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Forward thinking: What does it mean to us and our customers?

At Aviva, we find new ways to deliver more fulfilling futures to our customers, and all our stakeholders. Forward thinking has been our business for 300 years. Today, it expresses our dedication to thinking beyond the immediate and the everyday, to building better tomorrows.

Forward thinking is at the heart of our business. It guides our daily actions, encourages us to look past what limits us now, and determines the steps that will carry us beyond those limits, tomorrow.

Within this report, you will find examples of forward thinking in action. Around the world, Aviva is a market leader in developing innovative new products and services as we seek to anticipate what people need and provide solutions.

Our vision of the future extends to recognising our responsibilities to society. We know that we must limit our impact on the environment in which we operate, for the benefit of future generations.

Richard Harvey
Group chief executive



*For me it's an
overwhelming
sense of
the future
being out there
somewhere*



A new racing challenge

Dee Caffari, supported by Aviva, is the first woman in history to sail single-handed, non-stop, around the world against the prevailing winds and currents.

Not content with one extraordinary record, she now plans to become the first woman to sail solo, non-stop around the world in both directions by competing in the gruelling 2008-09 Vendée Globe.

The inspiration and willpower that Dee embodied in completing the Aviva Challenge in May 2006 – an epic, 178-day journey the “wrong way” around the world – was a masterclass in skill, guts and determination.

She said: “When I was sailing against the winds deep in the Southern Ocean, when the storms seemed endless and the horrific conditions forced me into survival mode, I moved my goalposts closer and focused on getting to the next step, so I constantly felt I was making progress towards the finish line.

“Aviva’s support helped me to discover and define my own future in life, and helped me do my own forward thinking. Aviva is a company that helps you take control of your own destiny.”

Aviva is proud of its continuing partnership with Dee. She is determined to push back the boundaries of her sport and inspires others to do the same in their own lives. Her sustained focus on the future and looking ahead to fresh challenges epitomises our “Forward thinking” campaign.



You can find out more about Dee Caffari's challenges at www.avivaoceanracing.com




Dee Caffari
Record-breaking
yachtswoman



Structure and performance

Aviva is the world's fifth largest insurance group and the largest insurance services provider in the UK. We are one of the leading providers of life and pension products in Europe and are actively growing our long-term savings businesses in Asian markets, Australia and the USA. Our main activities are long-term savings, fund management and general insurance*.

We have premium income and investment sales of £41.5 billion and £364 billion of assets under management. We have 59,000 employees serving over 40 million customers.

UK	Europe	International and Morley
Total sales	Total sales	Total sales
£19,541m (2005: £16,472m)	£17,018m (2005: £15,581m)	£4,905m (2005: £3,841m)
PVNB ^{**} £11,146m	PVNB ^{**} £12,840m	PVNB ^{**} £1,866m
Investment sales £2,455m	Investment sales £891m	Investment sales £1,564m
Net written premiums £5,940m	Net written premiums £3,287m	Net written premiums £1,475m
£19,541m	£17,018m	£4,905m
Main operations	Main operations	Main operations
 	   	 
	Geographic presence	Geographic presence
	France Ireland Italy Netherlands Poland Spain Lithuania Turkey Hungary Czech Republic Romania	Singapore Hong Kong India China Russia Australia USA Canada Sri Lanka
→24-31	→32-41	→42-49
Read more about our performance and future direction on pages 24 to 31 of this report	Read more about our performance and future direction on pages 32 to 41 of this report	Read more about our performance and future direction on pages 42 to 49 of this report

* Typically includes motor, household, creditor, health, commercial motor, commercial property and commercial liability insurance.

** Present value of new business premium (PVNB) is equal to total single premium sales received in the year plus the discounted value of annual premiums expected to be received over the term of new contracts, and is expressed at the point of sale.

Strengths and highlights

We have a balanced portfolio that benefits from diversification of distribution, products and geography

We have achieved strong growth in sales and profits across our worldwide portfolio of businesses

We have completed the purchase of AmerUs in the United States, giving us greater access to the world's largest savings market

We have commenced significant new bancassurance partnerships in Ireland (with Allied Irish Banks) and in India (with Centurion Bank of Punjab)

Our European and International businesses have announced their confidence in achieving average annual sales growth[†] of at least 10% over the next five years, while growing profits[‡] at least as quickly

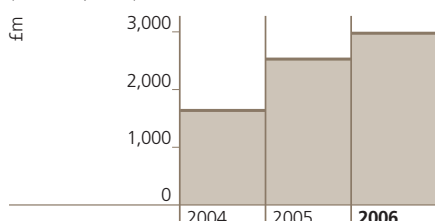
We outlined plans to deliver £250 million of annualised cost savings by the end of 2007 across our UK businesses, at a one-off cost of £250 million

The integration of RAC was completed on time and we met our 2006 cost saving targets

IFRS profit before tax attributable to shareholders

£2,977m

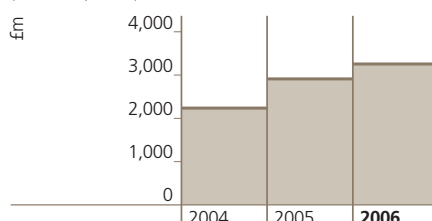
(2005: £2,528m)



EEV operating profit[#]

£3,245m

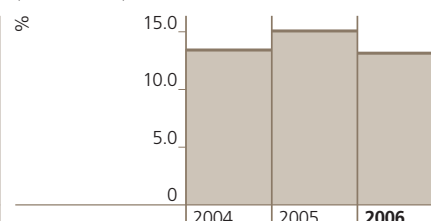
(2005: £2,904m)



Return on equity shareholders' funds[#]

13.1%

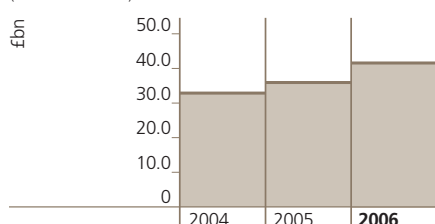
(2005: 15.0%)



Worldwide sales[~]

£41.5bn

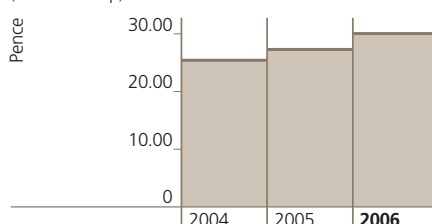
(2005: £35.9bn)



Full year dividend

30.00p

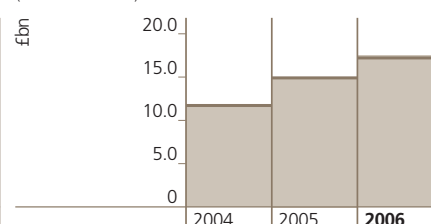
(2005: 27.27p)



Equity shareholders' funds[™]

£17.5bn

(2005: £14.9bn)



[†] Our growth ambition is an annual average growth after minority interests and before acquisitions, from 2006 to 2010 inclusive, and assuming no major changes in economic conditions.

[‡] New business contribution after required capital, tax and minority interest.

[#] From continuing operations, including long-term savings result on a European Embedded Value (EEV) basis before adjusting items.

[~] Return based on opening equity shareholders' funds on an EEV basis.

[™] From continuing operations, including share of associates' premiums.

[™] On an EEV basis.



Getting help when
you need it

Chairman's statement

Dear Shareholder,

As I come to the end of my first year as chairman of Aviva, I am delighted to be able to report on a thriving business. We have made progress towards our stated aim of providing prosperity and peace of mind for our customers. Our record financial results are proof that we are in the right markets, at the right time, and are providing the products and services that our customers want.

During the year, we completed the purchase of AmerUs in the US, giving us greater access to the world's largest savings and capital market. Our challenge is now to integrate and grow this business quickly and to demonstrate the value that we believe it brings to our Group. We also completed major new bancassurance partnerships in Ireland (with Allied Irish Banks) and in India (with Centurion Bank of Punjab). Already, we are seeing strong performances from both partnerships. In March, we approached the board of Prudential plc with a proposal to merge our respective companies on an agreed basis. The proposal set out the significant commercial benefits and value-creation potential of the merger. The board of Prudential plc declined to enter into discussions with us and the proposal was consequently withdrawn.

External view

Across the world, the need for individuals to provide adequately for their retirement is being recognised as an increasingly important issue. The situation is particularly severe in Western countries where an ageing population is placing a greater strain on national purses and we are shortly to see the retirement of the "baby boomer" generation. Additionally, people in rapidly developing countries such as China and India are starting to pick up the savings habit. These conditions present a sizeable opportunity for us, and we are fully committed to working with customers, governments, the insurance industry and regulatory bodies to provide innovative and practical solutions.

Richard Harvey

In January 2007, Richard Harvey announced his intention to retire as our group chief executive and to move on to other charitable and business challenges. Richard is a class act by anyone's standards. He has led the Group through numerous challenges and merger activity with professionalism, skill, and foresight. He has made a lasting impression on Aviva and on the wider international insurance industry. I wish him an enjoyable and relaxing break when he leaves us in July, and great success with whatever he chooses to do next. Furthermore, I am delighted that Andrew Moss, our group finance director has agreed to succeed Richard. Andrew has an extensive knowledge of the insurance industry and a strong track record in international financial services. I am looking forward to working with him as he leads Aviva through its next phase of growth.

Legal reforms

I have recently been involved with the development of the Companies Act 2006 and its progress through Parliament in the UK. The Bill is one of the largest ever to be passed and is a significant step towards a far-reaching reform of UK company law. It clarifies the requirements being placed on public companies and pushes them to consider further their internal governance and their social and economic impacts. I strongly support the reforms and am certain that Aviva is in excellent shape to handle the upcoming changes.

Dividend

I am pleased to announce that our recommended final ordinary dividend is 19.18 pence per share, bringing the total dividend for the year to 30.00 pence, an increase of 10% against last year (2005: 27.27 pence). This increase reflects our intention to increase the dividend on a basis judged prudent, while retaining capital to support future business growth, using dividend cover on an IFRS operating earnings after tax basis in the 1.5 to 2.0 times range as a guide.

Board developments

During 2006, we held the first meetings of the newly formed risk and regulatory committee and corporate social responsibility committee. The board remains committed to maintaining the highest levels of governance and compliance particularly in light of the increasing demands in this area. We are also keenly aware of the need to develop our business to be sustainable and responsive to the needs of customers, staff and the wider community. Both committees will provide clear leadership and give the board oversight of the work we are

doing in these areas. In September, we met in India, and combined the meeting with visits to some of our key sites there and in Sri Lanka. It is important that, as a board, we speak directly to people in our business, and see first-hand the exciting developments that are going on. This particular visit gave us a valuable insight into one of the fastest-growing insurance markets in the world, and the excellent work being performed by our people.

Employees

I would like to thank our employees for their hard work and commitment in helping to deliver an excellent set of results. This admirable performance comes against the backdrop of the reduction in the number of UK staff we announced as part of our cost-efficiency programme. During 2006, we made progress in aligning the remuneration of our senior management with the needs of employees and customers. For the first time this year, an element of senior management pay and bonuses will be dependent on employee engagement and customer satisfaction measures, helping to acknowledge that the longer term performance of Aviva depends on motivated staff and satisfied customers.

It was very pleasing to see that Aviva has been recognised as one of the top 50 best places for women to work in the UK, according to *The Times*. Particularly satisfying for me was that we were the only company to be named in each of the assessed categories, emphasising our progressive approach.

Recognition

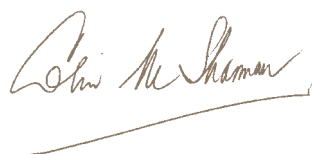
We have earned awards in a large number of our businesses across Europe, Asia and North America. The recognition has come in areas such as product innovation, sustainability, fund performance, diversity, customer satisfaction, media campaigns and many more. The sheer breadth of this recognition demonstrates to me that across the group we are performing to a high level and pushing ourselves to be the best.

Outlook

We are in a great position and our businesses around the world are performing strongly. We have a diverse geographic spread and multiple product types and distribution channels in our core markets. This balance, particularly the split between long-term savings and general insurance, is a significant advantage as it allows us to be flexible and to fund organic growth internally. When allied to the external market environment and the increasing need for higher retirement savings, it is clear that we have a significant opportunity ahead of us.

2006 has been a year of considerable progress and I fully expect these positive trends to continue through 2007.

Lord Sharman of Redlynch OBE
Chairman



Left to right:

Andrew Moss
Group finance director

Richard Harvey
Group chief executive

Lord Sharman of Redlynch OBE
Chairman

Group chief executive's statement

Dear Shareholder,

It has been a good year for Aviva. During 2006 we produced our best ever set of financial results and we ended the year in a strong position to continue our good progress. This success was achieved while completing the integration of RAC in the UK and the purchase of AmerUs in the US.

AmerUs represents a significant move for us, creating a dynamic and thriving business with greater access to the largest savings market in the world. I'm delighted to welcome Tom Godlasky and his team to Aviva. Our priority is to integrate AmerUs quickly with our existing US business, achieving our projected cost savings and enhancing the profile of Aviva in the US.

Exceptional growth in the UK

In the UK, we have generated exceptional growth in our long-term savings business. Total sales increased by 31% to over £13 billion, helped by strong pension sales resulting from changes brought about by pension simplification following "A-Day" in April. We have increased our share of a market that is itself growing very strongly.

In October, we communicated our plans for the UK long-term business to analysts and investors. Our focus is on developing the business to exploit new market opportunities, continuing to improve service, rationalising our cost base, simplifying our legacy systems and managing the retention of existing customers. We also announced annual cost savings across both the long-term savings and general insurance businesses of £250 million by 2008, at a cost of £250 million. These cost savings will mean a reduction of 4,000 in our UK headcount, although we will seek to minimise the number of compulsory redundancies through natural staff turnover and voluntary measures.

Our UK general insurance and health businesses produced a strong result, proving again that we are able to produce sustainable returns from this business. During the year, we completed the integration of RAC and the disposal of its non-core subsidiaries.

Continued international expansion

Our international businesses continue to grow and develop. To recognise the increasingly diverse and complex nature of these businesses, I asked Tidjane Thiam to take responsibility for continental Europe. This allowed Philip Scott to focus on our rapidly developing businesses across North America and the Asia-Pacific region during 2006.

Our confidence in our international businesses was highlighted by our announcement that we expect to achieve double-digit sales growth* over the next five years, while growing new business contribution at least as quickly.

During 2006, we saw strong sales from our new bancassurance partnership with Allied Irish Banks in Ireland and continuing rapid expansion in Asia. This growth demonstrates our commitment to the continued development of our distribution capacity and our ability to deliver results from new opportunities.

Forward thinking

We continue to make progress as a "forward thinking" company. It is vital that we don't see this as simply a slogan, it has to be fundamental to the way we operate. It means positioning ourselves for tomorrow's opportunities, anticipating our customer's aspirations and finding ways that lead to exceptional performance and customer service from our people.

"Forward thinking" also means helping our customers to think about and plan for their future.

Two developments that take us a step further down that road are websites devoted to financial planning. We created and are supporting a website called www.six-steps.org, which focuses on retirement planning. In the UK, Norwich Union has launched a "make sense of it" website to help people understand investments and to highlight the benefits of taking professional advice.

If we are to achieve our growth plans, it is important for us to have a strong brand to support us. We've made great progress in building the Aviva brand this year. The "Forward thinking" campaign has been hugely successful in raising our brand profile with our target audience this year and we will continue to invest in it over the next three years.

Financial results

Our pre-tax operating profit** of £3,245 million (2005: £2,904 million) reflects continued strong operational performances from our portfolio of businesses and the success of our proven strategy. Our return on equity shareholders' funds was 13.1% (2005: 15.0%). On an IFRS basis, the group operating profit before tax was £3,110 million (2005: £2,128 million). The group delivered an overall profit before tax attributable to shareholders of £2,977 million (2005: £2,528 million).

Retirement

In January, I announced my intention to retire in July this year. I'm proud to have had the opportunity to help create a leading company in the global insurance industry. With almost ten years as group chief executive under my belt, there are other dimensions to my life and other things that I want to achieve in both international charity work and the business world. Now is the right time for me to set out on those adventures while I have the energy and desire to make a difference. I wish Andrew Moss and Philip Scott every success as they step into their new roles of group chief executive and group finance director, respectively.

Our people

In September, we conducted our second global employee survey, and our first to cover all business units in the group. The results of the survey are helping us to identify the differing needs of employees around the world, share examples of good practice and provide a fulfilling and supportive work environment.

We are a diverse organisation, something that I see as an important strength. Diversity not only benefits individuals, it enriches our pool of talent, offers new ways of thinking and improves our understanding of customers.

Outlook

We are continually working to get the right balance between risk, return and growth, and I think that this set of results shows that we are making excellent progress. Managing risk against return is integral to everything that we do and will remain a consistent theme in 2007. We continue to benefit from our diverse geography, distribution and product range and we actively use this balanced portfolio approach to manage away a significant proportion of risk.

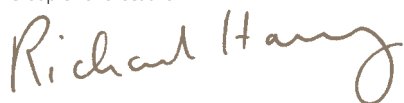
In the stable and mature markets of the UK and continental Europe, I believe that access to distribution will be our key driver of growth. We will seek to expand our bancassurance channel and significantly enhance our direct capability. We see the capital generated by our general insurance and health businesses and our superior understanding of customer needs as key differentiators.

The rapidly developing markets in the Asia-Pacific region represent a substantial longer term area of growth for us. We will be looking to accelerate our growth in India and China, while continuing to explore the potential of other markets. Across the region, we will be working to expand distribution through bancassurance, independent financial advisers and the direct sales force.

In North America, the AmerUs acquisition provides us with a scalable platform for growth in what is the largest single market in the world. Our focus is on successfully integrating AmerUs and achieving our projected costs savings.

I believe that we are in the right markets, at the right time. We have produced an excellent set of results for 2006 and have put ourselves in a strong position to build on these results in 2007.

Richard Harvey
Group chief executive



* Growth ambitions are annual averages after minority interests, before acquisitions, and assuming no major changes in economic conditions.

** On an EEV basis.



I'm not sure yet

Basis of preparation

This business review complies with the recommendations of the European Union (EU) Modernisation Directive, the Companies Act 1985 (Operating and Financial Review and Directors' Report) Regulations 2005 (the Companies Act) and is in line with current best practice. It is addressed to, and written for, the members of Aviva plc with the aim of providing a fair review of our business development, performance and position at the current time. In producing this review, we aim to present a view that is balanced and comprehensive and that is consistent with the size and complexity of our business. The review is written in the context of the risks and uncertainties facing our business. We anticipate that the format and content of the review will evolve over time, along with developments in our business and the external environment.

Key performance indicators

The Companies Act requires that a fair review of the business contains financial and, where applicable, non-financial key performance indicators (KPIs). We consider that our financial KPIs are those that communicate to the members the financial performance and strength of the group as a whole. These KPIs comprise:

- Return on equity shareholders' funds
- Proposed ordinary dividend
- Dividend cover
- Operating profit (International Financial Reporting Standards basis)
- Operating profit (European Embedded Value basis)

Management also use a variety of Other Performance Indicators (OPIs) in both running and assessing the performance of individual business segments and units, rather than the group as a whole. OPIs include measures such as present value of new business premiums, new business margins, combined operating ratio and underwriting profit.

In addition to reporting on our financial performance, it is important that as a forward thinking company we are aware of our wider responsibilities and report on the non-financial aspects of our performance. We consider that our employees and customers are fundamental to the success of our business; as such, they form the basis for our non-financial measures, and include:

- Leadership and employee engagement
- Customer satisfaction

This is the first time that we have sought to report externally on either of these measures and we expect that our reporting on both will evolve. In particular, reporting on customer satisfaction is complicated by the differing needs of customers in the countries in which we operate and the relative maturities of those businesses.

Forward-looking statements

This business review contains "forward-looking statements" about:

- Our future plans
- Our current goals
- Our expectations of our future financial condition, performance and results

By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events that are beyond our control. For example, certain insurance risk disclosures are dependent on our choices about assumptions and models, which by their nature are only estimates. As such, actual future gains and losses could differ materially from those that we have estimated. Other factors that could cause actual results to differ materially from those estimated by the forward-looking statements include, but are not limited to:

- UK domestic and global economic business conditions
- Monetary and interest rate policies
- Foreign currency exchange rates
- Equity and property prices
- The impact of competition, inflation and deflation
- Changes to regulations, taxes or UK and foreign legislation
- The timing and impact of acquisitions and business combinations in relevant industries
- Natural and other disasters
- Changes to consumer saving and spending habits
- Our success in managing the above factors

Consequently, our actual future financial condition, performance and results could differ materially from the plans, goals and expectations set out in our forward-looking statements. We undertake no obligation to update the forward-looking statements contained in this review or any other forward-looking statements we make.

Accounting basis of preparation

In addition to presenting our results and financial position on an International Financial Reporting Standards basis, we also use European Embedded Value (EEV) as an alternative performance measure and reporting basis. Details of the accounting basis of preparation are set out in the "financial reporting" section of this business review on pages 60 and 61.

Group strategy

Our core purpose, the reason we exist, is to provide prosperity and peace of mind for our customers. Our ambition is to be the world’s most trusted savings, investment and insurance provider. To achieve this ambition, we need to be a clear leader in helping our customers grow their wealth and protect their assets and their health.

Our objectives for this are:

Offering a superior range of long-term savings, investment and protection products in markets that offer significant opportunities for growth

Providing a broad range of competitive motor, property, health and related insurance services to individuals and small- to medium-sized enterprises in chosen markets

To achieve the above goal, we have identified our key strategic priorities. These are set out below:

Understanding and meeting the evolving needs of our customers

Working closely with business partners to deliver efficient and effective distribution channels

Attracting, motivating and retaining talented people who are committed to our values and ambitions

Using brands to widen leadership positions

Using scale to deliver benefits, including cost-competitiveness

Building profitable businesses in selected areas where we have, or can, achieve market leading positions

Delivering growth organically and through carefully selected acquisitions designed to increase shareholder value

The table overleaf provides greater detail on how we are implementing these strategic priorities. We have set out the measures and targets that we use to assess our success in achieving our strategic priorities, some of our achievements in 2006 and what we plan to do next year.

Group strategy continued

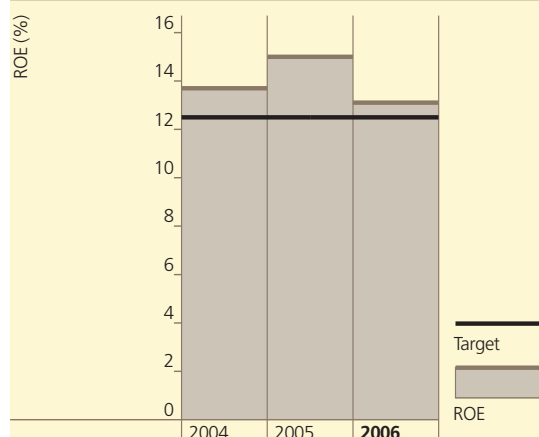
Strategic priority	Understanding and meeting the evolving needs of our customers	Working closely with business partners to deliver efficient and effective distribution channels	Attracting, motivating and retaining talented people who are committed to Aviva's values and ambitions
How we measure progress	<p>Meeting or exceeding customer advocacy and satisfaction targets, at group and individual business level</p> <p>Generating increased profitable sales by providing the products and services that our customers want at a fair price</p>	<p>Meeting or exceeding sales and service targets jointly agreed with each business partner</p> <p>Improving our score in independent external assessments of service (eg the FASA rating in the UK)</p> <p>Maintaining our leading position with insurance brokers</p> <p>Increasing sales to the customers of our bancassurance partners</p>	<p>Meeting targets for our external hire, internal promotion and voluntary staff turnover rates</p> <p>Improving further our employee engagement and leadership performance in our global employee survey and against the global financial services benchmark</p>
Progress in 2006	<p>Established performance measures in our businesses based on customer satisfaction and advocacy (ie actively recommending us to others)</p> <p>Linked senior management remuneration to performance against these measures</p> <p>Came second overall in independent insurance customer satisfaction surveys in China and India</p> <p>Surveyed over 23,000 consumers across 21 countries in our third annual survey of consumer attitudes to savings, providing valuable insights on consumer trends</p> <p>Introduced a group-wide customer policy, setting common governance standards for how we deal with customers</p>	<p>Established new key partnerships in the UK with Barclays Bank, the Post Office, Cooperative Insurance Services and Volkswagen</p> <p>Expanded our bancassurance partnerships, eg, in Ireland with AIB and in India with a further 11 bank partnerships, bringing the total to over 30</p> <p>Voted the <i>Insurance Times</i> "General Insurer of the Year" for the fourth consecutive year in the UK</p> <p>Won the "service Award for excellence" from brokers in Ireland</p> <p>Grew our direct sales forces in India, where it almost doubled</p> <p>Enhanced our e-commerce capabilities (eg in Canada) making us easier to do business with</p>	<p>Improved our group-wide employee survey results in the key areas of leadership and employee engagement</p> <p>Linked senior management remuneration to the measures of employee and customer measures</p> <p>Maintained staff morale while undertaking significant change and restructurings, particularly in the UK</p> <p>Put 300 employees through the Aviva Leadership Academy, run in partnership with leading international business schools</p> <p>Progressed our diversity agenda, being recognised by inclusion in <i>The Times</i> "Top 50 places where women want to work," and gained an Opportunity Now gold award</p>
2007 priorities	<p>Implementing specific local initiatives to improve service to attract and retain customers</p> <p>Setting and meeting customer advocacy and satisfaction benchmarks, both at group level and across all of our businesses</p> <p>Conducting our fourth consumer attitudes to savings survey, covering 24 countries</p>	<p>Continuing to roll out our successful bancassurance distribution model, tailored to the specific needs of developing and mature markets</p> <p>Continuing to strengthen our relationships with key brokers and other partners</p> <p>Broadening and strengthening our direct distribution capabilities</p> <p>Improving on our two star (out of five) Financial Adviser Service Awards (FASA) rating in our UK life operations</p>	<p>Developing leadership behaviours that improve staff commitment and customer experience</p> <p>Developing a robust talent management mindset and culture throughout Aviva</p> <p>Making the most of our international presence when deploying and developing people</p> <p>Building a strong employment brand to attract and retain high quality staff</p> <p>Implementing talent management processes across the group</p>

	Using brands to widen leadership positions	Using scale to deliver benefits, including cost-competitiveness	Building profitable businesses in selected areas where we have, or can achieve, market-leading positions	Delivering growth organically and through carefully selected acquisitions designed to increase shareholder value
	<p>Measuring awareness and favourability using the International Aviva brand tracker</p> <p>Improving further our key stakeholders' perceptions of Aviva (e.g. regulators, shareholders and investors)</p>	<p>Delivering annualised savings of £250 million from the UK cost and efficiency programme by the end of 2007</p> <p>Meeting published cost and revenue targets for the acquisitions of AmerUs and Ark Life</p> <p>Meeting cost-saving and service targets in Aviva Global Services</p>	<p>Growing our overall EEV and IFRS operating profit steadily and sustainably</p> <p>Meeting or beating the group's 12.5% return on equity shareholders' funds target</p> <p>Meeting or beating our group-wide 98% general insurance combined operating ratio target for the foreseeable future</p>	<p>Growing UK long-term sales at least as quickly as the market in 2007</p> <p>Growing our long-term sales in our European and International regions by on average at least 10% pa over next five years, while growing new business profit at least as quickly</p> <p>Establishing a 10% market share in China in ten cities/provinces by 2010</p> <p>Establishing a top-five market position and a 10% life market share in Russia within five years</p>
	<p>Invested in the Aviva brand, significantly increasing awareness and favourability in the financial and business community</p> <p>Reinforced the message that Aviva is a progressive company in all it does through our pan-European "Forward thinking" campaign</p> <p>Gained valuable media exposure when Dee Caffari was the first woman to successfully sail solo non-stop around the world against the prevailing wind and currents</p> <p>Strengthened our local market-leading brands, including RAC and Hibernian</p>	<p>Completed the RAC integration, delivering cost savings of £100 million</p> <p>Initiated a major cost and efficiency programme in the UK that will reduce costs by £250 million per annum by the end of 2007</p> <p>Established Aviva Global Services to provide offshore support to UK and Canadian businesses</p> <p>Relocated both of our Irish businesses to a single site</p> <p>Maintained the most cost-efficient operating platform in the Spanish market</p>	<p>Maintained a strong group long-term new business margin of 3.5%</p> <p>Increased general insurance only operating profits by £156 million despite modest growth in net written premiums</p> <p>Focused in France on capital-efficient unit-linked products through Fourgous transfers</p> <p>Maintained a balance between profitability and sales volumes in a challenging Dutch market</p> <p>Collected investment awards in France (best fund manager over five years) and the UK (two property fund manager awards)</p>	<p>Achieved growth of 21% in total long-term savings sales</p> <p>Completed successfully the acquisitions of:</p> <ul style="list-style-type: none"> – AmerUs (USA) – Ark Life (Ireland) – Eagle Insurance (Sri Lanka) <p>Rapidly grew our organic start-ups in China and India</p> <p>Commenced limited trading in Russia, ahead of plan</p> <p>Gained access to additional bank branches in Italy through our joint venture with UniCredit Group</p> <p>Won the "Best of European Business" award for introducing new products and acquiring and integrating new businesses</p>
	<p>Developing further the Aviva brand through co-ordinated "Forward thinking" campaigns across our markets</p> <p>Establishing an international Aviva brand tracker to provide a global baseline and local targets</p> <p>Maximising the benefit we obtain from our portfolio of strong global and local brands</p>	<p>Delivering on our cost-saving targets in the UK</p> <p>Delivering on our target integration benefits in the USA and Ireland</p> <p>Continuing to exploit our scale by sharing knowledge and skills in multi-channel distribution, product development and service delivery</p> <p>Leveraging our low-cost flexible operating model to maximise the benefits of scale</p>	<p>Exploiting the know-how and product set that AmerUs has in the indexed-annuity market segment</p> <p>Simplifying our business model in the UK to reduce duplication and drive efficiencies</p> <p>Continuing to focus on higher-margin unit-linked products in France</p> <p>Generating increased sales in the Netherlands through our focus on small to medium enterprise pension contracts and developing "white label" products</p>	<p>Leveraging the benefits of our recent acquisitions</p> <p>Capturing the opportunities presented by the retirement of the "baby boomer" generation</p> <p>Monitoring closely opportunities that may arise to gain scale or expand distribution</p> <p>Growing faster than the market in Western Europe where low growth is expected in 2007</p> <p>Capturing opportunities arising from increasing wealth in Russia and Central and Eastern Europe by continuing to invest in our businesses</p>

Key performance indicators

In 2006, the group's strategy was underpinned by focusing on a number of key financial performance measures. The key measures that are used to assess performance at a group level are set out below:

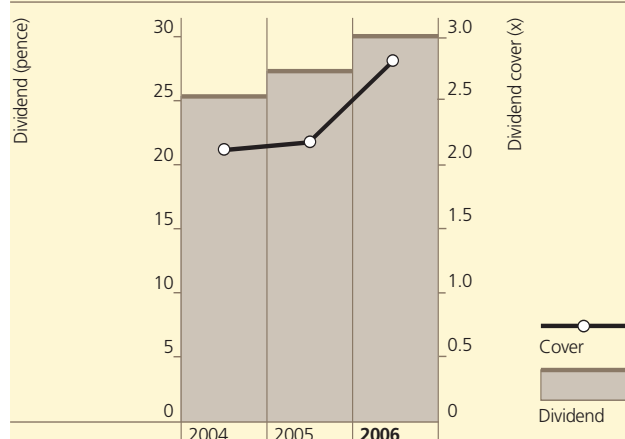
Return on equity shareholders' funds*



We aim to deliver an after-tax operating return on opening equity shareholders' funds, including life profits on a European Embedded Value (EEV basis), equivalent to 12.5%. This is a change to our previously stated aim of a 10% net real return.

Our post-tax operating return on equity shareholders' funds was 13.1% (2005: 15.0%), ahead of our 12.5% target, notwithstanding opening shareholders' funds being £3.2 billion higher and so impacting the return.

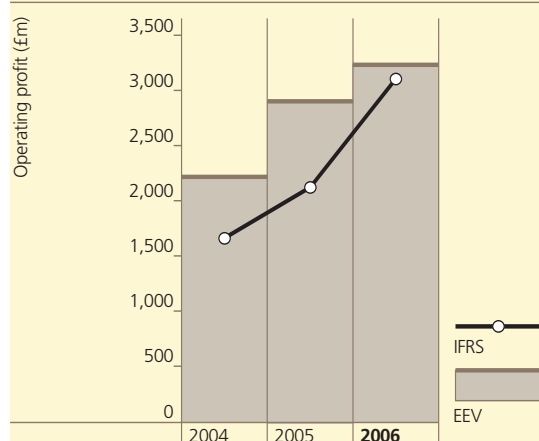
Proposed ordinary dividend per share and dividend cover**



Our intention is to increase the total dividend on a basis judged prudent using a dividend cover in the 1.5 to 2.0 times range as a guide, while retaining capital to support future business growth.

Our board has recommended a final dividend of 19.18 pence (2005: 17.44 pence), bringing the total dividend for the year to 30.00 pence (2005: 27.27 pence). This is a 10% (2005: 7.5%) increase. Dividend cover is 2.80 times (2005: 2.17 times). Excluding the beneficial impacts of one-offs in 2006 and applying a normalised tax rate, the dividend cover was 2.0 times.

Group operating profit before tax†



We aim to achieve steady sustainable growth in our operating profit, both on an EEV and IFRS basis. In seeking to achieve this growth, we continue to adopt strict financial management disciplines underpinned by strong corporate governance.

Our EEV operating profit grew by 12% to £3,245 million (2005: £2,904 million). On an IFRS basis, operating profit before tax amounted to £3,110 million (2005: £2,128 million). Both results reflect strong operational performance, expanding and strengthening distribution channels and the benefit of rising investment markets.

* Return on equity shareholders' funds is calculated using opening equity capital and after-tax return based on operating profit, including long-term savings profit on a European Embedded Value (EEV) basis before adjusting items.

** Dividend cover is measured on operating earnings after tax on an IFRS basis, expressed as a multiple of the ordinary dividend in respect of the financial year.

† Group EEV operating profit is calculated using long-term savings operating profit on an EEV basis before adjusting items. Group IFRS operating profit is calculated using long-term savings operating profit on an IFRS basis before adjusting items.

Employee engagement and leadership



Our global employee climate survey provides a measure of employee engagement. For Aviva, employee engagement represents the degree of effort that our people put into the organisation, the quality of that effort and their loyalty to the company. The survey results are used to plan for the year ahead, with the aim of achieving continuous improvement. The climate survey also measures employees' perceptions of leadership, verifying that employee engagement is harnessed and aligned with our strategic direction and immediate business plans. Our aim is to improve both measures over time and to meet or exceed a global financial services benchmark.

During 2006, our employee engagement score has risen by 8% to 67% and our leadership metric has risen by 4% to 55%. These increases represent ongoing improvement and actions taken in response to our 2005 employee climate survey. Additionally, we are making progress towards a global financial services benchmark[‡].

Customer satisfaction

All Aviva business units are required to measure customer satisfaction. The maturity of our business units and the varied business models and distribution channels mean that, at present, a single, combined measure of group-wide customer performance is not available. While different metrics are in place in business units, key principles govern the methodology for defining customer satisfaction KPIs. These principles include that KPIs should reflect the level of satisfaction/advocacy achieved with customers and that the KPIs should reference a meaningful external benchmark.

In 2006, the majority of our business units reached an "on target" level of customer performance, with four business units achieving "stretch" goals. Every business unit has produced an action plan as a result of 2006 customer performance and stretching targets have been set for 2007 to drive continuous improvement. In 2007, we will be exploring ways to consolidate the various approaches to customer performance measurement such that in future years, aggregated performance data may be disclosed.

[‡] The global financial services benchmark and our global employee climate survey measure employee engagement using slightly different definitions. Using the global financial services definition our employee engagement score was 70% (3% below the benchmark) and our leadership score was 55% (2% below the benchmark).

Group performance

Operating profit

Group operating profit – IFRS basis

	2006 £m	2005 £m
Long-term business*	1,896	1,065
Fund management*†	155	124
General insurance and health	1,680	1,551
Other:		
Other operations*†	(80)	(40)
Corporate costs	(160)	(136)
Net unallocated interest charges	(381)	(436)
IFRS operating profit before tax and adjusting items	3,110	2,128

Group operating profit – EEV basis

	2006 £m	2005 £m
Long-term business*	2,033	1,814
Fund management*†	96	83
General insurance and health	1,680	1,551
Other:		
Other operations*†	(23)	28
Corporate costs	(160)	(136)
Net unallocated interest charges	(381)	(436)
EEV operating profit before tax and adjusting items	3,245	2,904

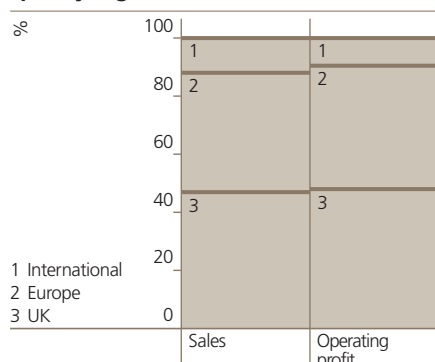
* The results of Norwich Union Equity Release, the proportion of the results of the group's UK and French asset management operations and the proportion of the results of Norwich Union Life Services that arise from providing fund management and other services to the life business have been included in the long-term business operating return on an EEV basis. On an IFRS basis, they are included in fund management and other operations.

† Profits on the sales of retail fund management products in the Netherlands have been reclassified from other operations to fund management following the recognition of a separate fund management segment locally.

Business unit performance

Our operating profit before tax, including long-term operating return on an EEV basis, grew by 12% to £3,245 million (2005: £2,904 million) reflecting strong operational performance. On an IFRS basis, operating profit before tax amounted to £3,110 million (2005: £2,128 million), an increase of 46%. This robust set of results has been achieved by our continued focus on profitable growth, by expanding and strengthening our distribution channels, leveraging our scale advantages in pricing and costs and our disciplined approach to underwriting and efficient claims management.

Total sales and EEV operating profit split by region



The operating results of our long-term savings, fund management and general insurance and health businesses are discussed in detail in the business unit overview section of this review on pages 22 to 49. Other components of our operating profit are discussed below.

Other operations

Our other operations reported a loss of £80 million (2005: loss of £40 million) on an IFRS basis. This loss comprises £45 million of profits from RAC non-insurance operations (2005: £30 million profit), lower losses from NU Life Services of £50 million (2005: loss of £66 million), a loss of £29 million relating to the development of the Lifetime and SIPP platforms (2005: £14 million) and a loss of £46 million (2005: £10 million profit) from our other non-insurance operations, including our Dutch banking division.

Our operating profit from RAC non-insurance operations, which include BSM, HPI, Auto Windscreens and Solus, amounted to £45 million, reflecting the inclusion of results for the entire year (2005: £30 million post-acquisition). In July 2006, we completed the sale of the Lex brand for a profit of £3 million. In total, this transaction, and the previous disposals of the other non-core operations of the RAC group in 2006, generated sale proceeds of £358 million, and a profit on disposal of £69 million (2005: £5 million). The disposed businesses contributed £17 million to our operating profit in the year.

The loss from other non-insurance businesses of £46 million (2005: £10 million profit) reflects the impact in the Netherlands of increased holding company costs, a fall in the banking result reflecting pricing competition on mortgage business in an environment of rising interest rates and the inclusion of a £19 million one-off cost relating to systems migration.

On an EEV basis, our other operations recorded a loss of £23 million (2005: £28 million profit) as this excludes the majority of NU Life Services Ltd losses which are incorporated within the life EEV operating return.

Corporate costs

Our corporate costs were higher at £160 million (2005: £136 million) despite the non-recurrence of global finance transformation costs (2005: £28 million). Within this, central costs relating to staff profit share and incentive plans rose to £17 million (2005: £7 million) while other corporate costs increased to £143 million (2005: £101 million) reflecting higher brand spend, pension funding and staff costs.

Net unallocated interest charges

Our unallocated interest charges comprise internal and external interest on borrowings, subordinated debt and intra-group loans not allocated to local business operations. Also included is net pension income, being the expected return on pension scheme assets less the interest charge on pension scheme liabilities. Interest costs in the year were lower at £458 million (2005: £468 million). External interest costs were lower at £230 million (2005: £248 million) as senior debt was repaid at the end of 2005 while internal interest costs amounted to £228 million (2005: £220 million). Net pension income increased to £77 million (2005: £32 million) due to a larger increase in the expected return on assets than the interest cost on the liabilities, reflecting gains in 2005 and accelerated deficit funding payments.

Interest on the £990 million direct capital instrument issued in 2004 of £52 million (2005: £42 million) is not included within unallocated interest, it is treated as an appropriation of profits retained in the year. The appropriation was charged upon declaration and settlement in the second half of the year. As the coupon payment attracts tax relief at 30%, the net impact on profit attributable to ordinary shareholders was £37 million (2005: £29 million).

Profit before tax

The tables below set out our financial and operational performance for the year ended 31 December 2006.

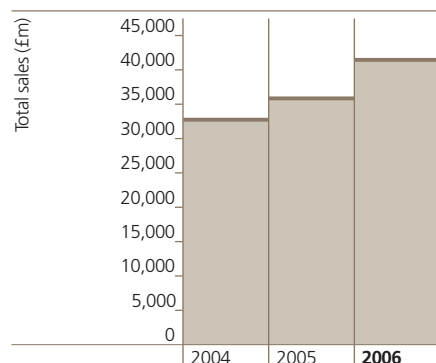
Reconciliation of group operating profit to profit before tax – IFRS basis

	2006 £m	2005 £m
Operating profit before tax – IFRS basis	3,110	2,128
Adjusted for the following:		
Impairment of goodwill	(94)	(43)
Amortisation and impairment of acquired value of in-force business	(100)	(73)
Amortisation and impairment of other intangibles	(70)	(45)
Financial Services Compensation Scheme and other levies	6	–
Short-term fluctuations in return on investments backing general insurance and health business	149	517
Profit on the disposal of subsidiaries and associates	222	153
Integration costs and restructuring	(246)	(109)
Profit before tax – IFRS basis	2,977	2,528
Tax	(588)	(630)
Profit for the financial year	2,389	1,898
Attributable to:		
Equity shareholders	2,215	1,767
Minority interests	174	131

Reconciliation of group operating profit to profit before tax – EEV basis

	2006 £m	2005 £m
Operating profit before tax – EEV basis	3,245	2,904
Adjusted for the following:		
Impairment of goodwill	(94)	(43)
Amortisation and impairment of other intangibles	(46)	(21)
Financial Services Compensation Scheme and other levies	6	–
Variation from longer term investment return	468	2,805
Effect of economic assumption changes	671	(406)
Profit on the disposal of subsidiaries and associates	161	153
Integration costs and restructuring	(246)	(109)
Profit before tax – EEV basis	4,165	5,283

Total sales



Our profit before tax on an EEV basis was lower at £4,165 million (2005: £5,283 million), and includes favourable investment return variances and short-term investment fluctuations of £468 million (2005: £2,805 million) and positive economic assumption changes of £671 million (2005: £406 million negative).

During the year, we completed the sale of our remaining RAC non-core businesses and our associate holding in a French online brokerage company generating disposal profits of £148 million. The sale of a minority stake in our Irish life business as part of the Ark life transaction contributed a lower profit on disposal on an EEV basis of £25 million compared to £86 million on an IFRS basis; the additional value of long-term in-force business is excluded from the IFRS balance sheet. Other small disposals produced a loss of £12 million.

Integration costs totalled £41 million following the successful integration of RAC in the UK, continuing integration of Ark Life in Ireland and activity relating to the integration of AmerUs. As previously announced in September 2006, our UK businesses plan to reduce duplication and improve efficiency to deliver annual cost savings of £250 million in 2008 at a cost of £250 million by the end of 2007. The project is on track and, by the end of 2006, £205 million of reorganisation costs have been recorded.

The variance from the longer term investment return primarily reflects higher than assumed equity returns, particularly in the second half of the year. The FTSE All Share index rose by 13%, the CAC 40 by 18% and the AEX by 13% from end of 2005 levels. This was partially offset by lower market values of fixed income securities due to the rise of 50 basis points and 70 basis points in UK and euro zone bond yields, respectively in 2006. Long-term economic assumptions, which are set by reference to long-term bond yields, were revised upwards at 31 December 2006 and these higher assumptions have increased the expected value of future profits from in-force life contracts, increasing profits by £671 million.

The non-life short-term fluctuations amounted to a profit of £149 million (2005: £517 million profit) as equity markets outperformed our longer term investment return assumptions in the year. The effect of the non-life investment market movements, profit on disposal together with integration and restructuring costs are included in the IFRS profit before tax attributable to shareholders' profits of £2,977 million (2005: £2,528 million).

Tax

Our taxation charge on an EEV basis was £1,286 million (2005: £1,601 million). This includes a charge of £1,028 million (2005: £927 million) in respect of operating profit, which is equivalent to an effective rate of 31.7% (2005: 31.9%). On an IFRS basis the effective tax rate on operating profit was 23.3% (2005: 25.2%), reflecting the use of tax losses in the life businesses and the release of prior year provisions following agreements reached with tax authorities on a number of issues.

Dividend

The Board has recommended a final dividend increase of 10% to 19.18 pence net per share (2005: 17.44 pence) payable on 17 May 2007 to shareholders on the register on 9 March 2007. This provides growth of 10% in the total dividend for the year of 30.00 pence (2005: 27.27 pence). Our IFRS post-tax operating profits cover this dividend 2.80 times (2005: 2.17 times).

Group performance continued

Financial highlights

	2006	2005
Worldwide sales*	£41,464m	£35,894m
Life and pensions new business contribution before required capital	£892m	£808m
Life and pensions new business contribution after required capital	£683m	£612m
Life and pensions margin before required capital	3.5%	3.6%
Life and pensions margin after required capital	2.6%	2.8%
General insurance business combined operating ratio	94%	95%
Return on equity shareholders' funds	13.1%	15.0%
Earnings per share		
Basic – EEV operating profit after tax basis	79.2p	74.5p
Basic – IFRS operating profit after tax basis	86.9p	60.5p

* Based on worldwide long-term savings new business sales, plus general insurance and health business net written premiums.

Worldwide sales

We achieved strong sales growth in 2006, with total worldwide sales increasing to £41,464 million (2005: £35,894 million).

Our long-term savings new business sales were up 21% to £30,762 million (2005: £25,583 million). The overall increase reflects growth in life and pension sales of 17% to £25,852 million (2005: £22,246 million), and exceptional growth in investment sales of 48% to £4,910 million (2005: £3,337 million). Net written premiums increased to £10,702 million (2005: £10,311 million).

Our UK total long-term sales increased by 31% to £13,601 million (2005: £10,345 million). Within this total, life and pension new business sales grew by 21% to £11,146 million (2005: £9,185 million), benefiting from strong growth in pension and bond sales. Investment sales were exceptionally strong, up 112% to £2,455 million (2005: £1,160 million), benefiting from new fund offerings and strong investment markets. Our share of sales through the joint venture with The Royal Bank of Scotland Group were up by 58% to £1,169 million (2005: £742 million), reflecting an increased focus from both partners and a rise in the number of sales advisers.

Our European and International total long-term savings new business sales increased by 13% to £17,161 million (2005: £15,238 million), reflecting strong growth in a number of our main markets and from businesses acquired during the year in Ireland and the United States. Growth in Asia was 91% and the region now accounts for 6% of our total international sales. Life and pension new business sales were 13% higher at £14,706 million (2005: £13,061 million), while investment sales grew by 14% to £2,455 million (2005: £2,177 million), primarily reflecting increased sales through our Navigator platform in Australia and Singapore.

In the UK, our net written premium reduced to £5,940 million (2005: £6,127 million), reflecting our continuing commitment to create value by writing profitable business and a degree of softening in commercial premium rates.

Our European and International net written premium increased to £4,762 million (2005: £4,184 million), benefiting primarily from strong sales growth in the Netherlands as a result of healthcare reforms that amalgamated public healthcare provision into the private sector. The majority of our other European and International business units have produced modest growth in net written premium as they continue to focus on strict underwriting disciplines.

Long-term new business contribution and margin

Our new business contribution before the effect of required capital grew by 11% to £892 million (2005: £808 million), generating a group-wide new business margin of 3.5% (2005: 3.6%). Within the total, our UK margin was maintained at 2.9% (2005: 2.9%), with the combined margin of our European and International business units falling to 3.8% (2005: 4.1%). This reduction was caused primarily by a lower margin in Ireland, resulting from an adverse lapse and other experience variances leading to consequential changes in operating assumptions. Additionally, the margin in our Dutch business was adversely affected by lower bond yields at the start of the year being included in our EEV operating assumptions. Conversely, the continued focus on higher-margin capital-efficient unit-linked business led to a higher margin in France, our second-largest business unit.

After the effect of required capital, our new business contribution increased by 12% to £683 million (2005: £612 million), producing a new business margin of 2.6% (2005: 2.8%). The movement in the margin reflects the factors affecting our European and International businesses noted above, and the strong growth in sales in the United States, where the margin is lower than the group average.

Combined operating ratio

Our general insurance combined operating ratio (COR) improved to 94% (2005: 95%), and is ahead of our stated target to meet or beat a worldwide COR of 98% for the foreseeable future. The improvement in the COR reflects our continued focus on disciplined underwriting and efficient claims handling.

The group COR benefited from better than expected weather in the UK, of £75 million (2005: neutral) below the longer term average. Additionally, the COR in our Dutch operations improved to 89% (2005: 93%), reflecting a strong premium rating environment and a favourable claims experience, including a low incidence of large claims. Across our other major general insurance businesses, the CORs were largely stable.

Our reserves are set conservatively with the aim to protect against adverse future claims experience and development. Our business is predominantly short tail in nature and loss development experience is generally stable. As a result of the prudence applied in setting the reserves, there are some releases in 2006 that reflect releases from the 2005 accident year and prior. The releases mainly arise in the UK and this favourable development benefits the UK underwriting result by £435 million with the remainder of releases arising mainly in our European businesses. We have increased our confidence levels in our reserves over the past few years and continue to maintain our reserves at very strong levels.

Return on equity shareholders' funds

Our post-tax operating return on equity shareholders' funds was 13.1% (2005: 15.0%), ahead of our 12.5% target despite opening shareholders' funds being £3.2 billion higher and therefore impacting the return. The return is based on the post-tax operating profit from continuing operations, including the EEV operating return, expressed as a percentage of the opening equity shareholders' funds.

Earnings per share

Our operating earnings per share after tax on an EEV basis increased to 79.2 pence (2005: 74.5 pence) and on an IFRS basis increased to 86.9 pence (2005: 60.5 pence). Both increases reflect the strength of our operational performance, the greater increase in earnings per share on the IFRS basis reflects the benefit of a lower effective tax rate on our operating profit.

Balance sheet and cash flow

Summarised group consolidated balance sheet

As at 31 December 2006

	IFRS basis		EEV basis	
	2006 £m	2005 £m	2006 £m	2005 £m
Assets				
Goodwill	2,910	2,274	2,910	2,274
Acquired value of in-force business and intangible assets	2,728	803	2,728	803
Additional value of in-force long-term business	–	–	6,794	6,454
Investment properties, properties and equipment	16,027	14,160	16,027	14,160
Investments in joint ventures and associates	3,690	3,014	3,690	3,014
Financial investments	202,853	182,388	202,853	182,388
Other assets	49,972	47,076	49,972	47,076
Cash and cash equivalents	14,542	13,732	14,542	13,732
Total assets	292,722	263,447	299,516	269,901
Equity				
Capital and reserves	11,176	8,774	10,714	8,468
Additional retained profit on an EEV basis	–	–	6,817	6,431
Equity attributable to ordinary shareholders of Aviva plc	11,176	8,774	17,531	14,899
Preference shares and direct capital instrument	1,190	1,190	1,190	1,190
Minority interests	1,698	1,128	2,137	1,457
Total equity	14,064	11,092	20,858	17,546
Liabilities				
Gross liability for insurance and investment contracts	232,588	209,911	232,588	209,911
Unallocated divisible surplus	9,465	8,978	9,465	8,978
Net asset value attributable to unitholders	3,810	3,137	3,810	3,137
Borrowings	12,137	11,013	12,137	11,013
Other liabilities	20,658	19,316	20,658	19,316
Total liabilities	278,658	252,355	278,658	252,355
Total equity and liabilities	292,722	263,447	299,516	269,901

Balance sheet

During 2006, the equity attributable to our ordinary shareholders on an IFRS basis increased by 27% to £11,176 million (2005: £8,774 million). This increase primarily reflects the growth in retained earnings, which in turn reflects our strong operational performance during the year. On an EEV basis, the equity attributable to ordinary shareholders was £17,531 million (2005: £14,899 million).

At 31 December 2006, our total assets were £293 billion (2005: £263 billion) on an IFRS basis. Under EEV principles, our total assets are £6,794 million (2005: £6,454 million) higher. The difference relates to the recognition as an asset under EEV of internally generated additional value of in-force (AVIF) long-term business. The growth in total assets was substantially driven by an increase of £20 billion in financial investments, reflecting strong new business sales and investment market performance.

Goodwill has increased by £636 million during the year primarily driven by the acquisitions of AmerUs and Ark Life. These acquisitions have also generated the majority of the £1,925 million increase in AVIF and intangibles.

At 31 December 2006 our total pension fund deficit at a group level had decreased by £498 million to £973 million (gross of tax) benefiting from deficit funding contributions during 2006. Following the finalisation of previously announced negotiations, agreement was reached that 12% of the future deficit funding payments were to be borne by UK with-profit funds from 2006. Following a further funding contribution in 2006 we have now paid £339 million of the £700 million additional funding announced in March 2006.

Summarised consolidated cash flow statement – IFRS basis

	Long-term business operations £m	Non- long-term business operations £m	Total Full year 2006 £m	Total Full year 2005 £m
Net cash from operating activities	1,473	387	1,860	2,409
Net cash from investing activities	(162)	(1,412)	(1,574)	(1,303)
Net cash flow from financing activities	(879)	1,538	659	(117)
Net increase in cash and cash equivalents	432	513	945	989
Cash and cash equivalents at 1 January	10,107	2,960	13,067	12,126
Effect of exchange rates	(119)	(47)	(166)	(48)
Cash and cash equivalents at 31 December	10,420	3,426	13,846	13,067

Cash flows from operating activities were £1,860 million (2005: £2,409 million). Investing activities generated a cash outflow of £1,574 million, primarily reflecting outflows of £1,889 million on the acquisitions of businesses including AmerUs and Ark Life, offset by cash inflows of £616 million relating to disposals of subsidiaries. Over the year, we generated a net increase in cash and cash equivalents of £945 million (2005: £989 million).

Business unit overview

Overview

The following section details the specific performance of our business units, split by region. This marks a change from the previous year, where we reported the business unit results by segment. The change was made to align our reporting with our management structure. Each business unit is now reported under the executive director who is responsible for the overall management of that region. Our main reporting regions are:

UK – headed by Patrick Snowball

Europe – headed by Tidjane Thiam

International and Morley – headed by Philip Scott

Each of the directors has written a letter to shareholders at the start of their regional section setting out their views on the businesses for which they are responsible. Additionally, the letters cover the key developments affecting the region during the year and the key priorities for the future.

Reconciliation of regional and business segment operating profit – EEV basis

				2006	2005
	UK £m	Europe £m	Morley and International £m	Total £m	Total £m
Long-term savings	744	1,171	118	2,033	1,814
Fund management	(6)	46	56	96	83
General insurance and health	1,075	417	188	1,680	1,551
	1,813	1,634	362	3,809	3,448
Other operations				(23)	28
Corporate costs				(160)	(136)
Net unallocated interest charges				(381)	(436)
EEV operating profit before adjusting items				3,245	2,904



Left to right:

Patrick Snowball
UK

Philip Scott
International
and Morley

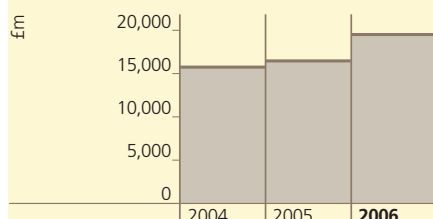
Tidjane Thiam
Europe

UK

Total sales

£19,541m

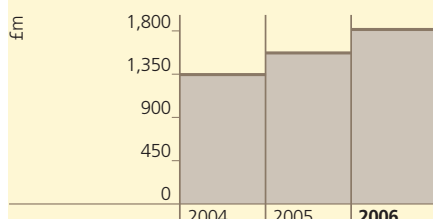
(2005: £16,472m)



EEV operating profit

£1,813m

(2005: £1,571m)



Developments in 2006

We completed the integration of RAC, meeting our 2006 cost saving commitments

We announced annualised cost savings of £250 million across our UK life and general insurance businesses by the end of 2007

We successfully implemented our pension simplification strategy, increasing long-term sales by 31% while maintaining margins

Focus for 2007

Rationalising the cost base and legacy systems of the UK businesses

Ongoing improvement in customer service standards

Active management of our customer retention

Continued focus on profitable underwriting in our general insurance business

Identifying and exploiting new market opportunities

Extracting value from the back book of our life business

→24-31

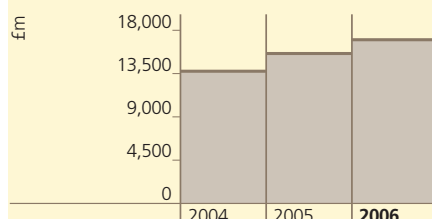
Read more about our performance and future direction on pages 24 to 31 of this report

Europe

Total sales

£17,018m

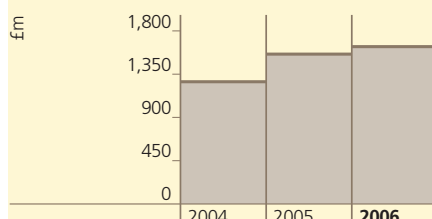
(2005: £15,581m)



EEV operating profit

£1,634m

(2005: £1,558m)



Developments in 2006

We commenced a major bancassurance partnership in Ireland with Allied Irish Banks

Our sales through bancassurance partnerships grew strongly, up 24%

We gained increased access to additional UniCredit branches in Italy, generating a significant increase in sales volumes

We balanced profitability against sales volumes in a challenging Dutch market

We focused on fund transfers in France that benefit ongoing profitability

Focus for 2007

Increasing the penetration of our bancassurance customer base

Increasing activity in central and eastern Europe, which is one of the fastest economic growth areas in the world

Growing our online general insurance business in Ireland

Obtaining further access to distribution in mature markets

→32-41

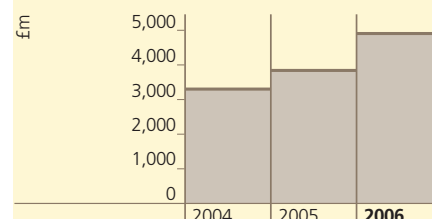
Read more about our performance and future direction on pages 32 to 41 of this report

International and Morley

Total sales

£4,905m

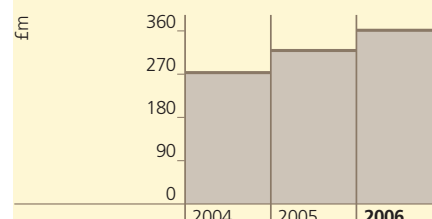
(2005: £3,841m)



EEV operating profit

£362m

(2005: £319m)



Developments in 2006

We completed the purchase of AmerUs in the United States

We commenced a major new bancassurance partnership in India with Centurion Bank of Punjab

We increased our presence in China and are now licensed in six provinces, with a total of 15 city branches.

We purchased Eagle insurance in Sri Lanka and commenced two bancassurance partnerships

We commenced trading in Russia, having received our licence in March 2006

Focus for 2007

Completing a quick and efficient integration of AmerUs

Continued expansion in India and China of our bancassurance and direct sales channels

Developing further our relationship with Development Bank of Singapore (DBS) in Singapore and Hong Kong

Adding corporate partnerships in our Canadian general insurance business

→42-49

Read more about our performance and future direction on pages 42 to 49 of this report

UK

Dear Shareholder,

Any international insurer must be strong in its home market, and our decision to bring together the Norwich Union life and general insurance businesses, including RAC, at the beginning of 2006, has been a key step in meeting this requirement.

Norwich Union (NU) is a leader in the UK. Every week we collect £360 million customer premiums, pay out £94 million in insurance claims, pay £100 million to pensioners and attend over 50,000 breakdowns.

Our financial performance this year once again shows our strength as a well-managed, disciplined composite insurance business. Now that Norwich Union's business units operate more closely together, we are poised to deliver additional benefits that were not available before.

Our 17 million customers expect us to deal with them in a joined up way, and closer working will enable us to meet this challenge. One example is bringing together our IT functions into one unit. This has removed overlap and enabled us to move forward with a new infrastructure to meet the demands of our customers in the emerging "e" world.

We have already taken action to improve the efficiency of our UK business, following our announcement in September 2006 that we plan to deliver £250 million of annualised cost savings by the end of 2007. This programme will enable us to strengthen our competitive position and take advantage of customer self-service.

2006 performance

Our UK life business has taken advantage of both improving market sentiment and pensions "A-Day" in the UK. Our focus has been on capturing our share of market growth, thanks to our unique combination of product range and broad distribution. Our combined businesses delivered an exceptional performance, with operating profits of £1,813 million (2005: £1,571 million), and our general insurance business produced a combined operating ratio of 95% (2005: 96%).

Forward thinking

2007 will see us continue to place our customers at the very centre of everything we do, in particular by making Norwich Union easy to do business with.

This is already occurring following the launch of our "make sense of it" website in NU life, which gives customers sound and simple financial advice. Our newly launched web-enabled fund centre offers comprehensive information for IFAs. Our simplified life cover product, also launched in 2006 and sold over the web, makes it easier to take out life cover and so helps tackle underprovision in the UK.

Within our general insurance business, we launched our Pay As You Drive™ proposition in October, partly in response to growing concerns about how, when and where people drive. Our aim is to bring down the cost of motoring and encourage safer driving, especially by young people at night time.

We believe Pay As You Drive™ will also encourage motorists to cut the number of miles they drive and help reduce carbon emissions. In fact, Norwich Union is playing a leading role helping to mitigate the effects of global warming. We are involved in a number of activities, from high profile (lobbying the Government to further invest in flood defences), to customer marketing (via our portfolio of ethical investments), to keeping our own house in order (giving our employees assistance in buying bicycles).

Conclusion

The actions we have taken in 2006 to extract value from the combined UK business will help us meet the challenge of intense competition in our markets, change and improve the ways we distribute our products to customers, and meet head on the threats and opportunities offered by new technology.

We still have plenty to do to reach our customer objectives, but through process improvement, investment in technology and sharing our expertise across the UK businesses, we will deliver further substantial improvements during 2007.

Our aim is to keep the promises we make to our customers and our shareholders, and to live up to our market leadership position in the UK.

Patrick Snowball
Group executive director





→ Norwich Union links up with eBay to launch online insurance hub

Norwich Union joined eBay.co.uk to launch a unique online insurance centre exclusive to eBay users.

eBay's 15 million customers can use the central "insurance hub" to access information on Norwich Union's motor, home and travel insurance offerings, obtain quotes and buy insurance via a click-through to Norwich Union Direct. Plus, they can benefit from Driveaway's seven days' free car insurance available on eBay Motors.

This unique partnership, which brings together the UK's largest insurer with the nation's leading online marketplace, reflects our forward thinking strategy.



For more examples of "Forward thinking" in our businesses visit www.aviva.com/forwardthinking



UK continued

UK Long-term savings

	IFRS profit before tax £m	IFRS operating profit £m	EEV operating profit £m	PVNB [*] £m	New business contribution ^{**} £m	New business margin ^{**} %
2006	970	683	744	11,146	327	2.9
2005	1,208	382	589	9,185	269	2.9

* Excludes investment sales. Investment sales totalled £2,455 million (2005: £1,160 million) giving overall new business sales of £13,601 million (2005: £10,345 million).

** Stated before the effect of required capital.

Our UK operation, Norwich Union, is a leader in the life and pensions market with a scale unparalleled in the UK sector. We are based in York, with significant operations in Norwich, Stevenage and Sheffield in the UK and overseas operations in India and Sri Lanka. We are regulated by the Financial Services Authority.

Our ambition is to create value for our customers and protect what is important to them. We aim to be easy to do business with and to keep the promises we make to both our customers and shareholders.

Our goal is to be a clear leader in our market. We will achieve this by offering a superior range of products to help our customers grow their wealth and protect their families. In the long term, we aim to grow the overall UK market by improving financial literacy and engaging with current and potential customers who are either underprovided or underprotected.

Our brand, product range, distribution breadth and financial strength mean that we are uniquely placed to deliver growth and returns for customers and shareholders.

Norwich Union is the leading brand in the UK life and pensions market. We have brand awareness and consideration that consistently rank above other traditional life and pension providers, and we are a top-four name within the overall UK financial services industry.

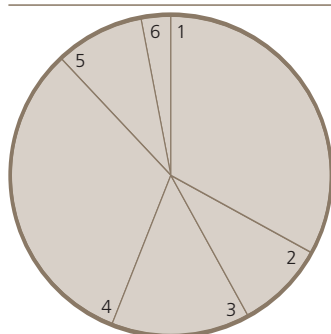
We are a leading provider in the financial adviser market with representation on 21 of 28 multi-tie panels. We are the largest provider to Sesame, Bankhall, Tenet and Simplybiz, the four largest financial adviser networks in the UK, providing access to over 20,000 advisers. We have a joint venture with The Royal Bank of Scotland Group (RBSG), tied relationships with 16 building societies and a strategic alliance with the Co-operative Insurance Society.

We offer a comprehensive range of investment and insurance products. We hold top-three positions in each of our key markets and are a major provider in each of our chosen product lines and channels. Our portfolio of products is diversified and is close to the overall market mix. Our scale and breadth means we have the flexibility to manage our portfolio for long-term value creation, sacrificing market share, where necessary, to secure profitability.

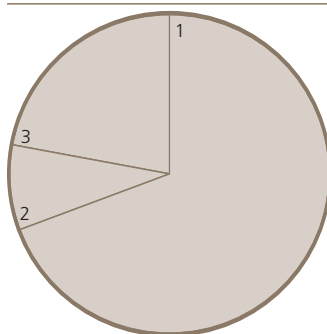
Our scale provides us with a sound financial base from which to operate. Our in-force book provides a significant, reliable and predictable source of profit, from which we can fund new business growth, business development and dividend payments.

2006 has seen an increase in the proportion of gross domestic product invested in savings and improving market sentiment, coupled with advisers' focus on their customers' pension arrangements. Our focus has been on capturing our share of this increased market as we create value for customers and shareholders by driving out efficiencies, improving customer service and continuing to develop our product range.

In September 2006, we announced an efficiency programme that will deliver £125 million of cost savings from 2008 at a one-off cost of £125 million by the end of 2007. Through initiatives such as simpler, faster and more customer-focused processes, stronger supplier management and further sharing of support services across our other UK businesses; we remain on track to deliver those savings. By the end of 2006 we had decommissioned 27 systems, reduced the number of roles by 194 and had already realised savings of £12 million.

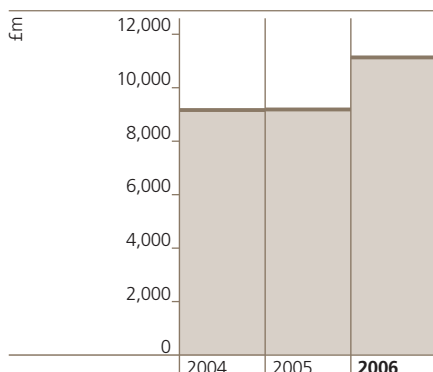
Split of UK PVNB^{*} by product type

- 1 Individual pensions
- 2 Group pensions
- 3 Annuities
- 4 Bonds
- 5 Protection
- 6 Equity release

Split of UK PVNB^{*} by distribution channel

- 1 Independent financial advisers
- 2 Bancassurance partnership with RBSG
- 3 Other partnerships and direct

UK PVNBP



Our people have continued to perform with dedication throughout this period of uncertainty and change. Our measure for the percentage of people who are broadly satisfied to be working at Norwich Union increased from 52% to 61%, whereas those who believe in our leadership increased from 77% to 82%, against a target of 75%.

Individual customer satisfaction improved throughout the year with the percentage of customers who are either extremely or very satisfied rising from 62% to 71%. Customer service complaints fell by 40%. This is the result of improvements to our overall service proposition, including the introduction of several successful "service promises". For example, following the redesign of our bond sales process, we promised to process all new business within five days and, by the end of 2006, we were achieving this in 99.8% of cases.

During 2006, we launched 18 new products, including our innovative "simplified life insurance" product that is sold directly to consumers. Products such as this will improve consumer accessibility and address the widening protection gap. We introduced a Retail Price Index Guarantee on with-profit bonds, resulting in 93% year-on-year growth. We also expanded our fund offering, including the launch of new equity funds, and built on our established property funds, most recently through the introduction of a global property fund managed by Morley.

We launched our "make sense of it" website, responding to consumer demand for information that is simple to understand and helps with the basics of investing. The website was received positively, with over 200,000 hits in the first three days and we have since added information on pensions and annuities. Our new IFA fund centre has significantly enhanced the adviser experience through the provision of online quotes and fund performance charting tools.

We improved our Financial Adviser Service Awards rating to two stars, reflecting our continued investment in improving service levels for advisers. Independent research shows that over the year the percentage of advisers who rate our service as excellent or good has increased from 35% to 52%. Adviser service complaints are down 53%, the lowest level for three years. This progress was made alongside strong sales growth and the implementation of required changes to our pension product set for Pension Simplification (A-Day).

We delivered record total sales, including investment sales, up 31% to £13,601 million (2005: £10,345 million). This result was driven by strong sales of pensions, bonds and collective investments.

Our new business contribution rose 22% to £327 million (2005: £269 million) largely driven by higher volumes, leading to a stable margin for the full year at 2.9% (2005: 2.9%) demonstrating the company's focus on value and volume.

On a post cost of capital basis, our new business contribution was £263 million (2005: £217 million) with a margin of 2.4% (2005: 2.4%).



↑ Norwich Union launches Simplified Life Cover

We have launched a new-style life insurance product that makes it faster and easier for customers and advisers to take out life policies. The new product, Simplified Life Cover, is available through Norwich Union's website and call centres. It uses a streamlined, interactive system that can produce instant policy quotations and acceptance offers. It will also tailor policy premiums to reflect an individual's circumstances. We are hopeful that this straightforward system will help to reduce the number of under-insured families in the UK.



For more information on Norwich Union Life products visit www.norwichunion.com/life

UK continued

Life EEV operating return was 26% higher at £744 million (2005: £589 million) reflecting higher levels of new business contribution and improved performance from our in force book. Total experience variances in the year were £140 million adverse (2005: £95 million adverse) driven by exceptional expenses and lower than expected persistency experience. Positive experience variances in areas such as credit and morbidity have continued, but at a lower level than in 2005.

Adverse exceptional expenses of £149 million (2005: £151 million adverse) are due to our ongoing investment in projects to deliver simpler products to the customer, and the continuing simplification of systems and processes used to administer the existing book. It is anticipated that the operational changes announced in September 2006 will serve to reduce, but not completely eliminate, this cost in 2007.

Persistency experience has continued to be adverse at £66 million (2005: £78 million adverse) particularly in relation to bonds and the re-broking of regular premium pensions business following A-Day. This is after a £75 million release from specific A-Day provisions made in 2005, in line with expectations.

As a result of further analysis of recent customer behaviours, we have changed the basis on certain persistency assumptions. This has included consideration of factors such as the increasing portability of pension products after A-Day, customer outlooks being based on shorter time horizons and advisers more actively managing their customers. This has resulted in a strengthening of persistency assumptions by £224 million. Offsetting this, the company has clarified the financial obligations of its with-profit funds in relation to our pension deficit, resulting in a £126 million benefit. Additionally, we have early adopted PS06/14 (non-profit reserving changes) resulting in a £50 million benefit. Other assumptions have also been reviewed, and while none are of individual significance, in aggregate they produce a further benefit of £108 million. In parallel with these assumption changes, we have begun to execute a wide-ranging customer retention strategy, and we are confident that this, along with an updated assumption set, will reduce future experience variances and place the business on a sustainable basis going forward.

Our bancassurance joint venture with RBSG has continued to perform well with growth in both sales and margin. The joint venture now accounts for more than 10% of our life and pension sales. Strong growth was supported by new product launches and a growth in sales advisers. There are now over 760 sales advisers and further investment in 2007 will increase adviser numbers to over 1,000.

We continue to review the possibility of a reattribution of the inherited estate of two of our with-profit funds, CGNU Life and Commercial Union Life Assurance Company. We have formally announced the appointment of Clare Spottiswoode as an independent policyholder advocate, and written directly to potentially eligible customers. At this stage, no decision has been taken to proceed with a reattribution, which will only take place if there is agreement on a fair outcome for both customers and shareholders.

We recognise that we still have more to do to deliver the level of customer service to which we aspire. In 2007, we will develop new ways for customers to interact with us, grow our direct to consumer channel, launch simpler products and introduce a self-service capability, enhancing the overall experience for our customers. We will pay particular attention to those customers who are traditionally underprovided or underinsured.

In the corporate market we will continue to quote on bulk purchase annuity business, only writing business where this adds value. We will also use our unique ability to combine life, general insurance and healthcare products to grow our position in the corporate benefit market.

We are confident that we will grow at least in line with anticipated market growth of 5%-10% in 2007. We will simplify our business model by reducing duplication, continuing to focus on reducing our number of systems. We will improve our processes, both to drive value and efficiency for our shareholders and to provide better service for our customers. We will thereby enhance our position and safeguard the interests of our shareholders and customers.



↑ Aviva launches six-steps website

Aviva's online financial education initiative, six-steps, was launched in November 2006. The website, at www.six-steps.org, is based around six simple steps that people can follow to help them take control of their finances and prepare for their retirement:

1. Take control
2. Know yourself
3. Save little and often
4. Invest for the future
5. Protect yourself, and
6. Get advice

The site features a retirement planner to help people understand their financial position better. Users can fill it in and save it online, or they can print it out and take it to a financial adviser.



