business. This core segment of our distribution underpins our continued investment in product and administration systems and processes. We own the systems used by the largest controlled mortgage adviser network in the UK, which along with advising on over £20bn of mortgage business 2006, also sells Legal & General's insurance products. IFAs too are an important distribution channel for us, as they are for many products in our industry. The wide variety of channels to market gives insight into customer buying trends, market pricing and the needs of our distribution partners.

Margin
Protection has historically been, and remains, one of our higher margin products, and so is a key driver of our return on embedded value and EEV operating profit. This reflects our scale and efficiency and the strength of our risk pricing and control mechanisms. Pricing remains competitive in the protection market, especially through the IFA segment. However the competitive advantages that we have built, along with our market leading systems, products and distribution support our confidence in our ability to continue to build this business, profitable.

Annuities – individual
When individuals reach retirement age, many choose to secure their income in retirement immediately, and most are required to do so by the age of 75. For many personal pension savers, this means using the proceeds of their accumulated savings to purchase an annuity from a life company. This annuity will promise a certain level of income – flat rate or indexed – for the rest of the individual's life. In addition, the benefits may include income for dependants, further into the future.

In 2006, individual annuity sales accounted for 4% of our UK new business APE. Our strategy in this highly price-driven market is centred on strict pricing discipline, requiring

that our target rates of return are met. This firm stance on pricing led to a lower market share in 2006 than might otherwise have been the case, given a heightened level of competitor activity in the first half of the year. Prices in the market were inadequate to meet our return requirements, and so we were comfortable to see our sales reduce. Our competitive position improved strongly in the latter part of the year, and sales recovered strongly. This long term, profit driven stance means that Legal & General sells good volumes of business, at good prices, without short term volume-driven risks to shareholder returns.

This highly disciplined approach is reinforced by our understanding of risk – we have a huge database of individual lives, over 3 million annuitant years of experience, giving us confidence in our pricing decisions and underpinning our long term profitable position in this market.

Annuities – Bulk Purchase

In 2006 we wrote over £1bn of single premium equivalent Bulk Purchase Annuity (BPA) business. BPAs represented 6% of our UK new business APE in 2006. BPAs are policies that allow company pension schemes to insure some or all of the retirement income their members expect in large block transactions. These schemes can range from a few lives in a small company, to very large policies. In each case, it is important to recognise that we are insuring the financial security of individual workers and pensioners, who will depend on Legal & General for their retirement income.

Key strengths

We have a number of key competitive advantages in this market.

- Exceptional experience and expertise. Last year was the 20th anniversary of our BPA business. Our customers and their advisers can see that we remain firmly committed to this market, and can see the reliability of our administrative infrastructure, and our financial strength.
- Reputation. Working with pension trustees, and insuring the income of a large number of pensioners and employees requires the trust of our clients. Our customers are relying on us to fulfil their promises to their members, and we take that responsibility very seriously.
- Scale. As a long established participant in the annuities markets, Legal & General has a market share in Individual and Bulk Purchase Annuities of 15%.

20%

Market Share (Individual Protection)

Fig 5. Life and Pensions – IFRS Operating Profit

Year ended 31 December	**2006 £m**	2005 £m
UK operating profit:		
Distribution relating to non profit and shareholder net worth	**388**	312
Subordinated debt interest	**34**	37
With-profits business	**95**	66
	517	415
USA	**58**	52
Netherlands	**7**	18
France	**10**	4
Operating profit	**592**	489

5.75m

Customers worldwide

Margin

Annuities are the highest margin business category for Legal & General on the EEV basis and are therefore a key driver of operating profit and return on embedded value. This reflects the extent of the risks that we are taking onto the balance sheet, and our assessment of the period of time over which those liabilities remain in force. The headline margin we report will depend on the mix of business between lower margin individual business and higher margin bulk annuity business. However, margins consistently reflect our determination to meet our target rates of return on capital.

Our ability to meet these rates of return is sensitive to a number of key factors:

- The competitive environment – we do not pursue irrational pricing to achieve volumes.
- Our investment expertise, including the ability to source attractive yields in the fixed interest market.
- Ongoing trends in longevity, and how this must be factored into our pricing.

Risk expertise

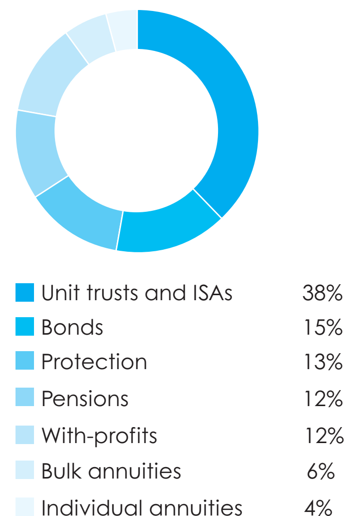
At their core, annuity and protection businesses are based on a statistical framework – the assessment of risk, setting a price for that risk, and continually analysing the developments in those risks.

The size of our database of annuitant lives and insured lives means that our underwriting of risk businesses is informed by statistically credible data. This means that we can aim to identify those segments of business where we can be more competitive than others, while remaining profitable. It also means that we can avoid taking on business that offers inadequate returns.

We have continued to invest in and build these businesses with the support of a very highly skilled team of specialists who understand the risks that we are underwriting, and how to price for them.

A further consequence of the risks inherent in annuities and protection is that significant capital must be dedicated to them. Our financial strength is clearly important in this respect. We believe the diversity of our risk businesses – group risk, individual protection, individual annuities and bulk annuities – allows us to allocate capital more efficiently, pursuing those categories of business where returns are most attractive. A less diversified risk business would, we believe, be significantly disadvantaged in this respect.

Fig 6. UK New Business Split APE for 2006



Unit trusts and ISAs	38%
Bonds	15%
Protection	13%
Pensions	12%
With-profits	12%
Bulk annuities	6%
Individual annuities	4%

Growth

We move and adapt with economic, demographic and market changes, and are positioned to grow in a growing market.

Kate Avery
Group Executive Director (Wealth Management)

...that deliver

Record LGIM Funds under Management

2006 saw record new business for Legal & General Investment Management (LGIM) with gross new inflows of £20.7bn, an increase of 21% over 2005. New business inflows continue to be dominated by flows from corporate pension schemes, which accounted for £18.5bn. New business from charities and other institutions enjoyed another excellent year with inflows of £2bn.

Existing clients contributed £10.4bn (2005: £8.8bn) of the total.

Growth in new business combined with excellent client retention levels and strong markets drove funds under management up to £233bn – up 14% from the start of the year.

rs value

Chelsea Financial Services

“One of our biggest growth sectors this year was unit linked bonds. We recommend Legal & General’s Portfolio Bond because it offers our customers a large choice of external funds backed by Legal & General’s brand, which stands for value for money and great service.”

Matthew Woodbridge,
Bond Manager at Chelsea Financial Services

New investment model for the 21st century

Cofunds has over £11bn of clients’ assets under administration and is currently the biggest platform provider in the UK market on this basis. Cofunds customers now have access to Legal & General life products, and to one of the widest choices of investment managers’ funds. IFAs now have both on platform and off platform ways of trading with their clients.

Legal & General’s Tied salesforce, circa 350 wealth advisors, have adopted a version of Cofunds Platform Technology through the deployment of the ‘Investor Portfolio Service’ from October 2006 in their Wealth advice branch network.

Over

£11bn

of clients’ assets under administration

Wealth Management

65% of our UK new business APE was generated through savings products in our Wealth Management division in 2006.

Our savings business encompasses a spectrum of products which allow customers to accumulate assets over a period of time on a cost effective basis. This ranges from more liquid investments such as unit trusts and ISAs, all the way through to very long term structured saving for retirement through pension products.

At the core of each of these products, however, is a series of unitised investment funds, allowing access to different investment styles and asset classes. The choice of product through which these are accessed then dictates the tax basis of the investment, the timescale over which the assets are likely to be held, and the eventual benefits that are withdrawn. Access to the best investment returns, at the most cost-effective price, with excellent administration and customer service are key to success in this business.

There are three major categories of investment business – pensions, investment bonds and retail investments.

Pensions

12% of our UK new business APE was represented by non profit pensions in 2006, representing an estimated market share of 6%. A pension contract allows a customer to invest for a very long time, perhaps as long as forty-five years, in order to accumulate sufficient assets to secure an income in retirement. Pensions attract some tax advantages, including limited deductibility of contributions, but require that assets remain invested until late in life. Contributions into pension contracts can either be regular or single premium.

Investment bonds

Bonds represented 15% of our UK new business APE in 2006, a market share of 9%. Bonds are normally single premium investment contracts, which combine asset accumulation with protection. There are tax benefits to qualifying investment bonds, such as tax-advantaged withdrawal of income, however, bonds must be held for a minimum period to qualify.

Retail investments

Retail investments accounted for 38% of UK new business APE in 2006, a market share of 4.3%. These are unitised investment contracts, like bonds and pensions, but are not insurance contracts. As a result they can be bought and then sold as soon as customers require their funds. A limited amount of money can currently be invested each year in a tax-advantaged ISA.

Distribution trends

We believe the distribution landscape for savings is changing. Recognising that the core of all savings products – unitised funds – is the same, the delineation between products is, we believe, less and less significant. At the same time customers and advisors are increasingly sophisticated, appreciating flexibility in investment as well as good service.

As a result, open architecture ‘platforms’ are a growing force in this market. They offer customers access to a wide variety of funds, not just those of the insurance company. They can also allocate these unit fund investments to a number of different product ‘wrappers’. As a result, customers will no longer need to consider different pools of savings in different companies’ bond, pension or retail investment contracts. Instead, they can consolidate all their long term savings, under one overall investment policy, with a number of different product ‘wrappers’, all in one place.

This is a powerful proposition for customers and their advisers, whether IFAs, or other distribution partners. Legal & General took an early and leading position through our investment in, and alliance with, Cofunds, a leading platform business with an established reputation with intermediaries. We have also built a platform using Cofunds architecture which is now available to our banking and building society partners – reinforcing our product offering, as well as increasing the market to which our savings business has access.

IFAs and other advisors can also access Legal & General’s savings products ‘off-platform’, and we continue to write significant volumes of business this way.

We also distribute retail investment products directly over the telephone and internet.

Margins

Savings contracts normally expose shareholders to relatively low investment risk, since customers’ benefits are normally linked directly to the performance of the underlying assets. As a result, the risk to shareholders’ funds in savings business is relatively lower than it is for risk businesses. This means that margins for pensions and investment bonds have generally been lower in the savings business, albeit achieving attractive returns.

For all savings businesses, a key driver of returns is persistency. In order to achieve our target margins, business needs to stay on our books for a certain amount of time. Persistency in pensions has been an industry-wide issue for many years, particularly where contributions have been made on a regular premium basis.

In pensions we have reported small negative margins in 2005 and 2006. This reflects the difficulty of achieving appropriate returns on capital in an industry where legislative price limits have been imposed in some areas. Pensions also account for around a half of all industry sales, and competition is always strong. This challenging environment has led Legal & General deliberately to focus on those segments of the pension market

where profitability is better. In particular we have seen progress in 2006 on high-quality corporate pension schemes, transfer business and early signs of success with our SIPP, launched in April 2006. As we continue to build the business, focused on more profitable lines, we aim to improve margins to more acceptable levels.

Bond business, which does not have any charge limits imposed upon it, reports a positive margin, reflecting our scale in this market, and the attractive economies of large single premium arrangements. This is a product market which remains attractive to many industry participants. Our scale and efficiency, as well as the attractions of purchasing bonds on the Cofunds platform mean we expect to remain profitable while still building our business in a competitive market.

Key strengths

Different advisory channels can choose to put business with a large number of insurance or investment companies. In order to continue to succeed, we recognise a number of key issues:

• Administrative capability

In order to attract savers to place large amounts of money with Legal & General, we need to ensure that our processes are efficient.

• Customer service

Savings customers are likely to come into regular contact with Legal & General. Requesting statements, increasing their investment, fund changes or surrenders all require significant administration.
We continue to refine our administrative infrastructure to improve our customers' experience of saving with Legal & General.

• Access to excellent investment funds

Our investment management business, LGIM, offers customers access to a number of very strong investment pools, including market leading index-tracking, active equity, fixed income and property funds. Through our platform model, customers can access over 800 competing funds, should they require a wider choice.

Capital discipline

We allocate significant capital to the savings business. However, the relatively low risk to shareholders from investment volatility makes this a less capital-intensive business than protection and annuities. Nevertheless for each individual contract, the early-year expenses can be significant, and can only be paid back if the business remains with Legal & General for sufficient time. It is critical, therefore, that we monitor our pricing, competitive position and new business volumes to ensure that we are not at risk of attracting too much business with poor relative persistency, and that we are well positioned to pick up more attractive, higher persistency business.

Fig 7. Operating Profit from Continuing Operations[1] (£m)

Year	£m
2006	1,233
2005	1,092
2004	762
2003	756
2002	686

1. Achieved Profits basis 2002-2003, EEV basis 2004-2006

Fig 8. EPS[1] Based on Operating Profit After Tax[2] (p)

Year	p
2006	13.45
2005	12.02
2004	8.46
2003	8.49
2002	8.49

1. EPS – Earnings Per Share
2. Achieved Profits basis 2002-2003, EEV basis 2004-2006

With-Profits

46%

Increase in UK new business APE (2006)

Legal & General's with-profits business accounted for 11% of our UK new business APE in 2006. Business written to the with-profits part of Society's long term fund comprises:

- participating business where beneficiaries receive bonuses as a direct participation in surplus profits. This is now predominantly with-profits bonds business.
- non-participating business where a with-profits investment option exists. This is largely pension business.

The significance of participating business has fallen across the industry in recent years. With a fund of over £30bn, expertise in the management of the with-profits business is very important for Legal & General. In 2006, our with-profits fund achieved a further year of strong performance, with assets backing with-profits participating policies generating an 11.2% return gross of tax and investment charges and paying £596m in with-profits bonuses to customers. Its five year return of 55% has exceeded the FTSE All-Share and the FTSE 100 indices.

There are a number of key success factors:

- Financial strength. The strength of our funds allowed Legal & General to continue to invest for the long term, retaining significant exposure to equities through the bear market. Policyholders are now benefiting from this strength. The overall asset mix applicable to with-profits policies eligible for bonuses at the end of 2006 consisted of 40% UK shares, 11% overseas shares, 29% fixed interest securities and 20% commercial property.
- Asset liability management. There are many different policy types within the funds. A detailed understanding of the guarantees that we offer, as well as the aim of longer term returns on investment, allows us to balance the expectations of our policyholders with minimising risk to shareholders.

Fig 9. Worldwide Operating Profit Before Tax – EEV basis

Year ended 31 December	**2006 £m**	2005 £m
Life and pensions	**1,030**	901
Investment management	**181**	136
General insurance	**9**	14
Other operational income	**13**	41
Operating profit from continuing operations	**1,233**	1,092

Fig 10. Worldwide Operating Profit Before Tax – IFRS basis

Year ended 31 December	**2006 £m**	2005 £m
Life and pensions	**592**	489
Investment management	**133**	103
General insurance	**9**	14
Other operational income	**18**	41
Operating profit from continuing operations	**752**	647

Balance

Our scale and capability across a broad, balanced product range enables us to reach an increasingly large and diverse customer base.

Robin Phipps
Group Executive Director (UK)

...through brea

Work life balance – Runners at Hove

Legal & General runners from Hove office enjoy a seafront outing. From an informal Monday evening running club a number of attendees have gone on to tackle five and ten kilometre and half marathon races – some have set their sights on the Flora London marathon this year. The Company supports track work at nearby Withdean Stadium to enable practice to continue when nights draw in.

dth and depth

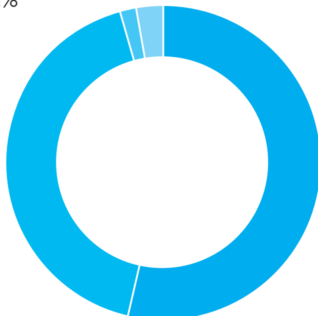
Strategic Distribution Agreement with Nationwide

In February 2007, Legal & General entered a strategic distribution agreement with Nationwide, Britain's largest building society. Nationwide is represented in over 860 locations and has a financial relationship with one in four households in the UK. Under the agreement, Legal & General products will be sold through the Nationwide's 2,000 strong team of advisers and consultants.

With the Nationwide, Legal & General now has business partnerships with over twenty retail financial institutions, with a total of around 45 million customers, across the country.

Wealth Distribution Split

- IFA 53%
- Banks 42%
- Tied Agents 2%
- Direct 3%



Distribution

One of Legal & General's great strengths over recent years has been our multi-channel approach to distribution. We work closely with a wide range of distribution partners in the UK including IFAs, employee benefit consultants, stockbrokers, mortgage brokers, high street banks and building societies.

We provide each with the products and service which meets the unique needs of their customers. We also deal direct with customers who want to trade over the phone or, increasingly, online. Our expertise in balancing the different needs of each of these distribution channels is one of the reasons why Legal & General continues to succeed in today's highly competitive market.

International

Legal & General's overseas life and pension businesses generated £156m in operating profits in 2006. This represented an increase of £56m over the prior year. The three principal overseas businesses are in the United States, the Netherlands and France. Each business focuses on selected lines of business. These respective business lines are protection contracts for high net worth customers in the United States, individual savings and protection products in the Netherlands, and single premium savings and group protection products in France.

During 2006, overseas results benefited from a combination of increasing new business contributions in the Netherlands, favourable persistency in savings and unit linked products in France and the Netherlands, and the positive effect of our Triple X securitisation which improved balance sheet efficiency in the United States.

Legal & General's strategy is to grow existing overseas operations profitably as part of a portfolio approach to its international operations. Investment overseas has to satisfy internal criteria, and our overseas businesses also complement our core competencies in our home market and our established business values. The Company periodically examines new opportunities in overseas markets to identify potential opportunities to build value.

Fig 11. 2006 Product Margin Analysis – EEV basis

Year ended 31 December 2006	Contribution[1] £m	PVNBP[2] £m	Margin %
Protection	131	1,201	10.9
Annuities	191	1,735	11.0
Savings			
– Unit linked bonds	51	2,612	2.0
– Pensions – Stakeholder and other non profit	(10)	1,326	(0.7)
With-profits	17	1,232	1.4
Total	380	8,106	4.7

Fig 12. 2005 Product Margin Analysis – EEV basis

Year ended 31 December 2005	Contribution[1] £m	PVNBP[2] £m	Margin %
Protection	82	1,051	7.8
Annuities	177	1,539	11.5
Savings			
– Unit linked bonds	49	2,082	2.3
– Pensions – Stakeholder and other non profit	(18)	935	(1.9)
With-profits	16	1,014	1.6
Total	306	6,621	4.6

1. Contribution from New Business
2. Present Value of New Business Premiums

£156m

Operating profit in international life and pensions

Legal & General Investment Management

Investment Management
With £233bn under management, Legal & General's Investment management business, LGIM, is one of the UK's largest asset managers. LGIM manages both institutional and retail funds. These include assets managed for corporate pension funds and other investing institutions as well as Legal & General's own funds.

LGIM's strength in its core index tracking investment product makes it the UK's passive investment market leader, both in terms of size and quality and demonstrated by survey evidence. LGIM continues to be market leaders in the management of UK Defined Contribution pension assets with over £10bn Defined Contribution pension assets at the end of 2006.

Growth and Profitability
In 2006, LGIM had another year of record-breaking gross new business inflows of £20.7bn, an increase of 21% on 2005. In addition, favourable persistency rates and rising markets have contributed to a 14% increase in funds under management to £233bn. The major part of the total gross new business of almost £21bn is from Corporate Pension clients, and over half of it from existing clients. In addition to its strength in index fund management, LGIM grew its active management business in 2006, winning £800m of Structured Solutions new business.

£233bn
Funds under management

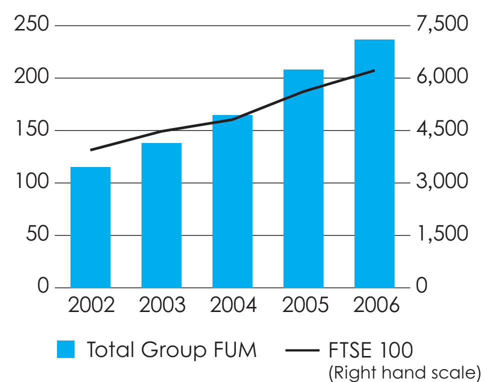
LGIM's operating profits for 2006 were £133m on the IFRS basis, an increase of 29% on 2005.

Strategy
LGIM's strategy is to continue enhancing its core investment product offerings, which are highly scalable. At the same time we plan to build LGIM's presence in the higher risk investment products ('high-alpha') end of the market. To support the delivery of this strategy we have been successfully investing in people across our business.

In line with our strategy to develop a Global Fixed Income capability, our US office was established in Chicago during 2006. The new subsidiary, LGIM America, will provide US fixed income expertise to complement and augment LGIM's UK based fixed income skills.

LGIM's Structured Solutions Team was strengthened during the year and significant progress was made in promoting our Structured Solutions capabilities in the corporate pensions market. LGIM is generally recognised as being one of the leaders in the field of Liability Driven Investments (LDI).

Fig 13. Growth of Funds under Management (FUM) (£bn)



A commitment to transparency

Financial Reporting Overview

Legal & General, in common with other European listed life assurers, reports financial information to shareholders under two complementary reporting bases.

The primary financial statements, which are found on pages 55 to 116 of this report, are prepared on the International Financial Reporting Standards (IFRS) basis. This basis is the one that all EU listed companies are required to follow. We believe this gives an insight into the Company's ability to generate cash flows to support dividends.

For companies which write long term insurance contracts, the emphasis of the IFRS basis on movements in a single year gives an incomplete assessment of performance as it does not provide information on the value created over the life of the contracts. Legal & General therefore provides supplementary financial statements on pages 117 to 133 which are prepared on the European Embedded Value (EEV) basis. Those statements provide an assessment of the value that has been generated by the business during a financial year.

In our Operating and Financial Review we focus on operating profit on the EEV basis which we believe provides shareholders with a better understanding of the Group's performance. Operating profit reports the change in embedded value in a financial year, but excludes fluctuations from assumed longer term investment returns.

The key differences between the EEV and IFRS bases are set out in Figure 14.

Financial Reporting Developments

Legal & General adopted the IFRS basis of reporting for its primary financial statements in 2005. In 2006, the International Accounting Standards Board (IASB) announced a period of stability in financial reporting. As a result of this, no major new standards, or changes to existing standards will become effective until 1 January 2009. Therefore, it is currently anticipated that few significant changes will be required to the Group's

Fig 14. Key differences between the EEV and IFRS bases

The total profit arising from a long term insurance contract over its entire life will be the same under both the EEV and IFRS bases of reporting. The main difference between the two bases is in respect of the timing of profit recognition. A description of when the profits are recognised for each basis is given in the table to the right.

EEV	IFRS
EEV seeks to recognise, at the point new business is written, the inherent value to shareholders of that business over its entire lifetime. This is achieved by projecting future shareholder cash flows arising from new business using best estimate assumptions and then discounting those cash flows using an appropriate risk discount rate.	IFRS does not recognise, in the year of sale, profits expected to arise on the contract in future years. Instead it recognises only the profit or loss arising on new business in the year it is written. Despite IFRS allowing some acquisition costs to be deferred, most product lines will incur a loss in the year business is first written, reflecting the initial cost and reserving "strain" of writing long term business.
EEV profit arising on in-force business represents the unwind of the risk discount rate, reflecting the fact that future cash flows projected are one year nearer to realisation, together with the impact of actual experience varying from previous best estimate assumptions used to determine projections.	Under IFRS, the loss recognised in the first year of writing new business due to the typical expense strains in acquiring it will be offset by the profits emerging in future years over the lifetime of the business.

Strength

Our business is underpinned by the strength of our finances and our human capital. This assures customers we will be there when they need us.

Andrew Palmer
Group Director (Finance)

...to build a se

Partnership with Amicus

This year Legal & General celebrates ten years of working in partnership with our Union, Amicus. Over 35% of our employees are Amicus members, and the Union is represented by three full-time secondees and around 40 part-time reps. Despite changes at Amicus over the last ten years, partnership working at Legal & General has been remarkably constant.

The Partnership Agreement recognises management's right and duty to manage, and Amicus' right to represent its members across a range of issues. Within a framework of mutual confidence and trust, the Agreement encourages workplace flexibility, fairness and equality in the treatment of employees. This includes transparent pay systems, contractual provisions which encourage equal treatment regardless of background or personal circumstances and access to good vocational training and development.

+35%

of employees are members of Amicus

ecure future

Systems Strength

Legal & General's IT Services use over 600 Windows, Unix and mainframe servers to support and deliver over 100 different IT functions: from the customer facing 'e' or internet services through to internal development services. A 24/7 support infrastructure ensures integrity is maintained at all times. All Legal & General's business data is stored on disk and critical business data is mirrored at its disaster recovery site at Hounslow. Over 700 terabytes of data is stored at both sites.

20%

Market leaders in our chosen sector

Market share in life

The strength of the Protection business arises from having market leading positions in all the key areas. We have access to the widest range of distribution and offer the best value products. Our service is industry leading and our technology continues to deliver even greater benefits for advisors. Our success has led to market leading scale, which in turn enables further investment to improve our business.

Fig 15. Balanced scorecard for capital management

	2006	Target operating range
IGD surplus capital *	£2.1bn	£1-2bn
Society surplus capital *	£4.9bn	£2.5-3.5bn
Economic capital	Very strong AA	Strong AA
Return on EV	12.5%	Increase over medium term

* Figures extracted from the draft regulatory returns

consolidated financial statements over the next two years.

The IASB continues to develop the accounting for insurance contracts. It is expected that an exposure draft will be released in 2008 followed by a final standard in 2009. We continue to monitor these developments closely and to contribute fully to the debate.

In 2005, Legal & General also adopted the European Chief Financial Officer (CFO) Forum's EEV methodology to prepare its supplementary financial statements. We anticipate that EEV methodology will continue to evolve during 2007, improving further the consistency of company disclosures. In particular, we anticipate that the CFO Forum will work to harmonise the disclosure framework for Market Consistent Embedded Value (MCEV) reporting. The MCEV methodology builds upon existing market-consistent valuation techniques and has been used by some European insurers in their adoption of EEV. When a stable framework of guidance exists, we will consider moving to a market-consistent methodology for our supplementary financial statements. As an active member of the CFO Forum, we expect to contribute fully to these developments.

Group Capital

Capital management

Legal & General has developed a balanced scorecard for capital management which can be seen in Figure 15, including 2006 values and target operating ranges. Our aim in developing the scorecard has been to help demonstrate how we manage capital and to provide a transparent framework for shareholders.

We use four inter-related measures for capital. The first two measures, the Insurance Groups Directive (IGD) surplus capital and the regulatory surplus capital for Legal & General Assurance Society Limited (Society) are key measures of financial strength for our regulator, the FSA. The Economic Capital measure reflects our aim to run the business to a strong AA financial strength rating. The fourth measure is Return on Embedded Value (RoEV) as we believe it is appropriate to include a performance metric in our capital balanced scorecard. This measure ensures that there is a healthy tension between quantum of capital and the return earned on that capital.

We anticipate that the scorecard will evolve over time as industry performance measures evolve and we develop our Economic Capital model.

Fig 16. Group Capital Review

2006
- Pensions and annuity company

2007
- Investment policy for with-profits business
- Investment policy for shareholders' funds
- Investment management contract
- Ongoing funding of pension fund

2007/2008
- Society capital structure
- Society transfer formula

External uncertainties
- HMRC consultation
- Regulatory approvals

Capital structure

During 2006, we initiated a wide ranging review of the Group's capital. An early conclusion was that although our current structure has proved very efficient over the last decade, we believe that we are able to enhance it to take account of the way our business model has developed and recent changes in the external environment.

It is essential to have a robust and stable capital structure, and any new structure needs to be capable of supporting our successful growing business for a number of years. In addition, we are seeking a clearer, more transparent structure, which will ultimately benefit shareholders.

The most significant areas being considered by the review and the high level timeline for implementation are set out in Figure 16. Some of these will deliver quickly, while others, such as the review of corporate capital structure, will take longer as there are more external dependencies and uncertainties. The most significant uncertainty is the outcome of the ongoing Her Majesty's Revenue & Customs (HMRC) consultation on the taxation of life companies and certainty is not expected in this area before the start of 2008.

The first change has already been made with the establishment of a new pensions and annuity reinsurance company called Legal & General Pensions Limited (LGP). On 31 December 2006, the pensions and annuity business of Society was ceded to LGP. The creation of a separate company provides greater capital transparency and flexibility, and will enhance Legal & General's ability to compete in the annuity and pensions markets. The structure will ensure that both non profit life and pensions business are taxed appropriately.

Further detail of the financial impact of this change is provided in the Operating and Financial Review on page 9.

Capital resources

The Group is required to measure and monitor its capital resources on a regulatory basis and to comply with the minimum capital requirements of regulators in each territory in which we operate. The regulators require more prudent assumptions than IFRS. Legal & General's total capital resources are substantially in excess of both total regulatory capital and the minimum level of regulatory capital we are required to hold.

Figure 17 compares the Group's available capital resources with the capital resources requirement for Legal & General Group Plc and Society.

Figure 18 shows the Group's structure. Total capital resources of £8.4bn on an IFRS basis comprise ordinary equity holders' capital (£5.4bn), subordinated debt (£0.8bn) and unallocated divisible surplus (£2.2bn, including £0.3bn of Sub-fund).

The largest allocation of capital has been made to Society, reflecting the significance of this operation and the importance of ensuring its financial strength to support long term growth of our business. Financial flexibility is achieved from Society's £5.5bn of shareholder capital. Of this total, £2.2bn is held outside any long term fund as Society Shareholder Capital (SSC), of which approximately £1bn is within LGP; the remainder of £3.3bn is held within Society's Long Term Fund as Shareholder Retained Capital. These assets maintain the financial strength of Society and fund new business growth.

Society continues to be one of the two highest rated European life insurers. As at March 2007, our financial strength ratings from Standard & Poor's, Moody's and A.M. Best were maintained at AA+, Aa1 and A+ respectively. All ratings have a stable outlook.

Fig 17. Regulatory Capital Surplus

As at 31 December 2006	Group[1] £bn	Society[1,2] £bn
Available capital resources	6.7	9.3
Capital resources requirement	4.6	4.4
Excess	2.1	4.9

1. Figures extracted from draft regulatory returns
2. Long term business only

The Group's Capital Position Statement prepared on the FRS 27 'Life Assurance' basis is included within Note 50 on page 103. This demonstrates the different sources of capital held within the Group.

Individual Capital Assessment (ICA)

The Financial Services Authority (FSA) requires insurers to hold capital on the greater of two bases. The first basis (Pillar 1) encompasses the rules-based regulatory capital requirements in the FSA's Prudential Source Book, including the with-profits realistic balance sheet. The second basis (Pillar 2) is the firm's own internal assessment of its capital requirements, together with any additional amount which may be required by the FSA.

During 2006, the FSA completed its first review of the Group's assessment of its Pillar 2 capital requirements.

Solvency II

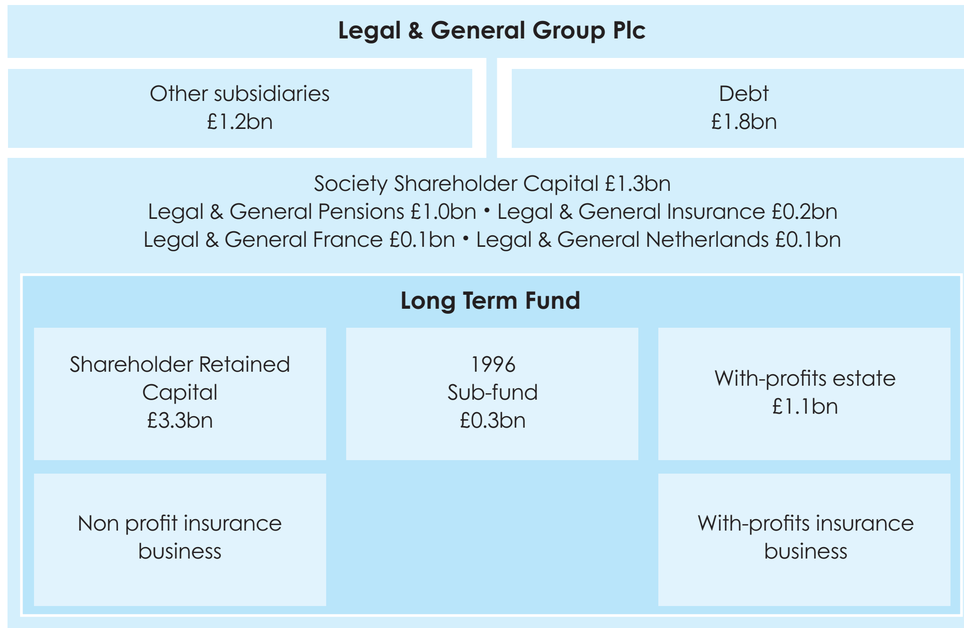
During 2006, the European Commission and its advisors have continued work on revised capital and solvency standards for EU insurers under the Solvency II project. It is expected that a draft EU directive will be laid before the European parliament in 2007.

Legal & General participates actively in the consultation process through the Association of British Insurers (ABI) and its links with the FSA and Government. The Group endorses the approach taken by FSA to ensure that Solvency II benefits from the experience of the FSA's implementation of ICA for UK insurers.

Group Cash Flows

In recent years, Society and LGIM have been the Group's main sources of subsidiary

Fig 18. Group Structure
As at December 2006



dividends. These amounts have been supplemented by regular, small dividends from the Netherlands and a series of one-off dividends from our General Insurance business. Society remains the largest source of dividends, with contributions from the non profit business and the with-profits business each year.

The Group dividend recommended to shareholders is determined by the directors after taking account of future capital requirements, our projections of future dividends from subsidiaries and current projected investment market conditions. The final dividend per share proposed for 2006 has been increased by 5% to 3.81p (2005: 3.63p) bringing the total dividend for the year up to 5.55p an increase of 5.1%.

Debt and Debt Facilities

Access to the capital markets is maintained through a £2bn Medium Term Note programme, which allows debt capital to be raised in both senior and subordinated form. The latter satisfies the FSA's criteria for upper tier II and lower tier II forms of capital for insurance companies. The Group also makes use of a US$2bn Commercial Paper programme, which facilitates access to both international and domestic money markets. Additionally, the Group has a £1bn five year revolving credit facility which matures in 2011. Together these facilities satisfy the Group's liquidity and working capital needs. At the end of 2006, we redeemed our £525m convertible bond at par, having thereby provided the Group with a very attractive low cost source of senior debt over the previous five years.

During 2006, Legal & General America completed a second securitisation for its term assurance business. This raised US$450m non recourse subordinated debt to finance Triple X reserve requirements on new business written in 2005 and 2006.

Total debt at the end of 2006 was £2.4bn (2005: £2.4bn) of which £0.6bn (2005: £0.4bn) was non recourse funding. £1.5bn (2005: £2.0bn) carries a fixed rate of interest. The weighted average cost of the Group's core borrowings during 2006 was 5.1% p.a. (2005: 5.3% p.a.).

The Group's current long term and short term debt ratings are, from Standard & Poor's, AA- and A1+ and, from Moody's, Al and P1.

Tax

Excluding the tax impact of corporate restructure and, in 2005, the effect of UK tax changes, the reported rate of tax on the EEV basis was 27% (2005: 27%). The principal reasons for the rate being slightly lower than the UK corporate tax rate of 30% were the lower rate of tax on the return on UK equities held in shareholder funds, and the fact that property income attributable to minority interests did not give rise to a tax charge.

Andrew Palmer
Group Director (Finance)

There is an ongoing process for identifying, evaluating and managing significant risks which is comprehensive and systematic.

Principal Risks and Uncertainties
A significant part of the Group's business involves the acceptance and management of risk. A detailed review of the Group's inherent exposures to market, credit, insurance, liquidity and operational risks, together with the framework for their management, is set out on page 38. An overview of the Group's risk management framework is given on page 38 as part of the review of Corporate Governance.

Whilst, at present, the Board considers that there are no immediate risks likely to have a significant impact on the short or long term value of the Group, principal risks and uncertainties may be categorised as follows:

- Legislation and Regulation
- Confidence in the UK Financial Services Sector
- Market and Economic conditions
- Mortality & Catastrophe risks
- Future Savings Market
- Resources

Legislation and Regulation
The financial services markets in which the Group operates are highly regulated, with regulation defining the overall framework for the design, marketing and distribution of products; the acceptance and administration of business; and the prudential capital that regulated companies should hold.

Governmental fiscal policy may also influence the design of products distributed by the Group and the mechanisms for reserving for future liabilities. Additionally, there is a growing international dimension and the volume of regulatory and legislative change is increasing. Principal risks and uncertainties impacting this year have been described in Note 51 on pages 106 to 116.

The Group's activities and strategies are based upon prevailing legislation and regulation, with continuous monitoring to ensure that the Group meets its regulatory obligations. The potential for change is continuously identified and analysed. Sudden, unanticipated changes in legislation, and the differing interpretation and application of regulation over time, may have a detrimental effect on the Group's strategy and profitability.

Confidence in the UK Financial Services Sector
The Group has followed a strategy of offering value-for-money products to its customers and continually improving customers' overall experience of doing business with Legal & General. Whilst this enables the Group to differentiate itself from its competitors, earnings and profitability are also influenced by the confidence of the retail investor in the financial services sector as a whole, a number of drivers of which are beyond the Group's control. Such factors include the adverse performance of investment markets, actions by regulators within the sector and shock events such as significant market failures.

Market and Economic Conditions
Legal & General is a significant provider of term assurance and critical illness products. These products are typically purchased as part of the house buying event or when a property is being re-mortgaged. The Group also provides household and buildings insurance. Whilst the Group is structured to enable resources to be re-directed at other product lines, a downturn in the housing market could impact product volumes and short term earnings.

Legal & General is also a leading provider of index-tracking funds to both pension schemes and retail customers. The fees for managing these funds are directly linked to the value of funds under management. As such, significant falls in the value of tracker funds would impact earnings for these businesses.

Mortality and Catastrophe Risks
The Group writes significant levels of immediate and deferred annuity business. The Group uses its pricing capability for longevity risks to ensure that an appropriate risk premium is applied to the business, taking account of all known risk factors. However, significant unforeseen medical advances may result in the requirement to increase reserves for these lines of business. With regard to the Group's significant portfolio of protection business, whilst the risk of adverse claims experience is fully assessed and reserved for, an event causing widespread mortality or morbidity, coupled with a re-insurer default, may impact the capital available to the Group.

Future Savings Market
A number of Legal & General's businesses are focused on the long terms savings and retirement product markets. The factors leading customers to save and to provide for old age are influenced by a number of factors including government policy, social conditions and the general economic environment. The Group seeks to participate actively in debate to highlight those matters which are key to encouraging consumers to save and make adequate provision for old age. However, consumer uncertainty in any of the above factors may have a detrimental effect on these markets.

Resources
Legal & General has market leading expertise in a number of the fields in which it operates. The Group actively focuses on retaining the best personnel and ensuring that key dependencies do not arise through employee training & development programmes, remuneration strategies and succession planning. However, the sudden unanticipated loss of teams of expertise may, in the short term, impact certain segments of Legal & General's businesses.

Making a difference

Through its products and services Legal & General makes a significant and valuable contribution, not only to millions of individuals but to society as a whole. Our scale and the long term nature of our products, where customer relationships may last for decades, create a duty to behave responsibly and make sound decisions.

For Legal & General, Corporate Social Responsibility (CSR) involves the proper management of our relationships with customers, suppliers, shareholders and employees, along with the impact our business makes upon society and the environment. Adherence to strong CSR principles is not just part of good business, but essential to our long term success.

Customers

Our customers are central to our strategy. Legal & General currently supplies products or services to over five million customers. Our successful business model is founded upon providing them with good value products, quality service and a choice of ways to buy through a wide range of distribution channels. We support the Association of British Insurers' (ABI) Customer Experience initiative and we are committed to applying the principles of the Financial Services Authority's (FSA) Treating Customers Fairly initiative consistently throughout our business. Our approach goes beyond mere regulatory compliance. We know that it is important to our customers that Legal & General is a good corporate citizen. Research has indicated to us how our customers think we should behave and we know that they have growing expectations. We listen to them and seek to understand and respond to their concerns.

Employees

Investing in our 9,700 employees is another key element of our strategy. Our workforce

Customer Experience Programme

Employees, customers and advisers want to join us, stay with us and recommend us.

Launched in March 2005, this is the vision for our Customer Experience Programme, which we believe is making real progress towards delivering a positive experience for our customers.

Delivering a positive experience for our customers

Customers are at the heart of our business, and we continually strive to meet the demands and challenges of delivering the products they want and need in order to develop a strong, sustainable business. We are committed to working with the FSA and the ABI and we firmly believe that they both play a vital part in boosting consumer confidence in the long term savings and protection market.

Training our employees

Training and communication are vital. During 2006, over 5,000 frontline employees attended workshops to learn about their role in improving customer experience. Ideas in Action, our programme to encourage employees to give us their ideas on how service could be improved, generated more than 3,000 ideas, which contributed to our winning four trophies at the independent annual 'ideasUK' awards.

Our Birmingham office supports Help the Aged's HandyVan scheme in the local area.

Improving customer service

When things go wrong it is important to us that we put them right in a way which encourages customers to stay with us and recommend us. One of our customer experience projects has focused on improving how customers feel about us by delivering improvements to the way we look after our customers when they complain.

Customer Feedback

"I found the site very clear. It goes to what you want it to go to and you know what to do next. Some sites are very unclear and I just give up on them. That means they lose my custom."

The Customer Impact Scheme

In February 2006, we were the first company to sign up to the ABI's new Customer Impact Scheme. As part of the Scheme, our Group Board has signed up to three key commitments to ensure that the needs of the customer are at the core of our business:

- Developing and promoting products and services which meet the needs of customers
- Providing customers with clear information and good service when they buy products
- Maintaining appropriate and effective relationships with customers, providing them with a good service after they have bought a product.

Advisers

Our Business Partners are a very important link with our customers so we are delighted with their positive response to the improvements we have made in communicating with them more effectively.

is our most valuable asset, and we have implemented a wide range of policies to maximise opportunities for all employees. Our strong, open partnership with our union, Amicus, is a critical part of the Legal & General culture. Our employees have told us that they want to work for an ethical company which takes its responsibilities to society and the environment seriously. We regard responsible behaviour and good management of our Company's social and environmental impact as an important factor in being able to recruit and retain a talented and motivated workforce.

Investment

As one of the UK's leading institutional investors, with over £230bn under management on behalf of investors, policyholders and institutions, we have a unique opportunity – and responsibility – to exert a positive influence on the companies in which we invest. We expect companies in which we invest to adopt a responsible approach to social, environmental and ethical (SEE) issues. We support the ABI Disclosure Guidelines, which call on companies to disclose that the business and reputational risks arising from these areas are being assessed and managed, and we regularly discuss both SEE and governance issues with FTSE 350 companies.

With many of our pension fund clients showing interest in the influence we bring to bear on companies on SEE issues, being a responsible and active shareholder is an increasingly important element of our investment strategy.

Environment

Our sphere of responsibility also includes managing and minimising our direct impact on the environment, and we have a number of targets which support our efforts in this area. Current initiatives include working to reduce the proportion of office waste going to landfill, establishing staff recycling points for telephones and computers, and promoting

Corporate Social Responsibility cont.

car sharing, as well as ensuring that environmental factors are taken into account in the construction of new office buildings. With climate change moving higher up the public agenda a current priority is considering new strategies to further reduce our carbon dioxide emissions. In 2005, we switched to recycled photocopier paper across the Company, and in 2006 we extended this environmental commitment by switching to 55% recycled paper for all our marketing material. As a result of these moves, every year Legal & General expects to save approximately 11,000 trees and two million kilowatt hours of electricity.

Supply Chain
We purchase goods and services from over 3,000 suppliers. Suppliers make an important contribution to our business and we seek to establish mutually beneficial commercial relationships with them. We have a duty to treat suppliers in a fair and ethical manner, and we also seek to influence our suppliers to adopt responsible business practices. In 2006, for the first time, 100% of our key suppliers were compliant with our environmental requirements, and we expanded our assessment of suppliers to include social and ethical issues. Guidelines were also developed to influence key suppliers and support their supplier managers, which reflect Legal & General's CSR standards.

Communities
Supporting the communities in which we operate, and where our employees and customers live and work, is important to us. Strategic and effective community involvement is an integral part of our business activity, and our programme involves developing partnerships with both national charities and those which are local to our main offices. We also operate a range of schemes designed to support and encourage employees in their community involvement, including a payroll giving scheme and sponsorship matching scheme whereby the Company matches employees' fundraising for charity. We also run a Young Excellence Scheme through which we support young people who have shown exceptional sporting, musical or creative talent. During 2006, Legal & General's total community contribution exceeded £2.5m.

Governance
Legal & General's CSR Committee meets four times a year, and is responsible for developing the Company's strategy, overseeing its implementation and monitoring performance. It is chaired by our Group Chief Executive, Tim Breedon, and includes a representative from Amicus. The Group Board reviews the minutes of the Committee and conducts an annual review of the Committee, policy and programme. The Board also receives an annual presentation on the CSR programme and specific elements of our CSR programme are discussed as appropriate throughout the year.

The CSR Guiding Principles described in our CSR Report set the tone for the work

55%

we switched to 55% recycled paper for all our marketing material

Promoting cycling and other environmental travel options is a key aspect of our environmental programme.

Award winning year for Legal & General's website
Legal & General was the first company in the financial services sector, and the first FTSE 100 company, to achieve Accessibility Accreditation for its website from Shaw Trust.

The Guild of Accessible Web Designers also voted our website 'Accessible site of the Month' (financial sector) in January 2007.

Gareth Hoskin (right), Resources and International Director, signing the Amicus Equal Pay Charter with Andy Case from Amicus (left).

Changes at a glance

- Increasing accessibility to screen readers and search engines
- 'Contact Us' facility that means customers can navigate their way to whatever they want in just two clicks
- Removal of jargon
- Being crystal clear about what can and cannot be bought online
- Quicker and easier quotations and online applications
- Information customers really want made easier to find
- More efficient and faster.

Highlights of 2006

- We retained our membership of the FTSE4Good index series and the Dow Jones Sustainability World index, and we qualified for the Dow Jones Sustainability STOXX index for the first time.
- Amicus gained collective representation for first level management.
- We consulted with Amicus about the redundancy payment terms for staff grade employees, which resulted in improved terms for most staff grade employees.
- Legal & General signed the Amicus Equal Pay Charter to demonstrate our commitment to paying the same salary and bonus to employees doing the same job.
- We introduced Childcare Vouchers for our employees to enable them to take advantage of tax benefits.
- Following extensive promotion of our Give As You Earn scheme during the year nearly 12% of employees now donate regularly to charity via the scheme, enabling us to retain the Payroll Giving Gold Award for the second consecutive year.
- We switched to 55% recycled paper for all our marketing material.
- We successfully transferred employees in our Hove office to new premises, which incorporate a wide range of energy-saving features.

of the Committee and its members. With reference to these Principles, the CSR Committee undertakes an annual review of social, environmental and ethical risks and opportunities. Responsibility for this review, for assessing likelihood and impact, and for managing the risks and opportunities, is delegated to the relevant Committee member, their management team or the appropriate sub-committee. Targets are established where appropriate.

The CSR Report is verified by Legal & General Group Internal Audit. The verification statement detailing the scope of work carried out, and the conclusions reached, can be found at the end of the 2006 CSR Report.

Feedback on Legal & General's CSR performance is obtained through stakeholder engagement and external rating agency surveys.

In summary, we recognise that CSR is a 'need to have' rather than a 'nice to have', and that responsible behaviour brings value to our business. Key challenges for 2007 include exploring how we can embed responsible behaviour even deeper into our business and develop new ways to communicate our activities with our many stakeholders. This will include a review of our CSR reporting structure and, as always, we value your views and suggestions.

For further information please visit our CSR Report 2006.
(www.legalandgeneralgroup.com/csr)

Board of Directors

1 2 3 4 5 6

1. Sir Rob Margetts CBE, Chairman, aged 60, was appointed as a non-executive director in June 1996 and Chairman in February 2000. Rob is a senior non-executive director of Anglo American Plc and Chairman of Ensus Plc. He is also a Trustee of the Council for Industry and Higher Education and a member of the Council for Science & Technology. Former roles include: Chairman of BOC Group Plc; Chairman of the Natural Environment Research Council and Vice Chairman of ICI Plc.

2. Tim Breedon, aged 49, was promoted to Group Chief Executive in January 2006 from Deputy Group Chief Executive. He joined the Board as Group Director (Investments) in January 2002 having joined Legal & General in 1987. Tim is a director of the Financial Reporting Council. Former roles include: Managing Director (Index Funds) and Director (Index Funds).

3. Andrew Palmer, Group Director (Finance), aged 53, was appointed to the Board in January 1996. He joined Legal & General in 1988. Andrew is a non-executive director of Slough Estates Plc, Chairman of the Association of British Insurers (ABI) Financial Regulation and Taxation Committee and is Chairman of the ABI's Financial Reporting Panel. Former roles include: Group Director (Corporate Business), Group Director (Services).

4. Kate Avery, Group Executive Director (Wealth Management), aged 47, was appointed to the Board in January 2001. She joined Legal & General in 1996. Kate is a non-executive director of Kelda Group Plc and is a member of the Association of British Insurers Distribution & Regulation Committees. Former roles include: Retail Customer Director and Director (Group Marketing and Direct). Before joining Legal & General, Kate was Managing Director, Barclays Stockbrokers Limited and Managing Director, Barclays Bank Trust Company Limited.

