

02338444

LEGAL & GENERAL FINANCE PLC

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED

31 DECEMBER 2016

LEGAL & GENERAL FINANCE PLC
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Registered Office
One Coleman Street
London
EC2R 5AA

Registered in England and Wales number 02338444

LEGAL & GENERAL FINANCE PLC STRATEGIC REPORT

The directors present their Strategic Report on Legal & General Finance PLC (the "Company") for the year ended 31 December 2016.

Principal activities

Legal & General Finance PLC is a public limited company incorporated in England and Wales whose ultimate controlling party is Legal & General Group Plc. The Company's registered office is at One Coleman Street, London, EC2R 5AA. It is registered in England and Wales under company registration number 02338444 and domiciled in the United Kingdom.

Review of business and future developments

The Company provides funding to other Legal & General group companies. In fulfilling this role, the Company issues listed debt through Legal & General Group Plc's £4bn Euro Note Programme and the Company's US \$2bn Commercial Paper Programme. All of the Company's issued listed debt under these programmes is guaranteed by Legal & General Group Plc.

Financial review and key performance indicators

The directors review a range of performance indicators to monitor the performance of the Company. Profit on ordinary activities before taxation and net assets are regarded as the principal key performance indicators.

The profit on ordinary activities before taxation of the Company for 2016 was £18.1m (2015: £1.8m). The increase in profit before tax in 2016 is driven by a one-off gain of £11.5m relating to an investment in bonds issued by a fellow group company being redeemed early. Net assets as at 31 December 2016 were £7.6m (2015: £6.1m).

Principal risks and uncertainties

The Company's business involves the acceptance and management of risk. A detailed review of the Company's exposure to risks, which comprise market risk, credit risk and liquidity risk, together with the framework for their management and analysis of the exposure of the Company's financial instruments to risk is set out in note 16. The principal risks and uncertainties facing the Company are:

a) Market infrastructure

The Company's investment and fund raising activities are reliant upon the availability of market infrastructure. The loss of a major financial centre may have a significant effect on the Company's operation and profitability.

b) Counterparties

A number of major banks operate as counterparties for the investments of the Company. Whilst the Company ensures that it only transacts with strongly rated counterparties and it regularly reviews its exposures, the financial failure of a significant counterparty could result in disruption and financial loss.

c) Liquidity and cash flow

Liquidity risk is the risk that the Company, though solvent, either does not have sufficient liquid financial resources available to enable it to meet its obligations as they fall due, or can only secure such liquid financial resources either at an excessive borrowing cost relative to that achieved in the recent past or that typically payable by a comparably rated borrower or through the sale of illiquid assets at a price significantly below the fair value of such assets in the recent past. This risk can arise from adverse market conditions or an unexpected event that causes liquidity stress in other entities within the group.

By order of the board:



H.A. Baker
For and on behalf of Legal & General Co Sec Limited
Company Secretary
07 March 2017

LEGAL & GENERAL FINANCE PLC DIRECTORS' REPORT

The directors present their Annual Report together with the audited financial statements of Legal & General Finance PLC (the "Company") for the year ended 31 December 2016.

Principal activities and future developments

The principal activity of the Company throughout the year was to operate as a finance company. The directors do not envisage any changes in activity for the foreseeable future.

The Company's prime objective is to provide funding to other Legal & General group companies. It does this by raising finance from the European capital markets.

The Company has issued the following primary financial instruments as at 31 December 2016 medium term notes and commercial paper. The overall objective of issuing these underlying financial instruments is to achieve a low real cost of funds for the Legal & General group.

The Strategic Report and financial risk management notes are on pages 2 and 22 to 26 respectively.

Results for the year and dividend

The results of the Company are set out on page 9. The directors do not recommend the payment of a final dividend (2015: nil). An interim dividend of £13m was paid in the year (2015: £8m).

Share capital

The Company's share capital is £50,000 (2015: £50,000). There were no changes to the issued share capital during the financial year.

Directors

The directors of the Company, who served during the year and up to the date of signing the financial statements, together with their dates of appointment and resignation, where appropriate, are shown below:

A. Price (resigned 04 November 2016)
F.B.Turley
G. O'Neill (appointed 04 November 2016)
M. J. Brookes (appointed 28 September 2016)
M. J. Gregory (Chairman)
P. R. Stanworth (resigned 28 September 2016)

Directors' Indemnities and insurance

The immediate and ultimate parent company, Legal & General Group Plc, maintains an appropriate level of directors' and officers' liability insurance which is reviewed annually. As permitted by the Articles of Association, the directors have the benefit of an indemnity which is a qualifying third party indemnity provision as defined by Section 234 of the Companies Act 2006. The indemnity was in force throughout the last financial year and is currently in force.