Find more examples of Forward thinking in our UK businesses at www.aviva.com/forwardthinking

UK – General insurance, health and related services

	IFRS profit before tax £m	IFRS operating profit £m	Combined operating ratio* %	Net written premium £m	Underwriting result £m
2006	1,087	1,075	95	5,940	380
2005	1,294	974	96	6,127	303

* General insurance business only.

Norwich Union Insurance (NUI) is the leading general insurer in the UK, with a market share of 15%. Our principal goal is to deliver consistent earnings, and we are committed to “meet or beat” a combined operating ratio of 98% across the insurance cycle. Our Norwich Union and RAC brands are both strong and trusted, and we have an excellent reputation for value and service to customers and distributors.

We focus on those markets where we can create long-term shareholder value, providing a wide range of insurance products for personal and small commercial customers, plus a range of motoring solutions through RAC and associated brands. We have a multi-distribution strategy, selling our full range of products through brokers, partners such as banks and building societies, and direct to our customers. Our headquarters are in Norwich and we operate from over 40 UK locations, with overseas operations in India and Sri Lanka.

We adhere to a clearly defined and communicated underwriting strategy supported by strong financial disciplines, and we aim to achieve continuous improvement in the efficiency, effectiveness and simplicity of our processes and structures.

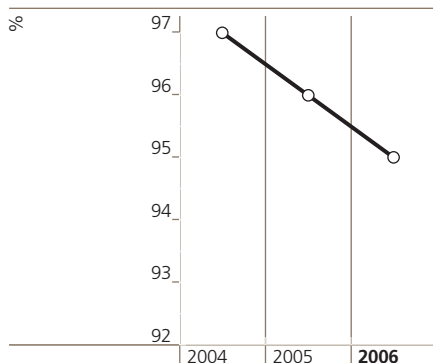
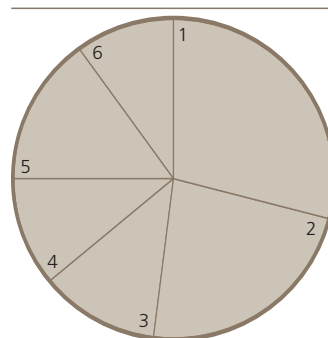
We believe the development of service excellence is key to enhancing long-term customer value and, during the course of the year, we implemented a range of service and rating measures to protect profitability in challenging market conditions. By investing in the quality of our customer experience and improving the appeal and range of propositions we offer, we are increasing cross-selling opportunities and strengthening customer retention.

**↑ Team RAC goes green**

Team RAC created history while taking part in the 2006 British Touring Car Championship by becoming the first motor sport team to achieve a podium finish using bio-fuels. The UK's premier motor sport series accepts the use of the road fuel E85 (85% renewable fuel bio-ethanol with 15% petrol), but no bio-ethanol cars had previously won a podium finish in the championship. We recognise that alternative fuel issues are high on the social and corporate agenda both in terms of environmental protection and fossil fuel sustainability. By demonstrating its use on the track we hope that other teams will recognise that the use of renewable fuel is viable in competition. Our wish is to see more teams and other motor sport championships switching to bio-fuels soon.



For more information on RAC visit www.teamrac.co.uk

UK General insurance – combined operating ratio**Split of UK net written premium by class of business (GI only)**

- 1 Personal motor
- 2 Homeowner
- 3 Personal other
- 4 Commercial motor
- 5 Commercial property
- 6 Commercial other

UK continued

We are also taking action to redress the impact of competitive pressures on our core personal insurance business, where the market's response to the underlying rise in the cost of claims has been slow and inadequate. In the second half of the year, we applied significant rate increases to selected segments of our personal motor account, producing an average increase of 5% in the year (2005: 4%). We expect the inevitable adverse pressure on business volumes to be short-term, and we are already seeing a positive impact on profitability with the full year combined operating ratio of 104%, 1% lower than at the half year. Homeowner rates have increased by 3% (2005: 6%).

We have seen some small rate increases in the fleet market at the end of the year, although the intense competition in commercial lines has led to an overall reduction in rates of around 3% (2005: 1% decrease). Our disciplined approach to risk selection and underwriting has maintained excellent levels of profitability in these accounts.

NUI has had another excellent year, delivering record operating profits of £1,075 million (2005: £970 million) and a COR of 95%, despite a reduction in general insurance net written premiums to £5,583 million (2005: £5,832 million), as we continue to focus on our commitment to increase shareholder value by writing profitable business. The result includes a benefit of £75 million from better than expected weather (2005: neutral), together with savings on prior year claims that have arisen as a result of management action to control costs and improve processes, and our reserving approach. Of the £435 million of prior year claims reserve releases, of which £50 million relates to weather, approximately half reflect exceptional releases as a result of the management actions noted above.

The record profits have enabled us to invest substantially in brand presence and technology to secure future profitability. As a consequence of this investment, we have seen a rise in distribution costs in 2006, with our expense ratio increasing to 13.9% (2005: 10.9%). The expense ratio has also been impacted by a full year of expenses associated with RAC Rescue, whose model includes higher costs of acquiring and administering business. In September, we announced details of our UK cost and efficiency programme, which will deliver cost base savings and enhanced cost flexibility.

The integration of RAC is complete and made a contribution of £160 million to operating profit in the year of which £115 million is recognised as general insurance, with the remainder included in the non-insurance result. Specifically, we have delivered cost savings of £100 million and we remain on track to meet the target profit of £220 million in 2008. The remaining RAC non-core businesses held at the end of 2005 have been sold, generating sale proceeds of £358 million, and a profit on disposal of £69 million in 2006 (2005: £5 million).



↑ RAC launches search for tomorrow's engineers

During 2006, we launched a £100,000 national initiative to find and train the motor engineers of the future. We are linking up with schools to provide vocational training that will give students a head-start in the automotive industry.

The project has begun with Ashfield School in Nottinghamshire, where we are building a state-of-the-art workshop equipped with the latest vehicle technology.

The aim of the initiative, which includes finding work placements with local businesses, is to provide students with a gateway into a range of automotive engineering qualifications and roles, not only as vehicle technicians but also in the manufacture and product design of vehicle systems, electronic controls and robotics, which are critical jobs for the future of manufacturing in the UK.



For more information on RAC visit www.rac.co.uk

RAC has continued to deliver excellent customer service and has been rated number one for motorists in the 2006 JD Power Roadside Assistance survey. In addition, RAC has agreed a three-year deal to provide breakdown assistance to all VW Group brands (including Audi, Lamborghini, Bentley, Seat and Skoda), commencing in the first quarter of 2007. This follows a new six-year deal with Lex Vehicle Leasing to provide roadside assistance and glass replacement, and a two-year UK roadside contract with AssetCo that were signed in the first half of the year. RAC also successfully renewed its contracts with Porsche and Volvo and, since the end of the year, its contract with Motability.

We have won Insurance Times General Insurer of the year for the fourth successive year and are a partner of choice to the UK's top brands. During 2006, we signed deals with the Post Office (to provide motor, homeowner and commercial van products), and with the broker Towergate (to provide creditor insurance). We also successfully renewed our contracts with Abbey and Saga to provide homeowner insurance, and our contract with Lloyds TSB to provide creditor insurance.

Our commitment to corporate social responsibility is reflected in the business decisions we take and the recognition we receive. In October, we announced the full launch of our "Pay As You Drive"TM product. This raises awareness of road safety (especially the increased dangers of driving at night to young drivers) and gives drivers greater control over their motor insurance, by enabling an informed choice about when, where and how often they use their car. RAC was named Breakdown/Recovery Company of the Year in the Greenfleet Awards, for its environmentally friendly roadside patrols.

NU Healthcare is a leading UK health insurer providing private medical insurance (PMI) and income protection to over 800,000 customers. The PMI health result was break-even (2005: £4 million profit) reflecting increased strategic focus and investment in the healthcare business.

UK – Fund management

	Operating profit IFRS basis		Operating profit EEV basis	
	2006 £m	2005 £m	2006 £m	2005 £m
The Royal Bank of Scotland	(7)	(1)	(7)	(1)
Norwich Union investment funds	1	9	1	9
Total	(6)	8	(6)	8

Our primary fund management business in the UK is Morley Fund Management, which falls under the responsibility of Philip Scott. Therefore, Morley's performance is reported within Philip Scott's business unit review, International and Morley.

In addition to sales under the Morley brand, we sell ISAs, unit trusts, open-ended investment companies (Oeics) and structured products under the Norwich Union and The Royal Bank of Scotland brands.

Our operating losses from these businesses amounted to £6 million (2005: £8 million profit) where increased sales through the company's collectives investment business with RBSG resulted in a higher new business strain.



WE ARE MACMILLAN. CANCER SUPPORT

↑ Norwich Union Healthcare offers dedicated support for cancer patients

During the year, we have improved further Norwich Union Healthcare's dedicated and comprehensive cancer claims service.

We have added to the existing group of nurses and advisers to create a team with a vast wealth of knowledge and experience in managing cancer cases.

As a result, this service is now available to all of Norwich Union's customers who have been diagnosed with cancer. Every customer handled by the team has a nominated claims handler allowing us to develop a supportive and customer focused relationship.

The team works in partnership with Macmillan Cancer Support and advises customers of the wide range of services the charity provides to people affected by cancer. In addition, Norwich Union has donated £35,000 to Macmillan Cancer Support to help fund a Macmillan nurse and consultant for teenagers and young adults at Southampton General Hospital. We previously helped to fund the building of a Macmillan support and information centre at the hospital, which continues to make a real difference to the lives of people affected by cancer.



For more information on Norwich Union health services please go to www.norwichunion.com/health

Europe

Dear Shareholder,

Europe is, and will continue to be, one of the world's main savings markets. We have secured a unique operating platform on the continent and are in a prime position to capture the opportunities that changing demographics, increasing private wealth and stretched public finances will create to provide customers with our products and services.

Continental Europe now contributes 41% of the group's total sales and is a key source of growth and profits for Aviva. We continued to grow at a healthy pace in 2006, increasing our total long-term sales by 8% to £14 billion.

Bancassurance is at the heart of our European strategy. In 2006, we completed a new distribution agreement with AIB in Ireland and significantly expanded our distribution in Italy with UniCredit Group. Elsewhere we have continued to work hard on increasing our penetration of the bank's customer base and have made good progress in France and Spain. Our Dutch operations have had a difficult year, largely as a result of increased competition in a number of markets and changing economic conditions. Local management continues to seek out new sales opportunities and has taken action to improve efficiency and competitiveness through cost control.

In the emerging markets of Central and Eastern Europe, we have made good progress. In Poland our long-term sales increased by 74% and profits by 19%. We are leveraging our multi-channel distribution skills acquired in the more mature markets of Western Europe to accelerate the development of strong long-term businesses in Hungary, the Czech Republic, Romania and Turkey.

Financial performance

Benefiting from our highly diversified geography and distribution network, we achieved growth of profits and sales in 2006 reflecting good operational performances across our long-term, fund management and general insurance businesses. Total operating profit was up to £1,634 million (2005: £1,558 million). Our general insurance and health operations across Europe have once again delivered a strong performance, achieving a general insurance only COR of 89% (2005: 92%), therefore beating the group target of 98%.

Strategic developments

Although the markets of continental Europe are highly competitive, we believe that they offer excellent growth opportunities to players who have the right skills and the right geographic spread. We invest significant resources in research and development to stay ahead of our competition, and to understand our customers and our distribution partners better.

Access to our customers – distribution – is crucial to unlocking Europe's growth potential. Our primary focus is to sell more to our existing 18 million customers; therefore, penetration rates, cross-selling and up-selling have become part of the day-to-day vocabulary of all our European staff. In Spain, for instance, working ever more closely with our banking partners, we have been able to more than double the proportion of the banks' customers using our products and services over the past five years. Organic growth is central to our strategy and critical to our success, yet we are also keen to capture value-creating opportunities to increase our distribution reach.

Finally, we will continue to invest in Central and Eastern Europe, which after Asia, is one of the fastest growing economic areas in the world. These economies are expected to grow at double the rate of Western European economies. As income and private wealth increase in these countries, we know that consumers will invest a significant proportion of their growing disposable income in the kind of products and services that we provide. Our 2006 achievements in Poland and Hungary, to name just two countries, illustrate the kind of potential available in that region.

Outlook

Our priority is to achieve strong, sustainable and profitable growth. We will continue to work hard to increase the penetration rate of our existing customer base, to increase our distribution reach through new partnerships and to grow our presence in the emerging markets of Central and Eastern Europe.

I strongly believe that Europe will continue to make a major contribution to the success of Aviva, and that we will build further on our current strong position to become the leading insurance company in Europe.

Tidjane Thiam
Chief Executive, Aviva Europe





Ukraine: Aviva staff build better tomorrows

We volunteered to partner international aid agency Habitat for Humanity to raise funds and build four new homes for families in Romania in one week. A hundred volunteers from across Aviva – Romania, UK, Turkey, Hong Kong and USA – travelled to Cluj to erect the new homes. Our contribution exceeded any previously achieved by Habitat for Humanity in Romania, both in terms of the number of volunteers from one company, and in the total size of the project. We are very proud of the employees involved and what they achieved.



For more information on our CSR programmes visit www.aviva.com/csr



Europe continued

Europe – Long-term savings

	IFRS profit before tax £m	IFRS operating profit £m	EEV operating profit £m	PVNBPI [†] £m	New business contribution [‡] £m	New business margin [†] %
France	259	273	402	3,552	153	4.3
Ireland	52	60	(40)	1,273	15	1.2
Italy	76	79	110	2,768	70	2.5
Netherlands*	453	458	329	2,346	56	2.4
Poland**	108	108	162	534	28	5.2
Spain	113	126	221	2,059	184	8.9
Other Europe	(16)	(16)	(13)	308	(4)	(1.3)
Continental Europe	1,045	1,088	1,171	12,840	502	3.9

	IFRS profit before tax £m	IFRS operating profit £m	EEV operating profit £m	PVNBPI [†] £m	New business contribution [‡] £m	New business margin [†] %
France	234	258	321	3,530	135	3.8
Ireland	56	28	20	665	16	2.4
Italy	35	53	96	2,294	59	2.6
Netherlands*	164	172	349	2,739	90	3.3
Poland**	90	91	132	320	16	5.0
Spain	75	89	214	2,013	175	8.7
Other Europe	(5)	(6)	(6)	240	(1)	(0.4)
Continental Europe	649	685	1,126	11,801	490	4.2

* Includes Belgium and Germany.

** Includes Lithuania.

† Excludes investment sales. Investment sales totalled £891 million (2005: £1,026 million) giving overall new business sales of £13,731 million (2005: £12,827 million).

‡ Stated before the effect of required capital.

France

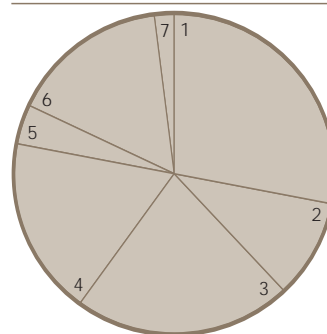
Aviva France is one of the top-ten long-term savings businesses in France with a market share of 4%. Our business focuses on higher-margin unit-linked products in which our market share is 6%. We offer a comprehensive range of life and savings products, mainly for private clients, with a strong focus on providing a lifetime service to customers and a long-term approach to savings and investments. Our distribution is multi-channel, including a direct sales force, brokers, AFER (the largest retirement savings association in France), the UFF network of financial advisers, a direct distribution channel, Aviva Assurances tied agents and our bancassurance partnership with Crédit du Nord.

In 2006, in line with our focus on unit-linked business and customers' needs, we accelerated our focus on encouraging Fourgous transfers, an area in which we have been very successful and which is based on our market position as a unit-linked specialist. To date, we have achieved over 80,000 policy conversions amounting to £4.2 billion of transferred funds, of which 33% have been transferred to unit-linked funds. The majority of transfers have been generated through AFER in 2006 and together we have generated approximately 30%[#] of all Fourgous transfers in the market.

The Fourgous amendment of 2005 enabled the tax-efficient transfer of existing 100% euro funds into more balanced euro and unit-linked portfolios.

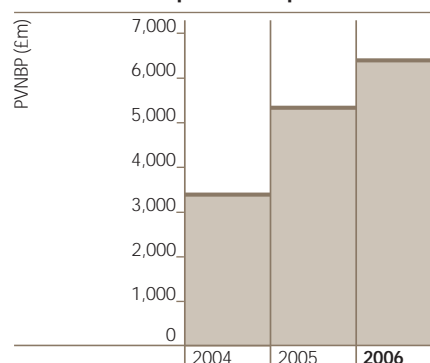
[#] Based on the value of funds converted.

Geographical split of European PVNBPI



- 1 France
- 2 Ireland
- 3 Italy
- 4 Netherlands
- 5 Poland
- 6 Spain
- 7 Other Europe

PVNBPI from major European bancassurance partnerships



Although we exclude these transfers from our new business sales figures, they enable a greater proportion of future new business from existing customers to be invested in unit-linked funds.

We continue to encourage our diverse and strong distribution networks to share best practice and initiatives. Further efficiency gains have enabled us to maintain a firm control on expenses despite the increased level of work in the area of process improvement. The standardisation of sales and administration processes is regarded as one of our key strengths. To complement our networks, a key focus of 2006 has been the launch of our customer internet site in November, which supplements the pre-existing AFER site. This site enables customers to view their policies online, offers customers some online transaction capabilities, promotes our products and creates greater awareness of our businesses. As the site develops, customers will be able to perform a greater number of transactions online.

Our life EEV operating return rose to £402 million (2005: £321 million). The underlying profitability of in-force life business has been enhanced with the proportion of AFER in-force funds invested in unit-linked products having increased to 18% at the end of 2006 up from 11% at the end of 2005. This increase reflects the positive impact of Fourgous transfers and is supported by the success of our sales networks' efforts in providing our market-leading "Le Bon Conseil" approach to advising existing customers. The operating return primarily reflects the increased contribution from new business sales, higher expected returns and experience variances partially offset by a reduced level of favourable operating assumption changes. The favourable experience variance of £71 million (2005: £32 million) includes mortality profits and the impact of the reduction in required capital following Fourgous transfers.

We generated sales growth of 1% to £3,552 million (2005: £3,530 million). Unit-linked sales increased by 10% to £1,556 million (2005: £1,423 million), with AFER unit-linked sales growing strongly by 32%, while sales through our bancassurance partnership with Crédit du Nord have increased to £838 million (2005: £728 million). These increases were offset by reduced euro fund sales in the non-bank channels. Our continued strategic focus on more profitable unit-linked sales resulted in a 14% increase in new business contribution to £153 million (2005: £135 million) giving a higher full year new business margin of 4.3% (2005: 3.8%).

We have built a strong base from which to grow while seeking to retain our focus on the higher-margin unit-linked market and on maintaining a competitive suite of products.

Ireland

Following the acquisition and merger with Ark Life in January, and the start of the associated bancassurance partnership with Allied Irish Banks (AIB), Hibernian is now the third-largest life and pension provider in Ireland with a 17% market share. This transformational deal provides exclusive access to Ireland's largest retail bank with over 280 branches and 1.6 million customers, adding to our existing channels, most notably our strong broker distribution capability. This development is a major step towards us achieving our longer term objective of growing our market-share in long-term savings and protection products.

The integration of Ark Life is proceeding well, including the successful migration of funds previously managed by AIB Investment Managers to Morley. At the end of 2006, our Irish life operations relocated to a single site along with our Irish general insurance business.

We have already seen the benefits of the partnership with AIB through the successful sales of the reopened property fund. During 2006, we have also successfully revised and relaunched the Horizon pension products. There have been further product developments aimed at the bancassurance channel and new rollover products designed to capture maturities from special savings incentive accounts (SSIAs) are in place.

Our life EEV operating return was a loss of £40 million (2005: £20 million profit) including £21 million of profit through the bancassurance partnership with AIB. The EEV operating loss reflects adverse persistency in the year and the impact of consequential changes in operating assumptions. Following the removal of market value adjustments at the beginning of 2006, Hibernian has experienced high rates of withdrawals from its with-profits Celebration bond. Lapse assumptions have also been strengthened for unit-linked pension business and for some other single premium life products. Other assumption changes include the strengthening of annuitant mortality following a detailed review of experience and industry trends, and a one-off change in expense assumptions.

Including sales through the bancassurance partnership with AIB, new business sales increased by 93% to £1,273 million (2005: £665 million). Sales through AIB, which commenced at the end of January 2006, amounted to £589 million. Sales through the Hibernian broker channel were 4% higher at £684 million (2005: £665 million). This was mainly driven by strong sales of single premium unit-linked business reflecting buoyant market conditions and the continued success of the limited-offer guaranteed fund prior to its closure in June. New business contribution of £15 million (2005: £16 million) included £8 million through the bancassurance partnership with AIB. The year-on-year movement in new business contribution and the lower new business margin of 1.2% (2005: 2.4%) mainly reflects continuing competitive pressures and the adverse impact of lapse assumption changes noted above.

One of our key strengths is the three strong brand names of Aviva, Hibernian and AIB. This market presence gives us a significant opportunity to increase sales. A significant proportion of SSIAs will mature in April 2007 and, while we anticipate some customer inertia, we are well positioned to benefit from this opportunity.

Europe continued



i Ireland: Hibernian publishes new report into pension crisis

In April 2006, Hibernian published a report called "The Global Pensions Puzzle", which examined the Irish pensions industry in an international context. It compared the situation in Ireland with conditions in France, the USA and the UK, and reviewed initiatives under way in countries such as New Zealand, Sweden, Chile and Australia.

The purpose of the report was to add to the debate around financial planning for retirement. The challenges that Ireland faces are not unique, nor are they as extensive as in some other developed economies. We believe that solutions from other countries such as those examined in the report deserve to be investigated further, as they could be adapted for use in many European countries.



For more information on Hibernian's pension products please visit www.hibernian.ie

Italy

Aviva Italy is the country's seventh-largest life insurer, with a market share of 7% at November 2006. Our distribution is principally through bancassurance and we have significant partnership relationships with UniCredit Group, Banca delle Marche, Banche Popolari Unite (BPU) and Banca Popolare Italiana (BPI).

Our main goal is to develop the business through profitable growth. To achieve our goal, we continue to work with our bancassurance partners to increase customer penetration and improve value for customers through product innovation. At the same time, we continue to focus on maintaining a cost-efficient operation. In all, we introduced or improved 32 products during the year and through access to additional branches in the UniCredit Group we have achieved strong sales growth in 2006. During the year, our bancassurance partners BPI and BPU both announced corporate mergers; our existing partnership agreements remain in force until 31 December 2009 and 31 December 2010, respectively. We continue to work on expanding our distribution and we expect approval in 2007 for the transaction involving BPI's financial adviser network, bipielle.net.

Our life EEV operating return increased to £110 million (2005: £96 million) due to a higher new business contribution. We achieved strong sales growth in 2006 up 22% to £2,768 million (2005: £2,294 million) benefiting from the launch of new and improved products and access to additional branches in the UniCredit Group. New business contribution increased to £70 million (2005: £59 million) due to significantly higher sales, representing a new business margin of 2.5% (2005: 2.6%).

The Italian long-term savings market has significant medium-term growth potential and Aviva's prospects for continued growth in 2007 are good.

Netherlands

Delta Lloyd Group is a top-five financial services group based in the Netherlands, with operations in Belgium and Germany. We sell a comprehensive range of life and pension products in both the group and individual markets through our principal distribution channels: our bancassurance joint venture with ABN AMRO Bank; directly to customers under our OHRA brand; and via independent financial advisers under our Delta Lloyd brand.

Our vision is to be the most trusted financial services provider by excelling in customer service, innovation, efficiency and financial strength through a combination of effective back-offices and strong financial disciplines.

During 2006, changing pension laws in the Netherlands, fiscal changes on life products in the Netherlands and Belgium and the impact of a reduction in the difference between short-term and long-term interest rates across the euro zone have adversely affected our results. Sales of our new "lifecycle" product in the Netherlands have not reached the levels of our previous pre-retirement products and, at the same time, increasing interest rates across the euro zone have reduced the demand for mortgages while making competing bank deposit-type products more attractive.

The increased competition experienced in 2006 is expected to continue, with distribution capability important for commercial success. We are optimistic that we will see results from our new pension strategy, which focuses on selling pension contracts in the small- to medium-sized enterprise market, supported by our expertise in providing dedicated pensions and employee benefits advice. In addition, our distribution arrangements with ABN AMRO have been extended and we are developing "white-label" products using the OHRA platform. In Germany, our market presence is strengthened by the name change to Delta Lloyd Leben and new product introductions, with a focus on annual premium products that will help to improve performance in 2007. In Belgium, the collaboration between our life and banking operations will be increased. Internally, product development activity and back offices will be shared to an increased extent in a programme of change that will run until 2009.

On 8 February 2007, Delta Lloyd announced its acquisition of the Erasmus Group in the Netherlands which remains subject to regulatory approval. This transaction has a good strategic fit and is expected to add approximately 3% to our existing life insurance business volumes.

Our EEV operating return of £329 million (2005: £349 million) reflected lower contribution from new business partly offset by increased expected returns due to a higher start of year embedded value. The reduced contribution from new business of £56 million (2005: £90 million) reflected lower sales volumes and the impact of a 40 basis point decrease in the bond yield within the EEV assumptions at the end of 2005 which resulted in a lower margin of 2.4% (2005: 3.3%). Our life and pension sales were £2,346 million (2005: £2,739 million) affected by the challenging market conditions. Profits on the IFRS basis of £458 million (2005: £172 million) benefited from the rise in long-term interest rates during 2006 prompting a release from the provision for guarantees on unit-linked contracts, and from an increase in equity and property investment gains.

Poland

In Poland, we sell principally through our 3,000-strong direct sales force, complemented by our bancassurance partners Deutsche Bank and BZ WBK. We have been the largest pension provider in Poland since 1999, with a 27% market share, and have the second-largest life insurance business, with a 12% market share. In Lithuania, we are the third-largest life and pension provider.

Supported by strong market growth in the year, we have seen success from our single premium unit-linked products, while there has also been improvement in our regular premium business sold to both individuals and groups. Our pension business sells a unit-linked regular premium product in the compulsory private pension market.

We are well positioned to capture a significant share of market growth through our wide client base and multi-channel distribution network. We aim to extend our leading position in the Polish pension market to the long-term savings market by providing excellent service and returns to our customers. Recently we have implemented plans to increase further the size of our direct sales force through the recruitment of advisers focused on selling only pension business.

New products were launched via the direct sales force channel in 2006 with additional developments planned for next year. In 2006, we have developed innovative methods of capturing new business, particularly in the pensions market, with the introduction of SMS and internet technology. Additionally, we were acknowledged as having the best pension fund in central and eastern Europe by the prestigious industry monthly magazine *Investment & Pensions Europe*.

Our life EEV operating return increased to £162 million (2005: £132 million) due to the higher contribution from new business together with favourable experience and operating assumption changes for persistency and mortality. Our life and pension sales grew by 63% to £534 million (2005: £320 million) with both life and pensions business showing strong performances. New business contribution was £28 million (2005: £16 million), resulting in a margin of 5.2% (2005: 5.0%).

We expect to grow and develop our business further next year following product developments, expanded distribution and tactical initiatives implemented in 2006, combined with the favourable development of the investment markets that will benefit the entire market.



i Aviva hat-trick at Milano Finanza awards

Aviva Italia won three awards at the annual Milano Finanza Insurance Awards in October 2006. Representing Aviva Italy, Cesare Brugola, chief executive officer, received the insurance elite award for the most distinctive strategy and the most respected and trusted executives. Our joint venture with Banco Popolari Unite (BPU), took the innovation award for its BPU Private Absolute product. Eurovita Assicurazioni SpA won another insurance elite award for the best organic growth performance.



For more information on Aviva Italy please visit www.avivaitalia.it

Europe continued

Spain

Aviva Spain operates in the long-term saving, pension and protection markets through a multi-distribution platform. We are the second-largest life insurer with an 8% market share at December 2006. Our distribution is dominated by five bancassurance partnerships with Bancaja, Caja España, Caixa Galicia, Unicaja and Caja de Granada. The majority of our products are marketed through the brands of our bancassurance partners. We use the Aviva brand in relation to our Aviva Vida y Pensiones (AVP) business, which distributes products through an agency-based network.

In January 2006, it was announced that there would be changes in the effective tax rates relating to insurance savings and investment policies on surrender or maturity. The detailed legislation remains under discussion by the Spanish Congress but has already introduced a new savings product, the Systematic Individual Savings Plan (PIAS), in 2007. PIAS savings products have valuable tax benefits if monies invested in the product are used to purchase an annuity after ten years.



i Aviva Spain won 1st prize for their pension plan Plusfondo Renta Fija

In Spain we won a top prize in the Expansión-Standard & Poor's Pension Plan Awards. Our Plusfondo Renta Fija pension plan came first in the "eurozone fixed income over three years" category. The award measures the profitability of funds versus the risk involved, allowing customers to identify, with greater ease, the funds, pension plans and agencies that offer more stable profitability.



For more information on Aviva Spain please visit www.aviva.es

During 2006, our protection sales have increased, buoyed by the strong housing market, while sales of savings products were adversely affected by uncertainty surrounding the details of tax changes noted above. We have developed our PIAS savings products that we launched at the start of 2007, which take advantage of the more favourable tax regime. We continue to seek opportunities to expand our distribution reach in Spain while continuing to work with our existing bancassurance partners to improve penetration of the customer base.

Our EEV operating return of £221 million (2005: £214 million) reflected a higher contribution from new business. We achieved underlying sales growth, excluding one-off sales, of 4% to £2,059 million (2005: £2,013 million), benefiting from concentrating on higher-margin protection and pension products. This focus has also seen an increase in our new business contribution to £184 million (2005: £175 million) and the new business margin to 8.9% (2005: 8.7%).

Other Europe

Our other European operations consist of our top-five businesses in Turkey, Hungary and Romania and our operation, ranked 13th, in the Czech Republic.

In Turkey, our main products are unit-linked pension plans supplemented by life, saving and protection policies, predominantly sold through our direct sales force. We continue to develop our direct sales force, exploiting pension opportunities as the market continues to grow rapidly, while exploring options to expand our distribution network.

In the Czech Republic, Hungary and Romania, we are seeking to achieve growth with unit-linked and other saving products focused on high net worth individuals. Programmes are underway to grow the direct sales force and to improve further performance. We aim to enhance our product range while developing further our alternative distribution channels particularly bancassurance and brokers. In Romania, we see the launch of new voluntary pension scheme products in 2007 as a growth opportunity for the business.

Strong underlying life and pension sales growth of 60% (excluding 2005 sales in Portugal) was achieved in our other European operations. Growth was principally generated by an increase in sales through the broker channel in Hungary, which benefited from high levels of new business, ahead of tax regime changes on 1 September 2006. Despite these tax changes, sales continued to be strong in the final quarter of 2006. In Turkey, we achieved higher sales of regular premium pensions business, boosted by an increase in the number of sales advisers and productivity in the final quarter of 2006. The business also benefited from increased transfers from existing life policies ahead of an October 2006 regulatory deadline.

We generated a life EEV operating loss of £13 million (2005: £6 million loss, including £3 million profit from Portugal) through our other European operations. Total life and pension sales were £308 million (2005: £240 million, including £45 million of sales from our Portuguese business, which was sold in 2005).

Europe – General insurance and health

	2006				
	IFRS profit before tax £m	IFRS operating profit £m	Combined operating ratio* %	Net written premium £m	Underwriting result £m
France	77	63	99	735	6
Ireland	297	172	77	519	121
Netherlands	107	139	89	1,755	50
Other Europe	26	43	100	278	12
Continental Europe	507	417	89	3,287	189
	2005				
	IFRS profit before tax £m	IFRS operating profit £m	Combined operating ratio* %	Net written premium £m	Underwriting result £m
France	68	35	101	726	(21)
Ireland	181	171	78	499	116
Netherlands	171	137	93	1,270	54
Other Europe	17	47	95	259	15
Continental Europe	437	390	92	2,754	164

* General insurance business only.

France

Our French general insurance business sells predominantly personal, small commercial and health insurance and has a market share of 2%. We sell products primarily through an 875-strong agent network. Our agent network is particularly focused in provincial cities where its key strength is its proximity to, and understanding of, customers. Eurofil is the second-largest direct insurer in the French market and is fully integrated with our other general insurance operations.

We continue to focus on increasing profitability through improvements to the quality of our underwriting and processes, and through further successful development of our agent network. To achieve these goals we have recruited additional agents this year as part of our strategy to renew and grow our agent network. We are also seeking to increase cross-selling of life products through our agents, particularly AFER unit-linked products.

During 2006, we have increased activity in our commercial operations, predominantly in our health business, and for self-employed customers in order to maintain the product spread of our portfolio. We also launched a credit insurance product on new car sales and plan to launch a new household product in 2007.

Following the release of a single IT system for agents and head office, all agents will soon be using a common portal and sharing claims functionality in addition to online sales information with head office.

Our combined general insurance and health business reported an operating profit of £63 million (2005: £35 million) with an underwriting result of £6 million (2005: loss of £21 million). The underwriting result benefited from cost savings due to our head office relocation and a favourable claims experience resulting in an improved general insurance COR of 99% (2005: 101%). Our performance reflects a highly competitive market place where competition is fierce and the cycle is following a downward trend. Our net written premiums increased by 2% to £735 million (2005: £726 million) reflecting limited rating increases. However, policy retention rates remain high, despite a change in the regulations regarding annually renewable policies**.

Ireland

Hibernian is the largest general insurer in Ireland, with a market share of 20%. The majority of our business is sourced through brokers with an increasing proportion sourced from direct and corporate partners. We expect further growth in the proportion of business written through our direct channel, particularly in the motor market, while broker distribution will continue to dominate the commercial market. Our strong brand name and expertise in the management of underwriting and claims has allowed us to maintain our leading position.



i Hibernian Direct launches partnership with Vivas Health

Hibernian Direct has linked up with health insurance provider Vivas Health to provide private medical cover under the brand name Hibernian Health Insurance Plan. The plan, launched in November 2006 on a pilot basis for six months, offers customers hospital cover, maternity benefits, out-patient benefits, accident and emergency cover abroad and comprehensive cover for scans. The partnership enhances the range of products that we can offer our customers in Ireland.

U

For more information on Hibernian's healthcare products please visit www.hibernian.ie

** The "Loi Chatel" introduced in August 2005 requires that an insurer must now inform their client in the annual review notice that the client has the right to cancel the policy.

Europe continued

We continue to focus on a multi distribution strategy with organic growth delivered through the enhanced flow of new offerings and creative solutions and the expansion of market segments where we operate.

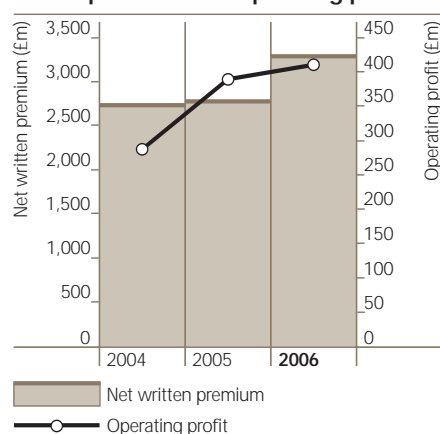
We won in all general insurance categories and retained the best overall general insurer at the 2006 Irish Broker Association service excellence awards. We also won the most effective use of software at the Information Age Effective IT awards. Our motor, van and home insurance policy documents have won the crystal mark for plain English.

During 2006 we have launched a number of new product initiatives providing innovative, customer-focused products. We are developing our internet sales capability to enable us to capitalise on the expected growth of this channel. Building on Hibernian Life & Pension's strategic partnership with Allied Irish Banks (AIB), we will commence selling motor insurance through AIB's website, and will seek to develop further opportunities with AIB in the future. Our partnership with Tesco, through which we sell motor insurance, has been successful, while we also continue to invest in flood mapping technology to improve underwriting and pricing.

Operating profit was stable at £172 million (2005: £171 million) while the COR improved marginally to 77% (2005: 78%). Despite the Irish general insurance market remaining highly competitive, net written premiums increased to £519 million (2005: £499 million). Lower claims costs resulted in an improvement to our underwriting result to £121 million (2005: £116 million).

The market has remained profitable in 2006; however, with premium rates being reduced in key classes of business at present, we expect to see a decline in market profitability from 2007 onwards. There also remains continued uncertainty regarding the impact on the cost of settling claims on the establishment of the Personal Injuries Assessment Board. However, the opportunities provided by the Ark Life acquisition give us the platform from which to grow our business in this developing market.

Europe – General insurance and health premium and operating profit



Netherlands

Delta Lloyd is a top-five general and health insurance provider in the Netherlands selling a range of products including personal motor, household and small commercial policies as well as healthcare policies. Distribution is through intermediaries under the Delta Lloyd brand, directly under the OHRA brand and through our bancassurance joint venture with ABN AMRO Bank.

Developments in our general insurance business in 2006 have included the introduction of the "Xclusive" range of prestige personal insurance products through the intermediary channel, and white label insurance product sales through a pharmacy chain.

In 2006, health provision has been reformed with the amalgamation of public healthcare provision into the private sector. These changes have resulted in lower profitability within the industry and Delta Lloyd has been active in exploring strategic options. One such option was the proposed merger with Agis Health Insurance and Menzis Health and Income that was rejected by Menzis' member council at a late stage in November. Nevertheless, Delta Lloyd remains confident in the future of its healthcare businesses, underlined by its success in writing 45,000 new policies in 2006.

On 8 February 2007, Delta Lloyd announced its acquisition of the Erasmus Group in the Netherlands, which remains subject to regulatory approval. This transaction has a good strategic fit and it is expected to add 12-15% to our existing general insurance business volumes.

Our general insurance and health operating profit was £139 million (2005: £137 million). Our general insurance COR improved to 89% (2005: 93%), reflecting a strong premium rating environment and favourable claims experience, including a low incidence of large claims. Conditions in the health market were less favourable as noted earlier, resulting in an operating profit of £11 million (2005: £40 million).

Profitability in general insurance has been strong, although we have witnessed some weakening of general insurance premium rates towards the end of 2006, a trend we expect will continue into 2007. However, with our focus on cost control through more efficient back-office processes and high quality customer service, we regard 2007 prospects as good.

Other Europe

Our other European general insurance operations are based in Italy, Poland and Turkey. They sell predominantly personal and small commercial insurance through networks of agents and brokers. Our aim for these businesses is to achieve profitable growth and to contribute cash generation in support of our life businesses.

The operating profit from our other European general insurance businesses was £43 million (2005: £47 million), reflecting broadly stable market conditions.

Europe – Fund management

	Operating profit IFRS basis		Operating profit EEV basis	
	2006 £m	2005 £m	2006 £m	2005 £m
France	33	26	10	8
Netherlands	37	32	33	32
Other Europe	3	2	3	2
Continental Europe	73	60	46	42

France

Aviva Gestion d'Actifs (AGA) is widely recognised in the French market as a leading asset manager and we primarily focus on managing funds of the Aviva group. At the end of December 2006, 96% of our managed funds were ranked in the top half for returns over five years. Our strong performance continues to be recognised through a number of awards. In September 2006, *Mieux Vivre Votre Argent* magazine ranked AGA as the best fund manager over the last five years. Eric Duval de la Guierce, head of AGA, was ranked top in Citywire's August league table of the 59 leading French fund managers for his performance over the last three years.

Operating profit has increased to £33 million (2005: £26 million), reflecting our well-established fund management expertise, an inflow of funds from unit-linked sales in our life business and strongly performing equity markets in the early and latter quarters of 2006. We have £50 billion (2005: £46 billion) of funds under management, mostly on behalf of group companies, including the non-linked funds of Antarius, our bancassurance partnership with Crédit du Nord.

Netherlands

Delta Lloyd Asset Management manages investments both for Delta Lloyd's own insurance operations and for third-parties including individual and institutional customers. As well as managing equity and fixed interest funds, our operations also include management of a property portfolio comprising residential premises, offices, shops, and participating interests in unlisted Dutch property funds.

Awareness of the Delta Lloyd mutual funds has improved markedly in the past two years following distinctive marketing campaigns. This development has been supported by recognition of strong investment performance that in 2006 included two Standard & Poor's cash fund awards over three and five years.

Operating profit from our fund management business in the Netherlands was £37 million (2005: £32 million previously reported within non-insurance business). This improvement reflected an increase in funds under management of 9% during 2006, which included an increase in net inflows into institutional funds of £913 million (2005: £573 million). Inflows from individual customers have been lower in 2006 following the exceptional success of Delta Lloyd's select dividend fund in 2005.

Other Europe

Our other European fund management businesses primarily consist of a small operation in Poland, which generated operating profits of £3 million (2005: £2 million).



France: Aviva Gestion d'Actifs wins top investment awards

In France, we won the prestigious Corbeille Long Terme de Mieux Vivre Award for our leading investment position over five years. The Corbeilles, awarded annually by the newspaper *Mieux Vivre Votre Argent*, are a leading benchmark in French asset management. This accolade, repeating our success of 2003, along with the La Tribune/S&P Golden Trophy award that we won in 2004 and 2005, has reinforced Aviva's reputation. This was in addition to the five gold investment awards our investment team had already won during 2006.



For more information on Aviva Gestion d'Actifs please visit www.vam.cgu.fr

International and Morley

Dear Shareholder,

We have made great progress during the past year with our rapidly expanding businesses across the Asia-Pacific region and in North America. The strong growth of profits and sales across the majority of our businesses demonstrates the effectiveness of our highly diversified distribution network and our ability to deliver results from new opportunities.

The purchase of AmerUs in the US has transformed our business in that country, giving us greater access to the world's largest savings market. AmerUs is a leader in the indexed market, ranking number one in sales of indexed life insurance and third in sales of indexed annuities. The combined Aviva USA business is now the fourth-largest long-term savings operation in the Aviva group.

During 2006 we completed a major new bancassurance agreement in India with Centurion Bank of Punjab, and are already seeing a strong performance from this partnership. Aviva India greatly strengthened its market presence, with nearly 200 branches across the country and over 30 bancassurance partnerships.

In February we acquired a 51% stake in Eagle Insurance, the third-largest insurer in Sri Lanka. Through Eagle, we have entered into bancassurance agreements with National Development Bank and Standard Chartered Bank.

Our business in China is now licensed in 15 cities across six provinces. We are on course to achieve our vision of 10% new business market share across ten cities by 2010. We are ranked fifth among foreign joint venture insurance companies in China.

We received a licence to operate in Russia from March 2006, and plan to build a leadership position, with a 10% market share and a top-five position, within the next five years.

Our general insurance business in Canada has broadened its distribution and has introduced innovative products during 2006.

Our confidence in our International long-term savings businesses is highlighted by our expectation that, combined with our European businesses, we shall achieve double-digit organic sales growth over the next five years, while growing new business contribution at least as quickly. We are also committed to meeting or beating the group COR target of 98%.

Strategic developments

Customers in our key markets show an increasing appetite to save for the future. They also want a choice of how to do business with us. These market conditions present a sizeable opportunity, and we are fully committed to working with governments and business partners to satisfy our customers' expectations.

We plan to grow our existing channels. This includes the successful integration of AmerUs into Aviva USA, acceleration of our bancassurance and direct sales success in India and China, deepening our relationship with DBS in Singapore and Hong Kong, and delivery of additional corporate partnerships in Canada.

During 2006, Morley, our largest fund management business, agreed to establish a single investment sales team with our UK long-term savings business, Norwich Union. This agreement will strengthen our presence in the retail and wholesale UK distribution channels. Additionally, Morley acquired ORN Capital, a hedge fund manager, accelerating the development of our alternative investment business. It is vital to the overall strength of the group that we have capacity to offer customers investment products that meet their individual needs.

We intend to diversify our distribution network. For example, we are exploring the development of our bancassurance business in the US by taking advantage of expertise gained elsewhere in the Aviva group and are looking to develop the broker channel in China.

Outlook

Through the acquisition of AmerUs we have created a dynamic and thriving business in the US. The developing markets of the Asia-Pacific region and Russia represent a substantial longer-term area of opportunity for us. We shall be looking to accelerate growth through our strong market positions and key capabilities, notably diversified distribution and product innovation, while continuing to explore the potential of other markets.

Philip Scott
Group executive director





Canada: 10% discount for environmentally friendly drivers

In Canada, we reward policyholders in Quebec who drive hybrid vehicles with an automatic 10% discount on their Aviva auto policy premium.

The discount supports our commitment to environmental management, and fits with our aim to make a leading contribution to the health of the communities in which we operate. It also rewards those of our policyholders who make a conscious choice to protect the environment.

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For more information on Aviva Canada visit www.avivacanada.com



International and Morley continued

Rest of the world – Long-term savings

	2006					
	IFRS profit before tax £m	IFRS operating profit £m	EEV operating profit £m	PVNB [*] contribution** £m	New business contribution** £m	New business margin** %
Asia	9	10	37	685	26	3.8
Australia	59	44	49	297	17	5.7
USA	17	71	32	884	20	2.3
Rest of the world	85	125	118	1,866	63	3.4

	2005					
	IFRS profit before tax £m	IFRS operating profit £m	EEV operating profit £m	PVNB [*] contribution** £m	New business contribution** £m	New business margin** %
Asia	(37)	(30)	30	396	20	5.1
Australia	49	32	44	337	16	4.7
USA	(4)	(4)	25	527	13	2.5
Rest of the world	8	(2)	99	1,260	49	3.9

* Excludes investment sales. Investment sales totalled £1,564 million (2005: £1,151 million) giving overall new business sales of £3,430 million (2005: £2,411 million).

** Stated before the effect of required capital.

Asia

Aviva has a broad range of operations throughout Asia with businesses based in Hong Kong, Singapore, India, Sri Lanka and China. The product ranges, distribution channels and strategies of each operation vary according to local market conditions.

Aviva Singapore and Hong Kong employ a multi-channel distribution strategy including a strong partnership with Development Bank of Singapore (DBS), South East Asia's largest banking group. In 2006, we are ranked fourth in Singapore and 14th in Hong Kong.

Our business in Singapore remains the market leader in the developing IFA segment and in the employee benefits and healthcare segment, with our employee benefits business covering one-in-three working Singaporeans. Our strategy is to broaden and deepen business opportunities with DBS while developing the IFA and international financial solutions market.

In Hong Kong, our business has progressed significantly over the last year with a strong increase in sales both through the development of our IFA channel, which now represents more than half of our sales, and through DBS. The overall insurance market is expected to continue to grow strongly, mainly by the bancassurance and IFA segments.

We expect continued growth in 2007 in the more mature markets of Singapore and Hong Kong.

Aviva India is our joint venture with the Dabur Group in which we have a 26% shareholding, the maximum stake currently allowed by law. Aviva India is ranked seventh overall among private insurance companies and we are a leader in the bancassurance market, where we have over 30 (2005: 17) bancassurance agreements in place. The most significant new agreement in 2006 was announced in January and is with the Centurion Bank of Punjab. On 16 January 2007, we announced a further major bancassurance agreement with IndusInd Bank, one of India's fastest-growing private sector banks with 1.4 million customers and 148 branches, thereby extending our leadership in the bancassurance market. The Indian long-term savings market has significant growth potential. We are continuing to increase our distribution relationships with banks, and have more than doubled our direct sales force to over 14,000 (2005: 6,700), with more than 6,000 in training.

On 1 February 2006, we acquired a 51% interest in Eagle Insurance Company Limited (Eagle), the third-largest insurer in Sri Lanka, for a cash sum of £15 million. At the same time, Eagle entered into a bancassurance agreement with National Development Bank Limited, Sri Lanka's biggest development bank and Eagle's other major shareholder. Eagle has now entered its second bancassurance agreement, with Standard Chartered Bank, and sales commenced in September 2006.

In China, our joint venture, Aviva-COFCO, operates a multi-channel, multi-product strategy. We distribute individual products through our direct sales force, agencies and brokers and banks. We also sell group business both directly and through intermediaries. As our business grows in China, we seek to obtain "first mover" advantage in new cities. In 2006, Aviva-COFCO increased its presence to six provinces, with a total of 15 city branches. We are looking forward to the rapid development of this new market. As at November 2006, Aviva-COFCO was the fifth-largest foreign joint venture (out of a total of 25), based on first year premiums.



i Aviva-COFCO wins consumers' award

Aviva-COFCO received an award for the "most reliable foreign life insurance company" in a poll co-ordinated by Hexun.com, China's leading financial website among Chinese consumers in middle to higher income groups. The poll had approximately 700,000 respondents, who voted for sectors such as insurance, banking, futures and fund management. The key measurements used for the insurance sector were product design and innovation, sales force quality and customer service.

Compared with other foreign life insurance players, Aviva-COFCO was recognised for its professionalism, integrity, and the Aviva parentage.



For more information on Aviva-COFCO visit
www.aviva-cofco.com.cn

Continued economic growth in both China and India offers high potential returns in the longer term and, in both countries, we are actively pursuing growth in cities and provinces with significant long-term potential.

In Taiwan, we have established a branch operation and have signed a memorandum of understanding with First Financial, the owner of First Commercial Bank, to explore a possible alliance.

We are working to finalise our new opportunity in Malaysia with Bumiputra-Commerce Holdings Berhad, which was announced in January 2007 and remains subject to regulatory approval.

Overall, the life EEV operating return from our Asia businesses was £37 million (2005: £30 million) principally due to higher new business contribution which increased by 30% to £26 million (2005: £20 million) driven by our substantial life and pension sales growth of 70% to £685 million (2005: £396 million). Our new business margin was 3.8% (2005: 5.1%), reflecting stronger sales of lower margin limited period single premium offerings in Singapore.

In Singapore and Hong Kong, sales increased to £319 million (2005: £227 million) and to £216 million (2005: £103 million) respectively, reflecting strong sales through our partnership with DBS together with an increase in sales through other distribution channels, notably in the developing IFA channel in Hong Kong. In India and China, sales continue to grow rapidly with our share of sales amounting to £84 million (2005: £32 million) and £50 million (2005: £35 million), respectively. In Sri Lanka, sales have amounted to £16 million since the acquisition of Eagle.

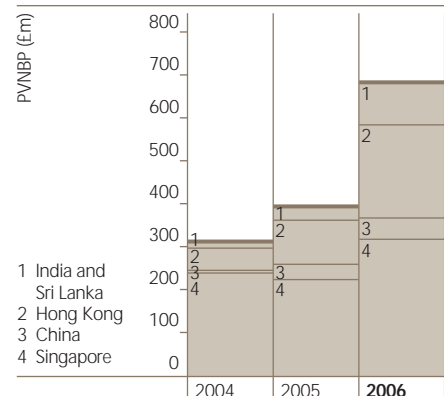
Australia

Aviva Australia primarily focuses on individual protection products and provides wealth management services through the Navigator platform (included under the fund management section). We are ranked seventh in the individual protection market with a rapidly growing market share and we provide market-leading products and services. New business sales in the protection market grew by 13% during 2006. Our strategy is to grow through expanding and diversifying our independent adviser distribution and continuing to expand into new distribution channels through alliances and bancassurance partnerships.

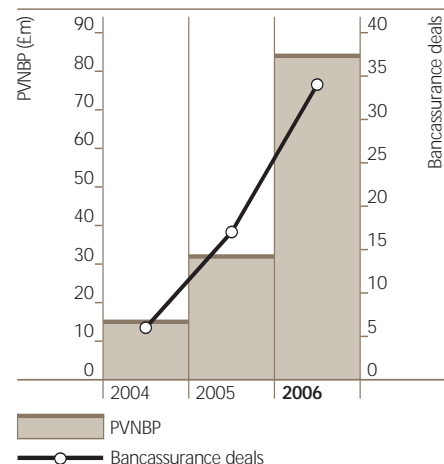
In 2006, new distribution arrangements have been established with AON and AMP for the distribution of our protection products. We have also been placed on the approved product list for Bendigo Bank and ANZ advisers, which provide access to significant new distribution. Our protection product is highly regarded and it was ranked ahead of all competitors in terms of business quality by NMG Consulting. Our business superannuation product has been given the top rating by Chant West Financial Services; however, we have seen a shift from corporate pension sales towards Navigator retirement funds, which we record as investment sales, as a result of changes to superannuation legislation. This trend is expected to continue and is reflected in lower life and pension sales of £297 million (2005: £337 million).

The life EEV operating return was £49 million (2005: £44 million) due to favourable experience variances. New business contribution was £17 million (2005: £16 million), while new business margin increased to 5.7% (2005: 4.7%) benefiting from improved business mix, in particular a higher proportion of protection business.

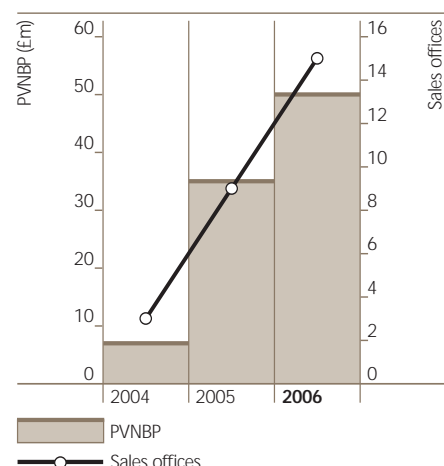
Growth in Asia PVNBP



India – Growth in sales and bancassurance partnerships



China – Growth in sales and sales offices



International and Morley continued

USA

Aviva's presence in the United States market increased four-fold* with the completion of the acquisition of AmerUs on 15 November 2006. AmerUs ranks in the top three in the fixed-indexed segment of the annuity markets and is number one in the indexed life segment, reflecting our strong customer focus and pioneering product development. We are currently integrating the operations of AmerUs with our long established operations based in Boston and generating economies of scale. We plan to grow the combined business by leveraging the knowledge, relationships, products and expertise of both constituent companies.

Our life EEV operating return increased to £32 million (2005: £25 million) including £22 million from AmerUs, which mainly represented contribution from new business and expected return on opening embedded value. In our operations based in Boston, the operating profit was lower at £10 million affected by some one-off negative lapse variances and operating assumption changes. 2006 full year pro forma new business contribution and life EEV operating return for AmerUs amounted to £94 million and £205 million, respectively.

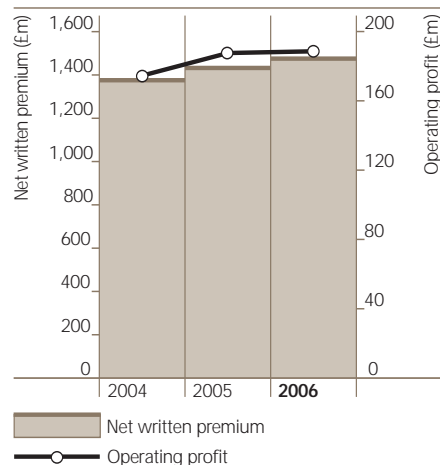
Total new business amounted to £884 million (2005: £527 million) of which £324 million was generated by AmerUs in the six weeks following acquisition. Sales in our operations based in Boston increased by 7% as a result of strong growth of structured settlement products following the A.M. Best rating upgrade to A+ in November 2005. Full year sales by the AmerUs business were £2,261 million (2005: £1,882 million) including £330 million of funding agreement sales (2005: £38 million). Excluding the impact of funding agreements, which are irregular by nature, sales of the underlying life and annuity products showed strong quarter on quarter growth throughout 2006, with the final quarter recording the best ever sales performance.

The medium-term outlook for this market is strong. The US is expected to be the main source of world savings growth in the next 15 years as the "baby boomer" generation of over 70 million people approach and enter retirement. The products of AmerUs, in particular, are tailored to appeal to this market. In the short term there is some disruption to the market, caused by high short-term bond yields and uncertainty regarding the future regulation of fixed-indexed annuities. We do not expect that these factors will diminish the medium- and long-term growth potential.

Russia

Aviva Russia was granted its licence in March 2006 and trading has commenced in corporate sales on a limited scale. Our strategy is to position the business to take advantage of the rapid growth expected to occur as the life insurance industry develops. We aim to achieve at least a top-five market position and a 10% share of the life insurance market within five years.

Rest of the World – General insurance and health premium and profit



i Australia: Navigator helps UK pensions move down under

Navigator, our online fund administration system, has improved the process involved in UK pension transfers. Now, Australian residents with money in UK pension schemes can transfer their funds quicker and more easily.

Navigator is one of the first providers internationally to register with UK regulators as a qualifying regulated overseas pension scheme, which allows UK pension plan members to transfer benefits overseas.

As a leading Australian retirement solutions provider and the UK's top insurer, we have many customers who will benefit from this new development, including many of the Australians who have worked in the UK, either before migrating or when visiting.

We are one of the first businesses in the world to offer this flexibility to our customers.



For more information on Navigator visit
www.navigator.com.au

* Measured in terms of pro forma PVNBP.

Rest of the world – General insurance and health

	IFRS profit before tax £m	IFRS operating profit £m	Combined operating ratio** %	Net written premium £m	Underwriting result £m
Canada	169	148	98	1,389	27
Other	48	40	85	86	11
Rest of the world	217	188	97	1,475	38

	IFRS profit before tax £m	IFRS operating profit £m	Combined operating ratio** %	Net written premium £m	Underwriting result £m
Canada	178	147	97	1,324	35
Other	86	40	97	106	3
Rest of the world	264	187	97	1,430	38

** General insurance business only.

Canada

Aviva Canada is the second-largest general insurer in Canada, with a 9% market share and is the leading insurer in Ontario, Canada's largest general insurance market. Supported by 3,200 employees, in 40 locations and by more than 3,000 independent broker partners, we provide innovative home, motor and business insurance, and a healthcare claims service to over three million personal and commercial customers.

Our business in Canada continues to meet the needs of customers through innovative, market-leading products and services. Where required, the "Premiere Healthcare" claims service provides quality medical services for customers delivered through a network of preferred healthcare providers and this service is also an effective method of managing the cost of claims. We are also continuing the expansion of Autograph, Canada's first pay-as-you-drive motor insurance product.

Our multi-channel, multi-distribution strategy is underpinned by relationships with independent brokers, combined with a commitment to developing corporate partnerships as well as new schemes offered to groups and affinity partners. We continue to develop our e-commerce portal capability, with online quotation and automated workflow tools, and are focused on making it easier for customers and brokers to do business with us.

We are increasing levels of customer and broker satisfaction by leveraging our scale and creating greater efficiencies through investment in claims supply-chain initiatives and in technology platforms.

Our operating profit was stable at £148 million (2005: £147 million) and our COR was 98% (2005: 97%). Our results benefited by £11 million from lower than average weather-related claims. However, this benefit has been offset by lower premium rates on commercial lines and flat rates on personal lines, driven by legislative rate changes. Additionally, rising claims inflation has caused a deterioration in the claims ratio. Although the number of policies written increased in 2006, small decreases in premium rates and high retention levels, which have resulted from customers' lower propensity to switch insurer, have led to net written premiums remaining stable on a local currency basis at £1,389 million (2005: £1,324 million).

We expect 2007 to be another competitive year and we expect that rates will fall slightly. Retention levels are high in the market given stable insurance rates and this is leading to consolidation in the broker channel driven by insurers seeking to buy distribution. During 2006, we have invested in two market-leading group brokers in Quebec, consolidating our position in this key market. The focus for 2007 is to increase our long-term value by broadening our distribution with innovative products, maintaining underwriting discipline and writing only profitable business.

Other

Our other international operations are a health insurance business in Asia, a captive reinsurer in Bermuda and a market-leading general insurer in Sri Lanka, which was acquired in February 2006. The operating profit from our other general insurance and health businesses was £40 million (2005: £40 million).

Morley and rest of the world – Fund management

	Operating profit IFRS basis		Operating profit EEV basis	
	12 months 2006 £m	12 months 2005 £m	12 months 2006 £m	12 months 2005 £m
Morley	76	49	44	26
Rest of the world	12	7	12	7
Morley and rest of the world	88	56	56	33

Our fund management businesses are a key element of the group's strength and balance. They manage the assets of our internal funds and provide fund management services to financial services companies, external pension funds, public sector organisations and specialist distributors of retail financial products. It is important for our customers that we are able to offer funds that are directly invested for the customer in addition to more traditional insurance products, and that we are able to offer a diverse range of funds that meet our customers' individual preferences.

Overleaf, we discuss the results of our largest fund management business, Morley, and our international operations. We have other significant fund management businesses that are reported in the UK and Europe business reviews on pages 31 and 41 respectively.

International and Morley continued

Morley

Morley is one of the largest UK-based active fund managers, with total funds under management of £166 billion (2005: £154 billion) and offices in London, Melbourne, Dublin, Luxembourg, Warsaw, Boston, Milan and Madrid.

We are recognised as a provider of a broad range of specialist fund management solutions to our clients, which include Aviva group companies, many of the UK's largest financial services companies, external pension funds, public sector organisations and public and private companies.

We seek to compete against the best in our industry, by offering high quality products with repeatable out performance in our core areas of fixed income, pan-European equities, property and tactical asset allocation. We also continue to provide and develop a small number of specialist asset classes in areas such as sustainable and responsible investment (SRI) and alternatives.

Our strategy is primarily one of organic growth; however, we actively consider acquisitions where synergies and strategic alignment are compelling. We aim to deliver sustainable and profitable growth through a focus on increasing our revenue by offering higher-margin products in our areas of strength while carefully managing our cost base.

During the year, Morley and our UK long-term savings business, Norwich Union Life, agreed to establish a single team, operating within a joint venture approach, responsible for the sale of collective investment products to consolidate and strengthen our participation in both the retail and wholesale UK sales channels over the long term*.

During 2006, we launched a number of new institutional and retail funds, sold under either the Morley or Norwich Union brand names in the UK, and under the new Aviva Morley Funds brand name overseas.

We also set up new specialist funds to satisfy increasing client demand for absolute return products: the Convertible Arbitrage Hedge Fund, the Absolute Bond Fund and the Absolute Tactical Asset Allocation Fund. Together with Barclays Capital, we launched the Global Balanced and Global Cautious funds, which use derivatives to deliver higher income than could normally be expected from a standard investment portfolio. Our innovative management of these products was recognised by Institutional Investor awarding our fund managers the "equity derivatives end user of the year" award, and we have seen strong early sales flows.

In June, we completed the purchase of a 56% stake in hedge fund management company ORN Capital as part of our strategy to accelerate our alternatives business, adding one multi-strategy and a number of single-strategy hedge funds to our range of absolute return products.

To meet high demand for new property-related investments, we launched new specialist funds, including the European institutional fund Encore+ and a global real estate investment trust product in conjunction with property company CB Richard Ellis Global Real Estate Securities.

The growth of our property funds under management continues apace with strong fund inflows. Our leading property team continues to be recognised by the industry, winning property fund manager of the year from both Property Week and Pensions Management.

People are our core asset and the competition for talent in fund management is particularly intense; hence, we are pleased to have been successful in attracting a number of high quality managers as part of a continuous programme of development and growth. We have been particularly successful in recruiting into our UK equity team during the year.

Corporate responsibility is integral to the way Morley runs its business. Through SRI and our corporate governance activity, we continue to build on Morley's reputation as a responsible investor. Our SRI team continues to be highly regarded in the market and was the only UK-based team to win a UK equities mandate from France's state pensions reserve fund. It was also recognised as "SRI Provider of the Year" by Global Pensions 2006.

Our funds under management increased by £12 billion. We achieved strong sales to third-party life companies and discretionary fund managers and also won a number of institutional mandates across our core asset classes of fixed income, UK equities, property, including specialist partnership vehicles, and asset allocation. Growth in funds under management also resulted from generally positive global investment returns. Finally, in May, we completed the take-on of £3.3 billion of funds from the Ark Life Assurance company resulting from Aviva's bancassurance joint venture with AIB.

The Morley group as a whole achieved strong profit growth in 2006 as operating profit increased to £79 million (2005: £52 million), including a £3 million contribution (2005: £3 million) from our pooled pension business which is reported in the UK long-term savings segment. Our fund management operating profit grew significantly to £76 million (2005: £49 million), reflecting increased investment management fee revenue and higher performance fees, which contributed £14 million (2005: £10 million) to profit and were mainly recognised in the second half of the year. £62 million of the profit was in respect of the UK (2005: £36 million) while overseas businesses, including Hibernian Investment Managers, accounted for £14 million (2005: £13 million). Our fee income benefited from new business mandates and strongly performing investment markets that, coupled with our management of our expense base, delivered a further improvement in our cost/income ratio to 72% (2005: 77%).

We continue to position our business to work with our clients to develop tailored investment solutions and capitalise on the growing demand for specialist investment products.

* Collective investment sales are reported in our UK long-term savings segment.

Rest of the world

Our International fund management businesses consist primarily of Navigator, operating in Australia and Singapore, and a small fund management operation in Canada.

In Australia, Navigator offers full-service and low-cost platforms that give customers access to wealth-creation and post-retirement products and we are ranked seventh in this platform market. Navigator had an excellent year with overall new business growing by 34% in 2006 to £1,110 million (2005: £848 million), benefiting from ongoing improvements in the product offering and a strong focus on customer service. In the 2006 S&P (Assirt) adviser survey, we improved our overall ranking for the third consecutive year and are now above the industry average for overall service levels.

During 2006, we completed a strategic investment in the financial advisory group Infocus Wealth Management as part of our strategy of acquiring strategic stakes in high potential distribution groups. Professional Investment Holdings and Financial Technology Services, in which we purchased stakes in 2005, are performing well.

The Australian financial services market is one of the fastest growing in the world, due in part to compulsory superannuation contributions. We are well placed to take advantage of this rapidly expanding market. Recently announced changes to pension laws and strongly favourable tax legislation are expected to have a positive impact on the platform and fund management industry.

In Singapore, Navigator is a fund administration platform that offers customers cost effective access to a range of mutual funds from different fund managers through one product wrapper. The business continued to grow strongly during 2006 with significantly higher sales of £261 million (2004: £90 million), reflecting strong distribution relationships with key brokers, an increased fund choice and an ongoing buoyant economic environment.

Our businesses reported operating profits of £12 million (2005: £7 million) reflecting strong product offerings and the benefit of buoyant investment markets.



i Morley – Awards:

Morley has enjoyed a year of award-winning progress, with expansion into Europe, innovative product launches and strong performance for our investors.

Our property team continues to be recognised by the industry, winning property fund manager of the year at Property Week Awards 2006 and Property Investment Manager of the Year at Pensions Management 2006, and winning two European awards – Outstanding Company of the Year and Investor of the Year at the Central and Eastern European Real Estate Quality Awards.

Our sustainable and responsible investment (SRI) team continues to be highly regarded in the market and was the only UK-based team to be awarded a UK equities mandate by France's state pension reserve fund. We were recognised as SRI provider of the year by Global Pensions 2006, and we retained our top ranking for our understanding of SRI and extra-financial issues in the Thomson Extel Survey for the fourth successive year.

We are delighted that our hard work, forward thinking approach to asset management and focus on SRI issues continues to be recognised by our peers, clients and industry associates.



For more information on Morley visit
www.morleyfm.co.uk

Finance

Dear Shareholder,

To achieve leading financial management and control, we are required to have an increasingly forward-looking view. We are actively involved in the many debates that will affect reporting developments in our industry such as IFRS phase II on insurance contracts and the EU's Solvency II directive. These are some time from being implemented, yet the debates that will influence their final positions are happening now.

Capital management

Capital strength is important to us since it gives us flexibility to take advantage of opportunities to create value for our shareholders and customers. We have further strengthened our capital position during the year. Equity shareholders' funds have increased by 18% to £17.5 billion and our excess solvency margin, as measured under the insurance group's directive, was £3.6 billion (2005: £3.6 billion), reflecting the acquisition of AmerUs having reduced the margin by £0.7 billion and the impact of funding the pension scheme deficit. The underlying strong operational performance demonstrates the capital generative nature of our businesses. The ability to generate capital is a key strength of the group and enables us to fund both organic growth and bolt-on acquisitions from our internal capital resources.

Additionally, rating agencies have recognised this strength by reaffirming the ratings of our main operating subsidiaries, AA/AA- (very strong) from Standard & Poor's and Aa3 (excellent) from Moody's, both with a stable outlook.

During 2006, we have continued to develop a capital management framework that utilises individual capital assessment (ICA) principles. Using an ICA model provides a close link between capital and risk management. It is important that we increasingly match the amount of capital that we hold to the relative risks that we face. Our ICA model clearly demonstrates that our diversified business, in terms of geography, products and distribution dramatically reduces the amount of economic capital required to protect against the risk of insolvency. Such risk-based capital models are increasingly being used to inform our decision-making processes and will, in time, allow us to improve capital efficiency.

Our return on equity shareholders' funds of 13.1% (2005: 15.0%), exceeds our stated target return of 12.5%, notwithstanding our opening shareholders' funds being £3.2 billion higher than a year earlier.

Reporting changes

2006 has been a year of considerable change and development in the financial reporting arena. In March, we published our first financial statements under IFRS, requiring changes to accounting systems and extra disclosures. Additionally, we are now seeing the introduction of enhanced requirements for the narrative elements of our reporting. These changes are challenging our finance teams to understand, produce and explain a much greater volume of information. I was therefore delighted that our hard work in these areas was recognised at the prestigious 2006 *IR Magazine* UK awards where we won the prize for "best disclosure by a FTSE-100 company", an excellent achievement.

Solvency II

Solvency II represents a great opportunity for us to establish a fairer deal while promoting Europe as a truly single market. The current system of insurance supervision and regulation is a blunt instrument that has not succeeded in creating a level playing field for insurers, is capital inefficient and can ultimately lead to higher prices for consumers. The industry already suffers from a myriad of different measures against which it is assessed. It will be important to align regulatory and accounting measures more closely with the underlying economics of the business. This is a unique opportunity to shape 21st century supervision to the benefit of all and we are fully committed to the project.

Outlook

We have built a reputation for professionalism and prudence, but we also have a forward thinking outlook. We remain committed to efficiently managing risk and capital, while continuing to seek out innovative ways to improve our processes, controls and risk and capital management.

Andrew Moss





Finance strategy

To cope with the ever-developing demands of the financial and regulatory landscape, we have refreshed and revised our finance strategy. The new strategy incorporates the four Cs:

- Capital – Increasingly integrating our management of risk and capital
- Capability – Attracting and retaining talented professionals who add value to our business
- Consistency – Generating trusted data from efficient processes and systems
- Cost – Running a cost-effective finance function across our businesses

The four strands of the strategy set out above are fundamental to us achieving our longer term aims for our finance community. They will allow us to provide an operating platform that has a robust risk and control environment, meets FSA requirements and meets the governance expectations of the Aviva board.



Finance continued

Capital

Capital structure

We maintain an efficient capital structure using a combination of equity shareholders' funds, preference capital, subordinated debt and borrowings. This structure is consistent with our risk profile and the regulatory and market requirements of our business. We believe that the European Embedded Value (EEV) provides a more meaningful view of our life operations than IFRS; accordingly, our capital structure is analysed on an EEV basis.

In managing our capital, we seek to:

- Match the profile of our assets and liabilities, taking into account the risks inherent in each business
- Maintain financial strength to support new business growth while still satisfying the requirements of policyholders, regulators and rating agencies
- Retain financial flexibility by maintaining strong liquidity, access to a range of capital markets and significant unutilised committed credit lines
- Allocate capital efficiently to support growth and repatriate excess capital where appropriate
- Manage exposures to movements in exchange rates by aligning the deployment of capital by currency with our capital requirements by currency.

Capital management principles

An important aspect of our capital management process is the setting of target rates of return for individual business units. The targets are adjusted to make allowance for risks faced by those business units. Management remuneration is partly based on performance against these targets, therefore encouraging focus on creation of value for the shareholder.

We have a number of sources of capital available to us and seek to optimise our debt to equity structure so we can maximise returns to our shareholders. We consider alternative sources of capital such as reinsurance and securitisation in addition to more traditional sources of funding. We select capital funding that is appropriate to its deployment and usage.

Capital employed by segment

The table below shows how our capital is deployed by segment and how that capital is funded:

	2006 £m	2005 £m
Long-term savings	19,663	15,598
General insurance and health	5,344	5,581
Other business	1,425	1,876
Corporate	(19)	(36)
Total capital employed	26,413	23,019
Financed by:		
Equity shareholders' funds and minority interests	19,668	16,356
Direct capital instrument	990	990
Preference shares	200	200
Subordinated debt	2,937	2,808
External debt	1,258	1,002
Net internal debt	1,360	1,663
	26,413	23,019

At 31 December 2006, we had £26.4 billion (*31 December 2005: £23.0 billion*) of total capital employed in our trading operations.

In 2006, the total capital employed increased by £3.4 billion reflecting growth in our long-term savings operations; these increased by £4.0 billion driven by the acquisitions of AmerUs, operational results and movements in equity markets in the year.

In addition to our external funding sources, we have internal debt arrangements in place. These arrangements have allowed the assets that support technical liabilities to be invested in a pool of central assets for use across the group. They have also allowed the redeployment of cash between parts of the business to fund growth. Although these arrangements are intra-group loans, they are included as part of the capital base for the purpose of capital management. Our intra-group loans satisfy arms length criteria and all interest payments have been made when due.

Net internal debt represents the upstream of internal loans from business operations to corporate and holding entities net of tangible assets held by these entities.

The corporate net liabilities represent the element of the pension scheme deficit held centrally.

Financial leverage

Financial leverage, the ratio of the group's external senior and subordinated debt to EEV capital and reserves was 20% (*2005: 22%*). Fixed charge cover, which measures the extent to which external interest costs, including subordinated debt interest and preference dividends, are covered by EEV operating profit was 10.3 times (*2005: 9.6 times*).

We are subject to a number of regulatory capital tests and employ realistic scenario tests to allocate capital and manage risk. Overall, the group and its subsidiaries satisfy all existing requirements and, as reported below, has significant resources and capital strength.

The ratings of the group's main operating subsidiaries are AA/AA- (very strong) with a stable outlook from Standard & Poor's and Aa3 (excellent) with a stable outlook from Moody's. These ratings reflect our strong liquidity, competitive position, capital base, increasing underlying earnings and positive strategic management.

Different measures of capital

We measure our capital using different bases that include measures that comply with the regulatory regime in which we operate and measures that the directors consider appropriate for effective management of the business. The measures that we use are:

Accounting basis

We are required to report our results on an IFRS basis; however, the directors consider that EEV principles provide a more relevant and meaningful view of our life operations and so we analyse and measure the net asset value and total capital employed for the group on this basis.