5. Robin Phipps, Group Executive Director (UK), aged 56, was appointed to the Board in January 1996. He joined Legal & General in 1982. Robin is Deputy Chairman of the ABI and Chairman of the ABI's Life Insurance Council. Former roles include: Group Director (UK Operations), Group Director (Retail Business); Group Director (Sales & Marketing) and IT Director.

6. John Pollock, Group Executive Director (Protection & Annuities), aged 48, was appointed to the Board in December 2003. He joined Legal & General in 1980. Former roles include: Director, UK Operations, Managing Director, Legal & General Asia and various posts in Customer Services and IT.

7 8 9 10 11 12 13

7. Frances Heaton, an independent non-executive director, aged 62, was appointed to the Board in July 2001. Frances is a non-executive director of Jupiter Primadona Growth Trust Plc and BMT Limited. Former roles include: non-executive director AWG PLC, member of the Court of Directors of the Bank of England; Deputy Chairman of WS Atkins PLC and executive director of Lazard Brothers & Co. Limited.

8. Beverley Hodson OBE, an independent non-executive director, aged 55, was appointed in December 2000. Beverley is currently a non-executive director of Robert Wiseman Dairies Plc, First Milk Limited and Vedior NV. Former roles include: non-executive director of M&G Group (Prudential); director of The National College for School Leadership Limited; member of the North Yorkshire & Humberside Regional Development Agency; Managing Director of WH Smith Group Plc; Managing Director of Children's World (part of Boots) and Managing Director of Dolcis, Bertie Shoes and Cable and Co.

9. Rudy Markham, aged 61, was appointed as an independent non-executive director in October 2006. Rudy is also a non-executive director of Standard Chartered PLC and is Chairman of its Audit & Risk Committee. Rudy is an executive director and Chief Financial Officer of Unilever PLC and Unilever NV. Former roles include: Director, Strategy & Technology, Unilever PLC; Chairman and Chief Executive Officer of Unilever Japan, Chairman of Unilever Australia and Group Treasurer of Unilever.

10. Dr Ronaldo Schmitz, aged 68, is an independent non-executive director, and was appointed in October 2000. Ronaldo is also a non-executive director of GlaxoSmithKline Plc, Rohm & Haas Company, Cabot Corporation and Sick AG. Former roles include executive director of Deutsche Bank AG.

11. Henry Staunton, aged 58, was appointed as an independent non-executive director in May 2004. Henry joined Ladbrokes Plc as a non-executive director during 2006 and is also a non-executive director of Standard Bank Plc. Former roles include: Finance Director of ITV Plc and Granada Group Plc; Chairman of Ashtead Group Plc and non-executive director of EMAP Plc and ITN.

12. James Strachan, aged 53, is an independent non-executive director who was appointed to the Board in December 2003. James is a member of the Court of Directors of the Bank of England, a non-executive director of Care UK Plc, Chairman of RNID, a visiting fellow at the London School of Economics and a Trustee of Somerset House. Former roles include: Chairman of the Audit Commission and Managing Director of Merrill Lynch.

13. Sir David Walker, Vice Chairman, aged 67, was appointed to the Board in March 2002 as the senior independent non-executive director. Former roles include: Chairman of Morgan Stanley International Limited; executive director of the Bank of England; Chairman of the London Investment Banking Association; Chairman of the Securities & Investments Board and Deputy Chairman of Lloyds Bank.

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The Board of Legal & General Group Plc is committed to high standards of corporate governance. It supports the Combined Code on Corporate Governance ('the Code'), which sets standards of good practice for UK listed companies.

This section of the Annual Report, together with the Directors' Report, the Remuneration Report and the Nominations Committee Report, explains how Legal & General complies with the principles and relevant provisions of the Code.

The Board

The Board of Legal & General Group Plc is collectively responsible for determining the strategic direction of the Group and for ensuring that Legal & General meets its obligations to shareholders. During 2006, the Board met 11 times and also held a separate strategy event at an offsite location.

At each Board meeting, the directors receive a detailed briefing from a senior manager on an important business issue. This is designed not only to help non-executive directors develop a thorough understanding of key issues facing Legal & General, but also to allow non-executive directors to build working relationships with senior managers below Board level. The Board has a formal schedule of matters specifically reserved to it, including decisions on strategic issues, capital expenditure and material contracts. In addition, the Board regularly reviews major projects, considers operating and financial issues and monitors performance against plan. The Chairman, in conjunction with the Group Secretary, ensures that the Board receives the information it needs to discharge its duties.

Board Composition and Structure

As at 31 December 2006, the Board consisted of 13 directors. Biographies of all directors currently holding office appear on pages 32 and 33.

The Board consists of a part-time non-executive Chairman, five executive directors and seven non-executive directors. Throughout 2006, the majority of directors were non-executive, all of whom (with the exception of the Chairman) the Board has determined to be independent in both character and judgement. Their diverse business experience and wide range of skills enable them to make a significant contribution at meetings of the Board and its Committees. Their remuneration consists only of fees and they do not participate in any performance-related pay arrangements. The terms and conditions of appointment of non-executive directors are available for inspection at the Company's registered office and at the Annual General Meeting (AGM). Attendance records for all directors who have held office during the year appear on page 39.

The following changes to the composition of the Board or to executive roles took place during 2006:

- On 1 January 2006, Tim Breedon, formerly Group Director (Investments), succeeded Sir David Prosser as Group Chief Executive
- Following a review of the structure of the UK business, Robin Phipps was appointed Group Executive Director, UK in March 2006. In May 2006, Kate Avery was appointed Group Executive Director (Wealth Management) and John Pollock was appointed Group Executive Director (Protection & Annuities).
- Barrie Morgans retired as a non-executive director at the AGM on 18 May 2006
- Rudy Markham was appointed as a non-executive director on 1 October 2006.

All the above changes have been achieved without undue disruption to the business.

The Chairman holds at least two meetings a year with the non-executive directors without executive directors being present. The Board has agreed a clear division of responsibilities between the Chairman and the Group Chief Executive. The roles of the Chairman, Group Chief Executive and directors are clearly defined so that no single individual has unrestricted powers of decision.

The Chairman, Sir Rob Margetts, is responsible for leadership of the Board and for ensuring effective communication with shareholders. As part of its regular evaluation, the Board considers the Chairman's availability and his capacity to undertake his role, against the background of his other commitments. The Board remains satisfied that the Chairman continues to be able to fulfil the normal time commitments required of his role and has the personal commitment and capacity to make himself available when unforeseen circumstances arise. In September 2006, Sir Rob Margetts resigned as a director and Chairman of the BOC Group Plc.

The Group Chief Executive is responsible for the day to day management of the Group and implementation of the strategy approved by the Board. The Board delegates responsibility to the Group Chief Executive, who is supported by the executive directors and heads of specialist functions. Throughout 2006, the Group Chief Executive chaired the Management Committee, which consists of all executive directors, the Resources and International Director, and the Group Secretary.

Sir David Walker, Vice Chairman, is the senior independent director. The senior independent director is available to shareholders if they have concerns which cannot be resolved through the usual channels.

The Group Secretary, through the Chairman, is responsible for advising the Board on all governance matters and for ensuring good information flows within the Board. All directors have access to the advice and services of the Group Secretary, as well as external advice, as required, at the expense of the Group.

Board Evaluation

The Board and its directors participate in an annual evaluation process, the aim of which is to assess the effectiveness of the Board's collective performance as well as the contributions of individual directors.

An externally facilitated evaluation is carried out in alternate years. In 2005, the process was facilitated by an external consultant from the London Business School. Consequently, the 2006 evaluation was conducted internally by means of questionnaires and interviews. All members of the Board participated in the 2006 process.

A summary of the key findings was provided to the Board by the Chairman. Overall, there was a high level of satisfaction with the way in which the Board functions and the changes implemented during the year. Feedback on individual performance was delivered to directors by the Chairman. In the case of the Chairman, feedback was delivered by the senior independent director.

Separate evaluations are carried out to assess the effectiveness of the Audit and Remuneration Committees.

In addition to the Board evaluation, executive directors are subject to an annual appraisal and to regular review of their performance by the Group Chief Executive. The Chairman conducts the annual appraisal, and the regular reviews of performance, of the Group Chief Executive.

Appointments to the Board
Appointments to the Board are the responsibility of the Board as a whole on the recommendation of the Nominations Committee.

All directors are subject to election by shareholders at the first AGM after their appointment and, thereafter, are subject to re-election once every three years. The removal and appointment of the Group Secretary are reserved to the Board.

Induction and Training
New directors participate in a formal induction programme tailored to their individual needs. The induction programme is designed to give directors an understanding of Legal & General, its business and the markets in which it operates. Introductory visits are arranged to Company sites and with key suppliers and stakeholders. All directors are required to maintain and develop their knowledge throughout their period of office. As part of its continuing training programme, Legal & General runs occasional training events solely for directors eg capital management and reserving.

In addition, all directors are invited to participate in Legal & General's educational and business awareness seminars for senior management. Recent sessions have included, Age Discrimination Legislation and Doing Business in the UK.

Relations with Shareholders
The Board attaches high importance to maintaining good relationships with shareholders. There is regular dialogue with institutional shareholders. Care is exercised to ensure that any price-sensitive information is released at the same time to all shareholders, whether institutional or private. The Board regards the AGM as an important opportunity to communicate directly with private investors. Board members, including the chairmen of the Remuneration, Nominations and Audit Committees, attend the meeting and are available to answer questions.

Board Committees
The Board has a number of standing committees:

Audit Committee
The role and work of the Audit Committee is set out on pages 48 and 49.

Corporate Social Responsibility Committee
The role and work of the Corporate Social Responsibility Committee is set out on pages 28 to 31.

Nominations Committee
The role and work of the Nominations Committee is set out on page 50.

Remuneration Committee
The role and work of the Remuneration Committee is set out on pages 40 to 47.

Group Risk and Compliance Committee (GRCC)
The role ond work of the Group Risk and Compliance Committee is set out on page 37.

Disclosure Committee
The Disclosure Committee advises the Board on the management and disclosure of insider information in accordance with the requirements of the Listing and Disclosure Rules. The Disclosure Committee is chaired by the Group Financial Controller and comprises the heads of specialist functions. It meets when circumstances dictate.

Internal Control
The Board has overall responsibility for the Group's internal control systems and for monitoring their effectiveness. Implementation and maintenance of the internal control systems are the responsibility of the executive directors and senior management. The performance of internal control systems is reviewed regularly by the Audit Committee, the GRCC and the boards of subsidiary companies.

The Board regularly reviews actual and forecast performance of its businesses compared with their one year plans, as well as other key performance indicators.

Lines of responsibility and delegated authorities are clearly defined. The Group's control policies and procedures are published on a dedicated intranet site, which is regularly updated and accessible throughout the Group. Directors are required to confirm compliance with these policies throughout the year. The results of this confirmation process are reported to the Audit Committee.

The Chairman and Group Chief Executive oversee the policies for employee selection, assessment and development and have direct involvement in senior management appointments. Succession planning and contingency arrangements are in place for senior management and have been reviewed by the Board. The Group seeks to conduct business in accordance with ethical principles and there is guidance for employees on the standards required.

The arrangements for establishing policies in respect of the key risks to the Group are set out below.

Review of Internal Control
The Combined Code requires directors to review and report to shareholders on the Group's internal control systems, which include financial, operational and compliance controls, and risk management.

The Board has controls in place to identify, evaluate and manage significant risks faced by the company on an ongoing basis and for determining the effectiveness of the system of internal control. Where failings or weaknesses are identified, necessary actions are taken to remedy any such failings or weaknesses.

Established procedures, including those already described, are in place to comply with the Combined Code. The Board assesses the effectiveness of internal control systems on the basis of:

- Regular reports by management to the main operating boards and the Audit Committee, on the adequacy and effectiveness of internal control systems and significant control issues;
- The GRCC's review of the continuous Groupwide process for formally identifying, evaluating and managing the significant risks to the achievement of the Group's objectives;
- Compliance reports and presentations from the Director, Compliance, on at least a quarterly basis; and
- Presentations of the results of internal audits, by the Group Chief Internal Auditor, to the Audit Committee.

The Board takes regular account of the significance of social, environmental and ethical matters to the businesses of the Group.

The GRCC's review of the significant risks to the Group includes these matters. The work of the Corporate Social Responsibility Committee, which is chaired by the Group Chief Executive, is set out on pages 28 to 31.

The Group's internal control systems are designed to manage, rather than eliminate, the risk of failure to meet business objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss. In assessing what constitutes reasonable assurance, the Board has regard to materiality and to the relationship between the cost of, and benefit from, internal control systems.

The results of the ongoing monitoring of financial, operational and compliance controls, and the risk management process, are reported to the Board. For 2006, the Board was able to conclude, with reasonable assurance, that appropriate internal control systems have been maintained throughout the year.

Internal Audit
Internal Audit advises management on the extent to which systems of internal control are adequate and effective to manage business risk, safeguard the Group's resources, and ensure compliance with legal and regulatory requirements. It provides objective assurance on risk and control to senior management and the Board.

Internal Audit's work is focused on areas of greatest risk to the Group as determined by a structured risk assessment process involving executive directors and senior managers. The output from this process is summarised in a plan which is presented to the Audit Committee. The Group Chief Internal Auditor reports regularly to the Group Chief Executive and to the Audit Committee.

Compliance
The Group Compliance function is responsible for oversight of the Group's compliance with regulatory requirements and standards. This encompasses the provision of policy advice and guidance to the regulated firms, oversight of regulated firms' compliance arrangements to assess whether firms have appropriate systems, procedures and controls in place to manage their permitted regulatory activities, and oversight of regulatory risks arising from authorised firms' compliance responsibilities. The Director, Compliance, reports monthly to the GRCC and regularly to the Group Board.

Management of Risk
The Group, in the course of its business activities, is exposed to Insurance, Market, Credit, Liquidity, and Operational risks. Overall responsibility for the management of these risks is vested in the Group Board. To support it in this role, a risk framework is in place comprising formal committees, risk assessment processes and risk review functions. The framework provides assurance that risks are being appropriately identified and managed and that an independent assessment of risks is being performed.

Committee Structure
Oversight of the risk management framework is performed on behalf of the Group Board by its sub-committee, the GRCC. The GRCC meets monthly and is chaired by the Group Chief Executive. All executive directors are members. In addition, senior managers drawn from across the Group are regular attendees. The Chairman of the Audit Committee and PricewaterhouseCoopers, as external auditors, have a standing invitation to attend.

The primary role of GRCC is to ensure there are appropriate processes in place across the Group to identify, assess, monitor and control critical risks facing the Group, including regulatory risks. It reports regularly to the Group Board and its minutes are provided to the Audit Committee.

The table below shows the sub committees of the GRCC that are in place. In addition, Risk and Compliance Committees (RCCs) are in place for each of the main operational business units of the Group. These committees are predominantly responsible for the oversight of the management of operational risks and regulation. RCCs formally report both to their operating boards and to the GRCC on a monthly basis. Management of risks arising from the Group's overseas subsidiaries is performed by the Boards of the local holding companies, which provide reports to the GRCC.

Committee	Role	Membership
Group Capital Committee	To assess the capital requirements (including the risk based capital requirements) of the Group; to monitor the sources of capital available to meet these requirements and oversee the allocation of capital to firms.	Group Chief Executive, Group Director (Finance), Group Executive Director (Protection & Annuities), Group Actuary, Actuary (UK)
Counterparty Credit Committee	To set limits for the Group's exposure to any single counterparty failure and to manage exposures within these established limits.	Group Director (Finance), Chief Executive Officer (LGIM), Group Treasurer
UK Asset and Liability Committee (ALCO)	To ensure that assets and liabilities for the UK insurance business are appropriately managed.	Group Director (Finance), Chief Executive Officer (LGIM), Group Actuary, Actuary (UK), Managing Director (Portfolio Managers)
UK Pricing and Insurance Risk Committee	To ensure that products for the UK Group are appropriately designed and priced, that product legal risks are assessed and that appropriate processes are in place to identify, assess, monitor and, where deemed appropriate, reinsure risk.	Group Executive Director (Protection & Annuities), Group Actuary, Actuary (UK), Director (UK Finance)
Group Operational Risk Assessment Committee	To ensure consistency in approaches to operational risk management across the Group.	Group Director (Finance), Senior Finance and Risk Managers, Group Secretary

Risk Assessment Processes
A continuous Groupwide process is in place formally identifying, evaluating and managing the significant risks to the achievement of the Group's objectives. A standard approach is used to assess risks. Senior management and the Risk Review Functions (see below) review the output of the assessments. A Groupwide risk assessment process is used to determine the key risks within the Group reported to the GRCC.

Risk Review Functions
Group and firm level Risk Review Functions provide oversight of the risk management processes within the Group. A central risk function is responsible for setting the risk management framework and standards. Risk Review Functions in each of the business operating units manage the framework in line with these standards. Their responsibilities include the evaluation of changes in the business operating environment and business processes, the assessment of these changes on risks to business and the monitoring of the mitigating actions. The Risk Review Functions also ensure that risk committees are provided with meaningful risk reports and that there is appropriate information to assess risk issues.

Details of the categories of risk to the Group, and high-level management processes, are summarised below. More detailed analysis may be found in pages 27 and 106. The Group has defined policies for the management of its key risks, the operation of which are supported by Risk Review Functions and are independently confirmed by Group Internal Audit. The GRCC reviews and approves these policies.

Insurance Risk
Insurance risk is the risk arising from higher claims being experienced than was anticipated.

Insurance risk is implicit in the Group's insurance business and arises as a consequence of the type and volume of new business written and the concentration of risk, in particular, policies, or groups of policies, subject to the same risks.

The Group controls its insurance exposures through policies and delegated authorities for underwriting, pricing and reinsurance. Pricing is based on assumptions, such as mortality and persistency, which have regard to past experience and to trends. Insurance exposures are further limited through reinsurance.

Market Risk
Market risk is the risk arising from fluctuations in interest and exchange rates, share prices and other relevant market prices. The investment policies for long term and other businesses have due regard to the nature of liabilities and guarantees and other embedded options given to policyholders. The interest rate risk of such liabilities is normally managed by investing in assets of similar duration, where possible. It is further managed by maintaining capital sufficient to cover the consequences of mismatch under a number of adverse scenarios and by the use of derivatives.

The Group is also potentially exposed to loss as a result of fluctuations in the value of, or income from, assets denominated in foreign currencies. Balance sheet foreign exchange translation exposure in respect of the Group's international subsidiaries is actively managed in accordance with a policy, agreed by the Group Board, which allows between 25% and 75% of net foreign currency assets to be hedged.

Credit Risk
Credit risk is the risk that the Group is exposed to loss if another party fails to perform its financial obligations to the Group.

Credit risk is not sought in its own right. However, the investment of shareholders' and policyholders' monies requires credit risks to be taken. Exposure to credit risk also arises in the reinsurance of insurance contracts. Credit risk is managed through the setting and regular review of detailed counterparty credit and concentration limits. Compliance with these limits for investment and treasury transactions is monitored daily.

Liquidity Risk
Liquidity risk is the risk that the Group, 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.

A degree of liquidity risk is implicit in the Group's businesses. Liquidity risk arises as a consequence of the uncertainty surrounding the value and timing of cash flows. The Group's Treasury function manages liquidity to ensure the Group maintains sufficient liquid assets and standby facilities to meet a prudent estimate of its net cash outflows.

Operational Risk
Operational risk is the risk arising from inadequate or failed internal processes, people and systems, or from external events.

The Group identifies and assesses operational risk as part of its continuous risk assessment processes. RCCs ensure that appropriate policies and procedures are in place for these risks and that they are properly controlled. There are detailed procedures covering specific areas of operational risk.

Contagion Risk
The occurrence of a risk in one part of the Group may result in contagion risk elsewhere in the Group. Such matters are assessed and monitored by the GRCC.

Prudential Regulation of Insurance Business
Most of the activities of the Group relate to the businesses which are subject to prudential regulation and require management to operate in a sound and prudent manner. In the UK, the Financial Services and Markets Act 2000 (the Act) established the Financial Services Authority (FSA) as the regulator for most Group operations. The Act, in particular, requires long term insurance business to be written within long term insurance funds, for which the actuaries appointed under the Act have certain legal accountabilities. These actuaries are subject to the disciplines of professional conduct and guidance and have a reporting relationship to the directors of the relevant insurance company and to the FSA. The actuaries have access to their boards and must report fully and impartially on the financial condition of the funds, annually quantifying and confirming each fund's liabilities and solvency position. The FSA receives a copy of these reports, which are also subject to audit and overall peer review.

Going Concern
The directors have prepared the financial statements on the going concern basis consistent with their view, formed after making appropriate enquiries, that the Group is operationally and financially robust.

Compliance with the Code
For the year ended 31 December 2006, the Company believes it complies with all principles and provisions of the Code to the extent applicable to Legal & General Group Plc except in relation to:

(i) Membership of the Remuneration Committee. The Combined Code was updated in June 2006 for the reporting periods commencing on or after 1 November 2006. One of the changes made was the removal of the restriction on the Chairman of the Board being appointed as a member of the Remuneration Committee. To enhance the membership of the Remuneration Committee, the Board anticipated this change and appointed Sir Rob Margetts as a member with effect from 12 December 2006.

(ii) Proxy votes. In compliance with the Code, the level of proxies lodged on each resolution at the AGM was made known after it had been dealt with on a show of hands. However, shareholders may also have received copies of the proxy votes in papers distributed at the start of the meeting.

Board Attendance

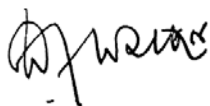
The number of full Board meetings and Committee meetings attended by each director during the year was as follows:

	Scheduled Board Meetings	Remuneration Committee	Audit Committee	CSR Committee	Nominations Committee	Group Risk and Compliance Committee
Sir Rob Margetts *Non-executive (Chairman)*	11(11)	3(3)	–	–	3(3)	–
Tim Breedon *Group Chief Executive*	11(11)	–	–	3(3)	–	12(12)
Andrew Palmer *Executive director* *Group Director (Finance)*	11(11)	–	–	–	–	12(12)
Kate Avery *Executive director* *Group Executive Director (Wealth Management)*	11(11)	–	–	–	–	10(12)[1]
Robin Phipps *Executive director* *Group Executive Director (UK)*	11(11)	–	–	–	–	12(12)
John Pollock *Executive director* *Group Executive Director (Protection & Annuities)*	11(11)	–	–	–	–	10(12)[1]
Frances Heaton *Non-executive director*	10(11)[1]	–	4(4)	–	3(3)	–
Beverley Hodson *Non-executive director*	11(11)	2(3)[1]	–	–	3(3)	–
Barrie Morgans *Non-executive director*[2]	3(4)[1]	–	2(4)[1]	–	0(1)[1]	–
Rudy Markham *Non-executive director*[3]	0(3)[3]	–	–	–	1(1)	–
Ronaldo Schmitz *Non-executive director*	8(11)[1]	3(3)	–	–	3(3)	–
Henry Staunton *Non-executive director* *(Chairman of the Audit Committee)*	11(11)	–	4(4)	–	3(3)	9(12)[4]
James Strachan *Non-executive director*	10(11)[1]	3(3)	4(4)	–	3(3)	–
Sir David Walker *Non-executive* *Vice Chairman, Chairman of the Remuneration Committee and Senior Independent Director*	11(11)	3(3)	–	–	3(3)	–

[1] Indicates that absence was agreed with the Chairman in advance.
[2] Barrie Morgans retired from the Board on 18 May 2006.
[3] It was known prior to Rudy Markham's appointment on 1 October 2006, that he would be unable to attend Board meetings for the remainder of 2006. He did, however, attend the two day Group Board Strategy event in October 2006 and has also attended corporate induction sessions.
[4] As Chairman of the Audit Committee, Henry Staunton has a standing invitation to attend the Group Risk & Compliance Committee but is not a member.

Dear Shareholder,
I am pleased to present the Remuneration Committee's report on directors' remuneration for 2006, the forthcoming financial year, and subject to ongoing review, subsequent years.

A resolution to vote for the Directors' remuneration report will be put to the Annual General Meeting (AGM). I hope that you will support this resolution.



Sir David Walker
Chairman of the Remuneration Committee

Directors' Report on Remuneration
The report of the Remuneration Committee has been prepared in accordance with the requirements of Schedule 7A to the Companies Act 1985 (as amended by the Directors' Remuneration Report Regulations 2002). It also describes the Group's compliance with the Combined Code of Corporate Governance in relation to remuneration.

Remuneration Committee
The Committee is chaired by Sir David Walker. The other members are Beverley Hodson, Ronaldo Schmitz, James Strachan and Sir Rob Margetts. Sir Rob Margetts (who was independent on appointment) was appointed to the Remuneration Committee on 12 December 2006, having previously attended by invitation. All other members of the Committee are independent.

By invitation the meetings are also attended by the Group Chief Executive. The Resources & International Director, Gareth Hoskin, attends as the executive responsible for advising on remuneration policy. No person is present during any discussion relating to their own remuneration. New Bridge Street Consultants LLP ('NBSC'), which the Committee appointed, acts as independent adviser to the Committee and attends the meetings. NBSC does not provide any other services to the Company, other than remuneration advice.

The remuneration strategy, policy and approach for all staff are reviewed annually by the Committee. The Committee considers the policy in relation to senior executive remuneration in the context of remuneration structures across the Group as a whole. All share schemes and long term incentive plans are established and monitored by the Committee. The Committee makes recommendations to the Board each year in respect of the Chairman, executive directors' and other senior executives' remuneration.

In March 2007, the recommendations were all accepted. The terms of reference of the Remuneration Committee are available on the Company's website or on request. The terms of engagement between the Company and NBSC are available on request.

During the year the Remuneration Committee undertook a formal review of its own effectiveness and is satisfied that it had been operating as an effective Remuneration Committee meeting all applicable regulatory requirements.

Remuneration Policy
The Group's remuneration policy is broadly consistent for all employees and is designed to support recruitment, motivation and retention. Remuneration is considered within the overall context of both the sector of which the Group is a part and the Group's individual businesses. The policy for the majority of employees continues to be to pay around the relevant mid-market level with a package designed to align the interests of employees with those of shareholders and with an appropriate proportion of total remuneration dependent upon performance. Management work in partnership with our trades union, Amicus, to ensure our pay policies and practices are free from unfair bias. This is monitored by an annual equal pay audit.

The policy for executive directors is described in more detail below.

Remuneration Policy for Non-Executive Directors
Non-executive directors are appointed for a period of three years. Their performance is reviewed annually. They may be reappointed for a further three years and, if considered appropriate and depending on performance, a final period of three years. Appointments may be terminated by either party without notice. Fees for the non-executive directors are determined by the Group Board, based on a range of external information and advice set within the aggregate limits contained in the Articles of Association.

During 2006, the fees of the non-executive directors including the Chairman were reviewed. The conclusion of the review was that no change should be made to the fees of the non-executive directors, which are set out below. The Chairman's fee (which is a single amount encompassing all his responsibilities) was increased to £325,000 per annum with effect from 1 January 2007. Other non-executive directors receive a base fee of £60,000. An additional fee of £40,000 is payable for the joint role of Chairman of the Remuneration Committee and Vice Chairman. An additional fee of £20,000 is payable to the Chairman of the Audit Committee. These additional fees reflect the responsibility and time commitment required of these roles. It is expected that non-executive directors will use 50% of their fees, after UK tax, to buy Legal & General shares, to be retained by them for their remaining period of office. There is no remuneration other than these non-pensionable fees except where the Company meets authorised expenses of non-executive directors incurred on Legal & General activities.

NED	Current contract start date	Current contract end date
Frances Heaton	June 2004	June 2007
Beverley Hodson	November 2006	May 2007
Sir Rob Margetts	October 2005	May 2008
Rudy Markham	October 2006	October 2009
Ronaldo Schmitz	November 2006	May 2010
Henry Staunton	May 2004	May 2007
James Strachan	December 2006	December 2009
Sir David Walker	February 2005	February 2008

Remuneration Policy for Executive Directors
The remuneration of the Group's executive directors comprises salary, participation in an annual bonus plan (paid partly in cash and partly in deferred shares) and the Group's Performance Share Plan (PSP), which is a long term incentive plan, plus pension and ancillary benefits. The variable elements of pay (for example, the annual bonus plan and PSP) are designed to provide a strong alignment of interest between the individual and the shareholders through providing rewards which are linked to the generation of superior returns to shareholders and strong financial performance. The chart illustrates that a significant proportion of pay is performance related. When setting remuneration, regard is given to levels of pay in individual market comparators, related to job size, function and sector, and individual and company performance. Data is obtained from a variety of independent sources (including NBSC, Towers Perrin, Watson Wyatt, Monks, which is part of PricewaterhouseCoopers, our auditors, and McLagan). Where possible, the practice is to use at least two independent sources of information for each individual role. The remuneration policy is to pay at or around the market median. The market against which the remuneration for the executive directors is measured is primarily the FTSE 100, with special reference to companies in the UK financial services sector.

SUMMARY OF KEY FEATURES OF EXECUTIVE DIRECTORS' REMUNERATION IN 2007

Element of remuneration package	Purpose	Policy	Summary of how it operates
Base Salary	• Help recruit and retain key employees • Reflect the individual's experience and role within the Group • Salary is supplemented with normal benefits available to senior executives including car allowance, medical insurance and staff discounts. Legal & General products can be acquired by executive directors on the terms available to other members of staff	• To pay at around the mid-market relative to the FTSE 100, with particular regard to other relevant financial institutions • Regard given to individual skills and experience • In specific circumstances (for example, a new appointment) may set salaries below mid-market, with a view to reaching mid-market level within two to three years	• Paid monthly in cash • Normally reviewed by the Remuneration Committee annually and fixed for the 12 months commencing 1 January
Annual Bonus	• Incentivise executives to achieve specific, pre-determined goals over a short term period • Reward ongoing stewardship and contribution to core values • Deferred element, awarded in shares, provides a retention element	• Maximum bonus potential set by reference to market comparators (currently 105% of base salary) • On-target bonus of 80% of base salary for the Group Chief Executive and 64% of base salary for the other executive directors • Percentage of bonus deferred and awarded in shares	• All executive directors have objectives related to Group KPIs, plus individual divisional and personal targets • Bonus out-turn determined by the Remuneration Committee after year end, based on performance against targets • Normally, 62.5% of the bonus paid in cash and 37.5% paid in deferred shares to be held for three years
Performance Share Plan	• Incentivise executives to achieve superior returns to shareholders • Align interests of executives and shareholders through building a shareholding • Retain key executives over three year performance period	• Awards of nil cost shares made annually, with vesting conditional on relative total shareholder return (TSR) measured over the three subsequent years • Maximum annual grant of basic award is 50% of salary • Maximum amount which may vest is four times basic award (ie. 200% of salary) and the minimum which may vest is nil	• Vesting condition measures the Group's TSR versus the FTSE 100 • The basic award of shares will vest if TSR is at median, with the maximum amount vesting if Legal & General is ranked at the twentieth percentile. No awards vest below median • The Remuneration Committee will also assess whether the underlying financial performance of the Company is reflective of the TSR out-turn and in exceptional cases may scale back vesting
Pension	• Reward sustained contribution	• Provide competitive post-retirement benefits • No compensation for public policy or tax changes	• Participation in a Group pension scheme • Accrue benefits according to length of service up to retirement • Cash alternative for executive directors opting for enhanced protection above the Lifetime Allowance, see Pension sections, page 47
Share Ownership Guidelines	• To align the interests of executive directors and shareholders	• The Group Chief Executive is required to build and maintain a shareholding of 200% of base salary and, for other executive directors, 100% of base salary	• Executives are expected to build a shareholding through the vesting of shares under the Group's share incentive plans. Existing shareholdings and shares acquired in the market are also taken into account

Proportion of Base Salary vs Performance Related Remuneration (%)

Remuneration Policy for Other Senior Executives

The remuneration policy for senior executives below Board level is consistent with that followed at executive director level. There are 28 executives in the UK whose salaries exceed £150,000.

Salary Range	Number of Executives
£150,000 – £175,999	16
£176,000 – £200,999	5
£201,000 – £225,999	4
£226,000 – £250,999	2
£251,000 +	1

The total salaries of these executives is £5,195,842.

Salary

The policy is to pay salaries around the mid-market level for the individual performance within the context of the relevant market for the job. However, when setting salaries, judgement is exercised by the Committee, having regard to individual experience and responsibility.

Accordingly, particularly when a new appointment is made, salary levels may be set at a lower level than the mid-market position, with a view to increasing towards this position over the two to three years following promotion. This approach is being followed in the case of Tim Breedon's appointment to the role of Group Chief Executive and in respect of John Pollock.

Salary is the only pensionable remuneration and it is normally reviewed annually with effect from January.

The base salaries for the executive directors for the financial year beginning on 1 January 2007 are as follows:

Tim Breedon	£740,000
Kate Avery	£350,000
Andrew Palmer	£440,000
Robin Phipps	£450,000
John Pollock	£320,000

Annual Bonus

For payments relating to 2007 performance the maximum annual bonus potential for the executive directors has been increased from 96% to 105% of salary of which approximately 62.5% of any bonus earned is normally paid in cash, with the balance being paid in shares under the Share Bonus Plan described below. This increase recognises the need to pay the executive directors competitively relative to other companies of a similar size and complexity. The proportion of bonusable targets based on empirical measures and group performance has been increased. The level of bonus payable for on-target performance has not increased, and is based on the mid-market bonus levels for the job in comparator companies. This remains at 80% of salary for the Group Chief Executive (of which a maximum of 50% is payable in cash and 30% in deferred shares), and for the other executive directors it is 64% of salary (comprising 40% cash and 24% deferred shares). Accordingly, bonus payments will only increase for the delivery of superior performance.

The executive directors' bonuses are based on a variety of targets, including Group KPIs (applicable to all directors), performance of the business unit for which the individual is responsible (where applicable), and personal targets. The bonus which results from the delivery of these objectives will be reviewed by the Committee based on its view of the executive's overall performance and regulatory compliance.

As stated above, 37.5% of any bonus earned is normally deferred into shares under the Share Bonus Plan. The Plan grants conditional shares which are held in a trust for three years during which time dividends are paid. It is a deferred bonus scheme with awards designed to encourage employee retention based on annual performance. It is not a long term incentive plan and there are no performance conditions for release. The value of the shares awarded to directors is reported in the year of performance. The chart overleaf summarises the key features of the bonuses for each executive director.

Performance Share Plan

Executive directors are entitled to participate in the Group's Performance Share Plan (PSP), which is the only long term incentive arrangement available to senior executives in the Group, though the Remuneration Committee is considering the introduction of a specific arrangement for the LGIM business. The PSP was approved by shareholders in 2004.

Under the PSP, basic awards of shares are made to top managers. The Committee reviews the quantum of basic awards made each year to ensure that it is in line with the market. The maximum annual basic award in 2006 and 2007 is 50% of salary.

The number of shares which vest is dependent on Legal & General's Total Shareholder Return (TSR) compared with that of the other FTSE 100 companies at the date of award measured over a fixed three year period. The award will lapse if Legal & General's TSR is ranked below median at the end of the three year period.

If the TSR is at median then the basic award will vest and be transferred to the executives. They will receive four times the basic award if Legal & General is ranked at the 20th position or above at the end of the three year period, with the amounts reducing on a pro rata basis between 20th position and median. The FTSE 100 is currently considered to be an appropriate comparator group. The TSR performance conditions are independently reviewed by NBSC.

Additionally, the Committee assesses whether the underlying performance of the Company is reflective of the TSR out-turn. In exceptional circumstances, the Committee may exercise their discretion to scale back the vesting of awards, if it was felt that the Company's financial performance did not justify the level of vesting. The parameters which the Committee use in making this assessment include market share, partnerships gained and maintained, cost constraint, capital management and shareholder perception.

Dilution Limits

The PSP and the Share Bonus Plan operate with market purchased shares which are held in an Employee Benefit Trust. The Company's all-employee plans may be satisfied using either new-issue or market purchased shares.

The Company's all-employee plans and the now closed Executive Share Option Plan operate within the ABI's dilution limit of 5% in 10 years for executive schemes and all its plans operate within the 10% in 10 years limit for all schemes. As at 31 December 2006, the Company had 4.37% share capital available under the 5% in 10 years limit, and 8.83% share capital available under the 10% in ten years limit.

EXAMPLES OF EXECUTIVE DIRECTORS' TARGETS FOR 2007

% weighting of total bonus

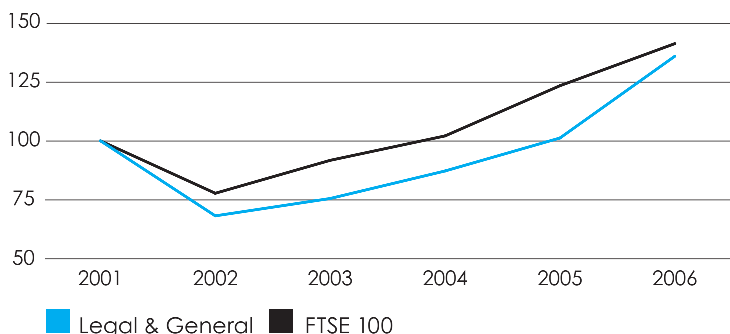
	Group KPI's	Other Group Financial Targets	Other Group Targets	Divisional Financial Targets	Other Divisional Targets	Example targets
Tim Breedon	30%	50%	20%			Deliver return to shareholders
Kate Avery	30%			30%	40%	Improve profits in the individual and corporate long term savings market and deliver customer experience targets
Andrew Palmer	30%	30%	40%			Manage Group external financial reporting, manage capital requirements, execute strategic projects, monitor and strengthen the control environment
Robin Phipps	30%			30%	40%	Deliver UK Operations sales and value added targets, manage regulatory risk and compliance requirements, develop and deliver distribution strategies
John Pollock	30%			30%	40%	Deliver profitable strategies for the general insurance, annuities and protection markets, whilst also delivering customer experience targets

Share Ownership Guidelines
In order to align further the interests of the executive directors and the shareholders, the executive directors are required to build a significant personal shareholding in the business. The Group Chief Executive is expected to build a holding of shares valued at twice salary while the other executive directors are expected to build towards a holding valued at one times their salary.

Although not contractually binding, the Committee retains the discretion to withhold future grants under the PSP if executives do not comply with the Guidelines.

Five Year Total Shareholder Return
The chart below shows the value, as at 31 December 2006, of a £100 investment in Legal & General shares on 31 December 2001, compared with £100 invested in the FTSE 100 on the same date.

Five Year Total Shareholder Return[1]



Source: Thomson Financial

1. Rebased 31 December 2001

Benefits
Other benefits for executive directors provided by the Group are:
– pension scheme;
– car allowance;
– medical insurance; and
– staff discounts. Legal & General products can be acquired by executive directors on the terms available to other members of staff.

Pensions
Each of the executive directors is a member of the Group UK Senior Pension Scheme ("the Plan"), details of which are given on page 47.

In response to the Government's changes to pensions legislation and, in particular, the introduction of a lifetime allowance, the Committee was mindful that the Company's policy is not to compensate for public policy or tax changes. Accordingly, those executives who elect solely for primary protection, remain in the company pension scheme and there has been no compensation, despite any potential additions to their personal tax burden.

For those executives who elected for enhanced protection, they may opt out of the Plan for future service accrual. In such circumstances, for future service accrual after 6 April 2006 these executives are eligible for a non-bonusable cash supplement up to 35% of base salary. The exact level of cash supplement is set at a level to ensure the cost to the Company, including allowance for National Insurance costs, does not increase. Consistent with the legislation, affected executives will be entitled to a pension determined by reference to pensionable earnings at retirement, provided this does not breach the enhanced protection requirements.

All-Employee Share Schemes
There are share schemes for all UK employees. Executive directors participate on the same terms as all UK employees in the Savings related share option scheme (SAYE), the Company Share Option Plan and the Employee Share Plan, which are all approved by Her Majesty's Revenue & Customs (HMRC).

DIRECTORS' REMUNERATION FOR FINANCIAL YEAR ENDED 31 DECEMBER 2006

	Salary/fees £'000	Benefits[1] £'000	Cash in lieu of pension £'000	Annual Bonus[2] Cash £'000	Annual Bonus[2] Deferred £'000	Total **2006 £'000**	Total 2005 £'000
Executive:							
Kate Avery[3]	320	20	8	172	103	**623**	589
Tim Breedon[4]	675	21	110	392	236	**1,434**	1,058
Andrew Palmer	415	35	-	233	140	**823**	760
Robin Phipps	425	21	-	234	140	**820**	772
John Pollock	280	20	50	157	95	**602**	464
	2,115	117	168	1,188	714	**4,302**	3,643
Non-executive:							
Frances Heaton	60	–	–	–	–	**60**	61
Beverley Hodson	60	1	–	–	–	**61**	62
Sir Rob Margetts	300	1	–	–	–	**301**	300
Rudy Markham[5]	15	–	–	–	–	**15**	-
Ronaldo Schmitz	60	7	–	–	–	**67**	64
Henry Staunton	80	–	–	–	–	**80**	73
James Strachan	60	–	–	–	–	**60**	60
Sir David Walker	100	–	–	–	–	**100**	100
	735	9	–	–	–	**744**	720
Former Chief Executive:							
Sir David Prosser[6]	174	2	–	72	–	**248**	1,503
	3,024	128	168	1,260	714	**5,294**	5,866

No directors received any compensation for loss of office.
The information in this table has been audited by the independent auditors, PricewaterhouseCoopers LLP.

1. Benefits include car allowances, medical insurance and travel expenses for work purposes.
2. In respect of the financial year, executive directors earned bonus of 86-93% of salary.
3. Prior to 6 April 2006, Kate Avery was capped at the statutory limit for pension contributions of £105,600 for 2005/6, and received a cash allowance of 15% of salary above these earnings, which is included in the "Cash in lieu of pension" column above. Since 6 April 2006 (A-day) onwards, her uncapped pay became pensionable for future accruals only and the cash allowance has, therefore, ceased.
4. The total remuneration for Tim Breedon for 2005 is £41,667 lower than the figure disclosed in the 2005 Annual Report and Accounts. The basic salary figure disclosed in the 2005 accounts, £500,000, was his basic salary from 1 June 2005. His basic salary from 1 January 2005 to 31 May 2005 was £400,000, giving basic salary earnings of £458,333 for the year.
5. This amount is paid to his employer and he therefore does not participate in the share purchase.
6. Sir David Prosser retired as Chief Executive and from the Board with effect from 31 December 2005, although he continued to be employed by the Company until March 2006. He received no compensation for loss of office and was a good leaver under the various share plans with details of his entitlement set out in last year's report.

DIRECTORS' SHARE INTERESTS

The holdings of directors in office at the end of the year in the shares of the Company, including shares awarded under the Employee Share Plan and Share Bonus Plan (2005 onwards) but not vested, are shown below. These exclude unvested awards made by the Company under the Share Bonus Plan (pre 2005) and the Performance Share Plan.

	31 December 2006	1 January 2006[1]
Kate Avery	**786,612**	**450,625**
Tim Breedon	**1,263,588**	**814,126**
Frances Heaton	**75,874**	**62,885**
Beverley Hodson	**75,961**	**62,972**
Sir Rob Margetts	**453,145**	**385,527**
Rudy Markham	**–**	**–**
Andrew Palmer	**721,816**	**561,460**
Robin Phipps	**1,403,222**	**966,830**
John Pollock	**381,606**	**250,709**
Ronaldo Schmitz	**83,235**	**70,246**
Henry Staunton	**96,247**	**78,879**
James Strachan	**61,821**	**47,396**
Sir David Walker	**217,147**	**187,134**

1. Or date of appointment if later

SHARE OPTIONS[1]

Options awarded to executive directors under the Company Share Option Plan (CSOP) and Executive Share Option Scheme (ESOS) or acquired under the Company's Savings related share option scheme (SAYE) comprise:

MOVEMENTS IN YEAR

		Share options 1 Jan 2006	Options (exercised/ lapsed) granted	**Share options 31 Dec 2006**	Exercise price (p)	Earliest exercise date	Latest exercise date
Kate Avery	(SAYE)	**32,272**		**32,272**	55	1.5.10	31.10.10
	(CSOP)	**545**		**545**	158.47	11.4.03	10.4.10
	(CSOP)	**19,589**		**19,589**	148.62	10.4.04	9.4.11
	(ESOS)	**220,430**		**220,430**	148.62	10.4.04	9.4.11
				272,836			
Tim Breedon	(SAYE)	**–**	9,220	**9,220**	101.4	1.10.09	31.3.10
	(CSOP)	**545**		**545**	158.47	11.4.03	10.4.10
	(ESOS)	**78,115**		**78,115**	162.36	23.4.02	22.4.09
				87,880			
Andrew Palmer	(SAYE)	**29,863**		**29,863**	55	1.5.08	31.10.08
	(CSOP)	**545**		**545**	158.47	11.4.03	10.4.10
	(CSOP)	**19,589**		**19,589**	148.62	10.4.04	9.4.11
	(ESOS)	**307,710**		**307,710**	148.62	10.4.04	9.4.11
	(ESOS)	**436,400**		**436,400**	147.48	10.4.05	9.4.12
	(ESOS)	**700,000**		**700,000**	78	10.4.06	9.4.13
				1,494,107			
Robin Phipps	(SAYE)	**2,493**		**2,493**	76	1.10.07	31.3.08
	(SAYE)	**13,745**	(13,745)	**–**	55	1.5.06	31.10.06
	(SAYE)	**–**	6,393	**6,393**	117	1.5.09	31.10.09
	(CSOP)	**545**		**545**	158.47	11.4.03	10.4.10
	(CSOP)	**19,589**		**19,589**	148.62	10.4.04	9.4.11
	(ESOS)	**362,260**		**362,260**	148.62	10.4.04	9.4.11
				391,280			
John Pollock	(SAYE)	**29,863**		**29,863**	55	1.5.08	31.10.08
	(CSOP)	**545**		**545**	158.47	11.4.03	10.4.10
				30,408			

Notes

- No options lapsed during 2006. As at 31 December 2006, there were 78,115 options outstanding for executive directors where the exercise price exceeded the market price of 160p. The range of share price during 2006 was 119.25p to 160p.
- The performance target applying to unvested share options under the ESOS and CSOP is that the Company's TSR performance must be at least at the median relative to the FTSE 100 over a fixed three year period from grant.
- The SAYE scheme is approved by HMRC and, in accordance with the relevant legislation, has no performance conditions.

The Company's register of directors' interests, which is open to inspection, contains full details of directors' shareholdings and share options.

GAINS ON THE EXERCISE OF SHARE OPTIONS

Gains on share options represent the difference between the market price of the shares at the date of exercise and the exercise price paid under options which have been exercised by the directors during the year.

		Options exercised	Exercise price (p)	Market price at date of exercise (p)	**Gain 2006 £'000**	Gain 2005 £'000
Robin Phipps	SAYE	13,745	55	139.75	**12**	–

Note
The information in these tables has been audited by the independent auditors, PricewaterhouseCoopers LLP.

SHARE BONUS PLAN (PRE 2005)

	Awards granted[1]	Number of shares awarded	Awards vesting during the year	**Outstanding awards as at 31 December 2006**
Kate Avery	10 April 2003	76,923	76,923	**–**
	8 April 2004	62,500	–	**62,500**
Tim Breedon	10 April 2003	107,692	107,692	**–**
	8 April 2004	112,500	–	**112,500**
Andrew Palmer	10 April 2003	121,154	121,154	**–**
	8 April 2004	87,500	–	**87,500**
Robin Phipps	10 April 2003	123,077	123,077	**–**
	8 April 2004	90,625	–	**90,625**
John Pollock	10 April 2003	42,308	42,308	**–**
	8 April 2004	43,750	–	**43,750**

Note
1. These awards vest on the third anniversary of the award date.

PERFORMANCE SHARE PLAN

	Awards granted[1]	Base award of shares	Maximum award receivable for stretch performance	Awards vesting	Awards lapsing	**Maximum outstanding awards as at 31 December 2006**
Kate Avery	10 April 2003	125,000	500,000	287,500	(212,500)	**–**
	8 April 2004	120,000	480,000			**480,000**
	7 April 2005	119,734	478,936			**478,936**
	24 April 2006	106,700	426,800			**426,800**
Tim Breedon	10 April 2003	156,250	625,000	359,375	(265,625)	**–**
	8 April 2004	150,000	600,000			**600,000**
	7 April 2005	158,758	635,032			**635,032**
	24 April 2006	240,076	960,304			**960,304**
Andrew Palmer	8 April 2004	170,000	680,000			**680,000**
	7 April 2005	158,758	635,032			**635,032**
	24 April 2006	142,267	569,068			**569,068**
Robin Phipps	10 April 2003	187,500	750,000	431,250	(318,750)	**–**
	8 April 2004	180,000	720,000			**720,000**
	7 April 2005	168,514	674,056			**674,056**
	24 April 2006	142,267	569,068			**569,068**
John Pollock	10 April 2003	37,500	150,000	86,250	(63,750)	**–**
	8 April 2004	75,000	300,000			**300,000**
	7 April 2005	93,126	372,504			**372,504**
	24 April 2006	87,138	348,548			**348,548**

Notes
1. These awards vest on the third anniversary of the award date subject to the satisfaction of performance targets as described above.
2. In 2007, in respect of performance in 2006, the Remuneration Committee decided that executive directors should be granted base awards of performance shares to the following values: Tim Breedon, £370,000; Kate Avery, £175,000; Andrew Palmer, £220,000; Robin Phipps, £225,000 and John Pollock, £160,000.
3. The table shows the maximum number of shares which could be awarded if awards were to vest in full.
4. The 2006 award share price was 140.58p.