Going concern

No material uncertainties that cast significant doubt about the ability of the company to continue as a going concern have been identified by the directors.

Internal control and risk management framework

The Board of Directors have overall responsibility for the Company's systems of risk management and internal controls. The Company operates within the risk management framework and under the policies, procedures and internal controls maintained by its parent company.

The Group Audit Committee, in conjunction with the Group Risk Committee, assists in ensuring the group operates within a framework of prudent and effective controls that allow risk to be identified, assessed and managed. The group's control policies and procedures are in accordance with the Financial Reporting Council's guidance on risk management, internal control and related financial and business reporting. The group's system of internal control is designed to manage rather than eliminate risk and can only provide reasonable and not absolute assurance against material loss.

The company adheres to all the practices through a system of timely preparation of management and financial statements, internal review of the statements within finance and a periodic review by Group Internal Audit. The Company's exposure to financial risks is contained in note 18.

The day to day operations of the company are managed by Legal & General Group Treasury Functions.

Independent auditors

A resolution to reappoint the auditors, PricewaterhouseCoopers LLP, who have expressed their willingness to be reappointed, will be proposed at the Annual General Meeting.

Statement of directors' responsibilities in respect of the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable United Kingdom Accounting Standards, comprising FRS 101, have been followed, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006.

The directors are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

LEGAL & GENERAL FINANCE PLC
DIRECTORS' REPORT

Statement of directors' responsibilities in respect of the financial statements (continued)

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

In the case of each director in office at the date the Directors' Report is approved:

- so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Disclosure of information to auditors

In accordance with Section 418 of the Companies Act 2006, each of the directors who held office at the date this report was approved, confirms that:

- (a) so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware.

By order of the board:



H.A. Baker
For and on behalf of Legal & General Co Sec Limited
Company Secretary
07 March 2017

Report on the financial statements

Our opinion

In our opinion, Legal & General Finance Plc's financial statements (the "financial statements"):

- give a true and fair view of the state of the company's affairs as at 31 December 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

What we have audited

The financial statements, included within the Annual Report and Financial Statements (the "Annual Report"), comprise:

- the Balance Sheet as at 31 December 2016;
- the Income Statement for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law (United Kingdom Generally Accepted Accounting Practice).

In applying the financial reporting framework, the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors Responsibilities, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Responsibilities for the financial statements and the audit (continued)

What an audit of financial statements involves

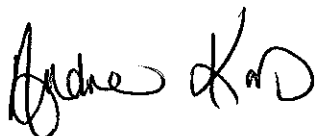
We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.



Andrew Kail (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
07 March 2017

LEGAL & GENERAL FINANCE PLC
INCOME STATEMENT

For the year ended 31 December 2016

	Note	2016	2015
		£m	£m
Finance and similar income:			
- Group undertakings		40.5	37.9
- Other	6	<u>7.1</u>	<u>6.6</u>
		47.6	44.5
Finance and similar costs:			
- Group undertakings		(6.2)	(4.2)
- Other	15	<u>(36.1)</u>	<u>(35.6)</u>
		(42.3)	(39.8)
Administrative expenses		(2.4)	(1.6)
Investment return	7	<u>15.2</u>	<u>(1.3)</u>
Profit on ordinary activities before income tax		18.1	1.8
Income tax expense	8	<u>(3.6)</u>	<u>(0.7)</u>
Profit on ordinary activities for the year		<u>14.5</u>	<u>1.1</u>

There's no other comprehensive income for the year. The profit for the year attributable to owners of the Company also reflects the total comprehensive income of the Company.