Regulatory basis

Relevant capital and solvency regulations are used to measure and report the financial strength of our insurance subsidiaries. These measures are based on local regulatory requirements and are consolidated under the European Insurance Groups Directive (IGD). The regulatory capital tests verify that we retain an excess of solvency capital above the required minimum level calculated using a series of prudent assumptions about the type of business written by our insurance subsidiaries.

In addition to the FSA realistic reporting regime, the UK Accounting Standards Board requires certain capital disclosures to be made in accordance with Financial Reporting Standard 27, *Life Assurance* (FRS 27). The purpose of the capital statement is to set out the financial strength of the entity and to provide an analysis of the disposition and constraints over the availability of capital to meet risks and regulatory requirements. The disclosures required by FRS 27 are set out in note 49.

Economic bases

We believe that economic capital provides a clear measurement of the risks facing our business. Additionally, it informs the amount of capital that we need to hold to mitigate the risk of insolvency. We provide full details of our economic measures of capital in the "Risk and capital management" section on page 57.

Group

Accounting basis

Our capital funding is allocated so that the capital employed by trading operations is greater than the capital provided to those operations by the shareholders and subordinated debt holders. As a result, we are able to enhance the returns earned on our equity capital.

	2006	2005
Shareholders' funds – EEV basis	£20.9bn	£17.5bn
Total capital employed – EEV basis	£26.4bn	£23.0bn
Net asset value per share – EEV basis	683p	622p

Shareholders' funds have increased by £3.4 billion to £20.9 billion (2005: £17.5 billion), reflecting our strong operational performance in 2006.

Accordingly, our net asset value per ordinary share, based on equity shareholders' funds was higher at 683 pence per share (2005: 622 pence per share).

Regulatory basis – European Insurance Groups Directive

	2006	2005
Insurance Groups Directive (IGD) excess solvency	£3.6bn	£3.6bn
Cover (times)	1.8 times	1.8 times

As at 31 December 2006, we had an estimated excess regulatory capital of £3.6 billion (2005: £3.6 billion), as measured under the European Insurance Groups Directive. This measure represents the excess of the aggregate value of regulatory capital employed in our business over the aggregate minimum solvency requirements imposed by local regulators, excluding the surplus held in our UK life funds.

In broad terms, for our long-term business, the minimum solvency requirements are set at 4% and 1% for non-linked and unit-linked reserves respectively. For our general insurance portfolio of business, the minimum solvency requirement is the higher of 18% of gross premiums or 26% of gross claims, in both cases adjusted to reflect the level of reinsurance recoveries. For our other major non-European businesses (USA, Australia and Canada), a risk charge on assets and liabilities approach is used.

Our excess solvency of £3.6 billion reflects operational performance generating solvency capital during the year, offset by the acquisition of AmerUs, which reduced the solvency surplus by £0.7 billion, and the funding of the pension deficit. From 31 December 2006, we have been required to have positive solvency on an IGD basis. Our risk management processes ensure adequate review of this measure at all times.

Finance continued

Long-term businesses

Regulatory basis

For our non-participating worldwide life insurance businesses, our capital requirements are set as the higher of:

- Target levels set by reference to internal risk assessment and internal objectives
- Minimum capital requirements (ie the level of solvency capital at which the local regulator is empowered to take action).

Having assessed the level of operational, demographic, market and currency risk of each of our life businesses, the required level of capital for each business is quantified and expressed as a percentage of the EU minimum. The required capital across our business varies between 100% and 250% of the EU minimum or equivalent.

The weighted average level of required capital for the whole of our non-participating life businesses, expressed as a percentage of the EU minimum solvency margin or equivalent is 134% (2005: 128%). This is a blended rate and is expected to change over time with changes in the product mix.

The required capital levels discussed above are used in the calculation of our embedded value to assess the cost of locked-in capital. At 31 December 2006, the aggregate regulatory capital, based on the requirements of the EU minimum test amounted to £4.3 billion (31 December 2005: £3.9 billion). As at this date, the actual net worth held in our long-term businesses was £8.9 billion (31 December 2005: £7.2 billion), which represents 206% (31 December 2005: 183%) of these minimum requirements. The increase in this ratio reflects the impact of favourable equity market performance on the net worth and acquisition of AmerUs.

UK life operations

Available capital

The realistic inherited estate represents the available capital of our with-profit funds. It is comprised of the assets of the long-term with-profit funds less the realistic liabilities of non-profit policies, less asset shares aggregated across the with-profit policies and any additional amounts expected at the valuation date to be paid to in-force policy holders in the future in respect of smoothing costs, guarantees and promises.

Realistic balance sheet information is shown below for the three main UK with-profit funds:

- CGNU Life
- Commercial Union Life Assurance Company (CULAC)
- Norwich Union Life & Pensions (NUL&P)

The realistic liabilities have been included in the gross insurance liabilities and the gross liability for investment contracts on our IFRS balance sheet at 31 December 2006.

	31 December 2006		31 December 2005		
	Estimated realistic assets Ebn	Realistic Liabilities*† Ebn	Estimated realistic inherited estate‡ Ebn	Estimated risk capital margin Ebn	Estimated excess Ebn
CGNU Life	14.3	(11.8)	2.5	(0.5)	2.0
CULAC	14.1	(11.6)	2.5	(0.5)	2.0
NUL&P#	27.7	(25.9)	1.8	(0.6)	1.2
Aggregate	56.1	(49.3)	6.8	(1.6)	5.2

* Realistic liabilities include shareholders' proportion of future bonuses of £0.7 billion (31 December 2005: £0.7 billion). Realistic liabilities adjusted to eliminate shareholders' proportion of future bonuses are £48.6 billion (31 December 2005: £50.5 billion).

† Realistic liabilities make allowance for guarantees, options and promises on a market consistent stochastic basis. The value of this provision included in realistic liabilities is £0.5 billion, £0.7 billion and £3.0 billion for CGNU Life, CULAC and NUL&P respectively (31 December 2005: £0.7 billion, £0.9 billion and £3.4 billion respectively).

‡ The estimated realistic estate at 31 December 2005 was £2.1 billion, £1.9 billion and £1.2 billion for CGNU Life, CULAC and NUL&P respectively.

The risk capital margin is 4.2 times covered by the estimated realistic inherited estate (31 December 2005: 2.7 times).

The NUL&P fund includes the Provident Mutual (PM) fund, which has realistic assets and liabilities of £2.3 billion and therefore does not impact the realistic inherited estate.

The aggregate investment mix of assets in the three main with-profit funds at 31 December 2006 was:

	31 December 2006 %	31 December 2005 %
Equity	42	42
Property	16	15
Fixed interest	36	37
Other	6	6
Total	100	100

The equity backing ratios, including property, supporting with-profit asset shares are 74% in CGNU Life, 74% in CULAC and 65% in NUL&P. With-profit business is mainly written through CGNU Life.

Possible reattribution of the inherited estate

We continue to investigate the possibility of a reattribution of the inherited estate of two of our with-profit funds: CGNU Life and CULAC. In February 2006, we announced the nomination of Clare Spottiswoode as policyholder advocate, a consumer led role created to represent policyholders, under new Financial Services Authority (FSA) rule governing reattribution.

In November, we agreed terms of reference with Clare Spottiswoode, and she has agreed to accept the role of independent policyholder advocate. The appointment has been approved by the FSA. We are confident that Clare Spottiswoode's experience as both a regulator, and as a company director, makes her qualified to represent independently the with-profit policyholders' interests and negotiate on their behalf. During her nomination period, Clare Spottiswoode has:

- Established an independent office
- Set up a technical team, including actuarial and legal support
- Familiarised herself with a reattribution scheme under FSA rules
- Prepared plans for extensive consultation with policyholders
- Agreed her terms of reference for any reattribution with Aviva, in consultation with the FSA.

At this stage, no decision has been taken to proceed with the reattribution, which will only take place if there is agreement on a fair outcome for policyholders and shareholders. This will include agreement by us and the independent policyholder advocate on any incentive payments to eligible with-profit policyholders.

General insurance

Economic basis

We use a number of measures of risk-based capital to assess the capital requirements for our general insurance businesses. Financial modelling techniques enhance our practice of active capital management, verifying that sufficient capital is available to protect against unforeseen events and adverse scenarios, and to manage risk. Our aim continues to be an optimal use of capital.

UK regulatory basis

Our main UK regulated general insurance subsidiaries are Aviva International Insurance Group (All) and Norwich Union Insurance (NUI). The combined businesses of All and NUI have strong solvency positions. The table below sets out the regulatory capital position of the general insurance groups at 31 December 2006:

	2006		2005	
	NUI	All group	NUI and All group pro forma	NUI and All group pro forma restated
Capital resources (£bn)	1.1	7.4	8.5	7.5
Capital resources requirements (£bn)	0.4	4.1	4.5	4.0
Solvency surplus (£bn)	0.7	3.3	4.0	3.5
Cover (times)	3.1	1.8	1.9	1.9

In aggregate, the estimated excess solvency surplus, representing the capital resources assets over the capital resources requirement, was £4.0 billion (*31 December 2005 restated: £3.5 billion*) after covering a minimum capital base of £4.5 billion (*31 December 2005 restated: £4.0 billion*).

The 2005 figures for All group, and consequently the NUI and All group pro forma, have been restated to reflect admissibility and counterparty restrictions relating to intercompany balances following a revised application of the technical rules. There is no economic impact on the All group or on our capital adequacy (IGD) calculation.

Finance continued

Risk

The Group's approach to risk and capital management

As part of our overall corporate governance framework described on pages 77 to 81 we have established a risk and financial management structure whose primary objective is to protect the group from events that hinder the achievement of our objectives, our financial performance, or cause us to fail to exploit opportunities.

We have established a number of policies that deal with the management of both financial and non-financial risks. These policies set out risk appetite, risk management and

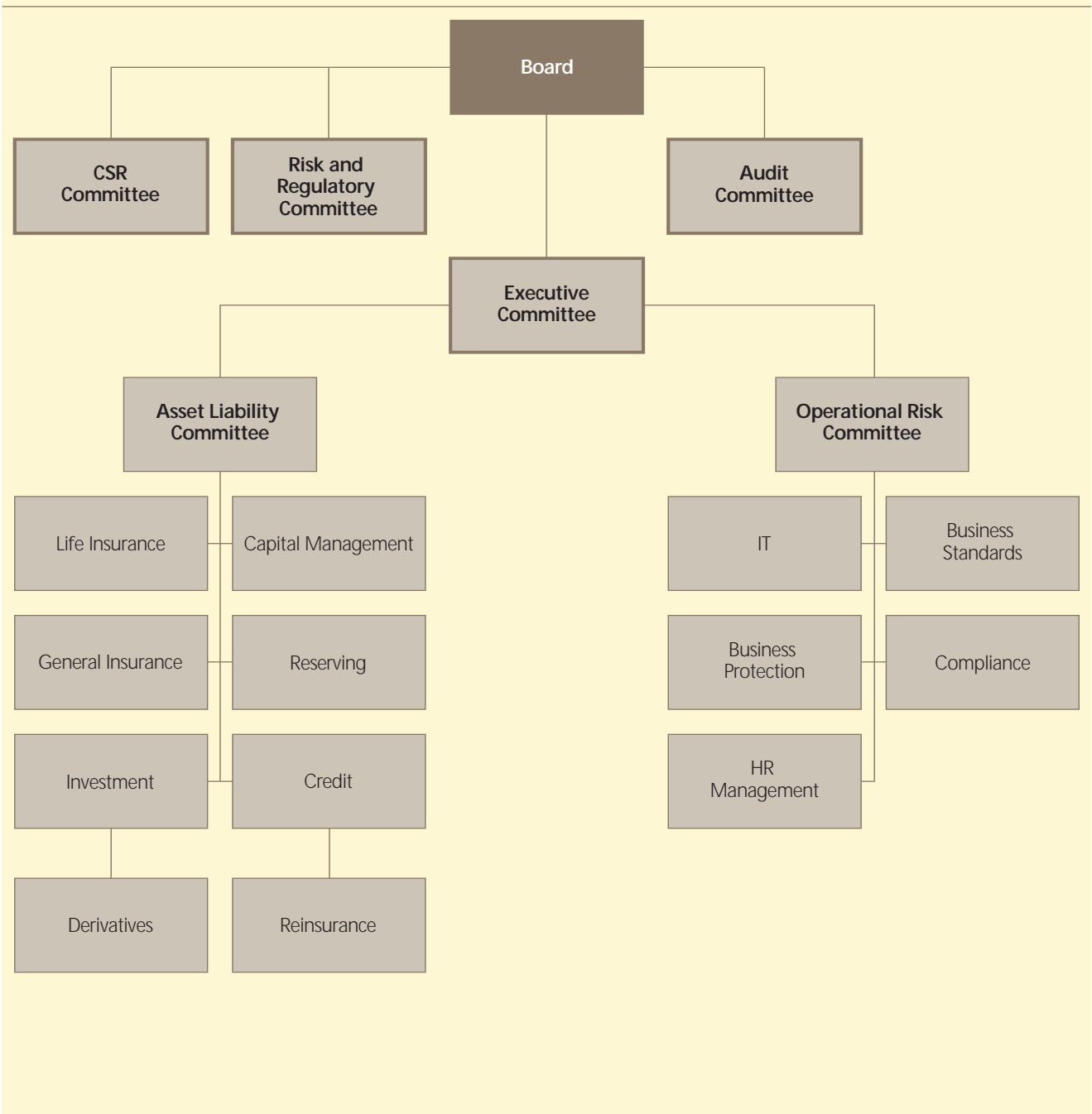
control and business conduct standards for the group's worldwide operations. They enable a broadly consistent approach to the management of risk by business units.

For each policy, a member of senior management is responsible for overseeing compliance with that policy throughout the group.

Additionally, we operate a number of oversight committees, to monitor aggregate risk data, take risk management decisions, and to enforce the implementation of the policies. Our finance and risk management committee structure is set out below.

Our governance structure and policies are regularly reviewed to reflect the changing commercial and regulatory environment, and our own organisational structure.

Risk Committees: Financial and Operating Risk



Risk and capital management

We believe that the measurement of economic capital provides a clear and consistent way to monitor and compare the risks in our businesses.

We have developed a capital management framework using Individual Capital Assessment (ICA) principles for identifying the risks that business units, and the group as a whole are exposed to, quantifying their impact on economic capital.

Our ICA estimates how much capital is needed to mitigate the risk of insolvency to a selected remote level, based on a number of stress tests applied to the capital position of the business. These tests, covering both investment and insurance scenarios, are specified centrally to provide consistency between business units to achieve a minimum standard. Additionally, business units can supplement the tests with others applicable to their own situation. The events that are tested may not occur at the same time; therefore we allow for the degree of correlation between them that we might expect. We also allow for diversification benefits (ie when two very different risks have offsetting impacts if they happen at the same time) when aggregating risks, or when aggregating business unit results. This means that the sum of the risks is less than the total of all the individual risks.

The ICA works to a 99.5% confidence level of solvency over one year (equivalent to events occurring in one out of 200 years), in line with UK Financial Services Authority (FSA) regulatory requirements. An ICA has been developed for all material parts of the group, and the results of financial and operating experience tests are linked to our risk reporting model. We also produce projections of the ICA requirement over a number of years to show how the economic capital position is likely to evolve.

ICAs have now been produced for a number of years and the results are used as a basis for discussion with the FSA. ICA analysis is now used in our key decision making processes.

Our ICA uses a mixture of scenario-based testing and risk-based capital models. We are continuing to develop our risk-based capital modelling capability for all of our businesses as part of our longer term program to introduce more complex risk modelling techniques. These risk-based capital techniques will provide a more detailed assessment of the capital needs of the business over a range of probabilities of insolvency and different time horizons. We intend to operate our business increasingly by reference to economic and risk-based capital (RBC) requirements.

We also use financial condition reports (FCRs). FCRs cover the medium-term financial outlook of the business, including forecasts of the overall financial position and key performance indicators under a variety of economic and operating scenarios, allowing for new business sales, to inform our capital and risk management decisions.

We monitor specific risks on a regular basis through our risk-monitoring framework. Our businesses are required to disclose all material risks along with information on the likelihood and severity of these risks and the mitigating actions taken or planned. This process enables us to assess the overall risk exposure of the group, to develop a group-wide risk map identifying concentrations of risk and to define the risks that we are prepared to accept. This risk map is continually monitored and is refreshed quarterly.

The risks facing Aviva

Our ICA models inform us about the relative impact on economic capital from the risks we face, enabling us to formulate mitigating strategies. The types of risks in our business and the way in which we manage them are discussed in detail below.

Market risk

We are exposed to considerable potential adverse financial impact from changes in the values of our investments, caused by changes to interest rates, property prices, and foreign exchange rates. Our business has market risk from fluctuations in both the values of assets held and the value of liabilities. At a group level, we have market risk from owning a portfolio of international businesses whose values can change, and from assets that support the liabilities of our staff pension scheme.

We recognise that such risk is inevitable from the businesses that we run, and that a certain level of market risk is acceptable in order to deliver benefits to both policyholders and shareholders.

For each type of market risk, we have developed clear policies and procedures on how that risk should be monitored and managed, either within our business units or at a group level. Our group investment committee (GIC) is responsible for overseeing market risk and asset liability management.

For example, the GIC identifies the levels of market movement at which mitigating actions should be taken. Actions could include buying downside protection against movements in equity prices or interest rates. The GIC also considers aggregation of market risk, including indirect market risk exposure from our staff pension schemes, and formulates risk appetite decisions for the amounts invested in different types of asset.

Finance continued

We also continually monitor the financial impact of changes to market values through a number of measurements of economic capital or sensitivities to key performance indicators.

Several of our longer term savings businesses sell products where the majority of the market risk is borne by the policyholder. Any market risk attributable to policyholders is prudently managed to satisfy the policyholders' objectives for risk and reward.

Our market risk policy sets out the minimum principles that business units are expected to follow in managing the assets backing the technical insurance liabilities. We have set standards for the way businesses should match their liabilities with appropriate assets, and have a clear decision-making and monitoring process to be followed when liabilities cannot be matched or a degree of mismatching is desired. We regularly monitor how business units are performing asset liability management (ALM) at both the group investment committee and group asset liability management committee. ALM issues are considered as part of our business risk reporting, and in determining ICA and RBC capital requirements.

Equity price risk

Our largest market risk exposure is to changes in equity prices. We believe in the long-term benefits of holding equities and are prepared to accept the consequential shorter term fluctuations in our shareholder funds. For example a 10% decrease in equity prices* causes a £768 million pre-tax decrease in the level of shareholders' funds on an IFRS basis and on an EEV basis would reduce embedded value by £1,065 million, net of tax.

Our GIC continually monitors exposure against a risk appetite set and agreed by the Board, and has a process in place to manage the exposure in different market conditions, including extreme movements.

We monitor concentrations of equity risk, for example from material shareholdings in our strategic business partners, or from equities held in our staff pension schemes. We formulate our equity risk management strategy taking into account the full range of our equity holdings.

Interest rate risk

Interest rate risk is the risk that arises from both the products we sell and the value of our investments due to changes in the level of interest rates. For example, long-term debt and fixed income securities are both exposed to fluctuations in interest rates. We are exposed to reductions in interest rates on business carrying investment return guarantees, and to interest rate increases on business carrying surrender value guarantees. A 1% decrease in interest rates would increase shareholders' funds on an IFRS basis by £806 million pre-tax and on an EEV basis would increase embedded value by £310 million, net of tax. Sensitivities to increases in interest rates are shown in note 50 and the section on EEV reporting.

We manage our interest rate risk in a number of ways. In some categories of our long-term business, we reduce interest rate risk through the close matching of assets and liabilities. On short-term business such as general insurance business, we require a close matching of assets and liabilities by duration to minimise this risk.

If we cannot entirely remove exposure through matching, we also use a variety of derivative instruments including futures, options, swaps, caps and floors in order to hedge against unfavourable market movements in interest rates.

Property price risk

We invest in property assets, in a variety of locations worldwide that are exposed to fluctuation in values. We believe investing in these assets provides long-term benefits for our businesses and clients. Investment in property is managed locally by our business units, subject to the risk appetite of that business unit, and within any local regulations on asset admissibility or liquidity.

Foreign currency exchange risk

We operate internationally and we are therefore exposed to the financial impact arising from changes in the exchange rates of various currencies. Over half of our premium income arises in currencies other than sterling and our net assets are denominated in a variety of currencies, but predominantly in sterling, euros and US dollars.

We generally do not hedge foreign currency revenues, as we prefer to retain revenue locally in each business to support business growth, to meet local and regulatory market requirements, and to maintain sufficient assets in their local currency to match local currency liabilities. We are also exposed to some exchange risk from assets held in staff pension schemes, as a part of the investment strategy agreed with the scheme trustees.

Movements in exchange rates may affect the value of consolidated shareholders' equity, which is expressed in sterling. This aspect of foreign exchange risk is monitored centrally against limits that we have set to control the extent to which capital deployment and capital requirements are not aligned. We use currency borrowings and derivatives when necessary to keep currency exposures within these predetermined limits, and to hedge specific foreign exchange risks when we feel it is appropriate; for example, in any acquisition or disposal activity.

Derivatives risk

We use derivatives in a number of our businesses to enable efficient investment management, to hedge investment risks, or as part of structured retail savings products. Derivatives can involve complex financial transactions and to minimise the risks involved we have set minimum standards we expect our businesses to adopt when using derivatives and our group derivatives committee monitors exposures, the control framework, and approves any proposed transactions that fall outside the local business unit policy limits.

* Effect of decrease in equity prices includes the effect of a 10% decrease in property prices.

Credit risk

We have a significant exposure to credit risk through our investments in corporate bonds, commercial mortgages, and other securities. We hold these investments for the benefit of both our policyholders and shareholders. We monitor and manage two types of credit risk. Firstly, we manage the exposure to individual counterparties, by measuring exposure against centrally set limits. The aggregate exposure we are prepared to accept takes account of credit ratings issued by rating agencies such as Standard & Poor's. We also manage the level of risk we are prepared to take, and we are using increasingly detailed analysis to define our optimal balance between risk and reward, monitoring the types of investment available to us to achieve best our aims.

Our group credit committee (GCC) takes responsibility for monitoring credit exposures to individual counterparties and determining who we are prepared to work with. Our GIC sets the credit risk appetite as part of our overall management of market risk.

We are also exposed to credit risk through our use of reinsurance. Our reinsurance security committee, part of our GCC, verifies that reinsurance arrangements are only placed with providers who meet our counterparty credit standards.

Life Insurance risk

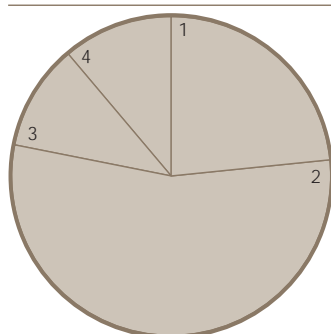
Our life insurance businesses are exposed to the full range of life insurance risks from the products that they have written, typically mortality, morbidity risk, as well as experience on persistency and unforeseen expenses.

Our policy on life insurance risk sets out the practice standards we expect our business units to follow in underwriting such risks, and our life insurance risk committee regularly monitors its application, and develops detailed guidance on managing the major areas of risk, and sponsors the sharing of best practice between businesses.

We have a significant exposure to annuity business and our most significant life insurance risk is associated with longevity. Longevity statistics are monitored in detail, compared with emerging industry trends, and the results are used to inform both the reserving and pricing of annuities. Inevitably, there remains uncertainty about the development of future longevity that cannot be removed. Should our annuitant mortality assumptions worsen by 5% then shareholders' equity would decrease by £300 million pre-tax on an IFRS basis and decrease embedded value by £185 million on an EEV basis, net of tax.

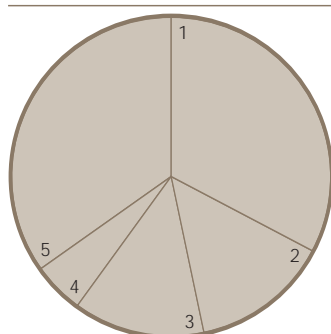
Our business units manage mortality and morbidity risk on protection business using reinsurance and while they can select reinsurers locally, we review reinsurance coverage across the group and our overall reinsurance program is assessed centrally to manage group-wide risk exposures. Sensitivity tests show that we are not materially affected by mortality risk. Our equity reduces by only £20 million for a 5% worsening in assurance mortality experience on an IFRS basis and decreases embedded value by £165 million on an EEV basis, net of tax.

Shareholders equity by currency



- 1 Sterling
- 2 Euro
- 3 US dollar
- 4 Other

Credit risk exposures



- 1 AAA
- 2 AA
- 3 A
- 4 BBB
- 5 Speculative grade and not rated**

** Not Rated includes mortgages and other debt that does not attract an external rating.

Finance continued

Persistency risk is managed at a business unit level through frequent monitoring of current experience, benchmarked against local market information. Actual experience against the expected level of lapses is also assessed within the analysis of embedded value operating profit. Where possible, the financial impact of lapses is reduced through appropriate product design. The group life insurance risk committee has developed guidelines on persistency management, sharing best practice on the setting of lapse assumptions, product design, experience monitoring, and management action.

Expenses are managed at a business unit level, as part of general business management.

General Insurance risk

Our general insurance businesses are exposed to a typical range of general insurance risks from the business that they underwrite. Such risks include:

- Fluctuation in the timing, frequency and severity of claims and claim settlements compared to that expected when the business was written
- Unexpected claims arising from a single source
- Inadequate reinsurance protection or other risk transfer techniques
- Inadequate reserves.

Our group general insurance risk committee (GIRC) oversees the risk management framework, within a clearly communicated underwriting strategy. We have, as a group, made a clear statement on the target for the combined operating ratio (COR). To achieve this goal, we operate technical management committees focusing on each of our key general insurance risks in detail for example, underwriting, claims management, and reinsurance.

Our largest risk is claims incurred from catastrophe events. This risk is controlled through monitoring risk aggregations and using catastrophe reinsurance cover.

Another material risk is the impact of worsening claims ratios. This risk is actively managed through business unit focus on underwriting discipline, control of claims management, and finding innovative solutions to the way we measure and price the risk we underwrite. For example, our UK business has developed digital flood mapping to understand better the risk to household insurance from flood damage, and has developed “telematics”, our Pay As You Drive™ technology to provide a closer link between risk and pricing.

We actively use reinsurance to help reduce the financial impact of a catastrophe and to manage the volatility of our earnings. Reinsurance purchases are reviewed annually at both business unit and group level to verify that the protection we have purchased matches the level of exposure. Reinsurance arrangements are only placed with providers who meet our counterparty security standards. We use extensive financial modelling and actuarial analysis to optimise the cost and risk management benefits from our reinsurance program.

We cede much of our worldwide catastrophe risk to third-party reinsurers, but retain a pooled element for our own account, gaining diversification benefits. Our total retained risk increases as catastrophe events become more remote, so that our total loss from our most concentrated exposure (northern European wind storm) is approximately £370 million for a one in ten year event, compared to approximately £700 million for a one in 100 year event.

Liquidity risk

Maintaining sufficient available liquid assets to meet our obligations as they fall due is an important part of our financial management practice. Our business units must all operate controls to identify sources of liquidity risk, monitor potential exposures, and manage their liquidity requirements. At group level, we maintain a prudent level of liquidity consistent with the expectations of the FSA and the investment community. We also maintain a buffer of liquid assets to cover unforeseen contingencies including the provision of temporary funds to any of our business units that experience temporary liquidity shortfalls.

Operational risk

We are also exposed to operational risk arising from inadequately controlled internal processes or systems, human error and from external events. This includes all risks that we are exposed to, other than the financial risks described above and strategic and group risks. Operational risks include, for example, information technology, information security, human resources, project management, outsourcing, tax, legal, fraud and compliance.

Our business units are primarily responsible for identifying, managing and reporting these risks as part of our quarterly risk reporting processes. Each operational risk is assessed by considering the potential impact and the probability of the event occurring. Impact assessments are made against financial, operational and reputational criteria.

Business unit management teams must be satisfied that all material risks falling outside our risk appetite are being mitigated, monitored and reported at an appropriate level. Any risks with a high impact level are continually monitored centrally.

Our operational risk committee (ORC) determines the risk appetite that the group can work within for these types of risk, assesses and monitors overall operational risk exposures, identifying any concentrations of operational risk across the group, and in particular verifies that mitigating action plans are implemented.

Accounting basis of preparation**International Financial Reporting Standards (IFRS)**

The consolidated financial statements and financial data contained in the report and accounts has been prepared using the group's accounting policies on an IFRS basis, as set out on pages 104 to 113. These policies are in accordance with standards issued by the IASB and endorsed by the EU, including the early adoption of IFRS 7 as detailed in policy A. The date of transition from UK GAAP to IFRS was 1 January 2004.

Where applicable, the financial statements have also been prepared in accordance with the Statement of Recommended Practice (SORP) on accounting for insurance business issued by the Association of British Insurers (ABI) in December 2005, as amended in December 2006.

IFRS 7 covers disclosures for financial instruments, and replaces earlier standards on this subject. Although the new standard extends the disclosures in the financial statements in several places, it does not affect the policies themselves.

The only change to the accounting policies in 2006 has been from an amendment to the financial instruments standard (IAS 39) that deals with accounting for financial guarantee contracts. While not material at the consolidated group level, this does affect the company and its subsidiaries in respect of inter-company guarantees given and taken.

European Embedded Value (EEV) basis of reporting

We present the results and financial position of our life and related businesses on an EEV basis, in addition to the IFRS basis. The directors' opinion is that the EEV basis provides a more relevant and transparent view of the performance of the life and related operations year-on-year than the results presented under the IFRS basis. The EEV methodology adopted is in accordance with the EEV Principles introduced by the CFO Forum in May 2004, and the additional guidance on EEV disclosures published by the CFO Forum in October 2005.

On an EEV basis, the value of a policy recorded in the year of sale takes into account future cash flows relating to that policy. Various assumptions are used to estimate the present value of a policy. In subsequent years, the present value of the policy is adjusted only to reflect changes in the assumptions used.

In contrast, on an IFRS basis, the value of a sale does not take into account future cash flows. These subsequent cash flows are recorded in the year in which they occur. The recorded value of a sale will reflect the premium received to date, the cost of setting up an appropriate reserve, costs incurred in acquiring that business and an allowance to recognise some of these acquisition costs should be deferred and earned in line with the premium. Therefore, the value associated with writing the same business will be recorded differently in the year of sale on EEV and IFRS bases. However, the total profit recognised over the full lifetime of an insurance policy is the same as under the IFRS basis of reporting. We believe that the EEV basis gives a fairer indication of the profitability of business on inception.

Additionally, shareholders' funds on an EEV basis incorporate internally generated additional value of in-force business (AVIF), which is excluded for IFRS reporting. Our incentive schemes and internal management reporting are aligned to the EEV basis. These financial statements include supplementary information on EEV reporting in the "Alternative method of reporting long-term business" section.

Longer term investment return

The long-term nature of much of our operations means that short-term realised and unrealised gains and losses on general insurance and health business are shown as an adjustment to operating profit. We focus instead on operating profit incorporating a longer term investment return (LTIR). Our rates of return that we use for equity and property in our LTIR methodology are aligned with the rates that we use under EEV principles. For fixed interest securities, we include the amortisation of premiums or discounts arising on purchase, thereby producing an LTIR that is equivalent to the gross redemption yield.

Critical accounting policies and estimates

The preparation of our financial statements requires us to make estimates and assumptions that affect items reported in the consolidated income statement, balance sheet, other primary statements and notes to the financial statements. All estimates are based on management's current knowledge, assumptions based on that knowledge, and their predictions of future events and actions. Actual results can always differ from estimates, possibly significantly.

The table below sets out those items that we consider particularly susceptible to changes in estimates and assumptions, and the relevant accounting policy. Full details of the accounting policies are set out on pages 104 to 113.

Item	Accounting policy
Insurance product classification	E
Insurance and participating investment contract liabilities	J
Goodwill, AVIF and other intangible assets	M
Impairment of financial investments	R
Fair value of derivative financial instruments	S
Deferred acquisition costs and other assets	U
Provisions and contingent liabilities	X
Pension obligations	Y
Deferred tax	Z

Future accounting developments

We seek to take an active role in the development of new accounting standards, via industry forums and working parties, and reviewing and providing comment on proposals from the International Accounting Standards Board (IASB).

Phase II of the IASB's project on insurance contracts remains the most significant area that we are tracking. During 2006, the insurance industry has worked closely with the IASB in seeking to develop a comprehensive global accounting standard for insurance that will reflect the economics of our business. In June 2006, the CFO Forum representing the large European insurers, in which we play an active role, published principles for measurement and recognition of insurance liabilities. We now await publication of the IASB's preliminary views in the first quarter of 2007. This is the first stage in the development of the IASB's standard and it is unlikely to be finalised before the end of 2009 at the earliest. The range of possible outcomes remains large; therefore, it is too early to predict the impact this change in accounting will have. While this standard is under development, we will continue to focus on EEV as the best measure of value for our long-term business.

We continue to monitor other major IASB projects including financial statement presentation, liabilities, revenue recognition and fair value measurement. The announcement from the IASB that no new standards or major amendments would become mandatory before 2009 and that the level of public consultation in the development of new standards would increase was welcomed.

Employees and responsibility

Dear Shareholder,

Around the world Aviva is committed to attracting and retaining the best talent available. We aim to engage our people in their work, achieve our ambitions and provide a great customer experience. The key to our success is great leaders, making the most of all our talents and exploiting our international opportunities. Aviva has to be a company people want to work with and our people strategy is focused on achieving that.

Responsibility

We are aware of our responsibilities and are committed to behaving in a socially responsible way. How we do business helps us to achieve our ambition of being the world's most trusted savings, investments and insurance provider.

I am determined that we will maintain our sector-leading reputation in corporate social responsibility (CSR) and we have further important initiatives underway to keep us there.

2006 developments

In 2006, we implemented a worldwide employee survey that allows us to benchmark our performance as an employer against the best in the world, identify and share good practice, and focus our efforts on issues that mean the most to our employees.

We launched task forces on three key people-related challenges: building great leadership across Aviva; delivering talent management offerings that enable our people to achieve their potential; and leveraging the power of the Aviva brand for our current and future employees. I am confident we will be able to report significant benefit from these initiatives next year.

Keeping Aviva fit for the future remains vital and not all the answers are easy ones. In 2006, we announced plans to restructure our UK businesses to improve both efficiency and the service we provide to our customers, with the loss of 4,000 jobs. We will do all we can to minimise the impact on individuals through management of turnover, redeployment and voluntary departure. We will help those who leave the business to do so with dignity and support.

The formation of a board CSR committee in 2006 raised further the profile of our CSR agenda. Our decision to carbon neutralise our operations worldwide represents a significant commitment. Aviva is the first global insurer to commit to doing so. We also became a founder member of Oxfam's 365 Alliance, ensuring that Oxfam has pre-committed, planned resource in anticipation of any disaster across the globe.

Valuing diversity and respect at work are a fundamental part of our culture. In 2006, we launched a global senior women's network group, introduced a range of recruitment practices aimed at attracting minority groups and provided tools to encourage our employees to engage with and understand our diversity agenda.

Our rapid progress as a forward thinking employer has been recognised through several awards, such as inclusion in *The Times* "top 50 places where women want to work," (Aviva being the only company to feature in all categories assessed) and the city category award from *Opportunity Now*.

Outlook

We have begun 2007 by welcoming, as Aviva employees, 1,500 people in India who had been serving our customers through third-party employers. That process will continue this year.

We will continue to build our reputation as an employer of choice and a responsible corporate citizen. Our people and CSR agendas are at the heart of that ambition and I look forward to reporting next year on the progress we have made in 2007.

John Ainley
Group human resources director





p Aviva joins Oxfam 365 Alliance

Aviva was one of the first companies to join the Oxfam 365 Alliance, a new initiative developed by Oxfam GB to support its global emergency response operations. To join the Alliance, companies must commit to providing between £500,000 and £1 million over three years. The funding will provide extra help for the international charity's expanding rapid response team of aid workers and will help run the warehouse which stores one of the world's largest supplies of emergency equipment. With these resources, Oxfam will always be ready to deal with disasters immediately, wherever and whenever they occur. Oxfam will also provide aid to crises which often go unnoticed by the world's media.

For Aviva, the Oxfam 365 Alliance is a perfect demonstration of forward thinking in practice. We are proud to be a part of it.

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For more information on our CSR programmes visit
www.aviva.com/csr



In Mwamakaranga village, Tanzania, approximately 300 children benefited from Oxfam's school feeding programme. Eight million people across East Africa faced an acute food livelihood crisis in 2006. Over the past year Oxfam has provided emergency support, helping people to deal with shortages of food and water, and more recently, with severe flooding. Alongside this, Oxfam is increasing its work with communities to find longer-term solutions.

Photo credit: Maite Alvarez/Oxfam

Employees and responsibility continued

Responsibility

Our ambition is simple: we want to be the world's most trusted savings, investment and insurance provider. This means that we must always work to the highest standards of business conduct. This sits at the heart of our approach to corporate social responsibility (CSR).

We recognise there are multiple stakeholders in our CSR activities:

- Our shareholders, who wish to receive a return on their investment, but also to be assured that the company is behaving responsibly in how it operates
- Our customers, who rightly expect us to treat them fairly and to be open and honest in the products and services we offer them
- Our staff, whose engagement and commitment to delivering a great service to our customers is key. They want to be treated with respect at work and to feel proud of being a part of Aviva
- The communities in which we operate, and the suppliers and organisations with which we work, who want us to be a responsible employer and partner, thinking about the way we do business and acting responsibly to the benefit of all.

This review seeks to set out how our CSR activities support our overall business strategy while taking account of the views of our different stakeholders.

We report our progress on CSR fully in a separate annual CSR report, which is available online at www.aviva.com/csr.

CSR governance

We report annually in accordance with the FORGE management and reporting guidelines, and respect the disclosure guidelines issued by the Association of British Insurers.

In 2006 we established a Board CSR Committee, which met three times during the year. It is chaired by Aviva's senior independent director, Wim Dik, and consists of Aviva's chairman, three other non-executive directors and the group chief executive. It is responsible for CSR strategy and policy, and for reviewing the progress of our CSR programme. The CSR Committee report can be found on page 86.

We held an annual CSR review group meeting, bringing together CSR representatives from our business units, partner non-governmental organisations and external auditors. The review group looks at performance, developments and best practice; it exchanges ideas and initiatives and sets the direction for the year ahead. A CSR steering group meets three times a year to review progress.

Developing a diversity strategy and programme has been an important initiative during the past two years. Supported by Aviva's annual global employee climate survey, our diversity aims have been integrated into our performance management process.

From January 2007, the CSR and diversity functions have been combined into one CSR team with a wider remit. This team will take the lead on a more comprehensive set of activities that form our CSR agenda. The wider remit establishes clearer accountability for the delivery of our CSR programme in one place.

To mitigate CSR risks, we have an established system of risk management embedded into our business planning and performance monitoring processes. Further details of this process are contained in the internal controls section of the corporate governance report.

Standards of business conduct

We are committed to conducting all aspects of our business to rigorous ethical, professional and legal standards. We regard ethical practice as critical to responsible business and have put in place measures to refresh regularly our employees' understanding of our standards of business conduct policy.

The policy is reinforced by specific measures to tackle the challenge posed by financial crime. We have implemented policies that meet the requirements of applicable legislation, regulatory guidance and industry best practice regarding anti-money laundering, fraud management and malpractice reporting worldwide.



i New board CSR committee

One of our chairman Lord Sharman's first initiatives was to demonstrate our commitment to corporate social responsibility by creating a board CSR committee.

The committee comprises Lord Sharman, group chief executive Richard Harvey and non-executive directors Carole Pivnicka, Guillermo de la Dehesa and is chaired by Aviva's senior independent director, Wim Dik. The CSR committee met three times in 2006 to provide guidance and direction for the group's CSR programme and monitor its progress.



For more information on our CSR programmes visit www.aviva.com/csr

Customers

Given our ambition, we put our customers at the heart of everything we do. We are committed to:

- Having better insight on the events that shape our customers financial needs and designing products and service to help them meet those needs
- Providing customers with good service and information that is clear, balanced, fair and not misleading when they buy our products
- Helping our customers after they have bought our products by honouring our promises, giving good service, and providing helpful information
- Where appropriate, working with our customers' financial advisers to serve our customer's interests.

In 2006, the Board approved a group customer policy that embeds these commitments into the way we work in our businesses around the world.

This policy means that leaders in our businesses must demonstrate an uncompromising standard of commitment to customers, with performance against the policy measured as part of the way we look at business performance.

We comment here on progress across our core business activities under our key operating regions: UK, Europe and International and Morley.

United Kingdom

Norwich Union Life helped develop the Association of British Insurers Customer Impact Scheme. The scheme aims to improve performance across the life insurance industry and so improve the experiences of our customers.

This scheme helps support our obligations under the Financial Services Authority's Treating Customers Fairly initiative. The Customer Impact Scheme includes:

- formal commitments by our board that put customer interests at the heart of our business
- participation in an annual in-depth customer survey to measure how well we are doing
- a detailed annual report showing how well we have met the customer commitments (available June 2007)
- a panel with members from both the industry and outside to oversee the scheme, advise the ABI and report on progress.

In helping to champion consumer issues, Norwich Union is collecting data from telematics black boxes on how often, when and where motorists drive. This enables both transparent insurance premiums and appropriate safety messages to different customers.

In addition, Norwich Union has numerous product innovations for example, discounted insurance for bio-ethanol fuelled Ford cars and a simplified life insurance product.

Europe

Aviva France has promoted the concept of "le bon conseil" stressing the importance of proper advice and research prior to purchase. In particular, we have been fast and efficient in our adaptation of new laws in comparison to market competition.

In Delta Lloyd, our Dutch subsidiary, all employees participated in a commercial training programme to help encourage the organisation to become more customer minded. Other initiatives included employees visiting customers to obtain their views on products and services. Further, to help improve transparency of life products and provision, Delta Lloyd simplified its cost structure and lowered the costs of life products. It also promotes transparency of life products on its website.

International and Morley

Aviva India has implemented various initiatives to help control mis-selling, from enforcing guidelines for policy sales, taking action against agents who do not comply and carrying out "mystery shopping" activities to monitor how policies are sold to carrying out independent customer satisfaction studies. Similarly, to avoid agent mis-selling in Aviva-COFCO China, we have training programmes in place that provide strict certification of agents across China.

During the year, Morley's sustainable and responsible investment (SRI) team reached the £1 billion mark in its SRI funds under management. The SRI team, has seen continued growth from both retail and institutional channels since joining Morley in 2001.



i Aviva remains in global lists of sustainable corporations

We continue to be the only UK insurer included in both the Dow Jones Sustainability World and STOXX Indexes, and we are a member of the FTSE4Good Index series. These indices track the performance of the leading sustainability-driven companies worldwide. We are particularly proud of our scores for environmental reporting (100%), social reporting (98%) and code of conduct (97%) in the Dow Jones Sustainability World Index.

These listings recognise the commitment we are making to thinking about the future in a socially responsible way. It is apparent that investors are increasingly taking account of these ratings when making investment decisions.



For more information on our CSR programmes visit www.aviva.com/csr

Employees and responsibility continued

Environment

We are committed to a programme of management, continuous improvement and reporting of our direct and indirect environmental impacts.

As a forward thinking insurer we are making provision for the effects of climate change through adapting and creating new products and services to meet this challenge. We will work with others to understand better the implications of climate change and play our part in helping to develop and deliver society's continuing response.

We are managing and reducing, where possible, our own CO₂ output and encourage others to do the same, using our influence as an investor and purchaser. In 2006, our total CO₂ emissions increased largely due to the inclusion of emissions data, for the first time, from the RAC and AutoWindscreen fleets and buildings, and our Asian businesses. From our existing businesses, emissions have shown a slight increase, reflecting more business travel related to operational requirements and the upgrading of our managed property portfolio in respect of air-conditioning. We will continue to focus on reducing our energy use and look to source zero emission power where we can. We will offset our remaining emissions on a retrospective basis starting with emissions generated in 2006. We will compensate for the carbon output of our consumption of non-renewable sourced electricity and gas from buildings and business travel, including air, car and train, across all of our global operations.

We are also looking at ways in which to help our customers reduce their own CO₂ emissions through the provision of innovative products such as "Pay As You Drive™" and by offering reduced premium insurance for drivers of hybrid and flexi-fuel Ford cars.

Our general insurance operations have been seeking solutions to limit the effects of climate change on customers through its flood mapping and lobbying on the issue of flood defences and floodplain planning.

Suppliers

We regard our suppliers as our partners and work with them to help us achieve our policy aspirations in the delivery of our products and services.

In 2006, we revised our group purchasing policy. We include CSR in our supplier tendering process and in some of our businesses, require suppliers to sign up to a code of conduct.



i First insurer to go carbon neutral worldwide

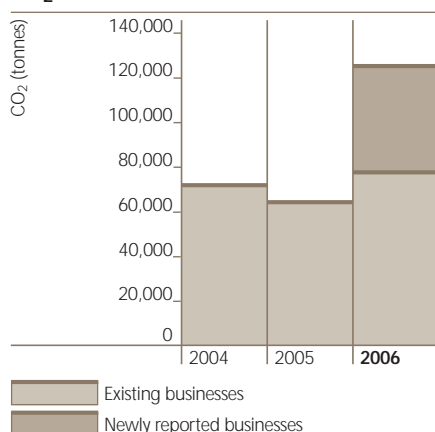
Aviva is committed to becoming the first insurer to carbon neutralise its operations on a worldwide basis. This is an important further step in our efforts to limit our environmental impact, following our progress with energy efficiency and use of zero emission electricity. For example, 55% of electricity used by Aviva globally is obtained from zero emission sources.

We shall offset the remaining emissions – about 125,000 tonnes a year group-wide – on a retrospective basis, starting with 2006. We will achieve this by compensating for carbon output from our use of non-renewable sourced electricity and gas in buildings and business travel by investing in projects that generate carbon credits. The credits will come from carbon mitigation methods, such as tree planting, and renewable energy generation projects that do not release carbon to the atmosphere, such as solar or wind power.

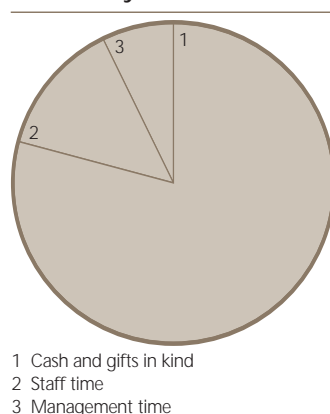
Our decision to go carbon neutral is a significant step. We believe climate change to be the most important environmental issue facing the world. As a forward thinking company, we are playing our part in addressing this challenge and would encourage other businesses to follow suit.

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For more information on our CSR programmes visit www.aviva.com/csr

CO₂ emissions

Community investment



Community

We are committed to working in partnership with the communities in which we operate. In 2006, we invested £6.3 million in community initiatives worldwide. Our investment includes 34,000 hours of staff volunteering.

Our forward thinking approach is reflected in our support for numerous community initiatives around the group.

In September 2006, Aviva became one of the founding partners of Oxfam's 365 Alliance. This unique alliance enables corporate donors to fund Oxfam's initial response operations that will enable it to immediately deal with disasters whenever and wherever they occur around the world. This includes a global rapid response team of aid workers and the UK's biggest warehouse with a stockpile of emergency supplies.

We supported two Breakthrough Breast Cancer walks in the UK to help raise money and awareness for this very worthy cause. Aviva Canada supported a similar event by hosting "pit stops" in seven Canadian cities during The Weekend to End Breast Cancer.

Looking ahead

Our business units have defined local challenges and relevant issues in their market environments. Across the group, we will continue to embed CSR and to identify suitable initiatives that will help to develop and progress this agenda.



i Sponsorship of breast cancer events – UK and Canada

In line with the spirit of our "Forward thinking" campaign, we supported two major events in 2006 with the shared vision of a future free from the fear of breast cancer.

In seven cities across Canada last summer, we were national sponsors of "The Weekend to End Breast Cancer", which saw thousands of people take part in fundraising walks. We sponsored a "pit stop" in each city – designated places along the 60km course where walkers could rest briefly during their trek. The stops were staffed by Aviva volunteers, friends and family, and £27 million was raised in total by the event.

In the UK in September, we were title sponsor of the Aviva Weekend to Breakthrough Breast Cancer. In London and Birmingham, more than 2,000 walkers raised a total of £5.3 million from the two events. Our staff were among the hundreds of volunteers who gave their time to help with tents, serve meals and distribute water and goodie bags to the walkers.

It was very gratifying that so much money was raised by these events on both sides of the Atlantic to help fund research into ways of combating breast cancer.



For more information on our CSR programmes visit www.aviva.com/csr



i Leading the way in micro-finance

In India, we continue to build on our partnerships with leading development finance institutions. These institutions excel in the provision of micro-financial services to the underprivileged section of Indian society. To date we have covered over 650,000 lives in the social sector.

Morley's socially responsible investment (SRI) team also supports micro-finance initiatives. It participated in the successful raising of \$60 million from investors in the UK, Europe and the US to lend to micro-finance institutions (MFIs) for a period of five years. MFIs provide people with small collateral-free loans at reasonable interest rates. Specifically, Morley purchased a \$1.5 million note for one of Norwich Union's sustainable future funds, which helped create the foundation for the entire structure. This initiative will finance approximately 300,000 micro-loans in Latin America, eastern Europe and southeast Asia over the five year life of the structure



For more information on our CSR programmes visit www.aviva.com/csr

Employees and responsibility continued

Employees

Our relationship with our people

Aviva's strategy and focus is changing. We know that fundamental to achieving our ambition to become the world's most trusted savings, investment and insurance provider is keeping our promises to customers and employees. We need to become a truly customer and employee centric organisation. As a result, in 2006, we have developed a new people strategy that looks to the future, towards positioning us as a great brand for our customers and employees, in both our mature and developing markets. Our people strategy comprises five aims:

- To create a "leaderful" organisation, recognising the right of each employee to be led by great leaders who excite their teams to exceptional performance in serving customers
- To move beyond succession planning to talent management, to maximise developmental and business rewards for the company and its people
- To internationalise Aviva, sharing and developing talent across our business units
- To measure our people assets, to understand our human capital and how it can be grown
- To build Aviva as a strong employment brand, clearly communicating what we stand for, so that we can draw talent into the organisation and deliver a great employee experience across the employment life cycle.

In each of our 32 business units around the world, this people strategy, along with our values and our human resources policies, drives and governs our interactions with our employees.

Our human resources policies govern our relationships with our people. The policies cover management development and training, reward, diversity, recruitment and health and safety. View these at www.aviva.com/csr.

In our annual global employee survey, we achieved further improvement in the measures of employee engagement and leadership.

Employee engagement	+8% on prior year
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Leadership	+4% on prior year
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Additionally, we are making progress against a global financial services benchmark

Employee engagement	3% below benchmark
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Leadership	2% below benchmark
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Our values

In everything that we do, we are mindful of our brand values. They inform not only what we do, but the manner in which we do it. Our values are set out below:

Progressiveness

Being progressive is having a vision of the future, encouraging innovation and improvement, and championing continuous learning. It is about leading the industry by listening and responding to customers and keeping ahead of the competition.

Integrity

Integrity is behaving in a way consistent with professional and ethical standards. It is being open, honest and keeping commitments, taking personal responsibility for what we say and do. It is about earning trust and respect through honesty and fairness.

Performance

Performance-driven is having clear goals and achieving them by everyone working towards them in an efficient manner.

Teamwork

Teamwork is the lifeblood of Aviva. It means commitment to a common vision and objectives, depending on one another, pulling together and sharing knowledge and learning. It is creating a sense of community and belonging in how we operate as a business. It means taking pride in Aviva's achievements.

Leadership and talent

We want our employees, the external recruitment market and our shareholders to recognise us as an organisation that develops exceptional leaders. At Aviva, we passionately believe that all our people have talent. We aim to create an environment where our people can give their best, feel valued and be able to develop competitive skills for the future. While adopting this inclusive view of talent, we need to become more rigorous in differentiation, providing our people with development paths that are tailored to their particular needs. The cornerstone of this approach will be the development and implementation of a common framework across the group for describing talent in terms of past performance and the predictive indicators of potential. The focus for 2007 will be the implementation of the infrastructure, systems and capabilities to enable this.

The Aviva leadership academy (ALA) underpins our talent development strategy and delivers a range of highly sought after, world-class programmes in conjunction with renowned international business schools.

To emphasise the importance of great leadership, each of our business units is required to measure leadership performance. This performance, along with measurements of engagement and customer satisfaction, is a key element of determining senior manager bonuses across the group.

A global workforce serving our customers

We are an international business, with a hugely diverse range of customers. In 2006, we employed 59,000 people in 22 countries, with 65% of these people telling us through our global climate survey that "my business unit is a great place to work."

A diverse workforce, meeting diverse customer needs

Our senior management population:

Total female 18%
Total male 82%

Total Aviva workforce:

Total female 49%
Total male 51%

To reflect our customer base, we continue our focus on diversity and on making our workforce increasingly international. In 2006, our global diversity steering group oversaw the implementation of a "respect" campaign promoting diversity best practice. The group also made a decision to sponsor networks for women and for lesbian, gay and bi-sexual employees. Plans are in place for 2007 to develop more networks, particularly to promote multi-cultural understanding, and to introduce targets for the number of international assignments in place around the business.

External surveys and monitoring organisations provide us with an opportunity to measure our progress in embracing diversity. Recognition in 2006 included the Opportunity Now "City" award, appearance in *The Times*' "Top 50 places where women want to work," an Opportunity Now Gold award (an improvement on 2004 and 2005's bronze and silver ratings) and a silver award from Race for Opportunity.

In the UK, to maintain Norwich Union's position as a highly efficient and effective company, and to respond to changing customer buying habits, a planned UK headcount reduction of 4,000 by 2008 was announced in 2006. Part of this reduction relates to duplication of roles in functional areas such as marketing, human resources, finance and information technology due to the bringing together of the Norwich Union Life and general insurance business. The remainder relates to increasing the number of roles (in line with plans announced in 2005) in the Indian and Sri Lankan operations that currently support Norwich Union and Aviva Canada customers. Reinforcing the importance of our brand values and of how we interact with our customers, we will be transferring more than 5,000 employees of third-party suppliers in India and Sri Lanka into our own offshore division, Aviva Global Services during the course of 2007.

We are seeking to minimise the number of compulsory redundancies from this restructuring through voluntary turnover and redeployment. In addition, we are supporting those who may be facing redundancy by offering consultancy, out placement, financial planning services and job search assistance.

Looking ahead

In 2007, we will be undertaking specific projects towards the goals articulated in our people strategy, including embedding a methodology for accounting for our human capital in the group's performance management system and in its external reporting.



INSEAD

i Aviva Leadership Academy

We believe in the talent of our employees and we aim to create an environment where they can give their best, feel valued and develop their skills. The Aviva leadership academy is an integral part of our talent management strategy and plays a key role in building and retaining leaders. The academy programmes emphasise experiential learning, networking and the development of everyday authentic leadership skills. The programmes are progressive and reflect the changing needs of our employees as they move through the organisation.

We are a leading member company of the Centre For Executive Development (Cedep) located in Fontainebleau, France and work in conjunction with this organisation and leading international business schools including Columbia Business School, The Centre for Creative Leadership, Wharton, INSEAD and Yale to design and develop cutting-edge programmes that respond to our changing environment.



For more information on our CSR programmes visit www.aviva.com/csr



It's you and me

Board of directors

Richard Harvey FIA (56)

Group chief executive

Appointed to the board in May 2000 and became group chief executive in April 2001. Joined Norwich Union in 1992, holding senior positions in New Zealand and the UK before joining the Norwich Union board in 1995 and becoming group chief executive of Norwich Union in 1998. Former chairman of the Association of British Insurers. Richard Harvey will retire as the group chief executive in July 2007.

Member of the nomination and corporate social responsibility committees.

Andrew Moss (48)

Group finance director

Appointed to the board in May 2004 upon joining the company. Previously director – finance, risk management and operations in Lloyd's (*insurance*) and formerly held a number of senior management positions at HSBC plc (*banking*). Andrew Moss will succeed Richard Harvey as the group chief executive in July 2007.

Philip Scott FIA (53)

Executive director

Appointed to the board in May 2000. Joined Norwich Union in 1973 and held a number of senior positions before joining the Norwich Union board in 1993. Currently responsible for the group's insurance businesses outside Europe and Morley, the group's UK fund management operations. Philip Scott will succeed Andrew Moss as the group finance director in July 2007.

Patrick Snowball (56)

Executive director

Appointed to the board in March 2001. Joined the group in 1989, holding a number of senior positions before joining the board of Norwich Union in 1999. Currently responsible for the group's United Kingdom businesses namely Norwich Union Insurance, Norwich Union Life and RAC. A member of the Financial Services Authority's Practitioner Panel.

Lord Sharman of Redlynch OBE (64)

Chairman

Appointed to the board in January 2005 and became chairman on 1 January 2006. Currently chairman of Aegis Group plc (*media services*), an independent non-executive director of BG Group plc (*utility*) and Reed Elsevier plc (*publisher*) and a member of the supervisory board of ABN AMRO N.V. (*banking*). Former chairman of KPMG International (*auditors*), former deputy chairman of Group 4 Securicor plc (*security services*) and a former independent non-executive director of Young & Co.'s Brewery PLC (*drinks*) and AEA Technology plc (*commercial/technology*).

Chairman of the board and nomination committees and a member of the corporate social responsibility committee.

Guillermo de la Dehesa (65)

Independent non-executive director

Appointed to the board in May 2000. Joined the board of Norwich Union as a non-executive director in 1999. Currently non-executive chairman of Aviva's operations in Spain, non-executive vice-chairman of Goldman Sachs Europe (*banking*) and a non-executive director of Campofrio (*consumer*), Unión Eléctrica Fenosa (*utility*) and Bank Santander Central Hispano (*banking*). Chairman of the Centre of Economic Policy Research and a member of the Group of Thirty (*consultative group on international economic and monetary affairs*). A former deputy governor of the International Monetary Fund and the World Bank, a former deputy general manager of the Bank of Spain and former Secretary of State of Finance in Spain.

Member of the nomination and corporate social responsibility committees.

Richard Harvey

Lord Sharman of Redlynch

Andrew Moss

Philip Scott

Patrick Snowball



Wim Dik (68)

Senior independent non-executive director

Appointed to the board in December 1999. Currently chairman of the supervisory board of Zesko Holding B.V. (*telecommunications*) and Tele Atlas N.V. (*information systems*), a non-executive director of Unilever N.V. and Unilever plc (*consumer*) and of LogicaCMG plc (*computer services*). Former Minister for Foreign Trade in the Netherlands. A former chairman of Nederlandse Unilever Bedrijven B.V. (*consumer*) and former chairman and chief executive officer of KPN Royal Dutch Telecom (*telecommunications*). A former chairman of the supervisory board of Holland Casino (*gaming*) and a former member of the supervisory boards of TNT Post Group (*mail services*), Vos Logistics (*transport*) and ABN AMRO N.V. (*banking*).

Chairman of the corporate social responsibility committee and member of the nomination and risk and regulatory committees.

Mary Francis CBE (58)

Independent non-executive director

Appointed to the board in October 2005. Currently senior independent non-executive director of Centrica plc (*utilities*), a non-executive director of St Modwen Properties plc (*property development*), a director of the Bank of England, Fund Distribution Limited and Almeida Theatre Company Limited. A member of the advisory board of the National Consumer Council and Governor of the Pensions Policy Institute. A former Director General of the Association of British Insurers and senior civil servant.

Chairman of the risk and regulatory committee and a member of the audit and remuneration committees.

Richard Karl Goeltz (64)

Independent non-executive director

Appointed to the board in May 2004. Currently a non-executive director of the Warnaco Group Inc (*clothing*), Federal Home Loan Mortgage Corporation (Freddie Mac) (*financial services*), New Germany Fund (*investment trust*) and a director of The London School of Economics and Political Science. A former chief financial officer of American Express Company (*financial services*), NatWest Group plc (*banking*) and The Seagram Company Ltd (*drinks*) and a former member of the Accounting Standards Board (UK).

Chairman of the remuneration committee and member of the audit committee.

Carole Piwnica (49)

Independent non-executive director

Appointed to the board in May 2003. A member of the New York and Paris bars, practising law in Europe and the US specialising in private equity and EU regulatory matters. Currently a non-executive director of Toepfer International GmbH (*trading*) and a member of the biotech advisory board of Monsanto. A former non-executive vice-chairman – governmental affairs for Tate & Lyle plc (*agricultural/industrial*), a former non-executive director of S A Spadel N.V. (*food and beverages*) and former chairman of Amylum Group (*agricultural/industrial*).

Member of the audit, remuneration and corporate social responsibility committees.

Russell Walls (63)

Independent non-executive director

Appointed to the board in May 2004. Currently a non-executive director of Signet Group plc (*retail*) and chairman of its audit committee. A former group finance director of BAA plc (*transport*), Wellcome plc (*pharmaceuticals*) and Coats Viyella plc (*textiles*). Former senior independent non-executive director of Stagecoach Group plc (*transport*) and of Hilton Group plc (*leisure*) and a former non-executive director of the Mersey Docks and Harbour Company plc (*transport*).

Chairman of the audit committee and a member of the risk and regulatory and nomination committees.

Richard Whitaker LLB, DMS, FCI

Group company secretary

Guillermo de la Dehesa

Wim Dik

Mary Francis

Richard Karl Goeltz

Carole Piwnica

Russell Walls



Directors' report

The directors submit their report and accounts for Aviva plc, together with the consolidated accounts of the Aviva Group of companies, for the year ended 31 December 2006. Pursuant to amendments made to the Companies Act 1985 in 2005 companies are required to produce a business review as part of their directors' report in respect of financial years beginning on or after 1 April 2005. The business review is contained on pages 12 to 69. Certain matters that are required to be disclosed within the directors' report have been included within the Business Review and accordingly, the review of the Group's operations, current position and future prospects together with a description of the principal activities of the Group can be found within the business review. Details of material acquisitions and disposals made by the Group during the year are contained in note 3 to the accounts.

Results

The Group results for the year are shown in the Consolidated income statement on page 114.

Dividends

The directors are recommending a final dividend of 19.18 pence per share (2005: 17.44 pence), which together with the interim dividend of 10.82 pence paid on 17 November 2006 (2005: 9.83 pence), produces a total dividend for the year of 30.00 pence per share (2005: 27.27 pence). The total cost of ordinary dividends for 2006, will amount to £693 million (2005: £598 million), leaving £1,468 million to be transferred to reserves (2005: £1,123 million to reserves). The final dividend for 2006 will be paid on 17 May 2007 to all holders of ordinary shares on the Register of Members at the close of business on 9 March 2007. The Company's Scrip Dividend Scheme will be available to shareholders in respect of the payment of the final dividend. In addition, a local currency payment service will be available to shareholders residing in certain participating countries outside the UK. Further details of these arrangements can be found in the shareholder services section on pages 246 to 248.

Share capital

At the Company's Annual General Meeting, held on 10 May 2006, shareholders approved an increase in the Company's authorised share capital from £1.45 billion and €700 million to £1.95 billion and €700 million by the creation of 500 million preference shares of £1 each.

The issued ordinary share capital of the Company was increased by 170 million ordinary shares during the year. 129 million new shares were allotted on 18 July 2006 in part consideration for the acquisition of AmerUs Group Co which completed on 15 November 2006. The balance of 41 million shares was allotted under the Group's employee share and incentive plans and the Aviva Scrip Dividend Scheme. At 31 December 2006 the issued ordinary share capital totalled 2,565.8 million shares. Details of the Company's share capital and shares under option at 31 December 2006 and shares issued during the year are given in notes 27 to 30 of the accounts.

Authority to purchase own shares

At the Company's Annual General Meeting held on 10 May 2006, shareholders renewed the Company's authority to make market purchases of up to 239 million ordinary shares, up to 100 million 8¾% preference shares and up to 100 million 8⅝% preference shares. This authority was not used during the year and, at the forthcoming Annual General Meeting, shareholders will be asked to renew these authorities for another year. Details are contained in the Notice of Meeting. The Company held no Treasury shares during the year.

Post balance sheet events

There have been no material events between 31 December 2006 and the date of this report that are required to be brought to the attention of shareholders.

Directors

The following persons served as directors of the Company during the year:

Guillermo de la Dehesa
Wim Dik
Mary Francis
Richard Karl Goeltz
Richard Harvey
Andrew Moss
Carole Piwnica
Philip Scott
Lord Sharman of Redlynch
Derek Stevens (retired 31 December 2006)
Patrick Snowball
André Villeneuve (retired 31 December 2006)
Russell Walls

The biographical details of the persons currently serving as directors appear on pages 72 to 73.

The Company's Articles of Association require one-third of the directors to retire by rotation each year. At the forthcoming Annual General Meeting Guillermo de la Dehesa, Wim Dik, Richard Karl Goeltz, and Russell Walls, all independent non-executive directors will retire and, being eligible, will offer themselves for re-election. Derek Stevens and André Villeneuve who were re-elected by shareholders at last year's Annual General Meeting had served on the Board for more than nine years and therefore retired on 31 December 2006 in line with the Board's plans to renew and refresh its composition. None of the directors retiring at the Annual General Meeting has a service contract with the Company.

Directors' interests and indemnity arrangements

At no time during the year did any director hold a material interest in any contract of significance with the Company or any of its subsidiary undertakings other than a third-party indemnity provision between each director and the Company and service contracts between each executive director and a Group company.

The Company has purchased and maintained throughout the year directors' and officers' liability insurance in respect of itself and its directors. The directors also have the benefit of the indemnity provision contained in the Company's Articles of Association.

The Company has executed deeds of indemnity for the benefit of each director of the Company, and each person who was a director of the Company during the year, in respect of liabilities that may attach to them in their capacity as directors of the Company or of associated companies. These provisions, which are qualifying third-party indemnity provisions as defined by Section 309B of the Companies Act 1985, were in force throughout the year and are currently in force. Details of directors' remuneration, service contracts and interests in the shares of the Company are set out in the Directors' remuneration report.

Substantial shareholdings

Until 19 January 2007 the Company maintained a register of substantial shareholdings in accordance with the provisions of Section 211 of the Companies Act 1985. At 19 January 2007, the register showed that the holdings exceeding the 3% disclosure threshold were those of Barclays Plc which held 102,377,279 ordinary shares (3.99%) of the issued ordinary share capital of the Company, Legal & General Group Plc which held 93,312,175 ordinary shares (3.65%) and AXA S.A. and its Group companies which held a total of 262,220,441 ordinary shares (10.22%) of which 29,277,260 (1.14%) were held beneficially and 232,943,181 (9.08%) were held non-beneficially.

On 20 January 2007 the Companies Act 1985 provisions in respect of substantial shareholdings were repealed and the Disclosure and Transparency Rules of the Financial Services Authority came into force. At 28 February 2007, the Company had received notifications that the holdings exceeding the 3% notification threshold were those of Barclays Plc which held 153,862,359 voting rights (representing 5.99% of the total voting rights attaching to the issued ordinary share capital of the Company), Legal & General Group Plc which held 93,312,175 voting rights (3.65%) and Axa S.A. and its Group companies which held a total of 262,220,441 voting rights (10.22%) of which 29,277,260 (1.14%) were held beneficially and 232,943,181 (9.08%) were held non-beneficially.

Financial instruments

Aviva Group companies use financial instruments to manage certain types of risks including those relating to credit, foreign currency exchange, cash flow, liquidity, interest rates, and equity and property prices. Details of the objectives and management of these instruments are contained in the Business Review and an indication of the exposure of the Group companies to such risks is contained in note 51 to the accounts.

Health and safety

The health and safety of the Group's employees is a priority and is reviewed at regular intervals. Each business within the Group has an appointed health and safety representative, whose role is to bring to the attention of senior management any areas of concern that should be addressed within the health and safety programme. Information on health and safety matters is communicated to staff through the normal communication channels. Under the Group's Health and Safety Policy the Group Chief Executive is accountable for health and safety.

Charitable donations

Aviva has continued to support community initiatives and charitable causes worldwide and the total Group commitment during the year, as measured in accordance with Business in The Community's PerCent Standard, was £6.3 million (2005: £5.7 million).

In 2006, the Group's community investment in the United Kingdom totalled £3.7 million (2005: £3.9 million) of which £1.4 million (2005: £1.7 million) was given in the form of donations to charitable organisations. The Company allocates a part of its budget to matching contributions raised by staff and to providing financial support to charities and communities where members of staff give a personal commitment in terms of their time. In addition, the Company provides a significant level of support to a number of national charities. During 2006, the Company continued its commitment to Breakthrough Breast Cancer, Wheelpower (the British wheelchair sports association), The Princess Royal Trust for Carers, NCH (the children's charity) and Muscular Dystrophy, which was chosen by employees in the United Kingdom as their "charity of the year". In support of its "Forward Thinking" initiative the Company has become a founder partner of the Oxfam 365 Alliance which provides immediate humanitarian aid to disasters occurring throughout the world. The Company has committed to support the 365 Alliance for three years.

Political donations

It is the Company's policy not to make donations to political organisations or for political causes, and it does not intend to change this policy. Accordingly, during the year the Company has made no donations to EU political organisations or incurred any EU political expenditure as defined in the Political Parties, Elections and Referendums Act 2000 (PPER) (2005: nil). In 2004, shareholders passed a resolution authorising the Board to incur expenditure, up to an aggregate limit of £100,000 per annum, on activities that fall under the PPER. The PPER introduced a very broad definition of political expenditure, such that some of the activities undertaken throughout the Group's businesses could arguably fall within that definition. The Board sought shareholders' authority to incur such expenditure in order to avoid any inadvertent breaches of the PPER. The Board does not believe that the Group has incurred any such political expenditure in the past year. The Board's authority to incur such political expenditure expires in 2008.

Directors' report continued

The Group acquired the AmerUs group of companies on 15 November 2006 and, in line with accepted practice in the United States that group made political donations totalling \$2,250 in December 2006. In common with other sizeable companies in the US, AmerUs also operates a Political Action Committee (PAC). The PAC allows employees to make contributions to be used for political donations and, in December 2006 a donation of \$1,000 was made by the employee PAC. These are not political donations made by the Company. Following the integration of AmerUs into the Aviva Group, no future political donations will be made by the Company although AmerUs will continue to operate its employee PAC.

Group employees

The Group's statement on its employees is set out in the Business Review.

In summary, the Group's commitment to communication and dialogue with employees continues. A strong emphasis is placed on the provision of news through a variety of media, including intranets (both a Group-wide intranet, Arena, and local business unit intranets), Aviva radio, which can be accessed via mobile phone or computer, and poster campaigns. Employees have opportunities to voice their opinions and ask questions through intranet sites and climate surveys. Face-to-face briefings and team meetings are actively encouraged and are held in all business units across the Group. During 2006, the Group's businesses in the United Kingdom established employee consultative forums.

Employee practice

Aviva Group companies are committed to providing equal opportunities to all employees, irrespective of their sex, sexual orientation, marital status, creed, colour, race, nationality, ethnic origin, disability, age, religion or union membership status. Aviva is an inclusive employer and values diversity in its employees. These commitments extend to recruitment and selection, training, career development, flexible working arrangements and promotion and performance appraisal. In the event of employees becoming disabled, every effort is made to ensure that their employment with the Group continues and to provide specialised training where this is appropriate.

Creditor payment policy and practice

It is the Group's policy to pay creditors when they fall due for payment. Terms of payment are agreed with suppliers when negotiating each transaction and the policy is to abide by those terms, provided that the suppliers also comply with all relevant terms and conditions. The Company has no trade creditors. In respect of Group activities in the UK, the amounts due to trade creditors at 31 December 2006 represented approximately 13 days of average daily purchases through the year (2005: 8 days).

Auditor and the disclosure of information to the auditor

Each person who was a director of the Company on the date that this report was approved, confirms that so far as the director is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Each director has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of Section 234ZA of the Companies Act 1985.

In accordance with Section 385 of the Companies Act 1985, a resolution is to be proposed at the Annual General Meeting for the reappointment of Ernst & Young LLP as auditor of the Company. A resolution will also be proposed authorising the directors to determine the auditor's remuneration. The Audit Committee reviews the appointment of the auditor, the auditor's effectiveness and relationship with the Group, including the level of audit and non-audit fees paid. Further details on the work of the auditor and the Audit Committee are set out below in the Audit Committee report.

Annual General Meeting

The Annual General Meeting of the Company will be held on 26 April 2007 at The Barbican Centre, Silk Street, London EC2Y 8DS at 11am. A separate document accompanying the Annual Report and Accounts contains the notice convening the Meeting and a description of the business to be conducted thereat.

By order of the Board.

Richard Whitaker

Group Company Secretary
28 February 2007

Registered Office: St. Helen's
1 Undershaft, London EC3P 3DQ
Registered in England No. 2468686

Corporate governance report

The Combined Code on Corporate Governance

The Combined Code on Corporate Governance sets out guidance in the form of principles and provisions on how companies should be directed and controlled to follow good governance practice. The Financial Services Authority requires companies listed in the UK to disclose, in relation to Section 1 of the Combined Code, how they have applied its principles and whether they have complied with its provisions throughout the accounting year. Where the provisions have not been complied with companies must provide an explanation.

The Combined Code was reviewed by the Financial Reporting Council during 2006 with a revised Code becoming effective in respect of financial years commencing on or after 1 November 2006 and accordingly the changes do not apply to the year under review.

It is the Board's view that the Company has been fully compliant throughout the accounting period with the provisions set down in Section 1 of the Combined Code (including the changes that became effective for financial years commencing on or after 1 November 2006). This report sets out details of how the Company has applied the principles and complied with the provisions of the Combined Code during 2006. Further information on the Code can be found on the Financial Reporting Council's website, www.frc.org.uk.

The Board

The directors are responsible to shareholders for ensuring that the Company is appropriately managed and that it achieves its objectives. It meets regularly to determine the strategic direction, to review the Company's operating and financial performance and to oversee that the Company is adequately resourced and effectively controlled. The specific duties of the Board are clearly set out in its terms of reference that address a wide range of corporate governance issues and list those items that are specifically reserved for decision by the Board. Matters requiring Board approval include:

- Group strategy and business plans;
- Acquisitions, disposals and other transactions outside delegated limits;
- Financial reporting and controls;
- Capital structure;
- Dividend policy;
- Shareholder documentation;
- The constitution of Board committees;
- Key business policies, including the remuneration policy.