PENSION ENTITLEMENTS[1]

	Age at 31 December 2006	Increase in accrued pension in 2006 £'000	Accumulated accrued pension at 31 December 2006 £'000	Transfer value of accrued benefits at 31 December 2006 £'000	Transfer value of accrued benefits at 31 December 2005 £'000	Increase/ (decrease) net of employee contributions in 2006 £'000
Kate Avery	46	5	22	308	226	69
Tim Breedon[1]	48	68	233	3,489	2,302	1,178
Andrew Palmer[1]	53	21	214	3,760	3,348	391
Robin Phipps	56	14	243	4,763	4,166	576
John Pollock	48	12	126	1,836	1,575	256

Notes
The information in this table has been audited by the independent auditors, PricewaterhouseCoopers LLP.
1. The transfer values of accrued benefits at 31 December 2005 for Tim Breedon and Andrew Palmer respectively, are £131,000 and £194,000 higher than the figures disclosed in the 2005 Annual Report and Accounts. The amounts disclosed at 31 December 2005 in the table above reflect a bonus sacrifice amounts in March 2005 which were not shown in the equivalent table in the prior year.

The increase in accrued pension during the year excludes any increase for inflation.

On retirement from Legal & General at age 60 and subject to statutory limits, executive directors are entitled to pensions as follows:

• Andrew Palmer and Robin Phipps: two thirds of their annual salary.
• Tim Breedon and John Pollock: one sixtieth of eligible salary for each year of service through to the date they opted for enhanced protection. Since opting for enhanced protection on 6 April 2006 they have received a cash supplement in lieu of pension accrual as shown in the Directors' Remuneration table. Consistent with the legislation their pensionable earnings at their retirement will be used to determine their ultimate pension entitlements.
• Kate Avery: one sixtieth of eligible salary for each year of service.

On death in service, a capital sum equal to four times salary is payable, together with a spouse's pension of four ninths of the member's pensionable remuneration. Protection is also offered in the event of serious ill health. This latter benefit has no transfer value in the event of the insured leaving service.

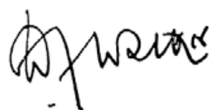
Directors, like all managers, may elect, before its award, to sacrifice all or part of their cash bonus into pension.

Directors' Loans
At 31 December 2006 and 31 December 2005 there were no loans outstanding made to directors.

Service Contracts
The policy and practice for the notice entitlement of all executive directors is a six month rolling notice period, plus a six months' salary, pension and car allowance entitlement on termination. These entitlements may be mitigated and/or spread over the period of notice. Copies of executive directors' service contracts are available for inspection during normal working hours at the registered office. The date of the contract is the appointment date in the section on directors.

External Appointments
The Company considers that certain external appointments can help to broaden the experience and capability of the executive directors. Any such appointments are subject to annual agreement by the Remuneration Committee and must not be with competing companies. Subject to the Committee's agreement, any fees may be retained by the individual. Tim Breedon receives £15,000 as a director of the Financial Reporting Council, Andrew Palmer receives fees of £44,000 as a non-executive director of Slough Estates plc and Kate Avery receives fees of £30,000 as a non-executive director of Kelda Group plc. Robin Phipps is an unpaid director of the ABI.

The Directors' Report on Remuneration was approved by the directors on 12 March 2007.



Sir David Walker
Chairman of the Remuneration Committee

Independent Verification Review
New Bridge Street Consultants LLP (NBSC) act as advisers to the Remuneration Committee. In addition, they were asked to verify that the 2006 remuneration practice for executive directors followed the Remuneration Policy put to the 2006 Annual General Meeting. In conducting this work, NBSC has reviewed the elements of executive director remuneration during 2006, as detailed in the policy statements of the Directors' Report on Remuneration 2005 (DRR 2005). They confirmed that they are satisfied that the remuneration practice during 2006 has been in line with the stated policy set out in the DRR 2005.

Summary of the Role of the Audit Committee
The Audit Committee is appointed by the Board from the non-executive directors of Legal & General Group Plc. It is a Committee of the Board established pursuant to Article 113 of the Articles of Association.

The Audit Committee's terms of reference include all matters indicated by the Combined Code, except the oversight of compliance risks, (including adherence to the Financial Services and Markets Act 2000), which is the direct responsibility of the Board. (The Group Risk & Compliance Committee, which reports to the Group Board and whose minutes are copied to the Audit Committee, supervises the Group's Risk Framework and therefore considers all risks including compliance risk.) The terms of reference are considered annually by the Audit Committee and are then referred to the Board for approval.

The primary objective of the Audit Committee is to assist the Board of Directors in fulfiling its responsibilities relating to:

- external financial reporting and associated announcements;
- the independence of the Group's external auditor;
- the resourcing, plans and overall effectiveness of the internal audit department;
- the adequacy and effectiveness of the control environment; and
- the Group's compliance with the Combined Code on Corporate Governance.

The Audit Committee Chairman reports the outcome of meetings to the Board, and the Board receives the minutes of all Committee meetings.

The Audit Committee has unrestricted access to Company documents and information, as well as to employees of the Company and the external auditor.

Composition of the Audit Committee
The members of the Audit Committee are:

	Date of appointment
Henry Staunton	26 July 2004 and appointed Chairman on 27 April 2005
Frances Heaton	14 November 2001
Barrie Morgans	5 March 1998 and resigned on 18 May 2006
James Strachan	21 January 2004

Membership of the Committee is reviewed by the Chairman of the Committee, Henry Staunton, and the Group Chairman, who is not a member of the Audit Committee, at regular intervals.

Where necessary, they will recommend new appointments to the Nominations Committee for onward recommendation to the Board. Appointments are for a period of three years and are extendible by no more than two additional three year periods. The Committee is normally comprised of four independent non-executive directors, with a minimum of three members at any time. Three members constitute a quorum.

The Audit Committee structure requires the inclusion of one financially qualified member (as recognised by the Consultative Committee of Accountancy Bodies). Currently the Audit Committee Chairman fulfils this requirement.

All Audit Committee members are expected to be financially literate and to have relevant corporate finance experience.

The Group provides an induction programme for new Audit Committee members and ongoing training to enable all of the Committee members to carry out their duties. The induction programme covers the role of the Audit Committee, its terms of reference and expected time commitment by members; and an overview of the Group's business, including the main business and financial dynamics and risks. New Committee members also meet some of the Group's staff. ongoing training includes attendance at formal conferences, internal Company seminars and briefings by external advisers.

The Board expects the Audit Committee members to have an understanding of the following areas:

- the principles of, contents of, and developments in financial reporting including the applicable accounting standards and statements of recommended practice;
- key aspects of the Company's operations and risk control framework including corporate policies, company financing, products and systems of internal control;
- matters that influence or distort the presentation of accounts and key figures;
- the principles of, and developments in, company law, sector-specific laws and other relevant corporate legislation;
- the role of internal and external auditing and risk management;
- the regulatory framework for the Group's businesses;
- environmental and social responsibility best practices; and
- current issues pertaining to the above areas.

Meetings
The Audit Committee is required to meet four times per year and has an agenda linked to events in the Group's financial calendar. The agenda is predominantly cyclical and is therefore approved by the Audit Committee Chairman on behalf of his fellow members; each Audit Committee member has the right to require reports on matters of interest in addition to the cyclical items.

The Audit Committee invites the Group Chief Executive, Group Director (Finance), Group Financial Controller, Group Chief Internal Auditor, Group Actuary and senior representatives of the external auditor to attend all of its meetings in full, although it reserves the right to request any of these individuals to withdraw. Other senior management are invited to present such reports as are required for the Committee to discharge its duties.

Overview of the Actions Taken by the Audit Committee to Discharge its Duties
In order to fulfil its terms of reference, the Audit Committee receives and challenges presentations or reports from the Group's senior management, consulting as necessary with senior representatives of the external auditor and the independent actuaries.

The Audit Committee is required to assist the Board to fulfil its responsibilities relating to external financial reporting and associated announcements. The Committee reviewed the interim and annual financial statements, together with the associated Stock Exchange announcements, having received information on:

- the accounting principles, policies and practices adopted in the Group's accounts;
- changes proposed to those principles, policies and practices;
- significant accounting issues;
- current actuarial issues;
- the level of insurance provisions and reserves;
- litigation and contingent liabilities affecting the Group; and
- potential tax contingencies and the Group's compliance with statutory tax obligations.

The Audit Committee is required to assist the Board to fulfil its responsibilities relating to the adequacy and effectiveness of the control environment and the Group's compliance with the

Combined Code. To fulfil these duties, the Committee reviewed:

- the report entitled 'Directors' view on Internal Controls' submitted to the Audit Committee by the Group Risk & Compliance Committee which sets out the framework of risk management, control monitoring, and any control issues that have arisen;
- the minutes of the Group Risk & Compliance Committee meetings during 2006;
- the annual Internal Control Report for 2005 presented by the external auditor;
- Internal Audit reports on key audit areas and significant control environment deficiencies; and
- reports on frauds perpetrated against the Group and current fraud trends.

The Audit Committee Chairman reports back to the Committee on the Group Risk & Compliance Committee meetings which he attends.

During the year the Audit Committee undertook a formal review of its own effectiveness and is satisfied that it had been operating as an effective Audit Committee meeting all applicable legal and regulatory requirements. These reviews are undertaken annually.

External Audit

The Audit Committee is responsible for the development, implementation and monitoring of the Group's policy on external audit. The policy assigns oversight responsibility for monitoring the independence, objectivity and compliance with ethical and regulatory requirements to the Audit Committee, and day-to-day responsibility to the Group Director (Finance). The policy states that the external auditor is jointly responsible to the Board and the Audit Committee and that the Audit Committee is the primary contact.

The Group's policy on external audit sets out the categories of non-audit services which the external auditor will and will not be allowed to provide to the Group. The policy requires pre-confirmation by the Audit Committee of any non-audit work subject to de minimis levels.

To fulfil its responsibility regarding the independence of the external auditors, the Audit Committee reviewed:

- the changes in key external audit staff in the plan for the current year presented by the external auditor;
- the arrangements for day-to-day management of the audit relationship;
- a report identifying the number of external audit staff now employed by the Group and their positions within the Group;
- a report from the external auditor describing their arrangements to identify, report and manage any conflicts of interest; and
- the overall extent of non-audit services provided by the external auditor, in addition to their case-by-case approval of the provision of non-audit services by the external auditor.

To assess the effectiveness of the external auditor, the Audit Committee reviewed:

- the fulfilment of the agreed audit plan and variations from the plan undertaken by the external auditor;
- the robustness and perceptiveness of the external auditor in handling the key accounting and audit judgements; and
- the content of the Internal Control Report presented by the external auditor.

To fulfil its responsibility for oversight of the external audit process, the Audit Committee reviewed:

- the terms, areas of responsibility, associated duties and scope of the audit as set out in the engagement letter for the forthcoming year from the external auditor;
- the overall work plan for the forthcoming year presented by the external auditor;
- the fee proposal presented by the external auditor;
- the major issues that arose during the course of the audit and their resolution;
- the key accounting and audit judgements;
- the levels of errors identified during the audit; and
- the recommendations made by the external auditor in the management letter, entitled 'The Internal Control Report', and the adequacy of management's response.

During 2006, the Audit Committee supervised the tender for the position of external auditor and, on the basis of the tender submissions and as a consequence of its satisfaction with the results of the activities outlined above, the Audit Committee has recommended to the Board that PricewaterhouseCoopers LLP is reappointed as external auditor.

Internal Audit Function

The Audit Committee is committed to supporting Internal Audit and maintaining its ongoing relationship with the department to enable Internal Audit to assist the Committee to fulfil its statutory responsibilities in relation to the adequacy and effectiveness of the control environment and the Group's compliance with the Combined Code.

The Audit Committee is also required to assist the Board to fulfil its responsibilities relating to the adequacy of the resourcing, plans and overall effectiveness of the Internal Audit department.

To fulfil all of these responsibilities, the Committee reviewed:

- Internal Audit's plans for 2006 and its achievement of the planned activity;
- the results of key audits and other significant findings, the adequacy of management's response and the timeliness of resolution;
- statistics on staff numbers, qualifications and experience and timeliness of reporting; and
- the level and nature of non-audit activity performed by Internal Audit.

The Group's Public Interest Disclosure Policy (the 'Whistleblowing' Policy) sets out arrangements for employees, contractors and third parties to raise concerns or complaints regarding accounting, risk issues, internal controls, auditing issues and related matters with relevant line management or senior Group managers. These are escalated to the Group Chief Internal Auditor (GCIA) in confidence, for reporting to the Audit Committee as appropriate.

The Audit Committee holds private meetings with the external auditors and with the GCIA after Committee meetings to review key issues within their spheres of interest and responsibility as considered necessary.

The GCIA reports functionally to the Committee and administratively to the Group Director (Finance). The GCIA has a private meeting with the Audit Committee Chairman at least four times during the course of the year and has regular monthly meetings with the Group Chief Executive and the Group Director (Finance) where key risk and control issues are discussed.

The Chairman of the Audit Committee will be present at the AGM to answer questions, through the Chairman of the Board, on the report on the Audit Committee's activities, matters within the scope of the Audit Committee's responsibilities and any significant matters brought to the Audit Committee's attention by the external auditor.

The Corporate Governance pages of the Legal & General website provide supplementary information including the terms of reference for the Audit Committee and the Group's policy on external audit.

The Committee is chaired by the Chairman of the Board and comprises all the non-executive directors. The meetings may be attended by executive directors, as appropriate.

The Nominations Committee leads the process for Board appointments and makes recommendations to the Board.

All members of the Committee are independent, non-executive directors. The Chairman does not chair the Nominations Committee when it is dealing with the appointment of a successor to the Chairmanship, in which case the Committee is chaired by the Senior Independent Director. The Committee met twice during 2006.

Duties

The Committee is responsible for identifying and nominating, for the approval of the Board, candidates to fill Board vacancies as and when they arise. Before making an appointment, the Committee evaluates the balance of skills, knowledge and experience on the Board and, in the light of this evaluation, prepares a description of the role and capabilities required for a particular appointment.

The Committee reviews annually the time required from a non-executive director. The annual performance evaluation is used to assess whether the non-executive director is spending enough time to fulfil his or her duties. Candidates from a wide range of backgrounds are considered. The Committee uses external advisers to facilitate searches for potential candidates.

The Committee gives full consideration to succession planning in the course of its work, taking into account the challenges and opportunities facing the Company and what skills and expertise are therefore needed on the Board in the future. The Committee reviews the structure, size and composition (including the skills, knowledge and experience) of the Board and, if appropriate, makes recommendations to the Board. In this respect, the Committee has regard to the results of the annual performance evaluation. The Committee keeps under review the leadership needs of the organisation, both executive and non-executive, with a view to ensuring the continued ability of the organisation to compete effectively in the marketplace.

Activities

The Committee makes recommendations to the Board on succession for executive directors, the reappointment of any non-executive director at the conclusion of their specified term of office, any matter relating to the continuation in office of any director at any time and the appointment of any director to executive or other office.

During 2006 the Nominations Committee recommended to the Board the appointment of Rudy Markham as a non-executive director. The Board adopted this proposal.

Corporate Website

The terms of reference of the Committee, which sets out the role and the authority delegated to it by the Board, are available for inspection at the Company's registered office and can be viewed on the Company's website.

The formal letters of appointment of non-executive directors are also available for inspection at the Company's registered office and can be viewed on the Company's Corporate website, www.legalandgeneralgroup.com.

Legal & General Group Plc is the ultimate holding company for a group of insurance, investment management and financial services companies. The Company's principal operating subsidiaries are set out on pages 99 and 100.

Business Review

Information on the Group's principal activities together with a review of the development and performance of the Group, including financial performance in accordance with Section 234ZZB Companies Act 1985 is set out on pages 9 to 33.

The Key Performance Indicators (KPIs) are defined in the table opposite. The KPIs for the Group in 2006 are shown in the following table:

	2006	2005
EEV operating profit	£1,233m	£1,092m
IFRS operating profit	£752m	£647m
Return on embedded value	12.5%	12.6%
IGD surplus*	£2.1bn	£2.4bn
Three year total shareholder return	80%	50%

*Figures extracted from draft regulatory returns

The Principal Risks and Uncertainties facing the Group are set out on page 27.

Result for the Year

The IFRS profit attributable to equity holders of the Company for the financial year was £1,564m (2005: £944m profit) and the earnings per share were 24.12p (2005: 14.33p). The consolidated balance sheet on page 56 and the consolidated income statement on page 55 show the affairs of the Group as at, and for the year ended, 31 December 2006. An analysis of worldwide gross written premiums is shown on page 70, Note 4(iv).

Dividend

The directors recommend the payment of a final dividend of 3.81p per share. With the interim dividend of 1.74p per share paid on 2 October 2006, this brings the total dividend recommended for 2006 to 5.55p per share (2005: 5.28p), an increase of 5.1%. The final dividend will be paid on 21 May 2007 to members registered at the close of business on 20 April 2007. The cost of the dividend paid for the year is £349m. The retained profit was £1,215m.

Directors

A list of the current directors of the Company, together with biographical notes, is shown on pages 32 and 33. All current directors remained in office throughout 2006 with the exception of Rudy Markham, who was appointed on 1 October 2006. Barrie Morgans retired from the Board at the conclusion of the Annual General Meeting (AGM) on 18 May 2006.

The following changes are proposed in 2007:

Beverley Hodson will retire from the Board at the conclusion of the AGM on 16 May 2007.

The directors retiring by rotation at the AGM are, Kate Avery, John Pollock, Dr Ronaldo Schmitz and James Strachan who, being eligible, offer themselves for re-election.

Rudy Markham has been appointed since the last AGM and, being eligible, offers himself for election.

Kate Avery and John Pollock have service contracts which are terminable by them or the Company on receipt of no less than six months' written notice. On termination, they would become entitled to six months' salary and benefits.

The terms and conditions of Rudy Markham, James Strachan and Dr Ronaldo Schmitz's appointment are available for inspection at the Company's registered office and at the AGM.

KPI Definitions

EEV Operating Profit

Definition: Legal & General provides supplementary financial statements prepared on the European Embedded Value (EEV) basis for long term insurance contracts (see pages 117 to 133). The EEV figures provide an assessment of the value which has been generated by the business during a period.

Calculation: Operating profit on the EEV basis reports the change in embedded value in a period, but excludes fluctuations from assumed longer term investment return.

Purpose: In the Board's opinion, EEV operating profit provides shareholders with a better understanding of the Group's performance than IFRS, as it provides information about the value which is being created on the Group's long term insurance contracts.

IFRS Operating Profit

Definition: The Group's primary financial statements (see pages 55 to 116) are prepared on the International Financial Reporting Standards (IFRS) basis which all EU listed companies are required to follow.

Calculation: IFRS operating profit measures the pre-tax result using an assumed longer term investment return. Any variance between actual and assumed investment return is reported below operating profit. For UK life and pensions, the maximum operating profit is based on a formula agreed with the FSA which is set out in Note 3(iv) of the Financial Statements.

Purpose: IFRS operating profit gives an insight into the Group's ability to generate cash flows to support dividends during a period.

Return on Embedded Value (ROEV)

Definition: ROEV measures the return earned by shareholders on shareholder capital retained within the business.

Calculation: ROEV is calculated as EEV operating profit after tax divided by opening EEV shareholders' funds.

Purpose: ROEV provides a link between performance and balance sheet management and ensures that an optimal balance is maintained.

IGD Surplus

Definition: The IGD surplus is an FSA regulatory measure which calculates surplus capital within the Group.

Calculation: IGD surplus is defined as Group regulatory capital employed less the Group regulatory capital requirement. Surplus capital held within our Society Long Term Fund cannot be included in the IGD definition of capital employed.

Purpose: IGD surplus is the dominant regulatory surplus capital measure for the Group.

Total Shareholder Return (TSR)

Definition: 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.

Calculation: TSR is the change in share price over a three year performance period, plus the value of reinvested dividends, relative to the performance of all the other companies in the FTSE 100.

Purpose: TSR measures total return to shareholders over the medium term.

The Directors' Report on Remuneration on pages 40 to 47 provides details of the current incentive schemes, the interests of directors in the share capital of the Company and details of their share options and other long term incentives.

The changes in directors' share interests between 31 December 2006 and 13 March 2007 are outlined in the tables below.

The executive directors' share purchases were made pursuant to their participation in the Employee Share Plan:

	2 January 2007	1 February 2007	1 March 2007
Tim Breedon	90	92	92
Kate Avery	90	92	92
Andrew Palmer	91	91	92
Robin Phipps	90	92	91
John Pollock	90	92	92

The non-executive directors acquired shares pursuant to the regular monthly purchase of shares as part of their remuneration.

	2 January 2007	1 February 2007	1 March 2007
Sir Rob Margetts	4,260	4,998	5,177
Frances Heaton	916	915	947
Beverley Hodson	916	915	947
Rudy Markham[1]	nil	nil	nil
Ronaldo Schmitz	916	915	947
Henry Staunton	1,225	1,223	1,267
James Strachan	916	915	947
Sir David Walker	1,225	1,223	1,267

1. See Remuneration Report for explanation of Rudy Markham's fee arrangements.

United Kingdom Employees

It is the Group's policy to treat its employees without discrimination and to operate equal opportunity employment practices designed to achieve this end.

Furthermore, it is the Group's policy to give full and fair consideration to applications for employment made by disabled persons; to continue, wherever possible, the employment of staff who become disabled and to provide equal opportunities for the training and career development of disabled employees.

The Group seeks to achieve an awareness among staff of corporate objectives and performance, financial and economic factors affecting the business and other matters of concern to them as employees. During the year, staff were provided with information through briefings by managers, training courses, email bulletins, staff newspapers and circulars.

The Company operates a savings related share option scheme (SAYE), a Company Share Option Plan and an Employee Share Plan, all of which are approved by Her Majesty's Revenue & Customs (HMRC).

Details of employee share schemes and long term incentives are included in the Directors' Report on Remuneration on Pages 40 to 47.

Purchase of Own Shares

The directors propose to seek shareholders' approval to increase from 5%-10% the authority for the Company to purchase its own shares up to a total of 653,252,004 ordinary shares of 2.5p each, having an aggregate nominal value of £16,331,300, being 10% of the issued nominal ordinary share capital as at 13 March 2007 (being the last practicable date prior to publication of the AGM Notice). A Special Resolution seeking shareholders' authority is set out in the notice of the AGM in the accompanying Circular to Shareholders.

Share Capital

As at 13 March 2007, the Company had received notifications from Aviva and its subsidiary companies, Swiss Reinsurance Company group of companies and Barclays Plc of holdings of the Company's share capital with voting rights amounting to 3.14%, 3.14% and 4.01%, respectively.

Resolution 11, set out in the notice of the AGM, will authorise the directors to allot up to an aggregate nominal amount of £8,165,650, being 5% of the total issued capital as at 13 March 2007 (being the last practicable date prior to publication of the AGM Notice).

Resolution 12, set out in the notice of the AGM, will authorise the directors to issue further shares up to the equivalent of 5% of the Company's issued share capital as at 13 March 2007 (being the last practicable date prior to publication of the AGM Notice) for cash without offering the shares first to existing shareholders by way of rights. It is not intended, without prior consultation with the Investment Committee of the Association of British Insurers, to issue in this way more than 7.5% of the unissued share capital in any rolling three year period. The resolution will also authorise the directors to allot shares in connection with a rights issue otherwise than strictly pro rata where practical considerations, such as fractions and foreign securities laws, make this desirable.

Details of the number, the consideration and the reason for the issue of shares by the Company during the year are set out on page 83, Note 28.

Other than the above, the directors have no current intention of issuing further share capital and no issue will be made which would effectively alter control of the Company without prior approval of the members in general meeting.

Directors' Indemnities

On 3 January 2006, the Company agreed in writing to indemnify each of the directors against any liability incurred by the director in respect of acts or omissions arising in the course of their office. The indemnity only applies to the extent permitted by law. Copies of the Deeds of Indemnity are available for inspection at the Registered Office and at the AGM.

Risk Management and Control

Details of the Company's risk management and control policies are disclosed in Note 51 to the Financial Statements on pages 106 to 116.

Insurance

Legal & General maintains an appropriate level of Directors' and Officers' liability insurance which is reviewed annually.

Environment

Details of the Group's commitment to environmental issues, as part of its Corporate Social Responsibility programme, are set out on pages 28 to 31.

United Kingdom Donations

During 2006, charitable donations totalling £2.3m (2005: £1.3m) were made. In 2005 purely charitable donations were disclosed. In 2006 both charitable donations and charitable sponsorship have been disclosed. No political donations were made during the year (2005: none).

Payments to Suppliers

The Group agrees terms and conditions for its business transactions with suppliers. Payment is made in accordance with these terms provided the supplier meets its obligations.

The Company has no trade creditors. As at 31 December 2006, the average number of days of payments outstanding for the Legal & General Group of companies was 31 (2005: 33).

Auditors
A resolution to re-appoint PricewaterhouseCoopers LLP as auditors to the Company will be proposed at the AGM.

Disclosure of Information to Auditors
Each of the directors at the date of approval of this report confirms that:
1. so far as the director is aware, there is no relevant information of which the Company's auditors are unaware; and
2. the director has taken all the steps that he/she ought to have taken as a director to make himself/herself aware of any relevant information and to establish that the Company's auditors are aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of Section 234ZA of the Companies Act 1985.

On behalf of the Board

Claire Davies
Group Secretary
13 March 2007

Statement of Directors' Responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the Group and of the profit or loss of the Group for that period, and which comply with the relevant provisions of the Companies Act 1985. In preparing those financial statements, the directors are required to:
- select suitable accounting policies and then apply them consistently;
- make judgements and estimates which are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The directors confirm that they comply with the above requirements. The directors are also responsible for:
- ensuring that the Company and Group have suitable internal controls for maintaining proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and of the Group;
- safeguarding the assets of the Company and the Group; and
- taking reasonable steps for the prevention and detection of fraud and other irregularities.

To the Members of Legal & General Group Plc

We have audited the Group financial statements of Legal & General Group Plc for the year ended 31 December 2006 which comprise the Consolidated Income Statement, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement, the Consolidated Statement of Recognised Income and Expense and the related notes. These Group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of Legal & General Group Plc for the year ended 31 December 2006 and on the information in the Directors' Remuneration Report that is described as having been audited.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the Group financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the Group financial statements give a true and fair view and whether the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the Group financial statements. The information given in the Directors' Report includes that specific information presented in the Operating and Financial Review that is cross-referred from the Business Review section of the Directors' Report.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the Combined Code 2003 specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited Group financial statements. The other information comprises only the Directors' Report, the unaudited part of Directors' Report on Remuneration, the Chairman's Statement, the Group Chief Executive's Review, the Operating and Financial Review, the Report of the Audit Committee, the Report of the Nominations Committee and the Corporate Governance Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Group financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the Group financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Group financial statements.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 December 2006 and of its profit and cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the Directors' Report is consistent with the Group financial statements.

Separate opinion in relation to IFRSs

As explained in Note 1 to the Group financial statements, the Group in addition to complying with its legal obligation to comply with IFRSs as adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board.

In our opinion the Group financial statements give a true and fair view, in accordance with IFRSs, of the state of the Group's affairs as at 31 December 2006 and of its profit and cash flows for the year then ended.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
13 March 2007

(a) The financial statements are published on the website of Legal & General Group Plc, www.legalandgeneralgroup.com. The maintenance and integrity of the Legal & General Group Plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

For the year ended 31 December 2006

	Notes	2006 £m	2005 £m
Revenue			
Gross written premiums	4	**4,286**	4,084
Outward reinsurance premiums		**(518)**	(406)
Net change in provision for unearned premiums		**7**	(6)
Net premiums earned		**3,775**	3,672
Fees from fund management and investment contracts		**535**	348
Investment return	6	**16,572**	26,931
Operational income		**84**	38
Total revenue	4	**20,966**	30,989
Expenses			
Claims and change in insurance liabilities		**1,938**	6,367
Reinsurance recoveries		**1,123**	19
Net claims and change in insurance liabilities	7	**3,061**	6,386
Change in provisions for investment contract liabilities		**13,878**	21,369
Acquisition costs		**987**	550
Finance costs		**153**	116
Other expenses	8	**674**	619
Transfers to unallocated divisible surplus		**284**	360
Total expenses	4	**19,037**	29,400
Profit before income tax	11	**1,929**	1,589
Income tax attributable to policyholder returns	13	**89**	(206)
Profit from continuing operations before income tax attributable to equity holders		**2,018**	1,383
Total income tax expense	13	**(298)**	(577)
Income tax attributable to policyholder returns	13	**(89)**	206
Income tax attributable to equity holders	13	**(387)**	(371)
Profit from continuing operations after income tax		**1,631**	1,012
Profit from discontinued operations	14	**–**	13
Profit from ordinary activities after income tax		**1,631**	1,025
Attributable to:			
Minority interests	31	**67**	81
Equity holders of the Company		**1,564**	944
Dividend distributions to ordinary equity holders of the Company during the year	15	**349**	331
Distributions during the year on subordinated borrowings designated as equity	15	**–**	16
Dividend distributions to ordinary equity holders of the Company proposed after the year end	15	**248**	236

		p	p
Earnings per share	16		
Based on profit from continuing operations after income tax attributable to ordinary equity holders		**24.12**	14.13
Based on profit attributable to ordinary equity holders of the Company		**24.12**	14.33
Diluted earnings per share	16		
Based on profit from continuing operations after income tax attributable to ordinary equity holders		**23.95**	13.76
Based on profit attributable to ordinary equity holders of the Company		**23.95**	13.95

As at 31 December 2006

	Notes	2006 £m	2005 £m
Assets			
Investment in associates	48	**16**	16
Plant and equipment	18	**43**	32
Investment property	19	**6,852**	5,774
Financial investments	20	**201,430**	176,622
Reinsurers' share of contract liabilities	22	**1,481**	2,779
Purchased interest in long term businesses	23	**23**	25
Deferred acquisition costs	24	**1,456**	1,375
Income tax recoverable	25	**12**	79
Other assets	26	**1,622**	1,162
Cash and cash equivalents	27	**4,930**	4,001
Total assets	4	**217,865**	191,865
Equity			
Share capital	28	**163**	163
Share premium account	28	**923**	908
Treasury shares	28	**(45)**	(36)
Other reserves	29	**49**	34
Retained earnings	30	**4,335**	3,188
Capital and reserves attributable to ordinary equity holders of the Company		**5,425**	4,257
Subordinated borrowings designated as equity	38	**–**	394
Capital and reserves attributable to equity holders of the Company		**5,425**	4,651
Minority interests	31	**414**	285
Total equity	4/32	**5,839**	4,936
Liabilities			
Subordinated borrowings	38	**818**	415
Participating insurance contracts	33	**12,660**	13,180
Participating investment contracts	34	**7,501**	7,476
Unallocated divisible surplus	35	**2,178**	1,894
Value of in-force non-participating contracts	36	**(391)**	(379)
Participating contract liabilities		**21,948**	22,171
Non-participating insurance contracts	33	**21,602**	23,152
Non-participating investment contracts	34	**162,016**	135,804
Non-participating contract liabilities		**183,618**	158,956
Senior borrowings	38	**1,607**	1,634
Provisions	40	**568**	582
Deferred income liabilities	41	**422**	351
Deferred tax liabilities	42	**472**	492
Income tax liabilities	25	**106**	197
Other liabilities	43	**1,663**	1,303
Net asset value attributable to unitholders		**804**	828
Total liabilities	4	**212,026**	186,929
Total equity and liabilities		**217,865**	191,865

The notes on pages 59 to 116 form an integral part of these financial statements.

The financial statements on pages 55 to 116 and the supplementary financial statements on pages 117 to 133 were approved by the directors on 13 March 2007 and were signed on their behalf by:

Rob Margetts

Sir Rob Margetts
Chairman

Tim Breedon
Group Chief Executive

Andrew Palmer
Group Director (Finance)

For the year ended 31 December 2006

	2006 £m	2005 £m
Fair value losses on cash flow hedges	**(3)**	–
Exchange differences on translation of overseas operations	**(35)**	20
Actuarial gains/(losses) on defined benefit pension schemes	**3**	(55)
Actuarial (gains)/losses on defined benefit pension schemes transferred to unallocated divisible surplus	**(1)**	22
Net change in financial investments designated as available-for-sale	**7**	(10)
Net[1] expense recognised directly in equity	**(29)**	(23)
Profit from ordinary activities after income tax	**1,631**	1,025
Total recognised income and expense	**1,602**	1,002
Attributable to:		
Minority interests	**67**	81
Equity holders of the Company	**1,535**	921

1. Net of tax.

Consolidated Cash Flow Statement

For the year ended 31 December 2006

	Notes	2006 £m	2005 £m
Cash flows from operating activities			
Profit from ordinary activities after income tax		**1,631**	1,025
Adjustments for non cash movements in net profit for the period			
Realised and unrealised gains on financial investments and investment properties		**(9,505)**	(20,962)
Investment income		**(6,630)**	(5,646)
Interest expense		**153**	116
Income tax payable		**298**	577
Other adjustments		**46**	40
Net (increase)/decrease in operational assets			
Investments designated as held for trading or fair value through profit or loss		**(9,599)**	(16,519)
Investments designated as available-for-sale		**(251)**	86
Other assets		**557**	(294)
Net increase/(decrease) in operational liabilities			
Insurance contracts		**(1,893)**	3,071
Transfer to unallocated divisible surplus		**285**	338
Investment contracts		**19,527**	33,173
Value of in-force non-participating contracts		**(12)**	55
Other liabilities		**596**	536
Cash used in operations		**(4,797)**	(4,404)
Interest paid		**(146)**	(96)
Interest received		**3,478**	2,967
Income tax paid		**(315)**	(240)
Dividends received		**3,095**	2,576
Net cash flows from operating activities		**1,315**	803
Cash flows from investing activities			
Net acquisition of plant and equipment		**(24)**	(22)
Net proceeds from disposal of Ventures' investments	14	**10**	23
Net proceeds from disposal of Gresham	14	**–**	73
Non-financial investments purchased		**(3)**	(19)
Net cash flows from investing activities		**(17)**	55
Cash flows from financing activities			
Dividend distributions to ordinary equity holders of the Company during the year		**(349)**	(331)
Distributions during the year on subordinated borrowings designated as equity		**–**	(16)
Proceeds from issue of ordinary share capital		**15**	1
Purchase of treasury shares		**(11)**	(15)
Proceeds from borrowings		**1,062**	764
Repayment of borrowings		**(1,051)**	(257)
Other		**–**	(1)
Net cash flows from financing activities		**(334)**	145
Net increase in cash and cash equivalents		**964**	1,003
Exchange (losses)/gains on cash and cash equivalents		**(35)**	6
Cash and cash equivalents at 1 January		**4,001**	2,992
Cash and cash equivalents at 31 December	27	**4,930**	4,001

The Group's consolidated cash flow statement includes all cash and cash equivalent flows, including those relating to the UK Long Term Funds.

1. ACCOUNTING POLICIES

Basis of preparation

The Group financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) and as adopted by the European Commission (EC) for use in the European Union. The Group's financial statements also comply with IFRSs as issued by the IASB.

The Group presents its balance sheet broadly in order of liquidity. This is considered to be more relevant than a before or after twelve months presentation, given the long term nature of the Group's core business. However, for each asset and liability line item which combines amounts expected to be recovered or settled before and after twelve months from the balance sheet date, disclosure of the split is made by way of note.

Financial assets and financial liabilities are disclosed gross in the balance sheet unless a legally enforceable right of offset exists and there is an intention to settle recognised amounts on a net basis. Income and expenses are not offset in the income statement unless required or permitted by any accounting standard or International Financial Reporting Interpretations Committee (IFRIC) interpretation, as detailed in the applicable accounting policies of the Group.

Use of estimates

The preparation of the financial statements includes the use of estimates and assumptions which affect items reported in the consolidated balance sheet and income statement and the disclosure of contingent assets and liabilities at the date of the financial statements. Although these estimates are based on management's best knowledge of current circumstances and future events and actions, actual results may differ from those estimates, possibly significantly. The significant estimates and assumptions used are disclosed in the relevant notes to these financial statements.

Summary of significant accounting policies

The Group has selected accounting policies which fairly state its financial position and financial performance for a reporting period. These accounting policies are applied after an assessment of complex issues, and may require subjective judgments to be made. Such judgments relate to insurance and investment contract liabilities and associated balances, deferred acquisition costs, pension schemes and the determination of fair values of unquoted financial investments.

The principal accounting policies adopted in preparing these financial statements are set out below. The accounting policies have been consistently applied to all years presented, unless otherwise stated.

Consolidation principles

Subsidiary undertakings

The consolidated financial statements incorporate the assets, liabilities, equity, revenues, expenses and cash flows of the Company and of its subsidiary undertakings drawn up to 31 December each year. All intra-group balances, transactions, income and expenses are eliminated in full. Subsidiaries are those entities (including special purpose entities, mutual funds and unit trusts) over which the Group directly or indirectly has the power to govern the operating and financial policies in order to gain economic benefits. Profits or losses of subsidiary undertakings sold or acquired during the period are included in the consolidated results up to the date of disposal or from the date of gaining control.

Associates and joint ventures

Associates are entities over which the Group has significant influence but which it does not control. Consistent with International Accounting Standard (IAS) 28, 'Investments in Associates', it is presumed that the Group has significant influence where it has between 20% and 50% of the voting rights in the investee. Joint ventures are entities where the Group and other parties undertake an activity which is subject to joint control.

The Group has interests in associates and joint ventures which form part of an investment portfolio held through venture capital partnerships, mutual funds, unit trusts and similar entities. In accordance with the choices permitted by IAS 28 and IAS 31, 'Interests in Joint Ventures', these interests have been classified as fair value through profit or loss and measured at fair value, with changes in fair value recognised in the income statement.

Associates which do not form part of an investment portfolio are initially recognised in the balance sheet at cost. The carrying amount of the associate is increased or decreased to reflect the Group's share of the profit or loss after the date of the acquisition.

Investment vehicles

Investment vehicles such as Open Ended Investment Companies, where a Group company exerts control over financial and operating policy, are consolidated. The interests of parties other than the Group in such vehicles are classified as liabilities and appear as 'Net asset value attributable to unitholders' in the consolidated balance sheet.

Product classification

The Group's products are classified for accounting purposes as either insurance contracts (participating and non-participating) or investment contracts (participating and non-participating). Insurance contracts are contracts which transfer significant insurance risk to the insurer at the inception of the contract. Contracts which do not transfer significant insurance risk to the insurer are classified as investment contracts. Hybrid contract types, containing both insurance and investment features, have been treated as investment contracts when accounting for premiums, claims and other revenue.

A number of insurance and investment contracts contain discretionary participating features (DPF) which entitle the policyholders to receive guaranteed benefits as well as additional benefits:

- the amount or timing of which is contractually at the discretion of the Group; and
- which are contractually based on:
    - the performance of a specified pool of contracts or a specified type of contract;
    - realised and/or unrealised investment returns on a specified pool of assets held by the issuer; or
    - the profit or loss of the Company, fund or other entity which issues the contract.

Contracts with DPF are referred to as participating contracts. Participating contracts consist of most with-profits contracts in the UK and most Guarantie Long Term contracts in France.

Long term insurance contracts

Premium income

Premiums are recognised as revenue when the liabilities arising from them are created. All other premiums, including annuity considerations, are accounted for when due for payment.

Claims

Death claims are accounted for on notification of death. Surrenders for non-linked policies are accounted for when payment is made. Critical illness claims are accounted for when admitted. All other claims and surrenders are accounted for when payment is due. Claims payable include the direct costs of settlement.

1. ACCOUNTING POLICIES continued

Acquisition costs
Acquisition costs comprise direct costs, such as initial commission, and the indirect costs of obtaining and processing new business. Acquisition costs relating to non-participating insurance contracts written outside the with-profits part of the UK Long Term Funds (LTF) which are incurred during a financial year are deferred by use of an asset which is amortised over the period during which the costs are expected to be recoverable, and in accordance with the expected incidence of future related margins. For participating contracts, acquisition costs are charged to the income statement when incurred.

Insurance contract liabilities
Under current IFRS requirements, insurance contract liabilities are measured using local Generally Accepted Accounting Principles (GAAP), as permitted by IFRS 4, 'Insurance Contracts'.

In the UK, insurance contract liabilities are determined following an annual investigation of the LTF in accordance with regulatory requirements. The liabilities are calculated on the basis of current information and using the gross premium valuation method. For participating contracts the liabilities to policyholders are determined on a realistic basis in accordance with Financial Reporting Standard (FRS) 27, 'Life Assurance'. This includes an assessment of the cost of any future options and guarantees included in this business valued on a market consistent basis. The calculation also takes account of bonus decisions which are consistent with Legal & General Assurance Society's (Society's) Principles and Practices of Financial Management (PPFM). The shareholders' share of the future cost of bonuses is excluded from the assessment of the realistic liability. In determining the realistic value of liabilities for participating contracts, the value of non-participating business written in the with-profits part of the fund is accounted for as part of the calculation. The present value of future profits (VIF) on this business is separately determined and its value is deducted from the sum of the liabilities for participating contracts and the unallocated divisible surplus.

The long term insurance contract liabilities for business transacted by overseas subsidiaries are determined on the basis of recognised actuarial methods which reflect local supervisory principles or, in the case of the USA, on the basis of US GAAP.

Long term business liabilities can never be definitive as to their timing or the amount of claims and are therefore subject to subsequent reassessment on a regular basis.

Unallocated divisible surplus
The nature of benefits for participating contracts is such that the allocation of surpluses between ordinary equity holders and participating policyholders is uncertain. The amount of surplus which has not been allocated at the balance sheet date is classified within liabilities as the unallocated divisible surplus. Adjustments made to comply with FRS 27 are charged to the unallocated divisible surplus.

Investment contracts

Premium income
For investment contracts, amounts collected as premiums are not included in the income statement but are reported as contributions to investment contract liabilities in the balance sheet.

Revenue from investment contracts
Fees charged for investment management services are recognised as revenue as the services are provided. Initial fees, which exceed the level of recurring fees and relate to the future provision of services, are deferred and amortised over the anticipated period in which the services will be provided.

Fees charged for investment management services for institutional and retail fund management are also recognised on this basis.

Claims
Claims are not included in the income statement but are deducted from investment contract liabilities. The movement in investment contract liabilities consists of claims incurred in the period less the corresponding elimination of the policyholder liability originally recognised in the balance sheet and the investment return credited to policyholders.

Acquisition costs
For participating investment contracts, acquisition costs comprise direct costs such as initial commission and the indirect costs of obtaining and processing new business. These costs are charged to the income statement when incurred.

For non-participating investment contracts, only directly related acquisition costs which vary with, and are related to, securing new contracts and renewing existing contracts, are deferred and amortised over the period during which the costs are expected to be recoverable from future revenue. All other costs are recognised as expenses when incurred.

Trail commission
The Group operates distribution agreements with intermediaries where further commission costs are payable in each period which a relevant policy remains in-force. For relevant non-participating investment contracts, a liability for the present value of this future commission cost is recognised in the balance sheet on inception of the contract. The present value of future commission costs is deferred as an asset and amortised over the period during which the related revenue will be recognised. At each subsequent reporting date, the liability is remeasured to fair value because this financial liability is part of a portfolio of unit linked assets and liabilities whose performance is evaluated on a fair value basis. Any increase in the liability is recognised as an additional deferred cost. Any change in lapse assumptions or revisions to the underlying assumptions for future cash flows will be reflected in the fair value movement for a period. If the future commission liability decreases, a corresponding adjustment is made to the amortisation of the asset.

Investment contract liabilities
Under current IFRS requirements, participating investment contract liabilities are measured using local GAAP, as permitted by IFRS 4 (see above for insurance contract liabilities). In the UK, participating investment contract liabilities are determined in accordance with FRS 27, in the same way as insurance contracts.

Non-participating investment contracts consist of unit linked contracts. Unit linked liabilities are measured at fair value by reference to the value of the underlying net asset values of the Group's unitised investment funds at the balance sheet date.

General insurance business
Results for the General insurance business are determined after taking account of unearned premiums, outstanding claims and unexpired risks using the annual basis of accounting.

Premium income
Premiums are accounted for in the period in which the risk commences. Estimates are included for premiums not notified by the year end and provision is made for the anticipated lapse of renewals not yet confirmed. Those proportions of premiums written in a year which relate to periods of risk extending beyond the end of the year are carried forward as unearned premiums.

Acquisition costs
A proportion of commission and other acquisition costs relating to unearned premiums is carried forward as deferred acquisition costs or, in respect of reinsurance outwards, as deferred income.

1. ACCOUNTING POLICIES continued

Technical liabilities
Liabilities, together with related reinsurance recoveries, are established on the basis of current information. Such liabilities can never be definitive as to their timing or the amount of claims and are therefore subject to subsequent reassessment on a regular basis.

Claims and related reinsurance recoveries are accounted for in respect of all incidents up to the year end. Provision is made on the basis of available information for the estimated ultimate cost, including claims settlement expenses, of claims reported but not yet settled and claims incurred but not yet reported. An unexpired risk provision is made for any overall excess of expected claims and deferred acquisition costs over unearned premiums and after taking account of investment return.

Liability adequacy tests
The Group performs liability adequacy testing on its insurance liabilities to ensure that the carrying amount of liabilities (less related deferred acquisition costs) is sufficient to cover current estimates of future cash flows. When performing the liability adequacy test, the Group discounts all contractual cash flows and compares this amount with the carrying value of the liability. Any deficiency is immediately charged to the income statement and the carrying value of the liability is adjusted accordingly.

Reinsurance
The Group's insurance subsidiaries cede insurance premiums and risk in the normal course of business in order to limit the potential for losses and to provide financing. Outwards reinsurance premiums are accounted for in the same accounting period as the related premiums for the direct or inwards reinsurance business being reinsured. Reinsurance assets include balances due from reinsurers for paid and unpaid losses and loss adjustment expenses, ceded unearned premiums and ceded future life policy benefits. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Reinsurance is recorded as an asset in the consolidated balance sheet unless a right of offset exists, in which case the associated liabilities are reduced commensurately.

Intangible assets

Goodwill
Goodwill on the acquisition of subsidiaries prior to 1998 has been charged directly to reserves. On disposal, goodwill held in reserves is transferred directly to retained earnings. From 1998 the Group's policy is to recognise goodwill on the balance sheet as an intangible asset, measured at cost less any accumulated impairment losses.

Purchased interest in long term businesses
A portfolio of in-force contracts acquired either directly or through the acquisition of a subsidiary undertaking is capitalised at an actuarially determined fair value. The value of business acquired represents the present value of future profits embedded in acquired insurance contracts. These amounts are amortised over the anticipated lives of the related contracts in the portfolio.

Investments

Investment property
Investment property comprises land and buildings which are held for long term rental yields and capital growth. It is carried at fair value with changes in fair value recognised in the income statement within investment return. Investment property in the UK is valued bi-annually by external chartered surveyors at open market values in accordance with the 'Appraisal and Valuation Manual' of The Royal Institution of Chartered Surveyors. Outside the UK, valuations are produced in conjunction with external qualified professional valuers in the countries concerned. In the event of a material change in market conditions between the valuation date and balance sheet date, an internal valuation is performed and adjustments made to reflect any material changes in fair value.

Financial investments
The Group classifies its financial investments on initial recognition as held for trading (HFT), designated at fair value through profit or loss (FVTPL), available-for-sale (AFS) or loans and receivables. Initial recognition of financial investments is on the trade date.

The Group's policy is to measure investments at FVTPL except in the US where the related liability is valued on a passive basis (not using current information), in which case investments are classified as AFS. All derivatives other than those designated as hedges are classified as HFT.

Certain financial investments held by the Group are designated as FVTPL as their performance is evaluated on a total return basis, consistent with asset performance reporting to the Board of Directors and the Groups' investment strategy. Assets designated as FVTPL include debt securities and equity instruments which would otherwise have been classified as AFS under IAS 39, 'Financial Instruments: Recognition and Measurement'. Assets backing participating and non-participating policyholder liabilities outside the US are designated as FVTPL. For participating contracts the assets are managed on a fair value basis to maximise the total return to policyholders over the contract life. The Group's non-participating contract liabilities outside of the US are measured on the basis of current information and are designated as FVTPL to avoid an accounting mismatch in the income statement.

The fair values of quoted financial investments are based on current bid prices. If the market for a financial investment is not active, the Group establishes fair value by using valuation techniques such as recent arm's length transactions, reference to similar listed investments, discounted cash flow models or option pricing models. Venture capital investments are valued in accordance with the International Private Equity and Venture Capital Valuation Guidelines, which represent current best practice, developed by the Association Français des Investisseurs en Capital, the British Venture Capital Association and the European Private Equity and Venture Capital Association. The policies used for determining fair value include earnings multiples, the price of a recent investment or a net asset basis.

Financial investments classified as HFT and FVTPL are measured at fair value with gains and losses reflected in the income statement.

Financial investments classified as AFS are measured at fair value with unrealised gains and losses recognised in a separate reserve within equity. Realised gains and losses, impairment losses, dividends, interest and foreign exchange movements on non-equity instruments are reflected in the income statement.

Loans and receivables are measured at amortised cost using the effective interest rate method.

Plant and equipment
The initial cost of an item of plant or equipment is capitalised where it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The cost is then depreciated on a straight line basis over the item's estimated useful working life. No residual values are imputed to any item of plant and equipment.

Impairment policy
The Group reviews the carrying value of its assets (other than those held at FVTPL) at each balance sheet date. If the carrying value of a financial asset is impaired, the carrying value is reduced through a charge to the income statement. There must be objective evidence of impairment as a result of one or more events which have occurred after the initial recognition of the asset. Impairment is only recognised if the loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

1. ACCOUNTING POLICIES continued

Non-financial assets which have an indefinite useful life are not subjected to amortisation and are tested annually for impairment. Assets which are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

Cash and cash equivalents
Cash and cash equivalents include cash in hand, deposits held at call with banks, treasury bills and other short term highly liquid investments with original maturities of three months or less.

