IMPACT OF INTERNATIONAL FINANCIAL REPORTING STANDARDS ON THE RESULTS FOR 31 DECEMBER 2004

Contents

Basis of preparation of restated financial information

From 2005, all European Union listed companies are required to prepare their consolidated financial statements using standards issued by the International Accounting Standards Board (IASB). The attached contains certain financial information presented as part of the Group's results in 2004 restated for the implementation of International Financial Reporting Standards (IFRS) and will form part of the comparatives for 2005 reporting purposes. The attached restated financial information has been prepared using the Group's accounting policies under IFRS, as set out on pages 19 to 32. The Group's revised accounting policies are in accordance with IFRS issued by the IASB. The European Union has endorsed all relevant IFRS with the exception of the Amendment to IAS19 *Employee Benefits (2004)* and the amendments to IAS39, *The Fair Value Option* published by the IASB in June 2005.

Both these amendments are expected to be endorsed by the European Commission during 2005 and although they are not mandatory until 2006, the Group has decided to adopt them early and reflect their impact within the 2004 restated financial information. The Group's full year financial statements at 31 December 2005 will be prepared in accordance with these endorsed IFRS and this announcement reflects the accounting policies expected to apply at the year end.

IFRS remains subject to possible amendment by interpretative guidance from the IASB or other external bodies and therefore are subject to change prior to publication of the Group's full IFRS financial statements early in 2006.

In line with the requirements of International Financial Reporting Standard 1, *First-Time Adoption of International Financial Reporting Standards* (IFRS1), Aviva has applied the Group's accounting policies under IFRS retrospectively at the date of transition being 1 January 2004, with exception of a number of permitted exemptions as detailed below:

Business combinations
The Group has elected not to apply retrospectively the provisions of International Financial Reporting Standard 3, *Business Combinations*, to business combinations that occurred prior to 1 January 2004. At the date of transition no adjustment was made between UK GAAP and IFRS shareholders' funds for any historical business combination.

Cumulative translation differences
The Group has elected that the cumulative translation differences of foreign operations were deemed to be zero at the transition date to IFRS.

Equity compensation plans
The Group has elected not to apply the provisions of International Financial Reporting Standard 2, *Share-based Payment*, to options and awards granted on or before 7 November 2002 which had not vested by 1 January 2005.

Employee benefits
All cumulative actuarial gains and losses on the Group's defined benefit pension schemes have been recognised in equity at the transition date.

Comparatives
The Group has not taken advantage of the exemption within IFRS1 that allows comparative information presented in the first year of adoption of IFRS not to comply with International Accounting Standard 32, *Financial Instruments: Disclosure and Presentation* (IAS32), International Accounting Standard 39, *Financial Instruments: Recognition and measurement* (IAS39) and International Financial Reporting Standard 4, *Insurance Contracts* (IFRS4).

Estimates
Where estimates had previously been made under UK GAAP, consistent estimates (after adjustments to reflect any difference in accounting policies) have been made for the same date on transition to IFRS (i.e., judgements affecting the Group's opening balance sheet have not been revisited for the benefit of hindsight).

Held for sale
The requirements of International Financial Reporting Standard 5, *Non-current Assets Held for Sale and Discontinued Operations* have been applied prospectively from 1 January 2005.

FRS27
Financial Reporting Standard 27, *Life Assurance* (FRS27) was issued by the UK's Accounting Standards Board (ASB) on 13 December 2004, following the Penrose inquiry. Aviva, along with other major insurance companies and the Association of British Insurers (ABI), has signed a Memorandum of Understanding (MoU) with the ASB relating to FRS27. Under this MoU, Aviva has agreed to adopt voluntarily in full the standard from 2005 within the Group's IFRS financial statements.

Within FRS27, the ASB acknowledged the difficulty of applying the requirements retrospectively and indeed it is the Group's view that it would be impractical to do so. Hence, in accordance with IAS8, only the balance sheet at 31 December 2004 has been restated for the impact of FRS27. No adjustments have been made, nor any required, to the 2004 income statement and the opening balance sheet at 1 January 2004.

Auditors' review
The restated results for the year ended 31 December 2004 have been audited by the auditor, Ernst & Young LLP. The summary IFRS information included in this document does not constitute statutory accounts as defined in section 240 of the Companies Act 1985 and does not include details of the Group's consolidated cash flows.

Summarised consolidated income statement – IFRS basis
For the twelve months to 31 December 2004

	Full year 2004 £m
Income	
Premiums written net of reinsurance	23,351
Net premiums earned	23,175
Fee and commission income	872
Net investment income	15,871
Share of profit/(loss) after tax of joint ventures and associates	99
Other operating income	509
	40,526
Expenses	
Change in insurance liabilities, net of reinsurance	(6,275)
Claims and benefits paid, net of recoveries from reinsurers	(17,794)
Change in unallocated divisible surplus	(1,330)
Expenses attributed to investment contracts	(5.613)
Fee and commission expense	(4,478)
Other operating expenses	(2,405)
Finance costs	(606)
Profit/(loss) before tax	**2,025**
Tax attributable to policyholders' returns	(383)
Profit/(loss) before tax attributable to shareholders' profits	**1,642**
Tax expense	(654)
Less: tax attributable to policyholders' returns	383
Tax attributable to shareholders' profits	(271)
Profit/(loss) for the year	**1,371**

Attributable to:	
Equity shareholders of Aviva plc	1,275
Minority interests	96

All profit for the year is from continuing operations.

	Full year 2004 £m
Earnings per share	
Basic (pence per share)	55.5
Diluted (pence per share)	54.9

Summarised consolidated pro forma operating profit statement for the year ended 31 December 2004

	UK GAAP £m	IFRS changes £m	Restated for IFRS changes £m	LTIR[1] (Note 6) £m	Restated for IFRS and LTIR[1] changes £m
Net premiums written (excluding associates)					
Life premiums	19,899	(6,357)[2]	13,542	-	13,542
General insurance and health	9,809	-	9,809	-	9,809
	29,708	(6,357)	23,351	-	23,351
Operating profit					
Long term business	1,185	(69)	1,116	-	1,116
Fund management	43	(3)	40	-	40
General insurance and health business	1,384	(28)	1,356	(97)	1,259
Non-insurance operations	(108)	(13)	(121)	-	(121)
Corporate costs	(178)	(10)	(188)	-	(188)
Unallocated interest charges	(465)	-	(465)	-	(465)
Unallocated income	-	28	28	-	28
Operating profit before tax attributable to shareholders' profits from continuing operations	**1,861**	**(95)**	**1,766**	**(97)**	**1,669**
Amortisation/impairment of goodwill	(120)	79	(41)	-	(41)
Amortisation of acquired additional value of in-force long-term business and other intangibles	(126)	34	(92)	-	(92)
Financial Services Compensation Scheme and other levies	(49)	-	(49)	-	(49)
Short-term fluctuation in return on investments	131	(67)	64	97	161
Change in the equalisation provision	(23)	23	-	-	-
Net loss on the disposal of subsidiary and associated undertakings	(136)	170	34	-	34
Exceptional costs for termination of operations	(50)	10	(40)	-	(40)
Profit before tax attributable to shareholders' profits	**1,488**	**154**	**1,642**	**-**	**1,642**
Tax attributable to shareholders' profits	(355)	84	(271)	-	(271)
Profit for the year	**1,133**	**238**	**1,371**	**-**	**1,371**
Attributable to:					
Equity shareholders of Aviva plc	1,057	218	1,275	-	1,275
Minority interests	76	20	96	-	96
Earnings per share based on operating profit after tax attributable to ordinary shareholders	57.2p		56.9p		53.9p
Earnings per share based on profit after tax attributable to ordinary shareholders	45.8p		55.5p		55.5p
Dividend cover[3]	2.25 times		2.23 times		2.11 times

[1] The Group has decided to adopt from 2005, as a discretionary change that is not required by IFRS, a change in rates and methodology in the calculation of LTIR as it applies to its general insurance and health business.
[2] Represents the application of deposit accounting for those contracts classified as non-participating investment contracts.
[3] Calculated as operating profit net of tax, minorities and preference dividend over interim and final ordinary dividends declared in respect of the financial year

Analysis of IFRS adjustments to the pro forma operating profit statement for the year ended 31 December 2004 as a result of the transition to IFRS

	Investment changes (Note 1) £m	Insurance changes (Note 2) £m	Employee benefits (Note 3) £m	Goodwill (Note 4) £m	Policyholder tax (Note 5) £m	Other items £m	Total adjustments £m
Operating profit							
Long term business	111	(77)	(27)		(93)	17	(69)
Fund management			(3)				(3)
General insurance and health business		5	(33)				(28)
Non-insurance operations			(3)			(10)	(13)
Corporate costs			(10)				(10)
Unallocated interest charges							-
Unallocated income			28				28
Operating profit before tax attributable to shareholders	**111**	**(72)**	**(48)**	**-**	**(93)**	**7**	**(95)**
Amortisation/ impairment of goodwill				79			79
Amortisation of AVIF and other intangibles					37	(3)	34
Financial Services Compensation Scheme and other levies							-
Short-term investment fluctuation	(67)						(67)
Change in equalisation provision		23					23
Net loss of the disposal of subsidiary and associated undertakings				169		1	170
Exceptional costs for termination of operations						10	10
Profit before tax attributable to shareholders profits	**44**	**(49)**	**(48)**	**248**	**(56)**	**15**	**154**
Tax attributable to shareholders' profits		(7)	15	-	56	20	84
Profit for the year	**44**	**(56)**	**(33)**	**248**	**-**	**35**	**238**

Summarised consolidated statement of recognised income and expense
For the year ended 31 December 2004