Matters that are not specifically reserved to the Board and its committees under its terms of reference, or to shareholders in General Meeting, are delegated to the Group Chief Executive. The Board's terms of reference also set out those matters that must be reported to the Board, such as significant litigation or material regulatory breaches, and cover how matters requiring consideration by the Board that arise between scheduled meetings should be dealt with.

The Board and its committees operate in line with work plans agreed prior to the start of each year. At Board and committee meetings, directors receive regular reports on the Group's financial position, risk management, regulatory compliance, key business operations and other material issues. Directors are fully briefed in advance of Board and committee meetings on all matters to be discussed. The Group Company Secretary is responsible for following Board procedures and advising the Board, through the Chairman, on governance matters. All directors have access to his advice and services.

The Board has adopted a procedure whereby directors may, in the performance of their duties, seek independent professional advice at the Company's expense if considered appropriate. No director obtained any such independent professional advice during 2006.

The directors

The Board currently comprises the Chairman, six independent non-executive directors and four executive directors. Each non-executive director serves for a fixed term not exceeding three years that may be renewed by mutual agreement. Subject to the Board being satisfied with a director's performance, independence and commitment, there is no specified limit regarding the number of terms a director may serve. All directors are required to be elected by shareholders at the Annual General Meeting following his/her appointment by the Board and be re-elected at least once every three years. Any non-executive director who has served on the Board for nine years or more is required to submit himself/herself for re-election annually. The Board's policy is to appoint and retain non-executive directors who can apply their wider knowledge and experiences to their understanding of the Aviva Group, and to review and refresh regularly the skills and experience it requires through a programme of rotational retirement. In addition to the strengths of experience, diversity and an international perspective, the Board also seeks to comply with the requirements of the Combined Code on the independence of directors. The process for appointing new directors is conducted by the Nomination Committee whose report, including a description of its duties, is set out below.

The Combined Code requires that at least half the Board, excluding the Chairman, should comprise independent non-executive directors as determined by the Board. The Nomination Committee performs an annual review of directors' interests in which all potential or perceived conflicts, including time commitments, length of service and other issues relevant to their independence, are considered. It is the Board's view that an independent non-executive director also needs to be able to present an objective, rigorous and constructive challenge to management, drawing on his/her wider experiences to question assumptions and viewpoints and where necessary defend their beliefs. To be effective, an independent director needs to acquire a sound understanding of the industry and the Company so as to be able to evaluate properly the information provided. Having considered the matter carefully the Board is of the opinion that all of the current non-executive directors are independent and free from any relationship or circumstances that could affect, or appear to affect their independent judgement. Accordingly, over half of the directors, excluding the Chairman, are independent non-executive directors. Each of the directors being proposed for re-election at the 2007 Annual General Meeting has been subject to a formal performance evaluation and took part in a peer evaluation review during 2006. Biographical details of all the directors, including those proposed for re-election, are set out on pages 72 and 73.

Corporate governance report continued

The Chairman

The respective roles of the Chairman and Group Chief Executive are set out in the Board's terms of reference. The Chairman's priority is the management of the Board and the Group Chief Executive's priority is the management of the Company. The Chairman's contractual commitment to the Company is two to three days per week and his main interests outside the Company are set out in his biographical details on page 72. There have been no material changes to these commitments during the year.

Senior independent director

The main responsibility of the senior independent director is to be available to shareholders should they have concerns that they have been unable to resolve through normal channels, or when such channels would be inappropriate. The senior independent director is also responsible for leading the Board's discussion on the Chairman's performance and the appointment of a new chairman, when appropriate. Wim Dik served as the senior independent director throughout 2006.

Board effectiveness

The effectiveness of the Board is vital to the success of the Group. The Company undertakes a rigorous evaluation each year in order to assess how well the Board, its committees, the directors and the Chairman are performing. The process is led by the Chairman and supported by the Group Company Secretary. All directors complete a questionnaire regarding the Board and committees' processes, their effectiveness and where improvements may be considered. The process also includes a peer review in which directors assess their fellow directors' performance against set criteria, including the skills that they bring to the Company and the contribution they make. This process is complemented by separate meetings between each director and the Chairman where feedback is discussed. In 2006 a new format was introduced whereby directors completed a much more comprehensive questionnaire which was returned to an independent third-party who had helped with the preparation of the questions, and who collated comments, drew the conclusions and presented the findings to the Board.

The performance of the Chairman is also included in the above process and therefore takes into account the views of both the executive, and non-executive, directors. The Chairman's evaluation is managed by the senior independent director who provides feedback to the Chairman. As part of the Chairman's evaluation the non-executive directors meet separately under the chairmanship of the senior independent director.

Following this comprehensive review, the directors have concluded that the Board and its committees operate effectively. Additionally, the Chairman has concluded that each director contributes effectively and demonstrates full commitment to his/her duties.

The Board evaluation process assesses the executive directors in their capacities as directors of the Company. They are evaluated in respect of their executive duties through a separate process whereby the Chairman and the non-executive directors assess the Group Chief Executive and the Group Chief Executive assesses the executive directors.

Training and development

The Board believes strongly in the development of all its employees and directors and it is a requirement of each director's appointment that they commit to continue their development. The form that this development takes is subject to individual director's requirements and the quality and relevance of the training available. During the year, directors attended a number of external courses on issues ranging from seminars for members of the Audit and Remuneration Committees to workshops on financial risks and individual capital assessments. In addition, members of the Risk and Regulatory Committee received two tailored training/induction sessions. Training sessions have been built into the Board's and committees' work plans for 2007. The Board made visits to the Group's businesses located in York and India during the year to gain a closer understanding of their operations.

The Board has a comprehensive induction programme consisting of 13 separate sessions which take place over a number of months at times convenient for the director. The sessions include presentations from key members of senior management, visits to the Group's main operating businesses, meetings with the external auditor, and one of the Company's corporate brokers. Further or follow-up meetings are arranged where a director requires a deeper understanding on a particular item.

Directors' attendance

The Company requires directors to attend all meetings of the Board and the committees on which they serve and to devote sufficient time to the Company in order to perform their duties. The attendance of the directors at the Board and committee meetings held in 2006 was as follows:

Board and Board committee attendance 2006

	Board	Audit Committee	Nomination Committee	Risk and Regulatory Committee	Corporate Social Responsibility Committee	Remuneration Committee
Number of meetings held	10	4	5	3	3	5
Number of meetings attended						
Guillermo de la Dehesa	9/10	–	5/5	–	2/3	–
Wim Dik	10/10	–	5/5	3/3	3/3	–
Mary Francis	10/10	–	–	3/3	–	5/5
Richard Goeltz	10/10	4/4	–	–	–	5/5
Richard Harvey	10/10	–	5/5	–	3/3	–
Andrew Moss	10/10	–	–	–	–	–
Carole Piwnica	10/10	4/4	–	–	3/3	5/5
Philip Scott	10/10	–	–	–	–	–
Lord Sharman	10/10	–	5/5	–	3/3	–
Patrick Snowball	10/10	–	–	–	–	–
Russell Walls	10/10	4/4	–	3/3	–	–
Former Directors						
Derek Stevens*	10/10	4/4	–	–	3/3	–
André Villeneuve*	10/10	–	5/5	–	–	5/5

– Indicates not a member of that committee.

* Retired 31 December 2006.

During 2006 the Chairman and the non-executive directors met on one occasion in the absence of the executive directors and there was one meeting of the non-executive directors chaired by the senior independent director at which the Chairman was not present.

Board committees

The Board has established the following standing committees to oversee and debate important issues of policy and oversight outside the main Board meetings.

- Audit Committee
- Nomination Committee
- Risk and Regulatory Committee
- Corporate Social Responsibility Committee
- Remuneration Committee.

Throughout the year the chairman of each committee provides the Board with a summary of the key issues considered at the meetings of the committees and the minutes of the committee meetings are circulated to the Board. The committees operate within defined terms of reference, copies of which are published on the Company's website www.aviva.com and are available from the Group Company Secretary upon request. Board committees are authorised to engage the services of external advisers as they deem necessary in the furtherance of their duties at the Company's expense.

Reports of the committee chairmen are set out below.

Internal controls

The Combined Code requires directors to review and report annually to shareholders on the effectiveness of the Company's systems of internal control which include financial, operational and compliance controls, and risk management. The Board has the overall responsibility for maintaining the systems of internal control of the Company and for monitoring their effectiveness; while the implementation of internal control systems is the responsibility of management. The Group's systems of internal control are designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material financial misstatement or loss.

The systems are designed to:

- Safeguard assets;
- Maintain proper accounting records;
- Provide reliable financial information;
- Identify and manage business risks;
- Maintain compliance with appropriate legislation and regulation;
- Identify and adopt best practice.

The principal features of the control framework and the methods by which the Board satisfies itself that it is operating effectively are detailed below.

Corporate governance report continued

Control environment

The Group has an established governance framework, the key features of which include:

- Terms of reference for the Board and each of its committees;
- A clear organisational structure, with documented delegation of authority from the Board to executive management;
- A Group policy framework, which sets out risk management and control standards for the Group's operations worldwide;
- Defined procedures for the approval of major transactions and capital allocation;
- Committees of senior executives responsible for reviewing the Group's financial risks (Asset and Liability Management Committee) and non-financial ie operational risks (Group Operational Risk Committee).

The Group's risk and governance framework has been structured in accordance with the Financial Services Authority's risk-based framework for integrating and embedding risk and capital management (Prudential Sourcebook).

Risk identification, assessment and management

There is in place an ongoing process for identifying, evaluating and managing the significant risks faced by the Group which has operated throughout 2006 and up to the date of signing this report. The Group's risk management and control framework is designed to support the identification, assessment, monitoring, management and control of risks that are significant to the achievement of the Group's business objectives. The Group has a set of formal policies which govern the management and control of both financial and non-financial risks. The adoption of these policies throughout the Group enables a broadly consistent approach to the management of risk at business unit level. At Group level, policy owners are responsible for the Group-wide aggregation and oversight of their specific risks.

The Asset and Liability Management Committee is responsible for reviewing and monitoring the financial risks to the Group and, with the assistance of its sub-committees, considers the risks relating to life assurance, general insurance, reserving, capital management, credit and investment. Similarly, a Group Operational Risk Committee monitors risks associated with information technology, business protection, human resource management, business standards and regulatory compliance.

Management monitors the completeness of the Group's risk profile on a regular basis through a Group risk monitoring framework. Each quarter, businesses report residual risk profiles and the adequacy of the mitigating action programmes, based on local materiality levels. These impact assessments are based on financial, reputational and operational criteria. This enables the Group risk function to assess the overall risk exposure and to develop a Group-wide risk profile that is refreshed quarterly. Material items in the Group risk report are reported to the committee of the Group's senior executives (Executive Committee), the Risk and Regulatory Committee and in respect of social, environmental and ethical risks, the Board's Corporate Social Responsibility Committee. The Executive Committee consider whether the residual risks are within the Group's risk appetite, and the adequacy of the mitigating actions.

The Boards, audit committees and management of the operational businesses also consider local risk reports in a similar way. Regular reports are supported by escalation procedures for new or

deteriorating risks that are classified at the highest impact levels. In addition, all business unit heads and Group functional heads provide a certificate every six months to confirm compliance with the Group's governance and risk management framework, and the terms of their delegated authority. They must also specify any risk or control issues not already reported through the regular risk management processes.

Control procedures and monitoring systems

The Group has a well-developed system of planning, incorporating Board approval of a rolling three-year Group plan. Performance against the plan is subsequently monitored and reported to the Board each time it meets. This report also includes updates on relevant measures of solvency and liquidity. Performance is reported through the half-yearly publication of the Company's results based on accounting policies that are applied consistently throughout the Group. Operational management reports quarterly to the Executive Committee on a wide range of key performance and other significant matters and the Board receives regular representations from the senior executives responsible for each principal business operation.

Whilst the Audit Committee has the overall responsibility of monitoring the Group's internal control process on behalf of the Board, it is assisted by the Risk and Regulatory Committee which oversees the regulatory compliance and non-financial control processes and reports to the Board regarding such. In addition, the Audit Committee performs an annual review of the effectiveness of the internal audit function and the framework for the Group's systems of internal control. Throughout 2006, the Audit Committee and the Risk and Regulatory Committee received quarterly reports from the Group Audit Director on issues arising, and updates on previously reported items. More detailed reports on the work of these committees during 2006 are set out below.

The Board has conducted a review of the effectiveness of the Group's systems of internal control. Where weaknesses are identified as part of the control review, mitigating actions are taken or plans are put in place. These are then monitored by the appropriate committee on behalf of the Board. The Board is not aware of any significant weaknesses that do not have mitigating actions in place.

Internal audit

The Group's internal audit function advises management on the effectiveness of its internal control systems, the adequacy of these systems to manage business risk and to safeguard the Group's assets and resources. Through the Group Audit Director, the internal audit function provides objective assurance on risk and control to both the Audit Committee and Risk and Regulatory Committee. The effectiveness of the Group's internal audit function is reviewed each year by the Audit Committee. During 2006, the effectiveness of the internal audit peer review process was independently evaluated by KPMG LLP (KPMG).

Communication with shareholders

The Company places considerable importance on communication with shareholders and engages with them on a wide range of issues.

The Group has an ongoing programme of dialogue and meetings between the executive directors and institutional investors, fund managers and analysts. At these meetings, a wide range of relevant issues including strategy, performance, management and governance are discussed within the constraints of the information already made public.

The Company's Investor Relations Department is dedicated to facilitating communication with institutional investors. The directors consider it important to understand the views of shareholders and, in particular, any issues which concern them. The Board receives reports on the matters that have been raised with management at the regular meetings held with the large investors. During the year the Chairman and the senior independent director held a meeting with the major institutional investors and the senior independent director attended investor meetings with management. In addition, the senior independent director is available to meet with major shareholders to discuss any areas of concern that cannot be resolved through normal channels of investor communication and arrangements can be made to meet with the senior independent director through the Group Company Secretary. Similarly, arrangements can be made for major shareholders to meet with newly appointed directors.

The Board consults with shareholders in connection with specific issues where it considers appropriate. For example, the chairman of the Remuneration Committee met with institutional shareholder bodies and a number of major shareholders in 2006 regarding the Company's proposed changes to the directors' pension arrangements and the introduction of a long-term savings arrangement, details of which are set out in the Directors' remuneration report below.

The Board is equally interested in the concerns of private shareholders and, on its behalf, the Group Company Secretary oversees communication with these investors. It is the practice of the Company to issue a postage paid reply form with its Annual General Meeting documentation to enable shareholders to put relevant questions to the directors. This is considered to be particularly helpful for those shareholders who are unable to attend the meeting. Written responses are provided through a brochure containing answers to the most frequently asked questions that is also placed on the Company's website. All material information reported to the regulatory news services is simultaneously published on the Company's website affording all shareholders full access to Company announcements.

The Company's Annual General Meeting provides a valuable opportunity for the Board to communicate with private investors. At the meeting, the Company complies with the Combined Code as it relates to voting, the separation of resolutions and the attendance of committee chairmen. Whenever possible, all directors attend the Annual General Meeting and shareholders are invited to ask questions during the meeting and have an opportunity to meet with the directors following the conclusion of the formal part of the meeting. In line with the revised Combined Code, details of proxy voting by shareholders, including votes withheld, are made available on request and are placed on the Company's website following the meeting.

The Company's annual report and accounts and annual review, together with the Company's interim reports, trading statements and other public announcements are designed to present a balanced and understandable view of the Group's activities and prospects. The Chairman's statement, Group Chief Executive's review, and Business review provide an assessment of the Group's affairs and they will be supported by a presentation to be made at the Annual General Meeting.

Institutional investor

Morley Fund Management Limited (Morley), the Group's asset management company, believes that good governance contributes to better performance and practices. Therefore, as a major investor, the Group monitors the governance of the companies in which it invests. To this end, Morley holds regular meetings with the senior management of companies where it will raise matters which may affect the future performance of those companies.

Morley maintains a detailed Corporate Governance and Voting Policy as part of its investment strategy, which underpins its approach to engaging and voting at company general meetings. The policy also extends to cover social, environmental and ethical issues. Its policy is applied pragmatically, after careful consideration of all relevant information. In addition, Morley makes detailed voting reports available to clients' and publishes summary statistics on its website.

Directors' responsibilities

The directors are required to prepare accounts for each accounting period that comply with the relevant provisions of the Companies Act 1985 and International Financial Reporting Standards (IFRS) as adopted by the European Union, and which present fairly the financial position, financial performance and cash flows of the Company and the Group at the end of the accounting period. A fair presentation of the financial statements in accordance with IFRS requires the directors to:

- select suitable accounting policies and verify they are applied consistently in preparing the accounts, on a going concern basis unless it is inappropriate to presume that the Company and the Group will continue in business;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company and the Group's financial position and financial performance; and
- state that the Company and the Group have complied with applicable IFRS, subject to any material departures disclosed and explained in the accounts.

The directors are responsible for maintaining proper accounting records which are intended to disclose with reasonable accuracy, at any time, the financial position of the Company and the Group. They are also ultimately responsible for the systems of internal control maintained by the Group for safeguarding the assets of the Company and the Group and for the prevention and detection of fraud and other irregularities. Further details of the systems of internal controls maintained by the Group are more fully described above.

Going concern

After making enquiries, the directors have a reasonable expectation that the Company and the Group as a whole have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Audit committee report

This report provides details of the role of the Audit Committee and the work it has undertaken during the year. The purpose of the Committee is to assist the Board in discharging its responsibilities for the integrity of the Company's financial statements, the assessment of the effectiveness of the systems of internal financial controls and monitoring the effectiveness and objectivity of the internal and external auditors. The full terms of reference for the Committee can be found on the Company's website www.aviva.com and are available from the Group Company Secretary.

The following independent non-executive directors, served on the Committee during the year:

Member	Period	
	From	To
Russell Walls (Chairman from 1 January 2007)	1 July 2004	To date
Richard Karl Goeltz	1 July 2004	To date
Carole Piwnica	24 September 2003	To date
Derek Stevens	8 August 1995	31 December 2006

Russell Walls succeeded Derek Stevens as the chairman of the Committee on 1 January 2007 and Mary Francis became a member from that date. The Committee met on four occasions in 2006 and each member attended every meeting. The Group Company Secretary acts as the secretary to the Committee.

Russell Walls, a Fellow Chartered Certified Accountant, is a former Group Finance Director of BAA plc, Wellcome plc and Coats Viyella plc. Richard Karl Goeltz is a former Chief Financial Officer of American Express Company, NatWest Group plc and The Seagram Company Ltd. The Board is satisfied that these directors have recent and relevant financial experience.

The Group Chief Executive, Group Finance Director, Group Audit Director and the external auditor normally attend, by invitation, all meetings of the Committee. Other members of senior management are also invited to attend as appropriate to present reports. It is the Committee's practice at each meeting to meet separately with the Group Audit Director and the external auditor without any members of management being present. In performing its duties, the Committee has access to the services of the Group Audit Director, the Group Company Secretary and external professional advice.

The Committee follows an agreed annual work plan. It reviews, with members of management and the internal and external auditors, the Company's financial announcements including the annual report and accounts to shareholders and associated documentation. It places particular emphasis on their fair presentation and the reasonableness of the judgemental factors and appropriateness of significant accounting policies used in their preparation. At each meeting, the Committee receives a report from the Group Audit Director concerning the Company's systems of internal financial control, including any significant new issues and actions taken on previously reported issues. Twice each year, the Committee receives reports on the adequacy of the Group's life assurance and general insurance reserves. The Committee also reviews the annual work plan for the Group's internal audit function. The Committee reports to the Board regarding the effectiveness of the Group's overall systems of internal control. The Committee itself reviews the financial controls and works closely with the Risk and Regulatory Committee which reviews the non-financial controls.

Prior to 2006, the Committee received regular reports on risk management, financial malpractice (including fraud, anti-money laundering and "whistleblowing"), regulatory and compliance matters. The responsibility for overseeing these matters as well as the oversight of the non-financial internal controls was transferred to the Risk and Regulatory Committee following its establishment in January 2006. A separate report from that committee is set out below.

In addition, the Committee reviewed the Group's capital and risk frameworks against the regulatory reforms incorporated in the Financial Services Authority's Prudential Sourcebook (PSB) concerning the Group's individual capital assessments (ICA). The Committee considered the proposed assumptions, methodology and process followed in determining the amount of capital required to support the Group's business plans and the adequacy of its capital resources.

Each of the Group's major business units has an audit committee that provides an oversight role for its business. All such committees include members who are independent of the relevant business. The Group Audit Director reviews the papers and minutes from these committees and brings all significant matters to the Committee's attention.

The Committee receives reports from the external auditor and regularly holds discussions with both the internal and external auditors in the absence of management. The chairman of the Committee reports to the subsequent meeting of the Board on the Committee's work and the Board receives a copy of the minutes of each meeting of the Committee.

Internal audit

The Group's internal audit function advises management on the effectiveness of the Company's internal control systems, the adequacy of these systems to manage business risk and to safeguard the Group's assets and resources. Through the Group Audit Director, the internal audit function provides objective assurance on risks and controls to the Committee. The plans and level of resources of the internal audit function are reviewed each year by the Committee, which also undertakes an annual review of the effectiveness of the Group's internal audit function against guidance criteria provided by the Institute of Chartered Accountants in England and Wales. As a result of the restructuring of the Group's internal audit function during 2006 and 2007, the proposed independent review of the function has been deferred. However, during 2006 the effectiveness of the internal audit peer review was independently evaluated by KPMG.

External auditor

Ernst & Young LLP (Ernst & Young) was appointed auditor of the Company in 2001 having previously been the auditor of Norwich Union plc. Following the 2005 external audit effectiveness review the Committee concluded that the audit was fit for purpose and recommended that a re-tender process should not be undertaken in 2006 but that the relationship and the effectiveness of the auditor be kept under review. The audit signing partner changed as part of a rotation process in 2002 and in line with that process there has been a further rotation in audit partner following the sign-off of the statements for the 2006 financial year. Ernst & Young audits the whole of the Group other than Delta Lloyd (the Group's subsidiary operating in the Netherlands, Belgium, Luxembourg and Germany), which is audited by PricewaterhouseCoopers LLP (PwC) and part of the RAC group which remains audited by KPMG. To fulfil its Group reporting responsibilities Ernst & Young reviews the work of PwC and KPMG in accordance with standard auditing practices.

The Company has policies aimed at safeguarding and supporting the independence and objectivity of the external auditors. The policies regulate the appointment of former audit employees to senior finance positions in the Group and set out the approach to be taken by the Group when using the services of the auditor. It distinguishes between those matters where an independent view is required, such as audit and assurance work, and other advisory services. In addition to statutory audits, audit and assurance work includes reviewing statutory returns, actuarial assurance, regulatory advice requiring auditor reporting, due diligence on acquisitions and disposals, fraud investigations and control reviews and audit reviews. As a general principle the auditor cannot be engaged by the Company for any other purpose, although the policy recognises that there may be areas of minor significance where, for pragmatic reasons, it may be in the Group's interests to use the external auditor for this work.

Annually, the Committee reviews a formal letter provided by the external auditor confirming its independence and objectivity within the context of applicable regulatory requirements and professional standards.

The Group paid £9.0 million to Ernst & Young LLP for audit services in 2006, relating to the statutory audit of the Group and Company financial statements and the audit of Group subsidiaries and associates pursuant to legislation (2005: £9.0 million). In addition, the Group engaged Ernst & Young LLP in relation to certain assurance work including verification of its Corporate Social Responsibility Report. The fees for other services which included advice on accounting and regulatory matters, reporting on internal controls, corporate governance matters, and due diligence work were £6.6 million giving a total fee to Ernst & Young LLP of £15.6 million (2005: £13.8 million). Further details are provided in note 11 to the accounts.

During the year, the Committee performed its annual review of the independence, effectiveness and objectivity of the external auditor; assessing the audit firm, the audit partner and audit teams. The process was conducted by means of a questionnaire, completed Group-wide by members of senior management and members of the Group's finance community. The questionnaire sought opinions on the importance of certain criteria and the performance of the auditor against those criteria. The questionnaires were collated by the Group Company Secretary. Based on this review, the Committee concluded that the audit service of Ernst & Young LLP was fit for purpose and provided a robust overall examination of the Group's business and the risks involved.

In line with the Combined Code requirement the Board undertook a review of the effectiveness of all its committees during the year, including the Audit Committee.

This report was reviewed and approved by the Board on 28 February 2007.

Russell Walls

Chairman, Audit Committee

Nomination committee report

This report provides details of the role of the Nomination Committee and the work it has undertaken during the year.

The main purpose of the Committee is to assist the Board by keeping the composition of the Board under review and conducting a rigorous and transparent process when making or renewing appointments of directors to the Board. It also advises the Board on issues of directors' conflicts of interest and independence. The full terms of reference for the Committee can be found on the Company's website www.aviva.com and are available from the Group Company Secretary.

The following directors served on the Committee during the year:

Member	From	Period
		To
Lord Sharman (Chairman)	25 January 2006	To date
Guillermo de la Dehesa	21 June 2000	To date
Wim Dik	26 April 2004	To date
Richard Harvey	21 June 2000	To date
André Villeneuve	24 September 2003	31 December 2006

The Committee met on five occasions in 2006 and the members' attendance record is set out in the Corporate governance report above. The Group Company Secretary acts as the secretary to the Committee. Russell Walls was appointed a member of the Committee on 23 January 2007.

The Committee keeps under review the skill requirements of the Board and the knowledge, experience, length of service and performance of the directors. It also reviews their external interests with a view to identifying any actual, perceived or potential conflicts of interests, including the time available to commit to their duties to the Company. The Committee also monitors the independence of each non-executive director and makes recommendations concerning such to the Board. The results of these reviews are important when the Board considers succession planning and the re-election and reappointment of directors. Members of the Committee take no part in any discussions concerning their own circumstances.

During the year the Committee reviewed its executive succession plans against an indication from Richard Harvey, the Group Chief Executive, that he may wish to retire in mid-2007, three years prior to his normal retirement date. As part of the succession process the Board, with the advice and assistance of MWM Consulting agreed a process and prepared an "ideal candidate" profile for the group chief executive role. A shortlist of external candidates considered able to match the profile was prepared against which the Company's internal candidates were benchmarked. Through this process the Committee was able to confirm that the internal candidates compared well against potential external candidates. The internal candidates were then interviewed and assessed externally and by a number of the Company's independent non-executive directors. As a result of this process the Committee was able, upon Richard Harvey confirming in January 2007 his intention to retire, to make a recommendation to the Board that Andrew Moss, the Group Finance Director be appointed to succeed Richard Harvey as the Group Chief Executive. As a consequence of the above the Committee also considered the position of the Group Finance Director and made a recommendation to the Board that Philip Scott, Executive Director, Aviva International, be appointed to succeed Andrew Moss in that position.

The above recommendations were approved by the Board and announced to the Market on 10 January 2007 and will become effective on 11 July 2007.

As part of the 2006 Board performance evaluation the Board reviewed its composition and skills against what it considers the future issues and challenges facing the Company will be. The outcome of this review will be taken forward by the Committee during 2007.

The Committee has also reviewed the processes for identifying and developing those senior managers throughout the Group who are considered to have the potential to succeed members of the Group's senior executive.

In line with the Combined Code requirement the Board undertook a review of the effectiveness of all its committees during the year, including the Nomination Committee.

This report was reviewed and approved by the Board on 28 February 2007.

Lord Sharman of Redlynch
Chairman, Nomination Committee

Risk and regulatory committee report

This report provides details of the role of the Risk and Regulatory Committee and the work it has undertaken during the year.

The Committee was established by the Board in January 2006 and held its first meeting in April 2006. The purpose of the Committee is to assist the Board in providing leadership, direction and oversight with regard to the Group's governance and regulatory policies and procedures, including those related to compliance, risk management, financial malpractice and internal non-financial controls. The Committee was established as the Governance and Regulatory Committee but changed its name in June 2006 to the Risk and Regulatory Committee to more closely describe its main accountabilities. The full terms of reference for the Committee can be found on the Company's website www.aviva.com and are available from the Group Company Secretary.

The following independent non-executive directors served on the Committee during the year:

Member	Period	
	From	To
Mary Francis (Chairman from 1 January 2007)	14 January 2006	To date
Russell Walls	14 January 2006	To date
Wim Dik	14 January 2006	To date

Russell Walls served as the chairman of the Committee from its inception until 31 December 2006 when he was succeeded as chairman by Mary Francis. There were no other changes in the membership of the Committee during the year. The Group Company Secretary acts as the secretary to the Committee. The Committee met on three occasions in 2006 and each member attended every meeting. In addition the Committee held separate meetings with members of senior management and Ernst & Young for the purpose of induction and training.

The Group Chief Executive, Group Finance Director, Group Audit Director and the external auditor normally attend, by invitation, all meetings of the Committee. Other members of senior management are also invited to attend as appropriate to present reports. It is the Committee's practice at each meeting to meet separately with the Group Audit Director and the external auditor without any members of management being present. In performing its duties, the Committee has access to the services of the Group Audit Director, the Group Regulatory and Tax Director, the Group Company Secretary, the Group Financial Management Director and external professional advice.

The responsibility for overseeing risk, regulatory and compliance issues, as well as the oversight of non-financial internal controls was transferred to the Committee from the Audit Committee in April 2006. The work of the Committee since its establishment has fallen into the following broad areas:

Risk management

The Committee has received regular reports on the Group's risk management processes, including the key risks facing the business and the measures being taken by management to contain them. It has also reviewed the processes and governance used by management to define the Group's risk appetite and has reviewed the internal non-financial controls used to monitor the effectiveness of the Group's risk management processes.

Regulation and compliance

The Committee has reviewed the Group's regulatory operating plan and has received regular reports on its relationships with its external regulators. In particular, the Committee monitors the actions being taken by management in relation to the Risk Mitigation Programme agreed with the Financial Services Authority. Reports on any material compliance issues are received by the Committee including any reputational issues which may arise. In addition, the Committee receives reports on legislative and regulatory developments which may impact the Group.

Business protection

Reports on financial malpractice are presented to the Committee including incidences of fraud, anti-money laundering procedures and arrangements whereby persons can report in confidence any concerns about matters of probity (whistleblowing). The Committee proposes to increase its focus into other areas of business protection as its work progresses.

The chairman of the Committee reports at the subsequent meeting of the Board on the Committee's work and the Board receives a copy of the minutes of each meeting of the Committee.

In line with the Combined Code requirement the Board undertook a review of the effectiveness of all its committees during the year, including the Risk and Regulatory Committee.

This report was reviewed and approved by the Board on 28 February 2007.

Mary Francis

Chairman, Risk and Regulatory Committee

Corporate social responsibility committee report

This report provides details of the role of the Corporate Social Responsibility Committee and the work it has undertaken during the year.

The Committee was established by the Board in January 2006 and held its first meeting in June 2006. The purpose of the Committee is to provide guidance and direction to the Group's corporate social responsibility (CSR) programme, review the risks and opportunities relating to the eight individual elements in the programme (namely; standards of business conduct, environment, human rights, health and safety, community, customers, suppliers and workforce) and to monitor progress. The full terms of reference for the Committee are available from the Group Company Secretary and can be found on the Company's website www.aviva.com.

The following directors served on the Committee during the year:

Member	From	Period
		To
Wim Dik (Chairman)	14 January 2006	To date
Guillermo de la Dehesa	14 January 2006	To date
Richard Harvey	14 January 2006	To date
Carole Piwnica	14 January 2006	To date
Lord Sharman	14 January 2006	To date
Derek Stevens	14 January 2006	31 December 2006

The Committee met on three occasions in 2006 and the members' attendance record is set out in the Corporate governance report. The Group Company Secretary acts as the secretary to the Committee.

During the year the Committee met to consider the conclusions of the Group's CSR Annual Conference that took place in June 2006, and which was addressed by both the Chairman of the Board and the Chairman of the Committee. The Committee reviewed the proposed content and scope of the Company's 2007 CSR Report, monitored the management of the CSR risks affecting the Group and helped establish a process by which CSR related targets and objectives within the Group's individual businesses are set and monitored.

The Committee considered a report from the Norwich Union business that explained how it was handling the social issues arising from a major cost and efficiency review in that business announced in September 2006, which would result in a significant reduction in its UK workforce.

During the Board's visit to the Group's Indian operations in September 2006, the Committee held a meeting with the senior managers responsible for CSR in the Group's life assurance business (Aviva India) and its offshoring operations (Aviva Global Services) in order to gain a deeper understanding of the relevant local issues and assess how CSR was being embedded in those businesses.

In line with the Combined Code requirement the Board undertook a review of the effectiveness of all its committees during the year, including the Corporate Social Responsibility Committee.

This report was reviewed and approved by the Board on 28 February 2007.

Wim Dik

Chairman, Corporate Social Responsibility Committee

Directors' remuneration report

This report sets out the remuneration policy for the Company's directors and senior executives in line with statutory requirements and good practice guidelines and describes the elements of their remuneration and discloses the amounts paid to the directors in 2006.

The Remuneration Committee

The key purposes of the Committee are to ensure that the remuneration of senior executives is aligned to the Company's strategy and that the Company is able to attract, retain and motivate high calibre people within a very competitive international market for talent.

The Committee reviews and recommends to the Board the Company's remuneration policy and strategy and, within the policy, makes decisions on individual remuneration terms and compensation packages for the executive directors with particular reference to the Company's performance. The Committee also sets the remuneration structure and terms for the Company's other senior executives; sets the Chairman's fee and exercises the powers of the Board in relation to the executive long-term incentive and all-employee share plans. The full terms of reference for the Committee are available from the Group Company Secretary and can be found on the Company's website www.aviva.com.

Remuneration Committee composition

The following independent non-executive directors served on the Committee during the year:

Member	From	Period
		To
Richard Karl Goeltz (Chairman)	3 May 2004	To date
Mary Francis	25 January 2006	To date
Carole Pivnicka	25 January 2006	To date
André Villeneuve	16 April 1996	31 December 2006

Richard Karl Goeltz succeeded George Paul as the chairman of the Committee in January 2006. The Committee met on five occasions in 2006 and each member attended every meeting. The Group Company Secretary acts as the secretary to the Committee.

The Group Chief Executive is normally invited to attend the meetings of the Committee, except when his own remuneration is being discussed, as is the Group Human Resources Director. The Chairman of the Board is invited to attend the Committee meetings when executive directors' pay is being discussed.

In line with the Combined Code requirements the Board undertook a review of the effectiveness of all its committees during the year, including the Remuneration Committee.

Advice to the Remuneration Committee

Hilary Oliver, the Group Reward Director, provided material assistance to the Committee during the year, advising on market trends, practices and appropriate levels of remuneration. Deloitte, which provided actuarial, tax and IT services to the Group during the year, advised the Committee on the calculation of total shareholder return for the purposes of the long-term incentive plans. In addition, Nic Nicandrou, in his previous role as Group Financial Control Director provided material assistance to the Committee in relation to its consideration of the financial objectives relevant to the Aviva Annual Bonus Plan and determining the extent to which the objectives had been met. Richard Whitaker, the Group Company Secretary and Linklaters LLP (Linklaters) advised the Committee in relation to the operation of the Company's share plans. Linklaters provided other legal services to the Group. In addition, the Committee considered the views of the Chairman and Group Chief Executive in assessing the performance of the executive directors.

A review of senior executive pension provisions as described in detail in this report was undertaken during 2005 and 2006. During the review Aon Consulting, which undertook other pensions related work for the Company, advised the Company and Lane Clark & Peacock LLP (LC&P), consulting actuary, was appointed by the Committee to provide an independent opinion on certain aspects of the recommendations arising from the review. LC&P provided no other services to the Group during the year.

Changes to remuneration policy

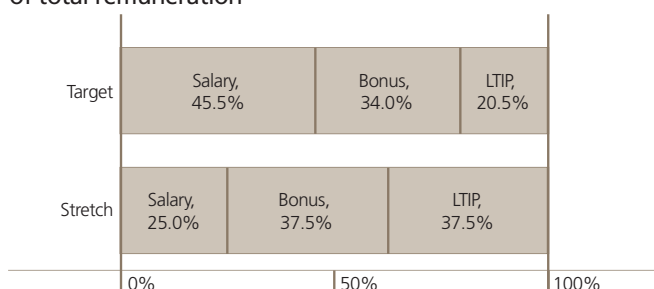
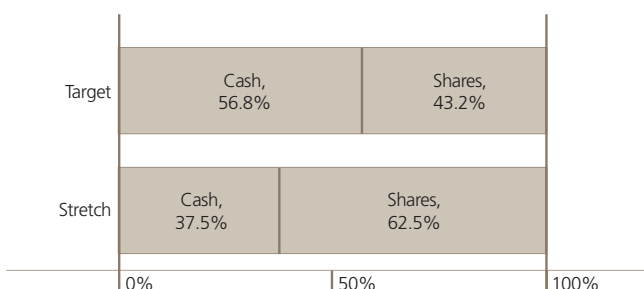
The remuneration policy is reviewed by the Committee on a regular basis to ensure that it is achieving its objectives and remains appropriate within the market. A major review was undertaken in 2004, which included salaries, annual bonus, share schemes and benefits. In respect of the Company's share incentive plans the review included all aspects of their operation including the discretions exercised, levels of grant, performance criteria and vesting schedules. The changes resulting from the review became effective in 2005. Pensions and long-term savings benefits were assessed in 2005 and 2006 with the changes becoming effective from 6 April 2006.

The only other modifications made during the year were to the rules of the share plans to ensure compliance with the age discrimination legislation which became effective in October 2006.

Directors' remuneration report continued

Remuneration package

The remuneration package for the Group's senior executives is described in the table below. It reflects the Board's philosophy that senior executives' interests should be aligned with those of the Company's shareholders, and that, while paying a competitive basic salary, a substantial proportion of the total remuneration package should be closely linked to the performance of the business and paid in shares.

Remuneration package overview: constituent elements at "target" and "stretch" (maximum)**Constituent elements of reward as a percentage of total remuneration****Proportion of remuneration paid in cash and shares**

The illustrations above would vary slightly for Richard Harvey, whose long-term incentive plan award is 175% of basic salary. The illustrations assume "on target" performance when 30% of an LTIP award vests and "stretch" performance when 100% of an LTIP award vests.

Policy	How delivered	Details
Total remuneration	<ul style="list-style-type: none"> – Basic salary – Annual bonus – LTIP – Pension – Long-term savings – Benefits – All-employee share schemes 	Positioned at median against a FTSE 30 comparator group, although account is taken of relative size and complexity of comparator organisations.
Basic salary Basic salary is benchmarked within the range of median to upper quartile for comparable jobs. Progression within this range is dependent upon performance.	<ul style="list-style-type: none"> – Monthly in cash – Reviewed annually 	Basic salary depends upon: <ul style="list-style-type: none"> – Benchmarked salaries for comparable roles in the FTSE 50 and UK/European financial institutions; – An individual's performance; – Predicted market movement; – Aviva's financial performance; and – Anticipated pay increases for other Aviva employees.
Annual bonus The discretionary annual bonus plan exists to motivate directors towards the achievement of the annual business plan. 75% of basic salary is payable for "on target" performance, and up to 150% is payable for "stretch" performance.	<ul style="list-style-type: none"> – Annually, one-third is paid in cash and two-thirds in deferred shares. – The shares vest on the third anniversary of the date of grant, subject to the recipient remaining in service. – A resignation in the year of a bonus award would result in the forfeiture of the shares awarded that year. A resignation in the following year would result in a 50% forfeiture, and in the year after that a 25% forfeiture. – All shares would be forfeited should the director be dismissed for cause. 	Business performance (of the Aviva Group in the case of the Group Chief Executive and the Group Finance Director and of the Group and appropriate business units in the case of the other executive directors) determines 70% of the bonus awards, with the remainder dependent upon the achievement of personal objectives, relating to strategic action, operating performance and leadership. "Business performance" covers, inter alia, new business contribution, operating profit, combined operating ratio, total expenses, return on capital employed, customer satisfaction and employee engagement. Target and maximum bonus levels (75% and 150% of basic salary respectively) were set with reference to the FTSE 30 and a global financial services comparator group. These levels are reviewed annually as part of the total compensation review.

Policy	How delivered	Details
Long-Term Incentive Plan This plan exists to motivate recipients to achieve the Company's longer term objectives, to aid the retention of key personnel and to align their interests to those of shareholders.	<ul style="list-style-type: none"> – Awards are made annually in the form of restricted shares that vest, subject to performance conditions, at the end of a three year performance period. – Awards that do not vest, lapse. – The Group Chief Executive is eligible to receive an annual award of shares to the value of 175% of his basic salary. The other executive directors are eligible to be awarded shares to the value of 150% of their basic salary. – Under the scheme rules no awards may exceed 200% of a participant's basic salary. – Awards made to other senior employees vary based on an individual's skills and longer term potential. Normally awards are made between 0% and 150% of basic salary. 	<p>Vesting of the shares is dependent upon two equally weighted performance measures; Return on Capital Employed (ROCE) and relative Total Shareholder Return (TSR), reflecting shareholders' long-term interests in both absolute (ROCE) and relative (TSR) performance.</p> <p>ROCE vesting – ROCE targets are set annually within the context of the Company's three-year business plan. Vesting depends upon the Company's performance over the three-year performance period against a target return. The Group's external auditor provides a formal opinion on the ROCE calculation.</p> <p>For awards granted for the three-year performance period commencing 1 January 2006, the Company's cumulative ROCE over the period must exceed 31.5% for 15% of the shares to vest, with the maximum 50% of shares vesting if the cumulative ROCE exceeds 37.5% over the period.</p> <p>TSR vesting – 15% of the award vests for median performance rising to 50% vesting for upper quintile performance.</p> <p>The group of companies against which the Company's TSR is measured comprises: AEGON, Allianz, AXA, Fortis, Friends Provident, Generali, HBOS, ING, Legal & General, Lloyds TSB, Prudential, The Royal Bank of Scotland, Royal & Sun Alliance and Zurich. These companies were chosen for their product and geographic match to Aviva. An independent consultant determines Aviva's performance within this group.</p> <p>In December 2006, the Committee reviewed the appropriateness of relative TSR as a performance measure and agreed to include Standard Life in the above comparator group in respect of future grants.</p>
All employee share plans To provide employees with the opportunity to acquire Aviva shares, where applicable.	<ul style="list-style-type: none"> – Eligible to participate in the Company's UK all employee share plans. 	See details below ("UK All Employee Share Plans").
Long-term savings Aviva has taken the opportunity presented by changes to pension legislation to introduce a new long-term saving arrangement, the Aviva Capital Accumulation Plan (ACAP). Contributions for the executive directors are shown in the Directors' remuneration table below.	<ul style="list-style-type: none"> – Discretionary payments into an employee benefit trust operated by independent trustees. Currently those executive directors who are participating are not accruing benefits in the Aviva Staff Pension Scheme. – The level of contribution varies but will not normally exceed 50% of basic salary. 	<ul style="list-style-type: none"> – Payments are held in trust for a minimum of five years. – A resignation or departure for breach of contract generally results in the forfeiture of contribution for the year in which resignation occurred.
Pension The Aviva Staff Pension Scheme (Pension Scheme) provides a competitive post retirement package.	<ul style="list-style-type: none"> – Deferred cash payable on retirement in the form of a lump sum/monthly payment. 	See details below ("Pension").

Directors' remuneration report continued

Pension

In anticipation of pension legislation ("pension simplification") that came into effect on 6 April 2006, the Committee undertook a review of the pension provisions for its senior executives and how they relate to the total remuneration package. The review was set against a number of design principles including:

- The Company's need to continue attracting and retaining top quality management;
- That future pension arrangements for senior executives should not cost the Company more than the arrangements previously in place;
- The Company would not pay or compensate managers for any increase in their personal tax liability arising from pension simplification; and
- The long-term cost exposure associated with the current final salary arrangements should be reduced.

The relevant features of the Pension Scheme defined benefit section, to which all the executive directors belonged prior to 1 April 2006, are:

- Accrual at either one thirtieth (Richard Harvey, Philip Scott and Patrick Snowball) or one forty-fifth (Andrew Moss) of final pensionable salary for each year of service (subject to a maximum pension of two-thirds of final pensionable salary);
- A contribution of 5% of pensionable salary is payable into the Pension Scheme by the employee;
- No pension benefits accrue on bonuses or other benefits;
- Lump sum death-in-service benefit of four times basic salary at the date of death;
- Spouse's pension equal to two-thirds of a member's actual or prospective pension;
- Post-retirement, annual review with increases guaranteed at a rate equivalent to the increase in the Retail Prices Index up to a maximum of 10% pa; and
- A normal retirement age of 60.

The benefits paid from the Pension Scheme to members who joined it after June 1989 were subject to Her Majesty's Revenue and Customs (HMRC) limits (Earnings Cap) which restricted the amount of pension which could be paid from an approved pension scheme. Where executives' benefits exceeded the Earnings Cap, the balance was provided through an Unapproved Unfunded Retirement Benefit (UURB). Richard Harvey and Andrew Moss were both affected by the Earnings Cap limit.

The effect of the pensions review on the executive directors was as follows:

Director	Impact of pensions simplification review
Richard Harvey	The value of Richard Harvey's UURB up to the newly introduced HMRC Lifetime Allowance (LTA) of £1.5 million was transferred into the Pension Scheme and therefore at retirement he will receive a deferred pension of £75,000 per annum as increased in line with deferred pensions (lower of the increase in RPI or 5%) subject to the LTA. The balance, valued at £11.6 million, was transferred into an Employer Funded Retirement Benefit Scheme (EFRBS).
Andrew Moss	The value of Andrew Moss' UURB was transferred into the Pension Scheme and therefore at retirement he will receive a deferred pension of currently c.£20,000 pa. Further accrual in the pension scheme ceased from April 2006.
Philip Scott	The value of Philip Scott's pension benefits on 6 April 2006 was in excess of the LTA. Philip Scott elected to register with HMRC for enhanced protection. As a consequence, he will remain a member of the Pension Scheme; however he will not be entitled to accrue any additional entitlement and on retirement his benefits will be based upon his final pensionable salary and years of service at that time. On this basis, it is anticipated that Philip Scott will not be subject to a recovery charge (additional tax). Philip Scott will continue to pay an annual contribution of 5% of his basic salary to the Pension Scheme. Should any recovery charge become payable, the cost would be borne by Philip Scott.
Patrick Snowball	The value of Patrick Snowball's pension benefits on 6 April 2006 was in excess of the LTA, and he elected to register with HMRC for primary protection. As a consequence, he will continue to accrue benefits in the Pension Scheme but may be subject to a recovery charge (additional tax) on his benefits in excess of the amount registered. Patrick Snowball will continue to pay an annual contribution of 5% of his basic salary to the Pension Scheme. The cost of any recovery charge will be borne by Patrick Snowball.

Other benefits

In addition to the benefits described above, senior executives are entitled to the benefit of a company car allowance and private medical insurance.

UK all employee share plans

Senior executives are eligible to participate in a number of HMRC approved all-employee share plans in the United Kingdom on the same basis as other eligible employees. These include the Free Share element of the Aviva All-Employee Share Ownership Plan (AESOP). Under this plan, eligible employees can receive up to a maximum of £3,000 per annum in the form of shares from the profits of the Company's UK business, free of tax, subject to a retention period. The partnership element of the AESOP allows participants to invest up to £125 per month out of their gross salary in the Company's shares.

The Aviva Savings Related Share Option Scheme allows eligible employees to acquire options over the Company's shares at a discount of up to 20% of their market value at the date of grant. In order to exercise these options, participants must have saved the consideration through a three, five or seven-year approved savings contract, subject to a maximum savings limit of £250 per month.

Executive directors' service contracts

Service contracts agreed with each executive director incorporate their terms and conditions of employment. Contracts were reviewed during the year and new contracts issued, bringing them into line with good market practice in respect of mitigation and phased payments. The main objective of the contracts is to strike a fair balance between the Company's and the employee's interests taking into account good market practice. The key terms are as follows:

Provision	Policy	
Notice period		
By the director	Six months	
By the Company	12 months, rolling. No notice or payment in lieu to be paid where the Company terminates for cause.	
Termination payment	Pay in lieu of notice up to a maximum of 52 weeks' basic salary. This may be increased by a discretionary redundancy payment (where appropriate) but any such further termination payment is capped at 52 weeks' basic salary. Any amount is subject to mitigation and phased payments.	
Remuneration and benefits	As described in this Report. The detailed operation of the annual bonus and LTIP plans is at the Company's discretion and in the case of the long-term savings plans at the trustees discretion.	
Expenses	Reimbursement reasonably incurred in accordance with their duties.	
Holiday entitlement	30 working days plus public holidays.	
Sickness	In line with senior management terms ie 100% basic salary for 52 weeks, and 75% thereafter.	
Non-complete	During employment and for six months after leaving.	
Contract dates	Director	Date current contract commenced
	Richard Harvey	6 December 2006
	Andrew Moss	16 January 2007
	Philip Scott	22 January 2007
	Patrick Snowball	15 November 2006

Policy on external Board appointments

The Company recognises that its senior executives can benefit by serving in a personal capacity as non-executive directors of non-Aviva Group companies. It therefore has a policy of allowing senior executives to serve as a non-executive director of an external company, subject to approval by the Board, and to retain any fee. However, during the year no executive director served in a personal capacity on the Board of a non-Aviva Group company.

Share ownership requirements

In line with investor guidelines, the Group Chief Executive and the executive directors are required to build, over a five-year period, a shareholding in the Company equivalent to 1.75 times annual salary and 1.5 times annual salary respectively.

Directors' remuneration report continued

Non-executive appointments

The non-executive directors, including the Chairman, have letters of appointment which set out their duties and responsibilities. The key terms of the appointments are as follows:

Provision	Policy		
Period	Three-year term which can be extended by mutual consent.		
Termination	By the director or the Company giving the other one month's written notice without compensation.		
Fees	As described below.		
Expenses	Reimbursement of travel and other expenses reasonably incurred in the performance of their duties.		
Time commitment	Between 25 and 50 days per annum depending upon Board and committee requirements and corporate activity.		
Non-compete	During employment and for six months after leaving.		
Appointment dates	Director	Date of last appointment	Date appointment terminates
	Guillermo de la Dehesa	30 May 2005	30 May 2008
	Wim Dik	7 December 2005	7 December 2008
	Mary Francis	1 October 2005	1 October 2008
	Richard Karl Goeltz	3 May 2004	3 May 2007
	Carole Piwnica	10 May 2006	AGM 2009
	Lord Sharman	14 January 2005	14 January 2008
	Russell Walls	3 May 2004	3 May 2007

Directors' service contracts and letters of appointment are available for inspection at the Company's registered office during normal hours of business. All the directors seeking re-election at the Company's 2007 Annual General Meeting are independent non-executive directors and therefore do not have a service contract with the Company.

It is the Company's policy to set the fees paid to its Chairman and non-executive directors at the median level for international companies of similar size and complexity. Non-executive directors receive a basic annual fee in respect of their Board duties. A further fee is paid to directors (other than the Chairman) in respect of their membership and, where appropriate, chairmanship of Board committees. Fees are reviewed regularly and are set by the Board to attract individuals with the range of skills and experience appropriate for a major international company. In determining the level of fees paid to the non-executive directors, the Board receives recommendations from the executive directors who consider the non-executive directors' duties and responsibilities, together with the time commitment required in preparing for and attending meetings, and the amounts paid by competitors and similar-sized companies. The Chairman and non-executive directors receive no benefits in addition to their fees nor do they participate in any incentive or performance plans or pension arrangements.

Non-executive directors' fees were reviewed in 2005 and will be reviewed again in 2007.

Directors' remuneration in 2006

This section of the report sets out the remuneration paid or payable to the directors in respect of the year to 31 December 2006. The following sections headed "Directors' Remuneration", "Executive Directors' Pension Arrangements" and "Share incentive plans" along with their associated footnotes have been subject to audit.

Basic salary decisions

The Committee's decisions on basic salary increases were made in February 2006 (and implemented from 1 April 2006) against a backdrop of strong financial performance by the Group as reported in the Company's 2005 Annual Report and Accounts.

In deciding basic salary increases, the Committee reviewed:

- FTSE 50 basic salaries for executive directors;
- Deloitte's and Towers Perrin's basic pay increase projections for 2006; and
- Individual performance in the role, relative to positioning within the FTSE 50 comparator group.

The 1 April 2006 pay review resulted in an increase of 10% to the aggregate basic salaries of the executive directors. This included increases for Richard Harvey and Andrew Moss that brought their basic salaries into line with FTSE 50 peers and reflected Mr Moss's increasing contribution to the Company. The basic salaries of the executive directors are positioned between the median and upper quartile ranking for companies with a market capitalisation over £16 billion. Given the executive directors' contribution and experience the Committee considers this to be an appropriate position. The basic salary increases for the Company's employees in the UK averaged 4% in 2006 and ranged from 0% to 15%.

Bonus decisions

In December 2005, the Remuneration Committee agreed business targets based upon the Group's annual business plan and each executive director's personal objectives. In August 2006 the financial assumptions used in the planning process were affirmed or amended by the Committee and in December 2006 it used its discretion to determine how corporate activity and changes in executive responsibilities during the year should be dealt with in deciding bonuses for 2006. In 2007, once the Group's results for 2006 were known, the Committee determined the executive directors' bonus payments. The Group's strong financial performance in 2006 resulted in the bonuses shown in the directors' remuneration table.

In 2006, customer and employee metrics were introduced to balance the financial objectives of the Annual Bonus Plan and to ensure that Aviva acted in the interests of all its stakeholders. As a result, 50% of the objectives were financial, 10% related to customer measures and 10% to employee morale and leadership. The final 30% of the bonus measures related to personal objectives. This split ensures that the environmental, social and governance responsibilities of Aviva are encouraged and that the performance measures address the broad range of Aviva's objectives. The committee reviews the Annual Bonus Plan targets annually and has discretion to make changes.

Directors' remuneration report continued

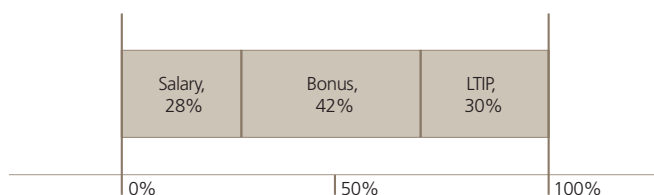
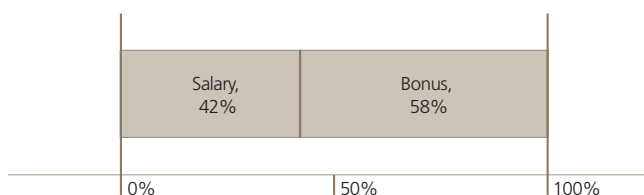
Directors' remuneration

	Basic salary/fees		Bonuses		ACAP		Benefits		Total	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000	2006 £'000	2005 £'000	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Chairman										
Lord Sharman	375	48	—	—	—	—	—	—	375	48
Executive directors										
Richard Harvey	875	790	1,296	1,028	450	—	61	104	2,682	1,922
Andrew Moss	533	470	744	589	275	—	36	20	1,588	1,079
Philip Scott	543	515	680	583	—	—	63	54	1,286	1,152
Patrick Snowball	543	503	763	693	—	—	39	104	1,345	1,300
Non-executive directors										
Guillermo de la Dehesa	86	77	—	—	—	—	—	—	86	77
Wim Dik	69	59	—	—	—	—	—	—	69	59
Mary Francis	64	13	—	—	—	—	—	—	64	13
Richard Karl Goeltz	78	63	—	—	—	—	—	—	78	63
Carole Piwnica	74	56	—	—	—	—	—	—	74	56
Russell Walls	64	56	—	—	—	—	—	—	64	56
Former directors										
Derek Stevens*	99	91	—	—	—	—	—	—	99	91
André Villeneuve*	65	59	—	—	—	—	—	—	65	59
Total emoluments of directors	3,468	2,800	3,483	2,893	725	—	199	282	7,875	5,975

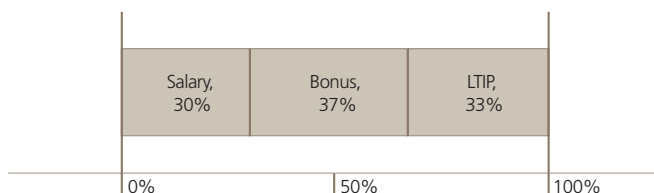
* Retired on 31 December 2006.

The charts below illustrate the balance between basic salary and variable performance based compensation (annual bonus and long-term incentive plans) received by each executive director in the year to 31 December 2006.

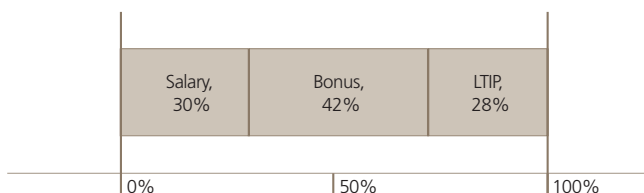
Richard Harvey

Andrew Moss⁶

Philip Scott



Patrick Snowball



Notes

- "Bonuses" include the value of shares granted under the free share part of the Aviva All-Employee Share Ownership Plan (maximum £3,000) and the total amounts earned in respect of 2006 performance under the Annual Bonus Plan (ie including the amounts deferred and granted in the form of shares).
- "Benefits". All the executive directors received life assurance benefits during the year that relate to the cost incurred by the Company of insuring the directors' life assurance and spouses' benefits which, had they died during the year, could not have been wholly paid by the pension scheme and would therefore have been met by the Company. The disclosure also includes the cost of private medical insurance, and when appropriate, accompanied travel, accommodation and car benefits. All the numbers disclosed include the tax charged on the benefits. No directors received an expense allowance during the year.
- Payments to former directors: Since his retirement as a director in 2003, Anthony Wyand has served as a consultant and as a director on the Boards of some of the Group's European operations. Under this arrangement, a fee of £145,000 was paid to him in 2006. During the year, shares granted to certain former executive directors under the company's incentive plans vested. Details of these awards were fully disclosed in the year of grant.
- For the purposes of the disclosure required by Schedule 6 to the Companies Act 1985 the total aggregate emoluments of the directors in respect of 2006 was £7.9 million. (2005: £6.0 million).
- No compensation payment for loss of office was made to any director, or former director, during the year.
- Andrew Moss did not benefit from the LTIPs that vested in 2006 as he was not an employee in 2003, when they were granted.

Pension benefits

During the year to 31 March 2006, each of the executive directors accumulated pension benefits under the defined benefits section of the Pension Scheme. Richard Harvey and Andrew Moss, who were subject to the pre-April 2006 Earnings Cap, ceased accruing further benefits in the scheme from that date.

Executive directors' pension arrangements

	Richard Harvey ¹ £'000	Andrew Moss ² £'000	Philip Scott ³ £'000	Patrick Snowball ³ £'000
Accrued annual pension at 1 January 2006	527	17	343	231
Transfer of UURB in excess of Lifetime Allowance	(458)	—	—	—
Increase in accrued annual pension during the year as a result of inflation	4	—	12	8
Augmentation of benefits	—	—	—	20
Adjustment to accrued annual pension as a result of salary increase relative to inflation	2	—	6	13
Increase in accrued annual pension as a result of additional service	—	3	—	17
Accrued annual pension at 31 December 2006 ⁴	75	20	361	289
Employee contributions during the year ⁵	10	6	27	27
Transfer value of accrued pension at 31 December 2005 ⁶	7,681	166	4,357	3,465
Transfer value of accrued pension at 31 December 2006 ⁶	1,252	231	5,236	4,833
Change in transfer value during the period less employee contributions ⁶	(6,433)	61	852	1,341
Age at 31 December 2006 (years)	56	48	52	56

Notes

1. Mr Harvey was subject to the HMRC Earnings Cap; hence a large part of the liability to pay his pension fell outside the Pension Scheme and was provided by the Company through an UURB. In line with material changes affecting pensions which became effective from 6 April 2006 the Company crystallised the value of its liability for Mr Harvey's UURB in excess of the LTA and transferred £11.6 million, being the actuarially calculated, and independently reviewed, value of the pension crystallised, into an EFRBS. As a result Mr Harvey's pension benefit, post March 2006 is £75,000 pa. and subject to increase in line with deferred pensions (the lower of the increase in the Retail Prices Index or 5%) subject to the LTA. In addition Mr Harvey is entitled to a pension benefit of cNZ\$25,000 pa from a New Zealand defined benefit scheme in respect of his service with the Group's former operations in that country. In calculating the actuarial value of the amount to be transferred to the EFRBS an appropriate reduction was made to reflect the benefit of his New Zealand pension.

The amount of the transfer of £11.6 million to the EFRBS was accounted for as follows:

- Amount provided on the Company's balance sheet for Richard Harvey as part of the IAS 19 charge at 31 March 2006, immediately prior to the change on 6 April 2006 is £10.8 million.
 - Less the amount of £700,000 transferred to the Pension Scheme to provide a pension up to the LTA.
 - The balance of £1.5 million was charged to the profit and loss account to take account of the increase in pension which would have been payable on his basic pay increase at 1 April 2006 (amount of pension increase £67,000 pa).
2. Mr Moss ceased accrual in the pension scheme after 31 March 2006 and as a result his pension benefit, post March 2006 is c£20,000 pa and subject to increase in line with deferred pensions (the lower of the increase in the Retail Prices Index or 5%) subject to the LTA.
3. Mr Snowball and Mr Scott have been accruing benefits in the Pension Scheme since before June 1989 and therefore were not subject to HMRC's Earnings Cap and can continue to accrue benefits in the Pension Scheme, which they did throughout 2006. For a number of years Mr Snowball had been accruing additional benefits which were due to accrue uniformly up to his normal retirement date in 2010. Mr Snowball's benefits were augmented to accrue in full in 2006, to reflect his increased duties following a restructuring of the UK businesses when no change was made to any other element of his remuneration. A payment of £429,000 was made into the pension scheme to fund this and therefore that part of the annual accrual ceased.
4. The "accrued pension" is the amount of annual pension to which the directors would have been entitled at age 60 had they left service at 31 December 2006.
5. Contributions of 5% of salary are made by Mr Scott and Mr Snowball towards their pension. As Mr Harvey and Mr Moss ceased accruing benefits in the Pension Scheme from March 2006 their 5% contributions ceased from that date and therefore the amounts disclosed are in relation to the period prior to that date.
6. The change in the transfer values over the year include the effect of changes made by the Trustee of the Pension Scheme to the assumptions used in respect of the market value of future investment returns and mortality. The significant reduction in relation to Mr Harvey reflects the reduction in his accrued pension benefit to £75,000 pa as described in note 1 above. Transfer values represent the estimated liability on the Scheme to pay the stated level of benefits. They are not sums paid, or due, to a director and do not represent the true cost of providing the pension benefit.
7. No former directors received any increase in retirement benefits in excess of the amount to which they were entitled on the later of the date when the benefits first became payable on 31 March 1997.

Directors' remuneration report continued

Share incentive plans

Details of the directors who held executive office for any part of the financial year, and hold or held options to subscribe for ordinary shares of the Company or hold or held awards over shares in the Company, pursuant to the Company's share-based incentive plans, are set out below.

Savings related share options

These are options granted under the HMRC approved Savings Related Share Option Scheme. Options are normally exercisable during the six month period following the end of the relevant (three, five or seven year) savings contract.

	At 1 January 2006 Number	Options granted during year Number	Options exercised during year Number	Options lapsing during year Number	At 31 December 2006 Number	Exercise price p	Exercise period
Richard Harvey							
Savings related options 2002	4,426	–	–	–	4,426	401.0	December 2009 – May 2010
Andrew Moss							
Savings related options 2005	3,279	–	–	–	3,279	491.0	December 2010 – May 2011
Philip Scott							
Savings related options 2002	4,096	–	–	–	4,096	401.0	December 2007 – May 2008
Patrick Snowball							
Savings related options 2003	2,272	–	2,272	–	–	406.0	–

The mid-market price of an ordinary share in the Company on 29 December 2006, being the last business day of the year, was 822 pence, and the mid-market prices during the year ranged from 690 pence to 850.5 pence. During the year, directors made an aggregate gain of £8,355 upon the exercise of share options.

Share awards

The Aviva Long-Term Incentive Plan 2005 was approved by shareholders at the 2005 Annual General Meeting and is described above. This "2005 Plan" replaced the original Aviva Long-Term Incentive Plan (Aviva LTIP) which was approved by shareholders in 2001 and under which awards were made on an annual basis up to and including 2004.

Performance testing under the Aviva LTIP

Under the Aviva LTIP, which granted awards between 2001 and 2004, shares vest subject to the attainment of TSR and ROCE performance conditions over a three-year performance period. The Company's TSR, when compared with the TSR of a comparator group of European financial services companies, needs to match at least median performance for 20% of the awards to vest. At upper decile performance, 70% of the awards vest. Between median and upper decile, vesting is determined on a straight-line basis. ROCE of 24% in excess of RPI over the three-year period results in 24% of the shares vesting, rising to a maximum of 30% if the ROCE exceeds 30% over the same period.

At the end of the performance period relating to the awards granted in 2003, the Company was ranked eight out of the 20 companies in the comparator group and the ROCE was 33.6%. As a result, 34.9% of the awards vested based on the TSR part of the Plan and 30.0% of the awards vested based on the ROCE part, making a total of 64.9% vested. The 35.1% of the awards, which did not vest, lapsed.

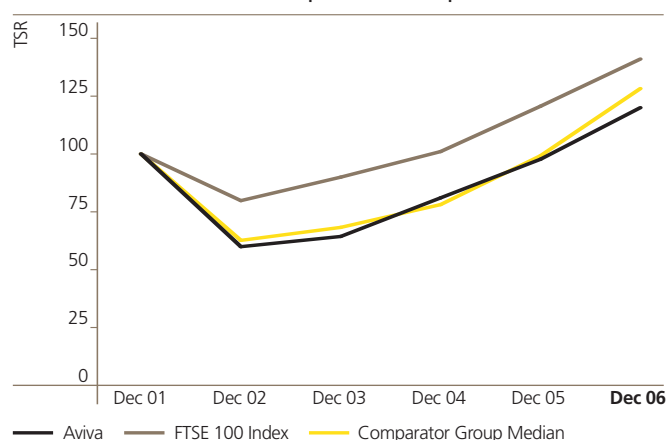
The vesting history under the Aviva LTIP is as follows:

Year of grant	Performance period	Percentage of award vesting		
		ROCE	TSR	Total
2001	January 2001 to December 2003	21.7	0.0	21.7
2002	January 2002 to December 2004	23.3	23.0	46.3
2003	January 2003 to December 2005	30.0	34.9	64.9

Performance graph

The following graph compares the TSR performance of the Company over the past five years with the TSR of the FTSE 100 Return Index. This index has been chosen because it is a recognised equity market index, of which Aviva is a member. The graph also includes the median TSR of the companies in the comparator group as this is the group against which performance is measured for the purpose of the Aviva Long-Term Incentive Plan. The companies which compose the comparator group for TSR purposes were amended when the new Long-Term Incentive Plan was introduced in 2005 so that the group matches more closely the companies which offer similar products in similar geographic markets to Aviva. The TSR graph for the comparator group has therefore been plotted using the 19 companies (excluding Aviva) in the comparator group pre-2005 and the 14 companies (excluding Aviva) in the group for 2005 and 2006.

Aviva five-year TSR performance against the FTSE100 Index and the median of the Comparator Group



The Aviva Annual Bonus Plan was approved by shareholders in April 2005 and it replaced the Aviva Deferred Bonus Plan.

The Aviva Deferred Bonus Plan was approved by shareholders at the 2001 Annual General Meeting. The awards disclosed include those made in lieu of some or all of the cash bonus earned and deferred under the Company's Annual Bonus Plan and also the matching awards granted on a "one-for-one" basis. The vesting of the awards on the third anniversary of their grant is not subject to performance conditions. This plan was replaced by the Aviva Annual Bonus Plan in 2005 and therefore no awards have been granted under the Plan since 2005.

The Aviva Share Plan was established in May 2004 specifically to facilitate the recruitment of Andrew Moss. The awards made under the Plan compensate Andrew Moss for the value of the long-term incentive awards granted to him by his previous employer and which lapsed when he resigned to join Aviva. Andrew Moss is the only participant in the Plan. On 10 May 2004, the date Andrew Moss joined the Company, 103,846 shares in the Aviva Employee Trust (with a market value of £540,000) were allocated to him. On 31 October 2004 67,307 of the shares vested, 23,077 vested on 31 December 2005 and the balance of 13,462 vested on 31 December 2006. The vesting of these shares was not subject to any performance conditions. This plan is now closed.

Directors' remuneration report continued

Long-Term Incentive Plan Awards

	At 1 January 2006 Number	Awards granted during year Number	Awards vesting during year Number	Awards lapsing during year Number	At 31 December 2006 Number	Market price at date awards granted p	Market price at date awards vested p	Vesting date
Richard Harvey								
Aviva Long-Term Incentive Plan								
– 2003	175,000	–	113,575	61,425	–	379.5	822.0	March 2006
– 2004	139,059	–	–	–	139,059	527.5	–	March 2007
Aviva Long-Term Incentive Plan 2005								
– 2005	207,437	–	–	–	207,437	633.5	–	March 2008
– 2006	–	170,731	–	–	170,731	814.0	–	March 2009
Aviva Deferred Bonus Plan								
– 2003	127,750	–	127,750	–	–	379.5	822.0	March 2006
– 2004	118,478	–	–	–	118,478	527.5	–	March 2007
– 2005	109,764	–	–	–	109,764	633.5	–	March 2008
Aviva Annual Bonus Plan								
– 2006	–	83,317	–	–	83,317	814.0	–	March 2009
Andrew Moss								
Aviva Share Plan	13,462	–	13,462	–	–	520.0	834.0	December 2006
Aviva Long-Term Incentive Plan								
– 2004	83,650	–	–	–	83,650	535.0	–	August 2007
Aviva Long-Term Incentive Plan 2005								
– 2005	102,803	–	–	–	102,803	633.5	–	March 2008
– 2006	–	87,804	–	–	87,804	814.0	–	March 2009
Aviva Deferred Bonus Plan								
– 2005	61,408	–	–	–	61,408	633.5	–	March 2008
Aviva Annual Bonus Plan								
– 2006	–	47,648	–	–	47,648	814.0	–	March 2009
Philip Scott								
Aviva Long-Term Incentive Plan								
– 2003	111,250	–	72,201	39,049	–	379.5	822.0	March 2006
– 2004	88,867	–	–	–	88,867	527.5	–	March 2007
Aviva Long-Term Incentive Plan 2005								
– 2005	116,822	–	–	–	116,822	633.5	–	March 2008
– 2006	–	95,121	–	–	95,121	814.0	–	March 2009
Aviva Deferred Bonus Plan								
– 2003	80,100	–	80,100	–	–	379.5	822.0	March 2006
– 2004	68,960	–	–	–	68,960	527.5	–	March 2007
– 2005	68,690	–	–	–	68,690	633.5	–	March 2008
Aviva Annual Bonus Plan								
– 2006	–	47,138	–	–	47,138	814.0	–	March 2009
Patrick Snowball								
Aviva Long-Term Incentive Plan								
– 2003	96,250	–	62,466	33,784	–	379.5	822.0	March 2006
– 2004	84,452	–	–	–	84,452	527.5	–	March 2007
Aviva Long-Term Incentive Plan 2005								
– 2005	107,943	–	–	–	107,943	633.5	–	March 2008
– 2006	–	95,121	–	–	95,121	814.0	–	March 2009
Aviva Deferred Bonus Plan								
– 2003	35,612	–	35,612	–	–	379.5	822.0	March 2006
– 2004	70,802	–	–	–	70,802	527.5	–	March 2007
– 2005	67,068	–	–	–	67,068	633.5	–	March 2008
Aviva Annual Bonus Plan								
– 2006	–	56,100	–	–	56,100	814.0	–	March 2009

Dilution

Awards granted under the Aviva Annual Bonus Plan 2005 and the Aviva Long-Term Incentive Plan 2005 are met by the issue of new shares at the time that the awards vest. The Committee monitors the number of shares issued under its various all employee and discretionary share plans and their effect on dilution limits. The relevant dilution limits established by the Association of British Insurers in respect of all share plans (10% in any rolling ten year period) and executive share plans (5% in any rolling ten year period) were, based on the Company's issued share capital at 31 December 2006, 2.60% and 1.12% respectively.

Between March 1998 and March 2003, the Company met its liability for shares awarded under the incentive plans by funding an employee trust that acquired shares in the market at the time of grant. Details of the shares currently held in the employee trusts are set out in note 29 to the accounts.

Accounting changes

Major changes to accounting policies and practices in 2005, including adopting International Financial Reporting Standards and European Embedded Value principles for supplementary reporting, affected a number of the key performance indicators and performance measures used in connection with the Company's long-term incentive plans. During the transition period the Committee received reports showing the impacts of these changes on the performance measures and satisfied itself that the evaluation of actual performance against the performance conditions which were originally set using prior accounting practices is appropriate having made allowance for the accounting changes.

Senior executives' remuneration

The total compensation paid during the year to key management personnel, being those having authority and responsibility for planning, directing and controlling the activities of the Company, including the Company's directors and non-executive directors (as required to be disclosed by International Accounting Standard 24) was £53 million (2005: £34 million) and is set out below in note 53 to the Accounts.

Non-executive directors' remuneration

The Company's Articles of Association provide that the total aggregate remuneration paid to the Chairman and non-executive directors will be determined by the Board within the limits set by shareholders. The current aggregate limit of £1.5 million was approved by shareholders at the Company's 2005 Annual General Meeting. Executive directors are remunerated under their service contracts and receive no additional fee for serving as directors.

Chairman	£375,000 pa
Board membership fee	£50,000 pa
Additional fees are paid as follows:	
Senior independent director	£10,000 pa
Committee Chairman – Audit	(inclusive of committee membership fee) £35,000 pa
– Remuneration	(inclusive of committee membership fee) £20,000 pa
Committee Membership – Audit	£10,000 pa
– Remuneration	£10,000 pa
– Nomination	£5,000 pa
– Risk and Regulatory	£5,000 pa
– Corporate Social Responsibility	£5,000 pa

Other than for the Chairman's fee, which was increased by £15,000 pa from 1 January 2006 to reflect the loss of a car allowance of £18,000 pa from that date, no increases were made to the level of directors' fees during the year. However, fees payable to the senior independent director, chairman of the Remuneration Committee and for membership of the Risk and Regulatory and Corporate Social Responsibility committees were introduced from 1 April 2006 following changes to the Board committee structure and directors' responsibilities.