**LEGAL & GENERAL FINANCE PLC
BALANCE SHEET**

02338444

As at 31 December 2016

	Note	2016 £m	2015 £m
Non-Current Assets			
Investments	10	601.2	601.2
Current Assets			
Financial investments	11	1,264.1	1,612.5
Other receivables	12	215.9	53.5
Cash and cash equivalents	13	1.0	56.2
		<u>1,481.0</u>	<u>1,722.2</u>
Total Assets		<u>2,082.2</u>	<u>2,323.4</u>
Non-Current Liabilities			
Borrowings	15	(597.9)	(597.8)
Current Liabilities			
Borrowings	15	(216.0)	(15.2)
Other payables	16	(1,260.7)	(1,704.3)
		<u>(1,476.7)</u>	<u>(1,719.5)</u>
Total Liabilities		<u>(2,074.6)</u>	<u>(2,317.3)</u>
Net Assets		<u>7.6</u>	<u>6.1</u>
Equity			
Share capital	14	-	-
Retained earnings		7.6	6.1
		<u>7.6</u>	<u>6.1</u>
Total Equity		<u>7.6</u>	<u>6.1</u>

The financial statements on pages 9 to 26 were approved by the board of directors on 07 March 2017 and signed on its behalf by:



G. O'Neill
Director

Registered number: 02338444
One Coleman Street
London EC2R 5AA
07 March 2017

LEGAL & GENERAL FINANCE PLC
STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2016

	Share capital £m	Retained earnings £m	Total equity £m
As at 1 January 2016	-	6.1	6.1
Total comprehensive income for the year	-	14.5	14.5
Dividends	-	(13.0)	(13.0)
As at 31 December 2016	-	7.6	7.6
As at 1 January 2015	-	13.0	13.0
Total comprehensive income for the year	-	1.1	1.1
Dividends	-	(8.0)	(8.0)
As at 31 December 2015	-	6.1	6.1

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies

The main accounting policies of the Company are as follows, these policies have been consistently applied to all the years presented, unless otherwise stated.

(a) Basis of preparation

The financial statements have been prepared on a going concern basis.

The financial statements of Legal & General Finance Plc. have been prepared in accordance with Financial Reporting Standard 101, 'Reduced Disclosure Framework' (FRS 101). The financial statements have been prepared under the historical cost convention, as modified by the revaluation of derivative financial assets and financial liabilities measured at fair value through profit and loss, and in accordance with the Companies Act 2006.

The preparation of financial statements, in conformity with FRS 101, requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are the determination of fair value for unquoted or illiquid financial instruments (Note 9).

The following exemptions from the requirements of IFRS have been applied in the preparation of these financial statements, in accordance with FRS 101:

- The following paragraphs of IAS 1, 'Presentation of financial statements':
 - (i) 10(d), (statement of cash flows);
 - (ii) 16 (a statement of compliance with all IFRS);
 - (iii) 38A (requirement for minimum of two primary statements, including cash flow statements);
 - (iv) 38B-D (additional comparative information);
 - (v) 111 (cash flow statement information);
 - (vi) 134-136 (capital management disclosures).
- IAS 7, 'Statement of cash flows';
- Paragraph 30 and 31 of IAS 8 'Accounting policies, changes in accounting estimates and errors' (requirement for the disclosure of information when an entity has not applied a new IFRS that has been issued but is not yet effective); and
- The requirements in IAS 24, 'Related party disclosures' to disclose related party transactions entered into between two or more members of a group.

The directors and key management of the Company had no material transactions with the Company or any other group undertakings.

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies (continued)

(b) Finance and similar income

Finance and similar income comprises interest receivable and is recognised using the effective interest rate method.

Dividend income is recognised when the right to receive payment is established.

(c) Distributions

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.

(d) Foreign currencies

Items included in the financial statements of the Company are measured using the currency of the primary economic environment in which it operates (the functional currency). The financial statements are presented in Sterling (£) which is also the Company's functional currency.

Transactions denominated in foreign currencies are translated into the functional currency at the rates of exchange prevailing at the time of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into Sterling at the rates of exchange prevailing at the balance sheet date. Non-monetary items are maintained at historic rates. All exchange gains or losses are recognised in the income statement.

(e) Taxation

Current tax comprises tax payable on current period profits, adjusted for non tax deductible or non-taxable items and any adjustment to tax payable in respect of previous periods. Deferred taxation is provided in full on all timing differences. 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.

(f) Investments

The Company classifies its financial investments on initial recognition at fair value through profit and loss (FVTPL) or as loans and receivables. Initial recognition of financial investments is on the trade date.

Investments classified as FVTPL are measured at fair value with gains and losses reflected in the income statement under Revaluation of investments held at fair value through profit and loss.

Loans and receivables are initially measured at fair value and subsequently held at amortised cost using the effective interest method.