	IFRS 2004 £m
Fair value gains, net of transfers to the profit and loss account	161
Actuarial gains and losses on pension schemes	(145)
Foreign exchange rate movements	57
Aggregate tax effect – shareholder tax	(15)
Net income recognised directly in equity	**58**
Profit for the year	1,371
Total recognised income and expense for the year	**1,429**

Summarised consolidated statement of changes in equity
For the year ended 31 December 2004

	IFRS 2004 £m
Total equity at 31 December 2003	**7,024**
Total recognised income and expense for the year	1,429
Dividend and appropriations for the year	(570)
Movement in shares held by employee trusts	1
Increase in share capital	25
Issue of Direct Capital Instrument	990
Issue costs of Direct Capital Instrument	(9)
Shares issued in lieu of dividends	103
Total equity	**8,993**
Minority interests	(910)
Equity attributable to shareholders	**8,083**

Notes to the Analysis of adjustments to the pro forma operating profit statement for the year ended 31 December 2004 as a result of the transition to IFRS

Note 1: Investment valuation

The main investment valuation change upon conversion to IFRS is that assets, which are not classified as being held to maturity, are required to be held at fair value. Under UK GAAP certain of the Group's bonds were held at amortised cost. This change in valuation of debt securities resulted in a £2,459 million increase in the valuation of securities at 31 December 2004. Most of this change was offset by corresponding movements in the unallocated divisible surplus and technical liabilities. However, there was a residual uplift which resulted in a positive increase in the Group's shareholders' funds and the year on year movement in respect of those investments classified as "at fair value through profit and loss account" is reported as increased profits in the 2004 income statement

In addition changes to investment accounting have resulted in £67 million of investment gains being reclassified from short term fluctuations to the life operating profit.

Note 2: Insurance liabilities

Insurance changes consist of:

- The removal of the claims equalisation provision, improving profit before tax by £23 million but with no impact on operating profit;
- The revaluation of liabilities and deferred acquisition costs on those contracts classified as non-participating investment contracts reducing operating profit by £91 million;
- The revaluation of certain life reinsurance treaties, increasing operating profit by £14 million;
- Other sundry changes to our general insurance business reserves increasing operating profit in 2004 by £5 million.

Of these changes the most significant impact occurs on our UK Life business where profit falls by £90 million as a result of the adoption of IAS 39. On the basis of 2004 gross written premiums, 44% of our total life business within the UK is classified as non-participating investment contracts and includes unit linked bonds and unit-linked pension contracts. IAS 39 reduces the level of deferred acquisition costs that can be recognised as well as requiring the removal from technical provisions of positive or negative non-unit reserves determined on the local valuation basis held over and above the unit fund value. The effect of these changes is that the profits on a non-participating investment contract will arise later in the contract term under IFRS than under UK GAAP.

The overall impact on annual profits arising from this accounting change is dependent upon levels of new business, product mixes, the ageing profile of the existing in-force business and reserving policies. Additional new business strain under IFRS would be expected to be mitigated by the emergence of higher IFRS basis profits of the in-force book of business. Until mid 2003, unit linked bond business sold by Norwich Union in the UK contained a guaranteed minimum death benefit and hence contained significant insurance risk, and, accordingly, as permitted by IFRS Phase 1, the UK GAAP basis profit profile has been retained. After mid 2003 this benefit was removed and business written since this time has been classified as non-participating investment business. The existing in-force business is therefore small and profits are insufficient to offset the new business strain. Therefore a significant conversion effect on profit arises.

This reduction in profit is no more than a timing adjustment. Aviva's main value measure remains European embedded value and the profit arising on this basis is unaffected by this technical accounting change.

Note 3: Employee benefits

The overall impact of adopting IAS 19 *Employee benefits* and IFRS 2 *Share based compensation* has been to increase costs by £48 million in 2004. The increase in costs partly reflects the fact that IAS 19 has used a more current actuarial valuation to measure the ongoing pension service cost. The charge under UK GAAP was based on the SSAP 24 valuation which, as disclosed in the 2004 Report & Accounts, was last updated for financial reporting purposes in April 2002.

Note 4: Goodwill

Goodwill is no longer amortised under IFRS but is subject to annual impairment review. There were £41 million of impairment charges incurred in 2004 relating to sundry small overseas businesses, which had been fully reflected within the UK GAAP amortisation charge of £120 million. No additional impairment arose as a result of the transition to IFRS.

A further £169 million credit arises to profit before tax, as goodwill previously charged directly to reserves was deducted from profit upon disposal of subsidiaries under UK GAAP. Under IFRS no such deduction is required. This change has no impact on operating profit or shareholders' funds.

Note 5: Policyholder tax

Operating profit before tax has fallen relative to MSSB by £93 million as a result of a change in the allocation of the tax charged to the life funds between policyholders and shareholders. This presentational change has no impact on operating profit after tax or the tax suffered by the life funds but merely represents how the tax charge is presented in the financial statements. The increase in tax costs charged to operating profit arises principally in the UK, but has been partly offset by a change in allocation in the Netherlands, where all tax is now deemed to be shareholder tax.

It is a feature of the UK tax regime that the tax attributable to life business operations is a single charge in respect of policyholder income and shareholder profits. Under UK GAAP, the difficulty of allocating this charge between policyholders and shareholders is generally acknowledged and hence, under UK GAAP, the total tax charge is deducted from life operating profit in the long-term technical account, the net result of which is then grossed up at the effective shareholder tax rate. Traditionally, Aviva has grossed up at 30% which represents its view of the long term effective rate. We remain of the view that this will be the rate suffered by shareholders over the longer term.

Under IFRS, all taxation must be reported within the taxation line. The profit before this total tax would presents a misleading picture of the group's profit as (i) much of the policyholder tax is in the with-profits funds where the Fund for Future Appropriations is adjusted on a net of tax basis; (ii) the cost of policyholder tax is priced into the relevant products and (iii) the level of tax will vary on an annual basis in line with the investment return on assets backing the long-term funds.

Therefore the UK industry has agreed that it is appropriate to adopt an income statement presentation which depicts profit before tax attributable to the shareholders. This requires an allocation of the total tax charge between policyholders and shareholders, with the policyholder charge being offset against operating profit. There is no universal view on how this allocation should be performed. Aviva has taken the view that the IFRS conceptual framework does not permit companies to use notional allocation or gross-up methods. Instead, the allocation to policyholder tax should reflect the actual tax payable at policyholder rates, including deferred tax. Aviva has therefore developed a conceptual methodology to achieve this consistently year on year.

In 2004 the level of tax attributed to the shareholders was reduced by the following arrangement. The £1.5 billion of capital injected into the life funds on the demutualisation of Norwich Union in 1997 had the effect that future distributions up to that amount by Norwich Union Life and Pensions are treated as already having suffered some shareholder tax. In 2004 £107 million representing this company's shareholders' surplus was sheltered by this arrangement and this has the impact of lowering the actual tax paid at shareholder rates. This is a genuine benefit to shareholders and resulted in higher profit after tax. This tax benefit has a finite capacity and we anticipate that it will be substantially exhausted by the end of 2005, such that over the long term there will be an increase in shareholder tax rates back towards 30%. The use of this capacity is dependent on the level of distributions made by Norwich Union Life & Pensions.

The impact of this is that operating profit before tax falls relative to MSSB as the actual shareholder rate suffered in the UK in 2004 was lower than 30%.

It should be noted that from an EEV perspective, an asset is already established representing this tax benefit and so 30% remains as an appropriate shareholder tax rate for this business.

Note 6: Longer term investment return

Aviva has chosen to revisit its longer term investment return ("LTIR") methodology from 2005 as part of a discretionary change not required by IFRS. In order to provide suitable trend analysis the Group has decided to present 2004 comparatives in accordance with this new methodology. The key changes are as follows:

- As highlighted in the 2004 results announcement, for properties and equity, we will apply lower start of year long-term rates of investment return consistent with those adopted for reporting life operating returns under EEV principles. This would have reduced operating profit in 2004 by £25 million;
- For fixed income securities we will include the amortisation of the premium or discount arising upon acquisition of a bond within our LTIR calculation. This has the effect of reducing would have reduced operating profit before tax by £72 million in 2004;
- The LTIR will only be applied to general insurance and health business.

These changes have no effect on profit before tax.

Summarised consolidated balance sheet at 31 December 2004

	UK GAAP as published	Adjustments	IFRS
Assets	**£m**	**£m**	**£m**
Intangible assets			
Goodwill	1,135	49	1,184
Acquired value of in-force business and other intangible assets	451	65	516
	1,586	114	1,700
Property and equipment	283	529	812
Investment property	9,407	1,650	11,057
Investments in joint ventures and associates	2,088	40	2,128
Financial investments and loans	140,763	47,648	188,411
Assets held to cover linked liabilities	51,144	(51,144)	-
Reinsurance assets	7,540	963	8,503
Tax assets	63	845	908
Other assets	16,275	(3,270)	13,005
Cash and cash equivalents	3,121	9,658	12,779
Total assets	232,270	7,033	239,303
Equity			
Share capital	1,760	-	1,760
Capital reserves	3,878	-	3,878
Revaluation and other reserves	-	736	736
Retained earnings	2,682	(973)	1,709
Equity attributable to shareholders' of Aviva plc	8,320	(237)	8,083
Minority interests	924	(14)	910
Total Equity	9,244	(251)	8,993
Liabilities			
Insurance liabilities	195,591	(71,469)	124,122
Liability for investment contracts	-	69,555	69,555
Unallocated divisible surplus	9,218	(1,669)	7,549
Provisions	340	1,785	2,125
Tax liabilities	1,617	848	2,465
Borrowings (including subordinated debt)	4,560	5,530	10,090
Other liabilities	11,700	457	12,157
Net asset value attributable to unitholders	-	2,247	2,247
Total liabilities	223,026	7,284	230,310
Total equity and liabilities	232,270	7,033	239,303