In addition to the Board membership and committee membership fees Derek Stevens received an additional amount of £10,000 per annum for serving as the chairman of the Aviva Staff Pension Scheme. The fee for Guillermo de la Dehesa includes an amount of €40,000 per annum for serving as the non-executive chairman of the Group's operations in Spain. No non-executive director accrued retirement benefits during the year.

Directors' remuneration report continued

Directors' interests in Aviva shares

The interests held by each person who was a director at the end of the financial year in the ordinary shares of 25 pence each in the Company are shown below. All the disclosed interests are beneficial. The table also summarises the interests in shares held through the Company's various all-employee and executive share schemes. Details of the options and long-term incentive awards are shown on pages 96 to 98 and the Aviva Share Plan is described on page 97.

	Shares ¹		Bonus Plan Awards ²		Long-Term Incentive Awards ³		Options ⁴		Aviva Share Plan ⁵	
	1 January 2006	31 December 2006	1 January 2006	31 December 2006	1 January 2006	31 December 2006	1 January 2006	31 December 2006	1 January 2006	31 December 2006
Guillermo de la Dehesa	144	144	—	—	—	—	—	—	—	—
Wim Dik	200	200	—	—	—	—	—	—	—	—
Mary Francis	1,000	1,000	—	—	—	—	—	—	—	—
Richard Karl Goeltz	2,500	2,500	—	—	—	—	—	—	—	—
Richard Harvey	44,781	198,758	355,992	311,559	521,496	517,227	4,426	4,426	—	—
Andrew Moss	35,040	43,337	61,408	109,056	186,453	274,257	3,279	3,279	13,462	—
Carole Piwnica	—	2,500	—	—	—	—	—	—	—	—
Philip Scott	170,004	274,896	217,750	184,788	316,939	300,810	4,096	4,096	—	—
Lord Sharman	—	2,000	—	—	—	—	—	—	—	—
Patrick Snowball	16,250	22,815	173,482	193,970	288,645	287,516	2,272	—	—	—
Russell Walls	1,500	1,500	—	—	—	—	—	—	—	—
Former directors										
Derek Stevens*	2,989	3,047	—	—	—	—	—	—	—	—
André Villeneuve*	640	640	—	—	—	—	—	—	—	—

* Retired 31 December 2006.

Notes

1. "Shares" are the directors' beneficial holdings in the ordinary shares of the Company and in respect of the executive directors include shares held in trust under the Company's All Employee Share Ownership Plan (AESOP) being shares purchased by them under the partnership element and shares granted under the free share element of the AESOP. Executive directors are required to build and maintain a beneficial interest in the Company's shares equal in value to 1.5 times their annual salary (1.75 times annual salary in the case of the Group Chief Executive). The requirement was introduced as part of the revised remuneration arrangements from 2005; the holding must be attained within five years.
2. "Bonus Plan Awards" relates to entitlements to shares arising through the current, or former, Aviva Bonus Plans. Under these plans some of the earned bonuses are paid in the form of shares and deferred for three years. The transfer of the shares to the director at the end of the period is not subject to the attainment of performance conditions but a proportion of the shares can be forfeited if the executive leaves service before the end of the period.
3. "Long-Term Incentive Awards" are awards granted under the Aviva Long-Term Incentive Plans which vest only if the performance conditions are achieved.
4. "Options" are options over shares granted under the Savings Related Share Option Scheme.
5. "Aviva Share Plan" relates to shares held under the Plan referred to above in which only Andrew Moss participated.

The following changes to directors' interests which relate to shares acquired each month under the partnership element of the AESOP during the period 1 January 2006 to 28 February 2007 have been reported to the Company.

	Number of shares
Richard Harvey	14
Philip Scott	15
Patrick Snowball	14

This report was reviewed and approved by the Board on 28 February 2007.

Richard Karl Goeltz

Chairman, Remuneration Committee

Independent auditor's report to the shareholders of Aviva plc

We have audited the group and parent company financial statements (the "financial statements") of Aviva plc for the year ended 31 December 2006 which comprise the Accounting Policies, the Consolidated and Parent Company Income Statements, the pro forma reconciliation of Group operating profit to profit before tax, the Consolidated and Parent Company Statement of recognised income and expense, the Consolidated and Parent Company Reconciliation of movements in shareholders' equity, the Consolidated and Parent Company Balance Sheets, the Consolidated and Parent company cash flow Statements and the related notes 1 to 53 and A to J. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members 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 to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

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

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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

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

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

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises only the Overview, the Business review, the Board of Directors, the Directors' report, the Corporate governance report, the Audit Committee report, the Nomination Committee report, the Risk and Regulatory Committee report, the Corporate Social Responsibility committee and the unaudited part of the Directors' Remuneration Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

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

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

Opinion

In our opinion:

- The financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs and the parent Company's affairs as at 31 December 2006 and of the Group's profit and the parent company's loss for the year then ended;
- The financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- The information given in the Directors' report is consistent with the financial statements.

Ernst & Young LLP

Registered Auditor
London
28 February 2007



Being with someone
you trust

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, further details of which are given in note 4.

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 consolidated financial statements using International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and endorsed by the European Union (EU). The date of transition to IFRS was 1 January 2004. The consolidated financial statements have been prepared in accordance with IFRS applicable at 31 December 2006.

In August 2005, the IASB issued IFRS 7, *Financial Instruments: Disclosures*, and an amendment to IAS 1, *Capital Disclosures*. Although their requirements are applicable for accounting periods beginning on or after 1 January 2007, the Group has decided to adopt IFRS 7 early and reflect its impact in these financial statements. The amendment to IAS 1 brings the capital disclosures into line with those already required by FRS 27 and, although the Group is not adopting it early, this is not expected to result in any material additional disclosures.

In November 2006, the IASB issued IFRS 8, *Operating Segments*, the requirements of which are applicable for accounting periods beginning on or after 1 January 2009. This standard has not yet been endorsed by the EU, nor has it yet been adopted by the Group. On adoption, it will result in amendments to the disclosure of our segmental results but will have no impact on the results overall.

In addition, IFRIC interpretation 8, *Scope of IFRS 2*, interpretation 9, *Reassessment of Embedded Derivatives*, interpretation 10, *Interim Financial Reporting and Impairment*, Interpretation 11, *IFRS 2 – Group and Treasury Share Transactions*, and interpretation 12, *Service Concession Arrangements*, have all been issued during 2006 but the last three have not yet been endorsed by the EU. None of them is applicable for the current accounting period and, on adoption, they will not have any impact on the Group's financial reporting.

In accordance with Phase I IFRS 4, *Insurance Contracts*, 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.

In August 2005, the IASB issued an amendment to IAS 39, *Financial Guarantee Contracts*, which requires financial guarantees issued to be recognised initially at their fair value, and subsequently measured at the higher of the expected liability (or receivable) under the guarantee and the amount initially recognised less any cumulative

amortisation. Whilst not material at the Company or consolidated Group level, the amendment affects the Company's subsidiaries in respect of intercompany guarantees given and taken in the ordinary course of business. Further details are given in note A to the Company's separate financial statements.

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. Unless otherwise noted, the amounts shown in these financial statements are in millions of pounds sterling (£m). As supplementary information, consolidated financial information is also presented in euros.

The separate financial statements of the Company are on pages 211 to 218.

FRS 27

Financial Reporting Standard 27, *Life Assurance*, (FRS 27) 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), signed a Memorandum of Understanding (MoU) with the ASB relating to FRS 27. Under this MoU, Aviva voluntarily agreed to adopt in full the standard from 2005 in the Group's IFRS financial statements.

(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. This is particularly so in the estimation of amounts for insurance and participating investment contract liabilities, for which further details are given in policy J below and in notes 35, 37 and 46 to these 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 inter-company 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.

The merger reserve is also used where more than 90% of the shares in a subsidiary are acquired and the consideration includes the issue of new shares by the Company, thereby attracting merger relief under the Companies Act 1985.

Investment vehicles

In several countries, the Group has invested in a number of specialised investment vehicles such as OIECs. These invest mainly in equities, bonds, cash and cash equivalents, and properties, and distribute most of their income. Where Group companies own more than 50% of such vehicles, they are consolidated. The interests of parties other than Aviva in such vehicles are classified as liabilities and appear as "Net asset value attributable to unitholders" in the consolidated balance sheet. Where the Group owns less than 50% of such vehicles, its interests are included in the consolidated balance sheet within financial investments as permitted by IAS 28, *Investments in Associates*.

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 if 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.

If 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.

The Company's investments

In the Company balance sheet, subsidiaries and joint ventures are stated at their fair values, estimated using applicable valuation models underpinned by the Company's market capitalisation.

These investments are classified as available for sale (AFS) financial assets, with changes in their fair value being recorded in a separate investment valuation reserve within equity.

(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. The cumulative translation differences were deemed to be zero at the transition date to IFRS.

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 and designated as held at fair value through profit or loss (FV) (see policy R) are included in foreign exchange gains and losses in the income statement. For monetary financial assets designated as AFS, translation differences are calculated as if they were carried at amortised cost and so are recognised in the income statement, whilst foreign exchange differences arising from fair value gains and losses are included in the investment valuation reserve within equity. Translation differences on non-monetary items, such as equities which are designated as FV, are reported as part of the fair value gain or loss, whereas such differences on AFS equities are included in the investment valuation reserve.

(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 make significant additional payments 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 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 later of the date of transition to IFRS or the date of the acquisition of the entity. Accounting for insurance contracts is determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers in December 2005, as amended in December 2006. However, in certain businesses, the accounting policies or accounting estimates have been changed, as permitted by IFRS 4 and IAS 8 respectively, to remeasure designated insurance liabilities to reflect current market interest rates and changes to regulatory capital requirements.

Accounting policies continued

(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 offset against premiums.

General insurance and health premiums written reflect business inception 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 calculated 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.

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

(G) Other investment contract fee revenue

Investment contract policyholders are charged fees for 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 expected term of the policy by an adjustment to the effective yield. 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. Further details of this analysis and the assumptions used are given in note 8.

(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 practices, with the exception of liabilities remeasured to reflect current market interest rates and those relating to UK with-profit and non-profit contracts. In the United States, shadow adjustments to the liabilities or related deferred acquisition costs are recognised directly in equity so that unrealised gains or losses on assets that are recognised directly in equity affect the measurement of the liability or related deferred acquisition costs in the same way as realised gains or losses. The Group has adopted FRS 27, *Life Assurance*, for liabilities relating to such contracts, which adds to the requirements of IFRS but does not vary them in any way. Further details are given in policy A above.

The long-term business provisions are calculated separately for each life operation, based either on local regulatory requirements or existing local GAAP at the later of the date of transition to IFRS or the date of the acquisition of the entity, 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. The principal assumptions are disclosed in note 35(b). 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. For certain UK non-profit insurance contracts, the Group has adopted the realistic regulatory basis as set out in the FSA Policy Statement 06/14 *Prudential Changes for Insurers* from 31 December 2006.

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 to 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 to either policyholders or shareholders has not been determined by the end of the financial year are held within liabilities as an unallocated divisible surplus.

Liability adequacy

At each reporting date, an assessment is made of whether the recognised long-term business provisions are adequate, using current estimates of future cash flows. If that assessment shows that the carrying amount of the liabilities (less related assets) is insufficient in the light of the estimated future cash flows, the deficiency is recognised in the income statement by setting up an additional provision in the balance sheet.

General insurance and health 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. Further details of estimation techniques are given in note 35(c).

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) is insufficient in light of the estimated future cash flows, the deficiency is recognised in the income statement by setting up a provision in the 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 in 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.

Contract liabilities

Deposits collected under 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.

The majority of the Group's contracts classified as non-participating investment contracts are unit-linked contracts and are measured at fair value. Certain liabilities for non-linked non-participating contracts are measured at amortised cost.

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. For non-linked contracts, the fair value liability is equal to the present value of expected cash flows on a market-consistent 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.

Accounting policies continued

(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) Goodwill, AVIF and 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 cumulative 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.

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 asset. In most cases, this is classified as AVIF but, for non-participating investment contracts, it is included within intangibles. 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.

The full embedded value of the long-term business and further details of the methodology and assumptions are included as supplementary information on pages 220 to 243.

Intangible assets

Intangibles consist primarily of brands, certain of which have been assessed as having indefinite useful lives, and contractual relationships such as access to distribution networks and customer lists. The economic lives of the latter are determined by considering relevant factors such as usage of the asset, typical product life cycles, potential obsolescence, maintenance costs, the stability of the industry, competitive position, and the period of control over the assets. These intangibles are amortised over their useful lives, which range from five to 22 years, using the straight-line method. The amortisation charge for the year is included in the income statement under "Other operating expenses".

Impairment testing

For impairment testing, goodwill and intangibles with indefinite useful lives have been allocated to cash-generating units by geographical reporting unit and business segment. The carrying amount of goodwill and intangible assets with indefinite useful lives is reviewed at least annually or when circumstances or events indicate there may be uncertainty over this value. Goodwill and indefinite life intangibles are written down for impairment where the recoverable amount is insufficient to support its carrying value. Further details on goodwill allocation and impairment testing are given in note 15(b).

(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 any provision for impairment in their values.

Land is not depreciated. 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, or lease term if longer
– 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.

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 in 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 Group 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 Group has transferred its rights to receive cash flows from the asset and has either transferred substantially all the risks and rewards of the asset, or 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) or financial assets available for sale (AFS). The classification depends on the purpose for which the investments were acquired, and is determined by local management at initial recognition. 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").

In general, the FV category is used as, in most cases, the Group's investment or risk management strategy is to manage its financial investments on a fair value basis. Debt securities and equity securities, which the Group buys with the intention to resell in the short term, are classified as trading, as are non-hedge derivatives (see policy S below). All other securities in the FV category are classified as other than trading. The AFS category is used where the relevant long-term business liability (including shareholders' funds) is passively managed.

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.

Financial guarantees are recognised initially at their fair value. They are subsequently measured at the higher of the expected receivable or liability under the guarantee and the amount initially recognised less any accumulated amortisation.

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 impairment. 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.

Accounting policies continued

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 remeasured 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. These amounts are disclosed in note 51.

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 rate 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 rate 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 potential 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:

- (i) a hedge of the fair value of a recognised asset or liability (fair value hedge);
- (ii) 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
- (iii) a hedge of a net investment in a foreign operation (net investment hedge)

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 of whether the hedge is expected to be, and has been, highly effective in offsetting the risk in the hedged item, both at inception and on an ongoing basis.

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 included in 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.

For certain securitised lifetime mortgages, the Group has taken advantage of the revised fair value option under IAS 39 to present the mortgages, associated borrowings and derivative financial instruments at fair value, since they are managed as a portfolio. This presentation provides more relevant information and eliminates any accounting mismatch that would otherwise arise from using different measurement bases for these three items. The fair values of mortgages classified as FV are estimated using discounted cash flow forecasts, based on a risk-adjusted discount rate which reflects the risks associated with these products. They are revalued at each period end, with movements in their fair values 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 and other assets

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 generally not deferred as the liability for these contracts is calculated in accordance with the FSA's realistic capital regime and 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.

Other assets include vehicles which are subject to repurchase agreements and inventories of vehicle parts. The former are carried at the lower of their agreed repurchase price or net realisable value, whilst the latter are carried at the lower of cost and net realisable value, where cost is arrived at on the weighted average cost formula or "first in first out" (FIFO) basis. Provision is made against inventories which are obsolete or surplus to requirements.

(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 in 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. Assets held for use in such leases are included in property and equipment, and are depreciated to their residual values over their estimated useful lives. Rentals from such leases are credited to the income statement on a straight-line basis over the period of the relevant 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 relevant leases.

(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, or if they are possible but not probable.

(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 the relevant Group companies, taking account of the recommendations of qualified actuaries.

Accounting policies continued

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. 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.

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 Canadian scheme are included within those for the defined benefit pension schemes in that country. 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), details of which are given in the Directors' remuneration report and in note 28.

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 vesting 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 against the cost of these shares, 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 taxation 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. In countries where there is a history of tax losses, deferred tax assets are only recognised in excess of deferred tax liabilities if there is convincing evidence that future profits will be available.

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 goodwill for which amortisation is not deductible for tax purposes, 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 at policyholder tax rates. Policyholder tax is accounted for as an income tax and is included in the total tax expense. The Group has decided to show separately the amounts of policyholder tax to provide a more meaningful measure of the tax the Group pays on its profits. In the pro forma 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. All borrowing costs are expensed as they are incurred.

Where loan notes have been issued in connection with securitised lifetime mortgages, the Group has taken advantage of the revised fair value option under IAS 39 to present the mortgages, associated liabilities and derivative financial instruments at fair value, since they are managed as a portfolio. This presentation provides more relevant information and eliminates any accounting mismatch which would otherwise arise from using different measurement bases for these three items.

(AB) Share capital and treasury shares

Equity instruments

An equity instrument is a contract that evidences a residual interest in the assets of an entity after deducting all its liabilities. Accordingly, 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.

Share issue costs

Incremental external costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds of the issue.

Dividends

Interim dividends on ordinary shares are recognised in equity in the period in which they are paid. Final dividends on these shares are recognised when they have been approved by shareholders. Dividends on preference shares are recognised in the period in which they are declared and appropriately approved.

Treasury shares

Where the Company or its subsidiaries purchase the Company's share capital or obtain 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 from fiduciary activities, 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 adjusting items, after tax, attributable to ordinary shareholders, as the directors believe this figure provides a better indication of operating performance. Details are given in note 13.

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) Operations held for sale

Assets and liabilities held for disposal as part of operations which are held for sale are shown separately in the consolidated balance sheet. The relevant assets are recorded at the lower of their carrying amount and their fair value, less the estimated selling costs.

Consolidated income statement

For the year ended 31 December 2006

2006 €m		Note	2006 £m	2005 £m
	Income	5		
42,257	Gross written premiums		28,735	26,299
(2,207)	Premiums ceded to reinsurers		(1,501)	(1,317)
40,050	Premiums written net of reinsurance		27,234	24,982
137	Net change in provision for unearned premiums		93	(123)
40,187	Net earned premiums	F	27,327	24,859
2,750	Fee and commission income	G & H	1,870	1,851
22,754	Net investment income	I	15,473	23,722
713	Share of profit after tax of joint ventures and associates	C	485	340
327	Profit on the disposal of subsidiaries and associates		222	153
66,731			45,377	50,925
	Expenses	6		
(34,476)	Claims and benefits paid, net of recoveries from reinsurers		(23,444)	(19,706)
(3,853)	Change in insurance liabilities, net of reinsurance		(2,620)	(10,376)
(8,826)	Change in investment contract provisions		(6,002)	(7,814)
(821)	Change in unallocated divisible surplus		(558)	(1,474)
(7,416)	Fee and commission expense		(5,043)	(4,330)
(5,231)	Other expenses		(3,557)	(3,166)
(1,221)	Finance costs		(830)	(609)
(61,844)			(42,054)	(47,475)
4,887	Profit before tax		3,323	3,450
(509)	Tax attributable to policyholders' returns	12	(346)	(922)
4,378	Profit before tax attributable to shareholders' profits		2,977	2,528
(1,374)	Tax expense	Z & 12	(934)	(1,552)
509	Less: tax attributable to policyholders' returns	12	346	922
(865)	Tax attributable to shareholders' profits		(588)	(630)
3,513	Profit for the year		2,389	1,898
	Attributable to:			
3,257	Equity shareholders of Aviva plc		2,215	1,767
256	Minority interests		174	131
3,513			2,389	1,898
	Earnings per share	AD & 13		
128.7c	Basic (pence per share)		87.5p	73.5p
127.4c	Diluted (pence per share)		86.6p	72.9p

For the year ended 31 December 2006

2006 €m		Note	2006 £m	2005 £m
	Operating profit before tax attributable to shareholders' profits			
2,788	Long-term business		1,896	1,065
228	Fund management		155	124
2,471	General insurance and health		1,680	1,551
	Other			
(118)	– other operations		(80)	(40)
(235)	– corporate costs		(160)	(136)
(560)	Unallocated interest charges		(381)	(436)
4,574	Operating profit before adjusting items and tax attributable to shareholders' profits		3,110	2,128
	Adjusted for the following:			
(138)	Impairment of goodwill – non-long-term business subsidiaries	15	(94)	(43)
	Amortisation and impairment of acquired value of in-force business			
(126)	– long-term business subsidiaries	16	(86)	(55)
(21)	– long-term business associates	18	(14)	(18)
(103)	Amortisation and impairment of intangibles	16	(70)	(45)
9	Financial Services Compensation Scheme and other levies		6	–
	Short-term fluctuation in return on investments backing			
219	general insurance and health business	8b	149	517
326	Profit on the disposal of subsidiaries and associates	3b	222	153
(362)	Integration and restructuring costs	3c	(246)	(109)
4,378	Profit before tax attributable to shareholders' profits		2,977	2,528
	Tax attributable to shareholders' profits			
(1,066)	Operating profit	13a(i)	(725)	(536)
201	Other activities	13a(i)	137	(94)
(865)			(588)	(630)
3,513	Profit for the year		2,389	1,898

Pro forma reconciliation of Group operating profit
to profit before tax continued
For the year ended 31 December 2006

Operating profit can be further analysed into the following geographical segments:

Year ended 31 December 2006	Long-term business £m	Fund management £m	General insurance and health £m	Total £m
UK	683	56	1,075	1,814
France	273	33	63	369
Netherlands	458	37	139	634
Other Europe	357	13	215	585
United States	71	—	—	71
Rest of the World	54	16	188	258
	1,896	155	1,680	3,731
Other operations				(80)
Corporate costs				(160)
Unallocated interest charges				(381)
				3,110

Year ended 31 December 2005	Long-term business £m	Fund management £m	General insurance and health £m	Total £m
UK	382	44	974	1,400
France	258	26	35	319
Netherlands	172	32	137	341
Other Europe	255	10	218	483
United States	(4)	—	—	(4)
Rest of the World	2	12	187	201
	1,065	124	1,551	2,740
Other operations				(40)
Corporate costs				(136)
Unallocated interest charges				(436)
				2,128

Consolidated statement of recognised income and expense

For the year ended 31 December 2006

2006 €m	Note	2006 £m	2005 £m
550	Fair value gains/(losses) on AFS securities, owner-occupied properties and hedging instruments	374	(52)
(238)	Fair value (gains)/losses transferred to profit	(162)	411
(3)	Impairment losses on revalued assets	(2)	(45)
–	Share of fair value changes in joint ventures and associates taken to equity	–	2
(168)	Actuarial (losses) on pension schemes	(114)	(547)
(509)	Foreign exchange rate movements	(346)	(2)
–	Aggregate tax effect – policyholder tax	–	3
(7)	Aggregate tax effect – shareholder tax	(5)	272
(375)	Net income recognised directly in equity	(255)	42
3,513	Profit for the year	2,389	1,898
3,138	Total recognised income and expense for the year	2,134	1,940
	Attributable to:		
2,909	Equity shareholders of Aviva plc	1,978	1,827
229	Minority interests	156	113
3,138		2,134	1,940

Reconciliation of movements in consolidated shareholders' equity

For the year ended 31 December 2006

2006 €m	Note	2006 £m	2005 £m
16,555	Balance at 1 January	11,092	8,993
3,185	Total recognised income and expense for the year	2,134	1,940
(1,137)	Dividends and appropriations	(762)	(657)
1,331	Issue of share capital for the acquisition of AmerUs (2005: RAC plc), net of transaction costs	892	530
64	Other issues of share capital, net of transaction costs	43	59
303	Shares issued in lieu of dividends	203	100
593	Capital contributions from minority shareholders	397	212
(112)	Minority share of dividends declared in the year	(75)	(70)
137	Minority interest in acquired/(disposed) subsidiaries	92	(36)
72	Reserves credit for equity compensation plans	48	22
–	Other movements	–	(1)
20,991	Balance at 31 December	14,064	11,092

Consolidated balance sheet

As at 31 December 2006

2006 €m		Note	2006 €m	2005 €m
Assets				
4,343	Goodwill	M & 15	2,910	2,274
4,072	Acquired value of in-force business and intangible assets	M & 16	2,728	803
4,172	Investments in joint ventures	C & 17	2,795	2,129
1,336	Investments in associates	C & 18	895	885
1,349	Property and equipment	N & 19	904	885
22,572	Investment property	O & 20	15,123	13,275
39,470	Loans	T & 21	26,445	24,544
	Financial investments	Q, R & 23		
168,718	Debt securities		113,041	103,917
84,719	Equity securities		56,762	52,044
49,328	Other investments		33,050	26,427
302,765			202,853	182,388
11,679	Reinsurance assets	L & 36	7,825	7,130
1,790	Deferred tax assets	Z & 40b	1,199	1,018
513	Current tax assets	40a	344	87
12,088	Receivables and other financial assets	24	8,098	7,706
5,188	Deferred acquisition costs and other assets	U & 25	3,476	3,766
3,858	Prepayments and accrued income	25d	2,585	2,363
21,704	Cash and cash equivalents	V & 48d	14,542	13,732
–	Assets of operations classified as held for sale	AE & 3d	–	462
436,899	Total assets		292,722	263,447
Equity				
	Capital	AB		
957	Ordinary share capital	27	641	599
299	Preference share capital	30	200	200
1,256			841	799
	Capital reserves			
1,775	Share premium	27	1,189	1,167
4,882	Merger reserve	C & 32a	3,271	3,271
6,657			4,460	4,438
1,482	Other reserves	32b	993	1,140
7,585	Retained earnings	33	5,082	2,597
16,980	Equity attributable to shareholders of Aviva plc		11,376	8,974
1,477	Direct capital instrument	31	990	990
2,534	Minority interests	34	1,698	1,128
20,991	Total equity		14,064	11,092
Liabilities				
215,269	Gross insurance liabilities	J & 35	144,230	132,602
131,878	Gross liabilities for investment contracts	K & 37	88,358	77,309
14,127	Unallocated divisible surplus	J	9,465	8,978
5,687	Net asset value attributable to unitholders	C	3,810	3,137
4,254	Provisions	X, Y & 41	2,850	2,875
4,593	Deferred tax liabilities	Z & 40b	3,077	2,458
1,884	Current tax liabilities	40a	1,262	1,033
18,115	Borrowings	AA & 43	12,137	11,013
13,784	Payables and other financial liabilities	Q & 44	9,235	9,485
6,317	Other liabilities	45	4,234	3,320
–	Liabilities of operations classified as held for sale	AE & 3d	–	145
415,908	Total liabilities		278,658	252,335
436,899	Total equity and liabilities		292,722	263,447

Approved by the Board on 28 February 2007.

Andrew Moss, Director

Consolidated cash flow statement

For the year ended 31 December 2006

The cash flows presented in this statement cover all the Group's activities and include flows from both policyholder and shareholder activities.

	Note	Long-term business operations 2006 £m	Non-long-term business operations 2006 £m	Total 2006 £m	Total 2005 £m
Cash flows from operating activities					
Cash generated from operations	48a	1,985	470	2,455	2,784
Tax paid		(512)	(83)	(595)	(375)
Net cash from operating activities		1,473	387	1,860	2,409
Cash flows from investing activities					
Acquisitions of subsidiaries, joint ventures and associates, net of cash acquired	48b	(96)	(1,793)	(1,889)	(1,423)
Disposals of subsidiaries, joint ventures and associates, net of cash transferred	48c	102	514	616	464
Net loans to joint ventures and associates	17a & 18a	(113)	9	(104)	(128)
Purchases of property and equipment	19	(55)	(240)	(295)	(206)
Proceeds on sale of property and equipment		10	146	156	50
Purchases of intangible assets		(10)	(48)	(58)	(60)
Net cash used in investing activities		(162)	(1,412)	(1,574)	(1,303)
Cash flows from financing activities					
Proceeds from issue of ordinary shares, net of transaction costs	27b	–	935	935	59
Net drawdown of borrowings	43c	(466)	1,367	901	856
Interest paid on borrowings		(367)	(458)	(825)	(609)
Preference dividends paid		–	(17)	(17)	(17)
Ordinary dividends paid		–	(490)	(490)	(498)
Coupon payments on direct capital instrument		–	(52)	(52)	(42)
Finance lease payments		–	(22)	(22)	(8)
Capital contributions from minority shareholders		295	9	304	212
Dividends paid to minority interests of subsidiaries		(53)	(22)	(75)	(70)
Non-trading cash flows between operations		(288)	288	–	–
Net cash from financing activities		(879)	1,538	659	(117)
Net increase in cash and cash equivalents					
Cash and cash equivalents at 1 January	48d	10,107	2,960	13,067	12,126
Effect of exchange rate changes on cash and cash equivalents		(119)	(47)	(166)	(48)
Cash and cash equivalents at 31 December	48d	10,420	3,426	13,846	13,067

Of the total cash and cash equivalents shown for 2005, £25 million was classified as held for sale (see note 3d).

Notes to the consolidated financial statements

1 – Exchange rates

The Group's principal overseas operations during the year were located within the Eurozone and the United States. The results and cash flows of these operations have been translated into sterling at an average rate for the year of €1 = £0.68 (2005: €1 = £0.68) and £1 = US\$1.84 (2005: £1 = US\$1.82). Assets and liabilities have been translated at the year end rate of €1 = £0.67 (2005: €1 = £0.69) and £1 = US\$1.96 (2005: £1 = US\$1.72).

Total foreign currency movements during 2006 resulted in a gain recognised in the income statement of £99 million (2005: £203 million loss).

2 – Presentation changes

The results of the Group's fund management business in the Netherlands were previously reported within the result of our other operations but are now shown as part of our fund management operations. The result reclassified in 2006 is £37 million (2005: £32 million). The related assets and liabilities reclassified at 31 December 2006 are £63 million (2005: £54 million) and £18 million (2005: £15 million) respectively.

3 – Subsidiaries

(a) Acquisitions

(i) Ark Life Assurance Company Limited

On 27 January 2006, Hibernian Life Holdings Limited (HLH), the parent company of Hibernian Life & Pensions Limited, acquired all the shares of Ark Life Assurance Company Limited (Ark Life) from Allied Irish Banks plc (AIB) in exchange for a 24.99% stake in the enlarged HLH and a balancing cash payment of €196 million (£134 million) which also reflects the transfer of the management of Ark Life funds to Hibernian Investment Managers Limited, part of the Group's fund management business. The final consideration has not yet been agreed with AIB but is expected to be finalised in 2007. However, any adjustment to the above figures is not expected to be material. In addition, a further deferred cash payment of up to €10 million (£7 million) is payable, subject to the fulfilment of certain performance criteria.

The results of Ark Life have been included in the consolidated financial statements of the Group with effect from 27 January 2006, and contributed £40 million to the consolidated profit before tax.

The transaction has been accounted for as the acquisition of 75.01% of Ark Life and the disposal of 24.99% of HLH. The realised gain on disposal of the Group's 24.99% interest in HLH was £86 million.

The Ark Life acquisition has given rise to goodwill on acquisition of £57 million, calculated as follows:

Purchase cost:

	£m
Fair value of shares in Hibernian Life Holdings Limited	184
Cash paid	134
Attributable costs	4
Total consideration	322

The assets and liabilities at the date of acquisition were:

	Book value £m	Fair value and accounting policy £m	Fair value £m
Assets			
Acquired value of in-force business on insurance and investment contracts	–	168	168
Other intangible assets	1	44	45
Investments	2,939	(74)	2,865
Other assets	1,225	(15)	1,210
Total assets	4,165	123	4,288
Liabilities			
Gross insurance liabilities	(1,767)	(22)	(1,789)
Gross liability for investment contracts	(2,066)	(25)	(2,091)
Other liabilities	(154)	96	(58)
Total liabilities	(3,987)	49	(3,938)
Total net assets	178	172	350
Net assets acquired (Group share)			265
Goodwill arising on acquisition			57

3 – Subsidiaries continued

The value of the agreement to distribute through AIB's networks has been identified as a separate intangible asset and valued by an independent third party at £45 million, using estimated post-tax cash flows and discount rates. It has been assessed as having a life of 25 years and is being amortised over that period, with a corresponding release of the applicable deferred tax provision.

The residual goodwill of £57 million represents future synergies expected to arise in the combined life operations.

As disclosed in the supplementary information on page 231, the embedded value of the long-term business acquired was £310 million, representing the net assets adjusted for other intangible assets net of tax.

(ii) Eagle Insurance Company Limited

On 1 February 2006, the Group acquired a 51% interest in Eagle Insurance Limited (Eagle), the third-largest insurer in Sri Lanka, by buying a majority shareholding in Eagle's immediate holding company, NDB Finance Lanka (Pvt) Limited. At the same time, Eagle entered into a ten year bancassurance agreement with National Development Bank Limited (NDB), Sri Lanka's biggest development bank and Eagle's other major shareholder. The cash consideration, including purchase costs, was £15 million. The fair value of the Group's share of net assets acquired was £12 million, including intangibles of £2 million, giving rise to £3 million of goodwill on acquisition.

As disclosed in the supplementary information on page 231, the embedded value of the long-term business acquired was £17 million, representing the net assets adjusted for other intangible assets net of tax.

(iii) Canadian brokers

On 28 April 2006, the Group acquired a 20% holding in Dale-Parizeau L.M. Inc, a Canadian insurance broker, for a consideration of £16 million which includes purchase costs. The allocation of the risks and rewards of ownership between the Group and third-party investors in the broker has led the Group to consolidate its results for the period since acquisition to 31 December 2006. The fair value of the net assets acquired, including intangibles of £10 million, was £9 million, giving rise to £7 million of goodwill on acquisition.

On 4 December 2006, the Group acquired a 20% holding in a second Canadian Insurance broker, Morris & Mackenzie Inc (M&M), for a consideration of £28 million including purchase costs. The allocation of the risks and rewards of ownership between the Group and third-party investors in the broker has led the Group to consolidate its results for the period since acquisition to 31 December 2006. Due to the proximity of the acquisition date to the year end, provisional fair values have been used and will be adjusted within 12 months. The provisional fair value of the net assets acquired, including intangibles of £14 million, was £12 million, giving rise to £16 million of goodwill on acquisition. On 31 December 2006, the Group completed the disposal of M&M's non-Quebec based operations for £9 million. The sale did not give rise to any gain or loss. Net assets at disposal represented goodwill, intangible assets and deferred tax liabilities.

(iv) AmerUs Group Co

On 15 November 2006, the Group acquired 100% of the common stock of AmerUs Group Co. (AmerUs) for US\$69 in cash per common share of AmerUs. AmerUs is a leading provider of equity-indexed life and annuity products to the United States retirement and savings markets, and the acquisition establishes a leading presence for the Group in these selected high-growth segments.

The total purchase price of US\$3.1 billion (£1.7 billion) represents cash consideration for AmerUs shares and stock options, and stock-based compensation vesting on change of control. The purchase consideration was partly financed by a £903 million placing of the Company's ordinary shares, with the balance of funding being provided by internal resources and external debt. The share placing was completed on 13 July 2006, with 129 million shares issued on 18 July, at £7 per share.

The issue of new shares in the Company has attracted merger relief under section 131 of the Companies Act 1985. Of the £903 million above, £32 million has been credited to share capital (see note 27) and £871 million has been credited to the merger reserve (see note 32(a)). Expenses of £11 million have been charged to the share premium account.

The AmerUs acquisition has given rise to goodwill on acquisition of £669 million, calculated as follows:

Purchase cost:

	£m
Cash paid	1,669
Attributable costs	11
Total consideration	1,680

Notes to the consolidated financial statements continued

3 – Subsidiaries continued

The assets and liabilities at the date of acquisition were:

	Book value £m	Fair value and accounting policy £m	Fair value £m
Assets			
Acquired value of in-force business on insurance and investment contracts	179	1,387	1,566
Other intangible assets	126	165	291
Investments	11,539	5	11,544
Other assets	2,717	(1,270)	1,447
Total assets	14,561	287	14,848
Liabilities			
Gross insurance liabilities	11,055	(50)	11,005
Gross liability for investment contracts	1,137	5	1,142
Other liabilities	1,503	187	1,690
Total liabilities	13,695	142	13,837
Total net assets acquired	866	145	1,011
Goodwill arising on acquisition			669

The largest fair value adjustments above relate to the recognition of a value for the in-force business on insurance and investment contracts acquired by the Group (the AVIF) and to a reduction in Other assets. The AVIF adjustment of £1,387 million represents the excess of the value of the acquired in-force life insurance contracts over their IFRS net asset value, and is calculated as the difference between the acquired net tangible assets on a European Embedded (EEV) value basis and the same net assets on an IFRS basis. Deferred acquisition costs (DAC) totalling £1,297 million, included in Other assets in the book value column above, are not recognised in the IFRS fair value balance sheet as they have no fair value at acquisition. As DAC is reflected in the calculation of AVIF, its write-off in fair value adjustments is offset by the recognition of a fair value in AVIF.

Other intangible assets of £291 million are represented by AmerUs' distribution channels and have been valued by an independent third-party, using estimated post-tax cash flows and discount rates. The distribution channels have been assessed as having a life of between six and nine years and their value is being amortised over that period, with a corresponding release of the applicable deferred tax provision.

The residual goodwill of £669 million represents future synergies expected to arise in the combined life operations, the value of new business from new distribution channels and customers going forward, and the value of the workforce and management, related know-how and other future business value not included in the intangibles and the AVIF.

As disclosed in the supplementary information on page 231, the embedded value of the long-term business acquired was £1,107 million, representing the net assets acquired, adjusted for other intangible assets net of tax and corporate debt.

(v) Material acquisitions summary

	£m
Total net assets	1,405
Less: Minority interests	(96)
Net assets acquired	1,309
Goodwill arising on acquisition	752
Total consideration	2,061
The total consideration comprised:	
Cash paid	1,862
Fair value of shares	184
Attributable costs	15
	2,061

(vi) Other

In addition to the goodwill arising on the above acquisitions, the Group also made a number of smaller acquisitions giving rise to additional goodwill of £9 million. Total goodwill arising in the year was £761 million (see note 15a). On 1 January 2006, following the introduction of a new Health Insurance Act, a Netherlands subsidiary acquired 100% of the share capital of O.W.M. Delta Lloyd and OHRA Zorgverzekerings U.A. for nil consideration. Assets and liabilities acquired amounted to £272 million and £258 million respectively giving rise to £14 million of negative goodwill which has been recognised in the income statement.

3 – Subsidiaries continued**(vii) Unaudited pro forma combined revenues and profit**

Shown below are unaudited pro forma figures for the Group's combined revenues and profit as though the acquisition date for all business combinations effected during the year had been 1 January 2006, after giving effect to purchase accounting adjustments and the elimination of intercompany transactions. The pro forma financial information is not necessarily indicative of the combined results that would have been attained had the acquisitions taken place at 1 January 2006, nor is it necessarily indicative of future results.

	2006 £m
Revenues (net earned premiums and fee income)	30,670
Profit before tax attributable to shareholders	3,076

Of the above pre-tax profit, £83 million has arisen since acquisition. No adjustments have been made to the profit figure above for any additional borrowing costs, integration costs or other synergies that might arise had the acquisitions been completed at 1 January 2006.

(viii) Non-adjusting post-balance sheet events

On 1 January 2007, the Group acquired 100% of the shares of the Eurolloyd companies (Eurolloyd Nederland BV and Eurolloyd Belgie NV) for cash of £11 million. In view of the very recent timing and immaterial nature of this transaction, it is currently impractical to comply with the requirements of paragraph 67 of IFRS 3, Business Combinations, and to state with any certainty the fair values of the assets and liabilities acquired, and therefore to estimate the goodwill arising on this acquisition.

In addition to the above transaction, subsequent to year end, the Group has announced that it will acquire two of the units of Bumiputra-Commerce Holdings Berhad (BCHB) – 49% of each of a Life and a Takaful business - for approximately £75 million. This transaction is subject to signature and regulatory approval but completion is expected to occur by the second quarter of 2007.

On 8 February 2007, the Group announced that it planned to acquire 100% of the shares in Erasmus Groep BV in the Netherlands. Erasmus writes both general insurance and long-term business and, at 31 December 2005, had gross assets of £648 million and net assets of £29 million. The acquisition, when completed, will be effective from 1 January 2007, subject to the approval of the Dutch regulator, the relevant works council and notification to the relevant competition authorities.

(b) Disposal of subsidiaries, joint ventures and associates

The profit on the disposal of subsidiaries and associates comprises:

	2006 £m	2005 £m
United Kingdom (see below)	69	10
Ireland (see note 3(a)(i))	86	–
France (see note 18(b))	79	–
Asia	–	165
Other small operations	(12)	(22)
Profit on disposal before tax	222	153
Tax on profit on disposal	13	(43)
Profit on disposal after tax	235	110

The tax credit on the profit on disposal reflects the benefit of prior year tax credits against charges on disposals in earlier years.

Sale of RAC non-core businesses

During 2006, the Group completed the disposal of the Manufacturer Support Services (MSS) and Lex Vehicle Leasing (LVL) divisions, which had been acquired with the RAC Group in 2005. The decision to sell was part of the Group's wider strategy to integrate RAC and exit non-core operations.

	2006 £m
Proceeds from sale	358
Net assets disposed of	(310)
Transaction costs	(15)
Profit before tax and pension curtailment gain	33
Pension curtailment gain	36
Profit on disposal before tax	69
Tax attributable to profit on disposal	(11)
Profit on disposal after tax	58

Notes to the consolidated financial statements continued

3 – Subsidiaries continued

The net assets disposed of, which total £310 million, comprised investment in joint ventures of £239 million, tangible assets of £102 million, other assets of £95 million and other liabilities of £126 million. The pension curtailment gain arose from the remeasurement of pension liabilities in the RAC plc defined benefit pension scheme, following the MSS and LVL disposals.

(i) Sale of MSS

The MSS disposal was completed in three stages during the first six months of 2006, following the disposals of certain operational assets and liabilities of Hyundai Cars (UK) and the commercial fleet business of Lex Transfleet in 2005. On 10 January 2006, the Group sold Hyundai Car Finance Limited, which provides vehicle instalment finance and leasing, to Lloyds TSB. On 14 February 2006, the Group sold Lex Autologistics Limited, Lex Commercial Limited and associated properties to Imperial Holdings. On 27 April 2006, the Group completed the sale of the remaining vehicle solutions businesses, comprising Lex Transfleet Limited, Lex Defence Limited, Lex Defence Management Limited and RAC Software Solutions Limited, to VT Group plc. Receipts from the completion of the disposal of the MSS division totalled £111 million, resulting in a profit of £12 million before tax.

In 2005, the Group sold certain operational assets and liabilities of Hyundai Cars (UK) and the commercial fleet business of Lex Transfleet for total consideration of £139 million. The sale resulted in a profit of £5 million, which is included in the 2005 figures above.

Of the total consideration of £250 million received for MSS disposals in 2005 and 2006, £73 million was in respect of retained liabilities to be settled by the Group.

(ii) Sale of LVL

On 31 May 2006, the sale of Aviva's 50% stake in Lex Vehicle Leasing (Holdings) Limited to HBOS plc was completed. Under the terms of the joint venture agreement, the change of control of RAC provided HBOS with the right to acquire Aviva's interest in LVL which HBOS chose to exercise. The proceeds consisted of a net cash receipt of £227 million, from which Aviva's estimated contribution of £16 million to the statutory debt funding of the RAC plc defined benefit pension scheme had been deducted. The gross consideration was therefore £243 million. In addition to the disposal of the investment in the joint venture of £239 million, HBOS will make an equivalent contribution to the statutory debt funding of the defined benefit pension scheme, estimated at £16 million. The sale resulted in a profit of £18 million before tax. A further £3 million profit arose on the sale of the Lex brand.

No other disposal is considered material for further disclosure.

(c) Integration and restructuring costs

£246 million of integration and restructuring costs have been included in the results for 2006. £21 million related to the restructuring of the combined Norwich Union Insurance and RAC businesses and this completes the integration spend on the RAC businesses. £8 million relates to the integration of Ark Life into the Hibernian business and £12 million to the integration of AmerUs into the US business. The remaining £205 million relates to Norwich Union's restructuring to reduce duplication and improve efficiency.

(d) Operations classified as held for sale

	2005 £m
Intangible assets	9
Investment and property and equipment	320
Receivables and other financial assets	68
Deferred acquisition costs and other assets	40
Cash and cash equivalents	25
Total assets	462
Payables and financial liabilities	(96)
Other liabilities	(49)
Total liabilities	(145)
Net assets	317

As described in note 3(b) above, the RAC non-core businesses, which were treated as held for sale as at 31 December 2005, have been sold during 2006. No operations have been classified as held for sale as at 31 December 2006.

3 – Subsidiaries continued

(e) Other information

Principal subsidiaries at 31 December 2006 are listed on pages 244 to 245.

One of the Group's wholly-owned subsidiaries, Delta Lloyd NV, is subject to the provisions of Dutch corporate law and particularly the Dutch "structure company" regime. Under this regime, Delta Lloyd operates under a Supervisory Board which has a duty to have regard to the interests of a wide variety of stakeholders. The Supervisory Board includes two Aviva Group representatives and is responsible for advising and supervising Delta Lloyd's Executive Board. The shareholder is one of the most important stakeholders to whom the Supervisory Board has a duty.

Dutch Law changed in October 2004 to ensure that Supervisory Board directors in Dutch companies were henceforth to be elected by a company's shareholders voting on nominations made by its Supervisory Board and the Works Council. Under the previous system, Supervisory Board directors appointed their own successors. In 2006, Delta Lloyd commenced proceedings against Aviva plc to try to compel the Company to adhere to the system that existed prior to the change in the law, on the basis of agreements they say were entered into in 1973 when the Group acquired Delta Lloyd. The Company disputes these claims and does not expect the litigation, whatever its outcome, to have any adverse effect on the financial or operational performance of Delta Lloyd or the Group.

4 – Segmental information

(a) Primary reporting format – business segments

(i) Reporting segments

The principal activity of the Group is financial services, which is managed using the following reportable segments: long-term business, fund management, general insurance and health.

Long-term business

Our long-term business comprises life insurance, long-term health and accident insurance, savings, pensions and annuity business written by our life insurance subsidiaries, including managed pension fund business and our share of the other life and related business written in our associates and joint ventures, as well as the Lifetime mortgage business written in the UK.

Fund management activities

Our fund management business invests policyholders' and shareholders' funds, provides investment management services for institutional pension fund mandates and manages a range of retail investment products, including investment funds, unit trusts, OEICs and ISAs. Clients include Aviva Group businesses and third-party financial institutions, pension funds, public sector organisations, investment professionals and private investors.

General insurance and health

Our general insurance and health business provides insurance cover to individuals and to small- and medium-sized businesses, for risks associated mainly with motor vehicles, property and liability, such as employers' liability and professional indemnity liability, and medical expenses.

Other

Other activities not related to the core business segments or which are not reportable segments due to their immateriality, such as the RAC non-insurance operations, our banking businesses and service companies, are included as "Other", in the following tables. Head office expenses, such as Group treasury and finance functions are also reported as "Other", together with eliminations and any other reconciling items. Certain financing costs and taxes are not allocated across the segments.

The accounting policies of the segments are the same as those for the Group as a whole. Any transactions between the business segments are on normal commercial terms and market conditions.

Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balance sheet but excluding items such as tax and certain borrowings.

Notes to the consolidated financial statements continued

4 – Segmental information continued*(ii) Segmental results by business segment*

For the year ended 31 December 2006	Long-term business £m	Fund management £m	General insurance and health £m	Other £m	Total £m
Gross written premiums	17,308	–	11,427	–	28,735
Premiums ceded to reinsurers	(776)	–	(725)	–	(1,501)
Net written premiums	16,532	–	10,702	–	27,234
Net change in provision for unearned premiums	–	–	93	–	93
Net earned premiums	16,532	–	10,795	–	27,327
Fee and commission income	630	452	172	616	1,870
Net investment income	17,162	452	10,967	616	29,197
Inter-segment revenue	13,928	17	1,299	229	15,473
Profit on the disposal of subsidiaries and associates	–	199	–	–	199
Profit on the disposal of subsidiaries and associates	12	–	88	122	222
Segment income	31,102	668	12,354	967	45,091
Claims and benefits paid, net of recoveries from reinsurers	(16,523)	–	(6,921)	–	(23,444)
Change in insurance liabilities, net of reinsurance	(2,594)	–	(26)	–	(2,620)
Change in investment contract provisions	(6,002)	–	–	–	(6,002)
Change in unallocated divisible surplus	(558)	–	–	–	(558)
Fee and commission expenses	(2,125)	(111)	(2,742)	(65)	(5,043)
Other operating expenses					
Depreciation	(12)	(3)	(19)	(89)	(123)
Amortisation of acquired value of in-force business	(58)	–	–	–	(58)
Net Impairment of acquired value of in-force business	(28)	–	–	–	(28)
Amortisation and net impairment of intangible assets	(32)	(1)	(18)	(19)	(70)
Impairment of goodwill	–	–	–	(94)	(94)
Other impairment losses recognised in the income statement	6	–	(5)	(1)	–
Inter-segment expense	(190)	–	(8)	(1)	(199)
Other expenses	(990)	(392)	(806)	(996)	(3,184)
Finance costs	(367)	–	(3)	(230)	(600)
Segment expenses	(29,473)	(507)	(10,548)	(1,495)	(42,023)
Segment result before share of profit/(loss) of joint ventures and associates	1,629	161	1,806	(528)	3,068
Share of profit/(loss) of joint ventures and associates	471	(7)	5	16	485
Segment result before tax	2,100	154	1,811	(512)	3,553
Unallocated costs					
Finance costs on central borrowings (see below)					(230)
Tax attributable to policyholders' returns					(346)
Tax attributable to shareholders' profits					(588)
Profit for the year					2,389

Finance costs on central borrowing comprise interest payable on borrowings by holding companies within the Group which is not allocated to operating companies.

Impairment losses, and reversal of such losses, recognised directly in equity were nil and £2 million respectively in long-term business.

4 – Segmental information continued

Pro forma reconciliation to operating profit before tax attributable to shareholders' profits

For the year ended 31 December 2006	Long-term business £m	Fund management £m	General insurance and health £m	Other £m	Total £m
Segment result before tax	2,100	154	1,811	(512)	3,553
Finance costs on central borrowings	–	–	(2)	(228)	(230)
Adjusted for the following:					
Impairment of goodwill	–	–	–	94	94
Amortisation and impairment of acquired value of in-force business	100	–	–	–	100
Amortisation and impairment of intangibles	32	1	18	19	70
Financial Services Compensation Scheme and other levies	–	–	(6)	–	(6)
Short-term fluctuation in return on investments backing general insurance and health business	–	–	(149)	–	(149)
Profit on the disposal of subsidiaries and associates	(12)	–	(88)	(122)	(222)
Integration and restructuring costs	21	–	95	130	246
Unallocated interest and corporate cost reallocation	1	–	1	(2)	–
	2,242	155	1,680	(621)	3,456
Less:					
Tax attributable to policyholders' returns	(346)	–	–	–	(346)
Operating profit before tax attributable to shareholders' profits	1,896	155	1,680	(621)	3,110

Notes to the consolidated financial statements continued

4 – Segmental information continued

For the year ended 31 December 2005	Long-term business £m	Fund management £m	General insurance and health £m	Other £m	Total £m
Gross written premiums	15,282	–	11,017	–	26,299
Premiums ceded to reinsurers	(611)	–	(706)	–	(1,317)
Net written premiums	14,671	–	10,311	–	24,982
Net change in provision for unearned premiums	–	–	(123)	–	(123)
Net earned premiums	14,671	–	10,188	–	24,859
Fee and commission income	598	318	218	717	1,851
	15,269	318	10,406	717	26,710
Net investment income	21,985	15	1,603	119	23,722
Inter-segment revenue	–	112	–	–	112
Profit/(loss) on the disposal of subsidiaries and associates	(10)	–	41	122	153
Total income	37,244	445	12,050	958	50,697
Claims and benefits paid, net of recoveries from reinsurers	(13,482)	–	(6,224)	–	(19,706)
Change in insurance liabilities, net of reinsurance	(10,004)	–	(372)	–	(10,376)
Change in investment contract provisions	(7,814)	–	–	–	(7,814)
Change in unallocated divisible surplus	(1,474)	–	–	–	(1,474)
Fee and commission expenses	(1,481)	(78)	(2,756)	(15)	(4,330)
Other operating expenses					
Depreciation	(11)	(6)	(17)	(78)	(112)
Amortisation of acquired value of in-force business	(27)	–	–	–	(27)
Net Impairment of acquired value of in-force business	(28)	–	–	–	(28)
Amortisation and net impairment of intangible assets	(24)	–	(5)	(16)	(45)
Impairment of goodwill	(14)	–	–	(29)	(43)
Other impairment losses recognised in the income statement	(37)	–	–	–	(37)
Inter-segment expense	(103)	–	(9)	–	(112)
Other expenses	(999)	(236)	(615)	(1,024)	(2,874)
Finance costs	(203)	–	(58)	(100)	(361)
Segment expenses	(35,701)	(320)	(10,056)	(1,262)	(47,339)
Segment result before share of profit/(loss) of joint ventures and associates	1,543	125	1,994	(304)	3,358
Share of profit/(loss) of joint ventures and associates	322	(1)	1	18	340
Segment result before tax	1,865	124	1,995	(286)	3,698
Unallocated costs					
Finance costs on central borrowings (see below)					(248)
Tax attributable to policyholders' returns					(922)
Tax attributable to shareholders' profits					(630)
Profit for the year					1,898

Finance costs on central borrowings comprise interest payable on borrowings by holding companies within the Group which is not allocated to operating companies.

Impairment losses, and reversal of such losses, recognised directly in equity were £45 million and nil respectively in long-term business.

4 – Segmental information continued

Pro forma reconciliation to operating profit before tax attributable to shareholders' profits

For the year ended 31 December 2005	Long-term business £m	Fund management £m	General insurance and health £m	Other £m	Total £m
Segmental result before tax	1,865	124	1,995	(286)	3,698
Finance costs on central borrowings	–	–	–	(248)	(248)
Adjusted for the following items:					
Impairment of goodwill	14	–	–	29	43
Amortisation and impairment of acquired value of in-force business	73	–	–	–	73
Amortisation and impairment of intangibles	24	–	5	16	45
Financial Services Compensation Scheme and other levies	–	–	–	–	–
Short-term fluctuations in return on investments backing general insurance and health business	–	–	(517)	–	(517)
Loss/(profit) on the disposal of subsidiaries and associates	10	–	(41)	(122)	(153)
Integration costs	–	–	77	32	109
Unallocated interest	–	(1)	25	(24)	–
Corporate cost reallocation	1	1	7	(9)	–
	1,987	124	1,551	(612)	3,050
Less:					
Tax attributable to policyholders' returns	(922)	–	–	–	(922)
Operating profit before tax attributable to shareholders' profits	1,065	124	1,551	(612)	2,128

(iii) Segmental balance sheet by business segment

As at 31 December 2006	Long-term business £m	Fund management £m	General insurance and health £m	Other £m	Total £m
Goodwill	1,316	9	390	1,195	2,910
Acquired value of in-force business and intangible assets	2,301	18	287	122	2,728
Investments in joint ventures and associates	3,526	44	39	81	3,690
Property and equipment	416	4	94	390	904
Investment property	14,714	–	384	25	15,123
Loans	18,805	–	735	6,905	26,445
Financial investments	188,050	30	11,248	3,525	202,853
Other assets	24,383	534	9,755	1,854	36,526
Segment assets	253,511	639	22,932	14,097	291,179
Unallocated assets – tax assets					1,543
Total assets					292,722
Insurance liabilities	126,224	–	18,006	–	144,230
Liability for investment contracts	88,358	–	–	–	88,358
Unallocated divisible surplus	9,465	–	–	–	9,465
Net asset value attributable to unitholders	3,786	1	23	–	3,810
External borrowings	3,894	–	11	4,037	7,942
Other liabilities, including inter-segment liabilities	6,999	313	(712)	9,719	16,319
Segment liabilities	238,726	314	17,328	13,756	270,124
Unallocated liabilities					4,195
Central borrowings (see below)					4,339
Total liabilities					278,658
Total equity					14,064
Total equity and liabilities					292,722
Capital expenditure (excluding business combinations)					
Intangible assets	29	14	15	32	90
Property and equipment	55	3	13	224	295
	84	17	28	256	385

Central borrowings are borrowings by holding companies within the Group which are not allocated to operating companies. In 2006, there has been a reclassification of Amstelhuys loans into "Other" business from our general insurance and health segment.

Notes to the consolidated financial statements continued

4 – Segmental information continued

As at 31 December 2005	Long-term business £m	Fund management £m	General insurance and health £m	Other £m	Total £m
Goodwill	631	–	398	1,245	2,274
Acquired value of in-force business and intangible assets	424	–	265	114	803
Investments in joint ventures and associates	2,815	46	39	114	3,014
Property and equipment	367	4	126	388	885
Investment property	12,895	–	338	42	13,275
Loans	18,240	–	3,661	2,643	24,544
Financial investments	166,211	22	12,496	3,659	182,388
Other assets	23,185	490	9,425	2,059	35,159
Segment assets	224,768	562	26,748	10,264	262,342
Unallocated assets – tax assets					1,105
Total assets					263,447
Insurance liabilities	114,176	–	18,426	–	132,602
Liability for investment contracts	77,309	–	–	–	77,309
Unallocated divisible surplus	8,978	–	–	–	8,978
Net asset value attributable to unitholders	3,137	–	–	–	3,137
External borrowings	4,060	–	2,565	578	7,203
Other liabilities, including inter-segment liabilities	6,149	293	(224)	9,607	15,825
Segment liabilities	213,809	293	20,767	10,185	245,054
Unallocated liabilities					
Central borrowings (see below)					3,810
Tax liabilities					3,491
Total liabilities					252,355
Total equity					11,092
Total equity and liabilities					263,447
Capital expenditure (excluding business combinations)					
Intangible assets	44	–	6	2	52
Property and equipment	26	3	11	166	206
	70	3	17	168	258

Central borrowings are borrowings by holding companies within the Group which are not allocated to operating companies.

(b) Secondary reporting format – geographical segments

(i) Reporting segments

Although the Group's business segments are managed on a worldwide basis, they operate in six main geographical areas. These are United Kingdom (UK), France, Netherlands (including Belgium, Germany and Luxembourg), Other Europe, United States and Rest of the World.

At a country level, certain classifications in 2005 have changed. Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland, and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the UK.

Revenue by destination does not differ materially from revenue by geographical origin, as most risks are located in the countries where the contracts were written.

4 – Segmental information continued**(ii) Segmental results and balance sheets – geographical segment**

Year ended 31 December 2006	United Kingdom £m	France £m	Netherlands £m	Other Europe £m	United States £m	Rest of the World £m	Total £m
Gross written premiums	12,276	4,376	3,956	5,118	959	2,050	28,735
Premiums ceded to reinsurers	(1,012)	(65)	(119)	(179)	(27)	(99)	(1,501)
Internal reinsurance revenue	(24)	(3)	(4)	(4)	–	35	–
Net written premiums	11,240	4,308	3,833	4,935	932	1,986	27,234
Net change in provision for unearned premiums	130	(5)	(3)	(15)	–	(14)	93
Net earned premiums	11,370	4,303	3,830	4,920	932	1,972	27,327
Fee and commission income	929	224	239	317	4	157	1,870
	12,299	4,527	4,069	5,237	936	2,129	29,197
Other income	10,303	1,873	1,459	1,643	377	239	15,894
Segment income	22,602	6,400	5,528	6,880	1,313	2,368	45,091
Segmental result before tax	1,286	425	417	668	14	743	3,553
Segment assets	141,597	48,328	40,059	34,889	18,519	7,787	291,179
Unallocated assets – tax assets							1,543
Total assets							292,722
Segment liabilities	137,424	46,770	36,542	31,190	16,411	1,787	270,124
Unallocated liabilities – central borrowings and tax liabilities							8,534
Total liabilities							278,658
Capital expenditure (excluding business combinations)	273	4	43	32	23	10	385

Year ended 31 December 2005	United Kingdom £m	France £m	Netherlands £m	Other Europe £m	United States £m	Rest of the World £m	Total £m
Gross written premiums	11,510	4,250	3,878	4,316	522	1,823	26,299
Premiums ceded to reinsurers	(914)	35	(22)	(306)	(5)	(105)	(1,317)
Internal reinsurance revenue	(10)	(6)	(4)	(1)	–	21	–
Net written premiums	10,586	4,279	3,852	4,009	517	1,739	24,982
Net change in provision for unearned premiums	(115)	(10)	6	23	–	(27)	(123)
Net earned premiums	10,471	4,269	3,858	4,032	517	1,712	24,859
Fee and commission income	1,002	200	192	239	–	218	1,851
	11,473	4,469	4,050	4,271	517	1,930	26,710
Other income	15,762	3,063	2,277	1,954	–	931	23,987
Segment income	27,235	7,532	6,327	6,225	517	2,861	50,697
Segmental result before tax	2,293	307	357	461	(4)	284	3,698
Segment assets	136,235	46,682	38,871	29,868	3,866	6,820	262,342
Unallocated assets – tax assets							1,105
Total assets							263,447
Segment liabilities	128,887	44,284	35,727	26,439	3,501	6,216	245,054
Unallocated liabilities – central borrowings and tax liabilities							7,301
Total liabilities							252,355
Capital expenditure (excluding business combinations)	167	5	31	32	–	23	258

Notes to the consolidated financial statements continued

4 – Segmental information continued**(iii) Life and pensions and investment sales – new business and total income**

For the purpose of recording life and pensions new business premiums, the Group's policy is to include life insurance, long-term health and accident insurance, savings, pensions and annuity business written by our life insurance subsidiaries, including managed pension fund business and our share of the other life and related business written in our associates and joint ventures, as well as the lifetime mortgage business written in the UK. This includes both insurance and investment contracts as defined under IFRS 4, *Insurance Contracts*, and is consistent with the definition of covered business used for our supplementary embedded value reporting.

An analysis of new long-term business sales is provided below. In this table, single premiums are those relating to products issued by the Group which provide for the payment of one premium only. Regular premiums are those where there is a contractual obligation to pay on an ongoing basis. Life and pensions total income represents all net written premiums in the year for insurance contracts and investment contracts, excluding non-participating investment contracts which are required to be accounted for under IAS 39, *Financial Instruments: Recognition and Measurement*, and IAS 18, *Revenue*.

	New single premiums		New regular premiums		Total income	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m
Life and pensions:						
United Kingdom – Group companies	7,617	6,204	549	456	5,300	4,459
– associates and joint ventures	695	501	59	29	236	217
	8,312	6,705	608	485	5,536	4,676
France	3,090	3,077	82	76	3,573	3,553
Netherlands	1,224	1,441	148	179	2,079	2,582
Other Europe						
Ireland	809	372	109	63	397	182
Italy	2,216	1,940	101	58	1,919	1,357
Poland	238	120	48	34	395	312
Spain	1,410	1,395	107	100	1,266	1,248
Other	83	78	55	43	159	152
United States	767	448	20	20	931	517
Rest of the World	490	350	116	93	582	353
Total life and pensions (including share of associates and joint ventures)	18,639	15,926	1,394	1,151	16,837	14,932
Retail sales of mutual fund type products:						
United Kingdom	2,411	1,139	44	21	2,455	1,160
Netherlands	285	563	–	–	285	563
Other Europe						
Poland	127	49	4	4	131	53
Other	475	410	–	–	475	410
Rest of the World	1,564	1,151	–	–	1,564	1,151
Total investment sales	4,862	3,312	48	25	4,910	3,337
Total long-term savings (including share of associates and joint ventures)	23,501	19,238	1,442	1,176	21,747	18,269

Included within new business sales is £6,365 million of single premiums and £615 million of regular premiums (2005: £5,071 million and £357 million respectively) in respect of contracts that meet the definition of "non-participating investment" contracts under IFRS 4, *Insurance Contracts*. Under IFRS, the premiums on these contracts are not included in the Group income statement under earned premiums, but are included on the balance sheet as a deposit.

Sales from the Navigator funds administration business, previously excluded from investment sales figures, are now included in the new single premiums figures above. This change has increased total investment sales for 2006 by £1,371 million (2005: £938 million).

5 – Details of income

	2006 £m	2005 £m
Gross written premiums (note 4a)		
Long-term:		
Insurance contracts	13,188	9,916
Participating investment contracts	4,120	5,366
General insurance and health	11,427	11,017
	28,735	26,299
Less: premiums ceded to reinsurers (note 4a)	(1,501)	(1,317)
Gross change in provision for unearned premiums (note 35e)	89	(216)
Reinsurers' share of change in provision for unearned premiums (note 36c)	4	93
Net change in provision for unearned premiums	93	(123)
Net earned premiums	27,327	24,859
Fee and commission income		
Fee income from investment contract business	410	288
Fund management fee income	395	274
Other fee income	779	925
Reinsurance commissions receivable	204	274
Other commission income	98	99
Net change in deferred revenue	(16)	(9)
	1,870	1,851
Total revenue	29,197	26,710
Net investment income		
Interest and similar income		
From financial instruments designated as trading and other than trading	5,444	5,500
From AFS investments and financial instruments at amortised cost	951	896
	6,395	6,396
Dividend income	2,115	1,778
Other income from investments designated as trading		
Realised gains and losses	124	(78)
Unrealised gains and losses	208	42
	332	(36)
Other income from investments designated as other than trading		
Realised gains and losses	4,989	4,502
Unrealised gains and losses	(998)	8,771
	3,991	13,273
Realised gains on AFS investments	162	154
Net income from investment properties:		
Rent	757	747
Expenses relating to these properties	(27)	(19)
Realised gains on disposal	46	41
Fair value gains on investment properties	1,507	1,571
Realised gains on loans	59	38
Foreign exchange gains and losses on investments other than trading	128	(207)
Other investment income/(expenses)	8	(14)
Net investment income	15,473	23,722
Share of profit after tax of joint ventures (note 17)	462	326
Share of profit after tax of associates (note 18)	23	14
Share of profit after tax of joint ventures and associates	485	340
Profit on disposal of subsidiaries and associates (note 3b)	222	153
Total income	45,377	50,925

Notes to the consolidated financial statements continued

6 – Details of expenses

	2006 £m	2005 £m
Claims and benefits paid		
Claims and benefits paid to policyholders on long term-business		
Insurance contracts	12,460	10,325
Participating investment contracts	4,350	2,465
Non-participating investment contracts	428	1,188
Claims and benefits paid to policyholders on general insurance and health business	7,232	6,523
	24,470	20,501
Less: Claim recoveries from reinsurers		
Insurance contracts	(1,009)	(697)
Participating investment contracts	(17)	(50)
Non-participating investment contracts	–	(48)
Claims and benefits paid, net of recoveries from reinsurers	23,444	19,706
Change in insurance liabilities		
Change in insurance liabilities	1,649	9,673
Change in reinsurance asset for insurance provisions	971	703
Change in insurance liabilities, net of reinsurance	2,620	10,376
Change in investment contract provisions		
Investment income allocated to investment contracts	3,122	3,633
Other changes in provisions		
Participating investment contracts	2,683	3,530
Non-participating investment contracts	198	69
Change in reinsurance asset for investment contract provisions	(1)	582
	6,002	7,814
Change in unallocated divisible surplus	558	1,474
Fee and commission expense		
Acquisition costs		
Commission expenses for insurance and participating investment contracts	2,919	2,700
Change in deferred acquisition costs for insurance and participating investment contracts	210	(208)
Deferrable costs for non-participating investment contracts	230	165
Other acquisition costs	1,376	1,245
Change in deferred acquisition costs for non-participating investment contracts	(159)	(258)
Reinsurance commissions and other fee and commission expense	467	686
	5,043	4,330

6 – Details of expenses continued

	2006 £m	2005 £m
Other expenses		
Other operating expenses		
Staff costs and other expenses	2,750	2,613
Central costs and sharesave schemes	160	108
Global finance transformation programme	–	28
Corporate costs	160	136
Depreciation (note 19)	122	112
Impairment of goodwill on subsidiaries (note 15)	94	43
Amortisation of acquired value of in-force business (note 16)	58	26
Amortisation of intangible assets (note 16)	72	39
Net impairment of acquired value of in-force business (note 16)	28	29
(Reversal of impairment)/impairment of intangible assets (note 16)	(2)	6
Integration and restructuring costs (note 3c)	246	109
	3,528	3,113
Impairments		
Net (reversal of impairment)/impairment on loans	(4)	4
Net (reversal of impairment)/impairment on financial investments	(1)	5
Net impairment on receivables and other financial assets	5	10
Net impairment on non-financial assets	–	38
	–	57
Other net foreign exchange losses/(gains)	29	(4)
	3,557	3,166
Finance costs		
Interest expense on:		
Subordinated debt	169	169
Debenture loans	29	41
Amounts owed to credit institutions	169	37
Commercial paper	29	24
Securitised mortgage loan notes		
At fair value	94	82
At amortised cost	197	101
	291	183
Banking customer deposits	95	79
	782	533
Other similar charges	48	76
	830	609
Total expenses	42,054	47,475

Notes to the consolidated financial statements continued

7 – Analysis of net investment return

The total investment return reflected in profit before tax comprises:

	2006 £m	2005 £m
Share of results after tax of joint ventures	462	326
Share of results after tax of associates	37	32
Net rental income from investment properties	730	728
Interest, dividend and similar income	8,510	8,174
Foreign exchange gains and losses on investments designated as at fair value through profit or loss	128	(207)
Realised investment gains on financial investments, loans, investment property and owner occupied property	5,380	4,657
Net impairment losses on investments designated as available for sale and on loans	–	(57)
Other investment income/(expenses)	8	(14)
Finance costs		
Allocated costs	(600)	(361)
Unallocated interest charges:		
Subordinated debt	(169)	(169)
Other borrowings	(61)	(79)
	(230)	(248)
Net investment return before unrealised gains	14,425	13,030
Unrealised investment gains on financial investments and loans designated as at fair value through profit or loss	717	10,384
Total net investment return included in profit before tax	15,142	23,414

In addition to the investment return recognised above, £347 million of investment gains (2005: losses of £110 million) have been recognised directly in equity as detailed in the statement of recognised income and expense.

8 – Longer term investment return

(a) The longer term investment return, net of expenses, attributable to the general insurance and health business result was £1,073 million (2005: £1,046 million).

(b) The longer term investment return and short-term fluctuation are as follows:

	General insurance and health business	
	2006 £m	2005 £m
Net investment income (note 4a(ii))	1,299	1,603
Less: Internal charges included under other headings	(77)	(40)
	1,222	1,563
Longer term investment return	1,073	1,046
Short-term fluctuation in investment return	149	517
	1,222	1,563

(c) The longer term investment return is calculated separately for each principal general insurance and health business unit. In respect of equities and properties, the return is calculated by multiplying the opening market value of the investments, adjusted for sales and purchases during the year, by the longer term rate of investment return. The longer term rate of investment return is determined using consistent assumptions between operations, having regard to local economic and market forecasts of investment return. The allocated longer term return for other investments is the actual income receivable for the year.

(d) The principal assumptions underlying the calculation of the longer term investment return are:

	Longer term rates of return Equities		Longer term rates of return Properties	
	2006 %	2005 %	2006 %	2005 %
United Kingdom	7.1	7.6	6.1	6.6
France	6.3	6.7	5.3	5.7
Ireland	6.3	6.7	5.3	5.7
Netherlands	6.3	6.7	5.3	5.7
Canada	7.0	7.4	6.0	6.4

The Group has applied the same economic assumptions for equities and properties as are used under EEV principles to calculate the longer term investment return for its general insurance and health business.

8 – Longer term investment return continued

(e) The table below compares the actual return on investments attributable to the general insurance and health business, after deducting investment management expenses and charges, with the aggregate longer term return over a three year period. This table will be built up over time to give aggregate and comparative figures over a five year period.

	2004 – 2006 £m
Actual return attributable to shareholders	3,934
Longer term return credited to operating results	(3,107)
Excess of actual returns over longer term returns	827

(f) The table below shows the sensitivity of the Group's general insurance and health operating profit before tax to changes in the longer term rates of return:

Movement in investment return for	By	Change in	2006 £m	2005 £m
Equities	1% higher/lower	Group operating profit before tax	31	29
Properties	1% higher/lower	Group operating profit before tax	4	4

9 – Employee information

The average number of persons employed by the Group during the year was:

	2006 Number	2005 Number
United Kingdom	35,701	33,827
France	4,303	4,351
Netherlands	6,447	6,338
Other Europe	6,091	5,667
United States	531	379
Rest of the World	4,946	4,229
	58,019	54,791

Total staff costs were:

	2006 £m	2005 £m
Wages and salaries	1,798	1,677
Social security costs	216	210
Post-retirement obligations		
Defined benefit schemes (note 42c)	213	158
Defined contribution schemes (note 42c)	71	47
Profit sharing and incentive plans	148	116
Equity compensation plans (notes 28d & 32b)	48	22
Termination benefits	31	10
	2,525	2,240

These costs are charged within:

	2006 £m	2005 £m
Acquisition costs	597	600
Claims handling expenses	253	221
Corporate costs	76	62
Other operating expenses	1,599	1,357
	2,525	2,240

Notes to the consolidated financial statements continued

10 – Directors

Information concerning individual directors' emoluments, interests and transactions is given in the Directors' remuneration report.

11 – Auditors' remuneration

The total remuneration payable by the Group, excluding VAT and any overseas equivalent thereof, to its principal auditors, Ernst & Young LLP, and its associates in respect of the audit of these financial statements is shown below, together with fees payable in respect of other work.

	2006 £000	2005 £000
Fees payable to Ernst & Young LLP for the statutory audit of the Aviva Group and Company financial statements	1,452	1,525
Fees payable to Ernst & Young LLP and its associates for other services to Group companies:		
Audit of Group subsidiaries pursuant to legislation	7,507	7,453
Other services pursuant to legislation	2,326	1,834
Tax services	187	114
Services relating to information technology	40	177
Services relating to corporate finance transactions	1,432	762
All other services – Supplementary reporting (see below)	885	862
– Other supplementary services	1,660	995
Fees payable to Ernst & Young LLP for services to Group pension schemes		
Audit of Group pension scheme	70	49
	15,559	13,771

In addition to the above amounts payable to the principal auditors, fees for audit services of £2.1 million (2005: £2.8 million) were payable to other firms. The total fees payable for audit services were therefore £11.1 million (2005: £11.8 million).

Fees for supplementary reporting are in respect of the audit of the Group's EEV figures. Although EEV is the Group's primary management reporting basis and our disclosures require a full audit, the relevant fees are not classified as being for statutory audit.