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS

1 Accounting policies (continued)

(g) Borrowings

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

(h) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with bank, treasury bills and other short term highly liquid investment with maturity of three months or less from the date of acquisition.

(i) Derivative assets and liabilities

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 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 Company's principal uses of hedge accounting are to:

- (i) 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 affects profit or loss or is no longer expected to occur; and
- (ii) 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 Consolidated 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 Consolidated Income Statement, within other expenses, in the current year.

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.

(j) Changes in accounting policy and disclosure

Certain standards, amendments and interpretations to existing standards have been published which will become mandatory for future accounting periods but which the Company has not adopted early, as follows:

• In July 2014, the IASB issued IFRS 9, 'Financial Instruments' which is effective for annual periods beginning on or after 1 January 2018, subject to EU endorsement and the IASB's consideration of its exposure draft, "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance contracts". On adoption, IFRS 9 contains three key elements:

- A principles-based model for classification and measurement of financial instruments driven by cash flow characteristics and the business model in which an asset is held. Financial assets are classified under either amortised cost, fair value through other comprehensive income (FVOCI) or fair value through profit and loss;
 - A single expected loss impairment model that will require more timely recognition of expected credit losses on assets classified as amortised cost or FVOCI. Specifically, the new Standard requires entities to account for expected credit losses from when financial instruments are first recognised, and it lowers the threshold for recognition of full lifetime expected losses; and
 - A substantially-reformed model for hedge accounting with enhanced disclosures about risk management activities, enabling entities to better reflect these activities in their financial statements.
- IFRS9 is not expected to have a material impact on the Company.

There are no other standards, amendments and interpretations to existing standards that have been published and will become mandatory for future accounting periods which are expected to have a material impact on the Company.

(j) Exchange rates

Principal rates of exchange used for translation into sterling at the end of the year were:

	2016	2015
US Dollars	1.24	1.47
Euros	1.17	1.36

2 Segmental disclosure

The Company has not made any segmental disclosure as its income is wholly attributable to its principal activity and is generated in the United Kingdom.

3 Auditors' remuneration

Auditors' remuneration of £31,450 (2015: £37,250) in respect of the audit of this company was incurred in the year, wholly in relation to audit work.

4 Foreign Exchange

Foreign exchange revaluation gains recognised in the income statement were £2.8m (2015: £1.0m).

5 Employee costs and pension

No incremental emoluments in respect of services to this company were paid to any director nor were any direct pension contributions paid (2015: £nil). There were no employees during 2016 (2015: nil).

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS

6 Finance and similar income other

During 2016 income from investments in LGIM managed funds was £4.2m (2015: £5.7m), income from investments in Commercial papers and other similar investments was £2.9m (2015: £0.8m).

7 Investment Return

Included within investment return is £11.5m (2015: nil) of gain relating to an investment in bonds issued by a fellow group company being redeemed early.

8 Tax on profit on ordinary activities	2016	2015
	£m	£m
<u>Total tax</u>		
UK corporation tax on profits for the year	3.6	0.4
Adjustments in respect of prior year	<u>-</u>	<u>0.3</u>
Income tax expense	<u>3.6</u>	<u>0.7</u>

Factors affecting the current tax charge for the year:

The tax assessed for the year is equal to (2015: not equal to) the standard rate of corporation tax in the UK for a company (20%) (2015: 20.25%). The differences are explained below:

	2016	2015
	£m	£m
Profit on ordinary activities before taxation	<u>18.1</u>	<u>1.8</u>
UK corporation tax at 20% (2015: 20.25%)	<u>3.6</u>	<u>0.4</u>
Effects of:		
Adjustments in respect of prior years	<u>-</u>	<u>0.3</u>
Total income tax expense for the year	<u>3.6</u>	<u>0.7</u>

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED

9 Dividends

	2016 £m	2015 £m
Interim dividend: £260 (2015: £160) paid per £1 share	<u>13.0</u>	<u>8.0</u>

10 Investments

	2016 £m	2015 £m
Loan to group undertaking	<u>601.2</u>	<u>601.2</u>

None of the investments above are past due or impaired. The loan to group undertaking is held at amortised cost. The fair value of loan is £849.5m (2015: £775.3m).

11 Financial investments

(a) Financial investments at fair value

The fair values of quoted financial investments are based on current bid prices. If the market for a financial investment is not active, the Company establishes fair value by using valuation techniques such as recent arm's length transactions, consensus market pricing, reference to similar listed investments or discounted cash flow models.