Derivative financial instruments and hedge accounting
The Group's activities expose it to the financial risks of changes in foreign exchange rates and interest rates. The Group uses derivatives such as foreign exchange forward contracts and interest rate swap contracts to hedge these exposures. The Group uses hedge accounting, provided the prescribed criteria in IAS 39 are met, to recognise the offsetting effects of changes in the fair value or cash flow of the derivative instrument and the hedged item. The Group's principal uses of hedge accounting are to:

(i) recognise in shareholders' equity the changes in the fair value of derivatives designated as hedges of a net investment in a foreign operation. Any cumulative gains and/or losses are recognised in the income statement on disposal of the foreign operation;

(ii) defer in equity the changes in the fair value of derivatives designated as the hedge of a future cash flow attributable to a recognised asset or liability, a highly probable forecast transaction, or a firm commitment until the period in which the future transaction is recognised or is no longer expected to occur; and

(iii) hedge the fair value movements in loans due to interest rate and exchange rate fluctuations. Any gain or loss from remeasuring the hedging instrument at fair value is recognised immediately in the income statement. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the income statement.

The relationship between the hedging instrument and the hedged item, together with the risk management objective and strategy for undertaking the hedge transaction, are documented at the inception of the transaction. The effectiveness of the hedge is documented and monitored on an ongoing basis. Hedge accounting is only applied for highly effective hedges (between 80% and 125% effectiveness) with any ineffective portion of the gain or loss recognised in the income statement, within other expenses, in the current period.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instruments which do not qualify for hedge accounting are recognised immediately in the income statement.

Where the risks and characteristics of derivatives embedded in other contracts are not closely related to those of the host contract and the whole contract is not carried at fair value, the derivative is separated from that host contract and measured at fair value, with fair value movements reflected within investment return.

Borrowings, including convertible bond
Borrowings are recognised initially at fair value, net of transaction costs. Borrowings classified as liabilities are subsequently stated at amortised cost. The difference between the proceeds and the redemption value is recognised in the income statement over the borrowing period using the effective interest method.

For a convertible bond which includes a cash settlement option in lieu of the issue of shares on conversion, the conversion option is separated and recognised as a derivative liability. It is revalued to fair value at each reporting period with fair value gains and losses taken through the income statement. The remainder of the proceeds less attributable expenses is allocated to the value of the debt portion of the convertible bond. This amount is recorded as a liability on an amortised cost basis using the effective interest rate until extinguished on conversion or on maturity of the bond.

Income taxes

Income tax
Income tax comprises current and deferred tax. Income tax is recognised in the income statement except where it relates to an item which is recognised in equity.

Current tax is the expected tax payable on the taxable profit for the period and any adjustment to the tax payable in respect of previous periods.

The total income tax expense for the period includes tax which is not related to profits earned by equity holders for the period, being the income tax paid by the Group in respect of UK life policyholder returns. The income statement income tax charge has therefore been apportioned between the element attributable to policyholder returns and the element attributable to equity holders' profits (equity holder tax).

For short term business all income tax is classified as equity holder tax.

The element of the net equity holders' profit from UK long term business represented by the transfer from Society's LTF (other than investment return on equity holders' funds within the LTF) has borne tax at the effective equity holder tax rate, which is sufficiently close to the standard rate of UK corporation tax for that to be used in the financial statements. The element represented by the net capital released into, or deducted from, profit from non profit business is deemed to have borne tax at the standard rate of UK corporation tax, although no tax in respect of this is included in the total income tax in the income statement. The balance of income taxes associated with long term business profits is then classified as income tax attributable to policyholder returns.

There is no definitive method of calculating the effective equity holder tax rate. A number of alternative methods are consistently used, in order to assess the validity of using the standard rate of UK corporation tax.

For equity holders' funds within Society's LTF, the equity holder income tax represents the actual income tax on the return on those funds. For international long term business the equity holder income tax is the total income tax in respect of profits earned from that business.

Deferred income tax
Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Deferred tax is measured using tax rates expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled, based on tax rates and law which have been enacted or substantively enacted at the balance sheet date.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

1. ACCOUNTING POLICIES continued

Deferred tax assets and liabilities are not discounted.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future (or if it will, then it will not generate any incremental tax liability for the Group).

No deferred tax is provided at the incremental rate on the undeclared surplus in Society's LTF represented by the Shareholder Retained Capital (SRC) on the grounds that, at the balance sheet date, no obligation to make a declaration of surplus exists and there is no expectation that such a declaration will occur.

Leases

Where a significant proportion of the risks and rewards of ownership is retained by the lessor, leases are classified as operating leases. Payments made as lessees under operating leases (net of any incentives from the lessor) are charged to the income statement on a straight line basis over the period of the lease.

Employee benefits

Pension obligations

The Group operates a number of defined benefit and defined contribution pension schemes in the UK and overseas. The assets of all UK defined benefit schemes are held in separate trustee administered funds which are subject to regular actuarial valuation every three years, updated by formal reviews at reporting dates.

The liability recognised in the balance sheet in respect of defined benefit pension schemes is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets. The defined benefit obligation is actuarially calculated each year using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows. The discount rate is based on market yields of high quality corporate bonds which are denominated in the currency in which the benefits will be paid, and that have terms to maturity which approximate to those of the related pension liability.

Where the unallocated divisible surplus or equity holders' funds are affected as a result of actuarial gains and losses on the defined benefit pension scheme, the charge is not recognised in the income statement but through the statement of recognised income and expense (SORIE).

The Group pays contractual contributions in respect of defined contribution schemes. The contributions are recognised as employee benefit expenses when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

Share-based payments

The Group operates a number of share-based payment schemes. The fair value at the date of grant of the equity instrument is recognised as an expense, spread over the vesting period of the instrument. The total amount to be expensed is determined by reference to the fair value of the awards, excluding the impact of any non-market vesting conditions. At each balance sheet date, the Group revises its estimate of the number of equity instruments which are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment is made to equity over the remaining vesting period. On vesting or exercise, the difference between the expense charged to the income statement and the actual cost to the Group is transferred to retained earnings. Where new shares are issued, the proceeds received are credited to share capital and share premium.

Share capital and treasury shares

Equity instruments

An equity instrument is any contract which evidences a residual interest in the net assets of an entity. It follows that a financial instrument is treated as equity if:

- there is no contractual obligation to deliver cash or other financial assets or to exchange financial assets or liabilities on unfavourable terms; and
- the instrument is either a non-derivative which contains no contractual obligation to deliver a variable number of shares, or is a derivative which will be settled only by the Group exchanging a fixed amount of cash or other financial assets, for a fixed number of its own equity instruments.

Share issue costs

Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. An incremental share issue cost is one which would not have arisen if shares had not been issued.

Treasury shares

Where any Group company purchases the Company's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to shareholders. Where such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity attributable to shareholders, net of any directly attributable incremental transaction costs and the related income tax effects.

Dividend recognition

A dividend distribution to the Company's shareholders is recognised as a liability in the period in which the dividends are authorised and are no longer at the discretion of the Company. Final dividends are accrued when approved by the Company's shareholders at the general meeting and interim dividends are recognised when paid.

Fiduciary activities

Assets and income arising from fiduciary activities, together with associated commitments to return such assets to customers, are not included in these financial statements. Where the Group acts in a fiduciary capacity, for instance as a trustee or agent, it has no contractual rights over the assets concerned.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The Group recognises a provision for onerous contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

Foreign currency translation

Foreign currency transactions

Foreign currency transactions are translated into the functional currency using the exchange rate prevailing at the date of the transactions. The functional currency of the Group's foreign operations is the currency of the primary economic environment in which these entities operate. Foreign exchange gains and losses are recognised in the income statement, except when recognised in equity as qualifying cash flow or net investment hedges.

1. ACCOUNTING POLICIES continued

Overseas subsidiaries
The assets and liabilities of all of the Group's foreign operations are translated into sterling, the Group's presentational currency, at the closing rate at the date of the balance sheet. The income and expenses for each income statement are translated at average exchange rates. On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to a separate component of shareholders' equity.

Investment return
The reporting of investment return comprises investment income, unrealised gains and losses from financial investments held at FVTPL and realised gains and losses from all financial assets.

Investment income includes dividends, interest and rent. Dividends are accrued on an ex-dividend basis. Interest and rent are included on an accruals basis. Interest income for financial assets which are not classified as FVTPL is recognised using the effective interest method.

Operational income and expenses
Operational income comprises fee income from estate agency operations, agency fee income relating to distribution services and any margin paid on written business acquired in a period. Operational income is accounted for when due.

Other expenses comprise primarily the expenses incurred in estate agency operations, institutional fund management and retail investment business, together with unallocated corporate expenses. Other costs are accounted for as they arise.

Earnings per share

Earnings per share
Earnings per share is calculated by dividing net income attributable to ordinary equity holders by the weighted average number of ordinary shares in issue during the year. For this purpose, net income is defined as the profit after tax derived from continuing operations, or as the profit after tax derived from both continuing and discontinued operations. In both instances, net income is adjusted for distributions made on any debt classified as equity.

Diluted earnings per share
For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares, such as convertible debt and share options granted to employees. Potential or contingent share issuances are treated as dilutive when their conversion to shares would decrease net earnings per share.

Segment reporting
The Group's segments are based on the dominant source and nature of the Group's risks and returns and the manner in which the Group's internal organisational and management structure operates and reflects its system of internal financial reporting to the Group Board and Group Chief Executive.

Institutional fund management services are provided to Legal & General Assurance Society (an element of the life and pensions segment) on a cost basis. The remaining transactions between the business segments are on normal commercial terms and conditions.

The primary segmental information is presented for business segments as this reflects the dominant source and nature of the Group's risks and returns. Secondary information is presented on geographic segments.

Standards, interpretations and amendments to published standards that are not yet effective
Certain new standards, amendments and interpretations to existing standards have been published which are mandatory for the Group's accounting periods beginning on or after 1 January 2007 or later periods but which the Group has not early adopted, as follows:

- IFRS 7, 'Financial Instruments: Disclosures' and a complementary amendment to IAS 1, 'Presentation of financial instruments – capital disclosures' (effective from 1 January 2007). IFRS 7 introduces new financial instrument disclosures. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk, market risk and sensitivity to market risk. It replaces the disclosure requirements in IAS 32. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Group has assessed the impact of IFRS 7 and the amendment to IAS 1 and believes that the main additional disclosures will be the inclusion of quantitative financial risk disclosures based on information used by management to manage the Group's financial risk.
- IFRS 8, 'Operating Segments' (effective from 1 January 2009). IFRS 8 introduces a new conceptual requirement that reportable segments should be formed on the same basis as is used internally by senior management for evaluating operating segment performance. The Group intends to carry out an impact assessment on the implementation of this standard in 2007.
- IFRIC 9, 'Reassessment of Embedded Derivatives' (effective for annual periods beginning on or after 1 June 2006). Under normal circumstances, IFRIC 9 prohibits the subsequent reassessment of contracts for the existence and separation of embedded derivatives once an initial assessment has been carried out. However, where a change in the terms of a previously assessed contract has occurred and this leads to a significant modification to the cash flows which would otherwise be required under the contract, reassessment is mandatory. The Group will apply IFRIC 9 from 1 January 2007, but it is not expected to have any significant impact on the Group financial statements.
- IFRIC 10, 'Interim Reporting and Impairment' (effective for annual periods beginning on or after 1 November 2006). IFRIC 10 prohibits the reversal of impairment losses recognised in an interim period (for instance, on goodwill, investments in equity instruments held as AFS and investments in financial assets carried at cost) at a subsequent balance sheet date. The Group will apply IFRIC 10 from 1 January 2007. The anticipated impact is expected to be immaterial based on past impairment experience, although, the actual impact will be contingent on future impairment events.
- IFRIC 11, 'IFRS 2 – Group and treasury share transactions' clarifies the appropriate accounting treatment for share-based payments in single entity financial statements. The interpretation is therefore not applicable to the Group financial statements.
- IFRIC 12, 'Service concession arrangements', has been issued to address the accounting by operators for public-to-private service concession arrangements. The interpretation applies only to public-to-private sector concessions and therefore has no impact on the Group financial statements.

2. IMPACT OF SIGNIFICANT EVENTS AND CHANGES IN 2006

Corporate restructure

On 31 December 2006, the non-linked non profit pensions and annuity business of Society was ceded to a new, wholly owned, reinsurance company, Legal & General Pensions Limited (LGP).

LGP has been capitalised using £1.3bn of Society shareholder capital, £400m of this is represented by subordinated debt (£200m upper tier II, £200m lower tier II) and £900m by equity. The reinsurance was effected on arm's length terms resulting in an initial regulatory loss in LGP. Further funds of £571m have been injected from Society's LTF into LGP's LTF by means of a contingent loan to cover this loss.

Prior to the capitalisation of LGP, the intra-group subordinated debt capital of £602m attributed to SRC was repaid to Group Plc and an equivalent amount was lent to Society shareholder capital on a subordinated basis (£301m upper tier II, £301m lower tier II).

The corporate restructuring has had no impact on the IFRS profit before tax for the year. The movement in liabilities and assets between Society and LGP is eliminated in the Group consolidation in accordance with the Group accounting policies. However, there is a £171m deferred tax benefit for 2006, which increases the IFRS profit after tax (see Note 13). This is the result of an initial tax loss in LGP.

The corporate restructuring has reduced Society's regulatory surplus capital by £0.5bn (2006 total surplus: £4.9bn) and the Insurance Groups Directive (IGD) regulatory surplus by £0.5bn (2006 total surplus: £2.1bn), primarily due to the requirement to hold solvency margins in both Society and LGP for the reinsured business. These amounts are extracted from draft regulatory returns.

Implementation of changes to FSA reporting and capital rules (Policy Statement 06/14)

In 2006, the FSA introduced a more realistic reserving framework for certain non profit business. As a result, the Group changed its insurance assumptions as detailed in Note 37. This lead to a reduction in the non-participating insurance contract liabilities and regulatory reserves required for term assurance business of £641m, and an elimination of the deferred acquisition cost asset relating to term assurance business amounting £145m (see Note 24(ii)), resulting in an increase to IFRS profit after tax of £496m.

The change to the reserving framework has also resulted in a consequent small reduction in the long term insurance capital requirement. The associated financial reinsurance previously in place to finance these reserves was terminated and no credit has been taken for implicit items in the regulatory balance sheet, of which approximately £240m related term assurance. The net impact on Society's regulatory capital surplus of the changes to reserving has been an increase of approximately £125m.

In addition, the FSA removed the requirement for Society to calculate a resilience capital requirement and changed the calculation of the With-Profits Insurance Capital Component which has resulted in a decrease in Society's capital resources requirement of £432m.

Review of annuity investment policy

During 2006, Society undertook a review of its asset liability matching policy for annuity business. Property assets backing annuity liabilities were replaced with corporate bonds and Society entered into inflation swaps to mitigate negative inflation risk (see Note 21). As a result, a closer match between assets and liabilities was achieved. Additionally, the margin within the reserves to cover an interest rate mismatch was reviewed and reduced. These actions reduced the regulatory reserves for Society, and increased the IFRS profit after tax, by £422m.

Tax effects

In accordance with the Group's policy for attributing tax to equity holders and policyholders, the IFRS profit before equity holder tax from the net capital released from UK non profit business is determined by grossing up after tax amounts at the standard rate of UK corporation tax (30%). In 2006, there was no current or deferred tax charge on these profits.

3. OPERATING PROFIT INFORMATION

This supplementary information provides further analysis of the results reported under IFRS and we believe gives shareholders a better understanding of the underlying performance of the business.

For UK life and pensions business, operating profit represents:

- the distribution of profit relating to non profit and shareholder net worth, grossed up for tax. The current distribution comprises:
  - 7% of the embedded value of the SRC and Sub-fund (shareholder net worth – SNW) adjusted to remove the impact from the contingent loan between SRC and LGP, and the SNW of LGP; and
  - 5% of the embedded value of the non profit business adjusted to remove the impact from the contingent loan between SRC and LGP;
- the subordinated debt interest on the intra-group subordinated debt included within the SRC, until it was repaid in December 2006;
- the shareholders' share of the with-profits surplus recognised in the year, grossed up for tax.

An analysis of the distribution of profit relating to non profit and shareholder net worth is included in Note 3(iv).

Operating profit includes a longer term investment return on shareholders', General insurance's and Netherlands' funds held outside a LTF. It excludes investment variances and the contribution from UK non profit business. The income statement comprises returns to shareholders and excludes policyholders' returns.

(i) Reconciliation between operating profit and profit from ordinary activities after income tax

	Notes	**2006 £m**	2005 £m
From continuing operations			
Life and pensions	(ii)	**592**	489
Investment management	(v)	**133**	103
General insurance	(vi)	**9**	14
Other operational income	(vii)	**18**	41
Operating profit		**752**	647
Investment return on SRC	(iii)	**303**	387
Net capital released from non profit business	(iii)	**1,255**	478
Distribution of operating profit from non profit business	(iii)	**(422)**	(349)
		1,888	1,163
Variation from longer term investment return		**63**	139
Property income attributable to minority interests		**67**	81
Profit from continuing operations before tax attributable to equity holders		**2,018**	1,383
Tax attributable to equity holders		**(387)**	(371)
Profit from continuing operations after tax		**1,631**	1,012
Profit from discontinued operations		**–**	13
Profit from ordinary activities after tax		**1,631**	1,025

(ii) Life and pensions operating profit

	Notes	**2006 £m**	2005 £m
Distribution relating to non profit and shareholder net worth	(iv)	**388**	312
Subordinated debt interest		**34**	37
Non profit business		**422**	349
With-profits business		**95**	66
UK		**517**	415
USA		**58**	52
Netherlands		**7**	18
France		**10**	4
		592	489

3. OPERATING PROFIT INFORMATION continued

(iii) Contribution from UK non profit business

	2006 £m	2005 £m
Investment income	75	67
Interest expense and charges	(3)	(3)
Realised investment gains	215	191
Unrealised investment gains	16	132
Investment return on SRC	303	387
Net capital released from non profit business[1]	1,255	478
Distribution of operating profit from non profit business	(422)	(349)
Contribution from UK non profit business before tax	**1,136**	516

1. The net capital released from non profit business for 2006 has been impacted by the matters discussed in Note 2.

(iv) Distributions to shareholders from Society's LTF

The transfer to shareholders from Society's LTF is limited by a formula agreed with our regulator. The formula is the aggregate of the shareholders' share of the with-profits surplus, a smoothed investment return of 7% on the embedded value of the SRC and Sub-fund and 5% on the embedded value of the non profit business of Society and LGP, adjusted to remove the impact from the contingent loan between SRC and LGP, and the SNW of LGP.

	2006 Non profit £m	2006 SNW £m	2005 Non profit £m	2005 SNW £m
Embedded value at end of year	1,643	3,828	2,387	1,762
Less: subordinated debt	–	–	–	(602)
Less: LGP shareholders' fund	–	(1,280)	–	–
Contingent loan	571	(571)	–	–
Add back: pension deficit attributable to SNW	(5)	60	–	51
Add back: distributions	–	272	–	219
	2,209	2,309	2,387	1,430
Distribution formula – full year	5.0%	7.0%	5.0%	7.0%
Distribution after tax	110	162	119	100
Tax gross up at 30%	47	69	51	42
Distribution before tax	**157**	**231**	170	142

(v) Investment management operating profit

	2006 £m	2005 £m
Managed pension funds	96	74
Ventures	4	4
Property	6	4
Retail investments	11	7
Other external income	6	5
Other income	10	9
	133	103

3. OPERATING PROFIT INFORMATION continued

(vi) General insurance operating profit, underwriting result and combined operating ratios

	Operating profit/ (loss) 2006 £m	**Under-writing result 2006 £m**	**Combined operating ratio 2006 %**	Operating profit 2005 £m	Under-writing result 2005 £m	Combined operating ratio 2005 %
From continuing operations						
Household	**(9)**	**(21)**	**111**	7	(6)	101
Other business	**18**	**13**	**89**	7	1	101
	9	**(8)**	**105**	14	(5)	101

The combined operating ratio is:

$$\left[\frac{\text{Net incurred claims}}{\text{Net earned premiums}} + \frac{\text{Expenses + Net commission}}{\text{Net written premiums}}\right] \times 100$$

(vii) Other operational income

	2006 £m	2005 £m
Shareholders' other income		
Investment return on ordinary shareholders' equity	**139**	127
Interest expense	**(106)**	(75)
	33	52
Other operations[1]	**(2)**	(5)
Unallocated corporate and development expenses	**(13)**	(6)
	18	41

1. Principally the Regulated mortgage network and Cofunds.

(viii) Earnings per share

	Notes	**Profit before tax 2006 £m**	**Tax charge 2006 £m**	**Profit after tax 2006 £m**	**Number of shares[1] 2006 m**	**Earnings per share 2006 p**
Operating profit from continuing operations	(i)	**752**	**(212)**	**540**	**6,483**	**8.33**
Variation from longer term investment return	(i)	**63**	**(11)**	**52**		**0.80**
Contribution from UK non profit business	(iii)	**1,136**	**(164)**	**972**		**14.99**
Profit from discontinued operations		**–**	**–**	**–**		**–**
Distributions on subordinated borrowings designated as equity				**–**		**–**
Profit attributable to ordinary equity holders/EPS[2]		**1,951**	**(387)**	**1,564**	**6,483**	**24.12**

	Notes	Profit before tax 2005 £m	Tax (charge)/ credit 2005 £m	Profit/ (loss) after tax 2005 £m	Number of shares[1] 2005 m	Earnings per share 2005 p
Operating profit from continuing operations	(i)	647	(191)	456	6,474	7.04
Variation from longer term investment return	(i)	139	(32)	107		1.66
Contribution from UK non profit business	(iii)	516	(148)	368		5.68
Profit from discontinued operations		12	1	13		0.20
Distributions on subordinated borrowings designated as equity				(16)		(0.25)
Profit attributable to ordinary equity holders/EPS[2]		1,314	(370)	928	6,474	14.33

The number of shares in issue at 31 December 2006 was 6,532,261,961 (2005: 6,507,421,932).

1. Weighted average number of shares.
2. Earnings per share.

3. OPERATING PROFIT INFORMATION continued

(ix) Group cash flow statement

The table below shows the cash flows in the year relating to the Group's parent company.

	2006 £m	2005 £m
Dividends received:		
UK life and pensions	**380**	533
General insurance	**–**	105
Investment management	**50**	69
Other	**3**	2
	433	709
Dividend distributions to ordinary equity holders of the Company during the year (Note 15)	**(349)**	(331)
Distributions during the year on subordinated borrowings designated as equity (Note 15)	**–**	(16)
Proceeds from issue of equity	**15**	1
Proceeds from issue of subordinated borrowings	**–**	397
Repayment of convertible bond	**(525)**	–
Working capital movements	**(52)**	(136)
Net cash (outflow)/inflow	**(478)**	624

4. SEGMENTAL ANALYSIS

The Group is organised into three main business segments:

– Long term business (includes insurance and investment business)

– Investment management

– General insurance

Other operations comprise Shareholders' assets, Estate agencies, Regulated mortgage network and Corporate expenses, none of which constitute a separately reportable segment.

(i) Income statement analysed by business segments (primary disclosures)

For the year ended 31 December 2006	Long term business[1] £m	Investment management £m	General insurance £m	Other operations £m	Elimination of inter segment amounts £m	Total £m
Total revenue from continuing operations	**8,355**	**12,013**	**315**	**526**	**(243)**	**20,966**
Total expenses from continuing operations	**6,802**	**11,849**	**314**	**315**	**(243)**	**19,037**
Profit from continuing operations after income tax	**1,344**	**93**	**1**	**193**	**–**	**1,631**
Profit from discontinued operations (Note 14)	**–**	**–**	**–**	**–**	**–**	**–**
Inter segment revenue	**(26)**	**(40)**	**(2)**	**(175)**	**243**	**–**

For the year ended 31 December 2005	Long term business £m	Investment management £m	General insurance £m	Other operations £m	Elimination of inter segment accounts £m	Total £m
Total revenue from continuing operations	11,512	18,833	328	559	(243)	30,989
Total expenses from continuing operations	10,373	18,724	311	235	(243)	29,400
Profit from continuing operations after income tax	650	71	13	278	–	1,012
Profit from discontinued operations (Note 14)	–	–	13	–	–	13
Inter segment revenue	–	(59)	(2)	(182)	243	–

1. The long term business segment for 2006 has been impacted by the matters discussed in Note 2.

4. SEGMENTAL ANALYSIS continued

(ii) Balance sheet analysed by business segments (primary disclosures)

As at 31 December 2006	Long term business £m	Investment management £m	General insurance £m	Other operations £m	Elimination of inter segment amounts £m	Total £m
Total assets	**69,729**	**144,725**	**534**	**4,519**	**(1,642)**	**217,865**
Total liabilities	**66,053**	**144,000**	**365**	**3,250**	**(1,642)**	**212,026**
Total equity	**3,676**	**725**	**169**	**1,269**	**–**	**5,839**

As at 31 December 2005	Long term business £m	Investment management £m	General insurance £m	Other operations £m	Elimination of inter segment amounts £m	Total £m
Total assets	65,146	123,304	516	4,676	(1,777)	191,865
Total liabilities	62,901	122,622	351	2,832	(1,777)	186,929
Total equity	2,245	682	165	1,844	–	4,936

(iii) Revenue and assets by geographic segments (secondary disclosures)

31 December 2006	UK £m	USA £m	Netherlands £m	France £m	Elimination of inter segment amounts £m	Total £m
Total revenue from continuing operations	**20,020**	**329**	**300**	**319**	**(2)**	**20,966**
Total assets	**212,185**	**2,478**	**1,415**	**1,807**	**(20)**	**217,865**

31 December 2005	UK £m	USA £m	Netherlands £m	France £m	Elimination of inter segment amounts £m	Total £m
Total revenue from continuing operations	29,918	321	362	388	–	30,989
Total assets	186,936	2,016	1,269	1,663	(19)	191,865

(iv) Gross written premiums

	2006 £m	2005 £m
From continuing operations		
UK life and pensions participating business	**376**	485
UK life and pensions non-participating business	**2,691**	2,428
Total UK life and pensions	**3,067**	2,913
USA	**347**	329
Netherlands	**266**	243
France	**283**	265
Total life and pensions	**3,963**	3,750
General insurance		
Household	**240**	234
Other business	**83**	100
Total General insurance	**323**	334
Total gross written premiums	**4,286**	4,084

Life and pensions gross written premiums by destination are not materially different from gross premiums written by origin.
The General insurance premiums arise wholly in the UK.

5. NEW BUSINESS (GROSS OF REINSURANCE)

New business is presented below for all long term business written by the Group including both insurance and investment contracts.
New annual premiums arise where the terms and conditions of a policy anticipate more than one premium being paid over its lifetime; new single premiums comprise all premiums which are not categorised as new annual premiums.

	Annual 2006 £m	Single 2006 £m	Annual 2005 £m	Single 2005 £m
UK life and pensions				
Protection	**231**	**–**	208	–
Annuities	**–**	**1,735**	–	1,539
Savings				–
– Unit linked bonds	**–**	**2,612**	–	2,082
– Pensions, stakeholder and other non profit[1]	**126**	**817**	97	549
With-profits	**117**	**827**	77	729
UK life and pensions	**474**	**5,991**	382	4,899
USA	**42**	**–**	42	–
Netherlands	**12**	**170**	13	158
France	**12**	**195**	17	191
	540	**6,356**	454	5,248
Investment management				
Retail investments				
ISAs – UK	**18**	**498**	14	422
Unit trusts				
– UK	**2**	**5,945**	1	2,577
– France	**–**	**25**	–	25
Institutional fund management				
UK managed pension funds[2]				
– Pooled funds		**17,878**		14,778
– Segregated funds		**608**		240
		18,486		15,018
Limited partnerships		**99**		87
Other funds		**2,065**		2,029
	20	**27,118**	15	20,158
Total new business	**560**	**33,474**	469	25,406

	Annual 2006 £m	Single 2006 £m	Annual 2005 £m	Single 2005 £m
Comprising:				
Insurance contracts				
Life and pensions				
– Participating	**7**	**608**	5	711
– Non-participating	**296**	**1,493**	263	1,263
Investment contracts				
Life and pensions				
– Participating	**6**	**286**	21	258
– Non-participating	**231**	**3,969**	165	3,016
Investment management	**20**	**27,118**	15	20,158
Total new business	**560**	**33,474**	469	25,406

1. Includes the recategorisation of £18m APE (£3m annual premiums and £149m single premiums) previously reported in with-profits individual pensions in the '2006 full year new business results' Stock Exchange Release announcement on 25 January 2007.
2. Excludes £4.4bn (2005: £4.1bn) which is held on a temporary basis, generally as part of a portfolio reconstruction.

The UK pooled managed funds of £17.9bn (2005: £14.8bn) reported above are classified as fund management contracts. The increase in the fair value of the investment contract liabilities is shown in the income statement.
There are two classes of business where there is a material difference between gross and net of reinsurance new business; term assurance, which is 51.9% (2005: 57.5%) reinsured, and permanent health insurance, which is 24.5% (2005: 22.6%) reinsured.

6. INVESTMENT RETURN

	2006 £m	2005 £m
Financial investment return	**15,610**	26,093
Property investment return	**962**	838
Investment return	**16,572**	26,931

Included within financial investment return is interest income on AFS investments of £74m (2005: £23m). Net gains of £15,529m (2005: £26,018m) arose on financial investments designated as FVTPL. Financial investment return includes dividends, interest received and fair value gains and losses, excluding fair value movements attributable to AFS investments.

Property investment return includes £345m (2005: £325m) of rental income.

7. NET CLAIMS AND CHANGE IN INSURANCE LIABILITIES

From continuing operations	Long term insurance 2006 £m	General insurance 2006 £m	Total 2006 £m	Long term insurance 2005 £m	General insurance 2005 £m	Total 2005 £m
Claims paid						
– gross	**3,603**	**206**	**3,809**	3,064	198	3,262
– reinsurance recoveries	**(254)**	**(4)**	**(258)**	(234)	(6)	(240)
	3,349	**202**	**3,551**	2,830	192	3,022
Change in insurance liabilities						
– gross	**(1,866)**	**(5)**	**(1,871)**	3,094	11	3,105
– reinsurance recoveries	**1,381**	**–**	**1,381**	258	1	259
Net claims and change in insurance liabilities	**2,864**	**197**	**3,061**	6,182	204	6,386

The change in insurance liabilities includes the financial effect of PS06/14 which is described in Notes 2 and 37.

8. OTHER EXPENSES

On 27 May 2005, the Financial Services and Markets Tribunal (the Tribunal) delivered a further decision in the case between Society and the Financial Services Authority (FSA). The decision built on the provisional view announced in January 2005 that there should be a reduction in the penalty imposed by the FSA on Society for the charge of endowment mis-selling. The FSA had imposed a penalty of £1.1m. The Tribunal reduced this to £575,000. There are no amounts occurring in 2006 of a similar nature.

9. AUDITORS' REMUNERATION

	2006 £m	2005 £m
Remuneration receivable by the Company's auditors for the audit of the consolidated and Company financial statements	**1.0**	0.9
Remuneration receivable by the Company's auditors and its associates for the supply of other services to the Company and its associates, including remuneration for the audit of the financial statements of the Company's subsidiaries comprises:		
Audit of the Company's subsidiaries, supplied under legislation	**1.4**	1.1
	2.4	2.0
Other services supplied under legislation	**0.5**	0.5
Tax services	**0.8**	0.3
Services relating to corporate finance transactions completed or proposed	**0.1**	–
Other services[1]	**1.3**	0.6
Auditors' remuneration	**5.1**	3.4

1. For 2006, Other services include £0.6m (2005: £nil) in respect of accounting and regulatory advice, project management services and assurance procedures for Group's capital review.

The 2005 auditors' remuneration is presented on a comparable basis following changes in the legislation applicable to auditors' remuneration disclosures.

In addition to the above, fees payable to the Company's auditor and its associates for audit services supplied to the Company's associated pension scheme amounted to £0.1m (2005: £0.1m).

10. EMPLOYEE INFORMATION

	2006 £m	2005 £m
Average number of staff employed during the year:		
UK	**9,051**	8,644
Europe	**332**	317
USA	**359**	312
Worldwide employees	**9,742**	9,273

	2006 £m	2005 £m
Salaries	**303**	283
Social security costs	**38**	34
Share-based incentive awards	**15**	13
Defined benefit pension costs (Note 40)	**41**	33
Defined contribution pension costs (Note 40)	**17**	16
	414	379

11. PROFIT BEFORE INCOME TAX

	2006 £m	2005 £m
The following items have been included in arriving at profit before tax:		
– Depreciation on plant and equipment (Note 18)	**15**	14
– Amortisation of purchased interest in long term businesses (Note 23)	**7**	4
– Operating lease rentals	**19**	17
– Reinsurance commissions	**(15)**	(15)
– Direct operating expenses arising from investment properties which generate rental income	**25**	28
– Direct operating expenses arising from investment properties which do not generate rental income	**1**	1

During the year, the Group entered into reinsurance arrangements which resulted in a profit of £192m (2005: £324m). This profit has been reflected in the consolidated income statement for the year.

12. FOREIGN EXCHANGE AND EXCHANGE RATES

Profit for the year includes foreign exchange gains and losses on financial instruments designated as FVTPL. The profit for the year also includes foreign exchange gains of £243m (2005: £64m) arising on conversion to sterling of other assets and liabilities.

Principal rates of exchange used for translation are:

	01.01.06-31.12.06 Average	2006 Year end	01.01.05-30.06.05 Average	01.07.05-31.12.05 Average	2005 Year end
United States Dollar	**1.84**	**1.96**	1.87	1.77	1.72
Euro	**1.47**	**1.48**	1.46	1.47	1.46

13. INCOME TAX EXPENSE

	2006 £m	2005 £m
Current tax		
– Current tax for the year	**280**	350
– Adjustments in respect of prior years	**21**	8
Total current tax	**301**	358
Deferred tax		
– Origination and reversal of temporary differences	**(3)**	219
Total income tax expense	**298**	577
Represented by:		
Income tax attributable to policyholder returns	**(89)**	206
Income tax attributable to equity holders	**387**	371
Total income tax expense	**298**	577

The tax assessed for the year is lower (2005: higher) than the standard corporation tax rate applicable to companies operating in the UK of 30% (2005: 30%). The differences are explained below:

	2006 £m	2005 £m
Income tax calculated at standard UK corporation tax rate	**579**	477
Effects of:		
Income tax relating to policyholder returns	**(62)**	144
Disallowable expenditure	**3**	–
Non taxable income including UK dividends	**(11)**	(8)
Adjustments in respect of prior years	**10**	1
Differences between taxable and accounting investment gains/losses	**(13)**	(8)
Unrelieved tax losses	**–**	1
Overseas tax	**4**	3
No tax in respect of property income attributable to minority interests	**(20)**	(24)
Lower tax on SRC investment return	**(15)**	(8)
Difference between tax relief and accounting expense for share releases and option exercises	**(6)**	–
Difference between tax and accounting losses (Note 2)	**(171)**	–
Other	**–**	(1)
Total income tax expense	**298**	577

The rate of tax for the year reflects the impact of the net capital released from non profit business into profit of £1,380m (2005: £335m) on which no current or deferred tax arose. The effect of this is within the reconciling item 'Income tax relating to policyholder returns'.

	2006 £m	2005 £m
Deferred tax recognised directly in equity		
Relating to net gains or losses recognised directly in equity	**4**	(32)
Exchange (losses)/gains	**(21)**	15
Deferred tax recognised directly in equity	**(17)**	(17)

No deferred tax is provided at the incremental rate on the undeclared surplus in the Society LTF represented by the SRC, on the grounds that, at the balance sheet date, no obligation to make a declaration of surplus actually exists and there is no expectation that such a declaration will occur. The maximum amount of incremental tax which would crystallise on such a declaration of surplus is estimated to be £717m (2005: £509m).

14. DISCONTINUED OPERATIONS

Gresham Insurance Company Limited

On 31 March 2005, the Group sold its 90% stake in its subsidiary Gresham to Barclays Bank PLC for a consideration of £85m, of which £4m was paid in dividends by Gresham and the remainder in cash by Barclays. The transaction resulted in an exceptional profit before tax of £15m (£15m after tax).

	2006 £m	2005 £m
Revenues	–	35
Expenses	–	(38)
Loss before tax	–	(3)
Gain on disposal of Gresham	–	15
Income tax attributable to equity holders	–	1
Profit from discontinued operations after income tax	–	13

The fair value of assets disposed and consideration received were as follows:

	2006 £m	2005 £m
Financial investments	–	108
Other assets	–	78
Cash and cash equivalents	–	8
Insurance contract liabilities	–	(118)
Other liabilities	–	(10)
Fair value of net assets disposed	–	66
Total cash consideration received	–	81
Less cash and cash equivalents in Gresham	–	(8)
Net proceeds from disposal of Gresham	–	73

	2006 £m	2005 £m
Net cash flows of Gresham attributable to:		
Operating activities	–	6
Investing activities	–	(8)
	–	(2)

Venture capital subsidiaries

During December 2004, the Group committed to reduce its investment in venture capital subsidiaries. These investments ceased to be subsidiaries of the Group in the first half of 2005. The continuing interests of the Group in these subsidiaries are now accounted for as investments. Of the total consideration of £33m due from the sale, £23m was received in 2005 and the final instalment of £10m was received in 2006. There was no gain or loss on the disposal of these investments.

15. DIVIDENDS AND OTHER DISTRIBUTIONS

	Per share 2006 p	Per share 2005 p	**Total 2006 £m**	Total 2005 £m
Ordinary share dividends paid in the year				
– Prior year final dividend	**3.63**	3.45	**236**	224
– Current year interim dividend	**1.74**	1.65	**113**	107
	5.37	5.10	**349**	331
Distributions paid on subordinated borrowings designated as equity			–	16
			349	347
Ordinary share dividend proposed[1]	**3.81**	3.63	**248**	236

1. The dividend proposed has not been included as a liability in the balance sheet.

16. EARNINGS PER SHARE

Earnings per share have been calculated using the weighted average number of ordinary shares in issue and the profits for the financial year. Reconciliations of the earnings and weighted average numbers of shares used in the calculations are set out below:

(i) Based on profit from continuing operations after income tax attributable to ordinary equity holders

	Profit 2006 £m	Number of shares[1] 2006 m	Earnings per share 2006 p	Profit 2005 £m	Number of shares[1] 2005 m	Earnings per share 2005 p
Profit attributable to equity holders	1,564			944		
Less:						
Distributions on subordinated debt designated as equity	–			(16)		
Profit from discontinued operations	–			(13)		
Profit from continuing operations after income tax attributable to ordinary equity holders	1,564	6,483	24.12	915	6,474	14.13
Net shares under options allocable for no further consideration	–	46	(0.17)	–	38	(0.08)
Convertible bonds outstanding	–	–	–	20	285	(0.29)
Diluted profit from continuing operations after income tax attributable to ordinary equity holders	1,564	6,529	23.95	935	6,797	13.76

(ii) Based on profit attributable to ordinary equity holders

	Profit 2006 £m	Number of shares[1] 2006 m	Earnings per share 2006 p	Profit 2005 £m	Number of shares[1] 2005 m	Earnings per share 2005 p
Profit attributable to equity holders	1,564			944		
Less:						
Distributions on subordinated debt designated as equity	–			(16)		
Profit attributable to ordinary equity holders	1,564	6,483	24.12	928	6,474	14.33
Net shares under options allocable for no further consideration	–	46	(0.17)	–	38	(0.08)
Convertible bonds outstanding	–	–	–	20	285	(0.30)
Diluted profit attributable to ordinary equity holders	1,564	6,529	23.95	948	6,797	13.95

(iii) Discontinued operations

Earnings per share and diluted earnings per share for discontinued operations were £nil (2005: 0.20p) and £nil (2005: 0.19p) respectively.

The number of shares in issue at 31 December 2006 was 6,532,261,961 (2005: 6,507,421,932).

1. Weighted average number of shares

17. SHARE-BASED PAYMENTS

The fair values of the share grants made during the year have been calculated using the following assumptions:

	SAYE	SAYE	PSP
Award date	13 Apr 06	25 Aug 06	24 Apr 06
Weighted average share price	141p	129p	139p
Weighted average exercise price	117p	101p	n/a
Expected volatility	25 – 35%	22 – 35%	n/a
Expected life	3 – 7 years	3 – 7 years	3 years
Risk free investment rate	4.6%	4.7 – 4.9%	n/a
Dividend yield	4.2%	4.1%	n/a

Expected volatility is a measure of the tendency of a security price to fluctuate in a random, unpredictable manner. Expected volatility is determined by calculating the historical volatility of the Group's share price over the previous ten years. The expected life has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

17. SHARE-BASED PAYMENTS continued

The Group provides the following equity settled share-based long term incentive plans for directors and eligible employees:

Savings related share option scheme (SAYE)

The SAYE allows employees to enter into a regular savings contract over either three, five or seven years, coupled with a corresponding option over shares of the Group. The grant price is equal to 80% of the quoted market price of the Group shares on the invitation date. Options are normally forfeited if the employee leaves the Group before the options vest.

	Options 2006	**Weighted average exercise price 2006 p**	Options 2005	Weighted average exercise price 2005 p
Outstanding at 1 January	**46,596,785**	**63**	47,968,315	63
Granted during the year	**13,066,802**	**109**	3,954,778	92
Forfeited during the year	**(749,812)**	**81**	(1,052,309)	61
Exercised during the year	**(19,515,404)**	**57**	(1,281,821)	81
Expired during the year	**(4,462,422)**	**107**	(2,992,178)	92
Outstanding at 31 December	**34,935,949**	**77**	46,596,785	63
Exercisable at 31 December	**186,023**	**90**	482,952	105

The fair values of the SAYE options granted during the year have been estimated using the Black-Scholes model. The assumptions used in the model are shown on page 76. The weighted average fair value of each SAYE option granted during the year was 35p (2005: 31p). The Group recognised total expenses of £2m (2005: £2m) related to the SAYE scheme. The intrinsic value of vested SAYE options was £nil (2005: £nil) at the year end. Intrinsic value of a share option is calculated as the current share price less the option price.

Company share option scheme (CSOP)/Executive share option scheme (ESOS)

The CSOP, approved by HMRC, and unapproved ESOS were designed to provide a long term incentive to directors and managers of the Group. The number of options granted is based on the manager's level, salary and performance. The options have a ten year life but do not normally vest in the first three years. In order to exercise the options, the Legal & General Total Shareholder Return (TSR) must exceed the median TSR of the FTSE 100 for a period of at least three years commencing on the date of the grant. Options are normally forfeited if the employee leaves the Group before the options vest.

	Options 2006	**Weighted average exercise price 2006 p**	Options 2005	Weighted average exercise price 2005 p
Outstanding at 1 January	**54,394,602**	**131**	55,122,387	131
Forfeited during the year	**(3,941,409)**	**133**	(399,511)	133
Exercised during the year	**(5,324,625)**	**79**	(180,628)	71
Expired during the year	**(3,776,552)**	**153**	(147,646)	155
Outstanding at 31 December	**41,352,016**	**136**	54,394,602	131
Exercisable at 31 December	**39,667,016**	**138**	38,145,502	153

The fair values of the options granted under the CSOP/ESOS are estimated using a binomial model, reflecting the historic exercise patterns. The assumptions used in the model are disclosed on page 76. No options were granted in 2006 or 2005 under these schemes.

The Group recognised total expenses of £nil (2005: £1m) related to the CSOP and ESOS. The intrinsic value of vested share options at the year end was £8m (2005: £nil).

Share bonus plan (SBP)

SBP awards granted before 2005 gave the recipient the right to receive a fixed number of shares three years after the grant date. SBP grants from 2005 award restricted shares which vest with employees three years after the grant date. From 2005 SBP grant recipients are entitled to both vote and receive dividends. In both cases the rights associated with SBP grants are normally forfeited on leaving the Group.

The fair value of the shares awarded has been calculated as the market value on the grant date. For pre-2005 awards, this has been adjusted by the estimated present value of future dividends to which the holder is not entitled.

During the year, 5,391,862 shares (2005: 6,080,335 shares) were awarded under the SBP. The weighted average fair value of the shares issued was 140p (2005: 113p). The Group recognised a total expense of £5m (2005: £4m) relating to the SBP.

17. SHARE-BASED PAYMENTS continued

Performance share plan (PSP)

Conditional shares can be granted to top managers under the PSP, based upon individual and Company performance. Under the PSP, the number of performance shares transferred to the individual at the end of the three year vesting period is dependant on Legal & General's TSR compared with that of the other FTSE 100 companies at the date of the award, measured over the vesting period. The minimum number of performance shares is transferred if the TSR is at median. The number increases proportionately to a maximum of four times the performance shares at or above 20th position.

The fair value of the granted performance shares has been calculated using a probabilistic model which incorporates the market-based performance conditions within the scheme.

During the year, 2,311,828 performance shares (2005: 2,184,481) were awarded. The weighted average fair value of each award issued was 279p (2005: 220p). The Group recognised a total expense of £5m (2005: £3m) relating to the PSP during the year.

Employee share plan (ESP)

Under the ESP, approved by HMRC, permanent UK employees may elect to purchase Group shares from the market at the prevailing market price on a monthly basis. The Group supplements the number of shares purchased by matching the first £20 of the employees' contributions. From time to time, the Group may make a grant of free shares. Both the free and matching shares must be held in trust for three years before they may vest to the employee. After vesting the shares remain within the trust until they are transferred to the employee or the employee leaves the Group. The Trust is consolidated into the results of the Group with the unvested shares disclosed as treasury shares.

The fair value of the granted shares is equal to the market value at the grant date.

During the year, 4,086,631 shares (2005: 3,959,530 shares) were granted under the ESP. The weighted average fair value of the shares issued was 136p (2005: 113p). The Group recognised a total expense of £3m (2005: £3m) relating to the ESP during the year.

Total recognised expense

The total recognised expense relating to share based payments in 2006 was £15m (2005: £13m), all of which related to equity settled share schemes.

Total options

Options over 76,287,965 shares are outstanding under CSOP, ESOS and SAYE at 31 December 2006 as shown below:

Option price pence per share	Number of shares	Option period ending in	Option price pence per share	Number of shares	Option period ending in
50.01 – 60.00	**16,469,778**	**2007 – 2010**	**110.01 – 120.00**	**3,682,378**	**2007 – 2012**
60.01 – 70.00	**–**	**–**	**120.01 – 130.00**	**148,902**	**2007 – 2009**
70.01 – 80.00	**11,997,735**	**2007 – 2013**	**130.01 – 140.00**	**37,390**	**2007**
80.01 – 90.00	**2,541,572**	**2008 – 2012**	**140.01 – 150.00**	**18,512,684**	**2011 – 2012**
90.01 – 100.00	**3,005,222**	**2008 – 2014**	**150.01 – 160.00**	**7,686,492**	**2010**
100.01 – 110.00	**7,092,258**	**2009 – 2013**	**160.01 – 170.00**	**5,113,554**	**2009**

18. PLANT AND EQUIPMENT

	2006 £m	2005 £m
Cost		
Balance at 1 January	**101**	124
Additions	**28**	24
Disposals	**(25)**	(47)
Balance at 31 December	**104**	101
Depreciation		
Balance at 1 January	**69**	101
Provided during the year	**15**	14
Disposals	**(23)**	(46)
Balance at 31 December	**61**	69
Net book value at 31 December	**43**	32

19. INVESTMENT PROPERTY

	Linked 2006 £m	**Other 2006 £m**	**Total 2006 £m**	Linked 2005 £m	Other 2005 £m	Total 2005 £m
Fair value at 1 January	**2,121**	**3,653**	**5,774**	1,041	3,862	4,903
Additions	**918**	**1,037**	**1,955**	937	70	1,007
Improvements	**16**	**118**	**134**	19	36	55
Disposals	**(307)**	**(939)**	**(1,246)**	(16)	(607)	(623)
Fair value gain	**166**	**69**	**235**	140	294	434
Exchange revaluation	**–**	**–**	**–**	–	(2)	(2)
Fair value at 31 December	**2,914**	**3,938**	**6,852**	2,121	3,653	5,774

20. FINANCIAL INVESTMENTS

	Linked 2006 £m	Other 2006 £m	Total 2006 £m	Linked 2005 £m	Other 2005 £m	Total 2005 £m
Financial investments at fair value designated as:						
Fair value through profit or loss	**162,451**	**36,838**	**199,289**	137,911	37,030	174,941
Available-for-sale	**–**	**1,255**	**1,255**	–	1,105	1,105
Held for trading	**37**	**39**	**76**	4	26	30
Financial investments at fair value (i)	**162,488**	**38,132**	**200,620**	137,915	38,161	176,076
Loans and receivables (ii)	**567**	**243**	**810**	331	215	546
Total financial investments	**163,055**	**38,375**	**201,430**	138,246	38,376	176,622
Expected to be settled within 12 months			**24,373**			20,915
Expected to be settled after 12 months			**177,057**			155,707

Investment risks on linked assets are borne by the policyholders.

Financial investments include £75m (2005: £63m) of debt securities pledged as collateral against derivative liabilities. The assets used as collateral are AAA rated Supranational Bonds (2005: UK gilts) having a residual maturity of over 15 years (2005: 25 years). The Group is entitled to receive all of the cash flows from the asset during the period when it is pledged as collateral. Further, there is no obligation to pay or transfer these cash flows to another entity. The Group can decide to substitute an asset which is designated as collateral at any time, provided the relevant terms and conditions of the International Swap Dealers Association (ISDA) agreement are met.

Financial investments have been allocated between those expected to be settled within 12 months and after 12 months in line with the expected settlement of the backed liabilities. Assets in excess of the insurance and investment contract liabilities have been classified as expected to be settled after 12 months.

(i) Financial investments at fair value

	Linked 2006 £m	Other 2006 £m	Total 2006 £m	Linked 2005 £m	Other 2005 £m	Total 2005 £m
Equity securities	**103,937**	**12,842**	**116,779**	89,324	12,894	102,218
Debt securities	**57,848**	**24,837**	**82,685**	48,068	24,873	72,941
Accrued interest	**666**	**413**	**1,079**	519	368	887
Derivative assets (Note 21)	**37**	**40**	**77**	4	26	30
Total investments at fair value	**162,488**	**38,132**	**200,620**	137,915	38,161	176,076

Venture capital investments are included within equity securities. £9m (2005: £4m) has been recognised in the income statement in respect of the fair value losses on these investments.