Analysis of adjustments to the balance sheet at 31 December 2004 as a result of the transition to IFRS

Assets	Investment valuation (Note 1) £m	Insurance changes (Note 2) £m	Employee benefits (Note 3) £m	Goodwill (Note 4) £m	Dividend recognition (Note 5) £m	Deferred taxation (Note 6) £m	Borrowings /Cash (Note 7) £m	FRS 27 (Note 8) £m	Other items (Note 9) £m	Total £m
Intangible assets:										
Goodwill				49					-	49
Acquired value of in-force business and other intangible assets				65					-	65
Property and equipment									529	529
Investment property									1,650	1,650
Investments in joint ventures and associates	8			15					17	40
Financial investments and loans	2,599						(3,598)		48,647	47,648
Assets held to cover linked liabilities									(51,144)	(51,144)
Reinsurance assets		(108)						417	654	963
Tax assets						845			-	845
Other assets		(19)	(475)					(13)	(2,763)	(3,270)
Cash and cash equivalents							8,792		866	9,658
Total assets	2,607	(127)	(475)	129	-	845	5,194	404	(1,544)	7,033
Equity										
Share capital									-	-
Capital reserves									-	-
Revaluation and other reserves	736								-	736
Retained earnings	(452)	166	(909)	129	364	(322)	(26)	-	77	(973)
Equity attributable to shareholders' of Aviva plc	284	166	(909)	129	364	(322)	(26)		77	(237)
Minority interests									(14)	(14)
Total Equity	284	166	(909)	129	364	(322)	(26)		63	(251)
Liabilities										
Insurance liabilities	250	(242)	(813)			28		4,226	(74,918)	(71,469)
Liability for investment contracts									69,555	69,555
Unallocated divisible surplus	2,073	(165)				(62)	17	(3,822)	290	(1,669)
Pension obligations and other provisions			1,643						142	1,785
Tax liabilities			(396)			1,201	(4)		47	848
Borrowings (inc. subordinated debt)							5,207		323	5,530
Other liabilities		114			(364)				707	457
Net asset value attributable to unitholders									2,247	2,247
Total liabilities	2,323	(293)	434	-	(364)	1,167	5,220	404	(1,607)	7,284
Total equity and liabilities	2,607	(127)	(475)	129	-	845	5,194	404	(1,544)	7,033

Notes to the analysis of adjustments to the balance sheet as at 31 December 2004 as a result of the transition to IFRS

The UK GAAP balance sheet has been presented in a format consistent with IFRS. The only significant change in heading is that the Fund for Future Appropriations is now renamed the Unallocated Divisible Surplus. The basis for the material adjustments between UK GAAP and IFRS is as follows:

Note 1: Investment valuation

The adjustments in respect of investment valuation arise from the following:

	£m
Increase in valuation of debt securities	2,459
Change in valuation of certain mortgages	119
Other sundry adjustments	21
	2,599

a) Debt securities

Under UK GAAP, equity securities and unit trusts are carried at current value. Debt and other fixed income securities are also carried at current value, with the exception of many non-linked long-term business debt securities and fixed income securities, which are carried at amortised cost.

As a result of applying IAS 39, the Group now carries all investments in debt and equity securities at fair value. The change in valuation of debt securities from amortised cost to fair value increases the valuation of investments by £2,459 million at 31 December 2004. This change in the valuation of debt securities is largely offset by corresponding movements in the unallocated divisible surplus and technical liabilities. The net impact on shareholders' funds at 31 December 2004 is £284 million.

b) Commercial mortgages backing certain annuity business

Under IFRS, the Group has chosen to move certain of its commercial mortgage portfolio to an active fair valuation basis in accordance with IAS 39, which has increased the value of investments by £119 million. The annuity liabilities which are backed by these assets have been correspondingly revalued, reflecting the use of current interest rates. Consequently, there is an insignificant impact on shareholders' funds at 31 December 2004.

Revaluation reserve

Under IFRS, certain investment gains are recorded as a separate component of shareholders' equity, whereas under UK GAAP they would be included in retained earnings.
Separate revaluation reserves are created for:

- Changes in the fair value of securities classified as available for sale:
- Changes in the value of owner-occupied property:
- Exchange differences arising from the translation of the net investment in foreign subsidiaries, associates and joint ventures and from borrowings designated as hedges of such items: and
- Changes in the fair value of derivatives that are designated and qualify as cash flow hedges.

The amounts included in the above reserves are, where appropriate, net of deferred tax and impairment losses.

The above requirements have resulted in a transfer from retained earnings of £736 million into separate revaluation reserves at 31 December 2004.

Note 2: Insurance change

The impact on shareholders' funds of insurance changes is as follows:

	£m
Derecognition of claims equalisation provision	388
Change in valuation of reinsurance treaties	(34)
Application of an active liability valuation basis in the Netherlands	(52)
Change in value of non-participating investment contracts and other sundry items	(136)
	166

The principal changes to the Group's insurance accounting upon transition to IFRS are discussed further below.

a) Product classification

International Financial Reporting Standard 4, *Insurance Contracts* (IFRS4) requires all products issued to be classified for accounting purposes into either insurance or investment contracts, depending on whether significant insurance risk exists. In the case of a life contract, insurance risk exists if the amount payable on death differs from the amount payable if the policyholder survives. The Group has deemed insurance risk to be significant if the difference exceeds 5% of the policy value, though the classification would be similar if a 10% test had been used.

Following a detailed review, 59% of life policy reserves on an MSSB basis at 31 December 2004 have been classified as insurance and 24% have been classified as participating investment contracts (being those investment contracts containing a discretionary participating features as defined within IFRS4) and both classes will continue to be accounted for under the Group's existing accounting policies. The remaining 17% have been classified as non-participating investment contracts and therefore are required to be accounted for under IAS39 and International Accounting Standard 18 – *Revenue* (IAS18). Virtually all our general insurance products are classified as insurance.

The product classification change results in technical provisions being allocated between insurance and investment contracts. As described in note 9, the "other" column includes £69,555 million of liabilities classified as investment contracts.

b) Equalisation provision

An equalisation provision is recorded in the balance sheet of individual general insurance companies in the UK and in a limited number of other countries, to eliminate, or reduce, the volatility in incurred claims arising from exceptional levels of claims in certain classes of business. The provision is required by law even though no actual liability exists at the balance sheet date and is included in the UK GAAP consolidated balance sheet. The annual change in the equalisation provision is recorded in the UK GAAP profit and loss account. Under IFRS, no equalisation provision is recorded, as no actual liability exists at the balance sheet date. There is an increase of £388 million in shareholders' funds as a result of the removal of the equalisation provision.

c) Reinsurance treaties

Following a full review of all our reinsurance contracts, a small number of the Group's reinsurance treaties have been revalued under IFRS, leading to a reduction in the value of reinsurance assets of £108 million. The majority of these changes relate to participating contracts and so these value changes affect principally the unallocated divisible surplus rather than shareholders' funds.

d) Application of an active liability valuation basis in the Netherlands

The conversion to IFRS has been a particular issue in the Dutch industry where traditionally both bond investments and associated insurance liabilities have been held at amortised cost. IAS 39 requires bonds to be held at fair value and hence to prevent an equity mis-match, the Group has chosen to move to a more active liability valuation basis for its insurance liabilities within the Netherlands. Gross liabilities increased by £213 million as a result of this change at 31 December 2004.

Having applied an active basis for valuing liabilities on traditional gross and individual savings business, the amount representing undistributed gains on investments backing these products, which were previously booked to the fund for future appropriations under UK GAAP, of £161 million has been released to equity.

e) Non-participating investment contracts and other sundry items

The liability for those contracts classified as non-participating investment contracts is valued in accordance with IAS 39. The majority of the Group's contracts classified as non-participating investment contracts are unit-linked contracts and have been valued at fair value. For unit-linked contracts the fair value liability is deemed to equal the current unit fund value, plus positive non-unit reserves if required on a fair value basis. This replaces the reserve held under UK GAAP which equals the unit fund value plus any positive or negative non-unit reserves determined on the local valuation basis, which differs from that required on a fair value basis.

In addition to the change in liability valuation, the accounting for deferred acquisition costs has been revised in accordance with IAS18. This restricts the types of acquisition costs that can be deferred leading to a reduction in deferred acquisition costs as compared to UK GAAP.

The net impact on shareholders' funds of the above changes and of other sundry items is £136 million.

In addition to the above, IFRS now requires that any front end fees received on non-participating investment contracts are included within an explicit deferred income reserve within creditors. Under UK GAAP, any deferred acquisition cost asset created would have been net of these fees. This has led to an increase in "Other assets" and "Other liabilities" of £114 million.

Note 3: Employee benefits

Under the Group's UK GAAP pension policy, as set out in Statement of Standard Accounting Practice, *Accounting for Pensions Cost* (SSAP24), the cost of providing pension benefits is expensed using actuarial valuation methods which gives a substantially even charge over the expected service lives of employees and results in either a prepayment or an accrual to the extent that this charge does not equate to the cash contributions made into the schemes. Under International Accounting Standard 19, *Employee Benefits* (IAS19), the projected benefit obligation is matched against the fair value of the underlying assets and other unrecognised actuarial gains and losses in determining the pension expense for the year. Any pension asset or obligation must be recorded in the balance sheet. Aviva has not applied the "corridor approach" to valuing pension deficits.

This change in accounting has resulted in the removal of the Group's SSAP24 balances, a net debtor of £279 million, after allowing for deferred tax, at 31 December 2004 and the recognition of a deficit of £630 million, net of deferred tax, valued in accordance with IAS19. This gives an overall impact on shareholders' funds of £909 million at 31 December 2004.