12 – Tax**(a) Tax charged to the income statement****(i) The total tax charge comprises:**

	2006 £m	2005 £m
Current tax		
For this year	1,022	799
Prior year adjustments	(287)	(212)
Total current tax	735	587
Deferred tax		
Origination and reversal of timing differences	221	881
Changes in tax rates or tax laws	(7)	(5)
Write-down of deferred tax assets	(15)	89
Total deferred tax	199	965
Total tax charged to income statement (note 12c)	934	1,552

(ii) The Group, as a proxy for policyholders in the UK, Ireland and Australia, is required to record taxes on investment income and gains each year. Accordingly, the tax benefit or expense attributable to UK, Irish and Australian life insurance policyholder returns is included in the tax charge. The tax expense attributable to policyholders' returns included in the charge above is £346 million (2005: £922 million).

12 – Tax continued

(iii) The tax charge can be analysed as follows:

	2006 £m	2005 £m
UK tax	479	1,150
Overseas tax	455	402
	934	1,552

(iv) Unrecognised tax losses and temporary differences of previous years were used to reduce current tax expense and deferred tax expense by £73 million and £24 million, respectively (2005: £49 million and £33 million, respectively).

(v) Deferred tax charged to the income statement represents movements on the following items:

	2006 £m	2005 £m
Long-term business technical provisions and other insurance items	364	(107)
Deferred acquisition costs	(47)	56
Unrealised (gains)/losses on investments	(144)	562
Provisions and other temporary differences	(192)	35
Impairment of assets	1	(1)
Pensions and other post-retirement obligations	166	19
Unused losses and tax credits	(247)	247
Other temporary differences	298	154
Total deferred tax charged to income statement	199	965

(b) Tax charged/(credited) to equity

(i) The total tax charge/(credit) comprises:

	2006 £m	2005 £m
Current tax	(9)	(13)
Deferred tax	14	(262)
Total tax charged/(credited) to equity	5	(275)

Deferred tax charged to equity includes £29 million credit (2005: £213 million credit) in respect of pensions and other post-retirement obligations, and a deferred tax charge of £43 million (2005: £49 million credit) in respect of unrealised gains on investments.

(ii) The tax credit attributable to policyholders' returns included in the credit above is £nil (2005: £3 million).

(c) Tax reconciliation

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the tax rate of the home country of the Company as follows:

	2006 £m	2005 £m
Profit before tax	3,323	3,450
Tax calculated at standard UK corporation tax rate of 30% (2005: 30%)	997	1,035
Different basis of tax for UK life insurance	209	616
Adjustment to tax charge in respect of prior years	(287)	(253)
Non-assessable dividends	(55)	(26)
Non-taxable profit on sale of subsidiaries and associates	(80)	(4)
Disallowable expenses	46	55
Different local basis of tax on overseas profits	201	168
Deferred tax assets not recognised	(60)	(25)
Other	(37)	(14)
Total tax charge to income statement (note 12a)	934	1,552

Notes to the consolidated financial statements continued

13 – Earnings per share**(a) Basic earnings per share****(i)** The profit attributable to ordinary shareholders is:

	2006			2005		
	Operating profit £m	Adjusting items £m	Total £m	Operating profit £m	Adjusting items £m	Total £m
Profit before tax	3,110	(133)	2,977	2,128	400	2,528
Tax attributable to shareholders' profits	(725)	137	(588)	(536)	(94)	(630)
Profit for the year	2,385	4	2,389	1,592	306	1,898
Minority interests	(185)	11	(174)	(131)	–	(131)
Preference dividends	(17)	–	(17)	(17)	–	(17)
Coupon payments in respect of direct capital instrument (net of tax)	(37)	–	(37)	(29)	–	(29)
Profit attributable to ordinary shareholders	2,146	15	2,161	1,415	306	1,721

(ii) Basic earnings per share is calculated as follows:

	2006			2005		
	Before tax £m	Net of tax, minorities, preference dividends and DCI £m	Per share p	Before tax £m	Net of tax, minorities, preference dividends and DCI £m	Per share p
Operating profit attributable to ordinary shareholders	3,110	2,146	86.9	2,128	1,415	60.5
Non-operating items:						
– impairment of goodwill (note 15)	(94)	(94)	(3.8)	(43)	(43)	(1.8)
– Amortisation and net impairment of acquired additional value of in-force business (note 16 & 18)	(100)	(83)	(3.4)	(73)	(73)	(3.1)
– Amortisation and net impairment of intangibles (note 16)	(70)	(48)	(1.9)	(45)	(42)	(1.8)
– Financial services compensation scheme and other levies	6	4	0.2	–	–	–
– Short-term fluctuation in return on investments backing general insurance and health business (note 8b)	149	189	7.7	517	430	18.2
– Profit on the disposal of subsidiary and associates (note 3b)	222	235	9.5	153	110	4.7
– Integration and restructuring costs (note 3c)	(246)	(188)	(7.7)	(109)	(76)	(3.2)
Profit attributable to ordinary shareholders	2,977	2,161	87.5	2,528	1,721	73.5

Earnings per share has been calculated based on the operating profit before impairment of goodwill and other non-operating items, after tax, attributable to ordinary shareholders, 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.

(iii) The calculation of basic earnings per share uses a weighted average of 2,469 million (2005: 2,340 million) ordinary shares in issue, after deducting shares owned by the employee share trusts. The actual number of shares in issue at 31 December 2006 was 2,566 million (2005: 2,396 million).

13 – Earnings per share continued**(b) Diluted earnings per share**

Diluted earnings per share is calculated as follows:

	2006			2005		
	Total £m	Weighted average number of shares m	Per share p	Total £m	Weighted average number of shares m	Per share p
Profit attributable to ordinary shareholders	2,161	2,469	87.5	1,721	2,340	73.5
Dilutive effect of share awards and options	–	27	(0.9)	–	20	(0.6)
Diluted earnings per share	2,161	2,496	86.6	1,721	2,360	72.9

Diluted earnings per share on operating profit attributable to ordinary shareholders is 86.0 pence (2005: 60.0 pence).

14 – Dividends and appropriations

	2006 £m	2005 £m
Ordinary dividends declared and charged to equity in the year		
Final 2004 – 16.00 pence per share, paid on 17 May 2005	–	364
Interim 2005 – 9.83 pence per share, paid on 17 November 2005	–	234
Final 2005 – 17.44 pence per share, paid on 17 May 2006	418	–
Interim 2006 – 10.82 pence per share, paid on 17 November 2006	275	–
	693	598
Preference dividends declared and charged to equity in the year	17	17
Coupon payments on direct capital instrument	52	42
	762	657

Subsequent to 31 December 2006, the directors proposed a final dividend for 2006 of 19.18 pence per ordinary share, £492 million in total, making a total dividend for the year of 30.00 pence (2005: 27.27 pence). Subject to approval by shareholders at the AGM, the dividend will be paid on 17 May 2007 and will be accounted for as an appropriation of retained earnings in the year ending 31 December 2007.

Interest on the direct capital instrument issued in November 2004 is treated as an appropriation of retained profits and, accordingly, it is accounted for when paid. Tax relief is obtained at a rate of 30%.

Irish shareholders who are due to be paid a dividend denominated in euros will receive a payment at the exchange rate prevailing on 28 February 2007.

Notes to the consolidated financial statements continued

15 – Goodwill**(a) Carrying amount**

	2006 £m	2005 £m
Gross amount		
At 1 January	2,359	1,225
Acquisitions	761	1,074
Additions	32	104
Disposals	(8)	(21)
Foreign exchange rate movements	(58)	(23)
At 31 December	3,086	2,359
Accumulated impairment		
At 1 January	(85)	(41)
Impairment losses	(94)	(43)
Foreign exchange rate movements	3	(1)
At 31 December	(176)	(85)
Carrying amount at 31 December	2,910	2,274

Goodwill additions relate to contingent consideration paid in respect of past acquisitions of subsidiaries. Goodwill arising on acquisitions completed before 1 January 1998 was charged directly to reserves. Goodwill arising on the Group's investment in joint ventures and associates is included within the carrying value of those investments (see notes 17 and 18).

(b) Goodwill allocation and impairment testing

A summary of the goodwill and intangibles with indefinite useful lives allocated to cash-generating units is presented below.

	UK (General insurance and health)		RAC (non-insurance operations)		Spain (Long-term business)		United States (Long-term business)		Other		Total	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m
Carrying amount of goodwill	314	311	892	892	518	503	635	–	551	568	2,910	2,274
Carrying amount of intangibles with indefinite useful lives	185	185	36	75	–	–	–	–	42	42	263	302
	499	496	928	967	518	503	635	–	593	610	3,173	2,576

As explained in accounting policy M, the carrying amount of goodwill and intangible assets with indefinite useful lives is reviewed at least annually or when circumstances or events indicate there may be uncertainty over this value. The tests led to impairment of goodwill of £94 million.

Goodwill and intangibles with indefinite useful lives have been tested for impairment in these businesses as follows:

UK (general insurance and health)

The recoverable amount of the UK general insurance and health unit has also been determined based on a value in use calculation. The calculation uses cash flow projections based on business plans approved by management covering a three year period and a risk adjusted discount rate of 10.45% (2005: 10.45%). Cash flows beyond that three year period have been extrapolated using a steady 3% growth rate (2005: 3%). The recoverable amount significantly exceeds the carrying value of the cash generating unit including goodwill and intangible assets with indefinite useful lives and a reasonably possible change in a key assumption will not cause the carrying value of the cash generating unit to exceed its recoverable amount.

Key assumptions used for the calculation were:

- Budgeted operating profit represents the operating profit in the business plans, approved by management and as such reflects the best estimate of future profits based on both historical experience and expected growth rates for the UK general insurance industry. Some of the assumptions that underlie the budgeted operating profit include market share, premium rate changes, claims inflation and commission rates.
- Growth rate represents the rate used to extrapolate future cash flows beyond the business plan period and has been based upon latest information available regarding future and past growth rates. The growth rate is considered to be consistent with both past experience and external sources of data (ABI Annual Market Statistics).

15 – Goodwill continued

RAC (non-insurance operations)

The recoverable amount of the RAC (non-insurance operations) has also been determined based on a value in use calculation. The calculation uses cash flow projections based on business plans approved by management covering a three year period and a risk adjusted discount rate of 10.27% (2005: 10.45%). Cash flows beyond that three year period have been extrapolated using a steady 2% growth rate. The recoverable amount significantly exceeds the carrying value of the cash generating unit including goodwill and intangible assets with indefinite useful lives and a reasonably possible change in a key assumption will not cause the carrying value of the cash generating unit to exceed its recoverable amount.

Key assumptions used for the calculation were:

- Budgeted operating profit represents the operating profit in the business plans, approved by management and as such reflects the best estimate of future profits based on both historical experience and expected growth. Some of the assumptions that underlie the budgeted operating profit include market share, fee income and customer numbers.

Spain (long-term business)

The recoverable amount of the Spanish unit has been determined based on a fair value less costs to sell calculation. This calculation is an actuarially-determined appraisal value and is based on the embedded value of the business together with the present value of expected profits from future new business. The recoverable amount significantly exceeds the carrying value of the cash generating unit including goodwill and a reasonably possible change in a key assumption will not cause the carrying value of the cash generating unit to exceed its recoverable amount.

Key assumptions used for the calculation were:

- Embedded value represents the shareholder interest in the life business and is calculated in accordance with the European Embedded Value (EEV) principles. The embedded value is the total of the net worth of the life business and the value of the in-force business. The underlying methodology and assumptions have been reviewed by a firm of actuarial consultants and by the Group's auditors;
- New business contribution represents the present value of projected future distributable profits generated from business written in a period. This is based on business plans approved by management;
- Growth rate represents the rate used to extrapolate new business contributions beyond the business plan period, and is based on management's best estimate of future growth. The rate is in line with industry expectations; and
- Risk adjusted discount rate represents the rate used to discount expected profits from future new business. The discount rate is a combination of a risk-free rate and a risk margin to make prudent allowance for the risk that experience in future years may differ from that assumed.

United States (long-term business)

The carrying value of the Group's cash-generating unit in the United States is principally represented by the former operations of AmerUs Group Co. (AmerUs), which was acquired by the Group on 15 November 2006. The unit's current business plan is consistent with the assumptions made at the time of the acquisition in determining the appraisal value of AmerUs, which was in excess of its current carrying value. Since the acquisition date, the assets and liabilities making up the unit have not changed significantly, and there have been no other events which might have materially affected the recoverable amount of the unit.

Other

During the year, goodwill allocated to a long-term business cash-generating unit in Germany, Berlinische, was tested for impairment. Following the impairment test, an impairment charge of £94 million has been recognised in the income statement. The impairment charge arose as a result of the fall off in contribution from new business in 2006 and current adverse experience within the in-force portfolio.

Notes to the consolidated financial statements continued

16 – Acquired value of in-force business (AVIF) and intangible assets

	AVIF £m	Intangible assets with indefinite useful lives £m	Intangible assets with finite useful lives £m	Total £m
Gross amount				
At 1 January 2005	613	44	189	846
Additions	13	–	60	73
Acquisition of subsidiaries	–	260	73	333
Foreign exchange rate movements	(12)	(2)	1	(13)
At 31 December 2005	614	302	323	1,239
Additions	22	–	58	80
Acquisition of subsidiaries	1,642	–	470	2,112
Disposals	–	–	(14)	(14)
Transfers	–	(39)	39	–
Foreign exchange rate movements	(93)	–	(23)	(116)
At 31 December 2006	2,185	263	853	3,301
Accumulated amortisation				
At 1 January 2005	(248)	–	(82)	(330)
Amortisation for the year	(26)	–	(39)	(65)
Impairment losses recognised	(29)	–	(6)	(35)
Foreign exchange rate movements	4	–	(1)	3
At 31 December 2005	(299)	–	(128)	(427)
Amortisation for the year	(58)	–	(72)	(130)
Disposals	–	–	1	1
Impairment losses recognised	(28)	–	2	(26)
Foreign exchange rate movements	6	–	3	9
At 31 December 2006	(379)	–	(194)	(573)
Carrying amount				
At 31 December 2005	315	302	195	812
Less: Amounts classified as held for sale	–	–	(9)	(9)
	315	302	186	803
At 31 December 2006	1,806	263	659	2,728

Additions to gross AVIF includes £20 million for the movement in the shadow adjustment made to the carrying value of the AVIF in Aviva USA.

Intangible assets with indefinite useful lives comprise the RAC and BSM brands, and the value of the Union Financière de France Banque sales force, where the existing lives of the assets and their competitive position in, and the stability of, their respective markets support this classification. Impairment testing on intangibles is covered in note 15(b).

17 – Investments in joint ventures**(a) Carrying amount**

	Goodwill and intangibles £m	Equity interests £m	Loans £m	Total £m
At 1 January 2005	–	1,255	–	1,255
Share of results before tax	–	332	–	332
Share of tax	–	(6)	–	(6)
Share of profit after tax	–	326	–	326
Acquisitions and additions	167	587	–	754
Disposals and reduction in Group interests	–	(43)	–	(43)
Reclassification to subsidiaries	–	(8)	–	(8)
Dividends received	–	(34)	–	(34)
Additional loans	–	–	128	128
Foreign exchange rate movements	–	1	–	1
Other movements and reclassifications as held for sale	(167)	(83)	–	(250)
Movements in carrying amount	–	746	128	874
At 31 December 2005	–	2,001	128	2,129
Share of results before tax	–	465	–	465
Share of tax	–	(3)	–	(3)
Share of profit after tax	–	462	–	462
Acquisitions and additions	–	372	–	372
Disposals and reduction in Group interests	–	(127)	–	(127)
Reclassification to subsidiaries	–	(93)	–	(93)
Dividends received	–	(59)	–	(59)
Additional loans	–	–	113	113
Foreign exchange rate movements	–	(2)	–	(2)
Movements in carrying amount	–	553	113	666
At 31 December 2006	–	2,554	241	2,795

The loans are not secured and no guarantees were received in respect thereof. They are interest-bearing and are repayable on termination of the relevant partnership.

(b) Property management undertakings

(i) As part of their investment strategy, the UK and certain European long-term business policyholder funds have invested in a number of property limited partnerships (PLPs), either directly or via property unit trusts (PUTs), through a mix of capital and loans. The PLPs are managed by general partners (GPs), in which the long-term business shareholder companies hold equity stakes and which themselves hold nominal stakes in the PLPs. The PUTs are managed by a Group subsidiary.

Most of the PLPs have raised external debt, secured on their respective property portfolios. The lenders are only entitled to obtain payment, of both interest and principal, to the extent that there are sufficient resources in the respective PLPs. The lenders have no recourse whatsoever to the policyholder or shareholders' funds of any company in the Aviva Group.

Accounting for the PUTs and PLPs as subsidiaries, joint ventures or other financial investments depends on the shareholdings in the GPs and the terms of each partnership agreement. Where the Group exerts control over a PLP, it has been treated as a subsidiary and its results, assets and liabilities have been consolidated. Where the partnership is managed by a contractual agreement such that no party exerts control, notwithstanding that the Group's partnership share in the PLP (including its indirect take via the relevant PUT and GP) may be greater than 50%, such PUTs and PLPs have been classified as jointly-controlled entities. These are accounted for as joint ventures, and are covered in this note. Where the Group holds minority stakes in PLPs, with no disproportionate influence, the relevant investments are included in financial investments at their fair value.

Notes to the consolidated financial statements continued

17 – Investments in joint ventures continued

(ii) The principal joint ventures are as follows:

Company	GP proportion held	PLP proportion held
Airport Property Partnership	50.0%	50.0%
Apia Regional Office Fund	50.0%	61.3%
Ashtenne Industrial Partnership	66.7%	38.8%
The Junction Limited Partnership	50.0%	46.0%
The Mall Limited Partnership	50.0%	33.5%
Queensgate Property Partnership Limited	50.0%	50.0%
Quercus Property Partnership Limited	50.0%	58.4%

All the above entities perform property ownership and management activities, and are incorporated and operate in Great Britain. All these investments are held by subsidiary entities.

(c) Other

The Group also has a 50% holding in AVIVA-COFCO Life Insurance Company Limited, a life assurance company incorporated and operating in China. These shares are held by the Company, with a share of net assets of £18 million (2005: £10 million) and a fair value of £35 million (2005: £22 million).

(d) Additional information

Summarised aggregate financial information on the Group's interests in its joint ventures is as follows:

	2006 £m	2005 £m
Income	510	394
Expenses	(45)	(62)
Share of results before tax	465	332
Long-term assets	4,273	3,333
Current assets	126	116
Share of total assets	4,399	3,449
Long-term liabilities	(1,695)	(1,311)
Current liabilities	(150)	(137)
Share of total liabilities	(1,845)	(1,448)
Share of net assets	2,554	2,001

The joint ventures have no significant contingent liabilities to which the Group is exposed, nor has the Group any significant contingent liabilities in relation to its interests in the joint ventures.

18 – Investments in associates**(a) Carrying amount**

	Goodwill £m	Equity interests £m	Loans £m	Total £m
At 1 January 2005	247	615	11	873
Share of results before tax	–	39	–	39
Share of tax	–	(7)	–	(7)
Share of results after tax	–	32	–	32
Amortisation of acquired value of in-force business	–	(18)	–	(18)
Share of profit after tax	–	14	–	14
Acquisitions and additions	5	65	–	70
Fair value (losses) taken to equity	–	(2)	–	(2)
Dividends received	–	(61)	–	(61)
Foreign exchange rate movements	–	(4)	–	(4)
Other movements and reclassifications as held for sale	–	(5)	–	(5)
Movements in carrying amount	5	7	–	12
At 31 December 2005	252	622	11	885
Share of results before tax	–	48	–	48
Share of tax	–	(11)	–	(11)
Share of results after tax	–	37	–	37
Amortisation of acquired value of in-force business	–	(14)	–	(14)
Share of profit after tax	–	23	–	23
Acquisitions and additions	28	10	–	38
Disposals	–	(26)	–	(26)
Dividends received	–	(12)	–	(12)
Foreign exchange rate movements	–	(4)	–	(4)
Loans repaid	–	–	(9)	(9)
Movements in carrying amount	28	(9)	(9)	10
At 31 December 2006	280	613	2	895

The loans are not secured and no guarantees were received in respect thereof, and bear interest at an annual rate of 4.2%.

Notes to the consolidated financial statements continued

18 – Investments in associates continued**(b) The principal associates included above are:**

Company	Type of business	Class of share	Proportion held	Country of incorporation and operation
Aviva Life Insurance Company India Pvt. Limited	Insurance	Ordinary Rs1 shares	26.0%	India
RBSG Collective Investments Limited	Investment	Ordinary £1 shares	49.99%	Great Britain
RBS Life Investments Limited	Insurance	Ordinary £1 shares	49.99%	Great Britain
The British Aviation Insurance Company Limited	Insurance	Ordinary £1 shares	38.1%	Great Britain

All investments in principal associates are unlisted and are held by subsidiaries.

In July 2006, our French operation, Aviva France, sold its holding in ProCapital SA, an online brokerage company, to Credit Mutuel for £98 million. The sale resulted in a profit on disposal of £79 million (see note 3b).

(c) Additional information

Summarised aggregate financial information on the Group's interests in its associates is as follows:

	2006 £m	2005 £m
Share of revenues	427	277
Share of results before tax	48	39
Share of assets	3,111	2,897
Share of liabilities	(2,498)	(2,275)
Share of net assets	613	622

The associates have no significant contingent liabilities to which the Group is exposed, nor has the Group any significant contingent liabilities in relation to its interest in the associates.

(d) Impairment testing

The Group's investments in RBS Life Investments Limited and RBSG Collective Investments Limited have been tested for impairment by comparing their carrying values (which include goodwill which arose on their acquisition) with their recoverable amounts. The recoverable amounts for both the investments have been determined based on value in use calculations. The calculations use cash flow projections based on business plans approved by management covering a five year period and a risk adjusted discount rate of 6.8%. Cash flows beyond that five year period have been extrapolated using a growth rate of 4.5%. The recoverable amounts significantly exceed the carrying values of both the investments and a reasonably possible change to the key underlying assumptions will not cause the carrying values of the investments to exceed their recoverable amounts.

19 – Property and equipment

	Properties under construction £m	Owner- occupied properties £m	Motor vehicles £m	Computer equipment £m	Other assets £m	Total £m
Cost or valuation						
At 1 January 2005	57	441	27	582	327	1,434
Additions	10	2	18	106	63	199
Capitalised expenditure on existing assets	7	–	–	–	–	7
Acquisitions of subsidiaries	–	35	44	9	49	137
Disposals	(19)	(7)	–	(42)	(70)	(138)
Fair value gains (see note 32b)	–	32	–	–	–	32
Foreign exchange rate movements	(1)	(4)	–	–	(1)	(6)
At 31 December 2005	54	499	89	655	368	1,665
Additions	31	43	1	154	66	295
Acquisitions of subsidiaries	–	6	1	2	2	11
Disposals	–	(78)	(78)	(99)	(72)	(327)
Transfers to investment property	–	(6)	–	–	–	(6)
Transfers	(19)	19	–	–	–	–
Reversal of impairment losses (see note 32b)	–	(2)	–	–	–	(2)
Fair value gains (see note 32b)	–	26	–	–	–	26
Foreign exchange rate movements	(1)	(8)	–	(10)	(5)	(24)
At 31 December 2006	65	499	13	702	359	1,638
Depreciation						
At 1 January 2005	–	–	(17)	(387)	(218)	(622)
Charge for the year	–	–	(4)	(77)	(31)	(112)
Disposals	–	–	–	26	12	38
Foreign exchange rate movements	–	–	–	1	–	1
At 31 December 2005	–	–	(21)	(437)	(237)	(695)
Charge for the year	–	–	(11)	(85)	(26)	(122)
Disposals	–	–	24	16	33	73
Foreign exchange rate movements	–	–	–	7	3	10
At 31 December 2006	–	–	(8)	(499)	(227)	(734)
Carrying amount						
At 31 December 2005	54	499	68	218	131	970
Less: Assets reclassified as available for sale	–	–	–	–	(85)	(85)
	54	499	68	218	46	885
At 31 December 2006	65	499	5	203	132	904

Owner-occupied properties are stated at their revalued amounts as assessed by qualified external valuers or by local qualified staff of the Group in overseas operations, all with recent relevant experience. Values are calculated on the basis of existing use, being the estimated arm's-length value at which the properties could be exchanged with vacant possession and without allowing for alternatives to their current use.

If owner-occupied properties were stated on a historical cost basis, the carrying amount would be £368 million (2005: £406 million).

The Group has no material finance leases for property and equipment.

Notes to the consolidated financial statements continued

20 – Investment property

	Freehold £m	Leasehold £m	Total £m
Carrying value			
At 1 January 2005	9,100	1,957	11,057
Additions	1,596	173	1,769
Capitalised expenditure on existing properties	126	61	187
Fair value gains	1,169	402	1,571
Disposals	(1,171)	(80)	(1,251)
Foreign exchange rate movements	(55)	(3)	(58)
At 31 December 2005	10,765	2,510	13,275
Additions	1,373	342	1,715
Capitalised expenditure on existing properties	125	48	173
Acquisitions of subsidiaries	35	–	35
Fair value gains	1,227	280	1,507
Disposals	(1,494)	(47)	(1,541)
Transfers from property and equipment	6	–	6
Foreign exchange rate movements	(41)	(6)	(47)
At 31 December 2006	11,996	3,127	15,123

Investment properties are stated at their market values as assessed by qualified external valuers or by local qualified staff of the Group in overseas operations, all with recent relevant experience. Values are calculated using a discounted cash flow approach and are based on current rental income plus anticipated uplifts at the next rent review, assuming no future growth in rental income. This uplift and the discount rate are derived from rates implied by recent market transactions on similar properties.

The fair value of investment properties leased to third-parties under operating leases was as follows:

	2006 £m	2005 £m
Freeholds	10,423	9,036
Long leaseholds – over 50 years	3,039	3,018
	13,462	12,054

21 – Loans**(a) Carrying amounts**

The carrying amounts of loans at 31 December 2006 and 2005 were as follows:

	2006 £m	2005 £m
Policy loans	1,217	1,020
Bank loans	170	125
Securitised mortgage loans (see note 22)	6,709	7,476
Non-securitised mortgage loans	15,185	15,224
Other loans	3,164	699
Total	26,445	24,544

Of the above loans, £23,243 million (2005: £23,031 million) is expected to be recovered more than one year after the balance sheet date.

The carrying amounts of the above loans are stated at amortised cost with the exception of £4,941 million (2005: £5,084 million) of securitised mortgage loans and £11,316 million (2005: £10,000 million) of non-securitised mortgage loans which are designated as other than trading and measured at fair value.

The fair value has been calculated by discounting the future cashflows using appropriate current interest rates for each portfolio of mortgages.

The change in fair value of these loans during the year, attributable to a change in credit risk, was £nil (2005: £nil). The cumulative change attributable to changes in credit risk to 31 December 2006 was £nil (2005: £nil).

(b) Collateral

The Group holds collateral in the form of liens or charges over properties and, in the case of policy loans, the underlying policy for the majority of the loan balances above. In the event of a default, the Group is able to sell or repledge the collateral. The Group did not hold any collateral which it was permitted to sell or repledge in the absence of default, at the end of either 2006 or 2005.

22 – Securitised mortgages and related assets

The Group has loans secured by mortgages, subject to non-recourse finance arrangements, in a UK long-term business subsidiary and in three Dutch subsidiaries. Details of the relevant transactions are as follows:

(a) UK

In a long-term business subsidiary (NUER), the beneficial interest in certain portfolios of lifetime mortgages has been transferred to five special purpose securitisation companies, Equity Release Funding (No 1) plc (ERF1), Equity Release Funding (No 2) plc (ERF2), Equity Release Funding (No 3) plc (ERF3), ERF Trustee (No 4) Limited (ERF4T) held on trust for the benefit of Equity Release Funding (No. 4) plc (ERF4), and ERF Trustee (No 5) Limited (ERF5T) held on trust for the benefit of Equity Release Funding (No. 5) plc (ERF5) (together “the ERF companies”), in return for initial consideration and, at later dates, deferred consideration. The deferred consideration represents receipts accrued within the ERF companies after meeting all their obligations to the noteholders, loan providers and other third-parties in the priority of payments. No gain or loss was recognised on the transfers to ERF1, ERF3 and ERF5T, and gains of £5 million and £9 million were recognised on the transfers to ERF2 and ERF4T respectively. The purchases of the mortgages were funded by the issue of fixed rate, floating rate and index-linked notes by the ERF companies.

All the shares in the ERF companies are held by independent companies, whose shares are held on trust. Although NUER does not own, directly or indirectly, any of the share capital of the ERF companies or their parent companies, these have been treated as subsidiaries in the consolidated financial statements. NUER has no right to repurchase the benefit of any of the securitised mortgage loans, other than in certain circumstances where NUER is in breach of warranty or loans are substituted in order to effect a further advance.

NUER has purchased subordinated notes and granted subordinated loans to some of the ERF companies. These have been eliminated on consolidation through offset against the borrowings of the ERF companies in the consolidated balance sheet.

(b) Netherlands and Belgium

In three subsidiaries, Delta Lloyd Levensverzekering NV (DLL), Amstelhuys NV (AMS), and Delta Lloyd Bank NV/SA (DLB), the principal benefits of certain portfolios of mortgage loans have been transferred to a number of special purpose securitisation companies, Arena 2000 – I BV, Arena 2001 – I BV, Arena 2002 – I BV, Arena 2003 – I BV, Arena 2004 – I BV, Arena 2004 – II BV, Arena 2005 – I BV, Arena 2006 – I BV, B-Arena NV/SA and DARTS Finance BV (the securitisation companies), which were funded primarily through the issue of fixed rate, floating rate and index-linked notes. No gains or losses were recognised on these transfers.

All the shares in the securitisation companies are held by independent trustee companies. Although DLL and AMS do not own, directly or indirectly, any of the share capital of the securitisation companies or their parent companies, these companies have been treated as subsidiaries in the consolidated financial statements. DLL, AMS and DLB have no right, nor any obligation, to repurchase the benefit of any of the securitised mortgage loans before the optional call date, other than in certain circumstances where they are in breach of warranty.

Delta Lloyd companies have purchased notes in the securitisation companies, which have been eliminated on consolidation through offset against the borrowings of the securitisation companies in the consolidated balance sheet.

(c) In all of the above transactions, the Company and its subsidiaries are not obliged to support any losses that may be suffered by the noteholders and do not intend to provide such support. Additionally, the notes were issued on the basis that noteholders are only entitled to obtain payment, of both principal and interest, to the extent that the available resources of the respective special purpose securitisation companies, including funds due from customers in respect of the securitised loans, are sufficient and that noteholders have no recourse whatsoever to other companies in the Aviva Group.

Notes to the consolidated financial statements continued

23 – Financial investments

(a) Financial investments comprise:

	2006			
	At fair value through profit or loss		Available for sale* £m	Total £m
	Trading £m	Other than trading £m		
Debt securities				
UK government	–	19,921	–	19,921
Non-UK government	7	19,388	434	19,829
Corporate – UK	19	12,230	80	12,329
Corporate – Non-UK	119	41,858	4,725	46,702
Other	–	6,544	7,716	14,260
	145	99,941	12,955	113,041
Equity securities				
Corporate – UK	–	30,580	140	30,720
Corporate – Non-UK	34	24,666	1,342	26,042
	34	55,246	1,482	56,762
Other investments				
Unit trusts and other specialised investment vehicles	5	28,860	147	29,012
Derivative financial instruments	1,325	–	–	1,325
Deposits with credit institutions	–	381	–	381
Minority holdings in property management undertakings (see note 17b)	–	542	–	542
Other	6	1,735	49	1,790
	1,336	31,518	196	33,050
Total financial investments	1,515	186,705	14,633	202,853

* The gain related to AFS investments recognised in equity was £347 million (2005: £110 million loss) and the amount recognised in the income statement on disposals was £162 million (2005: £154 million gain). (See notes 5 and 32b).

Of the above total, £115,004 million (2005: £19,509 million) is expected to be recovered more than one year after the balance sheet date.

	2005			
	At fair value through profit or loss		Available for sale* £m	Total £m
	Trading £m	Other than trading £m		
Debt securities				
UK government	–	22,845	–	22,845
Non-UK government	4	22,908	438	23,350
Corporate – UK	–	11,492	58	11,550
Corporate – Non-UK	81	31,345	5,237	36,663
Other	–	8,834	675	9,509
	85	97,424	6,408	103,917
Equity securities				
Corporate – UK	–	29,036	13	29,049
Corporate – Non-UK	58	21,610	1,327	22,995
	58	50,646	1,340	52,044
Other investments				
Unit trusts	4	24,202	3	24,209
Derivative financial instruments	467	–	–	467
Deposits with credit institutions	–	165	–	165
Minority holdings in property management undertakings (see note 17b)	–	499	–	499
Other	(6)	1,069	24	1,087
	465	25,935	27	26,427
Total financial investments	608	174,005	7,775	182,388

23 – Financial investments continued

(b) The following is a summary of the cost/amortised cost, gross unrealised gains and losses and fair value of financial investments:

	2006			
	Cost/ amortised cost £m	Unrealised gains £m	Unrealised losses £m	Fair value £m
Debt securities	111,409	2,402	(770)	113,041
Equity securities	45,045	12,330	(613)	56,762
Other investments				
Unit trusts and specialised investment vehicles	26,433	2,642	(63)	29,012
Derivatives financial instruments	–	1,325	–	1,325
Deposits with credit institutions	381	–	–	381
Minority holdings in property management undertakings	542	–	–	542
Other	1,712	86	(8)	1,790
	185,522	18,785	(1,454)	202,853

	2005			
	Cost/ amortised cost £m	Unrealised gains £m	Unrealised losses £m	Fair value £m
Debt securities	99,086	5,006	(175)	103,917
Equity securities	42,578	9,562	(96)	52,044
Other investments				
Unit trusts and specialised investment vehicles	22,335	1,885	(11)	24,209
Derivative financial instruments	–	467	–	467
Deposits with credit institutions	165	–	–	165
Minority holdings in property management undertakings	499	–	–	499
Other	1,040	49	(2)	1,087
	165,703	16,969	(284)	182,388

(c) Other information on investments

Included within financial investments are shareholdings held on a long-term basis as follows:

							Market value of shareholding		
	Long-term business		Non-long-term business		Total		Proportion held		Country of incorporation
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 %	2005 %	
UniCredit Group	437	383	591	501	1,028	884	2.2%	2.1%	Italy

UniCredit Group is a banking company.

(d) Stocklending

The Group has entered into stocklending arrangements in the UK and overseas during the year in accordance with established market conventions. In the UK, investments are lent to locally-domiciled counterparties and governed by agreements written under English law. Other investments are specifically deposited under local laws in various countries overseas as security to holders of policies issued there.

Included within financial investments are £722 million (2005: £461 million) of debt securities and other fixed income securities which have been sold under stock repurchase arrangements. The obligations arising under these arrangements are included in other financial liabilities (see note 44).

The carrying amounts of financial assets received and pledged as collateral under stocklending arrangements at 31 December 2006 are £21,153 million and £nil respectively (2005: £20,037 million and £nil respectively). In certain markets, the Group or the Group's appointed stocklending managers obtain legal ownership of the collateral received and can re-pledge as collateral elsewhere or sell outright. The value of collateral re-pledged or sold is £nil (2005: £nil).

Notes to the consolidated financial statements continued

24 – Receivables and other financial assets

	2006 £m	2005 £m
Amounts owed by contract holders	1,921	1,873
Amounts owed by intermediaries	1,258	1,543
Deposits with ceding undertakings	1,028	1,050
Amounts due from reinsurers	707	820
Other financial assets	3,184	2,488
Total	8,098	7,774
Less: Amounts classified as held for sale	–	(68)
	8,098	7,706
Expected to be recovered in less than one year	7,668	7,210
Expected to be recovered in more than one year	430	496
	8,098	7,706

Concentrations of credit risk with respect to receivables are limited due to the size and spread of the Group's trading base. No further credit risk provision is therefore required in excess of the normal provision for doubtful receivables.

25 – Deferred acquisition costs and other assets

(a) The carrying amount comprises:

	Total 2006 £m	Total 2005 £m
Deferred acquisition costs in respect of:		
Insurance contracts – Long-term business	848	1,118
Insurance contracts – General insurance and health business	1,422	1,281
Participating investment contracts	364	3
Non-participating investment contracts	566	752
Retail fund management business	22	21
	3,222	3,175
Surpluses in the staff pension schemes (note 42d(v))	56	–
Other assets	198	631
Total	3,476	3,806
Less: Amounts classified as held for sale	–	(40)
	3,476	3,766

Deferred acquisition costs on long-term business are generally recoverable in more than one year whereas such costs on general insurance and health business are generally recoverable within one year after the balance sheet date.

(b) The movements in deferred acquisition costs during the year were:

	2006 £m	2005 £m
Carrying amount at 1 January	3,175	2,709
Acquisition costs deferred during the year	3,248	3,108
Amortisation	(3,224)	(2,704)
Impairment losses	–	(4)
Foreign exchange rate movements	(49)	10
Other movements	72	56
Carrying amount at 31 December	3,222	3,175

Amortisation of deferred acquisition costs includes £271 million (2005: nil) for the effect of adjusting to PS06/14 realistic basis.

(c) Other assets include £2 million (2005: £472 million) that is expected to be recovered more than one year after the balance sheet date.

(d) Prepayments and accrued income include £62 million (2005: £467 million) that is expected to be recovered more than one year after the balance sheet date.

26 – Assets held to cover linked liabilities

Certain unit-linked products have been classified as investment contracts, while some are included within the definition of an insurance contract. The assets backing these unit-linked liabilities are included within the relevant balances in the consolidated balance sheet, while the liabilities are included within insurance and investment contract provisions disclosed in notes 35 and 37.

The carrying values of assets backing these unit-linked liabilities are as follows:

	2006 £m	2005 £m
Loans	879	–
Debt securities	15,308	12,959
Equity securities	25,839	21,593
Other investments	26,712	21,704
Reinsurance assets	1,136	1,232
Cash and cash equivalents	3,648	2,675
	73,522	60,163

27 – Ordinary share capital

(a) Details of the Company's ordinary share capital are as follows:

	2006 £m	2005 £m
The authorised share capital of the Company at 31 December 2006 was: 3,000,000,000 (2005: 3,000,000,000) ordinary shares of 25 pence each	750	750
The allotted, called up and fully paid share capital of the Company at 31 December 2006 was: 2,565,753,431 (2005: 2,395,693,688) ordinary shares of 25 pence each	641	599

(b) During 2006, a total of 170,059,743 ordinary shares of 25 pence each were allotted and issued by the Company as follows:

	Number of shares	Share capital £m	Share premium £m
At 1 January	2,395,693,688	599	1,167
Shares issued under the Group's Employee and Executive Share Option Schemes	14,204,808	3	40
Shares issued in connection with acquisitions, net of transaction costs	129,000,000	32	(11)
Shares issued in lieu of dividends	26,854,935	7	(7)
At 31 December	2,565,753,431	641	1,189

Ordinary shares in issue in the Company rank *pari passu*. All the ordinary shares in issue carry the same right to receive all dividends and other distributions declared, made or paid by the Company.

Shares in lieu of the 2005 final and 2006 interim dividends were issued on 17 May and 17 November 2006 respectively. The issue of shares in lieu of cash dividends is considered a bonus issue under the terms of the Companies Act 1985 and the nominal value of the shares is charged to the share premium account.

28 – Equity compensation plans**(a) Description of the plans**

The Group maintains a number of active stock option and award schemes. These are as follows:

(i) Savings-related options

These are options granted under the Inland Revenue-approved Save As You Earn (SAYE) share option schemes in the UK and in Ireland. Options are normally exercisable during the six month period following either the third, fifth or seventh anniversary of the start of the relevant savings contract.

(ii) Executive share options

These are options granted on various dates from 1996 to 2004, under the Aviva Executive Share Option Scheme or predecessor schemes. Options granted between 1997 and 2000 were subject to the satisfaction of conditions relating to either the Company's return on equity shareholders' funds (ROE) or its relative total shareholder return (TSR) against a chosen comparator group. In respect of options granted from 2000 the performance condition has been a mixture of both ROE and TSR measures. In all cases, performance is measured over a three year performance period and the options are normally exercisable between the third and tenth anniversary of their grant.

(iii) Deferred bonus plan options

These are options granted in 1999 and 2000 under the CGU Deferred Bonus Plan. Participants who deferred their annual cash bonus in exchange for an award of shares of equal value also received a matching award over an equal number of share options. The exercise of these options is not subject to the attainment of performance conditions. These options are exercisable up to the tenth anniversary of their grant.

Notes to the consolidated financial statements continued

28 – Equity compensation plans continued*(iv) Long-term incentive plan awards*

These awards have been made to senior Group executives since 2001 and are described in section (b) below and in the Directors' remuneration report.

(v) Deferred bonus plan awards

These awards have been made under the Aviva Deferred Bonus Plan, and are described in section (b) below and in the Directors' remuneration report. The Group has established various employee share trusts to facilitate the delivery of shares under the above schemes. Details of these trusts are given in note 29.

(vi) Annual bonus plan awards

These awards have been made under the Aviva Bonus Plan, and are described in section (b) below and in the Directors' remuneration report.

(b) Outstanding options and awards*(i) Share options*

At 31 December 2006, options to subscribe for ordinary shares of 25 pence each in the Company were outstanding as follows:

Aviva Savings Related Share Option Scheme	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	750.00	25,725	2006	406.00	1,565,926	2006, 2008 or 2010
	895.20	59,053	2005 or 2007	428.00	1,754,101	2007, 2009 or 2011
	664.00	435,637	2006 or 2008	491.00	4,548,158	2008, 2010 or 2012
	401.00	4,914,256	2005, 2007 or 2009	593.00	3,623,585	2009, 2011 or 2013
Hibernian Savings Related Share Option Scheme (in euros)	Option price c	Number of shares	Normally exercisable	Option price c	Number of shares	Normally exercisable
	1,087.56	10,114	2006	630.12	103,642	2007 or 2009
	662.85	82,057	2005 or 2007	719.00	168,230	2008 or 2010
	586.00	164,017	2006 or 2008	879.00	243,008	2009 or 2011
RAC Savings Related Share Option Scheme	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	291.27	20,252	2004 or 2006	354.94	606,313	2007 or 2009
	312.27	377,770	2006 or 2008			
Aviva Executive Share Option Scheme	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	677.50	6,587	2000 to 2007	822.00	48,629	2003 to 2010
	725.50	2,345	2000 to 2007	972.33	14,459	2003 to 2010
	857.50	19,987	2000 to 2007	960.00	55,763	2003 to 2010
	1073.31	8,385	2001 to 2008	1035.00	710,408	2004 to 2011
	1119.00	35,193	2001 to 2008	499.00	14,272	2005 to 2012
	853.00	223,724	2001 to 2008	516.00	1,172,983	2005 to 2012
	965.00	7,425	2002 to 2009	512.00	1,600,043	2006 to 2013
	870.83	44,742	2002 to 2009	526.00	3,732,102	2007 to 2014
	919.00	454,892	2002 to 2009			
General Accident Executive Share Option Scheme	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	766.42	71,913	2000 to 2007			
Aviva Executive Share Option Scheme (Delta Lloyd)	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	739.00	246,142	2002 to 2007	380.00	327,961	2003 to 2008
RAC Executive Share Option Scheme	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	347.49	4,136	2005 to 2009			
CGU plc Deferred Bonus Plan	Option price p	Number of shares	Normally exercisable	Option price p	Number of shares	Normally exercisable
	899.50	15,462	2002 to 2009	875.00	29,316	2003 to 2010
	966.50	1,986	2002 to 2009			

28 – Equity compensation plans continued

The following table summarises information about options outstanding at 31 December 2006:

Range of exercise prices	Outstanding options Number	Weighted average remaining contractual life Years	Weighted average exercise price p
£1.75 – £4.89	9,927,374	2	399.71
£4.90 – £8.04	15,900,844	5	538.45
£8.05 – £11.19	1,708,401	4	959.35

The comparative figures as at 31 December 2005 were:

Range of exercise prices	Outstanding options Number	Weighted average remaining contractual life Years	Weighted average exercise price p
£1.75 – £4.89	15,587,971	2	389.20
£4.90 – £8.04	18,090,563	5	532.73
£8.05 – £11.19	2,305,625	4	950.85

(ii) Share awards

At 31 December 2006, awards issued under the Company's executive incentive plans over ordinary shares of 25 pence each in the Company were outstanding as follows:

Aviva Long-Term Incentive Plan	Number of shares	Vesting period
	2,630,279	2004 to 2006

Aviva Long-Term Incentive Plan 2005	Number of shares	Vesting period	Number of shares	Vesting period
	3,683,739	2005 to 2007	3,232,004	2006 to 2008

Aviva Deferred Bonus Plan	Number of shares	Vesting date	Number of shares	Vesting date
	3,135,710	26 March 2007	3,049,330	24 March 2008

Aviva Annual Bonus Plan	Number of shares	Vesting date
	3,226,201	31 March 2009

The vesting of awards under the Aviva Long-Term Incentive Plan is subject to the attainment of performance conditions as described in the Directors' remuneration report. Shares which do not vest, lapse.

(iii) Shares to satisfy awards and options

Prior to March 2003, it was the practice to satisfy awards and options granted under the executive incentive plans through shares purchased in the market and held by employee share trusts which were established for the purpose of satisfying awards under the various executive incentive plans and funded by the Company. Since March 2003, no shares have been purchased by the trusts, it being the Company's current practice to satisfy the awards granted after that date by the issue of new shares at the time of vesting. At 31 December 2006, 682,202 shares were held by the employee share trusts with an aggregate nominal value of £170,550 and market value of £6 million. The trustees have waived their right to dividends on the shares held in the trusts. Further details are given in note 29.

Notes to the consolidated financial statements continued

28 – Equity compensation plans continued**(c) Movements in the year**

A summary of the status of the option plans as at 31 December 2006 and 2005, and changes during the years ended on those dates, is shown below.

	2006		2005	
	Number of options	Weighted average exercise price p	Number of options	Weighted average exercise price p
Outstanding at 1 January	35,984,159	497.34	39,617,478	516.75
Granted during the year	3,912,011	593.00	7,956,344	434.64
Forfeited during the year	–	–	(890)	719
Exercised during the year	(5,665,668)	394.93	(5,918,840)	419.69
Expired during the year	(6,693,883)	569.15	(5,669,933)	581.58
Outstanding at 31 December	27,536,619	514.54	35,984,159	497.34
Exercisable at 31 December	12,757,480	516.30	8,238,435	600.59

(d) Expense charged to income statement

The total expense recognised for the year arising from equity compensation plans was as follows:

	2006 £m	2005 £m
Equity-settled expense	48	22
Cash-settled expense	–	–
	48	22

(e) Fair value of options and awards granted after 7 November 2002

The weighted average fair value of options and awards granted during the year, estimated by using the Black-Scholes option-pricing model, was £2.35 and £6.70 (2005: £1.88 and £4.50) respectively.

(i) Share options

The fair value of the options was estimated on the date of grant, based on the following weighted average assumptions:

Weighted average assumption	2006	2005
Share price	781p	618p
Exercise price	593p	491p
Expected volatility	26%	35%
Expected life	3.82 years	3.81 years
Expected dividend yield	3.70%	4.10%
Risk-free interest rate	4.80%	4.20%

The expected volatility used was based on the historical volatility of the share price over a period equivalent to the expected life of the options prior to its date of grant.

The risk-free interest rate was based on the yields available on UK government bonds as at the date of grant. The bonds chosen were those with a similar remaining term to the expected life of the options.

No options granted after 7 November 2002 were exercised during the year (2005: nil).

28 – Equity compensation plans continued**(ii) Share awards**

The fair value of the awards was estimated on the date of grant, based on the following weighted average assumptions:

Weighted average assumption	2006	2005
Share price	814p	632p
Expected volatility*	23%	41%
Expected volatility of comparator companies' share price*	22%	44%
Correlation between Aviva and competitors' share price*	50%	64%
Expected life	3.0 years	3.0 years
Expected dividend yield	3.60%	4.00%
Risk-free interest rate*	4.50%	4.70%

* For awards with market-based performance conditions.

The expected volatility used was based on the historical volatility of the share price over a period equivalent to the expected life of the options prior to its date of grant.

The risk-free interest rate was based on the yields available on UK government bonds as at the date of grant. The bonds chosen were those with a similar remaining term to the expected life of the options.

29 – Shares held by employee trusts

Movements in the carrying value of shares held by employee trusts comprise:

	2006		2005	
	Number	£m	Number	£m
Cost debited to shareholders' funds				
At 1 January	1,823,788	–	5,894,264	–
Distributed in year	(1,141,586)	–	(4,070,476)	–
Balance at 31 December	682,202	–	1,823,788	–

These shares are owned by employee share trusts in the Company and a subsidiary undertaking to satisfy awards under the Group's Long Term Incentive Plan and Deferred Bonus Plans. The shares were purchased in the market and are carried at cost less amounts charged to the income statement in prior years. Further details of the shares held can be found in note 28b. Details of the features of the plans can be found in the Directors' remuneration report.

30 – Preference share capital

The preference share capital of the Company at 31 December 2006 was:

	2006 £m	2005 £m
Authorised		
200,000,000 cumulative irredeemable preference shares of £1 each	200	200
500,000,000 Sterling preference shares of £1 each	500	500
500,000,000 Sterling new preference shares of £1 each	500	–
	1,200	700
	2006 €m	2005 €m
700,000,000 Euro preference shares of €1 each	700	700
	£m	£m
Issued and paid up		
100,000,000 8¾% cumulative irredeemable preference shares of £1 each	100	100
100,000,000 8¾% cumulative irredeemable preference shares of £1 each	100	100
	200	200

Notes to the consolidated financial statements continued

30 – Preference share capital continued

At the Annual General Meeting on 10 May 2006, the Company's authorised preference share capital was increased to £1,200 million and €700 million by the creation of 500 million sterling new preference shares of £1 each.

The new preference shares, if issued and allotted, would rank, as to payment of a dividend and capital, ahead of the Company's ordinary share capital but behind the cumulative irredeemable preference shares currently in issue. The issued preference shares are non-voting except where their dividends are in arrears, on a winding up or where their rights are altered. On a winding up, they carry a preferential right of return of capital ahead of the ordinary shares.

31 – Direct capital instrument

Notional amount	2006 £m	2005 £m
5.9021% £500 million direct capital instrument	500	500
4.7291% €700 million direct capital instrument	490	490
	990	990

The euro and sterling direct capital instruments (the DCIs) were issued on 25 November 2004. They have no fixed redemption date but the Company may, at its sole option, redeem all (but not part) of the DCIs at their principal amount on 28 November 2014 and 27 July 2020 for the euro and sterling DCIs respectively, at which dates the interest rates change to variable rates, or on any respective coupon payment date thereafter. In addition, under certain circumstances defined in the terms and conditions of the issue, the Company may at its sole option:

(i) redeem all (but not part) of the DCIs at their principal amount at any time prior to 28 November 2014 and 27 July 2020 for the euro and sterling DCIs respectively;

(ii) substitute at any time all (but not some only) of the DCIs for, or vary the terms of the DCIs so that they become, Qualifying Tier 1 Securities or Qualifying Upper Tier 2 Securities;

(iii) substitute all (but not some only) of the DCIs for fully paid non-cumulative preference shares in the Company. These preference shares could only be redeemed on 28 November 2014 in the case of the euro DCIs and on 27 July 2020 in the case of the sterling DCIs, or in each case on any dividend payment date thereafter. The Company has the right to choose whether or not to pay any dividend on the new shares, and any such dividend payment will be non-cumulative.

The Company has the option to defer coupon payments on the DCIs on any relevant payment date. Deferred coupons shall be satisfied only in the following circumstances, all of which occur at the sole option of the Company:

(i) Redemption; or

(ii) Substitution by, or variation so they become, alternative Qualifying Tier 1 Securities or Qualifying Upper Tier 2 Securities; or

(iii) Substitution by preference shares.

No interest will accrue on any deferred coupon. Deferred coupons will be satisfied by the issue and sale of ordinary shares in the Company at their prevailing market value, to a sum as near as practicable to (and at least equal to) the relevant deferred coupons. In the event of any coupon deferral, the Company will not declare or pay any dividend on its ordinary or preference share capital.

32 – Reserves**(a) Merger reserve**

	2006 £m	2005 £m
Balance at 1 January	3,271	2,763
Merger relief on acquisition of AmerUs (note 3(a)(iv))	871	–
Merger relief on acquisition of RAC plc	–	508
Transfer to retained earnings on realisation (note 33)	(871)	–
Balance at 31 December	3,271	3,271

The issue of new shares to fund the acquisition of AmerUs was effected by a share placing. As part of the share placing, the Company issued 129,000,000 ordinary shares for consideration of £903 million through a special purpose entity. £32 million was taken to share capital and the balance of £871 million was taken to a merger reserve, since the placing structure utilised attracted merger relief under s.131 of the Companies Act 1985. £871 million was then transferred to retained earnings following the redemption of shares in the special purpose entity.

(b) Other reserves

	Currency translation reserve (see accounting policy D) £m	Owner- occupied properties reserve (see accounting policy N) £m	Investment valuation reserve (see accounting policy R) £m	Hedging instruments reserve (see accounting policy S) £m	Equity compensation reserve (see accounting policy Y) £m	Total £m
Balance at 1 January 2005	57	146	498	14	21	736
Arising in the year:						
Fair value gains/(losses)	–	32	(65)	(19)	–	(52)
Fair value losses transferred to profit	–	–	411	–	–	411
Share of fair value changes in joint ventures and associates taken to equity	–	2	–	–	–	2
Impairment losses on revalued assets	–	–	(45)	–	–	(45)
Reserves credit for equity compensation plans (note 28d)	–	–	–	–	22	22
Foreign exchange rate movements	(2)	–	–	19	–	17
Aggregate tax effect – policyholders' tax	–	3	–	–	–	3
Aggregate tax effect – shareholders' tax	–	(4)	45	5	–	46
Balance at 31 December 2005	55	179	844	19	43	1,140
Arising in the year:						
Fair value gains	–	26	347	–	–	373
Fair value gains transferred to profit	–	–	(162)	–	–	(162)
Fair value gains transferred to retained earnings on disposals (note 33)	–	(9)	–	–	–	(9)
Impairment losses on revalued assets	–	(2)	–	–	–	(2)
Reserves credit for equity compensation plans (note 28d)	–	–	–	–	48	48
Shares issued under equity compensation plans (note 33)	–	–	–	–	(18)	(18)
Foreign exchange rate movements	(386)	–	–	59	–	(327)
Aggregate tax effect – policyholders' tax	–	–	–	–	–	–
Aggregate tax effect – shareholders' tax	–	–	(50)	–	–	(50)
Balance at 31 December 2006	(331)	194	979	78	73	993

The above reserves are shown net of minority interests.

Notes to the consolidated financial statements continued

33 – Retained earnings

	2006 £m	2005 £m
Balance at 1 January	2,597	1,709
Profit for the year attributable to equity shareholders	2,215	1,767
Actuarial losses on pension schemes (note 42d (iii))	(114)	(547)
Dividends and appropriations (note 14)	(762)	(657)
Shares issued in lieu of dividends	203	100
Shares issued under equity compensation plans (note 32b)	18	–
Transfer from merger reserve on realisation (note 32a)	871	–
Fair value gains realised from reserves (note 32b)	9	–
Aggregate tax effect	45	226
Other movements	–	(1)
Balance at 31 December	5,082	2,597

The shares issued in lieu of dividends are in respect of the transfer to retained earnings from the ordinary dividend account, arising from the treatment of shares issued in lieu of the 2005 final and 2006 interim dividends, as explained in note 27(b).

34 – Minority interests

(a) Minority interests at 31 December comprised:

	2006 £m	2005 £m
Equity shares in subsidiaries	850	320
Share of earnings	284	153
Share of other reserves	308	399
	1,442	872
Preference shares in General Accident plc	250	250
Preference shares in other subsidiaries	6	6
	1,698	1,128

(b) Movements in the year comprised:

	2006 £m	2005 £m
Balance at 1 January	1,128	910
Profit for the year attributable to minority interests	174	131
Minority share of movements in other reserves	1	1
Foreign exchange rate movements	(19)	(19)
Recognised income and expense attributable to minority interests	156	113
Capital contributions from minority shareholders	397	212
Minority share of dividends declared in the year	(75)	(70)
Minority interest in acquired/(disposed) subsidiaries	92	(36)
Other movements	–	(1)
Balance at 31 December	1,698	1,128

35 – Insurance liabilities**(a) Carrying amount**

Insurance liabilities at 31 December comprise:

	2006			2005		
	Long-term business £m	General insurance and health £m	Total £m	Long-term business £m	General insurance and health £m	Total £m
Long-term business provisions						
Participating	63,705	–	63,705	59,958	–	59,958
Unit-linked non-participating	21,004	–	21,004	17,999	–	17,999
Other non-participating	41,905	–	41,905	36,473	–	36,473
	126,614	–	126,614	114,430	–	114,430
Outstanding claims provisions	696	10,165	10,861	605	10,641	11,246
Provision for claims incurred but not reported	–	2,553	2,553	–	2,324	2,324
	696	12,718	13,414	605	12,965	13,570
Provision for unearned premiums	–	5,182	5,182	–	5,381	5,381
Provision arising from liability adequacy tests	–	49	49	–	48	48
Other technical provisions	–	57	57	16	32	48
Total	127,310	18,006	145,316	115,051	18,426	133,477
Less: Obligations to staff pension schemes transferred to provisions (note 41a)	(1,086)	–	(1,086)	(875)	–	(875)
	126,224	18,006	144,230	114,176	18,426	132,602

(b) Long-term business liabilities**(i) Business description**

The Group underwrites long-term business in a number of countries as follows:

- In the UK mainly in
 - “with-profit” funds of CGNU Life Assurance (CGNU Life), Commercial Union Life Assurance (CULAC) and the with-profit and Provident Mutual funds of Norwich Union Life & Pensions (NUL&P), where the with-profit policyholders are entitled to at least 90% of the distributed profits, the shareholders receiving the balance;
 - “non-profit” funds of Norwich Union Annuity and NUL&P, where shareholders are entitled to 100% of the distributed profits. Shareholder profits on unitised with-profit business written by Norwich Union Life & Pensions and on stakeholder unitised with-profit business are derived from management fees and policy charges, and emerge in the non-profit funds.
- In France, where the majority of policyholders’ benefits are determined by investment performance, subject to certain guarantees, and shareholders’ profits are derived largely from management fees. In addition, a substantial number of policies participate in investment returns, with the balance being attributable to shareholders.
- In the Netherlands, the balance of profits, after providing appropriate returns for policyholders and after tax, accrues for the benefit of the shareholders. The bases for determining returns for policyholders are complex, but are consistent with methods and criteria followed generally in the Netherlands. In addition, a substantial number of policies provide benefits that are determined by investment performance, subject to certain guarantees, and shareholders’ profits are derived largely from management fees.
- In the United States, there are two main business segments - protection products and accumulation products. Protection products include interest-sensitive whole life, term life, universal life and indexed life insurance policies. The accumulation product segment includes traditional fixed and indexed deferred annuities for individuals and funding agreements for business customers. In addition, there are two closed blocks of participating contracts arising from demutualisations of subsidiary companies. All products are classified as insurance contracts except for the funding agreements and term certain immediate annuities, which are classified as non-participating investment contracts.
- In other overseas operations.

Notes to the consolidated financial statements continued

35 – Insurance liabilities continued**(ii) Group practice**

The long-term business provision is calculated separately for each of the Group's life operations. The provisions for overseas subsidiaries have generally been included on the basis of local regulatory requirements, mainly using the net premium method, modified where necessary to reflect the requirements of the Companies Act.

Material judgement is required in calculating the provisions and is exercised particularly through the choice of assumptions where there is discretion over these. In turn, the assumptions used depend on the circumstances prevailing in each of the life operations. Provisions are most sensitive to assumptions regarding discount rates and mortality/morbidity rates.

Bonuses paid during the year are reflected in claims paid, whereas those allocated as part of the bonus declaration are included in the movements in the long-term business provision.

(iii) Methodology and assumptions

There are two main methods of actuarial valuation of liabilities arising under long-term insurance contracts – the net premium method and the gross premium method – both of which involve the discounting of projected premiums and claims.

Under the net premium method, the premium taken into account in calculating the provision is determined actuarially, based on the valuation assumptions regarding discount rates, mortality and disability. The difference between this premium and the actual premium payable provides a margin for expenses. This method does not allow for voluntary early termination of the contract by the policyholder, and so no assumption is required for persistency. Explicit provision is made for vested bonuses (including those vesting following the most recent fund valuation), but no such provision is made for future regular or terminal bonuses. However, this method makes implicit allowance for future regular or terminal bonuses already earned, by margins in the valuation discount rate used.

The gross premium method uses the amount of contractual premiums payable and includes explicit assumptions for interest and discount rates, mortality and morbidity, persistency and future expenses. These assumptions can vary by contract type and reflect current and expected future experience. Explicit provision is made for vested bonuses and explicit allowance is also made for future regular bonuses, but not terminal bonuses.

The principal assumptions in the UK, France, the Netherlands and the United States are:

(a) UK

With-profit business The valuation of with-profit business uses the methodology developed for the Realistic Balance Sheet, adjusted to remove the shareholders' share of future bonuses. The key elements of the Realistic Balance Sheet methodology are the with-profit benefit reserve (WPBR) and the present value of the expected cost of any payments in excess of the WPBR (referred to as the cost of future policy-related liabilities). The realistic liability for any contract is equal to the sum of the WPBR and the cost of future policy-related liabilities. The WPBR for an individual contract is generally calculated on a retrospective basis, and represents the accumulation of the premiums paid on the contract, allowing for investment return, taxation, expenses and any other charges levied on the contract.

For a small proportion of business, the retrospective approach is not available or is inappropriate, so a prospective valuation approach is used instead, including allowance for anticipated future regular and final bonuses.

The items included in the cost of future policy-related liabilities include:

- Maturity Guarantees;
- Smoothing (which can be negative);
- Guaranteed Annuity Options;
- GMP underpin on Section 32 transfers; and
- Expected payments under Mortgage Endowment Promise.

In the Provident Mutual and with-profit funds in NUL&P, this is offset by the expected cost of charges to WPBR to be made in respect of guarantees.

The cost of future policy-related liabilities is determined using a market-consistent approach and, in the main, this is based on a stochastic model calibrated to market conditions at the end of the reporting period. Non-market-related assumptions (for example, persistency, mortality and expenses) are based on experience, adjusted to take into account future trends. Where policyholders have valuable guarantees, options or promises, then future persistency is assumed to improve, and future take-up rates of guaranteed annuity options are assumed to increase.

35 – Insurance liabilities continued

The principal assumptions underlying the cost of future policy related liabilities are as follows:

Future investment return A “risk-free” rate equal to the spot yield on gilts, plus a margin of 0.1% is used. The rates vary, according to the outstanding term of the policy, with a typical rate as at year end 2006 being 4.84% for a policy with ten years outstanding.

Volatility of investment return The volatility of returns is assumed to be distributed as follows:

Financial investment	Volatility
Equities	17% (for UK stocks)
Property	15%
Gilts	3.25% (NUL&P WP)/4.5% (other WP funds)
Corporate bonds	5.25% (NUL&P WP)/6.5% (other WP funds)

Future regular bonuses Annual bonus assumptions for 2007 have been set consistently with the year end 2006 declaration. Future annual bonus rates reflect the principles and practices of the fund. In particular, the level is set with regard to the projected margin for final bonus and the change from one year to the next is limited to a level consistent with past practice.

Mortality Mortality assumptions are set with regard to recent company experience and general industry trends.

	Mortality table used	
	2006	2005
Assurances, pure endowments and deferred annuities before vesting	Nil or AM92/AF92	Nil or AM92/AF92 or AM80/AF80 adjusted
Pensions business after vesting and pensions annuities in payment	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement	PCMA00/PCFA00 or PMA92/PFA92 adjusted plus allowance for future mortality improvement

Non-profit business Conventional non-profit contracts, including those written in the with-profit funds, are valued using gross premium methods which discount projected future cash flows. The cash flows are calculated using the amount of contractual premiums payable, together with explicit assumptions for investment returns, inflation, discount rates, mortality, morbidity, persistency and future expenses. These assumptions vary by contract type and reflect current and expected future experience.

For unit-linked and some unitised with-profit business, the provisions are valued by adding a prospective non-unit reserve to the bid value of units. The prospective non-unit reserve is calculated by projecting the future non-unit cash flows on the assumption that future premiums cease, unless it is more onerous to assume that they continue. Where appropriate, allowance for persistency is based on actual experience.

Valuation discount rate assumptions are set with regard to yields on the supporting assets and the general level of long-term interest rates as measured by gilt yields. An explicit allowance for risk is included by restricting the yields for equities and properties with reference to a margin over long-term interest rates or by making an explicit deduction from the yields on corporate bonds, mortgages and deposits, based on historical default experience of each asset class. A further margin for risk is then deducted for all asset classes.

The provisions held in respect of guaranteed annuity options are a prudent assessment of the additional liability incurred under the option on a basis and method consistent with that used to value basic policy liabilities, and includes a prudent assessment of the proportion of policyholders who will choose to exercise the option.

Changes have been made to the assumptions for certain non-profit business during 2006, resulting from a decision taken by management to adopt changes permitted by the FSA Policy Statement 06/14, *Prudential Changes for Insurers*, issued in December 2006. These are as follows:

- For certain blocks of protection business, the reserve for some policies may now be negative, where previously it would have been set to zero.
- Prudent lapse assumptions have been introduced for these blocks of protection business. Prudent assumptions will be lower than expected for policies with positive reserves and higher than expected for policies with negative reserves.
- For certain blocks of unit-linked business, lower levels of expenses are allowed for in the calculation of individual policy reserves, with the remaining expenses being covered by future valuation margins on the overall block of similar policies.

Notes to the consolidated financial statements continued

35 – Insurance liabilities continued

The changes in the valuation discount rates since 2005 reflect the changes in the yields on the supporting assets.

	Valuation discount rates	
	2006	2005
Assurances		
Life conventional non-profit	3.1% to 3.9%	2.9% to 3.6%
Pensions conventional non-profit	3.9% to 4.1%	3.6% to 4.0%
Deferred annuities		
Non-profit – in deferment	3.9% to 4.1%	3.6% to 4.6%
Non-profit – in payment	4.3%	3.6%
Annuities in payment		
Convention annuity	4.3% to 4.9%	4.0% to 4.6%
Non-unit reserves		
Life	3.4%	3.2%
Pensions	4.2%	3.9%

Mortality assumptions are set with regard to recent company experience and general industry trends. Since 2005, there have been changes to both assurance and annuity mortality bases, although the same standard mortality tables are still used. The assurance mortality basis is unchanged from 2005 for most blocks of business, though has been weakened for certain blocks of business where experience reviews have indicated that this is appropriate.

	Mortality tables used	
	2006	2005
Assurances		
Non-profit	AM80/AF80 or AM92/AF92 or TM92/TF92 adjusted for smoker status and age/sex specific factors	AM80/AF80 or AM92/AF92 or TM92/TF92 adjusted for smoker status and age/sex specific factors
Pure endowments and deferred annuities before vesting	Nil or AM80/AF80 or AM92/AF92 adjusted	Nil or AM80/AF80 or AM92/AF92 adjusted
General annuity business after vesting	IML00/IFL00 adjusted plus allowance for future mortality improvement	IML00/IFL00 adjusted plus allowance for future mortality improvement
Pensions business after vesting	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement
Annuities in payment		
General annuity business	IML00/IFL00 adjusted plus allowance for future mortality improvement	IML00/IFL00 adjusted plus allowance for future mortality improvement
Pensions business	PCMA00/PCFA00 adjusted or IML00/IFL00 adjusted plus allowance for future mortality improvement	PCMA00/PCFA00 adjusted plus allowance for future mortality improvement

(b) France

The majority of provisions arise from a single premium savings product and are based on the accumulated fund value, adjusted to maintain consistency with the value of the assets backing the policyholder liabilities. The net premium method is used for prospective valuations, in accordance with local regulation, where the valuation assumptions depend on the date of issue of the contract. The valuation discount rate also depends on the original duration of the contract and mortality rates are based on industry tables.

	Valuation discount rates		Mortality tables used
	2006 and 2005	2006	2005
Life assurances	1.75% to 4.5%	PM60-64, TD73-77, TD 88/90, TF00-02, TH00-02	PM60-64, TD73-77, TD 88/90
Annuities	1.75% to 4.5%	TPRV (prospective table), TGF05, TGH05	TPRV (prospective table)

35 – Insurance liabilities continued*(c) Netherlands*

On transition to IFRS, the valuation of most long-term insurance and participating investment contracts was changed from existing methods that generally used historic assumptions to an active basis using current market interest rates. A liability adequacy test is performed in line with IFRS requirements. Where liabilities are based on current market interest rates and assets are valued at market value, the margin in the liability adequacy test is determined by comparison of the liabilities with the present value of best estimate cash flows.

	Valuation discount rates		Mortality tables used	
	2006 and 2005		2006 and 2005	
Life assurances	Actual swap rate		GBM 61-65, GMB71-75, GBMV 76-80, GBM 80-85, GBMV 85-90 and GBMV 90-95	
Annuities in deferment and in payment	Actual swap rate		GBMV 76-80, GBMV 85-90, GBMV 95-00, Coll 1993/2003 and DIL 98, plus further allowance for future mortality improvement	

(d) United States

For the major part of our US business, insurance liabilities are measured in accordance with US GAAP as at the date of acquisition.

The liability for future policy benefits for traditional life insurance is computed using the net level method, based on guaranteed interest and mortality rates as used in calculating cash surrender values. Reserve interest assumptions range from 2.00% to 7.50%. The weighted average interest rate for all traditional life policy reserves in 2006 was 4.48%.

Future policy benefit reserves for universal life insurance, indexed life, deferred annuity products and funding agreements are computed under a retrospective deposit method and represent policy account balances before applicable surrender charges. The weighted average interest crediting rates for universal life products were 4.37% in 2006. The range of interest crediting rates for deferred annuity products, excluding sales inducement payouts, was 2.75% to 7.00% in 2006. An additional liability is established for universal life contracts with death or other insurance benefit features, which is determined using an equally-weighted range of scenarios with respect to investment returns, policyholder lapses, benefit election rates, premium payout patterns and mortality. The additional liability represents the present value of future expected benefits based on current product assumptions.

The indexed life and annuity products guarantee the return of principal to the customer, and credit interest based on certain indices. A portion of the premium from each customer is invested in fixed income securities and is intended to cover the minimum guaranteed value. A further portion of the premium is used to purchase call options to hedge the growth in interest credited to the customer as a direct result of increases in the related indices. Both the call options and the options embedded in the policy are valued at their fair value.

Deferred income reserves are established for fees charged for insurance benefit features which are assessed in a manner that is expected to result in higher profits in earlier years, followed by lower profits or losses in subsequent years. The excess charges are deferred and amortised using the same assumptions and factors used to amortise deferred acquisition costs. Shadow adjustments may be made to deferred acquisition costs, acquired value of in-force business, deferred income reserves and contract liabilities. The shadow adjustments are recognised directly in equity so that unrealised gains or losses on investments that are recognised directly in equity affect the measurement of the liability, or related assets, in the same way as realised gains or losses.

(e) In all other countries, local generally-accepted interest rates and published standard mortality tables are used for different categories of business as appropriate. The tables are based on relevant experience and show mortality rates, by age, for specific groupings of people.

Movements

The following movements have occurred in the long-term business provisions during the year:

	2006 £m	2005 £m
Carrying amount at 1 January	114,430	106,491
Provisions in respect of new business	8,750	6,589
Expected change in existing business provisions	(5,678)	(2,703)
Variance between actual and expected experience	1,209	3,784
Effect of adjusting to PS06/14 realistic basis	(800)	–
Impact of other operating assumption changes	(333)	(1,034)
Impact of economic assumption changes	(1,727)	2,411
Other movements	314	340
Change in liability recognised as an expense	1,735	9,387
Effect of portfolio transfers, acquisitions and disposals	12,454	(360)
Foreign exchange rate movements	(2,005)	(684)
Other movements	–	(404)
Carrying amount at 31 December	126,614	114,430

Notes to the consolidated financial statements continued

35 – Insurance liabilities continued

The effect of changes in the main assumptions is given in note 39.

Included within portfolio transfers is £287 million reclassified to investment contracts (see note 37) as a result of Prudential Rule No 49 issued by the Australian Prudential Regulation Authority (APRA), which requires further unbundling of certain savings products between insurance liabilities and investment contracts.

(c) General insurance and health liabilities**Provisions for outstanding claims**

Delays occur in the notification and settlement of claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the balance sheet date. The reserves for general insurance and health are based on information currently available; however, it is inherent in the nature of the business written that the ultimate liabilities may vary as a result of subsequent developments.

Provisions for outstanding claims are established to cover the outstanding expected ultimate liability for losses and loss adjustment expenses (LAE) in respect of all claims that have already occurred. The provisions established cover reported claims and associated LAE, as well as claims incurred but not yet reported and associated LAE.

Outstanding claims provisions are based on undiscounted estimates of future claim payments, except for the following classes of business for which discounted provisions are held:

Country	Class	Rate		Mean term of liabilities	
		2006	2005	2006	2005
Netherlands	Permanent health and injury	3.61%	3.21%	9 years	7 years

The net outstanding claims provisions before discounting were £12,768 million (2005: £13,014 million). The period of time which will elapse before the liabilities are settled has been estimated by modelling the settlement patterns of the underlying claims.

Assumptions

Outstanding claims provisions are estimated based on known facts at the date of estimation. Case estimates are generally set by skilled claims technicians, applying their experience and knowledge to the circumstances of individual claims. The ultimate cost of outstanding claims is then estimated by using a range of standard actuarial claims projection techniques, such as the Chain Ladder and Bornhuetter-Ferguson methods. The main assumption underlying these techniques is that a company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios. Historical claims development is mainly analysed by accident period, although underwriting or notification period is also used where this is considered appropriate. Claim development is separately analysed for each geographic area, as well as by each line of business. Certain lines of business are also further analysed by claim type or type of coverage. In addition, large claims are usually separately addressed, either by being reserved at the face value of loss adjuster estimates or separately projected in order to reflect their future development.