	2016 £m	2015 £m
Financial investments at fair value:		
Managed funds	1,260.0	1455.8
Debt securities	1.5	156.5
Accrued interest	-	0.2
Derivative assets	<u>2.6</u>	<u>-</u>
Total financial investments	<u>1,264.1</u>	<u>1,612.5</u>

All of the financial investments are designated as fair value through profit and loss (FVTPL) other than derivative assets which are designated as held for trading (HFT).

None of the financial investments above are past due or impaired. The managed funds investments are holdings in Legal & General Investment Management Ltd managed funds which invest solely in cash, cash equivalents and debt securities.

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable willing parties in an arms length transaction.

Fair value measurements are based on observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflects the Company's view of market assumptions in the absence of observable market information. The Company utilises techniques that maximise the use of observable inputs and minimise the use of unobservable inputs.

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS

11 Financial investments (continued)

Fair value hierarchy (continued)

The table that follows presents an analysis of the assets held at fair value in accordance with the measurement technique, defined below:

Level 1: fair values measured using quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: fair values measured using valuation techniques for all inputs significant to the measurement other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: fair values measured using valuation techniques for any input for the asset or liability significant to the measurement that is not based on observable market data (unobservable inputs).

Financial assets by hierarchy levels

At 31 December 2016

	Carrying value £m	Level 1 £m	Level 2 £m	Level 3 £m
Managed funds	1,260.0	1,260.0	-	-
Debt securities	1.5	-	-	1.5
Derivative assets	2.6	-	2.6	-
Total financial investments	1,264.1	1,260.0	2.6	1.5

The company's policy is to re-assess categorisation of financial assets at the end of each year and to recognise transfers between levels at that point in time.

There were no significant transfers in the year between levels (2015: £56m).

At 31 December 2015

	Carrying value £m	Level 1 £m	Level 2 £m	Level 3 £m
Managed funds	1,455.8	1,455.8	-	-
Debt securities	156.5	5.2	91.8	59.5
Accrued interest	0.2	0.1	0.1	-
Derivative assets	-	-	-	-
Total financial investments	1,612.5	1,461.1	91.9	59.5

LEGAL & GENERAL FINANCE PLC
NOTES TO THE FINANCIAL STATEMENTS

11 Financial investments (continued)

Assets measured at fair value based on level 3

Level 3 assets include a small portion of debt securities where broker quotes were not supported by adequate explanations on assumptions used.

	Debt securities	Debt securities
	2016	2015
	£m	£m
As at 1 January	59.5	1.8
Total gains or losses for the year recognised:		
- realised and unrealised gains/(losses) in the income statement	12	1.7
Sales	(69.8)	
Transfers into level 3	-	56.0
As at 31 December	<u>1.5</u>	<u>59.5</u>

A shift by +/-5% in broker quotes would impact profit or loss by £nil (2015: £3.0m).

12 Other receivables

	2016	2015
	£m	£m
Amounts owed by group undertakings	<u>215.9</u>	<u>53.5</u>

None of the receivables above are past due or impaired.

13 Cash and cash equivalents

	2016	2015
	£m	£m
Cash at bank and in hand	<u>1.0</u>	<u>56.2</u>
	<u>1.0</u>	<u>56.2</u>

14 Share capital

	2016	2015
	£	£
Allotted and partly paid:		
50,000 (2015: 50,000) £1 ordinary shares partly paid of 25p each	<u>12,500</u>	<u>12,500</u>

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15 **Borrowings**

The fair value of quoted financial debt included in the disclosures is based on current offer prices. If the market for a financial debt is not active, the Company establishes fair value by using valuation techniques such as recent arm's length transactions, reference to similar listed debt or discounted cash flow models.

	Carrying amount 2016 £m	Coupon rate 2016 %	Fair value 2016 £m	Carrying amount 2015 £m	Coupon rate 2015 %	Fair value 2015 £m
Core Borrowings						
Sterling medium term notes 2031-2041	597.9	5.87	834.3	597.8	5.87	768.7
Operational borrowings						
Euro Commercial paper	216.0	0.96	216.0	15.2	0.47	15.2
	813.9		1050.3	613.0		783.9

£36m (2015: £35.4m) of interest expense relating to the borrowings above is included in other finance and similar costs in the Income Statement, the remaining £0.1m (2015: £0.2m) relates to legal costs.