The Group has assumed that substantially all of the pension deficit will fall to be borne by the shareholders. This is particularly relevant to the UK pension scheme deficit, which forms the majority of the deficit recognised by the Group. Costs, including pension costs, are charged to the UK Life companies and with-profits funds on the basis of a pre-determined Management Services Agreement (MSA). As reported at the time of the conversion to EEV, where similar assumptions have been made in connection with deficit funding, under the MSA, NU Life Services Ltd can renegotiate the terms relating to the recharging of the costs to the UK with profits funds in 2008, subject to regulatory approval. In evaluating the impact on IFRS, Aviva has not sought to pre-empt the outcome of this renegotiation. Any changes to the recharges in respect of the pension deficit will be credited to equity in the period agreement is obtained.

In some countries, the pension schemes have invested in the Group's Life funds. IAS 19 requires the liquidity of the scheme's assets to be considered and if these are non-transferable, the presentation of the total obligation to the scheme must include these amounts.

The Group has chosen to review its presentation of these investments. Non-transferable obligations to staff pension schemes included within technical provisions under UK GAAP are deducted from Insurance liabilities and included within Provisions under IFRS. At 31 December 2004, the amount described as Provisions on the balance sheet comprises the following amounts:

	£m
Deficit in the Staff pension scheme	893
Other obligations to staff pension schemes –Insurance policies issued by Group companies	813
Total IAS 19 obligations to staff pensions schemes	1,706
Other provisions	419
	2,125

Note 4: Goodwill / Other intangibles

Under IAS 36, *Impairment of Assets*, goodwill is no longer amortised but is tested for impairment, at least annually. Any goodwill amortised prior to the date of transition (1 January 2004) or, for goodwill arising before 1 January 1998, eliminated against shareholders' funds has not been reinstated. Amortisation charged in 2004 under UK GAAP is not charged to profit under IFRS to the extent that it does not relate to an impairment and hence shareholders' funds upon conversion to IFRS increase. In addition, negative goodwill of £37 million at 31 December 2004 previously recognised under UK GAAP is included directly in retained earnings.

IFRS 3 *Business combinations* requires that intangible assets such as customers lists, which can be separately identified and valued, must be recognised separately in the balance sheet. The Group has applied IFRS 3 to acquisitions since 1 January 2004, which has resulted in £65 million of goodwill being reclassified as other intangibles upon conversion to IFRS.

Note 5: Dividend recognition

Under UK GAAP, dividends are accrued in the period to which they relate regardless of when they are declared and approved. Under IAS10, *Events after the Balance Sheet Date*, shareholders' dividends are accrued only when declared and appropriately approved. This has increased shareholders' funds by £364 million.

Note 6: Deferred taxes

Under UK GAAP, provision is made for deferred tax assets and liabilities, using the liability method, arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. No provision is made for tax that might arise on undistributed earnings of subsidiaries unless a binding agreement for distribution exists. Deferred tax is recognised as a liability or asset if the transactions or events that give the entity an obligation to pay more tax in future or a right to pay less tax in future have occurred by the balance sheet date. The Group policy is to discount its deferred tax balances.

Under International Accounting Standard 12, *Income taxes* (IAS12), deferred taxes are provided under the liability method for all relevant temporary differences, being the difference between the carrying amount of an asset or liability in the balance sheet and its value for tax purposes. IAS 12 does not require all temporary differences to be provided for, in particular the Group does not provide for deferred tax on undistributed earnings of subsidiaries where the Group is able to control the timing of the distribution and the temporary difference created is not expected to reverse in the foreseeable future. Deferred tax assets are recognised for unused tax losses and other deductible temporary differences to the extent that it is probable that future taxable profit will be utilised against the unused tax losses and credits. Discounting is prohibited under IAS12.

The changes to deferred tax arise from the removal of discounting, changes to the valuation of the Group's assets and liabilities under IFRS and presentational changes to disclosure of tax assets and liabilities. The main net increases in deferred tax at 31 December 2004 that reduce shareholders' funds are:

	£m
Reversal of discounting (the total discounting applied to UK GAAP deferred tax liabilities was £277 million, of which £215 million relates to non-life and shareholders' interests)	215
Deferred tax impact of the removal of the equalisation provision	117
Deferred tax impact of other changes to technical provisions, valuation of investments and other sundry adjustments	(10)
Net decrease to shareholders' funds	322

Note 7: Borrowings and cash

IFRS requires a number of presentational changes to borrowings and cash. The most significant change is that the linked presentation can no longer be adopted for the Group's borrowing securitised on certain of its mortgage portfolios. This increases borrowings and investments by £5,110 million. The equity impact of £26 million relates to the use of the fair value option to mortgages of the UK equity release business, the loan notes which are securitised upon them and backing derivatives. This has increased borrowings by £97 million. Additionally, £8,792 million of the Group's investments meet the definition of cash equivalents and so have been reclassified to "cash and cash equivalents".

Note 8: FRS 27 Life Assurance

In December 2004, the UK's Accounting Standards Board (ASB) issued Financial Reporting Standard 27, *Life Assurance* (FRS27).In accordance with the Memorandum of Understanding (MoU) signed by the Group along with other major insurance companies, the Association of British Insurers (ABI) and the ASB, the Group has adopted FRS 27 in its 2004 IFRS balance sheet. FRS 27 requires insurance companies to measure their liabilities on with-profit business, on a "realistic basis" (i.e. the FSA's definition of a 'realistic' valuation.). The use of the 'realistic' basis to measure liabilities for with-profit business does not impact reported profits, as an offsetting adjustment is made to the fund for future appropriations ("FFA").

Note 9: Other items

The other changes that arise as a result of the transition to IFRS are principally reclassifications and presentational changes. The total effect of the other changes to shareholders' funds is £77 million.

The other significant reclassification and presentational changes which have no impact on shareholders' funds are:

- Assets held to cover linked liabilities of £51,144 million are no longer disclosed in a single line but have been reported in the various asset classifications. Of this amount assets of £4,965 million have been netted off technical liabilities, reducing the gross assets and investment contract liabilities of the Group. There is no impact on profit or shareholders' funds as a result of this change.
- Technical provisions are disclosed as either insurance contracts or investment contracts, reflecting the product classification included in Note 2(a). The Group held investment contracts of £69,555 million at 31 December 2004.
- The assets and liabilities of the banking business are no longer disclosed entirely in "other debtors" and "other creditors" but have been reported in the appropriate balance sheet classifications.
- Owner occupied properties have been reclassified from "investment property" to property and equipment. We continue to hold these properties at fair value.
- Mutual funds have been consolidated as these vehicles meet the definition of a subsidiary. This has resulted in an increase in gross assets of £ 2,247 million, representing the part of the funds owned by third parties. This third party interest is recorded in the line "net assets attributable to unitholders" within liabilities. The consolidation of mutual funds has no impact on shareholders' funds or profit after tax.

Summarised consolidated profit and loss account – EEV basis
For the year ended 31 December 2004

	Year ended 31 December 2004		
	Previously published £m	**Restated for IFRS £m**	**Restated for IFRS and LTIR changes[1] £m**
Operating profit			
Life EEV operating return	1,611	1,611	1,611
Fund management [2]	23	20	20
General insurance and health	1,384	1,356	1,259
Non-insurance operations [3]	(31)	(41)	(41)
Corporate costs	(178)	(188)	(188)
Unallocated interest charges	(465)	(465)	(465)
Centre unallocated income	-	28	28
Operating profit from continuing operations before tax	**2,344**	**2,321**	**2,224**
Amortisation/Impairment of goodwill	(120)	(41)	(41)
Amortisation and impairment of other intangibles	-	(3)	(3)
Financial Services Compensation Scheme and other levies	(49)	(49)	(49)
Variation from longer-term investment return	565	565	662
Effect of economic assumption changes	(318)	(318)	(318)
Change in the equalisation provision	(23)	-	-
Net profit/(loss) on the disposal of subsidiary and associated undertakings	(136)	34	34
Exceptional costs for termination of operations	(50)	(40)	(40)
Profit before tax	**2,213**	**2,469**	**2,469**
Tax on operating profit from continuing operations	(651)	(647)	(618)
Tax on profit/(loss) on other activities	4	(3)	(32)
Profit after tax from continuing operations	**1,566**	**1,819**	**1,819**
Minority interests	(166)	(178)	(178)
Profit for the year	**1,400**	**1,641**	**1,641**
Earnings per share based on operating profit after tax attributable to ordinary shareholders	67.2p	65.8p	62.8p
Earnings per share based on profit after tax attributable to ordinary shareholders	61.0p	71.7p	71.7p
Net asset value per share	532p	511p	511p
Return on capital employed	14.4%	14.3%	13.6%

Summarised consolidated balance sheet – EEV basis
As at 31 December 2004

	Restated 2004 £m	**Restated 2003 £m**
Total assets	244,321	218,208
Equity attributable to shareholders of Aviva plc	11,661	10,388
Non-equity: preference shares and direct capital instrument	1,190	200
Minority interests	1,160	946
Total equity	14,011	11,534
Total liabilities	230,310	206,674

[1] The Group has decided to adopt from 2005, as a discretionary change of policy that is not required by IFRS, a change in rates and methodology in the calculation of LTIR as it applies to its general insurance and health business.

[2] Excludes the proportion of the results of Morley's fund management businesses and of our French asset management operation Aviva Gestion d'Actifs (AGA) that arise from the provision of fund management services to our life businesses. These results are included within the life EEV operating return.

[3] Excludes the results of Norwich Union Equity Release (NUER). Also excludes the proportion of the results of Norwich Union Life Services relating to the services provided to the UK life business. These results are included within the life EEV operating return. Other subsidiaries providing services to our life businesses do not significantly impact the Group results.