Property investments which are held via partnerships or unit trust vehicles are also included within equity securities. £198m (2005: £162m) has been recognised in the income statement in respect of the movement in fair value of these investments.

Included within linked equity securities are £308m (2005: £223m) of debt instruments which incorporate an embedded derivative linked to the value of the Group's share price.

(ii) Loans and receivables

	Linked 2006 £m	Other 2006 £m	Total 2006 £m	Linked 2005 £m	Other 2005 £m	Total 2005 £m
Deposits with credit institutions	**567**	**178**	**745**	331	143	474
Policy loans	**–**	**63**	**63**	–	71	71
Other loans	**–**	**2**	**2**	–	1	1
Total loans and receivables	**567**	**243**	**810**	331	215	546

There are no material differences between the carrying values reflected above and the fair value of these loans.

21. DERIVATIVE ASSETS AND LIABILITIES

	Contract/ notional amount 2006 £m	Fair values Assets 2006 £m	Fair values Liabilities[1] 2006 £m
Non-linked derivatives:			
Convertible debt derivative liability	**–**	**–**	**–**
Interest rate contracts – fair value hedges	**411**	**–**	**17**
Interest rate contracts – cash flow hedges	**–**	**–**	**–**
Interest rate contracts – held for trading	**2,029**	**30**	**112**
Forward foreign exchange contracts – net investment hedges	**446**	**1**	**2**
Forward foreign exchange contracts – held for trading	**405**	**6**	**1**
Equity/index derivatives – held for trading	**142**	**2**	**–**
Other derivatives – held for trading[2]	**47**	**1**	**–**
Total non-linked derivatives		**40**	**132**
Linked derivatives:			
Inflation swap contracts – held for trading[3]	**2,574**	**2**	**8**
Interest rate contracts – held for trading	**530**	**9**	**25**
Forward foreign exchange contracts – held for trading	**–**	**23**	**8**
Equity/index derivatives – held for trading	**355**	**3**	**4**
Total linked derivatives		**37**	**45**
Total derivative assets and liabilities		**77**	**177**

	Contract/ notional amount 2005 £m	Fair values Assets 2005 £m	Fair values Liabilities[1] 2005 £m
Non-linked derivatives:			
Convertible debt derivative liability	525	–	3
Interest rate contracts – fair value hedges	411	4	–
Interest rate contracts – cash flow hedges	20	–	–
Interest rate contracts – held for trading	981	6	92
Forward foreign exchange contracts – net investment hedges	316	–	3
Forward foreign exchange contracts – held for trading	411	13	–
Equity/index derivatives – held for trading	99	3	–
Other derivatives – held for trading	1	–	–
Total non-linked derivatives		26	98
Linked derivatives:			
Inflation swap contracts – held for trading	–	–	–
Interest rate contracts – held for trading	–	2	2
Forward foreign exchange contracts – held for trading	–	–	17
Equity/index derivatives – held for trading	71	2	1
Total linked derivatives		4	20
Total derivative assets and liabilities		30	118

1. Derivative liabilities are reported in the balance sheet within other creditors.
2. Relates to currency swap contracts entered into in the year (2005: £nil).
3. The inflation rate swap contracts have been entered into as part of the change in the annuity investment strategy, as described in Note 2.

21. DERIVATIVE ASSETS AND LIABILITIES continued

The notional amounts of some derivative instruments provide a basis for comparison with instruments recognised on the balance sheet. However, these amounts do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit or price risks.

Net investment hedges – forward foreign exchange contracts
The Group hedges part of the foreign exchange translation exposure on its net investment in its overseas subsidiaries, using forward foreign exchange contracts. It recognises the portion of the gain or loss which is determined to be an effective hedge through reserves within shareholders' equity, along with the gain or loss on revaluation of the foreign subsidiaries.

Fair value hedges – interest rate swap contracts
The Group uses interest rate swap contracts to hedge fixed rate loans in particular to hedge the movement in the fair value of a loan due to interest rates.

Cash flow hedges – interest rate swap contracts
The Group uses interest rate swap contracts to hedge the variability of future interest payments on certain floating rate financial instruments. Hedge accounting defers the recognition of gains and losses on the hedging instrument until the cash flow being hedged appears in the income statement.

Derivative contracts – held for trading
The Group uses certain derivative contracts which are effective hedges of economic exposures but are not designated within a formal hedge accounting relationship. Gains and losses on these contracts are recognised immediately in the income statement.

22. REINSURERS' SHARE OF CONTRACT LIABILITIES

	2006 £m	2005 £m
Reinsurers' share of:		
Insurance contract liabilities (Note 33)	**1,254**	2,664
Investment contract liabilities (Note 34)	**227**	115
Reinsurers' share of contract liabilities	**1,481**	2,779

23. PURCHASED INTEREST IN LONG TERM BUSINESSES

	2006 £m	2005 £m
Net balance at 1 January	**25**	24
Amortisation charged to income	**(7)**	(4)
Net exchange difference	**(2)**	1
Other	**7**	4
Net balance at 31 December	**23**	25
Accumulated amortisation at 31 December	**154**	154
To be amortised within 12 months	**4**	5
To be amortised after 12 months	**19**	20

The net book value of purchased interest in long term businesses represents the remaining unamortised portion of the fair values of purchased long term in-force businesses which is amortised over their economic lives.

24. DEFERRED ACQUISITION COSTS

(i) Analysis of deferred acquisition costs

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Insurance contract deferred acquisition costs (ii)	**695**	**(69)**	897	(78)
Investment contract deferred acquisition costs (iii)	**761**	**–**	478	–
Deferred acquisition costs	**1,456**	**(69)**	1,375	(78)

(ii) Insurance contract deferred acquisition costs

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**897**	**(78)**	772	(71)
Acquisition costs deferred	**231**	**(1)**	238	(1)
Amortisation charged to income	**(251)**	**5**	(244)	6
(Decrease)/increase due to currency translation	**(79)**	**9**	55	(8)
Other[1]	**(103)**	**(4)**	76	(4)
Balance at 31 December	**695**	**(69)**	897	(78)
To be amortised within 12 months	**133**	**(8)**	214	(9)
To be amortised after 12 months	**562**	**(61)**	683	(69)

1. Included in Other is a £145m reduction which results from the adoption of the provisions of PS06/14 which has resulted in the acceleration of the recognition of margins previously used to support the deferral of these costs. The related deferred acquisition costs have therefore been charged to the income statement during the period. The implementation of PS06/14 is described in Note 2.

(iii) Investment contract deferred acquisition costs

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**478**	**–**	300	–
Acquisition costs deferred	**324**	**–**	188	–
Amortisation charged to income	**(41)**	**–**	(10)	–
Decrease due to currency translation	**–**	**–**	(1)	–
Other	**–**	**–**	1	–
Balance at 31 December	**761**	**–**	478	–
To be amortised within 12 months	**52**	**–**	37	–
To be amortised after 12 months	**709**	**–**	441	–

25. INCOME TAX

	2006 £m	2005 £m
Due within 12 months	**5**	19
Due after 12 months	**7**	60
Income tax recoverable	**12**	79

	2006 £m	2005 £m
Due within 12 months	**245**	301
Due after 12 months	**(139)**	(104)
Income tax liabilities	**106**	197

26. OTHER ASSETS

	2006 £m	2005 £m
Reinsurance debtors	**83**	153
Accrued interest and rent	**135**	147
Prepayments and accrued income	**258**	236
Other debtors		
– Linked	**297**	167
– Other	**849**	459
Other assets	**1,622**	1,162
Due within 12 months	**1,617**	1,161
Due after 12 months	**5**	1

27. CASH AND CASH EQUIVALENTS

	2006 £m	2005 £m
Cash at bank and in hand	**216**	181
Cash equivalents	**4,714**	3,820
Cash and cash equivalents	**4,930**	4,001

Cash and cash equivalents of £4,214m (2005: £3,132m) held within UK LTFs are not available to settle liabilities outside the LTFs.

28. SHARE CAPITAL, SHARE PREMIUM AND TREASURY SHARES

(i) Share capital and share premium

Authorised share capital	2006 Number of shares	2006 £m	2005 £m
At 31 December: ordinary shares of 2.5p each	**9,200,000,000**	**230**	230

Issued share capital, fully paid	Number of shares	Share capital £m	Share premium £m
Balance at 1 January 2006	**6,507,421,932**	**163**	**908**
Options exercised under share option schemes			
– Executive share option scheme (Note 17)	**5,324,625**	**–**	**4**
– Savings related share option scheme (Note 17)	**19,515,404**	**–**	**11**
Balance at 31 December 2006	**6,532,261,961**	**163**	**923**
Balance at 1 January 2005	6,505,959,483	163	907
Options exercised under share option schemes			
– Executive share option scheme (Note 17)	180,628	–	–
– Savings related share option scheme (Note 17)	1,281,821	–	1
Balance at 31 December 2005	6,507,421,932	163	908

There is one class of ordinary shares. All shares issued carry equal voting rights.

The holders of the Company's ordinary shares are entitled to receive dividends as declared and are entitled to one vote per share at shareholder meetings of the Company.

(ii) Treasury shares

The Group uses the Employee Share Ownership Trust (ESOT), Employee Share Trust (EST) and the Legal & General Group Employee Share Plan (ESP) to purchase and hold shares of the Group for delivery to employees under various employee share schemes. Shares owned by these vehicles are included at cost in the consolidated balance sheet and are shown as a deduction from shareholders' equity. They are disclosed as treasury shares until they vest to employees. Share-based liabilities to employees may also be settled via purchases directly from the market or by the issue of new shares.

The ESOT has waived its voting rights and its rights to some of the dividends payable on the shares it holds. Employees are entitled to dividends on the shares held on their behalf within the EST and the ESP.

	Number of shares	2006 £m	2005 £m
Balance at 1 January	**34,310,450**	**36**	27
Shares purchased	**12,134,237**	**11**	15
Shares vested	**(5,382,943)**	**(2)**	(6)
Balance at 31 December	**41,061,744**	**45**	36

29. OTHER RESERVES

	Currency translation reserve £m	Share-based payments reserve £m	Hedging reserve £m	AFS £m	Total £m
Balance at 1 January 2006	**(2)**	**30**	**2**	**4**	**34**
Net change in financial investments designated as AFS	**–**	**–**	**–**	**7**	**7**
Net change in hedging reserve	**–**	**–**	**(3)**	**–**	**(3)**
Shares vested	**–**	**(12)**	**–**	**–**	**(12)**
Currency translation differences	**9**	**–**	**–**	**–**	**9**
Net gains/(losses) not recognised in income statement	**9**	**(12)**	**(3)**	**7**	**1**
Employee share schemes:					
– Value of employee services	**–**	**14**	**–**	**–**	**14**
Balance at 31 December 2006	**7**	**32**	**(1)**	**11**	**49**

	Currency translation reserve £m	Share-based payments reserve £m	Hedging reserve £m	AFS £m	Total £m
Balance at 1 January 2005	10	14	2	12	38
Net change in financial investments designated as AFS	–	–	–	(10)	(10)
Net change in hedging reserve	–	–	–	–	–
Shares vested	–	–	–	–	–
Currency translation differences	(12)	–	–	2	(10)
Net losses not recognised in income statement	(12)	–	–	(8)	(20)
Employee share schemes:					
– Value of employee services	–	16	–	–	16
Balance at 31 December 2005	(2)	30	2	4	34

30. RETAINED EARNINGS

	2006 £m	2005 £m
Balance at 1 January	**3,188**	2,594
Profit for the year	**1,564**	944
Dividend distributions to ordinary equity holders of the Company during the year (Note 15)	**(349)**	(331)
Distributions during the year on subordinated borrowings designated as equity (Note 15)	**–**	(16)
Actuarial gains/(losses) on defined benefit pension schemes	**3**	(55)
Actuarial (gains)/losses on defined benefit pension schemes transferred to unallocated divisible surplus	**(1)**	22
Transfer from share-based payments reserve	**2**	–
Fair value loss after tax on reclassification of subordinated borrowings as debt	**(28)**	–
Exchange (losses)/gains	**(44)**	30
Balance at 31 December	**4,335**	3,188

31. MINORITY INTERESTS

Minority interests represent third party interests in property investment vehicles which are consolidated in the Group's results.

	2006 £m	2005 £m
Balance at 1 January	**285**	214
Share of net profit in subsidiaries	**67**	81
Movement in third party interests	**62**	(10)
Balance at 31 December	**414**	285

32. TOTAL EQUITY

	2006 £m	2005 £m
Balance at 1 January	**4,936**	4,283
Total recognised income and expense	**1,602**	1,002
Issue of ordinary share capital	**15**	1
Net movements in employee share schemes and treasury shares	**(5)**	7
Dividend distributions to ordinary equity holders of the Company during the year	**(349)**	(331)
Distributions during the year on subordinated borrowings designated as equity	**–**	(16)
Movements in minority interests including disposals	**62**	(10)
Reclassification of subordinated borrowings from equity to debt	**(394)**	–
Fair value loss after tax on reclassification of subordinated borrowings as debt (Note 38)	**(28)**	–
Balance at 31 December	**5,839**	4,936

33. INSURANCE CONTRACT LIABILITIES

(i) Analysis of insurance contract liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Life and pensions participating insurance contracts (iii)	**12,660**	**(1)**	13,180	(1)
Life and pensions non-participating insurance contracts (iv)	**21,321**	**(1,237)**	22,860	(2,649)
General insurance contracts (v)	**281**	**(16)**	292	(14)
Insurance contract liabilities	**34,262**	**(1,254)**	36,332	(2,664)

(ii) Expected insurance contract net cash flows

	Date of cash flow					
As at 31 December 2006	**0-5 years £m**	**5-15 years £m**	**15-25 years £m**	**Over 25 years £m**	**Total £m**	**Carrying value £m**
Life and pensions participating insurance contracts	**7,124**	**7,086**	**1,403**	**470**	**16,083**	**12,659**
Life and pensions non-participating insurance contracts	**4,797**	**9,754**	**8,946**	**11,782**	**35,279**	**14,132**
General insurance contracts	**129**	**–**	**–**	**–**	**129**	**129**
Insurance contract liabilities	**12,050**	**16,840**	**10,349**	**12,252**	**51,491**	**26,920**

	Date of cash flow					
As at 31 December 2005	0-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m	Total £m	Carrying value £m
Life and pensions participating insurance contracts	6,366	8,068	1,592	638	16,664	12,978
Life and pensions non-participating insurance contracts	4,378	8,774	8,422	11,165	32,739	14,598
General insurance contracts	278	–	–	–	278	278
Insurance contract liabilities	11,022	16,842	10,014	11,803	49,681	27,854

Insurance contract net cash flows are based on the expected date of settlement. Unit linked contracts have been excluded from the table due to the exact matching of cash flows to those of the linked backing assets.

(iii) Movement in participating insurance contract liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**13,180**	**(1)**	12,388	(1)
New liabilities in the year	**240**	**–**	224	–
Liabilities discharged in the year	**(1,671)**	**–**	(1,142)	–
Unwinding of discount rates	**432**	**–**	402	–
Effect of change in non-economic assumptions	**29**	**–**	305	–
Effect of change in economic assumptions	**487**	**–**	1,148	–
Other	**(37)**	**–**	(145)	–
Balance at 31 December	**12,660**	**(1)**	13,180	(1)
Expected to be settled within 12 months (net of reinsurance)	**1,431**		1,153	
Expected to be settled after 12 months (net of reinsurance)	**11,228**		12,026	

In 2005, the largest impact of changes to non-economic assumptions was from the strengthening of the provision for claims on the endowment book (£240m). The assumption setting process is outlined in Note 37.

33. INSURANCE CONTRACT LIABILITIES continued

(iv) Movement in non-participating insurance contract liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**22,860**	**(2,649)**	20,509	(2,887)
New liabilities in the year	**1,995**	**(287)**	2,370	(457)
Liabilities discharged in the year	**(1,630)**	**75**	(1,350)	215
Unwinding of discount rates	**958**	**(134)**	926	(225)
Effect of change in non-economic assumptions	**90**	**(33)**	(709)	706
Effect of change in economic assumptions	**(417)**	**9**	899	(1)
Foreign exchange adjustments	**(176)**	**26**	95	(19)
Other	**(2,359)**	**1,756**	120	19
Balance at 31 December	**21,321**	**(1,237)**	22,860	(2,649)
Expected to be settled within 12 months (net of reinsurance)	**1,492**		1,244	
Expected to be settled after 12 months (net of reinsurance)	**18,592**		18,967	

Included within Effect of economic assumption changes is the impact of Society's review of its annuity investment policy as described in Note 2.

In 2006, Other includes £2,248m gross (£1,756m reinsurance) relating to the impact of applying PS06/14. The implementation of PS06/14 is described in Note 2.

(v) Analysis of General insurance contract liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Outstanding claims	**101**	**(4)**	97	(5)
Claims incurred but not reported	**36**	**(1)**	45	–
Unearned premiums	**144**	**(11)**	150	(9)
General insurance contract liabilities	**281**	**(16)**	292	(14)

(vi) Movement in General insurance claim liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**142**	**(5)**	180	(6)
Claims arising	**247**	**(3)**	272	(6)
Claims paid	**(206)**	**2**	(219)	6
Adjustments to prior year liabilities	**(46)**	**1**	(38)	1
	137	**(5)**	195	(5)
Disposal of Gresham	**–**	**–**	(53)	–
Balance at 31 December	**137**	**(5)**	142	(5)
Expected to be settled within 12 months (net of reinsurance)	**85**		91	
Expected to be settled after 12 months (net of reinsurance)	**47**		46	

(vii) Unearned premiums

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**150**	**(9)**	223	(16)
Earned in the period	**(150)**	**(11)**	(145)	(9)
Gross written premiums in respect of future periods	**144**	**9**	150	12
Disposal of Gresham	**–**	**–**	(78)	4
Balance at 31 December	**144**	**(11)**	150	(9)
Expected to be settled within 12 months (net of reinsurance)	**131**		138	
Expected to be settled after 12 months (net of reinsurance)	**2**		3	

33. INSURANCE CONTRACT LIABILITIES continued

(viii) Claims development – General insurance

Changes may occur in the amount of the Group's obligations at the end of a contract period. The top section of each table below illustrates how the estimate of total claims outstanding for each accident year developed over time. The bottom section of the table reconciles the cumulative claims to the amount appearing in the balance sheet. The claims development tables exclude amounts relating to Gresham which was disposed of in 2005.

Gross of reinsurance

Accident year	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	Total £m
Estimate of ultimate claims costs:						
– At end of accident year	137	147	171	209	205	
– One year later	133	145	166	195	–	
– Two years later	133	141	160	–	–	
– Three years later	132	142	–	–	–	
– Four years later	133	–	–	–	–	
Estimate of cumulative claims	133	142	160	195	205	835
Cumulative payments	(131)	(135)	(151)	(172)	(121)	(710)
Outstanding claims provision	2	7	9	23	84	125
Prior period outstanding claims						9
Claims handling provision						3
Total claims liabilities recognised in the balance sheet						137

Net of reinsurance

Accident year	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	Total £m
Estimate of ultimate claims costs:						
– At end of accident year	134	142	162	205	200	
– One year later	130	140	161	193	–	
– Two years later	130	137	157	–	–	
– Three years later	129	139	–	–	–	
– Four years later	129	–	–	–	–	
Estimate of cumulative claims	129	139	157	193	200	818
Cumulative payments	(127)	(132)	(149)	(171)	(119)	(698)
Outstanding claims provision	2	7	8	22	81	120
Prior period outstanding claims						9
Claims handling provision						3
Total claims liabilities recognised in the balance sheet						132

34. INVESTMENT CONTRACT LIABILITIES

(i) Analysis of investment contract liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Participating investment contracts	**7,501**	**(88)**	7,476	(64)
Non-participating investment contracts	**162,016**	**(139)**	135,804	(51)
Investment contract liabilities (ii)	**169,517**	**(227)**	143,280	(115)
Expected to be settled within 12 months (net of reinsurance)	**21,365**		18,518	
Expected to be settled after 12 months (net of reinsurance)	**147,925**		124,647	

The UK participating liabilities are valued under the requirements of FRS 27.

(ii) Movement in investment contract liabilities

	Gross 2006 £m	Reinsurance 2006 £m	Gross 2005 £m	Reinsurance 2005 £m
Balance at 1 January	**143,280**	**(115)**	110,144	(67)
Reserves in respect of new business	**28,423**	**(93)**	24,542	(31)
Amounts paid on surrenders and maturities during the year	**(15,633)**	**3**	(12,389)	1
Investment return and related benefits	**13,804**	**(22)**	21,289	(18)
Management charges	**(339)**	**–**	(269)	–
Foreign exchange adjustments	**(18)**	**–**	(37)	–
Balance at 31 December	**169,517**	**(227)**	143,280	(115)

Fair value movements of £13,393m (2005: £20,483m) are included within the income statement arising from movements in investment contract liabilities designated as FVTPL.

35. UNALLOCATED DIVISIBLE SURPLUS

	2006 £m	2005 £m
Balance at 1 January	**1,894**	1,559
Transferred from the income statement	**284**	360
Actuarial gains/(losses) on defined benefit pension schemes transferred from the SORIE	**1**	(22)
Foreign exchange adjustments	**(1)**	(3)
Balance at 31 December	**2,178**	1,894

Unallocated divisible surplus is expected to be allocated after more than 12 months.

36. VALUE OF IN-FORCE NON-PARTICIPATING CONTRACTS

	2006 £m	2005 £m
Balance at 1 January	**379**	434
Unwinding of the discount rates	**18**	30
Investment return	**(1)**	39
Change in valuation approach	**–**	(53)
Other	**(5)**	(71)
Balance at 31 December	**391**	379
Expected to be settled within 12 months	**47**	39
Expected to be settled after 12 months	**344**	340

37. LONG TERM INSURANCE VALUATION ASSUMPTIONS

The Group's insurance assumptions, described below, relate exclusively to the UK insurance business. The non-UK businesses do not constitute a material component of the Group's operations and consideration of geographically determined assumptions is therefore not included.

Non-participating business

For its non-participating business the Group seeks to make prudent assumptions about its future experience based on current market conditions and recent experience. The approach used to set non-participating assumptions is generally similar to that used to determine the assumptions used for FSA statutory peak 1, although the actual assumptions may sometimes differ from those used for regulatory reporting purposes. These assumptions incorporate margins to reduce the possibility of actual experience being less favourable than assumed.

During the year, the regulatory requirements for the measurement of non-participating contracts were amended by the FSA's Policy Statement 06/14 (PS06/14) which introduced a more realistic reserving framework. For the Group, the principal impacts on the valuation assumptions are:

- the liability for individual non-participating contracts with no guaranteed surrender value is now permitted to be negative; and
- the persistency assumption now allows for the expected pattern of persistency, adjusted to incorporate a margin for adverse deviation, (a prudent persistency basis).

The effect of these changes (which have been applied to the Group's protection business) on technical provisions, net of reinsurance, is shown below:

	2006 £m
Allowance for lapses	**(79)**
Allowance for negative reserves	**(562)**

Valuation rates of interest and discount rates

The valuation interest rate for each contract type is based on the yield on the assets backing the contract. This yield is the gross redemption yield on fixed interest securities and the running yield on variable interest securities. For corporate debt, yields are adjusted to reflect the risk of default associated with these investments. The adjustment is based on historic published information by credit rating agencies. For equity investments, the yield is based on the current dividend yield, adjusted for prudence. For property holdings, yields are based on the rental income payable calculated by considering different categories of tenant separately, adjusted for the possibility of default. Default rates used in the calculation vary by tenant category.

Mortality and morbidity

Mortality and morbidity assumptions are set with reference to standard tables drawn up by the Continuous Mortality Investigation Bureau (CMIB) of the Institute and Faculty of Actuaries. These tables are based on industry wide experience.

The majority of internal statistical investigations are carried out at least annually to determine the extent to which the Group's experience differs from that of the industry and suggest appropriate adjustments which need to be made to the valuation assumptions.

Persistency

The Group monitors its persistency experience and carries out detailed investigations annually. Persistency can be volatile and past experience may not be an appropriate future indicator.

The Group tries to balance past experience and future conditions by making prudent assumptions about the future expected long term average persistency levels.

For non profit non-protection contracts, this prudence is also incorporated into the liabilities by ensuring that they are sufficient to cover the more onerous of the two scenarios where the policies either remain in-force until maturity or where they discontinue at the valuation date.

For non profit protection contracts, a prudent persistency basis has been assumed for the first time, as described earlier.

Expenses

The Group monitors its expense experience and carries out detailed investigations regularly to determine the expenses incurred in writing and administering the different products and classes of business. Adjustments may be made for known future changes in the administration processes, in line with the Group's business plan. An allowance for expense inflation in the future is also made, taking account of both salary and price information.

Participating business

For its participating business the Group seeks to establish its liabilities at their realistic value in line with the requirements set out in FRS 27 'Life Assurance'.

Non-economic assumptions are set to represent the Group's best estimates of future experience.

Economic assumptions

Realistic valuation requires a market consistent economic model. The model is calibrated using market data from a variety of market sources. This enables assumptions to be determined for the term structure of risk free interest rates, property and equity volatility. Risk free interest rates are determined with reference to the gilt yield curve on the valuation date increased by ten basis points.

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.

Future bonuses

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

Value of in-force non-participating contracts

The Group makes a deduction from the liabilities for the expected value of future profits arising on non-participating contracts written in the with-profits part of the Society LTF.

The economic assumptions used to calculate the value of these profits are consistent with those used to calculate liabilities for with-profits participating business. Non-economic assumptions represent best estimates of expected future experience on this business.

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.

37. LONG TERM INSURANCE VALUATION ASSUMPTIONS continued

The table below sets out the current valuation assumptions used to establish the long term liabilities for Society, LGP, and Legal & General Assurance (Pensions Management) Limited.

Full disclosure of the valuation assumptions are set out in the Abstract of the Valuation Report contained within the FSA returns.

	2006	2005
Rate of interest/discount rates		
Non-participating business		
Life assurances	**3.00% pa and 7.60% pa**[1]	3.00% pa
Pension assurances	**3.00 – 4.00% pa and 7.60% pa**[1]	3.00 – 4.00% pa
Annuities in deferment	**4.11 – 4.80% pa**	2.65 – 4.45% pa
Annuities in deferment (RPI-linked; net rate after allowance for inflation)	**0.89 – 1.65% pa**	0.65 – 1.50% pa
Vested annuities	**4.72 – 4.80% pa**	4.45% pa
Vested annuities (RPI-linked; net rate after allowance for inflation)	**1.20 – 1.65% pa**	1.50% pa
Participating business		
Risk free rate (10 years)	**4.84% pa**	4.24% pa
Future bonuses	**Determined stochastically in line with bonus policy as stated in PPFM**	Determined stochastically in line with bonus policy as stated in PPFM
UK equity volatility (10 year option term)	**21.5%**	22.2%
Property volatility	**15.0%**	15.0%
Mortality tables		
Non-participating business		
Non-linked individual term assurances:		
Smokers	**125 – 145% TMS00/TFS00 Sel 5**[2]	125 – 166% TMS00/TFS00 Sel 5[2]
Non-smokers	**105 – 110% TMN00/TFN00 Sel 5**[2]	105 – 110% TMN00/TFN00 Sel 5[2]
Smoker status unknown	**145% TM00/TF00 Sel 5**[2]	140% TM00/TF00 Sel 5[2]
Non-linked individual term assurances with critical illness	**63 – 108% CIBT93M/F Ult Comb**[2]	63 – 108% CIBT93M/F Ult Comb[2]
Other non-linked non profit life assurances	**A67/70 suitably age adjusted**	A67/70 suitably age adjusted
Annuities in deferment	**75 – 85% AM92/AF92**	80% A67/70 Ult-3 yrs
Vested annuities[3]		
Bulk purchase annuities	**97 – 102% PCMA00/PCFA00**	101 – 104% PCMA00/PCFA00
Other annuities	**50 – 92% PCMA00/PCFA00**	48 – 94% PCMA00/PCFA00

1. For product groups where liabilities are positive, the lower interest rate of 3.00-4.00% is used. However, for product groups where liabilities are negative, the higher rate of 7.60% is used.
2. For term assurance, mortality rates are assumed to increase at a rate of 0.5% pa. For term assurance with critical illness, morbidity rates are assumed to deteriorate at a rate of 1% pa for males and 1.75% pa for females. There is also an allowance for AIDS of 33% (Institute of Actuaries AIDS Working Party Bulletin No. 5 projection R6A).
3. For vested annuities, mortality rates are assumed to reduce according to the average of CMI Working Paper 1 projection MC and LC with a minimum of 0.8% pa for males and according to CMI projection MC with a minimum of 0.8% pa for females. For certain annuities a further allowance is made for the effect of initial selection.

37. LONG TERM INSURANCE VALUATION ASSUMPTIONS continued

Premiums – non-participating business
For those contracts where the policyholder does not have the right to vary the amount of the premium paid, full credit is taken for the premiums contractually due at the valuation date. For contracts where the policyholder has the option to vary the rate of premium, the provision is taken as being the higher of the amount calculated as if the policyholder continues to make premium payments or, alternatively, ceases to pay premiums altogether.

Persistency – non-participating business
At 31 December 2005, valuation liabilities were calculated as being the greater of the liability assuming that the contract continues in-force until maturity, or discontinues at the valuation date. The one exception to this was for certain term assurances where there is a liability to reinsurers on discontinuance within the first four years from inception and provisions were calculated assuming lapse rates as follows:

	2005
Year 1	10%
Year 2	15%
Year 3	25%
Year 4	25%

For all years after Year 4 a nil lapse rate was assumed.

With the introduction of PS06/14 at 31 December 2006, it is permissible to value all long term business assuming a prudent lapse basis. The approach taken as at the end of 2005 has therefore changed for non-participating protection business. For this business, the valuation persistency basis is set by applying a prudential margin over the best estimate assumptions. The margin acts to increase the best estimate lapse rate in the early part of a policy's lifetime (when it is being treated as an asset) but to reduce the best estimate lapse rate later in the policy's lifetime (when it is treated as a liability). The crossover point at which the margin changes direction is assessed for broad product groups but applied at a policy by policy level. Any liability to reinsurers on discontinuance within the first four years from inception is allowed for explicitly in the cash flows using the valuation lapse basis, together with a prudent allowance for clawback of commission from agents upon lapse. A summary of the lapse basis for major classes of business, as defined by the requirements of the annual returns to the FSA, is shown below.

	2006 average lapse rate for the policy years			
Product	**1-5** %	**6-10** %	**11-15** %	**16-20** %
Level term	**12.2**	**9.7**	**3.2**	**3.2**
Decreasing term	**12.2**	**10.1**	**6.0**	**5.9**
Accelerated critical illness cover	**16.7**	**11.2**	**5.7**	**5.6**
Pensions term	**10.5**	**9.1**	**5.4**	**5.2**

Overseas Business
In calculating the long term business provisions for international long term business operations, local actuarial tables and interest rates are used.

Endowment reserve
The endowment reserve has been set taking reasonable account of an assessment of the expected future population of complaints, the expected uphold rate for these complaints, the potential impact of any Financial Ombudsman Service decisions on referred complaints and the average compensation per complaint.

38. BORROWINGS

Analysis by nature

	Carrying amount 2006 £m	Coupon rate 2006 %	Fair value 2006 £m	Carrying amount 2005 £m	Coupon rate 2005 %	Fair value 2005 £m
Subordinated borrowings designated as equity						
5.875% sterling undated subordinated notes	–	–	–	394	5.88	434
Subordinated borrowings						
5.875% sterling undated subordinated notes	429	5.88	411	–	–	–
4.0% Euro subordinated notes 2025	389	4.00	397	415	4.00	424
Total subordinated borrowings	818		808	809		858
Senior borrowings						
2.75% sterling convertible bond 2006	–	–	–	509	2.75	521
Sterling medium term notes 2031-2041	608	5.87	682	608	5.87	716
Euro commercial paper 2007	370	4.66	370	110	2.30	110
Bank loans 2007	3	5.28	3	6	4.90	6
Non recourse financing						
– US Dollar Triple X securitisation 2025	270	5.37	270	308	4.40	308
– US Dollar Triple X securitisation 2037	226	5.72	226	–	–	–
– Sterling property partnership loans 2011	130	5.91	130	93	5.50	93
Total senior borrowings	1,607		1,681	1,634		1,754
Total borrowings	2,425		2,489	2,443		2,612
Total borrowings (excluding non recourse financing)	1,799		1,863	2,042		2,211

During 2006, £602m of borrowings which were previously attributed to the SRC were attributed to Society shareholders. £106m of interest expense was incurred during the period (2005: £75m) on borrowings (excluding non recourse financing).

Subordinated borrowings
The sterling undated subordinated notes are treated as upper tier II capital for regulatory purposes and the Euro dated subordinated notes as lower tier II capital.

5.875% sterling undated subordinated notes
Legal & General Group Plc has issued £400m of 5.875% undated subordinated notes. These notes are callable on 1 April 2019 and every five years thereafter. If not called, the coupon from 1 April 2019 will be reset to the prevailing five year benchmark gilt yield plus 2.33% per annum. As at 31 December 2005 the undated subordinated notes were classified as equity because their perpetual nature meant that in certain circumstances interest could be deferred indefinitely. On 13 March 2006 the Group entered into a supplementary deed to remove the discretionary nature of the interest in certain circumstances. This had the effect of reclassifying the notes from equity to liability and coupon payments from distributions to interest. Upon reclassification the debt was recognised at fair value.

4.0% Euro subordinated notes 2025
Legal & General Group Plc has also issued €600m of 4.0% Euro dated subordinated notes. The proceeds were swapped into sterling. The notes are callable on 8 June 2015 and each year thereafter. If not called, the coupon from 8 June 2015 will reset to a floating rate of interest based on prevailing three month Euribor plus 1.7% per annum.

Non recourse financing

US Dollar Triple X securitisation 2025
A subsidiary of Legal & General America has issued US$550m of non recourse debt in the US capital markets to meet the Triple X reserve requirements on the US term insurance business. It is secured on the cash flows related to this business.

US Dollar Triple X securitisation 2037
In 2006, a subsidiary of Legal & General America issued US$450m of non recourse debt in the US capital markets to meet the Triple X reserve requirements on the US term insurance business. It is secured on the cash flows related to this business.

Sterling property partnership loans 2011
The property partnership loans are secured on specific properties.

38. BORROWINGS continued

Analysis by maturity

As at 31 December 2006	Effective interest rate %	Carrying amount £m	Maturity Within 1 year £m	1-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m
Subordinated borrowings designated as equity							
5.875% sterling undated subordinated notes	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Subordinated borrowings							
5.875% sterling undated subordinated notes	**5.23**	**429**	**–**	**–**	**–**	**–**	**429**
4.0% Euro subordinated notes 2025	**4.12**	**389**	**–**	**–**	**–**	**389**	**–**
Senior borrowings							
2.75% sterling convertible bond 2006	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Sterling medium term notes 2031-2041	**5.83**	**608**	**–**	**–**	**–**	**353**	**255**
Euro commercial paper 2007	**4.66**	**370**	**370**	**–**	**–**	**–**	**–**
Bank loans 2007	**5.28**	**3**	**3**	**–**	**–**	**–**	**–**
Non recourse financing							
– US Dollar Triple X securitisation 2025	**5.37**	**270**	**–**	**–**	**–**	**270**	**–**
– US Dollar Triple X securitisation 2037	**5.72**	**226**	**–**	**–**	**–**	**–**	**226**
– Sterling property partnership loans 2011	**5.91**	**130**	**–**	**130**	**–**	**–**	**–**
Total borrowings		**2,425**	**373**	**130**	**–**	**1,012**	**910**

As at 31 December 2005	Effective interest rate %	Carrying amount £m	Maturity Within 1 year £m	1-5 years £m	5-15 years £m	15-25 years £m	Over 25 years £m
Subordinated borrowings designated as equity							
5.875% sterling undated subordinated notes	6.03	394	–	–	–	–	394
Subordinated borrowings							
5.875% sterling undated subordinated notes	–	–	–	–	–	–	–
4.0% Euro subordinated notes 2025	4.12	415	–	–	–	415	–
Senior borrowings							
2.75% sterling convertible bond 2006	5.67	509	509	–	–	–	–
Sterling medium term notes 2031-2041	5.83	608	–	–	–	–	608
Euro commercial paper 2006	2.30	110	110	–	–	–	–
Bank loans 2006	4.90	6	6	–	–	–	–
Non recourse financing							
– US Dollar Triple X securitisation 2025	4.40	308	–	–	–	308	–
– US Dollar Triple X securitisation 2037	–	–	–	–	–	–	–
– Sterling property partnership loans 2011	5.50	93	–	–	93	–	–
Total borrowings		2,443	625	–	93	723	1,002

As at 31 December 2006 the Group had in place a five year £1bn syndicated committed revolving credit facility with a number of its key relationship banks. The facility also has a one year extension option at the end of 2007.

The maturity profile above is calculated on the basis that a facility to refinance a maturing loan is not recognised unless the facility and loan are related. If refinancing under the Group's syndicated facility was recognised, then all amounts shown as repayable within one year would be reclassified as repayable between one and five years.

The effective interest rate is the rate which discounts exactly future cash payments over the life of the borrowing and will include all transaction costs and premia or discounts on issue. For the 5.875% sterling undated subordinated notes, the effective rate includes the impact of reclassification of the notes from equity to debt on 13 March 2006 at fair value.

Convertible bond

The convertible bond matured in 2006 and was redeemed at par without being converted into ordinary shares.
The debt component, net of expenses, of the convertible bond recognised in the balance sheet is calculated as follows:

	2006 £m	2005 £m
Balance at 1 January	**509**	493
Interest expense	**30**	30
Coupons paid	**(14)**	(14)
Repayment of debt	**(525)**	–
Balance at 31 December	**–**	509

The fair value of the debt component of the convertible bond at 31 December 2005 was £517m. Interest expense on the bond was calculated using the effective interest rate of 5.7% on the debt component.

39. EVENTS AFTER THE BALANCE SHEET DATE

On 7 February 2007, the Group entered into an agreement with the Nationwide Building Society to purchase Nationwide Life Limited and Nationwide Unit Trust Managers Limited for a consideration estimated at £285m. Consideration will be set by reference to the financial position of the two companies at the date of completion using an agreed basis of valuation. In addition, the arrangement provides access to Nationwide's distribution network, through which it is anticipated that a wide range of the Group's investment, pensions and life insurance products will be sold. The sale is conditional on the consent of the FSA to the change of control of the companies, and other customary conditions, and is expected to complete in the summer of 2007, when the distribution arrangements are expected to be launched.

40. PROVISIONS

Retirement benefit obligations
Defined contribution plans
The Group operates the following defined contribution pension schemes in the UK and overseas:

- Legal & General Group Personal Pension Plan (UK).
- Legal & General Staff Stakeholder Pension Scheme (UK).
- Legal & General America Inc Savings Plan (US).
- Régime de Retraite Professionnel (France).

Contributions of £17m (2005: £16m) were charged as expenses during the year in respect of these plans.

Defined benefit plans
The Group operates the following defined benefit pension schemes in the UK and overseas:

- Legal & General Group UK Pension and Assurance Fund (the Fund). The Fund was closed to new members from January 1995; last full actuarial valuation as at 31 December 2004.
- Legal & General Group UK Senior Pension Scheme (the Scheme). The Scheme was, with a few exceptions (principally transfers from the Fund), closed to new members from August 2000; last full actuarial valuation as at 31 December 2004.
- Legal & General America Inc. Cash Balance Plan; last full actuarial valuation as at 31 December 2005.
- Legal & General Nederland Stichting Pensioenfonds; last full actuarial valuation as at 31 December 2006.
- Régime de Retraite à Prestations Définies de Legal & General (France); last full actuarial valuation as at 31 December 2006.

The benefits paid from the defined benefit schemes are based on percentages of the employees' final pensionable salary for each year of credited service. The Group has no liability for retirement benefits other than for pensions, except for a small scheme in France (Indemnites de Fin Carriere), which provides lump sum benefits on retirement. The Fund and Scheme account for virtually all of the UK and over 98% of worldwide assets of the Group's defined benefit schemes.

The principal actuarial assumptions for the UK defined benefit scheme were:

	2006 Fund and Scheme %	2005 Fund and Scheme %
Rate used to discount liabilities	**5.10**	4.70
Expected return on plan assets	**6.72**	6.59
Rate of increase in salaries	**3.60**	3.25
Rate of increase in pensions in payment	**3.25**	3.00
Rate of increase in deferred pensions	**4.00**	4.00
Rate of general inflation (RPI)	**3.20**	3.00
Rate of wage inflation	**4.00**	4.00

Post retirement mortality	
– 2006	**100% PCMA/PCFA 00 with improvement at 100% MC males, 70% MC females, minimum improvement 0.6% pa**
– 2005	100% PMA/PFA 92 with improvement at 100% MC males, 100% MC females, projected to calendar year 2010

40. PROVISIONS continued

	2006 Fund and Scheme £m	2006 Overseas £m	2005 Fund and Scheme £m	2005 Overseas £m
Change in present value of defined benefit obligations				
Balance at 1 January	**(1,284)**	**(20)**	(1,089)	(17)
Current service cost	**(18)**	**(1)**	(16)	(2)
Interest expense	**(60)**	**(1)**	(58)	(1)
Plan participants' contributions	**(3)**	**–**	(3)	–
Actuarial (loss)/gain (recognised in SORIE)	**(5)**	**1**	(154)	(1)
Benefits paid	**43**	**1**	36	1
Exchange differences	**–**	**1**	–	–
Balance at 31 December	**(1,327)**	**(19)**	(1,284)	(20)
Change in fair value of plan assets				
Balance at 1 January	**706**	**16**	589	14
Expected return on plan assets	**46**	**1**	43	1
Actuarial gain (recognised in SORIE)	**10**	**–**	76	–
Employer contributions	**39**	**2**	31	2
Plan participants' contributions	**3**	**–**	3	–
Benefits paid	**(43)**	**(1)**	(36)	(1)
Exchange differences	**–**	**(1)**	–	–
Balance at 31 December	**761**	**17**	706	16
Gross pension obligations included in provisions	**(566)**	**(2)**	(578)	(4)
Annuity obligations insured by Society	**392**	**–**	367	–
Gross defined benefit pension deficit	**(174)**	**(2)**	(211)	(4)
Deferred tax on defined benefit pension deficit	**52**	**1**	63	1
Net defined benefit pension deficit	**(122)**	**(1)**	(148)	(3)

The total amount of actuarial gains/(losses) net of tax recognised in the SORIE for the year was £3m; cumulative £(95)m (2005: £(55)m; cumulative £(98)m). Actuarial gains/(losses) net of tax relating to with-profits policyholders of £1m (2005: £(22)m) have been allocated to the unallocated divisible surplus.

The historic funding and experience adjustments are as follows:

	2006 £m	2005 £m	2004 £m	2003 £m
Present value of defined benefit obligations	**(1,346)**	(1,304)	(1,106)	(951)
Fair value of plan assets	**778**	722	603	540
Gross pension obligations	**(568)**	(582)	(503)	(411)
Experience adjustments on plan liabilities	**(13)**	(9)	(9)	(9)
Experience adjustments on plan assets	**10**	76	36	59

The fair value of the plan assets and expected return at the end of the year is made up as follows:

As at 31 December 2006	UK £m	Expected return %	Overseas £m	Expected return %
Equities	**460**	**7.6**	**5**	**8.8**
Bonds	**244**	**5.1**	**10**	**4.5**
Properties	**57**	**6.6**	**–**	**–**
Other investments	**–**	**–**	**2**	**3.5**
	761		**17**	

As at 31 December 2005	UK £m	Expected return %	Overseas £m	Expected return %
Equities	428	7.5	6	8.8
Bonds	220	4.7	7	3.8
Properties	58	7.0	–	–
Other investments	–	–	3	5.4
	706		16	

The expected rate of return for bonds is based on the current yield on a medium to long term AA bond index. The expected rates of return on equities and properties are based on margins over bond yields reflecting risk premiums. The return on plan assets in 2006 was £57m (2005: £120m).

40. PROVISIONS continued

The following amounts have been charged/(credited) to the income statement:

	2006 £m	2005 £m
Current service costs	**19**	18
Interest expense	**61**	59
Expected return on plan assets	**(47)**	(44)
Total included in other expenses	**33**	33

41. DEFERRED INCOME LIABILITIES

	2006 £m	2005 £m
Due within 12 months	**64**	46
Due after 12 months	**358**	305
Deferred income liabilities	**422**	351

42. DEFERRED TAX LIABILITIES

The movement in deferred tax liabilities during the year is as follows:

	As at 31 December 2005 £m	Charged/ (credited) to the income statement £m	Charged/ (credited) to equity £m	Movements from disposal of business £m	As at 31 December 2006 £m
Unrealised gains and losses on investments and debt liabilities	**570**	**131**	**2**	**–**	**703**
Excess of depreciation over capital allowances	**(30)**	**(3)**	**–**	**–**	**(33)**
Temporary differences between the accounts and tax deduction for expenses	**7**	**(34)**	**(19)**	**–**	**(46)**
Temporary differences between the accounts and tax deduction for actuarial reserves	**49**	**94**	**(7)**	**–**	**136**
Tax (losses)/gains carried forward	**(37)**	**(200)**	**5**	**–**	**(232)**
Temporary differences in relation to the pension fund deficit	**(64)**	**9**	**2**	**–**	**(53)**
Other temporary differences	**(3)**	**–**	**–**	**–**	**(3)**
Deferred tax liabilities	**492**	**(3)**	**(17)**	**–**	**472**

	As at 31 December 2004 £m	Charged/ (credited) to the income statement £m	Charged/ (credited) to equity £m	Movements from disposal of business £m	As at 31 December 2005 £m
Unrealised gains and losses on investments and debt liabilities	392	189	(6)	(5)	570
Excess of depreciation over capital allowances	(34)	4	–	–	(30)
Temporary differences between the accounts and tax deduction for expenses	(21)	15	13	–	7
Temporary differences between the accounts and tax deduction for actuarial reserves	19	28	2	–	49
Tax losses carried forward	(11)	(24)	(2)	–	(37)
Temporary differences in relation to the pension fund deficit	(47)	7	(24)	–	(64)
Other temporary differences	(3)	–	–	–	(3)
Deferred tax liabilities	295	219	(17)	(5)	492

42. DEFERRED TAX LIABILITIES continued

No deferred tax is recognised on the unremitted earnings of overseas subsidiaries, as the Group is able to control the remittance of earnings to the UK and there is no intention to remit any such earnings to the UK in the foreseeable future if the remittance would trigger any incremental UK tax liability. The maximum estimated temporary differences unprovided for are set out below, grouped by country. The calculation of the maximum temporary difference takes no account of any foreign tax suffered on the earnings in the jurisdiction of the foreign entity which might be available by way of double tax relief to reduce any UK tax liability arising on remittance.

	2006 £m	2005 £m
USA	**346**	351
France	**48**	33
	394	384

Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

The Group has unrelieved trading losses carried forward of £12m (2005: £3m) in its overseas operations. No deferred tax asset has been recognised in respect of these losses as at 31 December 2006 (or 31 December 2005), as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these losses will only be obtained if there are suitable profits arising in future periods. The potential deferred tax asset unrecognised as at 31 December 2006 is £3m (2005: £1m).

The Group has unrelieved post-cessation trading losses carried forward of £17m (2005: £18m). No deferred tax asset has been recognised in respect of these losses as at 31 December 2006 (or 31 December 2005), as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these losses will only be obtained if there are suitable post-cessation trading profits arising in future periods. The potential deferred tax asset unrecognised as at 31 December 2006 is £5m (2005: £5m).

The Group has surplus non-trading loan relationship deficits and management expenses carried forward of £17m (2005: £17m). No deferred tax asset has been recognised in respect of these deficits and expenses as at 31 December 2006 (or 31 December 2005), as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these deficits and expenses will only be obtained if there are suitable profits arising in future periods. The potential deferred tax asset unrecognised as at 31 December 2006 is £5m (2005: £5m).

The Group has net realised and unrealised capital losses carried forward of £2m (2005: £nil). No deferred tax asset has been recognised in respect of these losses as at 31 December 2006 as it is probable that there will be no suitable profits emerging in future periods against which to relieve them. Relief for these losses will only be obtained if there are suitable profits arising in future periods. The potential deferred tax asset unrecognised as at 31 December 2006 is £1m (2005: £nil).

43. OTHER LIABILITIES

	2006 £m	2005 £m
Accruals	**256**	111
Derivative liabilities	**177**	118
Reinsurers' share of deferred acquisition costs	**69**	78
Other	**1,161**	996
Other liabilities	**1,663**	1,303
Settled within 12 months	**1,405**	1,138
Settled after 12 months	**258**	165

The accruals balance includes a provision of £112m (2005: £nil) for future commission payments that have contingent settlement provisions. This liability has been determined using the net present value of the future commission that will be payable on fund values relevant to the provision. This valuation technique uses assumptions that are consistent with the Group's effective rate of interest, investment return assumptions and persistency assumptions as used in other valuations, but are not determined by reference to published price quotations.

The undiscounted value that is expected to be paid at maturity in respect of such commission is £164m.

Since this liability is being initially recognised and the cost deferred as an origination cost, no change in fair value has been recognised in the income statement for the year ended 31 December 2006. This amount is sensitive to persistency and market value assumptions.

44. RELATED PARTY TRANSACTIONS

There were no material transactions between directors or key managers and the Legal & General Group of companies. All transactions between the Group, its directors and key managers are on commercial terms which are no more favourable than those available to employees in general. Contributions to the post-employment benefit plans are outlined in Note 40. The UK defined benefit pension schemes have purchased annuity contracts issued by Society for consideration of £57m (2005: £37m) during the year, priced on an arm's length basis.