The sterling medium term notes are senior debt with a face value of £600m issued in the following tranches:

Issuance	Maturity	Face Value £m	Coupon rate %
December 2000 - September 2001	December 2031	350.0	5.875
April 2001	April 2033	40.0	5.750
April 2001	April 2041	10.0	5.800
April 2002	April 2033	200.0	5.875

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15 **Borrowings (continued)**

Analysis by nature and maturity

At 31 December 2016	Maturity date of undiscounted cash flows						Total £m
	Carrying Value £m	Within 1 yr £m	1-5 yrs £m	5-15 yrs £m	15-25 yrs £m	Over 25 yrs £m	
Core Borrowings							
Medium term notes	597.9	-	-	350.0	250.0	-	600.0
Operational borrowings							
Euro commercial paper	216.0	216.0	-	-	-	-	216.0
	813.9	216.0	-	350.0	250.0	0.0	816.0
Contractual undiscounted interest payments		35.2	140.8	352.0	32.8	0.0	560.8
Total contractual undiscounted cash flows		251.2	140.8	702.0	282.8	0.0	1,376.8
At 31 December 2015	Maturity date of undiscounted cash flows						Total £m
	Carrying Value £m	Within 1 yr £m	1-5 yrs £m	5-15 yrs £m	15-25 yrs £m	Over 25 yrs £m	
Core Borrowings							
Medium term notes	597.8	-	-	-	590.0	10.0	600.0
Operational borrowings							
Euro commercial paper	15.2	15.2	-	-	-	-	15.2
	613.0	15.2	-	-	590.0	10.0	615.2
Contractual undiscounted interest payments		35.2	140.8	352.0	68.0	0.0	596.0
Total contractual undiscounted cash flows		50.4	140.8	352.0	658.0	10.0	1,211.2

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16 **Other payables**

	2016	2015
	£m	£m
Amounts owed to group undertakings	1,246.1	1,691.5
Accrued interest on medium term notes	10.8	10.7
Income tax payable	3.6	0.7
Derivative Liabilities	0.2	1.4
	<u>1,260.7</u>	<u>1,704.3</u>

Amounts owed to group undertakings are unsecured. The derivative liabilities are classified as level 2 in the fair value hierarchy.

17 **Parent and holding company**

The immediate and ultimate parent company, and the smallest and largest group to consolidate these financial statements, is Legal & General Group Plc, a company incorporated in England & Wales. These financial statements therefore provide information about the Company as an individual undertaking. Copies of the financial statements of the ultimate holding company, Legal & General Group Plc, are available on the Group website, www.legalandgeneralgroup.com or from the Company Secretary at the Registered Office, One Coleman Street, London, EC2R 5AA.

18 **Financial risk management**

Management of risk

The Company, in the course of its business activities, is exposed principally to market, credit and liquidity risks. As part of the Legal & General Group the Company operates within a formal risk management framework to ensure that all significant risks are identified and managed.

A risk identification and assessment process is operated to formally evaluate and manage 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.

Control framework

The Company manages its exposure to financial instruments by maintaining an appropriate control structure. Dealing authority is formally approved by the Legal & General Group Capital Committee. The Group Treasurer directs dealing operations and reports monthly to the Treasury Oversight Group and to the Board of this Company. The activities of the Group Treasury department are subject to review via periodic independent reviews and audits by internal auditors. The internal control framework within the Group Treasury department includes segregation of duties between dealing and settlement.

18 Financial risk management (continued)

Risk review function

The Group's risk review function provides oversight of the risk management processes of the Legal & General group companies. 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.

Details of the categories of risk to the Company and high-level management processes are set out below. Legal & General Group policies are in place setting out the framework for the management of its key risks, the operation of which are supported by the Group's risk review functions and are independently confirmed by Group Internal Audit.

Market risk

(a) Currency

Currency risk is the risk arising from fluctuations in exchange rates which may affect assets, liabilities and any mismatch between the two.

The Company is also potentially exposed to loss as a result of fluctuations in the value of, or income from, assets denominated in foreign currencies. The Company's objective is to have minimal residual foreign exchange risk on its assets and liabilities. It achieves this by matching the currency of its assets with those of its borrowings. Where an opportunity exists to borrow in a different currency on an advantageous basis to that for which funding is actually required, cross currency swaps or forward foreign exchange contracts are used to convert to the desired currency.