IFRS accounting policies

Aviva plc (the "Company"), a public limited company incorporated and domiciled in the United Kingdom (UK), together with its subsidiaries (collectively, the "Group" or "Aviva") transacts life assurance and long-term savings business, fund management, and most classes of general insurance and health business through its subsidiaries, associates and branches in the UK, Ireland, Continental Europe, United States (US), Canada, Asia, Australia and other countries throughout the world. The Group also invests in securities, properties, mortgages and loans and carries on the business of trading in property.

The Group is managed using reportable segments based on the above activities. These are long-term business, fund management, general insurance and health.

The principal accounting policies adopted in the preparation of these financial statements are set out below.

(A) Basis of presentation

From 2005, all European Union listed companies are required to prepare their consolidated financial statements using standards issued by the International Accounting Standards Board (IASB). The preliminary IFRS financial statements of the Group for the year ended 31 December 2004 have been prepared using the accounting policies set out below, which are in accordance with IFRS issued by the IASB. The European Union has endorsed all relevant IFRS with the exception of the amendment to IAS 19 *Employee Benefits* published by the IASB in December 2004 and amendments published to IAS39 *The Fair Value Option* published by the IASB in June 2005.

Both these amendments are expected to be endorsed by the European Commission during 2005 and, although they are not mandatory until 2006, the Group has decided to adopt them early. The Group's interim results and full year financial statements at 31 December 2005 will be prepared in accordance with these endorsed IFRS and this announcement reflects the accounting policies the directors expect to apply at the year end. The IFRSs themselves are subject to possible amendment by interpretative guidance from the IASB or external bodies and are therefore subject to change prior to publication of the Group's full year financial statements for the year ended 31 December 2005 in March 2006.

In accordance with the standard for Phase I of insurance contracts (IFRS 4), the Group has applied existing accounting practices for insurance and participating investment contracts, modified as appropriate to comply with the IFRS framework and applicable standards. Further details are given in policy E below.

This is the Group's first set of financial results prepared in accordance with IFRS accounting policies and its previously reported 2004 consolidated financial statements have accordingly been restated to comply with IFRS. The principal effects of the adoption of IFRS have been reflected within pages 4 to 16.

Items included in the financial statements of each of the Group's entities are measured in the currency of the primary economic environment in which that entity operates (the "functional currency"). The consolidated financial statements are stated in sterling, which is the Company's functional and presentation currency.

(B) Use of estimates

The preparation of financial statements requires the Group to make estimates and assumptions that 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 facts, circumstances and to, some extent, future events and actions, actual results ultimately may differ from those estimates, possibly significantly.

(C) Consolidation principles

Subsidiaries

Subsidiaries are those entities (including Special Purpose Entities) in which the Group, directly or indirectly, has power to exercise control over financial and operating policies in order to gain economic benefits. Subsidiaries are consolidated from the date on which effective control is

transferred to the Group and are excluded from consolidation from the date of disposal. All intragroup transactions, balances and unrealised surpluses and deficits on transactions between Group companies have been eliminated.

From 1 January 2004, the date of first time adoption of IFRS, the Group is required to use the purchase method of accounting to account for the acquisition of subsidiaries. Under this method, the cost of an acquisition is measured as the fair value of assets given up, shares issued or liabilities undertaken at the date of acquisition, plus costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the net assets of the subsidiary acquired is recorded as goodwill (see policy M below). Any surplus of the acquirer's interest in the subsidiary's net assets over the cost of acquisition is credited to the income statement.

Prior to 1 January 2004, certain significant business combinations were accounted for using the "pooling of interests method" (or merger accounting), which treats the merged groups as if they had been combined throughout the current and comparative accounting periods. Merger accounting principles for these combinations have given rise to a merger reserve in the consolidated balance sheet. These transactions have not been restated, as permitted by the IFRS 1 transitional arrangements.

Investment vehicles

Investment vehicles such as OEICs, where a Group company owns more than 50%, are consolidated. The minority interests in such vehicles are classified as liabilities and appear as "Net asset value attributable to unitholders" in the consolidated balance sheet.

Associates and joint ventures

Associates are entities over which the Group has significant influence, but which it does not control. Generally, it is presumed that the Group has significant influence where it has between 20% and 50% of voting rights. Joint ventures are entities whereby the Group and other parties undertake an economic activity, which is subject to joint control arising from a contractual agreement. In a number of these, the Group's share of the underlying assets and liabilities may be greater than 50% but the terms of the relevant agreements make it clear that control is not exercised. Such jointly-controlled entities are referred to as joint ventures in these financial statements.

Gains on transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's interest in the associates and joint ventures. Losses are also eliminated, unless the transaction provides evidence of an impairment of the asset transferred between entities.

Investments in associates and joint ventures are accounted for using the equity method of accounting. Under this method, the cost of the investment in a given associate or joint venture, together with the Group's share of that entity's post-acquisition changes to shareholders' funds, is included as an asset in the consolidated balance sheet. The Group's share of their post-acquisition profits or losses is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in reserves. Equity accounting is discontinued when the Group no longer has significant influence over the investment.

When the Group's share of losses in an associate or joint venture equals or exceeds its interest in the undertaking, the Group does not recognise further losses unless it has incurred obligations or made payments on behalf of the entity.

(D) Foreign currency translation

Income statements and cash flows of foreign entities are translated into the Group's presentation currency at average exchange rates for the year while their balance sheets are translated at the year end exchange rates. Exchange differences arising from the translation of the net investment in foreign subsidiaries, associates and joint ventures, and of borrowings and other currency instruments designated as hedges of such investments, are taken to the currency translation reserve within equity. On disposal of a foreign entity, such exchange differences are transferred out of this reserve and are recognised in the income statement as part of the gain or loss on sale.

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions, and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement.

Translation differences on debt securities and other monetary financial assets measured at fair value are included in foreign exchange gains and losses in the income statement. Translation differences on non-monetary items, such as equities which are held at fair value through profit or loss (see policy R below),are reported as part of the fair value gain or loss, whereas such differences on available-for-sale equities are included in the investment valuation reserve within equity.

(E) Product classification

Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. Contracts can be reclassified as insurance contracts after inception if insurance risk becomes significant. Any contracts not considered to be insurance contracts under IFRS are classified as investment or service contracts.

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

As noted in policy A above, insurance contracts and participating investment contracts in general continue to be measured and accounted for under existing accounting practices at the date of transition to IFRS. However, in certain businesses, the accounting policies have been changed, as permitted by IFRS4, to remeasure designated insurance liabilities to reflect current market interest rates.

Deposits collected under investment contracts without a discretionary participating feature (non-participating investment contracts) are not accounted for through the income statement, except for the investment income attributable to those contracts, but are accounted for directly through the balance sheet as an adjustment to the investment contract liability.

(F) Premiums earned

Premiums on long-term insurance contracts and participating investment contracts are recognised as income when receivable, except for investment-linked premiums which are accounted for when the corresponding liabilities are recognised. For single premium business, this is the date from which the policy is effective. For regular premium contracts, receivables are taken at the date when payments are due. Premiums are shown before deduction of commission and before any sales-based taxes or duties. Where policies lapse due to non-receipt of premiums, then all the related premium income accrued but not received from the date they are deemed to have lapsed is debited to premiums.

General insurance and health premiums written reflect business incepted during the year, and exclude any sales-based taxes or duties. Unearned premiums are those proportions of the premiums written in a year that relate to periods of risk after the balance sheet date. Unearned premiums are computed principally on either a daily or monthly pro rata basis. Premiums collected by intermediaries, but not yet received, are assessed based on estimates from underwriting or past experience, and are included in premiums written.

Non-participating investment contracts have no associated premium income. Fee income on such contracts is covered in policy G below.

(G) Other investment contract fee revenue

Investment contract policyholders are charged fees for mortality, policy administration, investment management, surrenders or other contract services. These fees are recognised as revenue in the period in which they are collected unless they relate to services to be provided in future periods. Amounts are considered to be assessed when the policyholder's balance has been adjusted for those fees. If the fees are for services to be provided in future periods, then they are deferred and recognised as the service is provided.

Initiation and other "front-end" fees (fees that are assessed against the policyholder balance as consideration for origination of the contract) are charged on some non-participating investment and investment fund management contracts. Where the investment contract is recorded at amortised cost, these fees are deferred and recognised over the term of the policy. Where the investment contract is measured at fair value, the front-end fees that relate to the provision of investment management services are deferred and recognised as the services are provided.

(H) Other fee and commission income

Other fee and commission income consists primarily of investment fund management fees, distribution fees from mutual funds, commission revenue from the sale of mutual fund shares, and transfer agent fees for shareholder record keeping. Revenue from investment management fees, distribution fees and transfer agent fees is recognised when earned. Reinsurance commissions receivable and other commission income are recognised on the trade date.

(I) Net investment income

Investment income consists of dividends, interest and rents receivable for the year, movements in amortised cost on debt securities, realised gains and losses, and unrealised gains and losses on FV investments (as defined in policy R). Dividends on equity securities are recorded as revenue on the ex-dividend date. Interest income is recognised as it accrues, taking into account the effective yield on the investment. It includes the interest rate differential on forward foreign exchange contracts. Rental income is recognised on an accruals basis.

The realised gain or loss on disposal of an investment is the difference between the proceeds received, net of transaction costs, and its original cost or amortised cost as appropriate. Unrealised gains and losses represent the difference between the carrying value at the year end and the carrying value at the previous year end or purchase value during the year, less the reversal of previously recognised unrealised gains and losses in respect of disposals made during the year.