At 31 December 2006 and 31 December 2005 there were no loans outstanding to officers of the Company.

Key management personnel compensation

The aggregate compensation for key management personnel, including executive and non-executive directors, is as follows:

	2006 £m	2005 £m
Salaries	**17**	14
Social security costs	**3**	2
Post-employment benefits	**7**	4
Share-based incentive awards	**6**	4
Key management personnel compensation	**33**	24
Number of key management personnel	**73**	57

The Group's investment portfolio includes investments in venture capital, property and financial investments which are held via collective investment vehicles. Net investments into associate investment vehicles totalled £1,542m during the year (2005: £375m). The Group has outstanding loans to these associates of £6m (2005: £12m) and received investment management fees of £31m during the year (2005: £25m). Distributions from these investment vehicles to the Group totalled £109m (2005: £88m).

45. CONTINGENT LIABILITIES, GUARANTEES AND INDEMNITIES

Provision for the liabilities arising under contracts with policyholders is based on certain assumptions. The variance of actual experience from that assumed may result in such liabilities differing from the provisions made for them. Liabilities may also arise in respect of claims relating to the interpretation of such contracts, or the circumstances in which policyholders have entered into them (together in this paragraph 'liabilities'). The extent of such liabilities is influenced by a number of factors including the actions and requirements of the FSA, by ombudsman rulings, by industry compensation schemes and by court judgements. The continuing general profile and emphasis being given by the FSA and other bodies to the suitability of the past sales of endowment policies in the context of some mortgage transactions has led to the continuing receipt of claims from holders of endowment policies.

Various Group companies receive claims and become involved in actual or threatened litigation and regulatory issues from time to time. Provision for liabilities continues to be made and is regularly reviewed. However, it is not possible to predict, with certainty, the extent and the timing of the financial impact to which these claims, litigation or issues may give rise. The relevant members of the Group nevertheless consider that each makes prudent provision, as and when circumstances calling for such provision become clear, and that each has adequate capital and reserves to meet all reasonably foreseeable eventualities.

In 1975, the Society was required by the Institute of London Underwriters (ILU) to execute the ILU form of guarantee in respect of policies issued through the ILU's Policy Signing Office on behalf of NRG Victory Reinsurance Company Ltd (Victory), a company which was then a subsidiary of the Society. In 1990, Nederlandse Reassurantie Groep Holding NV (the assets and liabilities of which have since been assumed by Nederlandse Reassurantie Groep NV under a statutory merger in the Netherlands) acquired Victory and provided an indemnity to the Society against any liability the Society may have as a result of the ILU's requirement, and the ILU agreed that its requirement of the Society would not apply to policies written or renewed after the acquisition. Whether the Society has any liability as a result of the ILU's requirement and, if so, the amount of its potential liability is uncertain. The Society has made no payment or provision in respect of this matter.

Group companies have given indemnities and guarantees, including interest rate guarantees, as a normal part of their operating activities or in relation to capital market transactions.

46. COMMITMENTS

(i) Capital commitments

	2006 £m	2005 £m
Authorised and contracted commitments not provided for in respect of investment property development, payable after 31 December		
– Long term business	**49**	44

(ii) Operating lease commitments

	2006 £m	2005 £m
The future aggregate minimum lease payments under non-cancellable operating leases are as follows:		
– Not later than 1 year	**23**	18
– Later than 1 year and not later than 5 years	**93**	52
– Later than 5 years	**232**	86
	348	156
Future aggregate minimum sublease payments expected to be received under operating subleases	**9**	12
The future aggregate minimum lease receivables under non-cancellable operating leases are as follows:		
– Not later than 1 year	**2**	3
– Later than 1 year and not later than 5 years	**4**	7
– Later than 5 years	**3**	3
	9	13

The Group leases offices and other premises under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights.

47. SUBSIDIARIES

(i) Operating subsidiaries

The principal operating subsidiaries consolidated in these financial statements are listed below. The Company holds, directly or indirectly, all of the ordinary share capital and voting rights of these companies.

Company name	Nature of business	Country of incorporation
Legal & General Finance Plc[1]	Treasury operations	England and Wales
Legal & General Resources Limited[1]	Provision of services	England and Wales
Legal & General Assurance Society Limited	Long term and general insurance	England and Wales
Legal & General Insurance Limited	General insurance	England and Wales
Legal & General Investment Management Limited	Institutional fund management	England and Wales
Legal & General Assurance (Pensions Management) Limited	Long term business	England and Wales
Legal & General Pensions Limited	Reinsurance	England and Wales
Legal & General Partnership Services Limited	Provision of services	England and Wales
Legal & General (Portfolio Management Services) Limited	Institutional fund management	England and Wales
Legal & General Property Limited	Property management	England and Wales
Legal & General (Unit Trust Managers) Limited	Unit trust management	England and Wales
Legal & General Ventures Limited	Venture capital management	England and Wales
Legal & General (France) SA	Long term business	France
Legal & General Bank (France) SA	Financial services	France
Legal & General Nederland Levensverzekering Maatschappij NV	Long term business	Netherlands
Banner Life Insurance Company Inc	Long term business	USA
William Penn Life Insurance Company of New York Inc	Long term business	USA
First British American Reinsurance Company	Reinsurance	USA
First British American Reinsurance Company II	Reinsurance	USA

1. Directly held by Legal & General Group Plc. All other subsidiaries are held through intermediate holding companies.

The main territory of operation of subsidiaries incorporated in England and Wales is the UK. For overseas subsidiaries the principal country of operation is the same as the country of incorporation.

The complete list of subsidiary undertakings can be obtained from the registered office at Temple Court, 11 Queen Victoria Street, London EC4N 4TP.

47. SUBSIDIARIES continued

(ii) Investment vehicles

The following mutual funds and partnerships have been consolidated as a result of the Group's ownership of the majority of the benefits arising from the investment vehicle.

Vehicle name	Vehicle type	Territory	% of equity held by the Group
Arlington Business Parks Unit Trust	Property unit trust	Jersey	53.8
Chineham Shopping Centre Limited Partnership	Property unit trust	Jersey	100.0
Ealing Shopping Centre Limited Partnership	Property unit trust	Jersey	100.0
Gresham Street Limited Partnership	Property unit trust	Jersey	100.0
Harrow Shopping Centre Limited Partnership	Property unit trust	Jersey	100.0
Legal & General City Offices Limited Partnership	Property unit trust	Jersey	100.0
Legal & General West End Offices Limited Partnership	Property unit trust	Jersey	100.0
Northampton Shopping Centre Limited Partnership	Property unit trust	Jersey	100.0
The Leisure Fund Limited Partnership	Property partnership	England and Wales	49.5
Legal & General Equity Trust	Equity unit trust	UK	81.0
Legal & General European Trust	Equity unit trust	UK	82.0
Legal & General Far Eastern Trust	Equity unit trust	UK	86.0
Legal & General Global Growth Trust	Equity unit trust	UK	64.0
Legal & General Growth Trust	Equity unit trust	UK	73.0
Legal & General High Income Trust	Fixed interest unit trust	UK	63.0
Legal & General Japanese Trust	Equity unit trust	UK	76.0
Legal & General North American Trust	Equity unit trust	UK	80.0
Legal & General Pacific Growth Trust	Equity unit trust	UK	93.0
Legal & General UK Smaller Companies Trust	Equity unit trust	UK	72.0

48. ASSOCIATES AND JOINT VENTURES

The Group has the following significant holdings which have been included as financial investments or investments in associates. The gross assets of these companies are in part funded by borrowings which are non recourse to the Group.

Company name	Country of incorporation	Accounting treatment	% of equity shares held by the Group
Cofunds (Holdings) Limited	England and Wales	Equity method	25.4
Bracknell Property Unit Trust	Jersey	FVTPL	50.5
English Cities Fund	England and Wales	FVTPL	37.5
The IPIF Feeder Unit Trust	Jersey	FVTPL	27.4
Legal & General UK Property Trust	England and Wales	FVTPL	59.3
Meteor Industrial Partnership	England and Wales	FVTPL	49.9
Performance Shopping Centre Limited Partnership	England and Wales	FVTPL	50.0
UK Logistics Fund Unit Trust	Jersey	FVTPL	43.2
Warrington Retail Unit Trust	Jersey	FVTPL	25.0
LGV 1 Private Equity Fund Limited Partnership	England and Wales	FVTPL	46.3
LGV 2 Private Equity Fund Limited Partnership	England and Wales	FVTPL	37.1
LGV 3 Private Equity Fund Limited Partnership	England and Wales	FVTPL	46.6
LGV 4 Private Equity Fund Limited Partnership	England and Wales	FVTPL	36.7
LGV 5 Private Equity Fund Limited Partnership	England and Wales	FVTPL	45.0
Mithras Investment Trust Plc	England and Wales	FVTPL	34.7
Legal & General Ethical Trust	England and Wales	FVTPL	36.0
Legal & General European Index Trust Plc	England and Wales	FVTPL	34.0
Legal & General Japanese Index Trust	England and Wales	FVTPL	37.0
Legal & General US Index Trust	England and Wales	FVTPL	37.0
Legal & General Distribution Trust	England and Wales	FVTPL	34.0
Legal & General Pacific Index Trust	England and Wales	FVTPL	39.0
Legal & General Fixed Interest Trust	England and Wales	FVTPL	20.0

48. ASSOCIATES AND JOINT VENTURES continued

Summarised financial information for associates which are classified as FVTPL is shown below:

	Venture capital £m	Property partnerships £m	Unit trusts £m	Total £m
Aggregate revenues	174	139	257	570
Aggregate profit	171	51	94	316
Gross assets	386	2,358	4,891	7,635
Gross liabilities	7	554	54	615

49. GOODWILL RESULTING FROM ACQUISITIONS

The cumulative goodwill charged to reserves prior to 1998, arising from acquisition of subsidiaries which are still part of the Group, amounted to £70m (2005: £70m).

50. MANAGEMENT OF CAPITAL RESOURCES

Capital fund structure

The Group's total capital resources of £8.4bn (2005: £7.0bn) on an IFRS basis comprise ordinary equity holders capital, £5.4bn (2005: £4.3bn), subordinated debt, £0.8bn (2005: £0.4bn), subordinated debt designated as equity, £nil (2005: £0.4m) and unallocated divisible surplus, £2.2bn (2005: £1.9bn).

The Group writes a range of long term insurance and investment business in the Long Term Fund (LTF) of its main operating insurance subsidiary, Legal & General Assurance Society Limited (Society). This fund is segregated from the Group's other assets. The fund includes participating (with-profits) business where policyholders and shareholders share in the risks and rewards, and non-participating (non profit) business, where the shareholders receive the profits. Capital in excess of an amount required to cover the liabilities within the non profit part of the Society LTF is known as the Shareholder Retained Capital (SRC). Retention of the SRC within the LTF provides support for new and existing non profit business.

On 31 December 2006, the non-linked non profit pensions and annuity business of Society was ceded to a new, wholly owned, reinsurance company, Legal & General Pensions Limited (LGP). The reinsurance was effected on arm's length terms. The reinsurance assets are held in a LTF and are separate from other assets within the Group.

Transfers from the Society LTF to shareholders is limited by a formula agreed with the FSA. In practice, the maximum transfer is the aggregate of the shareholders' share of the with-profits surplus, a smooth investment return of 7% on the embedded value of the SRC and Sub-fund and 5% on the embedded value of the non profit business of Society and LGP, adjusted to remove the impact of the contingent loan between SRC and LGP, and the shareholder net worth of LGP.

Managed pension fund business is written through Legal & General Assurance (Pensions Management) Limited (PMC), which is a life company writing predominantly non-participating group pension business effected by trustees of occupational schemes in the UK (or their equivalent overseas). The assets are held in a LTF and are separate from other assets within the Group.

In addition, General insurance business is written in the UK by Legal & General Insurance Limited, and long term insurance business is written by subsidiaries in America, the Netherlands and in France.

Capital management policies and objectives

The Group aims to manage its capital resources to maintain financial strength, policyholder security and relative external financial strength ratings advantage. The Group also seeks to maximise its financial flexibility by maintaining strong liquidity and by utilising a range of alternative sources of capital including equity, senior debt, subordinated debt and reinsurance.

Capital measures

The Group measures its capital on a number of different bases, including those which comply with the regulatory framework within which the Group operates and those which the directors consider most appropriate for managing the business. The measures used by the Group include:

- *Accounting bases*
  The directors believe that the supplementary accounts prepared using European Embedded Value (EEV) principles provide the most accurate and meaningful reflection of the Group's long term operations and the value of the business to shareholders. Accordingly the Group's net asset value and total capital employed are analysed and measured on this basis.
  In addition, management have regard to the primary financial statements prepared under IFRS in order to manage capital and cash flow usage and to determine dividend paying capacity.
- *Regulatory basis*
  The financial strength of the Group's insurance subsidiaries is measured under local regulatory requirements (see page 102). One of these regulatory measures, Individual Capital Assessment (ICA), measures capital using risk based techniques, and provides a measure of economic capital.

Basis of regulatory capital and corresponding regulatory capital requirements

In each country in which the Group operates, the local insurance regulator specifies rules and guidance for the minimum amount and type of capital which must be held by long term insurance subsidiaries in excess of their insurance liabilities. The minimum required capital must be maintained at all times throughout the year. This helps to ensure that payments to policyholders can be made as they fall due. The Group has not breached any regulatory capital requirements at any time during the year.

The required capital is calculated by either assessing the additional assets which would be required to meet the insurance company's liabilities in specified, stressed financial conditions, or by applying fixed percentages to the insurance company's liabilities and risk exposures. The requirements in the different jurisdictions in which the Group operates are detailed overleaf:

50. MANAGEMENT OF CAPITAL RESOURCES continued

UK regulatory basis

Required capital for the life business is based on the rules of the FSA. Society must hold assets in excess of the higher of two amounts, the first being calculated using the FSA rules (pillar 1), the second being an economic capital assessment by the Company which is reviewed by the FSA (pillar 2, otherwise known as ICA).

The public pillar 1 capital calculation is the total of two amounts. The first amount is based on the most onerous of a number of stress tests which are applied to both assets and insurance liabilities. The second amount is calculated by applying fixed percentages to liabilities and sums assured at risk. There are further stress tests for participating liabilities as measured in the Realistic Balance Sheet, which may increase the required capital.

The private pillar 2 capital calculation is an assessment of the economic capital required to ensure that the Company can meet its liabilities, with a high likelihood, as they fall due. This is achieved by stochastic modelling and scenario testing. The result is reviewed and may be modified by the FSA.

Regulatory capital for the General insurance business is also calculated using FSA pillar 1 and pillar 2 requirements. The pillar 1 calculation applies fixed percentages to premiums and claims. Pillar 2 creates a higher capital requirement and is therefore applied.

US regulatory basis

Required capital is determined to be the Company Action Level Risk Based Capital (RBC) based on the National Association of Insurance Commissioners RBC model. RBC is a method of measuring the minimum amount of capital appropriate for an insurance company to support its overall business operations taking into account its size and risk profile. The calculation is based on applying factors to various asset, premium, claim, expense and reserve items, with the factors determined as higher for those items with greater underlying risk and lower for less risky items.

French and Dutch regulatory bases

The minimum required capital is defined by the French Ministry of Finance's 'Code des Assurances' and the 'De Nederlandsche Bank N.V.' (Dutch Supervisory Body) respectively. The basis of the calculation is a percentage of the liabilities plus a percentage of the sum assured at risk and, for some contracts, the premium. The percentages depend on the guarantees given and the amount of reinsurance cover.

Group regulatory basis

In addition to the regulatory capital calculations for the individual firms, the Group is required to comply with the requirements of the Insurance Groups Directive (IGD). This is a very prudent measure of capital resources, as it excludes any amount of surplus capital within a LTF.

Available regulatory capital resources

Capital resources available to meet the UK capital requirements are determined using FSA valuation rules. The asset valuation rules are based on UK GAAP, adjusted for both admissibility limits and specific valuation differences. The Group's regulatory capital position statement in Table 1 sets out the different sources of capital held within the Group. The Group's total available capital resources, based on the unaudited[1] FSA returns, are £6,897m (2005: £6,172m) of which £5,835m (2005: £4,607m) is held by the life businesses. The use of capital held by the UK and overseas life businesses is generally constrained by local regulatory requirements, and may not be available to provide funding for other businesses.

The total available capital resources of the Group's with-profits business of £1,128m (2005: £842m) is determined in accordance with the realistic balance sheet rules prescribed by the FSA. The capital resources reflect the surplus in that part of the fund which is in excess of any constructive obligation to policyholders. The liabilities within the consolidated balance sheet do not include the amount representing the shareholders' share of future bonuses. However, for capital reporting, the shareholders' share is deducted from capital resources in the capital statement.

At 31 December 2006, the realistic value of the UK participating liabilities was £19,756m (2005: £20,338m) under the FSA realistic capital regime. The excess of realistic assets over realistic liabilities was £1,128m (2005: £842m).

1. The FSA returns are audited and filed subsequent to the publication of the Group's capital position.

50. MANAGEMENT OF CAPITAL RESOURCES continued

Table 1 – Regulatory capital position statement

	UK with-profits 2006 £m	UK non profit, SRC and Sub-fund 2006 £m	LGP 2006 £m	Overseas and PMC 2006 £m	Total life 2006 £m	Shareholders' equity and other activities 2006 £m	Total 2006 £m
Ordinary shareholders' equity outside the LTF[1]	–	–	550	906	1,456	706	2,162
Ordinary shareholders' equity in the LTF	–	3,263	–	–	3,263	–	3,263
Capital and reserves attributable to ordinary equity holders of the Company	–	3,263	550	906	4,719	706	5,425
Adjustments onto regulatory basis[2]:							
Unallocated divisible surplus	1,862	302	–	14	2,178	–	2,178
Other[3]	(734)	(242)	(70)	(428)	(1,474)	(29)	(1,503)
Other qualifying capital:							
Subordinated borrowings[4]	–	–	–	–	–	797	797
Internal loans[5]	–	(571)	971	12	412	(412)	–
Implicit item[6]	–	–	–	–	–	–	–
Total available capital resources	1,128	2,752	1,451	504	5,835	1,062	6,897
IFRS liability analysis:							
UK participating liabilities on realistic basis							
– Options and guarantees	520	–	–	–	520	–	520
– Other policyholder obligations	18,117	37	–	–	18,154	–	18,154
Overseas participating liabilities	–	–	–	1,487	1,487	–	1,487
Unallocated divisible surplus	1,862	302	–	14	2,178	–	2,178
Value of in-force non-participating contracts	(391)	–	–	–	(391)	–	(391)
Participating contract liabilities	20,108	339	–	1,501	21,948	–	21,948
Unit linked non-participating life assurance liabilities	678	4,307	–	971	5,956	–	5,956
Non-linked non-participating life assurance liabilities	1,996	11,847	–	1,522	15,365	–	15,365
Unit linked non-participating investment contract liabilities	7,468	11,069	–	143,479	162,016	–	162,016
General insurance liabilities	–	–	–	–	–	281	281
Non-participating contract liabilities	10,142	27,223	–	145,972	183,337	281	183,618

50. MANAGEMENT OF CAPITAL RESOURCES continued

Table 1 – Regulatory capital position statement continued

	UK with-profits 2005 £m	UK non profit, SRC and Sub-fund 2005 £m	LGP 2005 £m	Overseas and PMC 2005 £m	Total life 2005 £m	Shareholders' equity and other activities 2005 £m	Total 2005 £m
Ordinary shareholders' equity outside the LTF[1]	–	–	–	901	901	1,398	2,299
Ordinary shareholders' equity in the LTF	–	1,958	–	–	1,958	–	1,958
Capital and reserves attributable to ordinary equity holders of the Company	–	1,958	–	901	2,859	1,398	4,257
Adjustments onto regulatory basis[2]:							
Unallocated divisible surplus	1,527	280	–	87	1,894	–	1,894
Other[3]	(685)	(207)	–	(409)	(1,301)	(27)	(1,328)
Other qualifying capital:							
Subordinated borrowings[4]	–	–	–	–	–	809	809
Internal loans[5]	–	602	–	13	615	(615)	–
Implicit item[6]	–	540	–	–	540	–	540
Total available capital resources	842	3,173	–	592	4,607	1,565	6,172
IFRS liability analysis:							
UK participating liabilities on realistic basis							
– Options and guarantees	686	–	–	–	686	–	686
– Other policyholder obligations	18,653	–	–	–	18,653	–	18,653
Overseas participating liabilities	–	–	–	1,317	1,317	–	1,317
Unallocated divisible surplus	1,527	280	–	87	1,894	–	1,894
Value of in-force non-participating contracts	(379)	–	–	–	(379)	–	(379)
Participating contract liabilities	20,487	280	–	1,404	22,171	–	22,171
Unit linked non-participating life assurance liabilities	661	4,136	–	820	5,617	–	5,617
Non-linked non-participating life assurance liabilities	2,073	13,559	–	1,611	17,243	–	17,243
Unit linked non-participating investment contract liabilities	6,514	7,110	–	122,180	135,804	–	135,804
General insurance liabilities	–	–	–	–	–	292	292
Non-participating contract liabilities	9,248	24,805	–	124,611	158,664	292	158,956

1. Society shareholder capital of £1,307m (2005: £1,896m) is included within Shareholders' equity and other activities.
2. Figures extracted from draft regulatory returns.
3. Shareholders' share in realistic liabilities of £749m (2005: £690m) and changes to the value of assets and liabilities on a regulated basis of £754m (2005: £638m) are included within Other.
4. Group has issued €600m of subordinated lower tier II borrowings and £400m of subordinated upper tier II borrowings both of which are treated as capital on a regulatory basis.
5. In 2006, LGP issued £200m of subordinated upper tier II borrowings and £200m of subordinated lower tier II borrowings to Society. In addition, £571m has been injected from Society's LTF into LGP's LTF by means of a contingent loan to cover the initial regulatory loss in LGP. These loans qualify as capital for regulatory purposes in LGP. Legal & General Overseas Holdings Limited has subscribed for a total of €18m (2005: €18m) of perpetual subordinated loan stock issued by Legal & General Holdings (France) SA. This loan qualifies as hybrid capital for Legal & General Holdings (France) SA.
6. The implicit item recognises profits in relation to in-force business written in the non profit part of Society's LTF which are expected on a prudent assessment to emerge over the next five years. The maximum amount permitted is determined by the FSA. In 2005, there was an implicit item of £540m. There is no implicit item in 2006.

50. MANAGEMENT OF CAPITAL RESOURCES continued

Available regulatory capital resource risks

The Group's available capital resources are sensitive to changes in market conditions, due to both changes in the value of the assets and to the effect that changes in investment conditions may have on the value of the liabilities. Capital resources are also sensitive to assumptions and experience relating to mortality and morbidity and, to a lesser extent, expenses and persistency.

The most significant sensitivities arise from the following four risks:

- market risk in relation to UK participating business which would crystallise if adverse changes in the value of the assets supporting this business could not be fully reflected in payments to policyholders because of the effect of guarantees and options. The capital position of this business would also deteriorate if increases to the market cost of derivatives resulted in an increase in the liability for guarantees and options in the realistic balance sheet.
- market risk in relation to the UK annuity business, which would crystallise if the return from the fixed interest investments supporting this business were lower than that assumed for reserving.
- mortality risk in relation to the UK annuity business, which would crystallise if the mortality of annuitants improved more rapidly than the assumptions used for reserving.
- mortality risk in relation to the UK and US term assurance businesses, which would crystallise if mortality of the lives insured was higher than that assumed, possibly because of an epidemic.

A range of management actions are available to mitigate any adverse impact from changing market conditions and experience. Examples of possible management actions available to mitigate such an effect include changes to with-profits bonus rates, changes to discretionary surrender terms and the potential for charging for guarantees. To the extent that management actions are expected only to partially offset adverse experience, then liabilities would be increased to anticipate the future impact of the worse experience and total capital resources would be reduced.

Movements in life business regulatory capital resources

The movement in the life business regulatory capital resources is shown in Table 2.

Table 2 – Movements in life business capital resources

	UK with-profits 2006 £m	**UK non profit, SRC and Sub-fund 2006 £m**	**LGP 2006 £m**	**Overseas and PMC 2006 £m**	**Total life 2006 £m**
Balance at 1 January	**842**	**3,173**	**–**	**592**	**4,607**
Effect of investment variations	**127**	**862**	**–**	**(42)**	**947**
Effect of changes in non-economic assumptions	**72**	**(75)**	**–**	**–**	**(3)**
Changes in management policy	**(4)**	**(1,297)**	**–**	**–**	**(1,301)**
Changes in regulatory requirements	**2**	**363**	**–**	**3**	**368**
New business	**16**	**(236)**	**–**	**(89)**	**(309)**
Cash distributions	**–**	**(272)**	**–**	**(68)**	**(340)**
Other factors	**73**	**234**	**1,451**	**108**	**1,866**
Balance at 31 December	**1,128**	**2,752**	**1,451**	**504**	**5,835**

Other factors within LGP represent the available capital resources of that Company on a regulatory basis.

	UK with-profits 2005 £m	UK non profit, SRC and Sub-fund 2005 £m	LGP 2005 £m	Overseas and PMC 2005 £m	Total life 2005 £m
Balance at 1 January	864	2,895	–	557	4,316
Effect of investment variations	294	684	–	42	1,020
Effect of changes in non-economic assumptions	(282)	(1)	–	–	(283)
Changes in management policy	72	175	–	–	247
Changes in regulatory requirements	(121)	(215)	–	(6)	(342)
New business	(11)	(459)	–	(103)	(573)
Cash distributions	–	(219)	–	(39)	(258)
Other factors	26	313	–	141	480
Balance at 31 December	842	3,173	–	592	4,607

51. RISK MANAGEMENT AND CONTROL

The pages which follow describe the Group's approach to risk management. The first section deals with the overall approach, applicable to all risks. It is followed by a detailed review of risks within the Group's key businesses.

Risk management objectives

The Group's primary objective in undertaking risk management activity is to minimise its exposure to unexpected financial loss and limit the potential for deviation from anticipated outcomes.

Risk management approach

A significant part of the Group's business involves the acceptance and management of risk. The Group is exposed to insurance, market, credit, liquidity and operational risks and operates a formal risk management framework to ensure that all significant risks are identified and managed. The risk factors mentioned below should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties.

Insurance risk: Insurance risk is the risk arising from higher claims being experienced than anticipated.

Market risk: Market risk is the risk arising from fluctuations in interest rates, exchange rates, share prices and other relevant market prices.

Credit risk: Credit risk is the risk of loss if another party fails to perform its financial obligations to the Group.

Liquidity risk: Liquidity risk is the risk that the Group, though solvent, does not have sufficient financial resources available to enable it to meet its obligations as they fall due, or can only secure them at excessive cost.

Operational risk: Operational risk is the risk arising from inadequate or failed internal processes, people and systems, or from external events.

Risk framework

Overall responsibility for the management of the Group's exposure to risk is vested in the Group Board. To support it in this role, a risk framework is in place comprising a structure of formal committees, risk assessment and reporting processes and risk review functions. The framework provides assurance that risks are being appropriately identified and managed and that an independent assessment of risks is being performed.

Oversight of the risk management framework is performed on behalf of the Group Board by its sub-committee, the Group Risk and Compliance Committee (GRCC). The GRCC is supported in this role by the following sub-committees:

Capital Committee: The Capital Committee assesses the capital requirements (including the risk based capital requirements) of the Group; monitors the sources of capital available to meet these requirements; oversees the allocation of capital to firms; and monitors at a Group level a number of performance and capital measures.

Counterparty Credit Committee: The Committee has oversight of counterparty credit risk across the Group, sets the limits for the Group's exposure to any single counterparty failure and manages exposures within these limits.

UK Asset and Liability Committee: The Committee has oversight of the management of market and liquidity risks arising within Legal & General Assurance Society Limited (Society), and its subsidiaries Legal & General Pensions Limited (LGP) and Legal & General Insurance Limited (LGI).

UK Pricing and Insurance Risk Committee: The Committee has oversight of the management of insurance risk arising within Society, LGP and LGI. Oversight of the management of insurance risks arising within the Group's overseas subsidiaries is performed by the boards of the local holding companies, which report directly to the GRCC.

Group Operational Risk Assessment Committee: The Committee has oversight of specific aspects of the Group's operational risk, particularly issues which are common across the Group, and seeks to ensure consistency in approaches to operational risk management.

In addition, Risk and Compliance Committees (RCCs) are in place for each of the Group's main operational businesses. These committees are predominantly responsible for reviewing the management of operational risks and compliance with regulation.

The local holding companies of the overseas subsidiaries have established RCCs to cover their trading subsidiaries. The Boards of overseas firms are responsible for ensuring appropriate processes are in place for the management of risk exposures. The GRCC receives reports from the RCCs of each overseas firm to confirm that risks remain acceptable.

Methods used to monitor and assess risk exposures

A continuous Groupwide process is in place formally identifying, evaluating and managing significant risks to the achievement of the Group's objectives. A standard approach is used to assess risks. Senior management and the risk review functions review the output of the assessments. A Groupwide risk assessment process is used to provide determination of key risks within the Group reported to the GRCC.

Group and firm level risk review functions provide oversight of the risk management processes within the Group. A central risk function is responsible for setting the risk management framework and standards. Risk review functions in each of the business operating units manage the framework in line with these standards. Their responsibilities include the evaluation of changes in the business operating environment and business processes, the assessment of these changes on risks to the business and the monitoring of the mitigating actions. The risk review functions also ensure that RCCs are provided with meaningful risk reports and that there is appropriate information to assess risk issues.

Management of risks

The Group seeks to manage its exposures to risk through control techniques so as to ensure that the residual risk exposures are within acceptable tolerances agreed by the Board. The key control techniques for the major categories of risk exposure are summarised in the following sections.

Insurance risk

Insurance risk is implicit in the Group's insurance business and arises as a consequence of the type and volume of new business written and the concentration of risk in particular policies or groups of policies subject to the same risks. A detailed review of the Group's inherent residual risks associated with insurance products is included in pages 112 to 116. Insurance risk is managed using the following techniques:

Policies and delegated authorities for underwriting, pricing and reinsurance

Pricing is based on assumptions, such as mortality and persistency, which have regard to past experience and to trends. Insurance exposures are limited through reinsurance. Overall, the Group seeks to be conservative in its acceptance of insurance risks by establishing strict underwriting criteria and limits. The underwriting policy is clearly documented, setting out risks which are unacceptable and the terms applicable for non-standard risks.

Reinsurance is used to reduce potential loss to the Group from individual large risks and catastrophic events. It may also be used to manage capital or to provide access to specialist underwriting expertise. The Group makes extensive use of reinsurance for its UK individual protection business, placing a proportion of all risks meeting prescribed criteria. The Group has also entered into external reinsurance arrangements, the primary effect of which is to reduce the capital requirements associated with this business.

The principal General insurance reinsurances are excess of loss catastrophe treaties, under which the cost of claims from a weather event, in excess of an agreed retention level, is recovered from reinsurers.

51. RISK MANAGEMENT AND CONTROL continued

Reserving policy

All subsidiaries writing insurance business have a documented reserving policy setting out the basis on which liabilities are to be determined using statistical analysis and actuarial experience. Policies for each subsidiary are in line with locally established actuarial techniques, relevant regulation and legislation. Further details of the assumption setting process are included in Note 37.

Market Risk

The Group is exposed to market risk as a consequence of fluctuations in values or returns on assets and liabilities, which are influenced by one or more external factors, including changes in specified interest rates, financial instrument prices, foreign exchange rates, and indices of prices or rates.

Significant areas where the Group is exposed to these risks are:

- assets backing insurance and investment contracts other than linked contracts;
- assets and liabilities denominated in foreign currencies; and
- other financial assets and liabilities

The Group manages market risk using the following methods:

Asset liability matching

The Group manages its assets and liabilities in accordance with relevant regulatory requirements, reflecting the differing types of liabilities it has in each business.

For business such as immediate annuities, which are sensitive to interest rate risk, cash flow analysis is used to create a portfolio of fixed income securities, the value of which changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits from changing interest rates. Interest rate risk cannot be completely eliminated, due to the nature of the liabilities and early redemption options contained in the assets.

For businesses where a range of asset types, including equity and property, are held to meet liabilities, the Group uses stochastic models to assess the impact of a range of future return scenarios on investment values and associated liabilities. This allows the Group to devise an investment and with-profits policyholder bonus strategy which optimises returns to its policyholders over time, whilst limiting the capital requirements associated with these businesses. The Group uses this method extensively in connection with its UK with-profits business.

Derivatives

The Group uses derivatives to reduce market risk. The most widely used derivatives are exchange traded equity futures and swaps. The Group may use futures to facilitate efficient asset allocation. In addition, derivatives are used to improve asset liability matching and to manage interest rate, foreign exchange and inflation risks. It is the Group's policy that amounts at risk through derivative transactions are covered by cash or corresponding assets and that swaps are collateralised to reduce counterparty exposure.

Interest rate risk

Interest rate risk is the risk that the Group is exposed to lower returns or loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets arising from changes in underlying interest rates.

The Group 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 Group's obligations to policyholders.

To mitigate the risk that guarantees and commitments are not met, the Group purchases financial instruments, 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. Additionally, fluctuations in interest rates will vary the repayments on variable rate debt issued by the Group (Note 38).

51. RISK MANAGEMENT AND CONTROL continued

Table 3 summarises the exposure of the Group's assets to changes in interest rates. Financial assets which are not directly exposed to interest rate risk (such as linked assets, equities, other debtors) have not been included. Asset liability matching significantly reduces the Group's exposure to interest rate risk. The expected cash outflows on insurance contract liabilities are shown in Note 33.

Table 3 – Interest rate risk

	Within 1 year		1-5 years		5-15 years		15-25 years		Over 25 years		Total
As at 31 December 2006	**£m**	**%[1]**	**£m**	**%[1]**	**£m**	**%[1]**	**£m**	**%[1]**	**£m**	**%[1]**	**£m**
Fixed rate securities	**218**	**–**	**1,773**	**5.4**	**8,912**	**5.2**	**6,402**	**5.1**	**6,126**	**5.3**	**23,431**
Variable rate securities	**192**	**5.4**	**660**	**5.1**	**285**	**4.9**	**15**	**4.6**	**167**	**5.1**	**1,319**
Loans and receivables	**178**	**4.1**	**17**	**4.5**	**12**	**6.8**	**5**	**6.4**	**31**	**6.8**	**243**
Interest rate swaps	**–**	**–**	**–**	**6.9**	**(85)**	**5.5**	**–**	**1.7**	**3**	**3.1**	**(82)**
Cash and cash equivalents	**2,079**	**4.8**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**2,079**
Investments exposed to interest rate risk	**2,667**		**2,450**		**9,124**		**6,422**		**6,327**		**26,990**

	Within 1 year		1-5 years		5-15 years		15-25 years		Over 25 years		Total
As at 31 December 2005	£m	%[1]	£m	%[1]	£m	%[1]	£m	%[1]	£m	%[1]	£m
Fixed rate securities	388	3.9	1,264	4.8	7,429	4.8	8,675	4.6	5,690	5.0	23,446
Variable rate securities	198	4.8	790	4.5	222	4.8	38	5.3	102	4.9	1,350
Loans and receivables	144	4.5	15	4.5	5	6.2	12	5.9	39	5.9	215
Interest rate swaps	–	–	–	–	(88)	–	–	–	6	–	(82)
Cash and cash equivalents	1,838	4.4	–	–	–	–	–	–	–	–	1,838
Investments exposed to interest rate risk	2,568		2,069		7,568		8,725		5,837		26,767

1. Weighted average effective interest rate.

Both fixed rate financial assets and variable rate securities are categorised by maturity dates.

Currency risk

The Group manages its currency risk exposure in the following way:

- In respect of long term business assets and liabilities denominated in non-sterling currencies, the Group protects its exposure to exchange rate fluctuations by backing obligations with investments in the same currency.
- Balance sheet foreign exchange currency translation exposure in respect of the Group's international subsidiaries is actively managed in accordance with a policy, agreed by the Group Board, which allows between 25% and 75% of net foreign currency assets to be hedged through the use of derivatives.

51. RISK MANAGEMENT AND CONTROL continued

Table 4 summarises the Group's exposure to foreign currency exchange risk, in sterling. Non-linked assets and liabilities are reported in their underlying currency.

Table 4 – Currency risk

As at 31 December 2006	Sterling 2006 £m	Euro 2006 £m	US Dollar 2006 £m	Japanese Yen 2006 £m	Other 2006 £m	Linked 2006 £m	Total 2006 £m
Assets							
Investment in associates	**16**	**–**	**–**	**–**	**–**	**–**	**16**
Plant and equipment	**40**	**2**	**1**	**–**	**–**	**–**	**43**
Investments	**35,693**	**2,854**	**2,339**	**643**	**890**	**170,793**	**213,212**
Purchased interests in long term business	**7**	**–**	**16**	**–**	**–**	**–**	**23**
Other operational assets	**3,001**	**200**	**846**	**–**	**1**	**523**	**4,571**
Total assets	**38,757**	**3,056**	**3,202**	**643**	**891**	**171,316**	**217,865**
Liabilities							
Subordinated borrowings	**429**	**389**	**–**	**–**	**–**	**–**	**818**
Participating contract liabilities	**20,448**	**1,273**	**–**	**–**	**–**	**227**	**21,948**
Non-participating contract liabilities	**14,121**	**375**	**1,149**	**–**	**1**	**167,972**	**183,618**
Senior borrowings	**990**	**121**	**496**	**–**	**–**	**–**	**1,607**
Provisions	**566**	**2**	**–**	**–**	**–**	**–**	**568**
Deferred liabilities	**715**	**21**	**158**	**–**	**–**	**–**	**894**
Creditors	**644**	**168**	**466**	**–**	**1**	**490**	**1,769**
Net asset value attributable to unitholders	**–**	**–**	**–**	**–**	**–**	**804**	**804**
Total liabilities	**37,913**	**2,349**	**2,269**	**–**	**2**	**169,493**	**212,026**

As at 31 December 2005	Sterling 2005 £m	Euro 2005 £m	US Dollar 2005 £m	Japanese Yen 2005 £m	Other 2005 £m	Linked 2005 £m	Total 2005 £m
Assets							
Investment in associates	16	–	–	–	–	–	16
Plant and equipment	28	2	2	–	–	–	32
Investments	37,426	2,352	2,476	809	804	142,530	186,397
Purchased interests in long term business	10	–	15	–	–	–	25
Other operational assets	3,860	202	913	–	1	419	5,395
Total assets	41,340	2,556	3,406	809	805	142,949	191,865
Liabilities							
Subordinated borrowings	415	–	–	–	–	–	415
Participating contract liabilities	20,767	1,203	–	–	–	201	22,171
Non-participating contract liabilities	15,921	350	1,262	–	2	141,421	158,956
Senior borrowings	1,215	110	308	–	1	–	1,634
Provisions	578	3	1	–	–	–	582
Deferred liabilities	656	32	155	–	–	–	843
Creditors	867	128	121	–	3	381	1,500
Net asset value attributable to unitholders	–	–	–	–	–	828	828
Total liabilities	40,419	1,826	1,847	–	6	142,831	186,929

Other price risk

Other price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices other than those arising from interest rate risk or currency risk. These changes may be as a result of features of the individual instrument, its issuer or factors affecting all similar financial instruments traded in the market.

The Group controls its exposure to geographic price risks by using internal country credit ratings. These ratings are based on macroeconomic data and key qualitative indicators. The latter take into account economic, social and political environments. Table 5 indicates the Group's exposure to different equity markets around the world. Linked equity investments are excluded from the table as the risk is retained by the policyholder.

51. RISK MANAGEMENT AND CONTROL continued

Table 5 – Exposure to worldwide equity markets

	2006 £m	2005 £m
UK	**8,557**	8,567
North America	**441**	366
Europe	**1,027**	986
Japan	**619**	741
Asia Pacific	**695**	611
Other	**35**	39
Listed equities	**11,374**	11,310
Unlisted UK equities	**201**	203
Holdings in unit trusts	**1,267**	1,381
Total equities	**12,842**	12,894

The Group holds non-linked commercial property investments totalling £3,751m (2005: £3,653m), of which £3,729m (2005: £3,587m) are located in the UK.

Credit risk

Credit risk is the risk that the Group is exposed to loss if another party fails to perform its financial obligations to the Group. Significant areas where the Group is exposed to credit risk are:

- The Group holds corporate bonds to back part of its insurance liabilities. Significant exposures are managed by the application of concentration limits, with allowance being made in the actuarial valuation of the insurance liabilities for possible defaults.
- The Group limits its exposure to insurance risk by ceding part of the risks it assumes to the reinsurance market. To limit the risk of reinsurer default the Group operates a credit rating policy when arranging cover. When selecting new reinsurance partners the Group considers only companies which have a minimum credit rating equivalent to A from Standard & Poor's and imposes limits on the level of exposure to any individual reinsurer.

Aggregate counterparty exposures are regularly monitored both at an individual subsidiary level and on a Groupwide basis.

The credit profile of the Group's assets exposed to credit risk is shown in Table 6. The credit rating bands are provided by independent rating agencies.

Table 6 – Exposure to credit risk

As at 31 December 2006	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated £m	Total £m
Government securities	**4,790**	**66**	**79**	**–**	**–**	**95**	**5,030**
Other fixed rate securities	**5,333**	**2,621**	**6,706**	**2,166**	**87**	**1,488**	**18,401**
Variable rate securities	**534**	**111**	**232**	**–**	**–**	**49**	**926**
Mortgage backed securities	**388**	**–**	**–**	**–**	**–**	**5**	**393**
Other investments	**17**	**66**	**87**	**–**	**–**	**58**	**228**
Derivative assets	**14**	**24**	**2**	**–**	**–**	**–**	**40**
Cash equivalents	**376**	**101**	**1,459**	**–**	**–**	**6**	**1,942**
Financial assets	**11,452**	**2,989**	**8,565**	**2,166**	**87**	**1,701**	**26,960**
Reinsurance assets	**7**	**978**	**108**	**2**	**317**	**106**	**1,518**
	11,459	**3,967**	**8,673**	**2,168**	**404**	**1,807**	**28,478**

As at 31 December 2005	AAA £m	AA £m	A £m	BBB £m	BB and below £m	Unrated £m	Total £m
Government securities	4,826	205	28	–	–	–	5,059
Other fixed rate securities	5,216	2,623	6,893	2,573	12	1,070	18,387
Variable rate securities	433	93	371	1	–	42	940
Mortgage backed securities	385	–	6	–	–	19	410
Other investments	–	–	142	–	–	73	215
Derivative assets	–	15	11	–	–	–	26
Cash equivalents	293	130	1,147	–	–	142	1,712
Financial assets	11,153	3,066	8,598	2,574	12	1,346	26,749
Reinsurance assets	–	1,528	1,071	25	9	299	2,932
	11,153	4,594	9,669	2,599	21	1,645	29,681

51. RISK MANAGEMENT AND CONTROL continued

Liquidity risk

Liquidity risk is the risk that the Group, 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. The Group's treasury function is responsible for managing the Group's banking relationships, capital raising activities, overall cash and liquidity position and the payment of dividends. The Group seeks to manage funds and liquidity requirements on a pooled basis and to ensure the Group maintains sufficient liquid assets and standby facilities to meet a prudent estimate of its net cash outflows. In addition it ensures that, even under adverse conditions, the Group has access to the funds necessary to cover surrenders, withdrawals and maturing liabilities. In practice, most of the Group's invested assets are marketable securities. This, combined with the fact that a large proportion of the liabilities contain discretionary surrender values or surrender charges, reduces the liquidity risk. The Group has in place a £1bn, five year syndicated borrowing facility which provides flexibility in the management of the Group's liquidity.

Operational risk

Operational risk is the potential for loss resulting from inadequate or failed internal processes, people and systems, or from external events. There are a number of headings under which operational risk and its management across the Group can be considered. Identified control issues are escalated to business unit RCCs.

Internal process failure

The Group is exposed to the risk of loss from failure of the internal processes with which it transacts its business. Each subsidiary is responsible for ensuring the adequacy of the controls over its processes and regular reviews are undertaken of their appropriateness and effectiveness. All business managers are required to confirm regularly the adequacy of controls from these reviews to business unit RCCs, the GRCC and the Group Audit Committee. Significant control issues which business areas identify are escalated to business unit RCCs, which oversee their resolution.

People

The Group is potentially exposed to the risk of loss from inappropriate actions by its staff. The risk is actively managed by business management and human resource (HR) functions. Recruitment is managed centrally by HR functions, and all new recruits undergo a formal induction programme. All employees have job descriptions setting out their accountabilities and reporting lines, and are appraised annually in accordance with agreed performance management frameworks. Employees in regulated subsidiaries are provided with appropriate training to enable them to meet the relevant regulatory requirements. Risks relating to health and safety and other legislation are managed through the provision of relevant training to all staff.

Outsourcing

The Group is potentially exposed to the actions or failure of suppliers contracted to provide services on an outsourced basis, although the Group is not a significant user of such services. The required minimum standards of control for outsourced arrangements are set out in the Group's outsourcing and key supplier policy. Compliance with this policy is monitored by business management and adherence is reported through the regular controls confirmation process undertaken across the Group.

Legal

Legal risk is the risk of loss from unclear or deficient product documentation; inadequate documentation in support of material contracts such as reassurance treaties; the incorrect interpretation of changes in legislation; employment related disputes and claims; and commercial disputes with suppliers. The risks are actively managed through the Group Legal Risk framework, which defines minimum standards of control to be applied to minimise the risk of loss.

Compliance

Compliance risk within the Group relates to the risk of non-adherence to legislative requirements, regulations and internal policies and procedures. Responsibility for ensuring adherence to relevant legal and regulatory requirements is vested in individual business managers. They are supported, where appropriate, by business standards functions which assess and confirm that business processes conform to these requirements. A Group compliance function has oversight of the Group's compliance with regulatory requirements and standards, providing policy advice and guidance and oversight of compliance arrangements and responsibilities.

Event

Event risk relates to the potential for loss arising from external significant events such as terrorism, financial crisis, major changes in fiscal systems or disaster. Typically, such events have a low likelihood of occurrence, a material impact and can be difficult to prevent. The Group's risk mitigation focuses on minimising the business disruption and potential financial loss which may ensue from such an event. This includes maintaining a framework for the management of major incidents, the maintenance and regular testing of detailed business, technical and location recovery plans and the provision of insurance cover for the loss of buildings, contents and information technology (IT) systems and for the increased cost of working in the event of business disruption.

Fraud

The Group is exposed to the risk of internal fraud, claim related fraud, and external action by third parties. The risk of internal fraud is managed through a number of processes including the screening of staff at recruitment, segregation of duties and whistle-blowing policies. The activities of internal audit also act to counter the risk. Claims related fraud is managed by ensuring business processes are designed to fully validate claims and ensure that only bona fide claims are settled. Anti-fraud techniques are regularly updated to mitigate risks and emerging threats.

Technology

The Group places a high degree of reliance on IT in its business activities. The failure of IT systems could potentially expose the Group to significant business disruption and loss. To mitigate this risk, standards and methodologies for developing, testing and operating IT systems are maintained. There is a centralised management for development activity and production systems to ensure consistency and adherence to standards. Disaster recovery facilities enable IT operations to be conducted at remote locations in the event of the loss of computer facilities at a principal office site. All records are remotely backed up and computer suites are equipped with alternative power sources.

51. RISK MANAGEMENT AND CONTROL continued

UK life and pensions
UK life and pensions products are structured as either participating products, or non-participating products, including annuities in payment and unit linked products. The level of shareholders' interest in the value of policies and their share of the related profit or loss varies depending upon the contract structure.

Non-participating contracts
Profits from non-participating business accrue solely to shareholders. Such business is written mainly in the non profit part of the Society LTF. In addition, there is some non-participating business in the with-profits part of the Society LTF.

Protection business (individual and group)
The Group offers protection products which provide mortality or morbidity benefits and may include health, disability, critical illness and accident benefits. These additional benefits are commonly used 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 are sold to 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.

Life savings business
A range of contracts is offered in a variety of different forms to meet customers' long term savings objectives. Policyholders may choose to include a number of protection benefits in their savings contracts. Typically, any guarantees under the contract would only apply on maturity or earlier death. On certain older contracts there may be provisions guaranteeing surrender benefits. Savings contracts may or may not guarantee policyholders an investment return. Where the return is guaranteed, the Group may be exposed to interest rate risk with respect to the backing assets.

Pensions (individual and corporate)
These are long term savings contracts through which policyholders accumulate pension benefits. Some older contracts contain a basic guaranteed benefit expressed as an amount of pension payable or a guaranteed annuity option which exposes the Group to interest rate and longevity risk. These guarantees become more costly during periods when interest rates are low or when annuitant mortality improves faster than expected. The ultimate cost will also depend on the take-up rate of any option and the final form of annuity selected by the policyholder.

Other options provided by these contracts include an open market option on maturity, early retirement and late retirement. The Group would generally have discretion over the terms on which these options are offered.

Annuities
Deferred and immediate 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 Group manages the assets and accepts the liabilities of a company pension scheme or a life fund.

Non-participating deferred annuities written by the Group do not contain guaranteed cash options.

Annuity products provide guaranteed income for a specified time, usually the life of the policyholder, in exchange for a lump sum capital payment. No surrender value is available under any of these products. The primary risks to the Group from annuity products are therefore mortality improvements and investment risk.

There is a block of immediate and deferred annuities within the UK non profit business with benefits linked to changes in the Retail Price Index (RPI), but with contractual maximum or minimum increases. In particular, most of these annuities have a provision that the annuity will not reduce if RPI falls. The total of such annuities in payment at 31 December 2006 was £136m (2005: £190m). Thus, 1% negative inflation, which was reversed in the following year would result in a guarantee cost of approximately £1m (2005: £2m). Negative inflation sustained over a longer period would give rise to significantly greater guarantee costs. Some of these guarantee costs have been partially matched through the purchase of negative inflation hedges and limited price indexation bonds.