In most cases, no explicit assumptions are made regarding future rates of claims inflation or loss ratios. Instead, the assumptions used are those implicit in the historic claims development data on which the projections are based. Additional qualitative judgement is used to assess the extent to which past trends may not apply in the future, for example, to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy conditions and claims handling procedures in order to arrive at the estimated ultimate cost of claims that represents the likely outcome, from the range of possible outcomes, taking account of all the uncertainties involved.

35 – Insurance liabilities continued**Movements**

The following changes have occurred in the general insurance and health claims provisions during the year:

	2006 £m	2005 £m
Carrying amount at 1 January	12,965	12,750
Impact of changes in assumptions	2	(6)
Claim losses and expenses incurred in the current year	7,639	7,124
Decrease in estimated claim losses and expenses incurred in prior years	(550)	(372)
Inurred claims losses and expenses	7,091	6,746
Less:		
Payments made on claims incurred in the current year	(3,765)	(3,379)
Payments made on claims incurred in prior years	(3,771)	(3,407)
Recoveries on claim payments	304	263
Claims payments made in the year, net of recoveries	(7,232)	(6,523)
Other movements in the claims provisions	(7)	(9)
Changes in claims reserve recognised as an expense	(148)	214
Effect of portfolio transfers, acquisitions and disposals	207	(153)
Foreign exchange rate movements	(306)	146
Other gross movements	–	8
Carrying amount at 31 December	12,718	12,965

The effect of changes in the main assumptions is given in note 39.

Included within portfolio transfers above is £259 million arising from the acquisition of a general insurance and investment portfolio in the Netherlands.

(d) Loss development tables

The tables that follow present the development of claim payments and the estimated ultimate cost of claims for the accident years 2001 to 2006. The upper half of the tables shows the cumulative amounts paid during successive years related to each accident year. For example, with respect to the accident year 2002, by the end of 2006 £5,466 million had actually been paid in settlement of claims. In addition, as reflected in the lower section of the table, the original estimated ultimate cost of claims of £6,250 million was re-estimated to be £6,205 million at 31 December 2006. This decrease from the original estimate is due to the combination of a number of factors. The original estimates will be increased or decreased, as more information becomes known about the individual claims and overall claim frequency and severity.

In 2005, the year of adoption of IFRS, only five years were required to be disclosed. This is being increased in each succeeding additional year, until ten years of information is included.

The Group aims to maintain strong reserves in respect of its non-life and health business in order to protect against adverse future claims experience and development. As claims develop and the ultimate cost of claims become more certain, the absence of adverse claims experience will then result in a release of reserves from earlier accident years, as shown in the loss development tables. However, in order to maintain strong reserves, the Group transfers much of this release to current accident year (2006) reserves where the development of claims is less mature and there is much greater uncertainty attaching to the ultimate cost of claims. The release from prior accident year reserves during 2006 is also due to an improvement in the estimated ultimate cost of claims.

Notes to the consolidated financial statements continued

35 – Insurance liabilities continued

Before the effect of reinsurance, the loss development table is:

Accident year	All prior years £m	2001 £m	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	Total £m
Gross cumulative claim payments								
At end of accident year		(3,029)	(2,952)	(2,819)	(2,971)	(3,345)	(3,653)	
One year later		(4,766)	(4,486)	(4,190)	(4,561)	(5,011)		
Two years later		(5,303)	(4,921)	(4,613)	(4,981)			
Three years later		(5,701)	(5,233)	(4,972)				
Four years later		(5,966)	(5,466)					
Five years later		(6,121)						
Estimate of gross ultimate claims								
At end of accident year		6,590	6,250	6,385	6,891	7,106	7,533	
One year later		6,770	6,372	6,172	6,557	6,938		
Two years later		6,775	6,287	6,124	6,371			
Three years later		6,798	6,257	6,036				
Four years later		6,754	6,205					
Five years later		6,679						
Estimate of gross ultimate claims		6,679	6,205	6,036	6,371	6,938	7,533	
Cumulative payments		(6,121)	(5,466)	(4,972)	(4,981)	(5,011)	(3,653)	
	3,244	558	739	1,064	1,390	1,927	3,880	12,802
Effect of discounting	(19)	(6)	(5)	(5)	(3)	(4)	(8)	(50)
Present value	3,225	552	734	1,059	1,387	1,923	3,872	12,752
Cumulative effect of foreign exchange movements	–	(7)	(8)	(10)	(15)	(55)	–	(95)
Effect of acquisitions	–	–	1	4	7	34	15	61
Present value recognised in the balance sheet	3,225	545	727	1,053	1,379	1,902	3,887	12,718

After the effect of reinsurance, the loss development table is:

Accident year	All prior years £m	2001 £m	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	Total £m
Net cumulative claim payments								
At end of accident year		(2,970)	(2,913)	(2,819)	(2,870)	(3,281)	(3,612)	
One year later		(4,624)	(4,369)	(4,158)	(4,378)	(4,925)		
Two years later		(5,088)	(4,779)	(4,565)	(4,712)			
Three years later		(5,436)	(5,064)	(4,924)				
Four years later		(5,648)	(5,297)					
Five years later		(5,763)						
Estimate of gross ultimate claims								
At end of accident year		6,186	6,037	6,218	6,602	6,982	7,430	
One year later		6,333	6,038	6,093	6,266	6,818		
Two years later		6,321	5,997	6,037	6,082			
Three years later		6,329	5,973	5,942				
Four years later		6,286	5,912					
Five years later		6,219						
Estimate of gross ultimate claims		6,219	5,912	5,942	6,082	6,818	7,430	
Cumulative payments		(5,763)	(5,297)	(4,924)	(4,712)	(4,925)	(3,612)	
	1,884	456	615	1,018	1,370	1,893	3,818	11,054
Effect of discounting	(15)	(4)	(4)	(5)	(3)	(4)	(8)	(43)
Present value	1,869	452	611	1,013	1,367	1,889	3,810	11,011
Cumulative effect of foreign exchange movements	–	(7)	(7)	(10)	(15)	(53)	–	(92)
Effect of acquisitions	–	–	1	4	7	34	15	61
Present value recognised in the balance sheet	1,869	445	605	1,007	1,359	1,870	3,825	10,980

In the loss development tables shown above, the cumulative claim payments and estimates of cumulative claims for each accident year are translated into sterling at the exchange rates that applied at the end of that accident year. The impact of using varying exchange rates is shown at the bottom of each table. Disposals are dealt with by treating all outstanding and IBNR claims of the disposed entity as "paid" at the date of disposal.

35 – Insurance liabilities continued

The loss development tables include information on asbestos and environmental pollution claims provisions from business written before 2001. The claims provisions, net of reinsurance, in respect of this business were £312 million (2005: £289 million). The movement in the year reflects strengthening of the provisions by £9 million (2005: £83 million) and timing differences between claim payments and reinsurance recoveries.

(e) Provision for unearned premiums**Movements**

The following changes have occurred in the provision for unearned premiums (UPR) during the year:

	2006 £m	2005 £m
Carrying amount at 1 January	5,381	4,923
Premiums written during the year	11,427	11,017
Less: Premiums earned during the year	(11,516)	(10,802)
Other movements in UPR	–	1
Changes in UPR recognised as an (income)/expense	(89)	216
Gross portfolio transfers and acquisitions	3	174
Foreign exchange rate movements	(113)	74
Other movements	–	(6)
Carrying amount at 31 December	5,182	5,381

36 – Reinsurance assets**(a) Carrying amounts**

(i) The reinsurance assets at 31 December comprised:

	2006 £m	2005 £m
Long-term business	5,601	4,733
General insurance and health	2,224	2,397
Total	7,825	7,130

Of the above total, £3,848 million (2005: £3,717 million) is expected to be recovered more than one year after the balance sheet date.

(ii) The following is a summary of the reinsurance assets and related insurance reserves as at 31 December.

	2006			2005		
	Gross provisions £m	Reinsurance assets £m	Net £m	Gross provisions £m	Reinsurance assets £m	Net £m
Long-term business provisions						
Long-term insurance contracts	(126,614)	4,139	(122,475)	(114,430)	3,816	(110,614)
Participating investment contracts	(49,400)	–	(49,400)	(47,258)	–	(47,258)
Non-participating investment contracts	(38,958)	1,395	(37,563)	(30,051)	890	(29,161)
	(214,972)	5,534	(209,438)	(191,739)	4,706	(187,033)
Outstanding claims provisions						
Long-term business	(696)	67	(629)	(605)	27	(578)
General insurance and health	(10,165)	1,659	(8,506)	(10,641)	1,832	(8,809)
	(10,861)	1,726	(9,135)	(11,246)	1,859	(9,387)
Provisions for claims incurred but not reported	(2,553)	79	(2,474)	(2,324)	82	(2,242)
	(228,386)	7,339	(221,047)	(205,309)	6,647	(198,662)
Provision for unearned premiums	(5,182)	484	(4,698)	(5,381)	482	(4,899)
Provision arising from liability adequacy tests	(49)	–	(49)	(48)	–	(48)
Other technical provisions	(57)	2	(55)	(49)	1	(48)
Totals	(233,674)	7,825	(225,849)	(210,787)	7,130	(203,657)

Notes to the consolidated financial statements continued

36 – Reinsurance assets continued**(b) Assumptions**

The assumptions used for reinsurance contracts follow those used for insurance contracts.

Reinsurance assets are valued net of an allowance for their recoverability.

(c) Movements

The following movements have occurred in the reinsurance asset during the year:

(i) In respect of long-term business provisions

	2006 £m	2005 £m
Carrying amount at 1 January	4,706	5,878
Asset in respect of new business	226	183
Expected change in existing business asset	57	(128)
Variance between actual and expected experience	(69)	257
Effect of adjusting to PS06/14 realistic basis	(502)	–
Impact of other operating assumption changes	(84)	(1,178)
Impact of economic assumption changes	(341)	159
Other movements	–	177
Change in asset	(713)	(530)
Effect of portfolio transfers, acquisitions and disposals	1,639	–
Foreign exchange rate movements	(99)	(78)
Other movements	1	(564)
Carrying amount at 31 December	5,534	4,706

(ii) In respect of general insurance and health outstanding claims provisions and IBNR

	2006 £m	2005 £m
Carrying amount at 1 January	1,914	2,196
Impact of changes in assumptions	–	–
Reinsurers' share of claim losses and expenses incurred in current year	102	146
Reinsurers' share of claim losses and expenses incurred in prior years	78	(10)
Reinsurers' share of incurred claim losses and expenses	180	136
Less:		
Reinsurance recoveries received on claims incurred in current year	(30)	(48)
Reinsurance recoveries received on claims incurred in prior years	(307)	(251)
Reinsurance recoveries received in the year	(337)	(299)
Other movements	–	5
Change in reinsurance asset recognised as income	(157)	(158)
Effect of portfolio transfers, acquisitions and disposals	(5)	(93)
Foreign exchange rate movements	(32)	26
Other movements	18	(57)
Carrying amount at 31 December	1,738	1,914

36 – Reinsurance assets continued*(iii) Reinsurers' share of the provision for unearned premiums (UPR)*

	2006 £m	2005 £m
Carrying amount at 1 January	482	398
Premiums ceded to reinsurers in the year	726	706
Less: Reinsurers' share of premiums earned during the year	(722)	(612)
Other movements	–	(1)
Changes in reinsurance asset recognised as income	4	93
Reinsurers' share of portfolio transfers and acquisitions	1	(6)
Foreign exchange rate movements	(3)	2
Other movements	–	(5)
Carrying amount at 31 December	484	482

37 – Liability for investment contracts**(a) Carrying amount**

The liability for investment contracts at 31 December comprised:

	2006 £m	2005 £m
Long-term business		
Participating contracts	49,400	47,258
Non-participating contracts at fair value	38,081	29,304
Non-participating contracts at amortised cost	877	747
	38,958	30,051
Total	88,358	77,309

(b) Long-term business investment liabilities

Investment contracts are those that do not transfer significant insurance risk from the contract holder to the issuer, and are therefore treated as financial instruments under IFRS.

Many investment contracts contain a discretionary participation feature in which the contract holder has a contractual right to receive additional benefits as a supplement to guaranteed benefits. These are referred to as participating contracts and are measured according to the methodology and group practice for long-term business liabilities as described in note 35. They are not measured at fair value as there is currently no agreed definition of fair valuation for discretionary participation features under IFRS. In the absence of such a definition, it is not possible to provide a range of estimates within which a fair value is likely to fall. The IASB has deferred consideration of participating contracts to Phase II of its insurance contracts project.

For participating business, the discretionary participation feature is recognised separately from the guaranteed element and is classified as a liability, referred to as unallocated distributable surplus. Guarantees on long-term investment products are discussed in note 38.

Investment contracts that do not contain a discretionary participation feature are referred to as non-participating contracts and the liability is measured at either fair value or amortised cost.

Most non-participating investment contracts measured at fair value are unit-linked in structure and the fair value liability is equal to the unit reserve plus additional non-unit reserves if required on a fair value basis. For this business, a deferred acquisition cost asset and deferred income reserve liability are recognised in respect of transaction costs and front-end fees respectively, that relate to the provision of investment management services, and which are amortised on a systematic basis over the contract term. The amount of the related deferred acquisition cost asset is shown in note 25 and the deferred income liability is shown in note 45.

In the United States, funding agreements consist of one to ten year fixed rate contracts. These contracts may not be cancelled by the holders unless there is a default under the agreement, but may be terminated by Aviva at any time. The weighted average interest rates for fixed-rate and floating-rate funding agreements in 2006 were 5.07% and 5.55%, respectively. The funding agreements are measured at fair value equal to the present value of contractual cash flows.

There is a small volume of annuity certain business for which the liability is measured at amortised cost using the effective interest method.

The fair value of contract liabilities measured at amortised cost is not materially different from the amortised cost liability.

Notes to the consolidated financial statements continued

37 – Liability for investment contracts continued**(c) Movements in the year**

The following movements have occurred in the year:

(i) Participating investment contracts

	2006 £m	2005 £m
Carrying amount at 1 January	47,258	43,974
Provisions in respect of new business	3,001	3,467
Expected change in existing business provisions	(2,237)	(1,720)
Variance between actual and expected experience	2,131	2,034
Effect of adjusting to PS06/14 realistic basis	(105)	–
Impact of operating assumption changes	(43)	5
Impact of economic assumption changes	(125)	513
Other movements	51	(153)
Change in liability recognised as an expense	2,673	4,146
Effect of portfolio transfers, acquisitions and disposals	125	4
Foreign exchange rate movements	(656)	(856)
Other movements	–	(10)
Carrying amount at 31 December	49,400	47,258

Included within portfolio transfers above is £122 million reclassified from insurance liabilities (see note 35) as a result of Prudential Rule No 49 issued by the Australian Prudential Regulation Authority (APRA), which requires further unbundling of certain savings products between insurance liabilities and investment contracts.

The effect of changes in main assumptions is given in note 39.

(ii) Non-participating investment contracts

	2006 £m	2005 £m
Carrying amount at 1 January	30,051	25,581
Provisions in respect of new business	5,695	5,247
Expected change in existing business provisions	(163)	936
Variance between actual and expected experience	265	(1,732)
Impact of operating assumption changes	15	2
Impact of economic assumption changes	(5)	–
Other movements	56	93
Change in liability	5,863	4,546
Effect of portfolio transfers, acquisitions and disposals	3,396	–
Foreign exchange rate movements	(352)	(76)
Carrying amount at 31 December	38,958	30,051

Included within portfolio transfers above is £165 million reclassified from insurance liabilities (see note 35) as a result of Prudential Rule No 49 issued by the Australian Prudential Regulation Authority (APRA), which requires further unbundling of certain savings products between insurance liabilities and investment contracts.

The effect of changes in main assumptions is given in note 39.

38 – Financial guarantees and options

As a normal part of their operating activities, various Group companies have given guarantees and options, including investment return guarantees, in respect of certain long-term insurance and fund management products. Further information on assumptions is given in notes 35 and 37.

(a) UK Life with-profit business

In the UK, life insurers are required to comply with the FSA's realistic reporting regime for their with-profit funds for the calculation of FSA liabilities. Under the FSA's rules, provision for guarantees and options within realistic liabilities must be measured at fair value, using market-consistent stochastic models. A stochastic approach includes measuring the time value of guarantees and options, which represents the additional cost arising from uncertainty surrounding future economic conditions.

The material guarantees and options to which this provision relates are:

(i) Maturity value guarantees – Substantially all of the conventional with-profit business and a significant proportion of unitised with-profit business have minimum maturity values reflecting the sums assured plus declared annual bonus. In addition, the guarantee fund has offered maturity value guarantees on certain unit-linked products.

(ii) No market valuation reduction (MVR) guarantees – For unitised business, there are a number of circumstances where a "no MVR" guarantee is applied, for example on certain policy anniversaries, guaranteeing that no market value reduction will be applied to reflect the difference between the accumulated value of units and the market value of the underlying assets.

(iii) Guaranteed annuity options – The Group's UK with-profit funds have written individual and group pension contracts which contain guaranteed annuity rate options (GAOs), where the policyholder has the option to take the benefits from a policy in the form of an annuity based on guaranteed conversion rates. The Group also has exposure to GAOs and similar options on deferred annuities.

(iv) Guaranteed minimum pension – The Group's UK with-profit funds also have certain policies that contain a guaranteed minimum level of pensions as part of the condition of the original transfer from state benefits to the policy.

In addition, while these do not constitute guarantees, the with-profit fund companies have made promises to certain policyholders in relation to their with-profit mortgage endowments. Subject to certain conditions, top-up payments will be made on these policies at maturity to meet the mortgage value up to a maximum of the 31 December 1999 illustrated shortfall.

(b) UK Life non-profit business

The Group's UK non-profit funds are evaluated by reference to statutory reserving rules, including changes introduced in 2006 under FSA Policy Statement 06/14 *Prudential Changes for Insurers*, as outlined in note 35(b)(iii)(a).

(i) Guaranteed annuity options – Similar options to those written in the with-profit fund have been written in relation to non-profit products. Provision for these guarantees does not materially differ from a provision based on a market-consistent stochastic model, and amounts to £39 million at 31 December 2006 (2005: £44 million).

(ii) Guaranteed unit price on certain products – Certain unit-linked pension products linked to long-term life insurance funds provide policyholders with guaranteed benefits at retirement or death. No additional provision is made for this guarantee as the investment management strategy for these funds is designed to ensure that the guarantee can be met from the fund, mitigating the impact of large falls in investment values and interest rates.

Notes to the consolidated financial statements continued

38 – Financial guarantees and options continued**(c) Overseas life businesses**

In addition to guarantees written in the Group's UK life businesses, our overseas businesses have also written contracts containing guarantees and options. Details of the significant guarantees and options provided by overseas life businesses are set out below.

(i) France***Guaranteed surrender value and guaranteed minimum bonuses***

Aviva France has written a number of contracts with such guarantees. The guaranteed surrender value is the accumulated value of the contract including accrued bonuses. Bonuses are based on accounting income from amortised bond portfolios, where the duration of bond portfolios is set in relation to the expected duration of the policies, plus income and releases from realised gains on equity-type investments. Policy reserves are equal to guaranteed surrender values. Local statutory accounting envisages the establishment of a reserve, "Provision pour Aléas Financiers" (PAF), when accounting income is less than 125% of guaranteed minimum credited returns. No PAF was established at the end of 2006.

The most significant of these contracts is the AFER Eurofund which has total liabilities of £21 billion at 31 December 2006 (2005: £22 billion). The guaranteed bonus on this contract equals 65% of the average of the last two years' declared bonus rates (or 60% of the TME index rates if higher) and was 3.30% for 2006 (2005: 3.51%) compared with an accounting income from the fund of 4.81% (2005: 4.91%).

Non-AFER contracts with guaranteed surrender values had liabilities of £6 billion (2005: £7 billion) at 31 December 2006 and guaranteed annual bonus rates are between 0% and 4.5% on 98.3% of liabilities. For non-AFER business, the accounting income return exceeded guaranteed bonus rates in 2006.

Guaranteed death and maturity benefits

In France, the Group has also sold unit-linked policies where the death and/or maturity benefit is guaranteed to be at least equal to the premiums paid. The reserve held in the Group's consolidated balance sheet at the end of 2006 for this guarantee is £8 million (2005: £14 million). The reserve is calculated on a prudent basis and is in excess of the economic liability. At the end of 2006, total sums at risk for these contracts were £38 million (2005: £73 million) out of total unit-linked funds of £13 billion (2005: £8 billion). The average age of policyholders was approximately 53. It is estimated that this reserve would increase by £3 million (2005: £1 million) if yields were to decrease by 1% per annum and by £2 million (2005: £0.1 million) if equity markets were to decline by 10% from year end 2006 levels. These figures do not reflect our ability to review the tariff for this option.

(ii) Netherlands***Guaranteed minimum return at maturity***

In the Netherlands, it is market practice to guarantee a minimum return at maturity on traditional savings and pension contracts. Guarantees on older lines of business are 4% per annum while, for business written since 1 September 1999, the guarantee is 3% per annum. On Group pensions business, it is often possible to recapture guarantee costs through adjustments to surrender values or to premium rates.

On transition to IFRS, Delta Lloyd changed the reserving basis for most traditional contracts to reflect current market interest rates, for consistency with the reporting of assets at market value. The cost of meeting interest rate guarantees is allowed for directly in the liabilities. Although most traditional contracts are valued at market interest rate, the split by level of guarantee shown below is according to the original underlying guarantee.

The total liabilities for traditional business at 31 December 2006 are £8 billion (2005: £8 billion) analysed as follows:

	Liabilities 3% guarantee 31 December 2006 £m	Liabilities 3% guarantee 31 December 2005 £m	Liabilities 4% guarantee 31 December 2006 £m	Liabilities 4% guarantee 31 December 2005 £m
Individual	1,222	1,148	2,989	3,074
Group pensions	518	408	3,180	3,333
Total	1,740	1,556	6,169	6,407

Delta Lloyd has certain unit-linked contracts which provide a guaranteed minimum return at maturity from 4% pa to 2% pa. Provisions consist of unit values plus an additional reserve for the guarantee. The additional provision for the guarantee was £76 million (2005: £127 million). An additional provision of £43 million (2005: £77 million) in respect of investment return guarantees on group segregated fund business is held. It is estimated that the provision would increase by £163 million (2005: £293 million) if yields were to reduce by 1% pa and by £25 million (2005: £44 million) if equity markets were to decline by 10% from year end 2006 levels.

38 – Financial guarantees and options continued

(iii) Ireland

Guaranteed annuity options

Products with similar GAOs to those offered in the UK have been issued in Ireland. The current net of reinsurance provision for such options is £152 million (2005: £145 million). This has been calculated on a deterministic basis, making conservative assumptions for the factors which influence the cost of the guarantee, principally annuitant mortality and long-term interest rates.

These GAOs are “in the money” at current interest rates but the exposure to interest rates under these contracts has been hedged through the use of reinsurance, using derivatives (swaptions). The swaptions effectively guarantee that an interest rate of 5% will be available at the vesting date of these benefits so there is no exposure to a further decrease in interest rates.

“No MVR” guarantees

Certain unitised with-profit policies containing “no MVR” guarantees, similar to those in the UK, have been sold in Ireland.

These guarantees are currently “out-of-the-money” by £69 million (2005: £84 million). This has been calculated on a deterministic basis as the excess of the current policy surrender value over the discounted value (excluding terminal bonus) of the guarantees. The value of these guarantees is sensitive to the performance of investments held in the with-profit fund. Amounts payable under these guarantees are determined by the bonuses declared on these policies. It is estimated that the guarantees would be out-of-the-money by £74 million (2005: £74 million) if yields were to increase by 1% per annum and by £31 million (2005: £39 million) if equity markets were to decline by 10% from year end 2006 levels.

Return of premium guarantee

In 2005, Hibernian Life wrote two tranches of linked bonds with a return of premium guarantee after five or six years. The provision for these at the end of 2006 is £nil (2005: £3 million). It is expected that the provision would not increase if equity markets were to decline by 10% from year end 2006 levels. We would not expect any significant impact on this provision as a result of interest movements.

(iv) Spain and Italy

Guaranteed investment returns and guaranteed surrender values

The Group has also written contracts containing guaranteed investment returns and guaranteed surrender values in both Spain and Italy. Traditional profit-sharing products receive an appropriate share of the investment return, assessed on a book value basis, subject to a guaranteed minimum annual return of up to 6% in Spain and 4% in Italy on existing business, while on new business the maximum guaranteed rate is lower. Liabilities are generally taken as the face value of the contract plus, if required, an explicit provision for guarantees calculated in accordance with local regulations. At 31 December 2006, total liabilities for the Spanish business were £3 billion (2005: £2 billion) with a further reserve of £18 million (2005: £20 million) for guarantees. Total liabilities for the Italian business were £5 billion (2005: £4 billion), with a further provision of £46 million (2005: £55 million) for guarantees. Liabilities are most sensitive to changes in the level of interest rates. It is estimated that provisions for guarantees would need to increase by £66 million (2005: £66 million) in Spain and £9 million (2005: £12 million) in Italy if interest rates fell by 1% from end 2006 values. Under this sensitivity test, the guarantee provision in Spain is calculated conservatively, assuming a long-term market interest rate of 1.42% and no lapses or premium discontinuances.

(v) United States

Indexed and total return strategy products

In the United States, the Group writes indexed life and deferred annuity products. These products guarantee the return of principal to the policyholder and credit interest based on certain indices, primarily the Standard & Poor's 500 Composite Stock Price Index. A portion of each premium is used to purchase call options to hedge the growth in interest credited to the policyholder. The call options held by the Group and the options embedded in the policy are both carried at fair value. At 31 December 2006, the total liabilities for indexed products were £5.4 billion. If interest rates were to increase by 1%, the provision for embedded options would decrease by £51 million and, if interest rates were to decrease by 1%, the provision would increase by £56 million.

The Group has certain products that credit interest based on a total return strategy, whereby policyholders are allowed to allocate their premium payments to different asset classes within the general account. The Group guarantees a minimum return of premium plus approximately 3% interest over the term of the contracts. The linked general account assets are fixed maturity securities, and both the securities and the contract liabilities are carried at fair value. At 31 December 2006, the liabilities for total return strategy products were £408 million.

(d) Sensitivity

In providing these guarantees and options, the Group's capital position is sensitive to fluctuations in financial variables including foreign currency exchange rates, interest rates, real estate prices and equity prices. Interest rate guaranteed returns, such as those available on guaranteed annuity options (GAOs), are sensitive to interest rates falling below the guaranteed level. Other guarantees, such as maturity value guarantees and guarantees in relation to minimum rates of return, are sensitive to fluctuations in the investment return below the level assumed when the guarantee was made.

Notes to the consolidated financial statements continued

39 – Effect of changes in assumptions and estimates during the year

Certain estimates and assumptions used in determining liabilities for insurance and investment contract business were changed from 2005 to 2006, and had the following effect on the profit recognised for the year with an equivalent effect on liabilities. This disclosure only allows for the impact on liabilities and related assets, such as reinsurance, deferred acquisition costs and AVIF, and does not allow for offsetting movements in the value of backing financial assets.

	Effect on profit 2006 £m	Effect on profit 2005 £m
Assumptions		
Long-term insurance business		
Interest rates	947	(1,078)
Expenses	16	(12)
Persistency rates	45	3
Mortality for assurance contracts	25	25
Mortality for annuity contracts	60	(39)
Tax and other assumptions	(17)	(3)
Investment contracts		
Interest rates	23	(11)
Expenses	87	(6)
Persistency rates	2	–
Tax and other assumptions	(4)	(2)
General insurance and health business		
Change in loss ratio assumptions	(2)	2
Change in expense ratio assumptions	–	4
Total	1,182	(1,117)

The impact of interest rates for long-term business relates primarily to the UK and the Netherlands. This results from the use of higher valuation interest rates on annuities and other business, reflecting the rise in market interest rates over the year. The mortality impacts relate primarily to assumption changes in the UK and Ireland.

The impact on existing business of implementing FSA Policy Statement 06/14, *Prudential Changes for Insurers*, in 2006 is £132 million, arising mainly on expenses and persistency rates in both insurance and investment contracts. This is reflected in reductions in insurance contract liabilities of £800 million (see note 35(b)), investment contract liabilities of £105 million (see note 37(c)), reinsurance recoveries of £502 million (see note 36(c)) and deferred acquisition costs of £271 million (see note 25(b)). The impact on new business in 2006 is £17 million, giving a total increase in pre-tax profit for the year of £149 million.

40 – Tax assets and liabilities**(a) General**

Current tax assets and liabilities recoverable or payable in more than one year are £81 million and £842 million (2005: £78 million and £339 million) respectively.

(b) Deferred tax

(i) The balances at 31 December comprise:

	2006 £m	2005 £m
Deferred tax assets	1,199	1,018
Deferred tax liabilities	(3,077)	(2,458)
Net deferred tax liability	(1,878)	(1,440)

(ii) The net deferred tax liability arises on the following items:

	2006 £m	2005 £m
Long-term business technical provisions and other insurance items	1,247	1,155
Deferred acquisition costs	(126)	(245)
Unrealised gains on investments	(2,379)	(2,561)
Provisions and other temporary differences	(712)	(223)
Impairment of assets	2	1
Pensions and other post-retirement obligations	344	488
Unused losses and tax credits	250	57
Other temporary differences	(504)	(112)
Net deferred tax liability	(1,878)	(1,440)

40 – Tax assets and liabilities continued

(iii) The movement in the net deferred tax liability was as follows:

	2006 £m	2005 £m
Net liability at 1 January	(1,440)	(635)
Acquisition of subsidiaries	(182)	(36)
Amounts charged to profit (note 12a)	(199)	(965)
Amounts (charged)/credited to equity (note 12b)	(14)	262
Exchange differences	16	6
Other movements	(59)	(72)
Net liability at 31 December	(1,878)	(1,440)

The Group has unrecognised tax losses of £1,746 million (2005: £1,035 million) to carry forward against future taxable income of the necessary category in the companies concerned. These tax losses will expire as follows: £26 million 0-10 years and £26 million 11-20 years (2005: £40 million within 0-10 years and £35 million within 11-20 years). The remaining losses have no expiry date. In addition, the Group has an unrecognised capital loss of £468 million (2005: £446 million). This tax loss can be offset against future capital gains and has not been recognised in these financial statements. These capital losses of £29 million will expire within 0-10 years. The remaining capital losses have no expiry date. (2005: no expiry date).

Deferred tax liabilities of £527 million (2005: £347 million) have not been established for temporary differences associated with investments in subsidiaries and interests in joint ventures and associates (including tax payable on remittance of overseas retained earnings) because the Group can control the timing of the reversal of these differences and it is probable that they will not reverse in the foreseeable future. Such unremitted earnings totalled £2,552 million at 31 December 2006 (2005: £1,659 million).

41 – Provisions**(a) Carrying amounts**

	2006 £m	2005 £m
Deficits in the staff pension schemes (note 42d (v))	1,029	1,471
Other obligations to staff pension schemes – insurance policies issued by Group companies (note 35a)	1,086	875
Total IAS 19 obligations to staff pension schemes	2,115	2,346
Restructuring provision	234	36
Other provisions	501	493
Total	2,850	2,875

Of the total, £2,262 million (2005: £2,370 million) is expected to be settled more than one year after the balance sheet date.

(b) Movements during the year on restructuring and other provisions

	Restructuring provision £m	Other provisions £m	Total £m
At 1 January 2006	36	493	529
Additional provisions	246	87	333
Unused amounts reversed	–	(55)	(55)
Change in the discounted amount arising from passage of time	–	5	5
Charge to income statement	246	37	283
Utilised during the year	(47)	(116)	(163)
Acquisition of subsidiaries	–	98	98
Disposal of subsidiaries	–	(2)	(2)
Exchange differences	(1)	(9)	(10)
At 31 December 2006	234	501	735

Other provisions comprise many small provisions throughout the Group for obligations such as costs of compensation, litigation, staff entitlements and reorganisation.

Notes to the consolidated financial statements continued

42 – Pension obligations**(a) Introduction**

The Group operates a large number of pension schemes around the world, whose members receive benefits on either a defined benefit basis (generally related to a member's final salary and length of service) or a defined contribution basis (generally related to the amount invested, investment return and annuity rates). The only material defined benefit schemes are in the UK, the Netherlands, Canada and Ireland and, of these, the main UK scheme is by far the largest.

The assets of the main UK, Irish and Canadian schemes are held in separate trustee-administered funds to meet long-term pension liabilities to past and present employees. In the Netherlands, the main scheme is held in a separate foundation which invests in the life funds of the Group. In all schemes, the appointment of trustees of the funds is determined by their trust documentation, and they are required to act in the best interests of the funds' beneficiaries. The long-term investment objectives of the trustees and the employers are to limit the risk of the assets failing to meet the liabilities of the schemes over the long term, and to maximise returns consistent with an acceptable level of risk so as to control the long-term costs of these schemes.

An actuarial report has been submitted for each of the defined benefit schemes within the last three years, using appropriate methods for the respective countries on local funding bases.

(b) Main UK scheme

In the UK, the Group operates two main pension schemes, the Aviva Staff Pension Scheme (ASPS) and the smaller RAC (2003) Pension Scheme. New entrants join the defined contribution section of the ASPS, as the defined benefit section is closed to new employees. This scheme is operated by a trustee company, with 11 trustee directors, comprising representatives of the employers, staff, pensioners and an independent trustee (referred to below as the trustees).

(i) Defined benefit section of the ASPS

The Company works closely with the trustees who are required to consult it on the funding of the scheme and its investment strategy. At 31 March 2005, the date of the last actuarial valuation, this section of the scheme had an excess of obligations over available assets. The Company is currently discussing with the trustees the period over which it will aim to eliminate the funding deficit and will monitor funding levels on an annual basis.

The employing companies' contributions to the defined benefit section of the ASPS throughout 2006 were 35% of employees' pensionable salaries, together with the cost of redundancies during the year, and additional deficit funding payments totalling £200 million. As this section of the scheme is closed to new entrants and the contribution rate is determined using the projected unit credit method, it is expected that the percentage cost of providing future service benefits will continue to increase as the membership ages, leading to higher pension costs, and the number of members falls, leading to a higher charge per member. The employers' contribution rate for 2007 has therefore been increased to 37% of pensionable salaries (expected to be £120 million), pending finalisation of the April 2006 valuation. The Group is also expecting to make further contributions of some £400 million into the ASPS prior to March 2008. Active members of this section of the ASPS contribute 5% of their pensionable salaries.

In 2005, the Group's UK life business carried out an investigation into the allocation of costs in respect of funding the ASPS, to identify the deficit that arose in respect of accruals prior to the introduction of the current management services agreements (MSAs) and to propose a split between individual product companies based on an allocation of the deficit into pre-and post-MSA amounts. The results of this review were updated during 2006 and agreed by the relevant company boards and accepted by the UK regulator. Consequently, with effect from 1 January 2006, the Company's UK with-profit product companies are liable for a share, currently 12%, of the additional payments for deficit funding referred to above. This has resulted in a transfer of £130 million from the unallocated divisible surplus (UDS) to the income statement, to reflect the position at the start of the year, and a movement of £30 million back to the UDS via the statement of recognised income and expense to reflect actuarial movements in the deficit during the year and therefore a change in the amount recoverable from the with-profit product companies.

For funding purposes, the scheme's valuation as at 1 April 2006 is currently being completed, with the obligations calculated using the Projected Unit Method (which is described below).

(ii) Defined contribution (money purchase) section of the ASPS

The trustees have responsibility for selecting a range of suitable funds in which the members can choose to invest and for monitoring the performance of the available investment funds. Members are responsible for reviewing the level of contributions they pay and the choice of investment fund to ensure these are appropriate to their attitude to risk and their retirement plans. The employers' contribution rates for members of the defined contribution section throughout 2006 were 8% of pensionable salaries, together with further contributions up to 4% where members contribute, and the cost of the death-in-service benefits. These contribution rates are unchanged for 2007.

42 – Pension obligations continued**(c) Charges to the income statement**

The total pension costs of the Group's defined benefit and defined contribution schemes were:

	2006 £m	2005 £m
UK defined benefit schemes	150	141
UK defined contribution schemes	51	33
Overseas defined benefit schemes	63	17
Overseas defined contribution schemes	20	14
	284	205

There were no significant contributions outstanding or prepaid as at either 31 December 2006 or 2005.

(d) IAS 19 disclosures

Disclosures under IAS 19 for the material defined benefit schemes in the UK, the Netherlands, Canada and Ireland are given below. Where schemes provide both defined benefit and defined contribution pensions, the assets and liabilities shown exclude those relating to defined contribution pensions.

Excluding the deficit funding in the UK schemes discussed above, total employer contributions for these schemes in 2007 are expected to be £270 million.

(i) Assumptions on scheme liabilities

The inherent uncertainties affecting the measurement of scheme liabilities require these to be measured on an actuarial basis. This involves discounting the best estimate of future cash flows to be paid out by the scheme using the projected unit credit method. This is an accrued benefits valuation method which calculates the past service liability to members and makes allowance for their projected future earnings. It is based on a number of actuarial assumptions, which vary according to the economic conditions of the countries in which the relevant businesses are situated, and changes in these assumptions can materially affect the measurement of the pension obligations.

There are alternative methods of measuring liabilities, for example by calculating an accumulated benefit obligation (the present value of benefits for service already rendered but with no allowance for future salary increases) or on a solvency basis, using the cost of buying out benefits at a particular date with a suitable insurer. However, neither of these is considered appropriate in presenting fairly the Group's obligations to the members of its pension schemes on an ongoing basis.

The valuations used for accounting under IAS 19 have been based on the most recent full actuarial valuations, updated to take account of that standard's requirements in order to assess the liabilities of the material schemes at 31 December 2006. The updating was made by actuaries in each country who, other than the actuary of the Aviva Staff Pension Scheme and Dutch arrangements, were independent of the Group. Scheme assets are stated at their fair values at 31 December 2006.

The main actuarial assumptions used to calculate scheme liabilities under IAS 19 are:

	UK		Netherlands		Canada		Ireland	
	2006	2005	2006	2005	2006	2005	2006	2005
Inflation rate	3.1%	2.8%	1.9%	1.4%	2.5%	2.5%	2.25%	2.0%
General salary increases	4.9%	4.6%	2.4%*	1.4%*	3.75%	3.75%	4.0%	3.75%
Pension increases	3.1%	2.8%	1.9%	1.4%	1.25%	1.25%	2.15%	1.9%
Deferred pension increases	3.1%	2.8%	1.9%	1.4%	0%	0%	2.15%	1.9%
Discount rate	5.1%	4.8%	4.6%	4.0%	5.0%	5.0%	4.7%	4.2%
Basis of discount rate	AA-rated corporate bonds		AA-rated corporate bonds		AA-rated corporate bonds		AA-rated Eurozone corporate bonds	

* Age-related scale increases plus 2.4% (2005: 1.4%).

The discount rate and inflation rate are the two assumptions that have the largest impact on the value of the liabilities, with the difference between them being known as the net discount rate. For each country, the discount rate is based on current average yields of high quality debt instruments taking account of the maturities of the defined benefit obligations. A 1% increase in this rate (and therefore the net discount rate) would reduce the liabilities by £1.7 billion.

Notes to the consolidated financial statements continued

42 – Pension obligations continued

Mortality assumptions are significant in measuring the Group's obligations under its defined benefit schemes, particularly given the maturity of these obligations in the material schemes. The mortality tables and average life expectancy used at 31 December 2006 for scheme members are as follows:

Country of scheme	Mortality table	Normal retirement age (NRA)	Life expectancy at NRA of a male		Life expectancy at NRA of a female	
			Currently aged NRA	20 years younger than NRA	Currently aged NRA	20 years younger than NRA
UK	PA92 (calendar year 2007) with a one year age rating deduction and an allowance for future improvements	60	27.7	28.9	30.6	31.7
Netherlands	Coll 2003	65	17.0	17.0	20.4	20.4
Canada	UP1994 projected to 2005, using Scale AA	65	18.2	18.2	21.2	21.2
Ireland	PA92c2015 (current pensioners)/2030 (future pensioners)	60	23.6	24.8	26.6	27.7

The above tables used to measure post-retirement mortality are considered appropriate based on the mortality experience of the schemes. However, the extent of future improvements in longevity is subject to considerable uncertainty and judgement is required in setting this assumption. In the UK schemes, which are by far the most material to the Group, the assumptions include an allowance for future mortality improvement, based on the actuarial profession's medium cohort projection table. In the main UK scheme, the effect of assuming all members were one year younger would increase the schemes' liabilities by £200 million.

The scheme liabilities have an average duration of 22 years in the UK schemes and between 14 and 16 years in the overseas schemes.

(ii) Assumptions on scheme assets

The expected rates of return on the schemes' assets are:

	UK		Netherlands		Canada		Ireland	
	2007	2006	2007	2006	2007	2006	2007	2006
Equities	8.0%	8.0%	6.5%	6.3%	7.8%	8.0%	7.5%	7.5%
Bonds	4.75%	4.45%	4.0%	3.6%	4.5%	4.4%	4.1%	3.6%
Property	6.0%	5.95%	6.2%	5.3%	n/a	n/a	5.5%	5.0%
Other	5.3%	4.1%	4.0%	3.6%	n/a	n/a	n/a	n/a

The overall rates of return are based on the expected returns within each asset category and on current asset allocations. The expected returns are developed in conjunction with external advisers and take into account both current market expectations of future returns, where available, and historical returns.

Plan assets in the UK and Dutch schemes include insurance policies with other Group companies. Where these policies are in segregated funds with specific asset allocations, their expected rates of return are included in the appropriate line in the table above.

(iii) Pension expense

As noted above, plan assets in the UK and Dutch schemes include insurance policies with other Group companies. To avoid double-counting of investment income on scheme assets and the assets backing the underlying policies, adjustments have been made to the former in the current year as shown in the tables below.

42 – Pension obligations continued

The total pension expense for these schemes comprises:

	2006 £m	2005 £m
Current service cost	196	158
Past service cost/(credit)	3	(7)
(Gain)/loss on curtailments	(39)*	(21)
Total pension cost	160	130
Charged to net operating expenses	196	130
Included in profit on disposal of subsidiaries and associates	(36)*	–
Total pension cost as above	160	130
Expected return on scheme assets	(530)	(439)
Less: Income accounted for elsewhere (see above)	40	–
	(490)	(439)
Interest charge on scheme liabilities	453	407
Credit to investment income	(37)	(32)
Total charge to income	123	98
Expected return on scheme assets	530	439
Actual return on these assets	(800)	(1,270)
Actuarial (gains) on scheme assets	(270)	(831)
Less: Gains accounted for elsewhere (see above)	19	–
	(251)	(831)
Experience (gains)/losses arising on scheme liabilities	(63)	86
Changes in assumptions underlying the present value of the scheme liabilities	430	1,292
Loss on acquisitions	1	–
Actuarial losses on the pension schemes	117	547
Less: Recoveries from unallocated divisible surplus and other movements	(3)	–
Actuarial losses recognised in the statement of recognised income and expense	114	547

* The current year credit mainly arises in the UK as a result of the remeasurement of pension liabilities in the RAC plc defined benefit scheme, following the MSS and LVL disposals (see note 3(b)).

The cumulative amount of actuarial gains and losses on the pension schemes recognised in the statement of recognised income and expenses since 1 January 2004 (the date of transition to IFRS) is a loss of £809 million at 31 December 2006 (2005: loss of £692 million).

(iv) Experience gains and losses

The following disclosures of experience gains and losses will be built up over time to give a five year history. These are based on the assets recorded in the schemes, before Group consolidation adjustments to remove insurance policies with Group companies and income on the assets underlying them.

	2006		2005		2004	
	£m	%	£m	%	£m	%
Fair value of scheme assets at the end of the year	9,223		8,209		6,286	
Present value of scheme liabilities at the end of the year	(10,196)		(9,680)		(7,179)	
Deficits in the schemes	(973)		(1,471)		(893)	
Difference between the expected and actual return on scheme assets						
Amount of (gains)/losses	(270)		(831)		(205)	
Percentage of the scheme assets at the end of the year		2.9%		10.1%		3.3%
Experience (gains)/losses on scheme liabilities (excluding changes in assumptions)						
Amount of (gains)/losses	(63)		86		(12)	
Percentage of the present value of scheme liabilities		0.6%		0.9%		0.2%

Notes to the consolidated financial statements continued

42 – Pension obligations continued

Excluding insurance policies with Group companies and income on the assets underlying them, the relevant figures are:

	2006		2005		2004	
	£m	%	£m	%	£m	%
Fair value of scheme assets at the end of the year	8,137		7,334		5,473	
Present value of scheme liabilities at the end of the year	(10,196)		(9,680)		(7,179)	
Deficits in the schemes	(2,059)		(2,346)		(1,706)	
Difference between the expected and actual return on scheme assets						
Amount of (gains)/losses	(251)		(798)		(184)	
Percentage of the scheme assets at the end of the year		3.1%		10.9%		3.4%
Experience (gains)/losses on scheme liabilities (excluding changes in assumptions)						
Amount of (gains)/losses	(63)		86		(12)	
Percentage of the present value of scheme liabilities		0.6%		0.9%		0.2%

(v) Scheme deficits and surpluses

The assets and liabilities of the schemes, attributable to defined benefit members, including investments in Group insurance policies (see footnote below), at 31 December 2006 were:

	UK		Netherlands		Canada		Ireland		Total	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m
Equities	4,682	4,251	310	223	129	141	249	235	5,370	4,850
Bonds	2,046	1,660	498	495	75	83	163	154	2,782	2,392
Property	581	480	46	36	–	–	25	22	652	538
Other	318	336	80	78	2	2	19	13	419	429
Total fair value of assets	7,627	6,727	934	832	206	226	456	424	9,223	8,209
Present value of scheme liabilities	(8,601)	(8,098)	(944)	(876)	(251)	(288)	(400)	(418)	(10,196)	(9,680)
(Deficits)/surplus in the schemes	(974)	(1,371)	(10)	(44)	(45)	(62)	56	6	(973)	(1,471)

The current year surplus in the Irish schemes of £56 million is included in Other assets (see note 25), whilst the deficits in the other schemes of £1,029 million are included in Provisions (see note 41).

Plan assets in the table above include investments in Group-managed funds in the consolidated balance sheet of £336 million (2005: £578 million) in the UK scheme, and insurance policies of £152 million and £934 million (2005: £143 million and £732 million) in the UK and Dutch schemes respectively. Where the investment and insurance policies are in segregated funds with specific asset allocations, they are included in the appropriate line in the table above, otherwise they appear in "Other". The Dutch insurance policies are backed by all the assets in the relevant column above, whilst the UK policies are included in "Other". These insurance policies, totalling £1,086 million (2005: £875 million) are considered non-transferable under the terms of IAS 19 and so have been treated as other obligations to staff pension schemes within provisions (see note 41).

42 – Pension obligations continued

Excluding these policies, the total IAS 19 obligations to the schemes are £2,059 million (2005: £2,346 million), as shown in the following table.

	UK		Netherlands		Canada		Ireland		Total	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m
Equities	4,682	4,251	–	–	129	141	249	235	5,060	4,627
Bonds	2,046	1,660	–	22	75	83	163	154	2,284	1,919
Property	581	480	–	–	–	–	25	22	606	502
Other	166	193	–	78	2	2	19	13	187	286
Total fair value of assets	7,475	6,584	–	100	206	226	456	424	8,137	7,334
Present value of scheme liabilities	(8,601)	(8,098)	(944)	(876)	(251)	(288)	(400)	(418)	(10,196)	(9,680)
IAS 19 (deficits)/surplus in the schemes	(1,126)	(1,514)	(944)	(776)	(45)	(62)	56	6	(2,059)	(2,346)
Included in other assets (note 25)	–	–	–	–	–	–	56	–	56	–
Included in provisions (note 41)	(1,126)	(1,514)	(944)	(776)	(45)	(62)	–	6	(2,115)	(2,346)
	(1,126)	(1,514)	(944)	(776)	(45)	(62)	56	6	(2,059)	(2,346)

As noted above, the long-term investment objectives of the trustees and the employers are to limit the risk of the assets failing to meet the liabilities of the schemes over the long term, and to maximise returns consistent with an acceptable level of risk so as to control the long-term costs of these schemes. To meet these objectives, each scheme's assets are invested in a diversified portfolio, consisting primarily of equity and debt securities. These reflect the current long-term asset allocation ranges chosen having regard to the structure of liabilities within the schemes.

(vi) Movements in the scheme deficits and surpluses

Movements in the pension schemes' deficits and surpluses comprise:

	2006				2005
	Scheme assets £m	Scheme liabilities £m	Pension scheme deficit £m	Adjust for Group insurance policies £m	IAS19 pension deficit £m
Deficits in the schemes at 1 January	8,209	(9,680)	(1,471)	(875)	(1,706)
Employer contributions	554	–	554	(94)	341
Employee contributions	24	(24)	–	(3)	(1)
Benefits paid	(313)	313	–	30	29
Current and past service cost (see (iii) above)	(4)	(195)	(199)	–	(151)
Gains on curtailments (see (iii) above)	–	39	39	–	21
Credit/(charge) to investment income (see (iii) above)	530	(453)	77	(40)	(3)
Acquisitions	4	(5)	(1)	–	(313)
Other actuarial gains/(losses) (see (iii) above)	270	(267)	3	(119)	(580)
Buy-outs and other transfers	2	16	18	(2)	–
Exchange rate movements on foreign plans	(53)	60	7	17	17
Deficits in the schemes at 31 December	9,223	(10,196)	(973)	(1,086)	(2,346)

The change in the pension schemes' deficits during 2006 is mainly attributable to additional contributions into the schemes and an increase in the market value of their assets, partially offset by changes in assumptions underlying the present value of the schemes' liabilities. In the UK, the value of the liabilities has increased due to a strengthening to the post-retirement mortality assumptions and higher assumed inflation, partially offset by an increase in the corporate bond yields used for the valuation discount rate. The increase in scheme assets is primarily due to an improvement in equity values since the previous year end, partially offset by a reduction in bond values, together with deficit contribution payments made by the employing companies.

Notes to the consolidated financial statements continued

43 – Borrowings**(a) Carrying amounts**

The following table provides information about the maturity periods of the Group's borrowings.

Borrowings are considered current if the contractual maturity dates are within a year.

			Maturity dates of undiscounted cashflows					2006
	Carrying value £m	Denominated currency	Within 1 year £m	1-5 years £m	5-10 years £m	10-15 years £m	Over 15 years £m	Total £m
Subordinated debt								
6.125% £700 million subordinated notes 2036	689	£	—	—	—	—	700	700
5.750% €800 million subordinated notes 2021	537	€	—	—	—	539	—	539
5.250% €650 million subordinated notes 2023	434	€	—	—	—	—	438	438
5.700% €500 million undated subordinated notes	334	€	—	—	—	—	337	337
6.125% £800 million undated subordinated notes	790	£	—	—	—	—	800	800
Floating rate US\$300 million subordinated notes 2017	153	US\$	—	—	—	153	—	153
	2,937		—	—	—	692	2,275	2,967
Debenture loans								
9.5% guaranteed bonds 2016	198	£	—	—	200	—	—	200
2.5% subordinated perpetual loan notes	116	€	—	—	—	—	330	330
5.95% senior notes 2015	165	Various	165	—	—	—	—	165
Other loans	165	Various	1	31	—	105	28	165
	644		166	31	200	105	358	860
Amounts owed to credit institutions								
Bank loans	751	Various	272	107	89	9	274	751
Commercial paper	737	Various	737	—	—	—	—	737
Securitised mortgage loan notes								
UK lifetime mortgage business	1,835	£	—	—	—	—	1,721	1,721
Dutch domestic mortgage business	5,233	€	—	—	—	—	5,233	5,233
	7,068		—	—	—	—	6,954	6,954
Total	12,137		1,175	138	289	806	9,861	12,269
Contractual undiscounted interest payments			603	2,126	2,658	2,491	9,939	17,817
Total contractual undiscounted cash flows			1,778	2,264	2,947	3,297	19,800	30,086

43 – Borrowings continued

	Carrying value £m	Denominated currency	Maturity dates of undiscounted cashflows					2005
			Within 1 year £m	1-5 years £m	5-10 years £m	10-15 years £m	Over 15 years £m	Total £m
Subordinated debt								
6.125% £700 million subordinated notes 2036	689	£	—	—	—	—	700	700
5.750% €800 million subordinated notes 2021	548	€	—	—	—	—	550	550
5.250% €650 million subordinated notes 2023	442	€	—	—	—	—	447	447
5.700% €500 million undated subordinated notes	340	€	—	—	—	—	344	344
6.125% £800 million undated subordinated notes	789	£	—	—	—	—	800	800
	2,808		—	—	—	—	2,841	2,841
Debenture loans								
9.5% guaranteed bonds 2016	198	£	—	—	—	200	—	200
2.5% subordinated perpetual loan notes	119	€	—	—	—	—	337	337
Other loans	17	Various	—	—	17	—	—	17
	334		—	—	17	200	337	554
Amounts owed to credit institutions								
Bank loans	1,065	Various	35	269	761	—	—	1,065
Commercial paper	503	Various	503	—	—	—	—	503
Securitised mortgage loan notes								
UK lifetime mortgage business	1,879	£	—	—	—	—	1,751	1,751
Dutch domestic mortgage business	4,424	€	—	—	—	—	4,424	4,424
	6,303		—	—	—	—	6,175	6,175
Total	11,013		538	269	778	200	9,353	11,138
Contractual undiscounted interest payments			518	1,971	2,195	2,070	7,255	14,009
Total contractual undiscounted cash flows			1,056	2,240	2,973	2,270	16,608	25,147

Where subordinated debt is undated or loan notes are perpetual, the interest payments have not been included beyond 15 years. Annual interest payments for these borrowings are £91 million (2005: £88 million).

Contractual undiscounted interest payments are calculated based on underlying fixed interest rates or prevailing market floating rates as applicable. Year end exchange rates have been used for interest projections on loans in foreign currencies.

All the above borrowings are stated at amortised cost, except for the loan notes issued in connection with the UK lifetime mortgage business which are carried at fair value. These have been designated at fair value through profit and loss in order to present the relevant mortgages, borrowings and derivative financial instruments at fair value, since they are managed as a portfolio. This presentation provides more relevant information and eliminates any accounting mismatch.

Notes to the consolidated financial statements continued

43 – Borrowings continued**(b) Description and features****(i) Subordinated debt**

A description of each of the subordinated notes is set out in the table below:

Notional amount	Issue date	Redemption date	Callable at par at option of the Company from	In the event the Company does not call the notes, the coupon will reset at each applicable reset date to
£700 million	14 Nov 2001	14 Nov 2036	16 Nov 2026	5 year Benchmark Gilt + 2.85%
€800 million	14 Nov 2001	14 Nov 2021	14 Nov 2011	3 month Euribor + 2.12%
€650 million	29 Sep 2003	02 Oct 2023	02 Oct 2013	3 month Euribor + 2.08%
€500 million	29 Sep 2003	Undated	29 Sep 2015	3 month Euribor + 2.35%
£800 million	29 Sep 2003	Undated	29 Sep 2022	5 year Benchmark Gilt + 2.40%
US\$300 million	19 Dec 2006	19 Jun 2017	19 Jun 2012	US LIBOR + 0.84%

The subordinated notes were issued by the Company. They rank below its senior obligations and ahead of its preference shares and ordinary share capital. The dated subordinated notes rank ahead of the undated subordinated notes. The fair value of these notes at 31 December 2006 was £3,076 million (2005: £3,148 million), calculated with reference to quoted prices.

(ii) Debenture loans

The 9.5% guaranteed bonds were issued by the Company at a discount of £1.1 million. This discount and the issue expenses are being amortised over the full term of the bonds. Although these bonds were issued in sterling, the loans have effectively been converted into euro liabilities through the use of financial instruments in a subsidiary.

The 2.5% perpetual subordinated loan notes were issued by a Dutch subsidiary to finance the acquisition of NUTS OHRA Beheer BV in 1999. They are convertible into ordinary shares in Delta Lloyd NV, should there be a public offering of those shares. These loan notes have a face value of €489.9 million but, because they are considered to be perpetual, their carrying value is €172.4 million, calculated in 1999 and based on the future cash flows in perpetuity discounted back at a market rate of interest. The rate of interest paid on the notes is being gradually increased to a maximum of 2.76% in 2009.

The 5.95% Senior Notes had been issued by a United States subsidiary prior to acquisition by the Group. These notes may be redeemed at the Group's option at any time, in whole or in part, subject to payment of a redemption premium. On 23 February 2007, the subsidiary exercised its option to redeem the notes early for an amount not significantly different to their carrying value. As a result, these notes have been shown in table (a) as maturing within one year.

Other loans comprise borrowings in the United States and the Netherlands.

Fixed rate borrowings comprise £535 million (2005: £317 million) of the total carrying value of £644 million (2005: £334 million).

The fair value of debenture loans at 31 December 2006 was £703 million (2005: £405 million), calculated with reference to quoted prices or discounted future cash flows as appropriate.

(iii) Bank loans

In September 2004, one of the Group's UK long-term business subsidiaries, Norwich Union Life & Pensions Limited (NULAP), entered into a securitisation arrangement with The Royal Bank of Scotland Group plc (RBSG), to provide funding to cover initial new business acquisition and administration costs. Under the arrangement, an RBSG company has provided a loan facility of £200 million to NULAP in respect of selected term assurance policies, secured on future premiums and repayment of commissions due from brokers where a policy has lapsed. The funding is repayable over four years from the date of advance, and interest is charged at a floating rate. RBSG has no recourse to the policyholder or shareholders' funds of any companies in the Aviva Group. The balance drawn on the facility at 31 December 2006 was £200 million (2005: £191 million). On 12 January 2007, under a Deed of Release and Termination, this arrangement was cancelled.

As explained in note 17b, the UK long-term business policyholder funds have invested in a number of property limited partnerships (PLPs). The PLPs have raised external debt, secured on their respective property portfolios, and the lenders are only entitled to obtain payment of both interest and principal to the extent there are sufficient resources in the respective PLPs. The lenders have no recourse whatsoever to the policyholder or shareholders' funds of any companies in the Aviva Group. Loans of £259 million (2005: £156 million) included in the tables relate to those PLPs which have been consolidated as subsidiaries.

The fair value of these loans is considered to be the same as their carrying value.

(iv) Commercial paper

The commercial paper consists of £733 million in the Company (2005: £499 million) and £4 million in France (2005: £4 million).

All commercial paper is repayable within one year and is issued in a number of different currencies, primarily sterling, euros and US dollars.

The fair value of the commercial paper is considered to be the same as its carrying value.

43 – Borrowings continued**(v) Securitised mortgage loan notes**

Loan notes have been issued by special purpose securitisation companies in the UK and the Netherlands. Details of these securitisations are given in note 22.

For the Dutch securitised mortgage loan notes carried at amortised cost of £5,233 million (2005: £4,424 million) their fair value is £5,271 million (2005: £4,508 million), calculated based on the future cash flows discounted back at the market rate of interest.

(c) Movements during the year

Movements in borrowings during the year were:

	2006 £m	2005 £m
New borrowings drawn down, net of expenses	6,119	5,441
Repayment of borrowings	(5,218)	(4,585)
Net cash inflow	901	856
Foreign exchange rate movements	(183)	(170)
Borrowings acquired for non-cash consideration	11	–
Acquisitions	442	173
Fair value movements	(52)	62
Amortisation of discounts and other non-cash items	5	2
Movements in the year	1,124	923
Balance at 1 January	11,013	10,090
Balance at 31 December	12,137	11,013

All movements in fair value in 2006 and 2005 on securitised mortgage loan notes designated as fair value through profit or loss were attributable to changes in market conditions. These loan notes have external credit ratings which have not changed since the inception of the loans.

(d) Undrawn borrowings

The Group has the following undrawn committed central borrowing facilities available to it, of which £1,000 million (2005: £1,000 million) is used to support the commercial paper programme:

	2006 £m	2005 £m
Expiring within one year	1,180	890
Expiring beyond one year	980	1,360
	2,160	2,250

44 – Payables and other financial liabilities

	2006 £m	2005 £m
Payables arising out of direct insurance	1,389	1,639
Payables arising out of reinsurance operations	408	618
Deposits received from reinsurers	1,244	883
Loans from associates	–	3
Bank overdrafts	696	690
Derivative liabilities	355	526
Bank customer accounts	2,008	2,317
Bank deposits received from other banks	1,013	565
Other financial liabilities	2,122	2,340
Less: Amounts classified as held for sale	–	(96)
	9,235	9,485
Expected to be settled within one year	8,200	7,384
Expected to be settled in more than one year	1,035	2,101
	9,235	9,485

Bank overdrafts arise substantially from unpresented cheques and amount to £266 million (2005: £115 million) in long-term business operations and £430 million (2005: £575 million) in general business and other operations. Other financial liabilities include the obligation to repay £722 million (2005: £467 million) received under stock repurchase arrangements entered into in the UK and the Netherlands.

Notes to the consolidated financial statements continued

45 – Other liabilities

	2006 £m	2005 £m
Deferred income	265	265
Reinsurers' share of deferred acquisition costs	221	146
Accruals	1,138	1,096
Other liabilities	2,610	1,862
Less: Amounts classified as held for sale	–	(49)
	4,234	3,320
Expected to be settled within one year	3,468	2,539
Expected to be settled in more than one year	766	781
	4,234	3,320

46 – Contingent liabilities and other risk factors**(a) Uncertainty over claims provisions**

Note 35 gives details of the estimation techniques used in determining the general business outstanding claims provisions and of the methodology and assumptions used in determining the long-term business provisions, which are designed to allow for prudence and the appropriate cost of future policy-related liabilities. Both are estimated to give a result within the normal range of outcomes. To the extent that the ultimate cost falls outside this range, for example where experience is worse than that assumed, or future general business claims inflation differs from that expected, there is uncertainty in respect of this liability.

(b) Asbestos, pollution and social environmental hazards

In the course of conducting insurance business, various companies within the Group receive general insurance liability claims, and become involved in actual or threatened litigation arising therefrom, including claims in respect of pollution and other environmental hazards. Amongst these are claims in respect of asbestos production and handling in various jurisdictions, including the UK, Australia and Canada. Given the significant delays that are experienced in the notification of these claims, the potential number of incidents which they cover and the uncertainties associated with establishing liability and the availability of reinsurance, the ultimate cost cannot be determined with certainty. However, the Group's net exposure to such liabilities is not significant and, on the basis of current information and having regard to the level of provisions made for general insurance claims, the directors consider that any costs arising are not likely to have a material impact on the financial position of the Group.

(c) Guarantees on long-term savings products

Note 38 gives details of guarantees and options given by various Group companies as a normal part of their operating activities, in respect of certain long-term insurance and fund management products. In the UK, in common with other pension and life policy providers, the Group wrote individual and group pension policies in the 1970s and 1980s with a guaranteed annuity rate option (GAO). Since 1993, such policies have become more valuable to policyholders, and more costly for insurers, as current annuity rates have fallen in line with interest rates and improving longevity. Reserving policies for the cost of GAOs varied until a ruling by the House of Lords in the Equitable Life case in 2000 which effectively required full reserving by all companies. Prior to the ruling, consistent with the Group's ordinary reserving practice in respect of such obligations, full reserves for GAOs had already been established. No adjustment was made, or was necessary, to the Group's reserving practice as a result of the ruling. The directors continue to believe that the existing provisions are sufficient.

(d) Pensions mis-selling

The pensions review of past sales of personal pension policies which involved transfers, opt outs and non-joiners from occupational schemes, as required by the Financial Services Authority (FSA), has largely been completed. A provision of some £31 million (2005: £42 million) remains to meet the outstanding costs of the very few remaining cases, the anticipated cost of any guarantees provided, and potential levies payable to the Financial Services Compensation Scheme. It continues to be the directors' view that there will be no material effect either on the Group's ability to meet the expectations of policyholders or on shareholders.

(e) Endowment reviews

In December 1999, the FSA announced the findings of its review of mortgage endowments and expressed concern as to whether, given decreases in expected future investment returns, such policies could be expected to cover full repayment of mortgages. A key conclusion was that, on average, holders of mortgage endowments had enjoyed returns such that they had fared at least as well as they would have done without an endowment. Nevertheless, following the FSA review, all of the Group's UK mortgage endowment policyholders received policy-specific letters advising them whether their investment was on track to cover their mortgage.

In May 2002, in accordance with FSA requirements, the Group commenced sending out the second phase of endowment policy update letters, which provide policyholders with information about the performance of their policies and advice as to whether these show a projected shortfall at maturity. The Group will send these updates annually to all mortgage endowment holders, in accordance with FSA requirements. The Group has made provisions totalling £128 million (2005: £195 million) to meet potential mis-selling costs and the associated expenses of investigating complaints. It continues to be the directors' view that there will be no material effect either on the Group's liability to meet the expectations of policyholders or on shareholders.

46 – Contingent liabilities and other risk factors continued

In August 2004, the Group confirmed its intention to introduce time barring on mortgage endowment complaints, under FSA rules. The Group now includes details of its endowment policyholders' time bar position within the annual reprojection mailings. Customers will be given at least 12 months individual notice before a time bar becomes applicable – double the six months' notice required by the FSA.

(f) Other

In the course of conducting insurance and investment business, various Group companies receive liability claims, and become involved in actual or threatened litigation arising therefrom. In the opinion of the directors, adequate provisions have been established for such claims and no material loss will arise in this respect.

The Company and several of its subsidiaries have guaranteed the overdrafts and borrowings of certain other Group companies. The total exposure of the Group and Company is £7 million (2005: £7 million) and £109 million (2005: £109 million) respectively but, in the opinion of the directors, no material loss will arise in respect of these guarantees and indemnities.

In addition, in line with standard business practice, various Group companies have been given guarantees, indemnities and warranties in connection with disposals in recent years of subsidiaries and associates to parties outside the Aviva Group. In the opinion of the directors, no material loss will arise in respect of these guarantees, indemnities and warranties.

47 – Commitments**(a) Capital commitments**

Contractual commitments for acquisitions or capital expenditures of investment property, property and equipment and intangible assets, which have not been recognised in the financial statements, are as follows:

	2006 £m	2005 £m
Investment property	135	10
Property and equipment	152	169
	287	179

Contractual obligations for future repairs and maintenance on investment properties are £3 million (2005: £8 million).

The Group has capital commitments to its joint ventures of £nil (2005: £34 million) and to other investment vehicles of £14 million (2005: £nil).

(b) Operating lease commitments

(i) Future contractual aggregate minimum lease rentals receivable under non-cancellable operating leases are as follows:

	2006 £m	2005 £m
Within 1 year	12	26
Later than 1 year and not later than 5 years	33	44
Later than 5 years	23	13
	68	83

(ii) Future contractual aggregate minimum lease payments under non-cancellable operating leases are as follows:

	2006 £m	2005 £m
Within 1 year	108	109
Later than 1 year and not later than 5 years	386	393
Later than 5 years	873	914
	1,367	1,416
The total of future minimum sublease payments expected to be received under non-cancellable subleases	200	200

Notes to the consolidated financial statements continued

48 – Cash flow statement

(a) The reconciliation of profit/(loss) before tax to the net cash inflow from operating activities is:

	2006 £m	2005 £m
Profit before tax	3,323	3,450
Adjustments for:		
Share of profits of joint ventures and associates	(485)	(340)
Dividends received from joint ventures and associates	71	95
Profit on sale of investment property	(46)	(41)
Profit on sale of property and equipment	(2)	(2)
Profit on sale of subsidiaries, joint ventures and associates	(222)	(153)
Profit on sale of investments	(5,334)	(4,616)
Fair value gains on investment property	(1,507)	(1,571)
Fair value losses/(gains) on investments	790	(8,813)
Fair value (gains)/losses on borrowings	(52)	62
Depreciation of property and equipment	122	112
Equity compensation plans, equity settled expense	48	22
Impairment of goodwill on subsidiaries	94	43
Impairment of other investments and loans	(5)	19
Impairment of acquired value of in-force business and intangibles	26	35
Impairment of non financial assets	5	38
Amortisation of premium or discount on debt securities	278	(93)
Amortisation of premium or discount on loans	–	(38)
Amortisation of premium or discount on borrowings	5	2
Amortisation of acquired value of in-force business and intangibles	130	65
Change in unallocated divisible surplus	558	1,474
Interest expense on borrowings	825	607
Finance income on pension deficit	(77)	(32)
Foreign currency exchange gain/loss	(99)	203
Changes in working capital		
(Increase)/decrease in reinsurance assets	966	1,192
(Increase)/decrease in deferred acquisition costs	51	(466)
(Increase)/decrease in insurance liabilities and investment contracts	9,974	18,581
(Increase)/decrease in other assets and liabilities	(4,301)	135
Net purchases of operating assets		
Purchases of investment property	(1,888)	(1,956)
Proceeds on sale of investment property	1,587	1,292
Net purchases of financial investments	(2,380)	(6,522)
Cash generated from operations	2,455	2,784

Purchases and sales of investment property, loans and financial investments are included within operating cash flows as the purchases are funded from cash flows associated with the origination of insurance and investment contracts, net of payments of related benefits and claims.

48 – Cash flow statement continued

(b) Cash flows in respect of the acquisition of subsidiaries, joint ventures and associates

	2006 £m	2005 £m
Cash consideration for subsidiaries, joint ventures and associates acquired	2,321	1,478
Less: Cash and cash equivalents acquired with subsidiaries	(432)	(55)
Cash flows on acquisitions	1,889	1,423

(c) Cash flows in respect of the disposal of subsidiaries, joint ventures and associates

	2006 £m	2005 £m
Cash proceeds from disposal of subsidiaries, joint ventures and associates	616	464
Net cash and cash equivalents divested with subsidiaries	–	–
Cash flows on disposals	616	464

(d) Cash and cash equivalents in the Cash flow statement at 31 December comprised:

	2006 £m	2005 £m
Cash at bank and in hand	4,087	3,530
Cash equivalents	10,455	10,227
	14,542	13,757
Bank overdrafts	(696)	(690)
	13,846	13,067

Of the total cash and cash equivalents shown above, £nil has been classified as held for sale (2005: £25 million) (see note 3d).

Notes to the consolidated financial statements continued

49 – Capital statement

FRS 27 requires us to produce a capital statement which sets out the financial strength of our Group entities and provides an analysis of the disposition and constraints over the availability of capital to meet risks and regulatory requirements. The capital statement also provides a reconciliation of shareholders' funds to regulatory capital.

The analysis below sets out the Group's available capital resources.

Available capital resources

	CGNU with-profit fund £m	CULAC with-profit fund £m	NUL&P with-profit fund ³ £m	Total UK life with-profit funds £m	Other UK life operations £m	Total UK life operations £m	Overseas life operations £m	Total life operations £m	Other operations ⁴ £m	2006 Total £m	2005 Total £m
Total shareholders' funds	35	34	35	104	3,219	3,323	9,546	12,869	1,195	14,064	11,092
Other sources of capital ¹	–	–	–	–	200	200	153	353	2,737	3,090	2,941
Unallocated divisible surplus	2,211	2,264	2,303	6,778	–	6,778	2,687	9,465	–	9,465	8,978
Adjustments onto a regulatory basis:											
Shareholders' share of accrued bonus	(79)	(87)	(564)	(730)	–	(730)	–	(730)	–	(730)	(700)
Goodwill and other intangibles	–	–	–	–	(68)	(68)	(3,549)	(3,617)	(2,021)	(5,638)	(3,077)
Regulatory valuation and admissibility restrictions ²	381	268	49	698	(1,438)	(740)	453	(287)	(459)	(746)	(1,211)
Total available capital resources	2,548	2,479	1,823	6,850	1,913	8,763	9,290	18,053	1,452	19,505	18,023
Analysis of liabilities:											
Participating insurance liabilities	9,755	9,116	18,258	37,129	2,853	39,982	23,723	63,705	–	63,705	59,958
Unit-linked liabilities	–	–	–	–	6,221	6,221	14,783	21,004	–	21,004	17,999
Other non-participating life insurance	1,157	1,857	705	3,719	13,557	17,276	24,239	41,515	–	41,515	36,219
Total insurance liabilities	10,912	10,973	18,963	40,848	22,631	63,479	62,745	126,224	–	126,224	114,176
Participating investment liabilities	2,001	2,413	7,833	12,247	2,817	15,064	34,336	49,400	–	49,400	47,258
Non-participating investment liabilities	53	18	–	71	22,840	22,911	16,047	38,958	–	38,958	30,051
Total investment liabilities	2,054	2,431	7,833	12,318	25,657	37,975	50,383	88,358	–	88,358	77,309
Total liabilities	12,966	13,404	26,796	53,166	48,288	101,454	113,128	214,582	–	214,582	191,485

1. Other sources of capital include Subordinated debt of £2,937 million issued by Aviva and £153 million of other qualifying capital issued by Dutch, Italian and US subsidiary undertakings.

2. Including an adjustment for minorities.

3. Includes the Provident Mutual with-profit fund.

4. Other operations include general insurance and fund management business.

The regulatory and valuation admissibility restrictions for 2005 have been changed following a revised application of the technical rules. This has increased total capital resources by £4.4 billion, all attributable to life operations.

49 – Capital statement continued
Analysis of movements in capital
For the year ended 31 December 2006

	CGNU with-profit fund £m	CULAC with-profit fund £m	NUL&P with-profit fund £m	Total UK life with-profit funds £m	Other UK life operations £m	Total UK life operations £m	Overseas life operations £m	Total life operations £m
Opening available capital resources	2,103	1,941	1,249	5,293	2,044	7,337	8,677	16,014
Effect of new business	(56)	(49)	–	(105)	(351)	(456)	(163)	(619)
Expected change in available capital resources	106	185	404	695	338	1,033	471	1,504
Variance between actual and expected experience	293	288	(4)	577	4	581	(490)	91
Effect of operating assumption changes	75	159	51	285	478	763	(27)	736
Effect of economic assumption changes	136	151	383	670	54	724	48	772
Effect of changes in management policy	(53)	(83)	(143)	(279)	–	(279)	(7)	(286)
Transfers, acquisitions and disposals	–	–	–	–	–	–	617	617
Foreign exchange movements	–	–	–	–	–	–	(202)	(202)
Other movements	(56)	(113)	(117)	(286)	(654)	(940)	366	(574)
Closing available capital resources	2,548	2,479	1,823	6,850	1,913	8,763	9,290	18,053

Further analysis of the movement in the liabilities of the long-term business can be found in notes 35 and 37.