The long-term nature of much of the Group's operations means that, for management's decision-making and internal performance management, short-term realised and unrealised investment gains and losses are treated as non-operating items. The Group focuses instead on an operating profit measure that incorporates a longer-term return on investments supporting its general insurance and health business. Total investment income, including realised and unrealised gains, is therefore analysed between that calculated using a longer-term return and short-term fluctuations from this.

(J) Insurance and participating investment contract liabilities

Claims

Long-term business claims reflect the cost of all claims arising during the year, including claims handling costs, as well as policyholder bonuses accrued in anticipation of bonus declarations.

General insurance and health claims incurred include all losses occurring during the year, whether reported or not, related handling costs, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years.

Claims handling costs include internal and external costs incurred in connection with the negotiation and settlement of claims. Internal costs include all direct expenses of the claims department and any part of the general administrative costs directly attributable to the claims function.

Long-term business provisions

Under current IFRS requirements, insurance and participating investment contract liabilities are measured using accounting policies consistent with those adopted previously under existing accounting policies, with the exception of liabilities remeasured to reflect current market interest rates and those relating to UK with-profit contracts. From 31 December 2004, the Group has adopted FRS 27 *Life Assurance* for liabilities relating to such contracts, FRS 27 adds to the requirements of IFRS but does not vary them in any way. Accounting for insurance contracts is determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers in November 2003.

Within FRS 27, the UK's Accounting Standards Board acknowledged the difficulty in applying the requirements retrospectively and it is the Group's view that it would be impractical to do so in accordance with IAS 8. Therefore, only the balance sheet at 31 December 2004 has been restated for the impact of FRS 27. This has no impact on net assets or profit for the year ended 31 December 2004, as the adjustments reflect changes in balance sheet presentation between the unallocated divisible surplus and insurance liabilities. No adjustments have been made to the balance sheet at 1 January 2004 or the income statement for the year ended 31 December 2004.

The long-term business provisions are calculated separately for each life operation, based on local regulatory requirements and actuarial principles consistent with those applied in the UK.

Each calculation represents a determination within a range of possible outcomes, where the assumptions used in the calculations depend on the circumstances prevailing in each life operation. [For liabilities of the UK with-profit fund, FRS 27 requires liabilities to be calculated as the realistic basis liabilities as set out by the UK's Financial Services Authority, adjusted to remove the shareholders' share of future bonuses.]

The liability in respect of guaranteed benefits for participating insurance contracts overseas is calculated in accordance with local actuarial principles, using a deterministic approach and a prudent set of valuation assumptions.

Present value of future profits (PVFP) on non-participating business written in a with-profit fund

For with-profit life funds falling within the scope of the FSA realistic capital regime, and hence FRS 27, an amount may be recognised for the present value of future profits on non-participating business written in a with-profit fund where the determination of the realistic value of liabilities in that with-profit fund takes account, directly or indirectly, of this value. This amount is recognised as a reduction in the liability rather than as an asset on the balance sheet, and is then apportioned between the amounts that have been taken into account in the measurement of liabilities and other amounts which are shown as an adjustment the unallocated divisible surplus.

Unallocated divisible surplus

In certain participating long-term insurance and investment business, the nature of the policy benefits is such that the division between shareholder reserves and policyholder liabilities is uncertain. Amounts whose allocation either to policyholders or shareholders has not been determined by the end of the financial year are held within liabilities as an unallocated divisible surplus.

General insurance and heath provisions

(i) Outstanding claims provisions

General insurance and health outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related claims handling costs. Significant delays are experienced in the notification and settlement of certain types of general insurance claims, particularly in respect of liability business, including environmental and pollution exposures, the ultimate cost of which cannot be known with certainty at the balance sheet date. Provisions for certain claims are discounted, using rates having regard to the returns generated by the assets supporting the liabilities. Any estimate represents a determination within a range of possible outcomes.

Outstanding claims provisions are valued net of an allowance for expected future recoveries. Recoveries include non-insurance assets that have been acquired by exercising rights to salvage and subrogation under the terms of insurance contracts.

(ii) Provision for unearned premiums

The proportion of written premiums, gross of commission payable to intermediaries, attributable to subsequent periods is deferred as a provision for unearned premiums. The change in this provision is taken to the income statement in order that revenue is recognised over the period of risk.

(iii) Liability adequacy

At each reporting date, the Group reviews its unexpired risks and carries out a liability adequacy test for any overall excess of expected claims and deferred acquisition costs over unearned premiums, using the current estimates of future cash flows under its contracts after taking account of the investment return expected to arise on assets relating to the relevant general business provisions. If these estimates show that the carrying amount of its insurance liabilities (less related deferred acquisition costs and additional value in force) is insufficient in light of the estimated future cash flows, the Group recognises the deficiency in the income statement by setting up a provision in the consolidated balance sheet.

Other assessments and levies

The Group is subject to various periodic insurance-related assessments or guarantee fund levies. Related provisions are established where there is a present obligation (legal or constructive) as a result of a past event. Such amounts are not included within insurance liabilities but are included under "Provisions" in the balance sheet.

(K) Non-participating investment contract liabilities

Claims

For non-participating investment contracts with an account balance, claims reflect the excess of amounts paid over the account balance released.

Provisions

Liabilities for non-participating investment contracts are measured at amortised cost unless previous company regulations permitted a fair valuation of liabilities to be used, such as in the case of unit-linked liabilities. The majority of the Group's contracts classified as non-participating investment contracts are unit-linked contracts and are measured at fair value.

The fair value liability is in principle established through the use of prospective discounted cash-flow techniques. For unit-linked contracts, the fair value liability is equal to the current unit fund value, plus additional non-unit reserves if required on a fair value basis.

Amortised cost is calculated as the fair value of consideration received at the date of initial recognition, less the net effect of principal payments such as transaction costs and front end fees, plus or minus the cumulative amortisation (using the effective interest rate method) of any difference between that initial amount and the maturity value, and less any write-down for surrender payments. The effective interest rate is the one that equates the discounted cash payments to the initial amount. At each reporting date, the amortised cost liability is determined as the value of future best estimate cash flows discounted at the effective interest rate.

(L) Reinsurance

The Group assumes and cedes reinsurance in the normal course of business, with retention limits varying by line of business. Premiums on reinsurance assumed are recognised as revenue in the same manner as they would be if the reinsurance were considered direct business, taking into account the product classification of the reinsured business. The cost of reinsurance related to long-duration contracts is accounted for over the life of the underlying reinsured policies, using assumptions consistent with those used to account for these policies. Gains or losses on buying retroactive reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised. Premiums ceded and claims reimbursed are presented on a gross basis in the consolidated income statement and balance sheet as appropriate.

Reinsurance assets primarily include balances due from both insurance and reinsurance companies for ceded insurance liabilities. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provisions or settled claims associated with the reinsured policies and in accordance with the relevant reinsurance contract.

Reinsurance contracts that principally transfer financial risk are accounted for directly through the balance sheet and are not included in reinsurance assets or liabilities. A deposit asset or liability is recognised, based on the consideration paid or received less any explicitly identified premiums or fees to be retained by the reinsured.

If a reinsurance asset is impaired, the Group reduces the carrying amount accordingly and recognises that impairment loss in the income statement. A reinsurance asset is impaired if there is objective evidence, as a result of an event that occurred after initial recognition of the reinsurance asset, that the Group may not receive all amounts due to it under the terms of the contract, and the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer.

(M) Intangible assets

Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary, associate or joint venture at the date of acquisition. Goodwill on acquisitions prior to 1 January 2004 (the date of transition to IFRS) is carried at its book value (original cost less amortisation) on that date, less any impairment subsequently incurred. Goodwill arising before 1 January 1998 was eliminated against reserves and has not been reinstated. Goodwill arising on the Group's investments in associates and joint ventures since that date is included within the carrying value of these investments.

The carrying amount of goodwill for each cash generating unit is reviewed when circumstances or events indicate that there may be uncertainty over its carrying value, and at least annually. Goodwill is written down for impairment where the recoverable amount is insufficient to support its carrying value.

Under UK GAAP, goodwill previously written off to shareholders' fund is taken back through the profit and loss account when calculating the profit or loss in the event of any subsequent disposal of the underlying investment. There is no requirement for this adjustment under IFRS.

Acquired value of in-force business ("AVIF")

The present value of future profits on a portfolio of long-term insurance and investment contracts, acquired either directly or through the purchase of a subsidiary, is recognised as an intangible asset. If this results from the acquisition of an investment in an associate, the AVIF is held within the carrying amount of that associate. In all cases, the AVIF is amortised over the useful lifetime of the related contracts in the portfolio on a systematic basis. The rate of amortisation is chosen by considering the profile of the additional value of in-force business acquired and the expected depletion in its value. The value of the acquired in-force long-term business is reviewed annually for any impairment in value and any reductions are charged as expenses in the income statement.

Other intangible assets

Other intangibles consist primarily of access to distribution networks and customer lists. These are amortised over their useful lives using the straight-line method. The amortisation charge for the period is included in the income statement under "Other operating expenses".

(N) Property and equipment

Owner-occupied properties are carried at their revalued amounts, which are supported by market evidence, and movements are taken to a separate reserve within equity. When such properties are sold, the accumulated revaluation surpluses are transferred from this reserve to retained earnings. All other items classed as property and equipment within the balance sheet are carried at historical cost less accumulated depreciation.

Investment properties under construction are included within property and equipment until completion, and are stated at cost less provision for any impairment in their values.

Land is not depreciated. No depreciation is provided on owner-occupied properties since such depreciation would be immaterial. Depreciation is calculated on the straight line method to write down the cost of other assets to their residual values over their estimated useful lives as follows:

Properties under construction	No depreciation
Motor vehicles	Three years
Computer equipment	Three to five years
Other assets	Three to five years

Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit.