Key risk factors
(a) Insurance risk
(i) Mortality risk
For contracts providing death benefits, higher mortality rates would lead to an increase in claims costs. For annuity contracts the Group 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. The Group regularly reviews its mortality experience and industry projections of longevity and adjusts the valuation and pricing assumptions accordingly.

The Group is exposed to mortality risk on protection and annuity business. For protection products, the Group has entered into reinsurance arrangements to mitigate this risk and provide financing. Annuity contracts are not generally reinsured externally.

(ii) Persistency
At early durations, lapses and surrenders are likely to result in a loss to the Group, as the acquisition costs associated with the contract would not have been recovered from product margins. Some contracts include surrender penalties to mitigate this risk.

At later durations, 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 Group has some discretion in determining the amount of the payment. As a result, the effect on profit at later duration is expected to be broadly neutral.

Following the adoption of PS06/14 in 2006, as described in Note 37, the persistency assumption for non-participating protection business allows for the expected pattern of persistency, adjusted to incorporate a margin for adverse deviation. Previously, the liabilities were established so that they were sufficient to cover the more onerous of the two scenarios, in which the policies either remain in force until maturity, or discontinue at the valuation date.

There is no persistency risk exposure for annuities in payment. These contracts do not provide a lapse or surrender option.

(iii) Morbidity rates
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 and duration would increase costs over the level currently assumed in the calculation of liabilities.

(iv) Expense variances
Higher expenses and/or expense inflation will tend to increase the value of the reserves required. The Group is exposed to the risk that its liabilities are not sufficient to cover future expenses.

(v) Geographic concentrations of risk
Insurance risk may be concentrated in geographic regions, altering the risk profile of the Group. The most significant exposure of this type arises for the group protection business, where a single event could result in a large number of related claims. To reduce the overall exposure, current contracts include an 'event limit' which caps the total liability. Additionally, excess of loss reinsurance arrangements further mitigate the exposure.

51. RISK MANAGEMENT AND CONTROL continued

(vi) Epidemics
The spread of an epidemic could cause large aggregate claims across the Group's portfolio. Quota share reinsurance contracts are used to manage this risk.

(vii) Accumulation of risks
There is limited potential for single incidents to give rise to a large number of claims across the different contract types written by the Group. In particular, there is little significant overlap between the long term and short term insurance business written by the Group. However, there are potentially material correlations of insurance risk with other types of risk exposure. These correlations are difficult to estimate though they 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 credit risk with mortality and morbidity exposures.

(b) Market risk
Investment of the assets backing the Group liabilities reflects the nature of the liabilities being supported. For non-participating business the objective is to maximise profits, while ensuring stability, by closely matching the cash flows of assets and liabilities. To achieve this matching, the strategy is to invest in fixed income securities of appropriate maturity dates.

Interest rate risk is reduced by managing the duration and maturity structure of each investment portfolio in relation to the estimated duration of the liabilities it supports. A number of derivatives are held to enable the matching of asset and liability to mitigate further exposure to interest rate movements, in particular to limit the exposure to any options and guarantees in contracts.

In addition, the exposure to these risks is allowed for in the actuarial valuation of liabilities under these contracts.

(c) Sensitivity analysis
Table 7 shows the impact on pre-tax profit and equity, net of reinsurance, under each sensitivity scenario for the non-participating business written in the non profit part of the UK LTF.

Table 7 – UK non profit life and pensions sensitivity analysis

	Impact on pre-tax profit net of reinsurance 2006 £m	Impact on equity net of reinsurance 2006 £m
Sensitivity test		
Market interest rate increase of 1%	**(139)**	**(98)**
Market interest rate decrease of 1%	**237**	**166**
Reduction in the mortality rates for annuitants of 5%	**(234)**	**(164)**
Protection claims increasing by 5%	**(73)**	**(51)**
Increase in expenses of 10%	**(59)**	**(41)**
Increase in lapse rates of 10%	**(25)**	**(18)**
Decrease in lapse rates of 10%	**27**	**19**

- In calculating the alternative values, all other assumptions are left unchanged. In practice, items of the Group's experience may be correlated.
- The Group seeks to actively manage its asset and liability position. A change in market conditions would lead to changes in the asset allocation or charging structure which may have a more significant impact on the value of the liabilities. The analysis also ignores any second order effects of the assumption change, including the potential impact on the Group asset and liability position and any second order tax effects.
- The sensitivity of the profit to changes in assumptions may not be linear as implied by these results. They should not be extrapolated to changes of a much larger order.
- The change in market interest rate test assumes a 100 basis point change in the gross redemption yields on UK life and pensions fixed interest securities together with a 100 basis point change in the real yields on variable securities. Valuation interest rates move in line with market yields adjusted to allow for the impact of FSA regulations.

51. RISK MANAGEMENT AND CONTROL continued

Participating contracts

Participating contracts are supported by the with-profits part of the Society LTF. They offer policyholders the possibility of the payment of benefits in addition to those guaranteed by the contract. The amount and timing of the additional benefits (usually called bonuses) are contractually at the discretion of the Group.

Policyholders and shareholders share in the risks and returns of the with-profits part of the Society LTF. The return to shareholders on virtually all participating products is in the form of a transfer to shareholders' equity, which is analogous to a dividend from the Society LTF and is dependent upon the bonuses credited or declared on policies in that year. The bonuses are broadly based on historic and current rates of return on equity, property and fixed income securities, as well as expectations of future investment returns.

UK life and pensions allocates discretionary increases to benefits on its participating contracts in one or both of regular and final bonus form. These bonuses are set in accordance with the principles outlined in the Group's PPFM for the management of the with-profits part of the Society LTF. These principles include:

- The with-profits part of the Society LTF will be managed with the objective of ensuring that its assets are sufficient to meet its liabilities without the need for additional capital.
- With-profits policies have no expectation of any distribution from the with-profits part of the Society LTF's inherited estate. The inherited estate is the excess of assets held within the Society LTF over and above the amount required to meet liabilities, including those which arise from the regulatory duty to treat customers fairly in setting discretionary benefits.
- Bonus rates will be smoothed so that some of the short term fluctuations in the value of the investments of the with-profits part of the Society LTF and the business results achieved in the with-profits part of the UK LTF are not immediately reflected in payments under with-profits policies.

Some older participating contracts include a guaranteed minimum rate of roll up of the policyholder's fund up to the date of retirement or maturity.

The nature of the participating contracts written in the with-profits part of the Society LTF is that more emphasis can be placed on investing to maximise future investment returns. This results in a broader range of investments being held within the fund.

With-profits bonds

These contracts provide an investment return to the policyholder which is determined by the attribution of regular and final bonuses over the duration of the contract. In addition, the contracts provide a death benefit, typically of 101% of the value of units allocated to the policyholder.

Pension contracts

The Group has sold pension contracts containing guaranteed annuity options which expose the Group to both interest rate and longevity risk. The market consistent value of these guarantees carried in the balance sheet is £75m (2005: £130m).

Deferred annuity contracts

The Group has written some deferred annuity contracts which have guaranteed minimum pensions. These options expose the Group to interest rate risk as the cost would be expected to increase with interest rates. These guarantees only apply with respect to premiums already received. The market consistent value of these guarantees carried in the balance sheet is £114m (2005: £120m).

Key risk factors

The insurance and market risk exposures for participating business are largely the same as those discussed for non-participating contracts. The notable differences in the operation of these contracts are discussed below.

(a) Insurance risk

(i) Persistency

At early durations, the nature of the persistency risks on with-profits business is largely the same as for non-participating business and is influenced mainly by the ability to recover acquisition costs from product margins. At later durations, there is less scope for withdrawal to result in a loss for the Group as these contracts typically provide explicit allowances for market conditions. Allowance for future withdrawals is made in the assessment of participating contract liabilities. The Group is generally exposed to the risk that future withdrawals are lower than assumed, resulting in higher future guarantee costs.

(b) Market risk

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.

These risks are managed by maintaining capital sufficient to cover the consequences of mismatch under a number of adverse scenarios and by the use of derivatives. 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 and are managed so as to provide a partial hedge to movements in fixed interest yields.

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 Group's investment policy, which aims to optimise returns to policyholders over time whilst limiting capital requirements for this business.

The distribution of surplus to shareholders depends upon the bonuses declared within the fund. Typically, bonus rates are set with regard to investment returns, although the Group has some discretion setting rates and would normally smooth bonuses over time. The volatility of investment returns could have both a favourable and unfavourable impact on the fund's capital position and its ability to pay bonuses. If future investment conditions were less favourable than anticipated, the lower bonus levels resulting would also reduce future distributions to shareholders.

However, business which is written in the with-profits part of the Society LTF is managed to be self-supporting. The unallocated divisible surplus in the fund would normally be expected to absorb the impact of these investment risks. Only in extreme scenarios, where shareholders were required to provide capital support to the with-profits part of the Society LTF, would these risks affect equity.

The Group's approach to setting bonus rates is designed to treat customers fairly. The approach is set out in the Society's PPFM for the with-profits part of the Society LTF. In addition, bonus declarations are also affected by FSA regulations relating to Treating Customers Fairly (TCF), which limit the discretion available when setting bonus rates. The Group's approach to setting bonuses and meeting the FSA's TCF regulations may increase the Group's exposure to market risk should the ability to cut bonuses, during periods when investment returns are poor, be reduced.

51. RISK MANAGEMENT AND CONTROL continued

(c) Sensitivity analysis

Future bonuses influence both the current capital requirements of the fund and future profitability.

The unallocated divisible surplus is accounted for as a liability. This represents the assets within the with-profits part of the Society LTF, in excess of the realistic liabilities, which are available to pay future bonuses. Changes in the key underlying variables will affect the value of the assets and liabilities in the fund. The level of unallocated divisible surplus will be adjusted to allow for changes in assets and liabilities and, as a result, there would normally be no impact on shareholders' equity.

In extreme scenarios shareholders may be called upon to provide additional capital support to the fund. However, the Group has discretion in the management actions it can take with regard to participating policies to mitigate the extent of any additional support required.

Participating policyholders and shareholders share in all surplus arising in the with-profits part of the Society LTF. 10% of the surplus is normally distributed to shareholders. The risk factors detailed in this section could affect future distributions of surplus and shareholders' 10% share thereof.

Linked contracts

For linked contracts (investment and insurance), there is a direct link between the investments and the obligations. Linked business is written in both the Society LTF and in the LTF of Legal & General Assurance (Pensions Management) Limited. The financial risk on these contracts is borne by the policyholders. The Group is, therefore, not exposed to any market risk, currency risk and credit risk for these contracts. The Group's primary exposure to financial risk from these contracts is the risk of volatility in asset management fees 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. The Group is also exposed to the risk of an expense overrun should the market depress the level of charges which could be imposed, although for some contracts the Group has discretion over the level of management charges levied.

International life and pensions

Legal & General America (LGA)

The principal products written by LGA are individual term assurance, universal life insurance and smaller blocks of deferred and immediate annuities.

The individual term assurances provide death benefits over the medium to long term. The contracts have level premiums for an initial period with premiums increasing annually thereafter. During the initial period, there is generally an option to convert the contract to a universal life contract. After the initial period, the premium rates are not guaranteed, but cannot exceed the age related guaranteed premium.

Reinsurance is used to reduce the insurance risk on this portfolio and manage liquidity risks, through the reinsurance commission received under quota share arrangements. Reinsurance and securitisation are used to provide regulatory solvency relief (including relief from regulation Triple X). These practices lead to the establishment of reinsurance assets on the Group's balance sheet.

The universal life insurance and deferred annuities provide a savings element. In addition to the savings component, the universal life contract provides substantial death benefits over the medium to long term. The savings element has a guaranteed minimum growth rate. LGA has exposure to loss in the event that interest rates decrease and it is unable to earn enough on the underlying assets to cover the guaranteed rate. LGA is also exposed to loss should interest rates increase, as the underlying market value of assets will generally fall without a change in the surrender value. The reserves for universal life and deferred annuities totalled $766m and $272m respectively at 31 December 2006 (2005: $799m and $277m respectively). The guaranteed interest rates associated with those reserves ranged from 1.5% to 5.5%, with the majority of the policies having a 4% guaranteed rate (the same rates applied in 2005).

The deferred annuity contracts also contain a provision that, at maturity, a policyholder may move the account value into an immediate annuity, at rates which are either those currently in effect, or rates guaranteed in the contract. The other annuity contracts have similar risks to those in the UK.

Legal & General Netherlands (LGN)

LGN principally writes non-participating individual unit linked savings, protection and annuity business. The unit linked savings business generally includes an element of exposure to mortality risk. The individual term assurances provide death benefits over the medium to long term. Reinsurance is used to reduce the share of insurance risk.

The annuity contracts have similar risks to those in the UK; however, the majority of annuity business has a term of three years or less.

Legal & General France (LGF)

LGF writes a range of long term insurance and investment business through its subsidiaries. The principal products written are life assurance and pensions savings, group protection, annuities and open ended investment vehicles.

The group protection business consists of group term assurance, renewable on an annual basis, sickness and disability, and medical expenses assurance. The group sickness and disability and medical expenses policies integrate with the social security benefits providing a level of top-up to those benefits. Reinsurance is used to manage exposure to large individual and group claims.

The annuity contracts have similar risks to those in the UK.

General insurance

LGI offers a range of general insurance contracts, including:

- Household contracts. These provide cover in respect of policyholders' homes, investment properties, contents, personal belongings and incidental liabilities which they may incur as a property owner, occupier or private individual. Exposure is normally limited to the rebuilding cost of the home, the replacement cost of belongings and a policy limit in respect of liability claims. LGI uses reinsurance to manage the exposure to an accumulation of claims arising from any one incident, usually severe weather. The catastrophe cover reinsures LGI for losses between £30m and £250m (2005: £25m and £225m) for a single weather event.
- Motor insurance. These contracts provide cover in respect of customers' private cars and their liability to third parties in respect of damage to property and injury. Exposure is normally limited to the replacement value of the vehicle, and a policy limit in respect of third party property damage. Exposure to third party bodily injury is unlimited in accordance with statutory requirements.
- Accident, sickness and unemployment (ASU). These contracts provide cover in respect of continuing payment liabilities incurred by customers when they are unable to work as a result of accident, sickness or unemployment. They protect predominantly mortgage payments. Exposure is limited to the monthly payment level selected by the customer sufficient to cover the payment and associated costs, up to the duration limit specified in the policy.

51. RISK MANAGEMENT AND CONTROL continued

- Healthcare. These contracts are primarily private medical insurance, which compensate customers for the costs of eligible medical consultations, diagnostic tests, in-patient, day care and outpatient treatment up to the limits specified in the policy. They are mainly exposed to the underlying incidence of morbidity, medical claims inflation and advances in medical treatments.
- Domestic mortgage indemnity (DMI). These contracts (primarily in run-off) protect a mortgage lender should an insured property be repossessed and subsequently sold at a loss. Since 1993, the contract has included a maximum period of cover of 10 years, and a cap on the maximum claim. For business accepted prior to 1993, cover is unlimited and lasts until the insured property is remortgaged or redeemed.

Key risk factors

Weather events

Significant weather events such as windstorms, and coastal and river floods can lead to significant claims.

The insurance of properties which are concentrated in high risk areas, or an above average market share in a particular region, can give rise to a concentration of insurance risk. This risk is managed by ensuring that the risk acceptance policy, terms and premiums both reflect the expected claim cost associated with the location and avoid adverse selection. Additionally, exposure and competitor activity is monitored by location to ensure that there is a geographic spread of business. Catastrophe reinsurance cover reduces the Group's exposure to concentrations of risk. The level of catastrophe cover is selected to manage the risk of an event which would be expected to occur once in every 200 years.

Subsidence

The incidence of subsidence can have a significant impact on the level of claims on household policies. The Group's underwriting and reinsurance strategy mitigates the exposure to concentrations of risk arising from geographic location or adverse selection.

Unlimited motor claims

A single motor policy can result in major multiple liability claims in extreme scenarios. To mitigate this risk, accident excess of loss reinsurance is in place for claims in excess of £1m (2005: £1m).

Sensitivity analysis

Table 8 shows material sensitivities for the General insurance business on pre-tax profit and equity, net of reinsurance.

Table 8 – General insurance sensitivity analysis

	Impact on pre-tax profit net of reinsurance 2006 £m	Impact on equity net of reinsurance 2006 £m
Sensitivity test		
Single storm event with 1 in 200 year probability	**(30)**	**(21)**
Subsidence event – worst claim ratio in last 30 years	**(37)**	**(26)**
Repeat of 1990 recession on ASU/DMI/household accounts	**(52)**	**(36)**
5% decrease in overall claims ration	**15**	**11**
5% surplus over claims liabilities	**7**	**5**

For any single event with claims in excess of £30m but less than £250m, the ultimate cost to the Group would be £38.5m. The impact of a 1 in 500 year event would exceed the catastrophe cover by approximately £100m.

For the year ended 31 December 2006

	Notes	2006 £m	2005 £m
From continuing operations			
Life and pensions	16/17	**1,030**	901
Investment management	22	**181**	136
General insurance		**9**	14
Other operational income	23	**13**	41
Operating profit		**1,233**	1,092
Variation from longer term investment return	20	**460**	870
Effect of economic assumption changes	16	**2**	8
Property income attributable to minority interests		**67**	81
Corporate restructure	14	**(216)**	–
Profit from continuing operations before tax attributable to equity holders		**1,546**	2,051
Tax charge on operating profit		**(361)**	(314)
Tax charge on other profits and losses		**(61)**	(249)
Tax charge on profit from ordinary activities	24	**(422)**	(563)
Effect of UK tax changes	25	**–**	(276)
Tax impact of corporate restructure	14/25	**322**	–
Profit from continuing operations after tax		**1,446**	1,212
Profit from discontinued operations		**–**	13
Profit from ordinary activities after tax		**1,446**	1,225
Profit attributable to minority interests		**(67)**	(81)
Profit attributable to equity holders of the Company		**1,379**	1,144

	Notes	p	p
Earnings per share	26		
Based on operating profit from continuing operations after tax		**13.45**	12.02
Based on profit attributable to ordinary equity holders of the Company		**21.27**	17.42
Diluted earnings per share	26		
Based on operating profit from continuing operations after tax		**13.36**	11.74
Based on profit attributable to ordinary equity holders of the Company		**21.12**	16.89

Supplementary Financial Statements – European Embedded Value Basis
Consolidated Balance Sheet

As at 31 December 2006

	Notes	2006 £m	2005 £m
Assets			
Investments		**213,228**	186,413
Long term in-force business asset		**2,529**	2,738
Other assets		**4,614**	5,427
		220,371	194,578
Equity and liabilities			
Ordinary shareholders' equity	28/29	**7,931**	6,970
Subordinated borrowings designated as equity		**–**	394
Minority interests		**414**	285
Total equity		**8,345**	7,649
Subordinated borrowings		**818**	415
Unallocated divisible surplus		**2,178**	1,894
Participating contract liabilities		**19,770**	20,277
Non-participating contract liabilities		**183,618**	158,956
Senior borrowings		**1,607**	1,634
Other liabilities and provisions		**4,035**	3,753
		220,371	194,578

Consolidated Statement of Recognised Income and Expense

For the year ended 31 December 2006

	2006 £m	2005 £m
Fair value losses on cash flow hedges	**(3)**	–
Exchange differences on translation of overseas operations	**(41)**	22
Actuarial gains/(losses) on defined benefit pension schemes	**3**	(55)
Actuarial (gains)/losses on defined benefit pension schemes transferred to unallocated divisible surplus	**(1)**	22
Expense recognised directly in equity, net of tax	**(42)**	(11)
Profit from ordinary activities after tax	**1,446**	1,225
Total recognised income and expense	**1,404**	1,214
Attributable to:		
Minority interests	**67**	81
Equity holders of the Company	**1,337**	1,133

1. BASIS OF PREPARATION

The supplementary financial statements have been prepared in accordance with the European Embedded Value (EEV) Principles issued in May 2004 by the European CFO Forum.

These supplementary financial statements have been audited by PricewaterhouseCoopers LLP and prepared in conjunction with our consulting actuaries – Tillinghast Towers-Perrin and, in the US, Milliman USA.

2. COVERED BUSINESS

The Group uses EEV methodology to value individual and group life assurance, pensions and annuity business written in the UK, Continental Europe and the US and within our UK managed pension funds company.

All other businesses are accounted for on the IFRS basis adopted in the primary financial statements.

There is no distinction made between insurance and investment contracts in the life and pensions businesses as there is under IFRS.

3. DESCRIPTION OF METHODOLOGY

The objective of EEV is to provide shareholders with more realistic information on the financial position and current performance of the Group than is provided within the primary financial statements.

The methodology requires assets of an insurance company, as reported in the primary financial statements, to be attributed between those supporting the covered business and the remainder. The method accounts for assets in the covered business on an EEV basis and the remainder of the Group's assets on the IFRS basis adopted in the primary financial statements.

The EEV methodology recognises as profit from the covered business the total of:

i. cash transfers during the relevant period from the covered business to the remainder of the Group's assets; and
ii. the movement in the present value of future distributable profits to shareholders arising from the covered business over the relevant reporting period.

4. EMBEDDED VALUE

Shareholders' equity on the EEV basis comprises the embedded value of the covered business plus the shareholders' equity on other businesses, less the value included for purchased interests in long term business.

The embedded value is the sum of the shareholder net worth (SNW) and the value of the in-force business (VIF). SNW is defined as those amounts, within covered business (both within the LTF and held outside the LTF but used to support long term business), which are regarded either as required capital or which represent free surplus.

The VIF is the present value of future shareholder profits arising from the covered business, projected using best estimate assumptions, less an appropriate deduction for the cost of holding the required level of capital and the time value of financial options and guarantees.

5. SERVICE COMPANIES

All services relating to the UK life and pensions business are charged on a cost recovery basis, with the exception of investment management services provided to Legal & General Pensions Limited (LGP), which are charged on an arm's length fee basis. Profits arising on the provision of these services are valued on a "look through" basis.

6. NEW BUSINESS

New business premiums reflect income arising from the sale of new contracts during the reporting period and any changes to existing contracts, which were not anticipated at the outset of the contract.

In-force business comprises previously written single premium, regular premium and recurrent single premium contracts.

DWP rebates have not been treated as recurrent and are included in single premium new business when received.

New business contribution arising from the new business premiums written during the reporting period has been calculated on the same economic and operating assumptions used in the embedded value at the end of the financial period. This has then been rolled forward to the end of the financial period using the risk discount rate applicable at the end of the reporting period.

The present value of new business premiums (PVNBP) has been calculated and expressed at the point of sale. The PVNBP is equivalent to the total single premiums plus the discounted value of regular premiums expected to be received over the term of the contracts using the same economic and operating assumptions used for the embedded value at the end of the financial period. The new business margin is defined as new business contribution at the end of the reporting period divided by the PVNBP. The premium volumes and projection assumptions used to calculate the PVNBP are the same as those used to calculate new business contribution.

7. PROJECTION ASSUMPTIONS

Cash flow projections are determined using realistic assumptions for each component of cash flow and for each policy group. Future economic and investment return assumptions are based on conditions at the end of the financial year. Future investment returns are projected by one of two methods. The first method is based on an assumed investment return attributed to assets at their market value. The second, which is used in the US, where the investments of that subsidiary are substantially all fixed interest, projects the cash flows from the current portfolio of assets and assumes an investment return on reinvestment of surplus cash flows. The assumed discount and inflation rates are consistent with the investment return assumptions.

Detailed projection assumptions including, mortality, persistency, morbidity and expenses, reflect recent operating experience and are reviewed annually. Allowance is made for future improvements in annuitant mortality based on experience and externally published data. Favourable changes in operating experience are not anticipated until the improvement in experience has been observed.

All costs relating to the covered business, whether incurred in the covered business or elsewhere in the Group, are allocated to that business. The expense assumptions used for the cash flow projections therefore include the full cost of servicing this business.

8. TAX

The projections take into account all tax which is expected to be paid, based on best estimate assumptions, applying current legislation and practice together with known or expected future changes. This includes tax which would arise if surplus assets within the covered business were eventually to be distributed. The future benefit of certain current UK tax rules on the apportionment of income has not been reflected. It is expected that these rules will be amended as part of the current consultation on life assurance taxation, such that the benefit is not expected to be realised.

9. ALLOWANCE FOR RISK

Aggregate risks within the covered business are allowed for through the following principal mechanisms:

i. setting required capital levels with reference to both the Group's internal risk based capital models, and an assessment of the strength of regulatory reserves in the covered business;
ii. allowing explicitly for the time value of financial options and guarantees within the Group's products; and
iii. setting risk discount rates by deriving a Group level risk margin to be applied consistently to local risk free rates.

10. REQUIRED CAPITAL AND FREE SURPLUS

Regulatory capital for UK life and pensions business is provided by assets backing the with-profits business or by the SNW. The SNW comprises the sum of the values of the Shareholder Retained Capital (SRC), the Sub-fund and the shareholder capital within LGP.

For UK with-profits business, the required capital is covered by the surplus within the with-profits part of the fund and no effect is attributed to shareholders except for the burn-through cost, which is described later. This treatment is consistent with the Principles and Practices of Financial Management for this part of the fund.

For UK non profit business, the required capital will be maintained at no less than the level of the EU minimum solvency requirement. This level, together with the margins for adverse deviation in the regulatory reserves, is, in aggregate, in excess of internal capital targets assessed in conjunction with the Individual Capital Adequacy (ICA) assessment.

In Society, the SRC is either required to cover EU solvency margin or is encumbered because its distribution to shareholders is restricted due to previous understandings with the Financial Services Authority. It is therefore classified as required capital and not as free surplus for the purposes of EEV reporting. SRC is valued by assuming it is distributed from the LTF over a 20 year period with allowance for tax payable on distribution. For this purpose, distribution of the SRC is restricted such that there is always sufficient SRC left to cover the EU solvency margin for in-force non profit business in Society.

In LGP, the shareholder capital covers the EU minimum solvency margin for the business.

The initial strains relating to new non profit business, together with the related EU solvency margin, are supported by releases from existing non profit business, the SRC and LGP shareholder capital. As a consequence, the writing of new business defers the release of capital from the SRC and LGP shareholder capital to free surplus. Any assets in LGP shareholder capital in excess of those required to cover the EU minimum solvency margin are treated as free surplus. Cost of holding required capital is defined as the difference between the value of the required capital and the present value of future releases of that capital. For new business, the cost of capital is taken as the difference in the value of that capital assuming it was available for release immediately and the present value of the future releases of that capital. As the investment return, net of tax, on that capital is less than the risk discount rate, there is a resulting cost of capital which is reflected in the value of new business.

The Sub-fund is also treated as required capital, because its distribution to shareholders is restricted by Society's Articles of Association.

For our UK managed pension funds business, management's capital policy has been used to set the level of required capital. The balance of net assets within the UK Managed Funds business is treated as free surplus.

For Legal & General America, the Company Action Level (CAL) of capital has been treated as required capital for modelling purposes. The CAL is the regulatory capital level at which the Company would have to take prescribed action, such as submission of plans to the State insurance regulator, but would be able to continue operating on the existing basis. The CAL is currently twice the level of capital at which the regulator is permitted to take control of the business.

For Legal & General Netherlands, required capital has been set at 100% of EU minimum solvency for all products which do not have any related financial options and guarantees (FOGs). For those products with FOGs, capital of between 112.5% and 130% of the EU minimum solvency margin has been used. The level of capital has been determined using risk based capital techniques.

For Legal & General France, 100% of EU minimum solvency margin has been used for EV modelling purposes for all products both with and without FOGs. The level of capital has been determined using risk based capital techniques.

The contribution from new business for our overseas businesses reflects an appropriate allowance for the cost of holding the required capital.

11. FINANCIAL OPTIONS AND GUARANTEES

In the UK, all FOGs are within the UK life and pensions business.

Under the EEV Principles an allowance for time value of FOGs is required where a financial option exists which is exercisable at the discretion of the policyholder. These types of option principally arise within the with-profits part of the fund and their time value is recognised within the with-profits burn-through cost described below. Additional financial options for non profit business exist only for a small amount of deferred annuity business where guaranteed early retirement and cash commutation terms apply when the policyholders choose their actual retirement date.

Further financial guarantees exist for non profit business, in relation to index-linked annuities where capped or collared restrictions apply. Due to the nature of these restrictions and the manner in which they vary depending on the prevailing inflation conditions, they are also treated as FOGs and a time value cost recognised accordingly.

The time value of FOGs has been calculated stochastically using a large number of real world economic scenarios derived from assumptions consistent with the deterministic EEV assumptions and allowing for appropriate management actions where applicable. The management action primarily relates to the setting of bonus rates. Future regular and terminal bonuses on participating business within the projections are set in a manner consistent with expected future returns available on assets deemed to back the policies within the stochastic scenarios.

In recognising the residual value of any projected surplus assets within the with-profits part of the fund in the deterministic projection, it is assumed that terminal bonuses are increased to exhaust all of the assets in the part of the fund over the future lifetime of the in-force with-profits policies. However, under stochastic modelling, there may be some extreme economic scenarios when the total projected assets within the with-profits part of the fund are insufficient to pay all projected policyholder claims and associated costs. The average additional shareholder cost arising from this shortfall has been included in the time value cost of options and guarantees and is referred to as the with-profits burn-through cost.

The same economic scenarios have been used to assess the time value of the financial guarantees for non profit business by using the inflation rate generated in each scenario. The inflation rate used to project index-linked annuities will be constrained in certain real world scenarios, for example, where negative inflation occurs but the annuity payments do not reduce below pre-existing levels. The time value cost of FOGs allows for the projected average cost of these constrained payments for the index-linked annuities. It also allows for the small additional cost of the guaranteed early retirement and cash commutation terms for the minority of deferred annuity business where such guarantees have been written.

11. FINANCIAL OPTIONS AND GUARANTEES continued

In the US, FOGs relate to guaranteed minimum crediting rates and surrender values on a range of contracts. The guaranteed surrender value of the contract is based on the accumulated value of the contract including accrued interest. The crediting rates are discretionary but related to the accounting income for the amortising bond portfolio. The majority of the guaranteed minimum crediting rates are between 4% and 5%. The assets backing these contracts are invested in US dollar denominated fixed interest securities.

In the Netherlands, there are two types of guarantees which have been separately provided for: interest rate guarantees and maturity guarantees. Certain contracts provide an interest rate guarantee where there is a minimum crediting rate based on the higher of 1-year Euribor and the policy guarantee rate. This guarantee applies on a monthly basis. Certain unit linked contracts provide a guaranteed minimum value at maturity where the maturity amount is the higher of the fund value and a guarantee amount. The fund values for both these contracts are invested in Euro denominated fixed interest securities.

In France, FOGs which have been separately provided for relate to guaranteed minimum crediting rates and surrender values on a range of contracts. The guaranteed surrender value of the contract is the accumulated value of the contract including accrued bonuses. The bonuses are based on the accounting income for the amortising bond portfolios plus income and releases from realised gains on any equity type investments. Policy liabilities equal guaranteed surrender values. Local statutory accounting rules require the establishment of a specific liability when the accounting income for a company is less than 125% of the guaranteed minimum credited returns, although this has never been required. In general, the guaranteed annual bonus rates are between 1.5% and 4.5%.

12. RISK DISCOUNT RATE

The risk discount rate (RDR) is a combination of the risk free rate and a risk margin, which reflects the residual risks inherent in the Group's covered businesses, after taking account of prudential margins in the statutory provisions, the required capital and the specific allowance for financial options and guarantees.

The risk margin has been determined based on an assessment of the Group's weighted average cost of capital (WACC). This assessment incorporates a beta for the Group, which measures the correlation of movements in the Group's share price to movements in a relevant index. Beta values therefore allow for the market's assessment of the risks inherent in the business relative to other companies in the chosen index.

The WACC is derived from the Group's cost of equity and debt, and the proportion of equity to debt in the Group's capital structure measured using market values. Each of these three parameters should be forward looking, although informed by historic information. The cost of equity is calculated as the risk free rate plus the equity risk premium for the chosen index multiplied by the Company's beta. Forward-looking or adjusted betas make allowance for the observed tendency for betas to revert to 1 and therefore a weighted average of the historic beta and 1 tends to be a better estimate of the Company's beta for the future period. We have computed the WACC using an arithmetical average of forward-looking betas against the FTSE 100 index.

The cost of debt used in the WACC calculations takes account of the actual locked-in rates for our senior and subordinated long term debt. All debt interest attracts tax relief at a rate of 30%.

Whilst the WACC approach is a relatively simple and transparent calculation to apply, subjectivity remains within a number of the assumptions. Management believes that the chosen margin, together with the levels of required capital, the inherent strength of the Group's regulatory reserves and the explicit deduction for the cost of options and guarantees, is appropriate to reflect the risks within the covered business. For these results the risk margin has been maintained at 3.0%.

A similar approach will be adopted when risk margins are reassessed in future periods.

Key assumptions are summarised below:

Risk free rate	Derived from gross redemption yields on relevant gilt portfolio
Equity risk premium	3.0% (UK only)
Property risk premium	2.0% (UK only)
Risk margin	3.0%

13. ANALYSIS OF PROFIT

Operating profit is identified at a level which reflects an assumed longer term level of investment return.

The contribution to operating profit in a period is attributed to four sources:

i. new business;
ii. the management of in-force business;
iii. development costs; and
iv. return on shareholder net worth.

Further profit contributions arise from actual investment return differing from the assumed long term investment return (investment return variances), and from the effect of economic assumption changes.

The contribution from new business represents the value recognised at the end of each period from new business written in that period, after allowing for the actual cost of acquiring the business and of establishing the required technical provisions and reserves and after making allowance for the cost of capital. New business contributions are calculated using closing assumptions.

The contribution from in-force business is calculated using opening assumptions and comprises:

i. expected return – the discount earned from the value of business in-force at the start of the year;
ii. experience variances – the variance in the actual experience over the reporting period from that assumed in the value of business in-force as at the start of the year; and
iii. operating assumption changes – the effects of changes in future assumptions, other than changes in economic assumptions from those used in valuing the business at the start of the year. These changes are made prospectively from the end of the year.

Development costs are associated with investment in building a new enterprise or exceptional development activity over a defined period.

The contribution from shareholder net worth comprises the increase in embedded value based on assumptions at the start of the year in respect of:

i. encumbered assets within the covered business – principally the unwind of the discount rate;
ii. LGP shareholder capital – the expected investment return; and
iii. residual assets – the expected investment return.

Further profit contributions arise from actual investment returns differing from the assumed long term investment returns (investment return variances) and from the effect of economic assumption changes.

Investment return variances represent the effect of actual investment performance and changes to investment policy on shareholder net worth and in-force business from that assumed at the beginning of the period.

Economic assumption changes comprise the effect of changes in economic variables, beyond the control of management, including associated changes to valuation bases to the extent that they are reflected in revised assumptions.

14. SIGNIFICANT IMPACTS

Corporate restructuring

On 31 December 2006, the non-linked non profit pensions and annuity business of Legal & General Assurance Society Limited (Society) was ceded to a new, wholly owned, reinsurance company, Legal & General Pensions Limited (LGP). The required capital and free surplus of LGP is included in the covered business.

LGP has been capitalised using £1.3bn of Society shareholder capital, £400m of this is represented by subordinated debt (£200m upper tier II, £200m lower tier II) and £900m by equity. The reinsurance was effected on arm's length terms resulting in an initial regulatory loss in LGP. Further funds of £571m have been injected from Society's LTF into LGP's LTF by means of a contingent loan to cover this loss.

Prior to the capitalisation of LGP, the intra-group subordinated debt capital of £602m attributed to SRC was repaid to Group Plc and an equivalent amount was lent to Society shareholder capital on a subordinated basis (£301m upper tier II, £301m lower tier II).

Overall, the corporate restructuring has increased the embedded value by £171m. This arises from tax benefits totalling £322m, which include a reversal of the adverse impact of the 2005 UK tax changes. This is offset by an additional cost of solvency capital of £119m in LGP and other impacts of £32m which together total £151m. The EEV impact of the net tax benefits is reported within the tax section of the income statement. The impact of the higher cost of solvency capital and other impacts is reported below operating profit and grossed up for tax at 30%. The tax gross up of £65m is included in the tax charge. The additional cost of solvency capital in respect of new business transferred to LGP has reduced the contribution from new business by £19m.

Implementation of changes to FSA reporting and capital rules (Policy Statement 06/14)

In 2006, the FSA introduced a more realistic reserving framework for certain non profit business. As a result, there has been a reduction in the regulatory reserves required for term assurance business of £641m. The associated financial reinsurance previously in place to finance these reserves was terminated.

The impact of these changes has been to increase the EEV operating assumption changes by £64m, and contribution from new business by £33m, due to the resulting lower capital requirements.

Review of annuity investment policy

During 2006, Society undertook a review of its asset liability matching policy for annuity business. Property assets backing annuity liabilities were replaced with corporate bonds and Society entered into inflation swaps to mitigate negative inflation risk. As a result, a closer match between assets and liabilities was achieved. Additionally, the margin within the reserves to cover an interest rate mismatch was reviewed and reduced.

EEV operating profit has increased by £18m due to the reduction in the capital requirement. However, the EEV variation from longer term investment return is reduced by £27m due to the change in asset mix.

15. PRESENT VALUE OF NEW BUSINESS PREMIUMS (PVNBP)

For the year ended 31 December 2006	Annual premiums £m	Present value of annual premiums £m	Capitalisation factor	Single premiums £m	PVNBP £m	New business margin %
UK	**474**	**2,115**	**4.5**	**5,991**	**8,106**	**4.7**
International	**66**	**459**	**7.0**	**365**	**824**	**4.6**
	540	**2,574**		**6,356**	**8,930**	**4.7**

For the year ended 31 December 2005	Annual premiums £m	Present value of annual premiums £m	Capitalisation factor	Single premiums £m	PVNBP £m	New business margin %
UK	382	1,722	4.5	4,899	6,621	4.6
International	72	524	7.3	349	873	2.9
	454	2,246		5,248	7,494	4.4

16. PROFIT FROM CONTINUING OPERATIONS AFTER TAX FROM COVERED BUSINESS

For the year ended 31 December 2006	Notes	UK £m	International £m	Life and pensions total £m	Investment management[1] £m	Total £m
Contribution from new business after cost of capital		**380**	**38**	**418**	**61**	**479**
Contribution from in-force business:						
– expected return		**323**	**70**	**393**	**24**	**417**
– experience variances	18	**41**	**19**	**60**	**34**	**94**
– operating assumption changes	19	**5**	**17**	**22**	**26**	**48**
Development costs		**(21)**	**–**	**(21)**	**(1)**	**(22)**
Contribution from shareholder net worth[2]		**146**	**12**	**158**	**7**	**165**
Operating profit		**874**	**156**	**1,030**	**151**	**1,181**
Variation from longer term investment return[3]		**387**	**(21)**	**366**	**13**	**379**
Effect of economic assumption changes		**(5)**	**7**	**2**	**–**	**2**
Corporate restructure		**(216)**	**–**	**(216)**	**–**	**(216)**
Profit from continuing operations before tax		**1,040**	**142**	**1,182**	**164**	**1,346**
Tax[2]		**(337)**	**(45)**	**(382)**	**(49)**	**(431)**
Tax impact of corporate restructure		**322**	**–**	**322**	**–**	**322**
Profit from continuing operations after tax		**1,025**	**97**	**1,122**	**115**	**1,237**

For the year ended 31 December 2005	Notes	UK £m	International £m	Life and pensions total £m	Investment management[1] £m	Total £m
Contribution from new business after cost of capital		306	25	331	49	380
Contribution from in-force business:						
– expected return		294	62	356	21	377
– experience variances	18	89	–	89	25	114
– operating assumption changes	19	(14)	(5)	(19)	14	(5)
Development costs		(20)	–	(20)	(1)	(21)
Contribution from shareholder net worth[2]		146	18	164	6	170
Operating profit		801	100	901	114	1,015
Variation from longer term investment return[3]		653	53	706	35	741
Effect of economic assumption changes		3	5	8	–	8
Profit from continuing operations before tax		1,457	158	1,615	149	1,764
Tax		(421)	(51)	(472)	(45)	(517)
Effect of UK tax changes		(276)	–	(276)	–	(276)
Profit from continuing operations after tax		760	107	867	104	971

1. For covered business, Investment management comprises managed pension funds and is included in the total Investment management result of £181m (2005: £136m). See Note 22.
2. In 2006, the contribution from shareholder net worth has been grossed up using a notional attributed tax rate of 30%. The 2006 impact of changing the notional attributed tax rate on the shareholder net worth to 30% is to increase operating profit by £12m and decrease profit before tax, and tax, by £3m. The contribution from shareholder net worth in 2005 has not been restated for this change in estimation technique. If the notional attributed tax rate had been 30% in 2005, the impact would have been to increase operating profit by £14m and profit before tax, and tax, by £23m.
3. UK life and pensions variation from longer term investment return comprises £185m (2005: £357m) relating to the value of in-force business and £202m (2005: £296m) relating to shareholder net worth.

17. LIFE AND PENSIONS OPERATING PROFIT

	2006 £m	2005 £m
UK	**874**	801
USA	**89**	24
Netherlands	**45**	43
France	**22**	33
	1,030	901

18. ANALYSIS OF EXPERIENCE VARIANCES

For the year ended 31 December 2006	UK £m	International £m	Life and pensions total £m	Investment management £m	Total £m
Persistency	**(15)**	**2**	**(13)**	**12**	**(1)**
Mortality/morbidity	**10**	**(9)**	**1**	**–**	**1**
Expenses	**2**	**–**	**2**	**–**	**2**
Other	**44**	**26**	**70**	**22**	**92**
	41	**19**	**60**	**34**	**94**

2006 UK other experience variances of £44m principally comprise the impact of the release of prudent margins as more data is loaded onto the Bulk Purchase Annuity (BPA) administration system (£33m) and opening adjustments (£34m) primarily to reflect a revision of assessments of prior and future tax. These opening adjustments had a broadly neutral effect on the embedded value, with the positive variance here being offset by a negative variance in the contribution from shareholder net worth. This is partially offset by differences between actual and modelled tax and an increase in deferred tax provisions (-£21m).

2006 International other experience variances relates primarily to the impact of Triple X financing.

2006 Investment management other experience variances of £22m includes the effect of higher average fee rates than assumed (£17m).

For the year ended 31 December 2005	UK £m	International £m	Life and pensions total £m	Investment management £m	Total £m
Persistency	2	2	4	15	19
Mortality/morbidity	14	(7)	7	–	7
Expenses	(6)	1	(5)	2	(3)
Other	79	4	83	8	91
	89	–	89	25	114

2005 UK other experience variances of £79m principally comprise the impact of the release of prudent margins as more data is loaded onto the BPA administration system (£73m).

2005 Investment management other experience variances of £8m include the effect of higher average fee rates than assumed.

19. ANALYSIS OF OPERATING ASSUMPTION CHANGES

For the year ended 31 December 2006	UK £m	International £m	Life and pensions total £m	Investment management £m	Total £m
Persistency	**(12)**	**21**	**9**	**–**	**9**
Mortality/morbidity	**(5)**	**(7)**	**(12)**	**–**	**(12)**
Expenses	**(80)**	**4**	**(76)**	**(1)**	**(77)**
Other	**102**	**(1)**	**101**	**27**	**128**
	5	**17**	**22**	**26**	**48**

2006 UK expenses of -£80m relates to an assumed increase in future expenses in relation to the management of existing protection policies (-£33m) and an anticipated rise in investment management costs (-£40m). The latter relates to the move to new City premises in 2007 and the development of our structured solutions and US based fixed income teams.

2006 UK other operating assumption changes of £102m primarily relate to the impact of PS06/14 on realistic protection reserving after the recapture of financial reinsurance (£64m) and changes to annuity investment policy (£19m), together with a reassessment of future reserve releases as data is loaded onto the BPA administration system (£23m).

2006 Investment management other operating assumption changes of £27m arise from the continuation of the ten year lapse assumption for all contracts through the extension of the modelling period (£15m) coupled with higher fee and income assumptions (£12m).

For the year ended 31 December 2005	UK £m	International £m	Life and pensions total £m	Investment management £m	Total £m
Persistency	30	(12)	18	–	18
Mortality/morbidity	11	(11)	–	–	–
Expenses	(24)	4	(20)	–	(20)
Other	(31)	14	(17)	14	(3)
	(14)	(5)	(19)	14	(5)

2005 UK other operating assumption changes of -£31m relate mainly to -£24m of reserve strengthening in respect of endowment compensation.

2005 Investment management other operating assumption changes of £14m arise from the continuation of the ten year lapse assumption for all contracts through the extension of the modelling period.

20. VARIATION FROM LONGER TERM INVESTMENT RETURN

	2006 £m	2005 £m
Total covered business	**379**	741
Investment management[1]	**(1)**	–
General insurance	**(7)**	8
Other operational income	**89**	121
	460	870

1. Non-covered Investment management business.

21. TIME VALUE OF OPTIONS AND GUARANTEES

	2006 £m	2005 £m
Life and pensions		
UK non profit	**4**	21
UK with-profits	**2**	2
International	**12**	5
	18	28

For UK non profit, the reduction in 2006 is primarily due to the purchase of negative inflation hedges coupled with higher inflation expectations resulting in a reduction in inflation guarantees.

For International, the increase in 2006 arises primarily from the rise in US interest rates on universal life contracts which have a guaranteed minimum crediting rate and a guaranteed surrender value.

22. INVESTMENT MANAGEMENT INCOME STATEMENT

	2006 £m	2005 £m
From continuing operations		
Managed pension funds	**151**	114
Ventures	**4**	4
Property	**6**	4
Retail investments	**11**	7
Other external income	**6**	5
Other income[1]	**3**	2
Operating profit from investment management	**181**	136
Variation from longer term investment return	**13**	35
Profit on ordinary activities before tax	**194**	171
Tax	**(58)**	(52)
Profit on ordinary activities after tax	**136**	119

Investment management comprises the managed pensions fund business on an EEV basis and other investment management business on an IFRS basis.

1. Other income excludes the element relating to managed pension funds on the IFRS basis.

23. OTHER OPERATIONAL INCOME

	2006 £m	2005 £m
Shareholders' other income		
Investment return on ordinary shareholders' equity[1]	**134**	127
Interest expense	**(106)**	(75)
	28	52
Other operations[2]	**(2)**	(5)
Unallocated corporate and development expenses	**(13)**	(6)
	13	41

1. Investment return on ordinary shareholders' equity exclude the element relating to LGP on the IFRS basis.
2. Principally the Regulated mortgage network and Cofunds.

24. ANALYSIS OF TAX

	Profit/(loss) before tax 2006 £m	**Tax (charge)/ credit 2006 £m**	Profit before tax 2005 £m	Tax charge 2005 £m
From continuing operations				
UK life and pensions	**874**	**(262)**	801	(230)
International life and pensions	**156**	**(51)**	100	(33)
	1,030	**(313)**	901	(263)
Investment management	**181**	**(54)**	136	(42)
General insurance	**9**	**(2)**	14	(4)
Other operational income	**13**	**8**	41	(5)
Operating profit	**1,233**	**(361)**	1,092	(314)
Variation from longer term investment return	**460**	**(128)**	870	(246)
Effect of economic assumption changes	**2**	**2**	8	(3)
Property income attributable to minority interests	**67**	**–**	81	–
Corporate restructure	**(216)**	**65**	–	–
Profit from continuing operations before tax/Tax	**1,546**	**(422)**	2,051	(563)

25. TAX IMPACT OF CORPORATE RESTRUCTURE/EFFECT OF UK TAX CHANGES

The tax benefit from the corporate restructure arose primarily from the reversal of the effect of the UK tax changes reported in 2005.

The tax charge in 2005 represented a one-off reduction in the embedded value arising from a change in tax law, which revised the way in which investment return was apportioned between categories of businesses for the purposes of computing taxable profits earned from writing pensions business.

26. EARNINGS PER SHARE

(a) Earnings per share

	Profit/(loss) before tax 2006 £m	Tax (charge)/ credit 2006 £m	Profit/(loss) after tax 2006 £m	Per share 2006 p	Profit before tax 2005 £m	Tax (charge)/ credit 2005 £m	Profit/(loss) after tax 2005 £m	Per share 2005 p
Operating profit from continuing operations	**1,233**	**(361)**	**872**	**13.45**	1,092	(314)	778	12.02
Variation from longer term investment return	**460**	**(128)**	**332**	**5.12**	870	(246)	624	9.64
Effect of economic assumption changes	**2**	**2**	**4**	**0.06**	8	(3)	5	0.08
Profit from discontinued operations	**–**	**–**	**–**	**–**	12	1	13	0.20
Corporate restructure	**(216)**	**65**	**(151)**	**(2.33)**	–	–	–	–
Tax impact of corporate restructure	**–**	**322**	**322**	**4.97**	–	–	–	–
Effect of UK tax changes	**–**	**–**	**–**	**–**	–	(276)	(276)	(4.27)
Distributions on subordinated borrowings designated as equity			**–**	**–**			(16)	(0.25)
Earnings per share based on profit attributable to equity holders	**1,479**	**(100)**	**1,379**	**21.27**	1,982	(838)	1,128	17.42

(b) Diluted earnings per share

(i) Based on operating profit from continuing operations after tax

	Profit after tax 2006 £m	Number of shares[1] 2006 m	Per share 2006 p	Profit after tax 2005 £m	Number of shares[1] 2005 m	Per share 2005 p
Operating profit from continuing operations after tax	**872**	**6,483**	**13.45**	778	6,474	12.02
Net shares under options allocable for no further consideration	**–**	**46**	**(0.09)**	–	38	(0.07)
Convertible bonds outstanding	**–**	**–**	**–**	20	285	(0.21)
Diluted earnings per share	**872**	**6,529**	**13.36**	798	6,797	11.74

(ii) Based on profit attributable to ordinary equity holders of the Company

	Profit after tax 2006 £m	Number of shares[1] 2006 m	Per share 2006 p	Profit after tax 2005 £m	Number of shares[1] 2005 m	Per share 2005 p
Profit attributable to ordinary equity holders of the Company	**1,379**	**6,483**	**21.27**	1,128	6,474	17.42
Net shares under options allocable for no further consideration	**–**	**46**	**(0.15)**	–	38	(0.09)
Convertible bonds outstanding	**–**	**–**	**–**	20	285	(0.44)
Diluted earnings per share	**1,379**	**6,529**	**21.12**	1,148	6,797	16.89

The number of shares in issue at 31 December 2006 was 6,532,261,961 (2005: 6,507,421,932).