During the year there were no material net exposures.

(b) Interest rate risk

Interest rate risk is the risk arising from fluctuations in interest rates which may affect assets, liabilities and any mismatch between the two.

The Company's borrowings comprise the current and long term liabilities set out in notes 13 and 14. All of the Company's borrowings were fixed rate loans under the medium term note programme throughout the year and at 31 December 2016, other than a small amount at floating rates of interest. The fixed rate loans were lent to another group company on a fixed rate basis with the same maturities.

All floating interest rate liabilities have interest rates based on the relevant currency LIBOR equivalents.

18 Financial risk management (continued)

Market risk (continued)

(b) Interest rate risk (continued)

A sensitivity analysis of a 100 basis point increase or decrease in LIBOR based interest rates was carried out on the financial statements of the Company. There was found to be an immaterial impact of £0.1m (2015: £0.1m) to the Company's reported results from this movement in interest rates. This exercise applied the interest rate shift to all balance sheet line items (using the position at 31 December 2016) and calculated the resulting potential change to the income statement.

(c) Exposure to worldwide equity markets

The only equity security investments held are in funds managed by L&G Investment Management Limited which solely invest in cash, cash equivalents and debt securities. The fund is unlisted and based in the UK. Therefore there is no underlying exposure on this fund to equity price risk.

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.

The investment of shareholders' monies requires some credit risk to be taken. Credit risk is managed through the setting and regular review of detailed counterparty credit and concentration limits. Compliance with these limits for treasury investments is monitored daily. The limits apply to cash deposits, money market investments, foreign exchange and interest rate management transactions. The Legal & General Group Plc Group Credit Risk Committee oversees this process.

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18 Financial risk management (continued)

Credit risk (continued)

The credit risk of the external financial assets based on long term ratings is outlined below. Ratings are provided by independent rating agencies and the average of these is used.

Exposure to credit risk	2016	2015
	£m	£m
Government fixed rate securities:		
AAA	-	5.2
	<u>-</u>	<u>5.2</u>
Other fixed rate securities:		
AAA	-	5.5
A	1.5	-
	<u>1.5</u>	<u>5.5</u>
Variable rate securities:		
AAA	-	45.4
AA	-	25.2
A	-	75.2
	<u>-</u>	<u>145.8</u>
Accrued interest:		
AAA	-	0.1
A	-	0.1
	<u>-</u>	<u>0.2</u>
Cash and cash equivalents:		
A	1.0	1.0
BBB	-	55.2
	<u>1.0</u>	<u>56.2</u>
Derivative assets:		
AA	1.0	-
A	1.6	-
	<u>2.6</u>	<u>-</u>
	<u>5.1</u>	<u>212.9</u>

Amounts owed by group undertakings have been excluded from the above analysis as the Company considers that such amounts will be repaid in all reasonably possible circumstances.

18 Financial risk management (continued)

Liquidity risk

Liquidity risk is the risk that the Company 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 activities of the Company. 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 that it maintains sufficient liquid assets which are able to be realised as well as standby facilities to meet a prudent estimate of its net cash outflows. The Group's formal governance structure oversees the management of liquidity risk.

See Borrowings note for cashflow maturity details (note 13).

Capital Management

The Company's capital is determined with reference to the requirements of the Company's stakeholders. In managing capital we seek to maintain sufficient, but not excessive, financial strength to support funding of the Legal & General Group, payment of dividends and the requirements of other stakeholders. The sources of capital used by the Company are equity shareholders' funds and retained earnings arising from the Company's operations. At 31 December 2016 the company had £12,500 of ordinary share capital and £7.6m of retained earnings. The company had £600m of senior long dated borrowings in issue which mature between 2031 and 2041.

19 Commitments

The Company has a number of loan agreements in place with group undertakings to provide funding for periods up to ten years.

The Company has one loan agreement under which it is committed to provide funding of £5m at 31 December 2016 (2015: £80m) to a fellow group subsidiary. This was undrawn as at 31 December 2016 (2015: undrawn). The agreement expires on 02 June 2020.

The Company has also provided an undertaking to a fellow group subsidiary to provide funding of up to £25m on a contingent basis. As at 31 December no monies have been drawn against this undertaking (2015: nil).

The undrawn amounts under all other loan agreements are cancellable at the request of either the borrower or lender.