All borrowing costs are expensed as they are incurred. Repairs and maintenance are charged to the income statement during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the most recently assessed standard of performance of the existing asset will flow to the Group and the renovation replaces an identifiable part of the asset. Major renovations are depreciated over the remaining useful life of the related asset.

(O) Investment property

Investment property is held for long-term rental yields and is not occupied by the Group. Completed investment property is stated at its fair value, which is supported by market evidence, as assessed by qualified external valuers or by local qualified staff of the Group in overseas operations. Changes in fair values are recorded in the income statement within net investment

income.

(P) Impairment of non-financial assets

Property and equipment and other non-financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows.

(Q) Derecognition and offset of financial assets and financial liabilities

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the company has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.
-

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(R) Financial investments

The Group classifies its investments as either financial assets at fair value through profit or loss (FV), available for sale financial assets (AFS), or loans and receivables (see policy T below). The classification depends on the purpose for which the investments were acquired, and is determined by local management at initial recognition. In general, the FV category is used as in most cases, the Group's strategy is to manage its financial investments on a fair value basis. In certain circumstances the fair value category is used where this eliminates an accounting mis-match. The AFS category is used where the relevant life liability (including shareholders' funds) is passively managed and carried at amortised cost.

The FV category has two sub-categories – those that meet the definition as being held for trading and those the Group chooses to designate as FV (referred to in this accounting policy as "other than trading"). Fixed maturities, purchased loans and equity securities, which the Group buys with the intention to resell in the near term (typically between three and six months), are classified as trading. All other securities in the FV category are classified as other than trading.

Purchases and sales of investments are recognised on the trade date**,** which is the date that the Group commits to purchase or sell the assets, at their fair values less transaction costs. Debt securities are initially recorded at their fair value which is taken to be amortised cost, with amortisation credited or charged to the income statement. Investments classified as trading, other than trading and AFS are subsequently carried at fair value. Changes in the fair value of trading and other than trading investments are included in the income statement in the period in which they arise. Changes in the fair value of securities classified as AFS, except for impairment losses and relevant foreign exchange gains and losses, are recorded in a separate investment valuation reserve within equity.

The fair values of investments are based on quoted bid prices or amounts derived from cash flow models. Fair values for unlisted equity securities are estimated using applicable price/earnings or price/cash flow ratios refined to reflect the specific circumstances of the issuer. Equity securities for which fair values cannot be measured reliably are recognised at cost less impairment. When securities classified as AFS are sold or impaired, the accumulated fair value adjustments are transferred out of the investment valuation reserve to the income statement.

Impairment

The Group reviews the carrying value of its investments on a regular basis. If the carrying value of an investment is greater than the recoverable amount, the carrying value is reduced through a

charge to the income statement in the period of decline. The following policies are used to determine the level of any impairment:

Listed AFS securities: The Group performs an objective review of the current financial position and prospects of the issuer on a regular basis, to identify whether any impairment provision is required. This review takes into account the likelihood of the current market price recovering to former levels.

Unlisted AFS securities: The Group considers the current financial position of the issuer and the future prospects in identifying the requirement for an impairment provision.

For both listed and unlisted AFS securities identified as being impaired, the cumulative unrealised net loss previously recognised within the AFS reserve is transferred to realised losses for the year.

Mortgages, investment property and securitised loans: Impairment is measured based on the present value of expected future cash flows discounted at the effective rate of interest of the loan, subject to the fair value of the underlying collateral. When a loan is considered to be impaired, the income statement is charged with the difference between the carrying value and the estimated recoverable amount. Interest income on impaired loans is recognised based on the estimated recoverable amount.

Reversals of impairments are only recognised where the decrease in the impairment can be objectively related to an event occurring after the write down (such as an improvement in the debtor's credit rating), and are not recognised in respect of equity instruments.

(S) Derivative financial instruments and hedging

Derivative financial instruments include foreign exchange contracts, interest rate futures, currency and interest rate swaps, currency and interest rate options (both written and purchased) and other financial instruments that derive their value mainly from underlying interest rates, foreign exchange rates, commodity values or equity instruments. All derivatives are initially recognised in the balance sheet at their fair value, which usually represents their cost. They are subsequently re-measured at their fair value, with the method of recognising movements in this value depending on whether they are designated as hedging instruments and, if so, the nature of the item being hedged. Fair values are obtained from quoted market prices or, if these are not available, by using valuation techniques such as discounted cash flow models or option pricing models. All derivatives are carried as assets when the fair values are positive and as liabilities when the fair values are negative. Premiums paid for derivatives are recorded as an asset on the balance sheet at the date of purchase, representing their fair value at that date.

Derivative contracts may be traded on an exchange or over-the-counter (OTC). Exchange-traded derivatives are standardised and include certain futures and option contracts. OTC derivative contracts are individually negotiated between contracting parties and include forwards, swaps, caps and floors. Derivatives are subject to various risks including market, liquidity and credit risk, similar to those related to the underlying financial instruments.

The notional or contractual amounts associated with derivative financial instruments are not recorded as assets or liabilities on the balance sheet as they do not represent the potential gain or loss associated with such transactions.

Interest rate and currency swaps

Interest rate swaps are contractual agreements between two parties to exchange periodic payments in the same currency, each of which is computed on a different interest date basis, on a specified notional amount. Most interest rate swaps involve the net exchange of payments calculated as the difference between the fixed and floating rate interest payments. Currency swaps, in their simplest form, are contractual agreements that involve the exchange of both periodic and final amounts in two different currencies. Exposure to gain or loss on both types of swap contracts will increase or decrease over their respective lives as a function of maturity dates, interest and foreign exchange rates, and the timing of payments.

Interest rate futures, forwards and options contracts

Interest futures are exchange-traded instruments and represent commitments to purchase or sell a designated security or money market instrument at a specified future date and price. Interest rate forward agreements are OTC where two parties agree on an interest rate and other terms that will become a reference point in determining, in concert with an agreed notional principal amount, a net payment to be made by one party to the other, depending what rate in fact prevails at a future point in time. Interest rate options, which consist primarily of caps and floors, are

interest rate protection instruments that involve the obligation of the seller to pay the buyer an interest rate differential in exchange for a premium paid by the buyer. This differential represents the difference between current rate and an agreed rate applied to a notional amount. Exposure to gain or loss on all interest rate contracts will increase or decrease over their respective lives as interest rates fluctuate.

Foreign exchange contracts

Foreign exchange contracts, which include spot, forward and futures contracts, represent agreements to exchange the currency of one country for the currency of another country at an agreed price and settlement date. Foreign exchange option contracts are similar to interest rate option contracts, except that they are based on currencies, rather than interest rates. Exposure to gain or loss on these contracts will increase or decrease over their respective lives as currency exchange and interest rates fluctuate.

Derivative instruments for hedging

On the date a derivative contract is entered into, the Group designates certain derivatives as either:

1 a hedge of the fair value of a recognised asset or liability (fair value hedge);
2 a hedge of a future cash flow attributable to a recognised asset or liability, a highly probable forecast transaction or a firm commitment (cash flow hedge); or
3 a hedge of a net investment in a foreign operation (net investment hedge).

The Group does not currently have any material fair value hedges.

Hedge accounting is used for derivatives designated in this way, provided certain criteria are met. At the inception of the transaction, the Group documents the relationship between the hedging instrument and the hedged item, as well as the risk management objective and the strategy for undertaking the hedge transaction. The Group also documents its assessment, both at inception and on an ongoing basis, of whether the hedge is expected to be, and has been, highly effective in offsetting the risk in the hedged item.

Changes in the fair value of derivatives that are designated and qualify as net investment or cash flow hedges, and that prove to be highly effective in relation to the hedged risk, are recognised in a separate reserve within equity. Gains and losses accumulated in this reserve are transferred to the income statement on disposal of the relevant investment or occurrence of the cash flow as appropriate.

For a variety of reasons, certain derivative transactions, while providing effective economic hedges under the Group's risk management positions, do not qualify for hedge accounting under the specific IFRS rules and are therefore treated as derivatives held for trading. Their fair value gains and losses are recognised immediately in other trading income.

(T) Loans

Loans with fixed maturities, including policyholder loans, mortgage loans on investment property, securitised mortgages and collateral loans, are recognised when cash is advanced to borrowers. The majority of these loans are carried at their unpaid principal balances and adjusted for amortisation of premium or discount, non-refundable loan fees and related direct costs. These amounts are deferred and amortised over the life of the loan as an adjustment to loan yield using the effective interest rate method. Loans with indefinite future lives are carried at unpaid principal balances or cost.

Certain mortgages, which back long-term business, have been classified at fair value through profit or loss in order to match the movement in those liabilities. These loans are revalued to fair value at each period end, with movements in valuation being taken to the income statement.

To the extent that a loan is uncollectible, it is written off as impaired. Subsequent recoveries are credited to the income statement.

(U) Deferred acquisition costs

The costs directly attributable to the acquisition of new business for insurance and participating investment contracts (excluding those written in the UK) are deferred to the extent that they are expected to be recoverable out of future margins in revenues on these contracts. For participating contracts written in the UK, acquisition costs are not deferred, as the liability for these contracts is calculated in accordance with the FSA's realistic capital regime in accordance with FRS 27. For

non-participating investment and investment fund management contracts, incremental acquisition costs and sales enhancements that are directly attributable to securing an investment management service are also deferred.

Where such business is reinsured, an appropriate proportion of the deferred acquisition costs is attributed to the reinsurer, and is treated as a separate liability.

Long-term business deferred acquisition costs are amortised systematically over a period no longer than that in which they are expected to be recoverable out of these margins. Deferrable acquisition costs for non-participating investment and investment fund management contracts are amortised over the period in which the service is provided. General insurance and health deferred acquisition costs are amortised over the period in which the related revenues are earned. The reinsurers' share of deferred acquisition costs is amortised in the same manner as the underlying asset.