1. Weighted average number of shares.

27. EMBEDDED VALUE RECONCILIATION

As at 31 December 2006	Notes	UK value of in-force £m	UK shareholder net worth[1] £m	UK life and pensions £m	International life and pensions £m	Life and pensions total £m	Investment management[2] £m	Total £m
At 1 January								
Value of in-force business (VIF)		3,142	–	3,142	570	3,712	238	3,950
Shareholder net worth (SNW)		–	1,762	1,762	298	2,060	184	2,244
		3,142	1,762	4,904	868	5,772	422	6,194
Exchange rate movements		–	–	–	(78)	(78)	–	(78)
		3,142	1,762	4,904	790	5,694	422	6,116
Profit for the period:								
– New business contribution		485	(219)	266				
– Expected return on VIF		226	–	226				
– Expected return – transfer to SNW		(293)	293	–				
– Experience variances		(160)	161	1				
– Operating assumption changes		(284)	286	2				
– Development costs		–	(14)	(14)				
– Expected return on SNW		–	112	112				
– Investment variances		(56)	320	264				
– Economic assumptions changes		(5)	2	(3)				
– Corporate restructure		(561)	410	(151)				
– Tax impact of corporate restructure		–	322	322				
Profit for the period[3]		(648)	1,673	1,025	97	1,122	115	1,237
Capital movements[4]		–	698	698	31	729	–	729
Distributions relating to:								
– Non profit			(110)	(110)				
– With-profits		(66)		(66)				
– Shareholder net worth			(162)	(162)				
– Subordinated debt			(24)	(24)				
Distributions		(66)	(296)	(362)	(5)	(367)	(62)	(429)
Movement in pension deficit		–	(9)	(9)	–	(9)	–	(9)
Embedded value	28/29	2,428	3,828	6,256	913	7,169	475	7,644
Represented by:								
– Non profit		1,643		1,643				
– With-profits		785		785				
Value of in-force business		2,428	–	2,428	652	3,080	281	3,361
Shareholder net worth		–	3,828	3,828	261	4,089	194	4,283

1. UK shareholder net worth (SNW) represents the amounts in the Society LTF and LGP shareholder capital which are regarded as either required capital or free surplus held within the covered business.
2. For covered business, Investment management comprises managed pension funds and is included in the total Investment management shareholders' equity of £592m.
3. Included in the profit for the period is an inter-fund transfer from non profit (included in VIF) to SRC (included in SNW) of £1,222m.
4. Capital movements comprise £300m equity capital, £600m capital contribution and £400m of intra-group subordinated debt attributed to LGP, less the repayment of £602m of intra-group subordinated debt previously attributed to the SRC.

27. EMBEDDED VALUE RECONCILIATION continued

As at 31 December 2005	Notes	UK value of in-force £m	UK shareholder net worth £m	UK life and pensions £m	International life and pensions £m	Life and pensions total £m	Investment management[1] £m	Total £m
At 1 January								
Value of in-force business (VIF)		2,885	–	2,885	431	3,316	191	3,507
Shareholder net worth (SNW)		–	1,560	1,560	276	1,836	162	1,998
		2,885	1,560	4,445	707	5,152	353	5,505
Exchange rate movements		–	–	–	51	51	–	51
		2,885	1,560	4,445	758	5,203	353	5,556
Profit for the period:								
– New business contribution		447	(232)	215				
– Expected return on VIF		206	–	206				
– Expected return – transfer to SNW		(340)	340	–				
– Experience variances		(151)	145	(6)				
– Operating assumption changes		14	(23)	(9)				
– Development costs		–	(14)	(14)				
– Expected return on SNW		–	96	96				
– Investment variances		250	296	546				
– Economic assumptions changes		2	–	2				
– Effect of UK tax changes		(125)	(151)	(276)				
Profit for the period[2]		303	457	760	107	867	104	971
Capital movements		–	–	–	5	5	–	5
Distributions relating to:								
– Non profit			(119)	(119)				
– With-profits		(46)		(46)				
– Shareholder net worth			(100)	(100)				
– Subordinated debt			(26)	(26)				
Distributions		(46)	(245)	(291)	(2)	(293)	(35)	(328)
Movement in pension deficit		–	(10)	(10)	–	(10)	–	(10)
Embedded value	28/29	3,142	1,762	4,904	868	5,772	422	6,194
Represented by:								
– Non profit		2,387		2,387				
– With-profits		755		755				
Value of in-force business		3,142	–	3,142	570	3,712	238	3,950
Shareholder net worth		–	1,762	1,762	298	2,060	184	2,244

1. For covered business, Investment management comprises managed pension funds and is included in the total Investment management shareholders' equity of £506m.
2. Included in the profit for the period is an inter-fund transfer from non profit (included in VIF) to SRC (included in SNW) of £282m.

28. ANALYSIS OF ORDINARY SHAREHOLDERS' EQUITY

As at 31 December 2006	UK £m	International £m	Life and pensions total £m	Investment management[1] £m	Other operations[2] £m	Total £m
Analysed as:						
IFRS basis ordinary shareholders' equity	**4,213**	**731**	**4,944**	**194**	**287**	**5,425**
Additional retained profit on an EEV basis	**2,043**	**182**	**2,225**	**281**	**–**	**2,506**
Ordinary shareholders' equity on an EEV basis	**6,256**	**913**	**7,169**	**475**	**287**	**7,931**
Comprising:						
Shareholder net worth						
– Free surplus	**652**	**110**	**762**	**176**		
– Required capital to cover solvency margin	**1,362**	**151**	**1,513**	**18**		
– Other required capital	**1,814**	**–**	**1,814**	**–**		
Value of in-force						
– Value of in-force business	**2,572**	**703**	**3,275**	**286**		
– Cost of capital	**(144)**	**(51)**	**(195)**	**(5)**		

As at 31 December 2005	UK £m	International £m	Life and pensions total £m	Investment management[1] £m	Other operations[2] £m	Total £m
Analysed as:						
IFRS basis ordinary shareholders' equity	2,560	737	3,297	184	776	4,257
Additional retained profit on an EEV basis	2,344	131	2,475	238	–	2,713
Ordinary shareholders' equity on an EEV basis	4,904	868	5,772	422	776	6,970
Comprising:						
Shareholder net worth						
– Free surplus	–	148	148	166		
– Required capital to cover solvency margin	689	150	839	18		
– Other required capital	1,073	–	1,073	–		
Value of in-force						
– Value of in-force business	3,148	618	3,766	243		
– Cost of capital	(6)	(48)	(54)	(5)		

Free surplus is the market value of any capital and surplus allocated to, but not required to support, the in-force covered business at the valuation date.

Total required capital includes any amount of assets attributed to the covered business, over and above that required to back liabilities, the distribution of which to shareholders is restricted.

1. Investment management comprises managed pension funds and is included in the total Investment management shareholders' equity of £592m (2005: £506m).
2. Other Investment management businesses included on an IFRS basis of £117m (2005: £84m) are included in other operations.

29. SEGMENTAL ANALYSIS OF ORDINARY SHAREHOLDERS' EQUITY

	Covered business EEV basis 2006 £m	Other business IFRS basis 2006 £m	Total 2006 £m	Covered business EEV basis 2005 £m	Other business IFRS basis 2005 £m	Total 2005 £m
UK[1]	**6,256**	**–**	**6,256**	4,904	–	4,904
Society shareholder capital[2]	**–**	**1,307**	**1,307**	–	1,896	1,896
	6,256	**1,307**	**7,563**	4,904	1,896	6,800
Embedded value of international life and pensions business						
– USA	**552**	**–**	**552**	566	–	566
– Netherlands	**228**	**–**	**228**	192	–	192
– France	**133**	**–**	**133**	110	–	110
	7,169	**1,307**	**8,476**	5,772	1,896	7,668
Investment management	**475**	**117**	**592**	422	84	506
	7,644	**1,424**	**9,068**	6,194	1,980	8,174
General insurance	**–**	**169**	**169**	–	167	167
Corporate funds[3]	**–**	**(1,306)**	**(1,306)**	–	(1,371)	(1,371)
	7,644	**287**	**7,931**	6,194	776	6,970

Further analysis of the covered business is included in Note 27.

	2006 £m	2005 £m
Movement		
At 1 January	**6,970**	6,186
Total recognised income and expense	**1,337**	1,133
Issue of ordinary share capital	**15**	1
Net movements in employee share schemes and treasury shares	**(5)**	7
Dividend distributions to ordinary equity holders of the Company during the year	**(349)**	(331)
Distributions during the year on subordinated borrowings designated as equity	**–**	(16)
Other reserve movements including pension deficit	**(9)**	(10)
Fair value loss after tax on reclassification of subordinated borrowings as debt	**(28)**	–
At 31 December	**7,931**	6,970

1. 2005 included £602m of intra-group subordinated debt capital attributed to the SRC, which was repaid in 2006. An equivalent amount (£602m) was then lent to Society shareholder capital on a subordinated basis, £400m of this was lent to LGP on similar terms.
2. Represents surplus capital held outside Society's LTF, including the rights issue proceeds, but excluding LGP shareholder capital which is regarded as either required capital or free surplus held within the covered business.
3. Includes the convertible debt of £nil (2005: £509m), subordinated borrowings of £818m (2005: £809m) and senior debt of £602m which has been lent to Society shareholder capital on a subordinated basis (2005: £602m lent to the SRC on a subordinated basis).

30. RECONCILIATION OF SHAREHOLDER NET WORTH (SNW)

	UK life and pensions 2006 £m	Total 2006 £m	UK life and pensions 2005 £m	Total 2005 £m
SNW of long term operations (IFRS basis)	**3,263**	**5,138**	2,560	3,481
Other assets (IFRS basis)	**950**	**287**	–	776
Ordinary shareholders' equity on the IFRS basis	**4,213**	**5,425**	2,560	4,257
Purchased interests in long term business	**(7)**	**(25)**	(10)	(25)
Sub-fund	**313**	**313**	287	287
Deferred acquisition costs/deferred income liabilities	**(115)**	**(677)**	(216)	(790)
Deferred tax[1]	**(693)**	**(520)**	(810)	(646)
Other[2]	**117**	**54**	(49)	(63)
Shareholder net worth on the EEV basis	**3,828**	**4,570**	1,762	3,020
Represented by:				
SNW of long term operations (EEV basis)	**2,878**	**4,283**	1,762	2,244
LGP shareholder capital (EEV basis)	**950**	**–**	–	–
Other assets (IFRS basis)	**–**	**287**	–	776
	3,828	**4,570**	1,762	3,020

1. Deferred tax represents all tax which is expected to be paid under current legislation, including tax which would arise if shareholders' assets were distributed.
2. Other relates primarily to the different treatment of sterling reserves, other long term reserves and the non profit result of LGP under EEV compared with IFRS.

31. SENSITIVITIES

In accordance with the guidance issued by the CFO Forum in October 2005 the table below shows the effect of alternative assumptions on the long term embedded value and new business contribution.

Effect on embedded value at 31 December 2006

	As published £m	1% lower risk discount rate £m	1% higher risk discount rate £m	1% lower interest rate £m	1% higher equity/ property yields £m	10% lower equity/ property values £m
Life and pensions						
– UK	6,256	431	(376)	138	275	(290)
– International	913	61	(54)	(8)	5	(6)
Total life and pensions	7,169	492	(430)	130	280	(296)
Investment management	475	12	(11)	(3)	9	(18)
Total covered business	7,644	504	(441)	127	289	(314)

	As published £m	10% lower maintenance expenses £m	10% lower lapse rates £m	5% lower mortality (UK annuities) £m	5% lower mortality (other business) £m
Life and pensions					
– UK	6,256	59	71	(104)	33
– International	913	10	34	n/a	67
Total life and pensions	7,169	69	105	(104)	100
Investment management	475	15	17	n/a	n/a
Total covered business	7,644	84	122	(104)	100

Effect on new business contribution for the year

	As published £m	1% lower risk discount rate £m	1% higher risk discount rate £m	1% lower interest rate £m	1% higher equity/ property yields £m	10% lower equity/ property values £m
Life and pensions						
– UK	380	74	(65)	10	37	(32)
– International	38	16	(14)	(3)	1	–
Total life and pensions	418	90	(79)	7	38	(32)
Investment management	61	3	(3)	(1)	1	–
Total covered business	479	93	(82)	6	39	(32)

	As published £m	10% lower maintenance expenses £m	10% lower lapse rates £m	5% lower mortality (UK annuities) £m	5% lower mortality (other business) £m
Life and pensions					
– UK	380	15	26	(11)	9
– International	38	2	6	n/a	10
Total life and pensions	418	17	32	(11)	19
Investment management	61	–	3	n/a	n/a
Total covered business	479	17	35	(11)	19

Opposite sensitivities are broadly symmetrical.

32. ASSUMPTIONS

UK assumptions

i. The assumed future pre-tax returns on fixed interest and RPI linked securities are set by reference to redemption yields available in the market at the end of the reporting period. The corresponding return on equities and property is equal to the fixed interest gilt assumption plus the appropriate risk premium. An asset mix consistent with the current investment policy and future management intentions has been assumed within the projections. The economic assumptions were:

	2006 % pa	2005 % pa
Equity risk premium	**3.0**	3.0
Property risk premium	**2.0**	2.0
Investment return		
– Gilts:		
– Fixed interest	**4.6**	4.1
– RPI linked	**4.7**	4.2
– Non gilts:		
– Fixed interest	**4.9 – 5.3**	4.4 – 4.8
– RPI linked	**4.6 – 5.1**	4.2 – 4.6
– Equities	**7.6**	7.1
– Property	**6.6**	6.1
Risk margin	**3.0**	3.0
Risk discount rate (net of tax)	**7.6**	7.1
Inflation		
– Expenses/earnings	**4.2**	3.9
– Indexation	**3.2**	2.9

The assumed returns on non gilt securities are net of an allowance for default risk of 0.2% pa (2005: 0.2% pa), other than for certain government supported securities where no such allowance is made.

UK life and pensions

ii. The value of the Sub-fund is the discounted value of total projected investment returns over its lifetime.

iii. Assets are valued at market value. For the projection of fixed interest and RPI linked investment returns, asset values are adjusted to reflect the assumed interest and inflation rates.

iv. Future bonus rates have been set at levels which would fully utilise the assets supporting the policyholders' portion of the with-profits business. The proportion of profits derived from with-profits business allocated to shareholders has been assumed to be 10% throughout.

v. The value of in-force business reflects the cost of providing for benefit enhancement or compensation in relation to certain products including administration expenses.

vi. Other actuarial assumptions have been set at levels commensurate with recent operating experience, including those for mortality, morbidity, persistency and maintenance expenses (excluding the development costs referred to below). These are reviewed annually. An allowance is made for future improvements in annuitant mortality based on experience and externally published data. Male annuitant mortality is assumed to improve in accordance with CMI Working Paper 1, projection MC for future experience with a minimum annual improvement of 0.6%, and the average of projections MC and LC for statutory reserving with a minimum annual improvement of 0.8%. Female annuitant mortality is assumed to improve in accordance with the MC projection from CMI Working Paper 1 for statutory reserving and at 70% of this rate for future experience, with the same underpinning minima as for males.

vii. The subordinated debt capital was repaid in 2006 but was included in the embedded value in 2005 at the face value of £602m (estimated market value of £699m at 31 December 2005). If the market value of the subordinated debt capital was used, total embedded value in 2005 would increase by £31m. £400m of subordinated debt attributed to LGP in 2006 has been included at face value. The estimated market value was not materially different to the face value.

viii. Development costs relate to strategic systems.

UK managed pension funds

ix. All contracts are assumed to lapse over a 10 year period. Fees are projected on a basis which reflects current charges or, if less, anticipated charges. New business consists of monies received from new clients and incremental receipts from existing clients, and excludes the roll-up of the investment returns. Development costs relate to strategic systems.

International

x. Key assumptions are:

	2006 % pa	2005 % pa
USA		
Reinvestment rate	**5.4**	5.1
Risk margin	**3.0**	3.0
Risk discount rate (net of tax)	**7.8**	7.4
Europe		
Government bond return	**4.0**	3.3
Risk margin	**3.0**	3.0
Risk discount rate (net of tax)	**7.0**	6.3

xi. Other actuarial assumptions have been set at levels commensurate with recent operating experience, including those for mortality, morbidity, persistency and maintenance expenses.

Tax

xii. EEV results are computed on an after tax basis and are grossed up by notional attributed tax for presentation in the income statement. The tax rate used for grossing up is the corporate tax rate in the territory concerned, which for the UK was 30% (2005: 30%).

To the Directors of Legal & General Group Plc on the Supplementary Financial Statements

We have audited the supplementary financial statements for the year ended 31 December 2006 that comprise the Consolidated Income Statement – European Embedded Value basis, Consolidated Balance Sheet – European Embedded Value basis and the Consolidated Statement of Recognised Income and Expense – European Embedded Value basis on pages 117 and 118 and the relevant Notes 1 to 32 ('the supplementary financial statements') which have been prepared in accordance with the European Embedded Value ('EEV') basis set out in Notes 1 to 13 and which should be read in conjunction with the Group's financial statements which are on pages 55 to 116.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the supplementary financial statements on the EEV basis in accordance with the EEV basis set out in Notes 1 to 13. Our responsibilities, as independent auditors, in relation to the supplementary financial statements are, as set out in our letter of engagement agreed with you dated 5 December 2006, to report to you our opinion as to whether the supplementary financial statements have been properly prepared, in all material respects, in accordance with the EEV basis. We also report to you if we have not received all the information and explanations we require for our audit of the supplementary financial statements. This report, including the opinion, has been prepared for and only for the Company's directors as a body in accordance with our letter of engagement dated 5 December 2006, and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or in to whose hands it may come save where expressly agreed by our prior consent in writing.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. Our audit included examination, on a test basis, of evidence relevant to the amounts and disclosures in the supplementary financial statements. This evidence included an assessment of the significant estimates and judgements made by the directors in the preparation of the supplementary financial statements, and of whether the accounting policies are appropriate to the Legal & General Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the supplementary financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the supplementary financial statements.

Opinion

In our opinion, the supplementary financial statements for the year ended 31 December 2006 have been properly prepared in all material respects in accordance with the EEV basis set out in Notes 1 to 13.

PricewaterhouseCoopers LLP
Chartered Accountants
London
13 March 2007

(a) The supplementary financial statements are published on the website of Legal & General Group Plc, www.legalandgeneralgroup.com. The maintenance and integrity of the Legal & General Group Plc website is the responsibility of the directors; the audit work does not involve consideration of these matters and, accordingly, we accept no responsibility for any changes that may have occurred to the supplementary financial statements since they were initially presented on the website.
(b) Legislation in the United Kingdom governing the preparation and dissemination of supplementary financial statements may differ from legislation in other jurisdictions.

To the Members of Legal & General Group Plc

We have audited the parent company financial statements of Legal & General Group Plc for the year ended 31 December 2006 which comprise the Balance Sheet, the Statement of Total Recognised Gains and Losses, the Reconciliation of Movement in Total Equity and the related notes. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Group financial statements of Legal & General Group Plc for the year ended 31 December 2006.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the parent company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the parent company financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the parent company financial statements. The information given in the Directors' Report includes that specific information presented in the Operating and Financial Review that is cross-referred from the Business Review section of the Directors' Report.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the Directors' Report, the unaudited part of the Directors' Remuneration Report, the Chairman's Statement, the Chief Executive's Statement, the Operating and Financial Review, the Report of the Audit Committee, the Report of the Nomination's Committee and the Corporate Governance Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

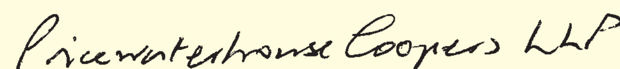
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent company financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the parent company financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the parent company financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the parent company financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 December 2006;
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the parent company financial statements.



PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
13 March 2007

(a) The financial statements are published on the website of Legal & General Group Plc, www.legalandgeneralgroup.com. The maintenance and integrity of the Legal & General Group Plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

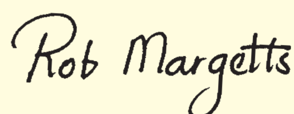
Company Balance Sheet

As at 31 December 2006

	Notes	2006 £m	2005 £m
Fixed assets			
Investments	8	**6,690**	5,594
Current assets			
Amounts owed by Group undertakings		**161**	119
Tax		**26**	18
Derivative assets	9	**22**	16
Other debtors		**–**	4
Creditors: amounts falling due within one year			
Amounts owed to Group undertakings		**(2)**	(2)
Other creditors and accruals	10	**(21)**	(19)
Convertible bond	11	**–**	(509)
Net current assets		**186**	(373)
Total assets less current liabilities		**6,876**	5,221
Creditors: amounts falling due after more than one year			
Dated subordinated borrowings	11	**(818)**	(415)
Amounts owed to Group undertakings		**(638)**	(160)
Shareholders' net assets		**5,420**	4,646
Representing capital and reserves			
Share capital	12	**163**	163
Share premium account	12	**923**	908
Subordinated borrowings designated as equity	11	**–**	394
Other reserves	13	**26**	26
Revaluation reserve	13	**3,431**	2,317
Profit and loss account	13	**877**	838
Total equity		**5,420**	4,646

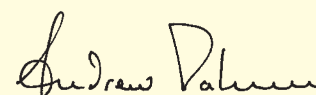
The notes on pages 138 to 143 form an integral part of these financial statements.

The financial statements on pages 136 to 143 were approved by the directors on 13 March 2007 and were signed on their behalf by:



Sir Rob Margetts
Chairman

Tim Breedon
Group Chief Executive



Andrew Palmer
Group Director (Finance)

Company Statement of Total Recognised Gains and Losses

For the year ended 31 December 2006

	2006 £m	2005 £m
Profit for the financial year	**414**	684
Gain on revaluation of investments in subsidiary undertakings	**1,114**	276
Prior year adjustment		2
Total recognised gains and losses relating to the year	**1,528**	962

Company Reconciliation of Movements in Total Equity

For the year ended 31 December 2006

	2006 £m	2005 £m
At 1 January	**4,646**	4,019
Total recognised gains and losses	**1,528**	960
Net movements in employee share schemes and treasury shares	**3**	13
Dividend distributions to ordinary equity holders of the Company during the year	**(349)**	(347)
Issue of ordinary share capital	**15**	1
Net change in hedging reserve	**(3)**	–
Transfer from share-based payments reserve	**2**	–
Reclassification of subordinated borrowings from equity to debt	**(394)**	–
Fair value loss after tax on reclassification of subordinated borrowings as debt	**(28)**	–
At 31 December	**5,420**	4,646

1. ACCOUNTING POLICIES

Basis of preparation

The Company's financial statements have been prepared under the historical cost convention, modified by the revaluation of certain assets, as required by the Companies Act 1985 and in accordance with applicable UK accounting standards.

The Company's financial statements have been prepared in compliance with Section 226 of, and Schedule 4 to, the Companies Act 1985 adopting the exemption of omitting the profit and loss account conferred by Section 230 of that Act.

In December 2005 the ASB issued an amendment to Financial Reporting Standard (FRS) 26 'Financial Instruments: Recognition and Measurement'. This amendment requires issued financial guarantees, other than those previously asserted by the entity to be insurance contracts, to be initially recognised at their fair value and subsequently measured at the higher of:

(a) the unamortised balance of the related fees received and deferred; and
(b) the expenditure required to settle the commitment at the balance sheet date.

The amendment is effective for accounting periods beginning on or after 1 January 2006 and has been adopted by the Company in the 2006 accounts.

Investment income

Investment income includes dividends and interest. Dividends receivable from Group companies are recognised in the period in which the dividends are declared and approved at the general meeting or paid. Interest income is recognised using the effective interest method.

Distributions

Dividend distribution to the Company's shareholders is recognised as a liability in the period in which the dividends are authorised and are no longer at the discretion of the Company. Final dividends are accrued when approved by the Company's shareholders at the general meeting and interim dividends are accrued when paid.

Interest expense

Interest expense reflects the underlying cost of borrowing, based on the effective interest method, and includes payments and receipts made under derivative instruments which are amortised over the interest period to which they relate.

Investment in subsidiary undertakings

Shares in subsidiary undertakings are stated at the Company's share of their net assets. Unrealised gains or losses arising on investments in subsidiary undertakings are taken to the revaluation reserve.

Loans and receivables

Loans and receivables are held at amortised cost using the effective interest rate method.

Derivative financial instruments and hedge accounting

The Company's activities expose it to the financial risks of changes in foreign exchange rates and interest rates. The Company uses derivatives, such as foreign exchange forward contracts and interest rate swap contracts, to hedge these exposures. The Company uses hedge accounting, provided the prescribed criteria are met, to recognise the offsetting effects of changes in the fair value or cash flow of the derivative instrument and the hedged item. The Company's principal use of hedge accounting is to hedge the fair value movements in loans due to interest rate and exchange rate fluctuations. Any gain or loss from remeasuring the hedging instrument at fair value is recognised immediately in the profit and loss account. Any gain or loss on the hedged item attributable to the hedged risk is adjusted against the carrying amount of the hedged item and recognised in the profit and loss account.

The relationship between the hedging instrument and the hedged item, together with the risk management objective and strategy for undertaking the hedge transaction, are documented at the inception of the transaction. The effectiveness of the hedge is documented and monitored on an ongoing basis. Hedge accounting is only applied for highly effective hedges (between 80% and 125% effectiveness) with any ineffective portion of the gain or loss recognised in the profit and loss account in the current period.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any such derivative instruments are recognised immediately in the profit and loss account.

Borrowings

Borrowings are recognised initially at fair value, net of transaction costs. Borrowings classified as liabilities are subsequently stated at amortised cost. The difference between the proceeds and the redemption value is recognised in the profit and loss account over the borrowing period using the effective interest method.

For a convertible bond which includes a cash settlement option in lieu of the issue of shares on conversion, the conversion option is separated and recognised as a derivative liability. The liability is revalued to fair value at each reporting period, with fair value gains and losses taken through the profit and loss account. The remainder of the proceeds, less attributable expenses, is allocated to the value of the debt portion of the convertible bond. This amount is recorded as a liability on an amortised cost basis, using the effective interest rate, until extinguished on conversion or on maturity of the bond.

Deferred tax

Deferred tax is recognised in respect of timing differences which have not reversed at the balance sheet date and which result in an obligation to pay more tax, or a right to pay less tax, at a future date. Deferred tax is measured at rates expected to apply when the timing differences reverse, based on current tax rates and law. Deferred tax assets are recognised to the extent that it is more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

Foreign currencies

Foreign currency transactions are translated into sterling, the Company's functional and presentational currency, using the exchange rate prevailing at the date of the transactions. Foreign exchange gains and losses are recognised in the profit and loss account.

Pension costs

The Company participates in multi-employer defined benefit schemes, within the meaning of FRS 17, 'Retirement Benefits', which, as its share of the underlying assets and liabilities cannot be identified, have been treated for reporting purposes as defined contribution schemes. In addition to these schemes the Company also contributes to defined contribution schemes. The Company charges the costs of its pension schemes against profit as incurred. Any difference between the cumulative amounts charged against profits and contribution amounts paid is included as a provision or prepayment in the balance sheet.

The assets of the defined benefit schemes are held in separate trustee administered funds, which have been subject to regular valuation every three years and updated by formal reviews at reporting dates by qualified actuaries who were employees of the Group.

Share-based payments

The Company operates a number of share based payment plans on behalf of its subsidiaries. The fair value of the equity instruments granted is spread over the vesting period of the instrument and

1. ACCOUNTING POLICIES continued

treated as a capital contribution to the respective subsidiary. The total capital contribution is determined by reference to the fair value of the awards, excluding the impact of any non-market vesting conditions.

At each balance sheet date, the Company revises its estimate of the number of equity instruments which are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the cost of the investment in the subsidiary and a corresponding adjustment is made to equity over the remaining vesting period. On vesting or exercise, the difference between the accumulated capital contribution and the actual cost to the Company is transferred to retained earnings. Where new shares are issued, the proceeds received are credited to share capital and share premium. Any capital contribution is subsequently recharged to the respective subsidiary as incurred and the corresponding cost of investment is reduced.

2. RISK MANAGEMENT

Management of risk

The Company, in the course of its business activities, is exposed to market, credit and liquidity risk. Overall responsibility for the management of these risks is vested in the Board. To support it in this role, a risk framework is in place comprising a structure of formal committees, risk assessment and reporting processes and risk review functions. The framework provides assurance that risks are being appropriately identified and managed and that an independent assessment of risks is being performed.

Risk assessment processes

A continuous process is in place formally identifying, evaluating and managing the significant risks to the achievement of the Company's objectives. A standard approach is used to assess risks.

Senior management and the risk review functions (see below) review the output of the assessments.

Risk review functions

The Company's risk review function provides an oversight of the risk management processes within the Company. Its responsibilities include the evaluation of changes in the business operating environment and business processes, the assessment of these changes on risks to business and the monitoring of the mitigating actions. The risk review function also ensures that risk committees are provided with meaningful risk reports and that there is appropriate information to assess risk issues.

Details of the categories of risk to the Company and high-level management processes are set out below. The Company has defined policies for the management of its key risks, the operation of which are supported by risk review functions and are independently confirmed by Group internal audit.

Market risk

Market risk is the risk arising from fluctuations in interest and exchange rates and market valuations.

Credit risk

Credit risk is the risk that the Company is exposed to loss if another party fails to perform its financial obligations to the Company.

Credit risk is not sought in its own right. Credit risk is managed through the setting and regular review of detailed counterparty credit and concentration limits. Compliance with these limits for investment and treasury transactions is monitored daily. The Group Credit Committee oversees these processes. Counterparties used for the provision of hedging derivatives have a minimum credit rating of A from Standard & Poor's. The Company's maximum exposure to credit risk on its financial assets at the balance sheet date is equal to the value of the derivative assets.

Liquidity risk

Liquidity 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 costs.

A degree of liquidity risk is implicit in the Company. Liquidity risk arises as a consequence of the uncertainty surrounding the value and timing of cash flows. The Company's treasury function manages liquidity to ensure that it maintains sufficient liquid assets and standby facilities to meet a prudent estimate of its net cash outflows over a period of two years.

3. DIVIDENDS AND OTHER DISTRIBUTIONS

	2006 Per share p	2005 Per share p	**2006 Total £m**	2005 Total £m
Ordinary share dividend paid in the year				
– Prior year final dividend	**3.63**	3.45	**236**	224
– Current year interim dividend	**1.74**	1.65	**113**	107
	5.37	5.10	**349**	331
Distributions paid on subordinated borrowings designated as equity			**–**	16
			349	347
Ordinary share dividend proposed[1]	**3.81**	3.63	**248**	236

1. The dividend proposed has not been included as a liability in the balance sheet.

4. DIRECTORS' EMOLUMENTS AND OTHER EMPLOYEE INFORMATION

Full disclosures of the Group Plc directors' emoluments are contained within those parts of the Directors' Report on Remuneration which are described as having been audited. At 31 December 2006 there were no loans outstanding with directors of the Company (2005: £nil). The Company has no other employees.

5. PENSIONS

The Company operates the following pension schemes in the UK. There were no contributions prepaid or outstanding at either 31 December 2006 or 31 December 2005 in respect of these schemes and the Company has no liability for retirement benefits.

- Legal & General Group UK Pension and Assurance Fund (the Fund). The Fund is a defined scheme which was closed to new members from January 1995; last full actuarial valuation as at 31 December 2004.
- Legal & General Group UK Senior Pension Scheme (the Scheme). The Scheme is a defined benefit scheme which, with a few exceptions (principally transfers from the Fund), was closed to new members from August 2000; last full actuarial valuation as at 31 December 2004.
- Legal & General Group Personal Pension Plan (UK) – a defined contribution scheme.
- Legal & General Staff Stakeholder Pension Scheme (UK) – a defined contribution scheme.

As the Fund and the Scheme are effectively closed to new members, under the projected unit method of valuation, the current service costs will increase as the age profile of active members rises.

In the UK, the Fund and the Scheme are multi-employer defined benefit schemes, which, as the Company's share of the underlying assets and liabilities cannot be identified, have been treated for reporting purposes as defined contribution schemes. There was a deficit in respect of these schemes for the year ended 31 December 2006 of £174m (2005: £211m) and the contributions in respect of them for the year were £39m (2005: £31m). Further information is given in Note 40 of the consolidated IFRS financial statements of the Group.

6. SHARE-BASED PAYMENTS

The Company grants share-based payments to employees of the Legal & General Group. Full disclosure of these awards is given in Note 17 in the consolidated Group IFRS financial statements. The total expense for the year relating to share awards was £15m (2005: £13m) of which £nil (2005: £nil) was retained by the Company.

7. AUDITORS' REMUNERATION

Remuneration receivable by the Company's auditor for the audit of the Company's financial statements is not presented. The Group consolidated financial statements disclose the aggregate remuneration receivable by the Company's auditor for the audit of the annual accounts of the Group, which include the Company's financial statements.

The disclosure of fees payable to the auditor and its associates for other (non-audit) services has not been made because the Group's consolidated financial statements are required to disclose such fees on a consolidated basis.

8. INVESTMENTS

	Shares in Group companies 2006 £m	**Loans to Group companies 2006 £m**	**Total 2006 £m**	Shares in Group companies 2005 £m	Loans to Group companies 2005 £m	Total 2005 £m
At valuation, 1 January	**4,290**	**1,304**	**5,594**	3,995	1,264	5,259
Additions	**4**	**624**	**628**	19	5	24
Repayment	**–**	**(606)**	**(606)**	–	–	–
Revaluation	**1,114**	**(40)**	**1,074**	276	35	311
At valuation, 31 December	**5,408**	**1,282**	**6,690**	4,290	1,304	5,594
At cost, 31 December	**2,011**	**1,364**	**3,375**	2,007	1,345	3,352

9. DERIVATIVE ASSETS AND LIABILITIES

	Contract/ notional amount 2006 £m	Fair values Assets 2006 £m	Fair values Liabilities[1] 2006 £m
Convertible debt derivative liability	**–**	**–**	**–**
Interest rate contracts – held for trading	**400**	**17**	**–**
Interest rate contracts – fair value hedges	**405**	**–**	**17**
Forward foreign exchange contracts – held for trading	**851**	**5**	**2**
Derivative assets and liabilities		**22**	**19**

	Contract/ notional amount 2005 £m	Fair values Assets 2005 £m	Fair values Liabilities[1] 2005 £m
Convertible debt derivative liability	525	–	3
Interest rate contracts – held for trading	430	–	3
Interest rate contracts – fair value hedges	411	4	–
Forward foreign exchange contracts – held for trading	727	12	3
Derivative assets and liabilities		16	9

1. Derivative liabilities are reported in the balance sheet within other creditors and accruals.

The descriptions of each type of derivative are given in Notes 21 and 51 of the consolidated Group IFRS financial statements.

10. OTHER CREDITORS AND ACCRUALS

	2006 £m	2005 £m
Derivative liabilities (Note 9)	**19**	9
Other creditors	**2**	6
Deferred tax	**–**	4
Other creditors and accruals	**21**	19

11. BORROWINGS

(i) Analysis by nature

	Carrying amount 2006 £m	Coupon rate 2006 %	Fair value 2006 £m	Carrying amount 2005 £m	Coupon rate 2005 %	Fair value 2005 £m
Subordinated borrowings designated as equity						
5.875% sterling undated subordinated notes	**–**	**–**	**–**	394	5.88	434
Subordinated borrowings						
5.875% sterling undated subordinated notes	**429**	**5.88**	**411**	–	–	–
4.0% Euro subordinated notes 2025	**389**	**4.00**	**397**	415	4.00	424
Convertible bond						
2.75% sterling convertible bond 2006	**–**	**–**	**–**	509	2.75	521
Total borrowings	**818**		**808**	1,318		1,379

£65m of interest expense was incurred during the period (2005: £38m).

Coupon payments on both subordinated issues may be deferred if no dividend is paid on the Group's ordinary shares. The sterling undated subordinated notes are treated as upper tier II capital for regulatory purposes and the Euro dated subordinated notes as lower tier II capital.

The Company has issued £400m of 5.875% undated subordinated notes. These notes are callable on 1 April 2019 and every five years thereafter. If not called, the coupon from 1 April 2019 will be reset to the prevailing five year benchmark gilt yield plus 2.33% pa. As at 31 December 2005, the undated subordinated notes were classified as equity because their perpetual nature meant that in certain circumstances interest could be deferred indefinitely. On 13 March 2006, the Group entered into a supplementary deed to remove the discretionary nature of the interest. This had the effect of reclassifying the notes from equity to liability and coupon payments from distributions to interest. Upon reclassification the new debt component was recognised at fair value.

The Company has also issued €600m of 4.0% Euro dated subordinated notes. The proceeds were swapped into sterling. The notes are callable on 8 June 2015 and each year thereafter. If not called, the coupon from 8 June 2015 will reset to a floating rate of interest based on prevailing three month Euribor plus 1.7% pa.

11. BORROWINGS continued

(ii) Analysis by maturity

As at 31 December 2006	Effective interest rate %	Carrying amount £m	Maturity Within 1 year £m	15-25 years £m	Over 25 years £m
Subordinated borrowings designated as equity					
5.875% sterling undated subordinated notes	–	–	–	–	–
Subordinated borrowings					
5.875% sterling undated subordinated notes	5.23	429	–	–	429
4.0% Euro subordinated notes 2025	4.12	389	–	389	–
Convertible bond					
2.75% sterling convertible bond 2006	–	–	–	–	–
Total borrowings		818	–	389	429

As at 31 December 2005	Effective interest rate %	Carrying amount £m	Maturity Within 1 year £m	15-25 years £m	Over 25 years £m
Subordinated borrowings designated as equity					
5.875% sterling undated subordinated notes	6.03	394	–	–	394
Subordinated borrowings					
5.875% sterling undated subordinated notes	–	–	–	–	–
4.0% Euro subordinated notes 2025	4.12	415	–	415	–
Convertible bond					
2.75% sterling convertible bond 2006	5.67	509	509	–	–
Total borrowings		1,318	509	415	394

As at 31 December 2006, the Company had in place a five year £1bn syndicated committed revolving credit facility with a number of its key relationship banks. The facility also has a one year extension option at the end of 2007.

The maturity profile above is calculated on the basis that a facility to refinance a maturing loan is not recognised unless the facility and loan are related. If refinancing under the Company's syndicated facility was recognised, then all amounts shown as repayable within one year would be reclassified as repayable between one and five years.

The effective interest rate is the rate which exactly discounts future cash payments over the life of the borrowing and will include all transaction costs and premia or discounts on issue. For the 5.875% sterling undated subordinated notes the effective rate includes the impact of reclassification of the notes from equity to debt on 13 March 2006 at fair value.

(iii) Convertible bonds

The convertible bond matured in 2006 and was redeemed at par without being converted into ordinary shares.

The debt component, net of expenses, of the convertible bond recognised in the balance sheet is calculated as follows:

	2006 £m	2005 £m
Balance at 1 January	509	493
Interest expense	30	30
Coupons paid	(14)	(14)
Repayment of debt	(525)	–
Balance at 31 December	–	509

The fair value of the debt component of the convertible bond at 31 December 2005 was £517m. Interest expense on the bond was calculated using the effective rate of 5.7% on the debt component.

12. SHARE CAPITAL AND SHARE PREMIUM

Authorised share capital	2006 Number of shares	2006 £m	2005 £m
At 31 December: ordinary shares of 2.5p each	9,200,000,000	230	230

Issued share capital, fully paid	Number of shares	Share capital £m	Share premium £m
Balance at 1 January 2006	6,507,421,932	163	908
Options exercised under share option schemes			
– Executive share option scheme	5,324,625	–	4
– Savings related share option scheme	19,515,404	–	11
Balance at 31 December 2006	6,532,261,961	163	923

	Number of shares	Share capital £m	Share premium £m
Balance at 1 January 2005	6,505,959,483	163	907
Options exercised under share option schemes			
– Executive share option scheme	180,628	–	–
– Savings related share option scheme	1,281,821	–	1
Balance at 31 December 2005	6,507,421,932	163	908

Options over the ordinary share capital of the Company are disclosed in Note 17 of the consolidated Group IFRS financial statements.

13. MOVEMENT IN RESERVES

	Hedging reserve £m	Share-based payments reserve £m	Subordinated borrowings £m	Revaluation reserve £m	Profit and loss account £m	Total £m
Balance at 1 January 2006	2	24	394	2,317	838	3,575
Retained profit after tax and dividends	–	–	–	–	65	65
Increase in the net assets of subsidiaries	–	–	–	1,114	–	1,114
Value of employee services	–	15	–	–	–	15
Net change in hedging reserve	(3)	–	–	–	–	(3)
Shares vested and transfer from share-based payments reserve	–	(12)	–	–	2	(10)
Reclassification of subordinated borrowings from equity to debt	–	–	(394)	–	–	(394)
Fair value loss after tax on reclassification of subordinated borrowings as debt	–	–	–	–	(28)	(28)
Balance at 31 December 2006	(1)	27	–	3,431	877	4,334

	Hedging reserve £m	Share-based payments reserve £m	Subordinated borrowings £m	Revaluation reserve £m	Profit and loss account £m	Total £m
Balance at 1 January 2005	2	11	394	2,041	501	2,949
Retained profit after tax and dividends	–	–	–	–	337	337
Increase in the net assets of subsidiaries	–	–	–	276	–	276
Value of employee services	–	13	–	–	–	13
Net change in hedging reserve	–	–	–	–	–	–
Shares vested and transfer from share-based payments reserve	–	–	–	–	–	–
Reclassification of subordinated borrowings from equity to debt	–	–	–	–	–	–
Fair value loss after tax on reclassification of subordinated borrowings as debt	–	–	–	–	–	–
Balance at 31 December 2005	2	24	394	2,317	838	3,575

14. SUBSIDIARY UNDERTAKINGS

Full disclosure of the Company's investments in subsidiary undertakings are contained within Note 47 in the consolidated Group IFRS financial statements.

Shareholders at 31 December 2006

Categories of ordinary shareholder and ranges of shareholdings at 31 December 2006 were:

	Shareholders		Shares	
	Number	%	Number	%
Category of shareholder				
Individuals	**36,016**	**73.1**	**361,937,741**	**5.6**
Banks	**10**	**–**	**53,047,266**	**0.8**
Nominee companies	**12,022**	**24.4**	**5,941,161,757**	**90.9**
Insurance companies and pension funds	**26**	**0.1**	**372,404**	**–**
Limited companies	**783**	**1.6**	**100,840,203**	**1.5**
Other corporate bodies	**389**	**0.8**	**74,902,590**	**1.2**
	49,246	**100.0**	**6,532,261,961**	**100.0**
Range of holdings				
1 – 20,000	**43,234**	**87.8**	**203,497,887**	**3.1**
20,001 – 100,000	**4,443**	**9.0**	**175,031,553**	**2.7**
100,001 – 500,000	**820**	**1.7**	**181,066,217**	**2.8**
500,001 and over	**749**	**1.5**	**5,972,666,304**	**91.4**
	49,246	**100.0**	**6,532,261,961**	**100.0**

OTHER SHAREHOLDER INFORMATION

Registrars: The Company's share register is administered by Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA (Tel: 0870 600 3954). All shareholder enquiries should be addressed to Lloyds TSB Registrars.

Electronic Share Service: This service allows you to hold shares in Legal & General without the need for a share certificate and enables you to benefit from shorter market settlement periods. Individual shareholders hold their shares in the Company in a nominee holding registered in the name of Lloyds TSB Registrars Corporate Nominee Limited.

If you would like to join this service, or require further information, you should contact the Registrars directly on 0870 600 3954. They will send you a booklet, which sets out the terms and conditions under which your shares will be held, together with the appropriate share transfer form. The booklet and the share transfer form are also available from the shareholder section of Legal & General's website at www.legalandgeneralgroup.com. You can view your shareholding in Legal & General Group Plc on the internet at www.shareview.co.uk. To register to use this service you should log onto www.shareview.co.uk and follow the instructions on screen. You will need your shareholder reference number, shown on your latest dividend counterfoil. Should you have any queries, please call the shareholder helpline on 0870 600 3954.

Dividend: The record date for the proposed final dividend for 2006, payable on 21 May 2007, is 20 April 2007 and the shares will trade ex-dividend on the London Stock Exchange from 18 April 2007.

Multiple Share Certificates: Shareholders with more than one certificate for shares may arrange for them to be consolidated into one certificate by contacting Lloyds TSB Registrars.

Individual Savings Account (ISA): Lloyds TSB Registrars provides a Single Company ISA for Legal & General Group Plc shares. If you would like more information please call the helpline on 0870 242 4244.

Capital Gains Tax: For the purpose of calculating UK capital gains tax, the market value on 31 March 1982 of each of the shares was 7.996p, after adjusting for the 1986 capitalisation issue and the 1996 and 1999 sub-divisions, but not reflecting any rights taken up under the 2002 rights issue.

Close Company Provisions: The Company is not a close company within the terms of the Income and Corporation Taxes Act 1988.

Dividend Reinvestment Plan: The Legal & General Dividend Reinvestment Plan (DRIP) enables shareholders to use their cash dividends in an inexpensive and efficient way to purchase Legal & General Group Plc shares.

Should you wish to participate in the DRIP in respect of the final dividend to be paid on 21 May 2007, a completed and signed DRIP mandate form should be received by the Registrars no later than 4 May 2007. For further details please contact Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA or call on 0870 241 3018. You can find further information, including the DRIP booklet and mandate form, in the shareholder section of Legal & General's website at www.legalandgeneralgroup.com.

2006 Preliminary Results Presentation: An audio recording of the presentation given to analysts and fund managers by Tim Breedon, Group Chief Executive and Andrew Palmer, Group Director (Finance) and the slides accompanying that presentation can be found in the shareholder section of Legal & General's website at www.legalandgeneralgroup.com. A full copy of the announcement, sent to the London Stock Exchange on 14 March 2007, can also be viewed on the shareholder site.

Registered Office: Temple Court, 11 Queen Victoria Street, London EC4N 4TP until 30 September 2007.
With effect from 1 October 2007, our registered office will be One Coleman Street, London EC2R 5AA.

No. 1417162

Registered in England and Wales

Financial Calendar

Ex-dividend date	18 April 2007
Annual General Meeting	16 May 2007
Payment of Final Dividend for 2006 (to members registered on 20 April 2007)	21 May 2007
Publication of Half Year Results for 2007 and Declaration of Interim Dividend	26 July 2007
Ex-dividend date	5 September 2007
Payment of Interim Dividend for 2007 (to members registered on 7 September 2007)	1 October 2007

Abbreviations

ABI Association of British Insurers
AFS Available-for-sale
AGM Annual General Meeting
ALCO UK Asset and Liability Committee
APE Annual Premium Equivalent
ARA Annual Report and Accounts
ASB Accounting Standards Board
ASU Accident, sickness and unemployment
BPA Bulk Purchase Annuity
CAL Company Action Level
CFO Chief Financial Officer
CMI Continuous Mortality Investigation
CSOP Company Share Option Plan
CSR Corporate Social Responsibility
DMI Domestic mortgage indemnity
DRIP Dividend Reinvestment Plan
DRR Directors' Report on Remuneration
EC European Commission
EEV European Embedded Value
EPS Earnings per share
ESOS Executive Share Option Scheme
ESOT Employee Share Ownership Trust
ESP Employee Share Plan
EST Employee Share Trust
EV Embedded Value
EVCA European Private Equity and Venture Capital Association
FOGs Financial options and guarantees
FRS Financial Reporting Standard
FSA Financial Services Authority
FTSE Financial Times Stock Exchange index
FUM Funds under Management
FVTPL Fair value through profit or loss
GAAP Generally Accepted Accounting Principles
GCIA Group Chief Internal Auditor
GI General insurance
GRCC Group Risk and Compliance Committee
Group Legal & General Group Plc
HFT Held for trading
HMRC Her Majesty's Revenue & Customs
HR Human resource function
IAS International Accounting Standards
IASB International Accounting Standards Board
ICA Individual Capital Assessment
IFA Independent Financial Adviser
IFRS International Financial Reporting Standards
IGD Insurance Groups Directive
ILU Institute of London Underwriters
ISA Individual Savings Account
IT Information Technology
KPIs Key Performance Indicators
LGA Legal & General America
LGF Legal & General France
LGI Legal & General Insurance Limited
LGIM Legal & General Investment Management Limited
LGN Legal & General Netherlands
LGP Legal & General Pensions Limited
LGPSL Legal & General Partnership Services Limited
LDI Liability Driven Investments
LTF Long Term Fund
MCEV Market Consistent Embedded Value
MTN Medium Term Note
NBSC New Bridge Street Consultants
PMC Legal & General Assurance (Pensions Management) Limited
PPFM Principles and Practices of Financial Management
PSP Performance Share Plan
PVNBP Present value of new business premiums
RBC Risk Based Capital
RCC Risk and Compliance Committees
RCM Risk Capital Margin
RDR Risk discount rate
ROEV Return on Embedded Value
RPI Retail Price Index
SAYE Savings related share option scheme
SBP Share Bonus Plan
SEE Social, environmental and ethical
SFS Summary Financial Statement
SIPP Self-Invested Personal Pension
SNW Shareholder net worth
Society Legal & General Assurance Society Limited
SORIE Statement of Recognised Income and Expense
SRC Shareholder Retained Capital
TCF Treating Customers Fairly
TSR Total Shareholder Return
VIF Value of in-force business
WACC Weighted average cost of capital

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