Deferred acquisition costs are reviewed by category of business at the end of each reporting period and are written off where they are no longer considered to be recoverable.

(V) Cash and cash equivalents

Cash and cash equivalents consist of cash at banks and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments with less than 90 days maturity from the date of acquisition. For the purposes of the cash flow statement, cash and cash equivalents also include bank overdrafts, which are included within payables and other financial liabilities on the balance sheet.

(W) Leases

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

(X) Provisions and contingent liabilities

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is 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 more probable than not.

The Group recognises a provision for onerous contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

Contingent liabilities are disclosed if the future obligation is probable and the amount cannot be reasonably estimated.

(Y) Employee benefits

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave and long-service leave as a result of services rendered by employees up to the balance sheet date.

Pension obligations

The Group operates a number of defined benefit and defined contribution plans throughout the world, the assets of which are generally held in separate trustee-administered funds. The pension plans are generally funded by payments from employees and by the relevant Group companies, taking account of the recommendations of qualified actuaries.

For defined benefit plans, the pension costs are assessed using the projected unit credit method**.** Under this method, the cost of providing pensions is charged to the income statement so as to spread the regular cost over the service lives of employees, in accordance with the advice of qualified actuaries. The pension obligation is measured as the present value of the estimated future cash outflows using a discount rate based on market yields for high quality corporate bonds. The resulting pension scheme surplus or deficit appears as an asset or obligation in the consolidated balance sheet. The Group has early adopted the December 2004 amendment to IAS 19, *Employee Benefits*, with the result that all actuarial gains and losses are recognised immediately in equity through the Statement of recognised income and expense.

For defined contribution plans, the Group pays contributions to publicly or privately administered pension plans. Once the contributions have been paid, the Group, as employer, has no further payment obligations. The Group's contributions are charged to the income statement in the year to which they relate and are included in staff costs.

In some countries, the pension schemes have invested in the Group's life funds.

Other post-retirement obligations

Some Group companies provide post-retirement healthcare or other benefits to their retirees. The entitlement to these benefits is usually based on the employee remaining in service up to retirement age and the completion of a minimum service period. None of these schemes is material to the Group. The costs of the Dutch and Canadian schemes are included within those for the defined benefit pension schemes in those countries. For such schemes in other countries, provisions are calculated in line with local regulations, with movements being charged to the income statement within staff costs.

Equity compensation plans

The Group offers share award and option plans over the Company's ordinary shares for certain employees, including a Save As You Earn plan ("SAYE plan").

The Group accounts for options and awards under share equity compensation plans, which were granted after 7 November 2002, until such time as they are fully vested, using the fair value based method of accounting (the "fair value method"). Under this method, the cost of providing equity compensation plans is based on the fair value of the share awards or option plans at date of grant, which is recognised in the income statement over the expected service period of the related employees and credited to the equity compensation reserve, part of shareholders' funds.

Shares purchased by employee share trusts to fund these awards are shown as a deduction from shareholders' funds at their original cost.

When the options are exercised and new shares are issued, the proceeds received, net of any transaction costs, are credited to share capital (par value) and the balance to share premium. Where the shares are already held by employee trusts, the net proceeds are credited to this account, with the difference between cost and proceeds being taken to retained earnings. In both cases, the relevant amount in the equity compensation reserve is then credited to retained earnings.

(Z) Income taxes

The current tax expense is based on the taxable profits for the year, after any adjustments in respect of prior years. Tax, including tax relief for losses if applicable, is allocated over profits before tax and amounts charged or credited to reserves as appropriate.

Provision is made for deferred tax liabilities, or credit taken for deferred tax assets, using the liability method, on all material temporary differences between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

The principal temporary differences arise from depreciation of property and equipment, revaluation of certain financial assets and liabilities including derivative contracts, provisions for pensions and other post-retirement benefits and tax losses carried forward; and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base. The rates enacted or substantively enacted at the balance sheet date are used to determine the deferred tax.

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

Deferred tax is provided on temporary differences arising from investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future.

Deferred taxes are not provided in respect of temporary differences arising from the initial recognition of goodwill or from the initial recognition of an asset or liability in a transaction which is not a business combination and affects neither accounting profit nor taxable profit or loss at the time of the transaction.

Deferred tax related to fair value re-measurement of available-for-sale investments, owner-

occupied properties and other amounts taken directly to equity is recognised in the balance sheet as a deferred tax asset or liability.

In addition to paying tax on shareholders' profits, the Group's life businesses in the UK, Ireland and Australia pay tax on policyholders' investment returns ('policyholder tax') on certain products. The Group has decided to show the amounts of policyholder tax included within total tax to provide a more meaningful measure of the tax the Group pays on its profits. Current policyholder tax is tax paid at policyholder tax rates. Deferred policyholder tax is the tax expected to be paid at policyholder tax rates when temporary differences unwind in future periods. In the proforma reconciliations, operating profit has been calculated after charging policyholder tax.

(AA) Borrowings

Borrowings are recognised initially at their issue proceeds less transaction costs incurred. Subsequently, most borrowings are stated at amortised cost, and any difference between net proceeds and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest rate method. Certain loan notes issued in connection with securitised mortgage portfolios, which are listed on local stock exchanges, are remeasured at their fair value, with any movements being taken to the income statement.

(AB) Share capital and treasury shares

Share issue costs

Incremental external costs directly attributable to the issue of new shares, other than in connection with business combination, are shown in equity as a deduction, net of tax, from the proceeds. Share issue costs incurred directly in connection with a business combination are included in the cost of acquisition.

Dividends

Dividends on ordinary shares are recognised in equity in the period in which they are declared and, for the final dividend, approved by shareholders. Dividends on preference shares are recognised in the period in which they are declared and appropriately approved.

Equity instruments

A financial instrument is treated as equity if:

(i) there is no contractual obligation to deliver cash or other financial assets or to exchange financial assets or liabilities on terms that may be unfavourable; and

(ii) the instrument is a non-derivative that contains no contractual obligation to deliver a variable number of shares or is a derivative that will be settled only by the Group exchanging a fixed amount of cash or other assets for a fixed number of the Group's own equity instruments.

Treasury shares

Where the Company or its subsidiaries purchase the Company's share capital or obtains rights to purchase its share capital, the consideration paid (including any attributable transaction costs net of income taxes) is shown as a deduction from total shareholders' equity. Gains and losses on sales of own shares are charged or credited to the treasury share account in equity.

(AC) Fiduciary activities

Assets and income arising thereon, together with related undertakings to return such assets to customers, are excluded from these financial statements where the Group has no contractual rights in the assets and acts in a fiduciary capacity such as nominee, trustee or agent.

(AD) Earnings per share

Basic earnings per share is calculated by dividing net income available to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding the average number of ordinary shares purchased by the Group and held as treasury shares.

Earnings per share has also been calculated on the operating profit before impairment of goodwill

and other non-operating items, after tax, attributable to ordinary shareholders for continuing operations, as well as on the profit attributable to ordinary shareholders. The directors believe the former earnings per share figure provides a better indication of operating performance.

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

(AE) Discontinued operations or those held for sale

Assets held for disposal as part of operations which are discontinued or held for sale are recorded at the lower of their carrying amount and their fair value, less the estimated cost to sell the assets.

Independent Auditors' Report to Aviva plc on the preliminary IFRS Consolidated Financial Statements for the year ended 31 December 2004

To the Board of Directors of Aviva Plc

We have audited the accompanying preliminary International Financial Reporting Standards ("IFRS") consolidated financial statements of the Group for the year ended 31 December 2004 which comprise the summarised consolidated income statement, summarised consolidated pro forma operating profit statement and analysis of IFRS adjustments to the pro forma operating profit statement as a result of the transition to IFRS, summarised consolidated statement of recognised income and expense and summarised consolidated statement of changes in equity for the year ended 31 December 2004 and the summarised consolidated balance sheet and analysis of adjustments to the balance sheet as a result of the transition to IFRS as at 31 December 2004, together with the related accounting policies note set out on pages 19 to 32.

This report is made solely to the Group in accordance with our engagement letter dated 17 June 2005. Our audit work has been undertaken so that we might state to the Group those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility or liability to anyone other than the Group for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

These preliminary IFRS consolidated financial statements are the responsibility of the Group's directors and have been prepared as part of the Group's conversion to IFRS. They have been prepared in accordance with the basis set out in Note A, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS consolidated financial statements as at 31December 2005.

Our responsibility is to express an independent opinion on the preliminary IFRS consolidated financial statements based on our audit. We read the other information accompanying the preliminary IFRS consolidated financial statements and consider whether it is consistent with the preliminary IFRS consolidated financial statements. This other information comprises the basis of preparation of restated financial information, the summarised consolidated profit and loss account – EEV basis and the summarised consolidated balance sheet – EEV basis. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the preliminary IFRS consolidated financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the preliminary IFRS consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the preliminary IFRS financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the preliminary IFRS consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

Emphasis of matter

Without qualifying our opinion, we draw attention to the fact that Note A explains why there is a possibility that the preliminary IFRS consolidated financial statements may require adjustment before constituting the final IFRS consolidated financial statements. Moreover, we draw attention to the fact that, under IFRSs only a complete set of financial statements with comparative financial information and explanatory notes can provide a fair presentation of the Group's financial position, results of operations and cash flows in accordance with IFRSs.

Opinion

In our opinion, the preliminary IFRS consolidated financial statements for the year ended 31December 2004 have been prepared, in all material respects, in accordance with the basis set out in Note A, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS consolidated financial statements as at 31December 2005.

Ernst & Young LLP
Registered Auditor

London

4 July 2005