The analysis of movements in capital provides an explanation of the movement in available capital of the Group's life business for the year. This analysis is intended to give an understanding of the underlying causes of changes in the available capital of the Group's life business, and provides a distinction between some of the key factors affecting the available capital.

For the UK with-profit funds, the increase in available capital has been driven by the favourable economic environment. Equity performance was positive, which had a direct effect on the equity content of the estate assets and an indirect impact from the reduction in maturity guarantee costs. Fixed interest yields have generally increased. Although this has led to capital depreciation of fixed interest assets it also resulted in a reduction of guarantee costs, with the increase in yield having a net benefit to the estates of all the funds. Also, the implied market volatility for equities has reduced, which lowers the assumed future asset share volatility, particularly in CGNU and CULAC, and consequently guarantee costs are reduced.

The changes in management policy relate to the review of bonus rates for with-profit business.

The capital position of the Other UK life operations was augmented by changes to reserving for UK non-profit business permitted under the FSA Policy Statement PS06/14 *Prudential Changes for Insurers*, as outlined in Note 35(b), which are included in operating assumption changes.

For the Overseas life operations, the negative variance between actual and expected experience is driven mainly by the increase in market interest rates, which has led to capital depreciation of fixed interest assets and consequential reduction of the unallocated divisible surplus in France and other European businesses.

In aggregate, the Group has at its disposal total available capital of £19.5 billion (2005: £18.0 billion), representing the aggregation of the solvency capital of all of our businesses. This capital is available to meet risks and regulatory requirements set by reference to local guidance and EU directives.

After effecting the year end transfer to shareholders, the UK with-profit funds' available capital of £6.9 billion (2005: £5.2 billion) can only be used to provide support for UK with-profit business and is not available to cover other shareholder risks. This is comfortably in excess of the required capital margin and, therefore, the shareholders are not required to provide further capital support to this business.

For the remaining life and general insurance operations, the total available capital amounting to £12.6 billion (2005: £12.8 billion) is significantly higher than the minimum requirements established by regulators and, in principle, the excess is available to shareholders. In practice, management will hold higher levels of capital within each business operation to provide appropriate cover for risk.

As the total available capital of £19.5 billion is arrived at on the basis of local regulatory guidance, which evaluates assets and liabilities prudently, it understates the economic capital of the business which is considerably higher. This is a limitation of the Group Capital Statement which, to be more meaningful, needs to evaluate available capital on an economic basis and compare it with the risk capital required for each individual operation, after allowing for the considerable diversification benefits that exist in our Group.

Notes to the consolidated financial statements continued

49 – Capital statement continued

Within the Aviva Group there exist intra-group arrangements to provide capital to particular business units. Included in these arrangements is a subordinated loan of £200 million from Aviva plc to the NUL&P non-profit fund to provide capital to support the writing of new business.

The available capital of the Group's with-profit funds is determined in accordance with the "Realistic balance sheet" regime prescribed by the FSA's regulations, under which liabilities to policyholders include both declared bonuses and the constructive obligation for future bonuses not yet declared. The available capital resources include an estimate of the value of their respective estates, included as part of the unallocated divisible surplus. The estate represents the surplus in the fund that is in excess of any constructive obligation to policyholders. It represents capital resources of the individual with-profit fund to which it relates and is available to meet regulatory and other solvency requirements of the fund and, in certain circumstances, additional liabilities may arise.

The liabilities included in the balance sheet for the with-profit funds do not include the amount representing the shareholders' portion of future bonuses. However, the shareholders' portion is treated as a deduction from capital that is available to meet regulatory requirements and is therefore shown as a separate adjustment in the capital statement.

In accordance with the FSA's regulatory rules under its realistic capital regime, the Group is required to hold sufficient capital in its UK life with-profit funds to meet the FSA capital requirements, based on the risk capital margin (RCM). The determination of the RCM depends on various actuarial and other assumptions about potential changes in market prices, and the actions management would take in the event of particular adverse changes in market conditions.

					31 December 2006	31 December 2005
	Realistic assets £bn	Realistic liabilities £bn	Realistic orphan estate £bn	Risk capital margin £bn	Excess £bn	Excess £bn
CGNU Life	14.3	(11.8)	2.5	(0.5)	2.0	1.6
CULAC	14.1	(11.6)	2.5	(0.5)	2.0	1.3
NUL&P	27.7	(25.9)	1.8	(0.6)	1.2	0.4
Aggregate	56.1	(49.3)	6.8	(1.6)	5.2	3.3

1. These realistic liabilities include the shareholders' share of future bonuses of £0.7 billion (31 December 2005: £0.7 billion). Realistic liabilities adjusted to eliminate the shareholders' share of future bonuses are £48.6 billion (31 December 2005: £50.5 billion).

2. These realistic liabilities make provision for guarantees, options and promises on a market consistent stochastic basis. The value of the provision included within the realistic liabilities is £0.5 billion, £0.7 billion and £3.0 billion for CGNU life, CULAC and NUL&P respectively. (31 December 2005: £0.7 billion, £0.9 billion and £3.4 billion for CGNU life, CULAC and NUL&P respectively).

3. The risk capital margin (RCM) is 4.2 times covered by the orphan estate (31 December 2005: 2.7 times).

Under the FSA regulatory regime, UK life with-profits business is required to hold capital equivalent to the greater of their regulatory requirement based on EU Directives ("regulatory peak") and the FSA realistic bases ("realistic peak") described above.

For UK non-participating business, the relevant capital requirement is the minimum solvency requirement determined in accordance with FSA regulations. The available capital reflects the excess of regulatory basis assets over liabilities before deduction of capital resources requirement.

For UK general insurance businesses, the relevant capital requirement is the minimum solvency requirement determined in accordance with the FSA requirements.

For overseas businesses in the EEA, US, Canada, Australia, Hong Kong and Singapore, the available capital and the minimum requirement are calculated under the locally applicable regulatory regimes. The businesses outside these territories are subject to the FSA rules for the purposes of calculation of available capital and capital resource requirement.

For fund management and other businesses, the relevant capital requirement is the minimum solvency requirement determined in accordance with the local regulator's requirements for the specific class of business.

All businesses hold sufficient available capital to meet their capital resource requirement.

The available capital resources in each regulated entity are generally subject to restrictions as to their availability to meet requirements that may arise elsewhere in the Group. The principal restrictions are:

49 – Capital statement continued

(i) UK with-profit funds – (CGNU Life, CULAC and NUL&P) – any available surplus held in each fund can only be used to meet the requirements of the fund itself or be distributed to policyholders and shareholders. With-profit policyholders are entitled to at least 90% of the distributed profits while the shareholders receive the balance. The latter distribution would be subject to a tax charge, which is met by the fund in the case of CGNU Life, CULAC and NUL&P.

(ii) UK non-participating funds – any available surplus held in these is attributable to shareholders. Capital in the non-profit funds may be made available to meet requirements elsewhere in the Group subject to meeting the regulatory requirements of the fund. Any transfer of the surplus may give rise to a tax charge subject to availability of tax relief elsewhere in the Group.

(iii) Overseas life operations – the capital requirements and corresponding regulatory capital held by overseas businesses are calculated using the locally applicable regulatory regime. The available capital resources in all these businesses are subject to local regulatory restrictions which may constrain management's ability to utilise these in other parts of the Group. Any transfer of available capital may give rise to a tax charge subject to availability of tax relief elsewhere in the Group.

(iv) General insurance operations – the capital requirements and corresponding regulatory capital held by overseas businesses are calculated using the locally applicable regulatory regime. The available capital resources in all these businesses are subject to local regulatory restrictions which may constrain management's ability to utilise these in other parts of the Group. Any transfer of available capital may give rise to a tax charge, subject to availability of tax relief elsewhere in the Group.

50 – Risk management

(a) Risk management framework

The Group has established a risk management framework whose primary objective is to protect the Group from events that hinder the sustainable achievement of the Group's performance objectives, including failing to exploit opportunities. Risk is categorised as follows:

- Market
- Credit
- Insurance
- Operational
- Liquidity

The Group recognises the critical importance of having efficient and effective risk management systems in place. To this end, the Group has an established governance framework, which has three key elements:

- Defined terms of reference for the Board, its committees, and the associated executive management committees;
- A clear organisational structure with documented delegated authorities and responsibilities from the Board to executive management committees and senior management; and
- A Group policy framework that sets out risk appetite, risk management, control and business conduct standards for the Group's worldwide operations. Each policy has a member of senior management who is charged with overseeing compliance with the policy throughout the Group.

Regulatory impact on risk and risk assessments

Where the Group's long-term savings businesses have written insurance products where the majority of investment risks are borne by its policyholders, these risks are actively and prudently managed in order to satisfy the policyholders' risk and reward objectives. In addition, the Group's worldwide insurance operations are subject to numerous local regulatory requirements that prescribe the type, quality, and concentration of investments, and the level of assets to be maintained in local currency in order to meet local insurance liabilities. These requirements help to maintain the Group's market risk levels at an acceptable level in each of the jurisdictions in which it operates.

The adoption of the Group's policies on risk management enables a consistent approach to management of risk at business unit level. The Group operates a number of oversight committees that monitor aggregate risk data and take overall risk management decisions.

The Group also monitors a set of specific risks on a regular basis through the Group risk monitoring framework. Businesses units are required to disclose to the Group risk function all material risks, along with information on likelihood and severity of risks, and the mitigating actions taken or planned. This enables the Group to assess its overall risk exposure and to develop a group-wide risk map, identifying any concentrations of risk that may exist, and to define which risks and what level of risk the Group is prepared to accept. The risk map is refreshed quarterly, and business units are required to escalate material changes intra-quarter.

Notes to the consolidated financial statements continued

50 – Risk management continued**(b) Market risk**

Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments from fluctuations in interest rates, equity prices, property prices, and foreign currency exchange rates. Market risk arises in business units due to fluctuations in both the value of liabilities and the value of investments held. At Group level, it also arises in relation to the overall portfolio of international businesses and in the value of investment assets owned directly by the shareholders.

The Group has established a policy on market risk which sets out the principles that businesses are expected to adopt in respect of management of the key market risks to which the Group is exposed. The Group monitors adherence to this market risk policy and regularly reviews how business units are managing these risks locally, through the Group Investment Committee and ultimately to the Asset Liability Management committee. For each of the major components of market risk, described in more detail below, the Group has put in place additional policies and procedures to set out how each risk should be managed and monitored, and the approach to setting an appropriate risk appetite.

The management of market risk is undertaken in both business units and at Group level. Business units manage market risks locally using their market risk framework and within local regulatory constraints. Business units may also be constrained by the requirement to meet policyholders' reasonable expectations and to minimise or avoid market risk in a number of areas. The Group Investment committee is responsible for managing market risk at Group level, and a number of investment related risks, in particular those faced by the shareholder funds throughout the Group.

The financial impact from changes in market risk (such as interest rates, equity prices and property values) is examined through stress tests adopted in the Individual Capital Assessments (ICA) and Financial Condition Reports (FCR), which both consider the impact on capital from variations in financial circumstances on either a remote scenario, or to changes from the central operating scenario. Both consider the management actions that may be taken in mitigation of the change in circumstances.

The sensitivity of Group earnings to changes in economic markets is regularly monitored through sensitivities to investment returns and asset values in EEV reporting.

The Group market risk policy sets out the minimum principles and framework for matching liabilities with appropriate assets, the approaches to be taken when liabilities cannot be matched and the monitoring processes that are required. The Group has criteria for matching assets and liabilities for all classes of business in order to manage the financial risk from the mismatching of assets and liabilities when investment markets change. The local regulatory environment for each business will also set the conditions under which assets and liabilities are to be matched.

Equity price risk

The Group is subject to equity price risk due to daily changes in the market values of its equity securities portfolio. The Group's shareholders are exposed to both direct equity shareholdings in its shareholder assets, from the indirect impact from changes in the value of equities held in policyholders funds from which management charges or a share of performance are taken, and from its interest in the free estate of long-term funds.

At business unit level, equity price risk is actively managed in order to mitigate anticipated unfavourable market movements where this lies outside the risk appetite of the fund concerned. In addition local asset admissibility regulations require that business units hold diversified portfolios of assets thereby reducing exposure to individual equities. The Group does not have material holdings of unquoted equity securities.

Businesses actively model the performance of equities through the use of stochastic models, in particular to understand the impact of equity performance on guarantees, options and bonus rates.

The Investment Committee actively monitors equity assets owned directly by the Group, which may include some material shareholdings in the Group's strategic business partners. Concentrations of specific equity holdings (eg the strategic holdings) are also monitored monthly by the Capital Management Committee.

A sensitivity to changes in equity prices is given in section (g) below.

Property price risk

The Group is subject to property price risk due to holdings of investment properties in a variety of locations worldwide. The investment in property is managed at business unit level, and will be subject to local regulations on asset admissibility, liquidity requirements and the expectations of policyholders. At 31 December 2006, no material derivative contracts had been entered into to mitigate the effects of changes in property prices.

A sensitivity to changes in property prices is given in section (g) below.

50 – Risk management continued**Interest rate risk**

Interest rate risk arises primarily from the Group's investments in long-term debt and fixed income securities, which are exposed to fluctuations in interest rates. Exposure to interest rate risk is monitored through several measures that include Value-at-Risk analysis, position limits, scenario testing, stress testing and asset and liability matching using measures such as duration.

Interest rate risk also exists in products sold by the group, in particular from policies that carry investment guarantees on early surrender or at maturity, where claim values can become higher than the value of backing assets when interest rates rise or fall. The Group manages this risk by adopting close asset liability matching criteria, to minimise the impact of mismatches between the value of assets and liabilities from interest rate movements. However where any mismatch is within our risk appetite, the impact is monitored through economic capital measures such as ICA.

On short-term business such as general insurance business the Group requires a close matching of assets and liabilities by duration to minimise this risk.

The impact of exposure to sustained low interest rates is regularly monitored.

Interest rate risk is also managed using a variety of derivative instruments, including futures, options and swaps, caps and floors, in order to provide a degree of hedging against unfavourable market movements in interest rates inherent in the assets backing technical liabilities.

At 31 December 2006, the Group had entered into a number of interest rate swap agreements to mitigate the effects of potential adverse interest rate movements, and to enable close matching of assets and liabilities.

A sensitivity to changes in interest rates is given in section (g) below.

Further information on borrowings is included in note 43.

Currency risk

The Group operates internationally and as a result is exposed to foreign currency exchange risk arising from fluctuations in exchange rates of various currencies. Approximately half of the Group's premium income arises in currencies other than sterling and the Group's net assets are denominated in a variety of currencies, of which the largest are euro, sterling, and US dollars. The Group does not hedge foreign currency revenues as these are substantially retained locally to support the growth of the Group's business and meet local regulatory and market requirements.

The Group's foreign exchange policy requires that each of the Group's subsidiaries maintain sufficient assets in their local currencies to meet local currency liabilities. Therefore, capital held by the Group's business units should be able to support local business activities regardless of foreign currency movements. However, such movements may impact the value of the Group's consolidated shareholders' equity which is expressed in sterling. This aspect of foreign exchange risk is monitored and managed centrally, against pre-determined limits. The Group's foreign exchange policy is to manage these exposures by aligning the deployment of capital by currency, with the Group's regulatory capital requirements by currency. Limits are set to control the extent to which the deployment of capital is not aligned fully with the Group's capital requirement for each major currency. Currency borrowings and derivatives are used to manage exposures within the limits that have been set.

At 31 December 2006, the Group's total equity deployment by currency was:

	Sterling £m	Euro £m	US\$ £m	Other £m	Total £m
Capital 31 December 2006	3,289	7,698	1,508	1,569	14,064
Capital 31 December 2005	1,772	7,458	177	1,685	11,092

Net assets are stated after taking account of the effect of currency swaps and forward foreign exchange contracts.

A 10% change in sterling to euro/US\$ foreign exchange rates would have had the following impact on net assets. Apart from the impact on financial instruments covered below, the changes arise from retranslation of Business Unit balance sheets from their functional currencies into sterling, with movements being taken through the currency translation reserve. These movements in exchange rates therefore have no impact on profit.

	10% increase in sterling/ euro rate £m	10% decrease in sterling/ euro rate £m	10% increase in sterling/ US\$ rate £m	10% decrease in sterling/ US\$ rate £m
Net assets at 31 December 2006	(770)	770	(151)	151
Net assets at 31 December 2005	(746)	746	(18)	18

The Group has minimal exposure to currency risk from financial instruments held by Business Units in currencies other than their functional currencies, as nearly all such holdings are backing either unit-linked or with-profit contract liabilities. For this reason, no sensitivity analysis is given for these holdings.

Notes to the consolidated financial statements continued

50 – Risk management continued**Derivatives risk**

Derivatives are used by a number of the larger businesses, within policy guidelines agreed by the Board of directors and overseen by a Group derivatives committee, which monitors implementation of the policy, exposure levels and approves large or complex transactions proposed by business units. Derivatives are primarily used for efficient investment management, risk hedging purposes or to structure specific retail-savings products. The Group also manages a number of hedge funds which use derivatives extensively within a defined derivative framework. Derivative transactions are fully covered by either cash or corresponding assets and liabilities. Speculative activity is prohibited, unless approval has been obtained from the Derivatives committee. Over the counter derivative contracts are entered into only with approved counterparties, in accordance with our Group policies, thereby reducing the risk of credit loss. The Group applies strict requirements to the administration and valuation processes it uses, and has a control framework that is consistent with market and industry practice for the activity that is undertaken.

Correlation risk

The Group recognises that identified lapse behaviour and potential increases in consumer expectations are sensitive to and interdependent with market movements and interest rates. These interdependencies are taken into consideration in the ICA in the aggregation of the financial stress tests with the operational risk assessment. FCRs also consider scenarios involving a number of correlated events.

A number of policyholder participation features have an influence on the Group's interest rate risk. The major features include guaranteed surrender values, guaranteed annuity options, and minimum surrender and maturity values. Details of material guarantees and options are given in note 38.

(c) Credit risk

Credit risk is the risk of loss in the value of financial assets due to counterparties failing to meet all or part of their obligations. The Group's management of credit risk includes monitoring exposures at a Group level and requiring business units to implement local credit risk policies. The local business unit credit risk policies involve the establishment and operation of specific risk management committees and the detailed reporting and monitoring of the financial asset portfolio against pre-established risk criteria. Large individual counterparty exposures exceeding £25 million are aggregated and monitored at Group level against centrally-set limits reflecting the credit ratings by companies such as Standard & Poor's. In addition, the Group evaluates the concentration of exposures by industry sector and geographic region through the Group Credit committee.

Financial assets are graded according to current credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. Financial assets which fall outside this range are classified as speculative grade. Credit limits for each counterparty are set based on default probabilities that are in turn based on the rating of the counterparty concerned.

The following table provides information regarding the aggregated credit risk exposure, for financial assets with external credit ratings, of the Group at 31 December 2006.

	Credit rating						Carrying value in the balance sheet £m
	AAA	AA	A	BB/ BBB	Speculative grade	Not-rated	
Debt securities	49.2%	16.7%	19.7%	7.8%	0.8%	5.8%	113,041
Reinsurance assets	14.5%	66.9%	5.1%	0.9%	–	12.6%	7,825
Other investments	3.1%	2.2%	2.8%	0.7%	–	91.2%	33,050
Loans	3.4%	1.2%	1.1%	0.5%	1.5%	92.3%	26,445

As at 31 December 2005

	Credit rating						Carrying value in the balance sheet £m
	AAA	AA	A	BB/ BBB	Speculative grade	Not-rated	
Debt securities	54.3%	18.3%	15.3%	7.1%	0.5%	4.5%	103,917
Reinsurance assets	23.4%	34.0%	33.5%	0.5%	–	8.6%	7,130
Other investments	1.3%	2.4%	5.5%	2.9%	–	87.9%	26,427
Loans	2.9%	1.2%	1.1%	0.2%	1.4%	93.2%	24,544

The carrying amount of assets included on the balance sheet represents the maximum credit exposure.

50 – Risk management continued

The long-term businesses and general insurance businesses are generally not individually exposed to significant concentrations of credit risk due to the regulations, applicable in most markets, limiting investments in individual assets and asset classes. In cases where the business is particularly exposed to credit risk (e.g. in respect of defaults on mortgages or debt matching annuity liabilities) this risk is translated into a more conservative discount rate used to value the liabilities, creating a greater capital requirement, and this credit risk is actively managed. The impact of aggregation of credit risk is monitored as described above. With the exception of AAA rated Governments the largest aggregated counterparty exposure does not exceed 1.6% of the Group's total financial assets.

Reinsurance credit exposures

The Group is exposed to concentrations of risk with individual reinsurers, due to the nature of the reinsurance market and the restricted range of reinsurers that have acceptable credit ratings. The Group operates a policy to manage its reinsurance counterparty exposures and the impact from reinsurer default is measured regularly, in particular through the ICA tests, and is managed accordingly. Both the Credit committee and Reinsurance Security committee have a monitoring role over this risk. The Group's largest reinsurance counterparty is National Indemnity Corporation, a member of the Berkshire Hathaway Group. At 31 December 2006 the reinsurance asset recoverable from National Indemnity Corporation was £1.3 billion. This exposure is monitored on a regular basis with the forecast to completion monitored for any shortfall in the claims history to verify that the contract is progressing as expected and that no further exposure for the Group will arise.

In the event of a catastrophic event, the counterparty exposure to a single reinsurer is estimated not to exceed 1.0% of shareholders' equity.

The following table provides information regarding the carrying value of financial assets that have been impaired and the ageing of financial assets that are past due but not impaired.

At 31 December 2006

	Neither past due nor impaired	Financial assets that are past due but not impaired				Financial assets that have been impaired	Carrying value in the balance sheet £m
		0–3 months	3–6 months	6 months– 1 year	Greater than 1 year		
Debt securities	100.0%	–	–	–	–	–	113,041
Reinsurance assets	98.5%	–	–	–	–	1.5%	7,825
Other investments	100.0%	–	–	–	–	–	33,050
Loans	99.3%	0.4%	–	–	0.1%	0.2%	26,445
Receivables and other financial assets	89.8%	8.8%	0.6%	0.4%	0.3%	0.1%	8,098

At 31 December 2005

	Neither past due nor impaired	Financial assets that are past due but not impaired				Financial assets that have been impaired	Carrying value in the balance sheet £m
		0–3 months	3–6 months	6 months– 1 year	Greater than 1 year		
Debt securities	100.0%	–	–	–	–	–	103,917
Reinsurance assets	99.9%	–	–	–	–	0.1%	7,130
Other investments	100.0%	–	–	–	–	–	26,427
Loans	99.3%	0.5%	–	–	–	0.2%	24,544
Receivables and other financial assets	94.6%	4.4%	0.5%	0.3%	0.2%	–	7,706

The fair value of collateral held against loans that are past due or impaired at 31 December 2006 was £61 million (2005: £130 million). This predominantly consists of commercial properties.

The credit ratings table above analyses the credit quality of the above balances where a credit rating is available. The credit quality of receivables and other financial assets is managed at the local business unit level with uncollectible amounts being impaired when necessary.

There were no material financial assets that would have been past due or impaired had the terms not been renegotiated.

Notes to the consolidated financial statements continued

50 – Risk management continued**(d) Insurance risk****(i) Life insurance risk***Type of risk*

Life insurance risk in the Group arises through its exposure to mortality and morbidity insurance and exposure to worse than anticipated operating experience on factors such as persistency levels and management and administration expenses.

Risk management

The Group has developed a life insurance risk policy and guidelines on the practical application of this policy. Individual life insurance risks are managed at a business unit level.

The management of life insurance risk is undertaken primarily in business units but is also monitored at Group level. The impact of life insurance risks is monitored by the business units as part of the control cycle of business management. Exposure is monitored through the assessment of liabilities, the asset liability management framework, profit reporting (under both IFRS and EEV), financial condition reporting, and the ICA process. Significant insurance risks will be reported through the Group Risk Monitoring framework and overseen by the Life Insurance Risk Committee. At Group level the overall exposure to life insurance risk is measured through the ICA, FCRs, and other management reporting.

The Life Insurance Risk Committee monitors the risk framework developed and implemented in each business, and receives management information on life insurance risks. The committee considers all areas of life insurance risk, but in particular has a remit to monitor mortality, longevity, morbidity, persistency, pricing, unit pricing and expenses. The committee also considers the reinsurance coverage across the life businesses. It confirms that guidance and procedures are in place for each of the major components of life insurance risk, and that businesses adopt a risk management framework to mitigate against any life insurance risk outside local appetite, within the parameters for the overall Group risk appetite. The framework adopted in business units is reviewed in detail and approved twice yearly.

The committee has also developed guidance for business units on management of a number of areas of life insurance risk to ensure best practice is shared throughout the group and common standards are adopted.

Mortality and morbidity risks are mitigated by use of reinsurance. The Group allows business units to select reinsurers, from those approved by the Group, based on local factors, but assesses the overall programme to manage group-wide risk exposures and monitor the aggregation of risk ceded to individual reinsurers is within appetite for credit risk.

Longevity risk is carefully monitored against the latest external industry data and emerging trends. Whilst individual businesses are responsible for reserving and pricing for annuity business, the Group monitors the exposure to this risk and the capital implications to manage the impact on the group-wide exposure and the capital funding that businesses may require as a consequence. The Group has used reinsurance solutions to reduce the risks from longevity where possible and desirable and continually monitors emerging market solutions to mitigate this risk further.

Persistency risk is managed at a business unit level through frequent monitoring of company experience, benchmarked against local market information. Where possible the financial impact of lapses is reduced through appropriate product design. The Group Life Insurance Risk Committee has developed guidelines on persistency management.

Expense risk is primarily managed by the business units through the assessment of business unit profitability and frequent monitoring of expense levels.

Apart from ICA and FCR, sensitivity testing is widely used to measure the capital required and volatility in earnings due to exposure to life insurance risks, typically through EEV reporting (examples of which are contained elsewhere in this report). This assessment is taken at both business unit level and at Group level where the impact of aggregation of similar risks can be measured. This enables the Group to determine whether action is required to reduce risk, or whether that risk is within the overall risk appetite.

Concentration risk

The Group writes a diverse mix of business in worldwide markets that are all subject to similar risks (mortality, persistency etc). The Group assesses the relative costs and concentrations of each type of risk through the ICA capital requirements and material issues are escalated to and addressed at the Life Insurance Risk committee. This analysis enables the Group to assess whether accumulations of risk exceeds risk appetite.

One key concentration of life insurance risk for the Group is improving longevity risk from pensions in payment and deferred annuities in the UK and the Netherlands where the Group has material portfolios. The Group continually monitors this risk and the opportunities for mitigating actions through reinsurance, improved asset liability matching, or innovative solutions that emerge in the market.

When looking at concentrations of risk, for example market risk, the risk within Aviva staff pension schemes is also considered.

ICA analysis and EEV sensitivity testing help identify both concentrations of risk types and the benefits of diversification of risk.

50 – Risk management continued

Embedded derivatives

The Group has exposure to a variety of embedded derivatives in its long-term savings business due to product features offering varying degrees of guaranteed benefits at maturity or on early surrender, along with options to convert their benefits into different products on pre-agreed terms. The extent of the impact of these embedded derivatives differs considerably between business units.

Examples of each type of embedded derivative affecting the Group are:

Options: call, put, surrender and maturity options, guaranteed annuity options, option to cease premium payment, options for withdrawals free of market value adjustment, annuity option, guaranteed insurability options.

Guarantees: embedded floor (guaranteed return), maturity guarantee, guaranteed death benefit, guaranteed minimum rate of annuity payment.

Other: indexed interest or principal payments, maturity value, loyalty bonus.

The impact of these is reflected in ICA and EEV reporting and managed as part of the asset liability framework.

(ii) General insurance risk

Type of risk

General insurance risk in the Group arises from:

- Fluctuations in the timing, frequency and severity of claims and claim settlements relative to expectations;
- Unexpected claims arising from a single source;
- Inaccurate pricing of risks when underwritten;
- Inadequate reinsurance protection or other risk transfer techniques; and
- Inadequate reserves.

The majority of the general insurance business underwritten by the Group is of a short tail nature such as motor, household and commercial property insurances. The Group's underwriting strategy and appetite is agreed by the Executive Committee and communicated via specific policy statements and guidelines. Like life insurance risk, General Insurance risk is managed at business unit level and Group level.

The vast majority of the Group's general insurance business is managed and priced in the same country as the domicile of the customer.

Risk management

Significant insurance risks will be reported through the Group Risk monitoring framework. Additionally, the ICA framework is used to assess the risks that each general insurance business unit, and the Group as a whole, is exposed to, quantifying their impact and calculating appropriate capital requirements.

Increasingly risk-based capital models are being used to support the quantification of risk under the ICA framework. All general insurance business units undertake a quarterly review of their insurance risks, the output from which is a key input into the ICA and risk-based capital assessments.

The General Insurance Risk Committee monitors and develops the management of insurance risk in the general insurance business units, and assesses the aggregate risk exposure. It is responsible for the development, implementation, and review of the Group policies for underwriting, claims handling, reinsurance and reserving that operate within the Group risk management framework. The implementation of these policies and the management of these risks is supported by sub-committees for each of these four areas of risk.

Business units have developed mechanisms that identify, quantify and manage accumulated exposures to contain them within the limits of the appetite of the Group. The Group has pioneered various developments, such as the Norwich Union UK Digital Flood Map to effectively manage exposures arising from specific perils. Where appropriate such projects are employed throughout the business units to promote the adoption of best practice as standard.

Notes to the consolidated financial statements continued

50 – Risk management continued*Actuarial management*

The adequacy of the Group's general insurance claims provisions is ultimately overseen by the Reserving Committee, which covers both life and general insurance reserving. Actuarial claims reserving is conducted by local actuaries in the various general insurance business units according to the General Insurance Reserving policy. The General Insurance Risk Committee monitors and maintains the General Insurance Reserving policy, and conducts quarterly reviews of the Group's general insurance claims provisions, and their adequacy. The reviews are conducted under the direction of the Aviva General Insurance Actuarial Director and include peer reviews of the business unit's own conclusions as well as independent analysis to confirm the reasonableness of the local reviews. A number of business units also have periodic external reviews by local consultant actuaries (often as part of the local regulatory requirement).

Reinsurance strategy

Reinsurance purchases are reviewed annually at both business unit and Group level, to verify that the levels of protection being bought reflect any developments in exposure and the risk appetite of the Group. The basis of these purchases is underpinned by extensive financial and capital modelling and actuarial analysis to optimise the cost and capital efficiency benefits. For the larger business units, this involves utilising externally sourced probabilistic models to verify the accumulations and loss probabilities based on the Group's specific portfolios of business. Where external models are not available, scenarios are developed and tested using the Group's data to determine potential losses and appropriate levels of reinsurance protection. The reinsurance is placed with providers who meet the Group's counterparty security requirements.

Concentration risk

Processes are in place to manage catastrophe risk in individual business units and at a Group level. The Group cedes much of its worldwide catastrophe risk to third party reinsurers but retains a pooled element for its own account gaining economic diversification benefit. Aviva's total retained risk increases as catastrophe events become more remote, so that the total Group loss from its most concentrated catastrophe exposure (Northern European windstorm) is approximately £370 million, one in ten years, compared to approximately £700 million, one in 100 years.

(e) Operational risk

Operational risk arises as a result of inadequately controlled internal processes or systems, human error, or from external events.

This definition is intended to include all risks to which the Group is exposed, other than the financial risks described previously, and strategic and Group risks that are considered elsewhere. Hence, operational risks include for example, information technology, information security, human resources, project management, outsourcing, tax, legal, fraud and compliance risks.

In accordance with Group policies, business unit management has primary responsibility for the effective identification, management, monitoring and reporting of risks to the business unit executive management team and to Group as part of the quarterly risk reporting process. Each operational risk is assessed by considering the potential impact and the probability of the event occurring. Impact assessments are made against financial, operational and reputational criteria.

Business unit risk management and governance functions are responsible for implementing the Group risk management methodologies and frameworks to assist line management in this work. They also provide support and independent challenge on the completeness, accuracy and consistency of risk assessments, and the adequacy of mitigating action plans. As a result, the business unit executive management team satisfies itself that all material risks falling outside our risk appetite are being mitigated, monitored and reported at an appropriate level. Any risks with a high impact level are continually monitored centrally.

The Group Operational Risk Committee (ORC) has been established and determines the risk appetite that the group can work within for these types of risk, assesses and monitors overall operational risk exposures, identifying any concentrations of operational risk across the group, and in particular verifies that mitigating action plans are implemented.

(f) Liquidity risk

The Group has a strong liquidity position and through the application of a Group Liquidity Management policy seeks to maintain sufficient financial resources to meet its obligations as they fall due. In addition to its strong liquidity position, the Group maintains significant committed borrowing facilities from a range of highly rated banks to further mitigate this risk.

50 – Risk management continued**Analysis of maturity of liabilities**

For each main category of insurance and investment business, the following table shows the gross liability at 31 December 2006 analysed by remaining duration. The total liability is split by remaining duration in proportion to the cash-flows expected to arise during that period.

	At 31 December 2006				
	Total £m	Within 1 year £m	1–5 years £m	5–15 years £m	Over 15 years £m
Long-term business					
Insurance contracts – non linked	99,482	9,140	25,959	40,651	23,732
Investment contracts – non linked	41,578	3,044	10,572	15,930	12,032
Linked business	73,522	5,617	18,695	29,111	20,099
General insurance and health	18,006	8,482	6,824	2,617	83

	At 31 December 2005				
	Total £m	Within 1 year £m	1–5 years £m	5–15 years £m	Over 15 years £m
Long-term business					
Insurance contracts – non linked	88,586	8,113	26,066	36,651	17,756
Investment contracts – non linked	42,736	3,111	11,767	16,688	11,170
Linked business	60,163	3,036	13,729	25,711	17,687
General insurance and health	18,426	8,636	7,416	2,189	185

A maturity analysis of borrowings is given in Note 43.

(g) Risk and capital management

The Group uses a number of sensitivity test-based risk management tools to understand the volatility of earnings, the volatility of its capital requirements, and to manage its capital more efficiently. Primarily, EEV, FCRs, and increasingly ICA are used. Sensitivities to economic and operating experience are regularly produced on all of the Group's financial performance measurements to inform the Group's decision making and planning processes, and as part of the framework for identifying and quantifying the risks that each of its business units, and the Group as a whole are exposed to.

For long-term business in particular, sensitivities of EEV performance indicators to changes in both economic and non-economic experience are continually used to manage the business and to inform the decision making process. More information on EEV sensitivities can be found in the presentation of results on an EEV basis in the supplementary notes to this report.

Life insurance and Investment contracts

The nature of long-term business is such that a number of assumptions are made in compiling these financial statements. Assumptions are made about investment returns, expenses, mortality rates, and persistency in connection with the in-force policies for each business unit. Assumptions are best estimates based on historic and expected experience of the business. A number of the key assumptions for the Group's central scenario are disclosed elsewhere in these statements for both IFRS reporting and reporting under EEV methodology.

General insurance and health business

General insurance and health claim liabilities are estimated by using standard actuarial claims projection techniques. These methods extrapolate the claims development for each accident year based on the observed development of earlier years. In most cases, no explicit assumptions are made as projections are based on assumptions implicit in the historic claims development on which the projections are based. As such, in the analysis below, the sensitivity of general insurance claim liabilities is primarily based on the financial impact of changes to the reported loss ratio.

Some results of sensitivity testing for long-term business, general insurance and health business and the fund management and non-insurance business are set out below. For each sensitivity test the impact of a reasonably possible change in a single factor is shown, with other assumptions left unchanged.

Sensitivity Factor	Description of sensitivity factor applied
Interest rate and investment return	The impact of a change in market interest rates by $\pm 1\%$ (e.g. if a current interest rate is 5%, the impact of an immediate change to 4% and 6%). The test allows consistently for similar changes to investment returns and movements in the market value of backing fixed interest securities.
Expenses	The impact of an increase in maintenance expenses by 10%.
Equity/property market values	The impact of a change in equity/property market values by $\pm 10\%$
Assurance mortality/morbidity (life insurance only)	The impact of an increase in mortality/morbidity rates for assurance contracts by 5%.
Annuitant mortality (life insurance only)	The impact of a reduction in mortality rates for annuity contracts by 5%
Gross loss ratios (non-life insurance only)	The impact of an increase in gross loss ratios for general insurance and health business by 5%.

Notes to the consolidated financial statements continued

50 – Risk management continued*Long-term business**Sensitivities as at 31 December 2006**Impact on profit before tax (£m)*

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality –5%
Insurance participating	(5)	–	35	(35)	–	–	(5)
Insurance non-participating	25	(210)	110	(130)	(5)	(20)	(295)
Investment participating	(30)	(35)	10	(10)	(5)	–	–
Investment non-participating	(15)	15	40	(40)	–	–	–
Assets backing life shareholders' funds	(280)	305	60	(60)	–	–	–
Total	(305)	75	255	(275)	(10)	(20)	(300)

Impact before tax on shareholders' equity (£m)

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality –5%
Insurance participating	(25)	25	35	(35)	–	–	(5)
Insurance non-participating	(240)	60	125	(140)	(5)	(20)	(295)
Investment participating	(30)	(35)	10	(10)	(5)	–	–
Investment non-participating	(70)	70	40	(40)	–	–	–
Assets backing life shareholders' funds	(320)	345	95	(95)	–	–	–
Total	(685)	465	305	(320)	(10)	(20)	(300)

*Sensitivities as at 31 December 2005**Impact on profit before tax (£m)*

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality –5%
Insurance participating	5	(35)	35	(35)	(5)	–	–
Insurance non-participating	60	(350)	105	(120)	(5)	(30)	(295)
Investment participating	10	(50)	10	(10)	–	–	–
Investment non-participating	–	–	35	(35)	–	–	–
Assets backing life shareholders' funds	(225)	240	65	(65)	–	–	–
Total	(150)	(195)	250	(265)	(10)	(30)	(295)

Impact before tax on shareholders' equity (£m)

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Assurance mortality +5%	Annuitant mortality –5%
Insurance participating	(10)	(20)	35	(35)	(5)	–	–
Insurance non-participating	20	(305)	120	(135)	(5)	(30)	(295)
Investment participating	(10)	(25)	10	(10)	–	–	–
Investment non-participating	(5)	–	35	(35)	–	–	–
Assets backing life shareholders' funds	(240)	255	90	(90)	–	–	–
Total	(245)	(95)	290	(305)	(10)	(30)	(295)

50 – Risk management continued

Changes in sensitivities between 2005 and 2006 arise primarily from the acquisitions of Ark Life and AmerUs, and the effect of increases in market interest rates. The different impacts of the economic sensitivities on profit and shareholders' equity arise from classification of certain assets as available for sale in some business units, for which movements in unrealised gains or losses would be taken directly to shareholders' equity. The economic impacts on profit before tax for insurance contracts relate mainly to the effect of minimum return guarantees in the Netherlands. However in the case of the interest rate sensitivities, the impacts on shareholders' equity are more than offset by the effect of changes in the market value of fixed interest securities in the United States that are classified as available for sale.

The mortality sensitivities relate primarily to the UK and Ireland.

The impact on the Group's results from sensitivity to these assumptions can also be found in the EEV sensitivities included in the alternative method of reporting long-term business profits section.

General insurance and health business**Sensitivities as at 31 December 2006***Impact on profit before tax (£m)*

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	(270)	290	370	(370)	(140)	(350)
Net of reinsurance	(270)	290	370	(370)	(140)	(325)

Impact before tax on shareholders' equity (£m)

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	(270)	290	370	(370)	(35)	(350)
Net of reinsurance	(270)	290	370	(370)	(35)	(325)

Sensitivities as at 31 December 2005*Impact on profit before tax (£m)*

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	(275)	285	330	(330)	(115)	(305)
Net of reinsurance	(275)	285	330	(330)	(115)	(305)

Impact before tax on shareholders' equity (£m)

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	(275)	285	330	(330)	(30)	(305)
Net of reinsurance	(275)	285	330	(330)	(30)	(305)

For general insurance, the impact of the expense sensitivity on profit also includes the increase in ongoing administration expenses, in addition to the increase in the claims handling expense provision.

Notes to the consolidated financial statements continued

50 – Risk management continued*Fund management and non-insurance business**Sensitivities as at 31 December 2006**Impact on profit before tax (£m)*

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%
Total	(26)	26	44	(44)

Impact before tax on shareholders' equity (£m)

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%
Total	(52)	51	78	(78)

*Sensitivities as at 31 December 2005**Impact on profit before tax (£m)*

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%
Total	(35)	35	26	(26)

Impact before tax on shareholders' equity (£m)

	Interest rates +1%	Interest rates –1%	Equity/ property +10%	Equity/ property –10%
Total	(70)	70	60	(60)

Limitations of sensitivity analysis

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs. For example, the Group's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation, adjusting bonuses credited to policyholders, and taking other protective action.

A number of the business units use passive assumptions to calculate their long-term business liabilities. Consequently, the actual impact of a change in the assumptions may not have any impact on the liabilities, whereas assets are held at market value on the balance sheet. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity. Similarly, for general insurance liabilities, the interest rate sensitivities only affect profit and equity where explicit assumptions are made regarding interest (discount) rates or future inflation.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Group's view of possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

51 – Derivative financial instruments

The Group uses cash flow, fair value and net investment hedges to mitigate risk, as detailed below.

(a) Cash flow hedges

The Group had no cash flow hedge activity at 31 December 2006 (2005: nil).

(b) Fair value hedges

The Group had no fair value hedge activity at 31 December 2006 (2005: nil).

(c) Net investment hedges

To reduce the Group's exposure to foreign currency risk, the Group has designated a portion of its Euro and US dollar denominated debt as a hedge of the net investment in its European and American subsidiaries. The carrying value of the debt at 31 December 2006 was £1,875 million (2005: £1,921 million) and its fair value at that date was £1,973 million (2005: £2,070 million).

The foreign exchange gain of £59 million (2005: £19 million) on translation of the debt to sterling at the balance sheet date was recognised in the hedging instruments reserve in shareholders' equity. This hedge was fully effective throughout the current and prior year.

(d) Non-hedge derivatives

The Group's non-hedge derivative activity at 31 December 2006 was as follows:

	2006			2005		
	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m
Foreign exchange contracts						
OTC						
Forwards	12,379	93	(7)	6,297	12	(10)
Interest and currency swaps	245	–	(52)	3,096	4	(34)
Options	–	–	–	1	–	–
Total	12,624	93	(59)	9,394	16	(44)
Interest rate contracts						
OTC						
Forwards	538	9	(4)	3,626	13	(6)
Swaps	9,412	184	(264)	7,682	67	(176)
Options	943	239	(2)	95	289	–
Exchange traded						
Futures	(2,060)	74	(5)	(2,589)	2	(638)
Options	30	–	–	624	19	–
Total	8,863	506	(275)	9,438	390	(820)
Equity/Index contracts						
OTC						
Forwards	8	–	–	903	1	(79)
Options	3,705	258	(3)	273	27	–
Exchange traded						
Futures	951	391	(9)	50	2	419
Options	93	27	(6)	4	5	(2)
Total	4,757	676	(18)	1,230	35	338
Other	305	50	(3)	–	26	–
Totals at 31 December	26,549	1,325	(355)	20,062	467	(526)

Fair value assets are recognised as "Derivative financial instruments" in note 23(a). Fair value liabilities are recognised as "other financial liabilities" in note 44.

The Group's derivative risk management policies are outlined in Note 50(b).

Notes to the consolidated financial statements continued

51 – Derivative financial instruments continued

The contractual undiscounted cash flows in relation to non-hedge derivative liabilities have the following maturities:

	2006 £m	2005 £m
Within one year	162	423
Between one and two years	63	8
Between two and three years	7	8
Between three and four years	7	8
Between four and five years	18	8
After five years	214	144
	471	599

52 – Assets under management

The total Group assets under management are:

	2006 £m	2005 £m
Total assets included in the consolidated balance sheet	292,722	263,447
Additional value of internally-generated in-force long-term business	6,794	6,454
Third party funds under management		
Unit trusts, OEICs, Peps and Isas	20,574	16,188
Segregated funds	43,672	35,427
Total assets under management	363,762	321,516

Third-party funds under management now include funds administered under the Navigator platform. This change has increased the total assets under management at 31 December 2006 by £6,058 million (2005: £4,606 million).

53 – Related party transactions

The Group received income from related parties from transactions made in the normal course of business. Loans to related parties are made on normal arm's length commercial terms.

Services provided to related parties

	2006		2005	
	Income earned in year £m	Receivable at year end £m	Income earned in year £m	Receivable at year end £m
Associates	50	1	47	12
Joint ventures	16	241	13	128
Employee pension schemes	6	–	3	–
	72	242	63	140

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms. Details of guarantees, indemnities and warranties provided on behalf of related parties are given in note 46(f).

There were no services provided by related parties in either 2005 or 2006.

Details of loans made to joint ventures and associates may be found in notes 17 and 18 respectively.

The total compensation to those employees classified as key management, being those having authority and responsibility for planning, directing and controlling the activities of the Group, including the executive and non-executive directors is as follows:

	2006 £m	2005 £m
Salary and other short-term benefits	32	24
Post-employment benefits	1	1
Equity compensation plans	16	9
Termination benefits	4	–
Total	53	34

Information concerning individual directors' emoluments, interests and transactions is given in the Directors' remuneration report.

Financial statements of the Company

Income statement

For the year ended 31 December 2006

	Note	2006 £m	2005 £m
Income			
Dividends received from subsidiaries		865	1,708
Interest receivable from Group companies		219	217
Profit on disposal of subsidiary	B	94	–
Net investment income/(expenses)		34	(10)
		1,212	1,915
Expenses			
Operating expenses	C	(201)	(160)
Interest payable to Group companies		(1,341)	(238)
Interest payable on borrowings		(215)	(224)
		(1,757)	(622)
(Loss)/profit before tax		(545)	1,293
Tax credit	D	521	54
(Loss)/profit after tax		(24)	1,347

Statement of recognised income and expenses

For the year ended 31 December 2006

	Note	2006 £m	2005 £m
Fair value gains on investments in subsidiaries	B	4,075	1,521
Fair value gains transferred to income statement		(94)	–
Aggregate tax effect		15	13
Actuarial losses on pension scheme		(4)	–
Net income recognised directly in equity		3,992	1,534
(Loss)/profit for the year		(24)	1,347
Total recognised income and expense for the year		3,968	2,881

Reconciliation of movements in shareholders' equity

For the year ended 31 December 2006

	Note	2006 £m	2005 £m
Balance at 1 January		18,746	15,812
Total recognised income and expense for the year		3,968	2,881
Dividends and appropriations	14	(762)	(657)
Issue of share capital for the acquisition of AmerUs (2005: RAC plc) net of transaction costs	3a	892	530
Other issues of share capital, net of transaction costs	27	43	59
Shares issued in lieu of dividends	33	203	100
Reserves credit for equity compensation plans	9	48	22
Other movements		(2)	(1)
Balance at 31 December		23,136	18,746

Where applicable, the accounting policies of the Company are the same as those of the Group on pages 104 to 113. The notes (identified alphabetically) on pages 214 to 218 are an integral part of these separate financial statements. Where the same items appear in the Group financial statements, reference is made to the notes (identified numerically) on pages 120 to 210.

Financial statements of the Company continued

Company balance sheet

At 31 December 2006

	Note	2006 £m	2005 £m
Assets			
Non-current assets			
Investments in subsidiaries	B	27,886	22,919
Investment in joint venture	17c	35	22
Loans owed by subsidiaries		2,641	3,612
Deferred tax assets	D	9	2
Current tax assets		545	200
		31,116	26,755
Current assets			
Loans owed by subsidiaries		645	869
Other amounts owed by subsidiaries		3,163	–
Other assets		78	55
Cash and cash equivalents		5	2
Total assets		35,007	27,681
Equity			
Ordinary share capital	27	641	599
Preference share capital	30	200	200
Called up capital		841	799
Share premium account	27b	1,189	1,167
Merger reserve	E	735	735
Investment valuation reserve	E	17,303	13,322
Equity compensation reserve	E	73	43
Retained earnings	E	2,005	1,690
Direct capital instrument	31	990	990
Total equity		23,136	18,746
Liabilities			
Non-current liabilities			
Borrowings	F	3,135	3,006
Loans owed to subsidiaries		3,720	3,514
		6,855	6,520
Current liabilities			
Borrowings	F	733	499
Loans owed to subsidiaries		1,031	1,121
Other amounts owed to subsidiaries		3,157	701
Other creditors		95	94
Total liabilities		11,871	8,935
Total equity and liabilities		35,007	27,681

Approved by the Board on 28 February 2007.

Andrew Moss, Director

Financial statements of the Company continued

Cash flow statement

For the year ended 31 December 2006

All the Company's operating and investing cash requirements are met by subsidiary companies and settled through intercompany loan accounts. As the direct method of presentation has been adopted for these activities, no further disclosure is required. In respect of financing activities, the following items pass through the Company's own bank accounts.

	2006 £m	2005 £m
Cash flows from financing activities		
Funding provided by subsidiaries	299	880
Net drawdown/(repayment) of borrowings	234	(370)
Preference dividends paid	(17)	(17)
Ordinary dividends paid	(490)	(497)
Interest paid on borrowings	(23)	(25)
Net cash from/(used in) financing activities	3	(29)
Net increase/(decrease) in cash and cash equivalents	3	(29)
Cash and cash equivalents at 1 January	2	31
Cash and cash equivalents at 31 December	5	2

Financial statements of the Company continued

Notes to the Company financial statements

For the year ended 31 December 2006

A – Change in accounting policy

In August 2005, the IASB issued an amendment to IAS 39, *Financial Guarantee Contracts*, which requires financial guarantees issued to be recognised initially at their fair value, and subsequently measured at the higher of the expected liability (or receivable) under the guarantee and the amount initially recognised less any cumulative amortisation. Whilst not material at the Company or consolidated Group level, the amendment affects the Company's subsidiaries in respect of intercompany guarantees given and taken in the ordinary course of business, where guarantee fees had not necessarily reflected the fair value to each party of the issued instrument. This value must now be reflected in each entity's financial statements, and will result in additional accruals (for fee income) and prepayments (for fees payable) in the balance sheets of the affected companies, with movements in these values credited or charged to profit in the relevant income statements. The amendment is effective for the year ended 31 December 2006 and the impact at a Company level was immaterial.

B – Investments in subsidiaries

(i) Movements in the Company's investments in its subsidiaries are as follows:

	2006 £m	2005 £m
Fair value as at 1 January	22,919	19,538
Additions	1,562	2,973
Disposals	(670)	(1,113)
Movement in fair value	4,075	1,521
At 31 December	27,886	22,919

As explained in note 3(a)(iv) of the consolidated financial statements, the Company raised £892 million, net of transaction costs, in July 2006 through the placing of new ordinary shares in connection with the acquisition of AmerUs Group Co. On 2 November 2006, the Company transferred this sum to AGH in return for the issue to it of further new shares in AGH for this amount, which is also included in Additions in the table above.

As part of the ongoing Group restructuring, the Company acquired all the shares in Norwich Union Limited from General Accident plc (GA) in December 2005. The acquisition was at fair value, settled via an intercompany loan, and gave rise to a profit on disposal in GA. The Company carries its investment in GA at its fair value less the balance on this loan. In April 2006, GA declared a dividend of £6,380 million which has been settled against the loan. This does not result in any further impairment of the Company's net investment in GA and therefore the dividend has not been reflected through the income statement.

On 31 July 2006, the Company transferred its entire shareholding in CGNU Holdings (Australia) Limited (renamed Undershaft (No 1) Limited on 12 July 2006) at its fair value to Norwich Union Holdings Limited (since renamed Aviva Group Holdings Limited (AGH)). This gave rise to a profit on disposal of £94 million. The consideration of £670 million was satisfied by the issue of new shares in AGH to the Company for this amount, which is included in Additions in the table above.

At 31 December 2006, the Company has three wholly-owned subsidiaries, all incorporated in Great Britain. These are General Accident plc, Norwich Union Limited and Aviva Group Holdings Limited. Aviva Group Holdings Limited is an intermediate holding company, whilst General Accident plc and Norwich Union Limited no longer carry out this function. The principal subsidiaries of the Aviva Group at 31 December 2006 are listed on pages 244 to 245.

C – Operating expenses

(i) Operating expenses comprise:

	2006 £m	2005 £m
Staff costs and other employee related expenditure	87	62
Other operating costs	71	120
Net foreign exchange losses/(gains)	43	(22)
At 31 December	201	160

(ii) Total staff costs were:

	2006 £m	2005 £m
Wages and salaries	53	43
Social security costs	6	5
Post-retirement obligations		
Defined benefit schemes (see (iii) below)	6	7
Defined contribution schemes	2	–
Profit sharing and incentive plans	1	–
Equity compensation plans (see (iv) below)	17	6
Termination benefits	2	1
At 31 December	87	62

C – Operating expenses continued**(iii) Pension costs**

The Company is one of a number of UK companies being charged for its employees participating in the Aviva Staff Pension Scheme, and its contributions are affected by the financial position of the scheme. There is no contractual agreement or policy for charging the net defined benefit cost for this scheme across the participating Group entities but, instead, this cost is recognised in the financial statements of the main UK employing company. The Company therefore recognises a pension expense equal to its contributions payable in the year for its staff, together with the service cost of any unfunded benefits, within staff costs above.

Full disclosure on the Group's pension schemes is given in note 42.

(iv) Equity compensation plans

All transactions in the Group's equity compensation plans involve options and awards for ordinary shares of the Company. Full disclosure of these plans is given in note 28. The cost of such options and awards is borne by all participating businesses and, where relevant, the Company bears an appropriate charge. As the majority of the charge to the Company relates to directors' options and awards, for which full disclosure is made in the Directors' remuneration report, no further disclosure is given here on the grounds of immateriality.

D – Tax**(i) Tax credited to income statement:**

	2006 £m	2005 £m
Current tax:		
For this year	438	29
Prior year adjustments	76	30
Total current tax	514	59
Deferred tax:		
Origination and reversal of timing differences	7	(5)
Total deferred tax	7	(5)
Total tax credited to income statement	521	54

(ii) Tax reconciliation

The tax on the Company's (loss)/profit before tax differs from the theoretical amount that would arise using the tax rate of the home country of the Company as follows:

	2006 £m	2005 £m
(Loss)/profit before tax	(545)	1,293
Tax calculated at standard UK corporation tax rate of 30% (2005: 30%)	163	(388)
Adjustment to tax charge in respect of prior years	76	30
Non-assessable dividends	259	513
Disallowable expenses	(12)	(23)
Non-taxable profit on sale of subsidiary	28	–
Deferred tax asset not recognised	7	(55)
Other	–	(23)
Total tax credited to income statement	521	54

(iii) The net deferred tax asset comprises:

	2006 £m	2005 £m
Provisions and other temporary differences	9	2
Net deferred tax asset	9	2

Financial statements of the Company continued

Notes to the Company financial statements continued

D – Tax continued

(iv) The movement in the net deferred tax asset was as follows:

	2006 £m	2005 £m
Net asset at 1 January	2	7
Amounts credited/(charged) to profit	7	(5)
Net asset at 31 December	9	2

The Company has unrecognised tax losses of £nil (2005: £167 million) to carry forward against future taxable profits.

E – Reserves

	Merger reserve £m	Investment valuation reserve £m	Equity compensation reserve £m	Retained earnings £m
Balance at 1 January 2005	227	11,801	21	888
Arising in the year:				
Profit for the year	–	–	–	1,347
Fair value gains on investments in subsidiaries	–	1,521	–	–
Dividends and appropriations	–	–	–	(657)
Reserves credit for equity compensation plans	–	–	22	–
Shares issued in lieu of dividends	–	–	–	100
Merger relief on acquisition of RAC plc	508	–	–	–
Aggregate tax effect	–	–	–	13
Other movements	–	–	–	(1)
Balance at 31 December 2005	735	13,322	43	1,690
Arising in the year:				
Loss for the year	–	–	–	(24)
Fair value gains on investments in subsidiaries	–	4,075	–	–
Fair value gains transferred to income statement	–	(94)	–	–
Actuarial losses on pension schemes	–	–	–	(4)
Dividends and appropriations	–	–	–	(762)
Reserves credit for equity compensation plans	–	–	48	–
Shares issued in lieu of dividends	–	–	–	203
Issue of share capital under equity compensation scheme	–	–	(18)	18
Merger relief on acquisition of AmerUs (note 3 (a)(iv))	871	–	–	–
Transfer to retained earnings on realisation of merger reserve	(871)	–	–	871
Aggregate tax effect	–	–	–	15
Other movements	–	–	–	(2)
Balance at 31 December 2006	735	17,303	73	2,005

The issue of new shares to fund the acquisition of AmerUs was effected by a share placing. The placing structure utilised attracted merger relief under section 131 of the Companies Act 1985, resulting in a credit to the merger reserve of £871 million. Subsequent internal transactions required to complete the placing structure have resulted in this part of the merger reserve being realised. Consequently, a transfer of £871 million has been made from the merger reserve to retained earnings.

F – Borrowings

The Company's borrowings comprise:

	2006 £m	2005 £m
Subordinated debt	2,937	2,808
9.5% guaranteed bonds 2016	198	198
Commercial paper	733	499
	3,868	3,505

Maturity analysis of contractual undiscounted cash flows:

	2006			2005		
	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m
Within 1 year	733	222	955	499	205	704
1 – 5 years	–	773	773	–	742	742
5 – 10 years	200	966	1,166	–	928	928
10 – 15 years	692	834	1,526	200	852	1,052
Over 15 years	2,275	260	2,535	2,841	788	3,629
Total contractual undiscounted cash flows	3,900	3,055	6,955	3,540	3,515	7,055

Where subordinated debt is undated, the interest payments have not been included beyond 15 years. Annual interest payments for these borrowings are £68 million (2005: £69 million).

The fair value of the subordinated debt at 31 December 2006 was £3,076 million (2005: £3,148 million). The fair value of the 9.5% guaranteed bonds 2016 at 31 December 2006 was £257 million (2005: £275 million). The fair value of the commercial paper is considered to be the same as its carrying value.

Further details of these borrowings can be found in note 43.

G – Derivative financial instruments**Non-hedge derivatives**

The Company's non-hedge derivative activity at 31 December 2006 was as follows:

	2006			2005		
	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m
Foreign exchange contracts						
OTC						
Forwards	73	–	(2)	40	–	(1)
Total	73	–	(2)	40	–	(1)

H – Contingent liabilities

Details of the Company's contingent liabilities are given in note 46(f).

I – Risk management policies

The business of the Company is managing its investments in subsidiary operations. Its risks are considered to be the same as those in the operations themselves and full details of the risk management policies are given in note 50. The fair values of the subsidiaries themselves are estimated using applicable valuation models, underpinned by the Company's market capitalisation. This uses a three month rolling average of the Company's share price and is therefore sensitive to movements in that price.

Financial statements of the Company continued

Notes to the Company financial statements continued

J – Related party transactions

The Company receives dividend and interest income from subsidiaries and pays interest and fee expense to those subsidiaries in the normal course of business. These activities are reflected in the table below.

Loans to and from subsidiaries, associates and joint ventures are made on normal arm's length commercial terms. The maturity analysis of the related party loans is as follows:

Loans owned by subsidiaries

Maturity analysis	2006 £m	2005 £m
Within 1 year	645	869
1-5 years	1,253	705
Over 5 years	1,388	2,907
	3,286	4,481

Loans owed to subsidiaries

Maturity analysis of contractual undiscounted cash flows	2006			2005		
	Principal £m	Interest £m	Total £m	Principal £m	Interest £m	Total £m
Within 1 year	1,031	240	1,271	1,121	233	1,354
1-5 years	3,372	353	3,725	2,019	540	2,559
Over 5 years	348	74	422	1,495	478	1,973
Total	4,751	667	5,418	4,635	1,251	5,886

Other related party balances comprise dividend and interest receivable and payable, as well as inter-company balances for fees and other transactions in the normal course of business.

Dividends, loans, interest

Services provided to related parties

	Income earned in year 2006 £m	Receivable at year end 2006 £m	Income earned in year 2005 £m	Receivable at year end 2005 £m
Subsidiaries	1,084	6,449	1,925	4,481

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms. Details of guarantees, indemnities and warranties given by the Company on behalf of related parties are given in note 46(f).

Services provided by related parties

	Expense incurred in year 2006 £m	Payable at year end 2006 £m	Expense incurred in year 2005 £m	Payable at year end 2005 £m
Subsidiaries	1,341	7,908	238	5,336

The related parties' payables are not secured and no guarantees were received in respect thereof. The payables will be settled in accordance with normal credit terms.

The directors and key management of the Company are considered to be the same as for the Group. Information on both the Company and Group key management compensation may be found in note 53.

Independent auditor's report to the directors of Aviva plc on the alternative method of reporting long-term business profits

We have audited the alternative method of reporting long-term business on pages 220 to 243 in respect of the year ended 31 December 2006, which comprises a European Embedded Value basis Summarised Consolidated Income Statement, Consolidated Statement of Recognised Income and Expense, Summarised reconciliation of movements in consolidated shareholders' funds, Summarised Consolidated Balance Sheet and the related notes on pages 220 to 243. The alternative method of reporting long-term business has been prepared in accordance with the European Embedded Value Principles published by the CFO Forum in May 2004 and the Additional Guidance on European Embedded Value Disclosures published by the CFO Forum in October 2005 as described on, and using the methodology and assumptions set out on, pages 224 to 226.

This report is made solely to the Company's directors, as a body. Our audit work has been undertaken so that we might state to the Company's directors 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 to anyone other than the Company and the Company's directors as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the alternative method of reporting long-term business on the above European Embedded Value basis.

Our responsibilities, as independent auditors, in relation to the alternative method of reporting long-term business are established in the UK by the Auditing Practices Board and our profession's ethical guidance. We report to you our opinion as to whether the alternative method of reporting long-term business has been properly prepared in accordance with the European Embedded Value basis. We also report to you if we have not received all the information and explanations we require for our audit of the alternative method of reporting long-term business.

Basis of audit opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the alternative method of reporting long-term business stated on the European Embedded Value basis is free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of the alternative method of reporting long-term business.

Opinion

In our opinion the alternative method of reporting long-term business for the year ended 31 December 2006 has been properly prepared in accordance with the European Embedded Value basis, using the methodology and assumptions set out on pages 224 to 226.

Ernst & Young LLP

Registered Auditor
London
28 February 2007

Alternative method of reporting long-term business profits

Summarised consolidated income statement – EEV basis

For the year ended 31 December 2006

2006 1m		2006 £m	2005 £m
	Operating profit before tax attributable to shareholders' profits		
2,990	Life EEV operating return	2,033	1,814
141	Fund management ¹	96	83
2,471	General insurance and health	1,680	1,551
	Other:		
(35)	Other operations ²	(23)	28
(235)	Corporate costs	(160)	(136)
(560)	Unallocated interest charges	(381)	(436)
4,772	Operating profit before tax attributable to shareholders' profits	3,245	2,904
	Adjusted for the following:		
(138)	Impairment of goodwill	(94)	(43)
(68)	Amortisation and impairment of intangibles	(46)	(21)
9	Financial Services Compensation Scheme and other levies	6	–
688	Variation from longer term investment return	468	2,805
987	Effect of economic assumption changes	671	(406)
237	Profit on the disposal of subsidiaries and associates	161	153
(362)	Integration and restructuring costs	(246)	(109)
6,125	Profit before tax	4,165	5,283
(1,512)	Tax on operating profit	(1,028)	(927)
(379)	Tax on other activities	(258)	(674)
4,234	Profit for the year	2,879	3,682
	Attributable to:		
3,894	Equity shareholders of Aviva plc	2,648	3,470
340	Minority interests	231	212
4,234		2,879	3,682

All profit is from continuing operations.

1. Excludes the proportion of the results of Morley's fund management businesses, of our French asset management operation Aviva Gestion d'Actifs (AGA) and other fund management operations within the Group that arises from the provision of fund management services to our Life businesses. These results are included within the Life EEV operating return.
2. 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 materially impact the Group results.

Earnings per share – EEV basis

For the year ended 31 December 2006

2006	Earnings per share	2006	2005
	Operating profit on an EEV basis after tax, attributable to ordinary shareholders in respect of Aviva plc		
116.5c	Basic (pence per share)	79.2p	74.5p
115.1c	Diluted (pence per share)	78.3p	73.9p
	Profit after tax for the year on an EEV basis, attributable to ordinary shareholders of Aviva plc		
154.6c	Basic (pence per share)	105.1p	146.3p
152.8c	Diluted (pence per share)	103.9p	145.1p

Consolidated statement of recognised income and expense – EEV basis

For the year ended 31 December 2006

2006 1m		2006 £m	2005 £m
62	Fair value gains on AFS securities, owner-occupied properties and hedging instruments	42	92
(26)	Fair value (gains)/losses transferred to profit	(18)	14
(3)	Impairment losses on revalued assets	(2)	(45)
(168)	Actuarial (losses) on pension schemes	(114)	(547)
(590)	Foreign exchange rate movements	(401)	(44)
40	Aggregate tax effect – shareholder tax	27	224
(685)	Net (expense) recognised directly in equity	(466)	(306)
4,234	Profit for the year	2,879	3,682
3,549	Total recognised income and expense for the year	2,413	3,376
	Attributable to:		
3,247	Equity shareholders of Aviva plc	2,208	3,184
302	Minority interests	205	192
3,549		2,413	3,376

Summarised reconciliation of movements in consolidated shareholders' funds – EEV basis

For the year ended 31 December 2006

2006 1m		2006 £m	2005 £m
26,188	Balance at 1 January	17,546	14,011
3,601	Total recognised income and expense for the year	2,413	3,376
(1,137)	Dividends and appropriations (note 15)	(762)	(657)
1,331	Issue of share capital for the acquisition of AmerUs Group Co. (2005: RAC plc), net of transaction costs	892	530
64	Other issues of share capital, net of transaction costs	43	59
303	Shares issued in lieu of dividends	203	100
593	Capital contribution from minority shareholders	397	212
(112)	Minority share of dividends declared in the year	(75)	(70)
228	Minority interest in acquired/(disposed) subsidiaries	153	(36)
72	Reserves credit for equity compensation plans	48	22
–	Other movements	–	(1)
31,131	Total equity	20,858	17,546
(3,189)	Minority interests	(2,137)	(1,457)
27,942	Balance at 31 December	18,721	16,089

Alternative method of reporting long-term business profits continued

Summarised consolidated balance sheet – EEV basis

As at 31 December 2006

2006 1m		2006 £m	2005 £m
	Assets		
4,343	Goodwill	2,910	2,274
4,072	Acquired value of in-force business and intangible assets	2,728	803
10,140	Additional value of in-force long-term business	6,794	6,454
4,172	Investments in joint ventures	2,795	2,129
1,336	Investments in associates	895	885
1,349	Property and equipment	904	885
22,572	Investment property	15,123	13,275
39,470	Loans	26,445	24,544
	Financial investments		
168,718	Debt securities	113,041	103,917
84,719	Equity securities	56,762	52,044
49,328	Other investments	33,050	26,427
11,679	Reinsurance assets	7,825	7,130
1,790	Deferred tax assets	1,199	1,018
513	Current tax assets	344	87
12,088	Receivables and other financial assets	8,098	7,706
5,188	Deferred acquisition costs and other assets	3,476	3,766
3,858	Prepayments and accrued income	2,585	2,363
21,704	Cash and cash equivalents	14,542	13,732
–	Assets of operations classified as held for sale	–	462
447,039	Total assets	299,516	269,901
	Equity		
957	Ordinary share capital	641	599
6,657	Capital reserves	4,460	4,438
793	Other reserves	531	834
7,585	Retained earnings	5,082	2,597
10,174	Additional retained profit on an EEV basis	6,817	6,431
26,166	Equity attributable to ordinary shareholders of Aviva plc	17,531	14,899
1,776	Preference share capital and direct capital instrument	1,190	1,190
3,189	Minority interests	2,137	1,457
31,131	Total equity	20,858	17,546
	Liabilities		
215,269	Gross insurance liabilities	144,230	132,602
131,878	Gross liabilities for investment contracts	88,358	77,309
14,127	Unallocated divisible surplus	9,465	8,978
5,687	Net asset value attributable to unitholders	3,810	3,137
4,254	Provisions	2,850	2,875
4,593	Deferred tax liabilities	3,077	2,458
1,884	Current tax liabilities	1,262	1,033
18,115	Borrowings	12,137	11,013
13,784	Payables and other financial liabilities	9,235	9,485
6,317	Other liabilities	4,234	3,320
–	Liabilities of operations classified as held for sale	–	145
415,908	Total liabilities	278,658	252,355
447,039	Total equity and liabilities	299,516	269,901

Approved by the Board on 28 February 2007

Andrew Moss, Director

Segmentation of summarised consolidated balance sheet – EEV basis

As at 31 December 2006

	Life and related businesses 2006 £m	General business and other 2006 £m	Group 2006 £m	Life and related businesses 2005 £m	General business and other 2005 £m	Group 2005 £m
Total assets before acquired additional value of in-force long-term business	252,955	37,961	290,916	224,453	38,679	263,132
Acquired additional value of in-force long-term business	1,806	–	1,806	315	–	315
Total assets included in the statutory IFRS balance sheet	254,761	37,961	292,722	224,768	38,679	263,447
Liabilities of the long-term business	(241,892)	–	(241,892)	(215,624)	–	(215,624)
Liabilities of the general insurance and other businesses	–	(36,766)	(36,766)	–	(36,731)	(36,731)
Net assets on a statutory IFRS basis	12,869	1,195	14,064	9,144	1,948	11,092
Additional value of in-force long-term business ¹	6,794	–	6,794	6,454	–	6,454
Net assets on an EEV basis²	19,663	1,195	20,858	15,598	1,948	17,546
Equity capital, capital reserves, shares held by employee trusts and other reserves			5,632			5,871
IFRS basis retained earnings			5,082			2,597
Additional EEV basis retained profit			6,817			6,431
Equity attributable to ordinary shareholders of Aviva plc on an EEV basis			17,531			14,899
Preference share capital and direct capital instrument			1,190			1,190
Minority interests			2,137			1,457
EEV basis total equity			20,858			17,546

1. The analysis between the Group's and the minority interest's share of the additional value of in-force long-term business is as follows:

	2006 £m	2005 £m	Movement in the year £m
Group's share included in shareholders' funds	6,817	6,431	386
Minority interest share	439	329	110
Movement in AFS securities	(462)	(306)	(156)
Balance at 31 December	6,794	6,454	340

2. Analysis of net assets on an EEV basis is made up as follows:

	2006 £m	2005 £m
Long-term business net assets on an EEV basis	19,663	15,598
Comprises:		
Embedded value	18,098	15,113
RBSG goodwill	217	217
Goodwill and intangible assets allocated to long-term business	1,527	631
Notional allocation of IAS 19 pension fund deficit to long-term business ^{3,4}	(179)	(363)
Long-term business net assets on an EEV basis	19,663	15,598

3. Effective from 31 December 2005, the value of the Aviva Staff Pension Scheme deficit has been notionally allocated between segments, based on current funding and the life proportion has been included within the long-term business net assets on an EEV basis.

4. Effective from 31 December 2006, the pension fund deficit notionally allocated to long-term business is net of the proportion of funding borne by the UK with-profits funds.

Alternative method of reporting long-term business profits continued

Basis of preparation – EEV basis

The summarised consolidated income statement and balance sheet on pages 220 to 222 present the Group's results and financial position for the life and related businesses on the European Embedded Value (EEV) basis and for its non-life businesses on the International Financial Reporting Standards (IFRS) basis. The EEV methodology adopted is in accordance with the EEV Principles introduced by the CFO Forum in May 2004 and the Additional Guidance on EEV Disclosures published by the CFO Forum in October 2005 applicable for financial reporting for the year ending 31 December 2006.

In the Directors' opinion, the EEV basis provides a more accurate reflection of the performance of the Group's life and related operations year on year than results presented under the IFRS basis. The Directors consider that the EEV methodology represents a more meaningful basis of reporting the underlying value of the Group's life and related businesses and the underlying drivers of performance. This basis allows for the impact of uncertainty in the future investment returns more explicitly and is consistent with the way the business is priced and managed.

The Group's approach to establishing economic assumptions (specifically investment returns, required capital and discount rates) was reviewed by Tillinghast, a firm of actuarial consultants, at the time of adopting the EEV principles in 2004. The approach is based on the well established capital asset pricing model theory and is in line with the EEV Principles and Guidance.

The results for 2006 and 2005 have been audited by our auditors, Ernst & Young LLP. Their report in respect of 2006 is included in the Report and Accounts on page 219 of this document.

Covered business

The EEV calculations cover the following lines of business: life insurance, long-term health and accident insurance, savings, pensions and annuity business written by our life insurance subsidiaries, including managed pension fund business and our share of the other life and related business written in our associated undertakings and joint ventures, as well as the equity release business written in the UK. The Group's definition of new business under EEV includes contracts that meet the definition of "non-participating investment" contracts under IFRS.

Covered business includes the Group's share of our joint venture operations including our arrangement with The Royal Bank of Scotland Group (RBSG) and our operations in India and China. In addition, the results of Group companies providing significant administration, investment management and other services and of Group holding companies have been included to the extent that they relate to covered business. Together these businesses are referred to as "Life and related businesses".

New business premiums

New business premiums include:

- premiums arising from the sales of new contracts during the year;
- non-contractual additional premiums, including future Department of Work and Pensions (DWP) rebate premiums; and
- expected renewals on new contracts and expected future contractual alterations to new contracts.

For products sold to individuals, premiums are generally considered to represent new business in certain circumstances, including where a new contract has been signed, or where underwriting has been performed. Renewal premiums include contractual renewals, non-contractual variations that are reasonably predictable and recurrent single premiums that are pre-defined and reasonably predictable.

For group products, new business includes new contracts and increases to aggregate premiums under existing contracts. Renewal premiums are based on the level of premium received during the reporting period and allow for premiums expected to be received beyond the expiry of any guaranteed premium rates.

Foreign exchange adjustments

Embedded value and other balance sheet items denominated in foreign currencies have been translated to sterling using the appropriate closing exchange rate. New business contribution and other income statement items have been translated using an average exchange rate for the relevant period. The exchange rates adopted in this announcement are shown on page 120.

EEV methodology

Overview

Under the EEV methodology, profit is recognised as it is earned over the life of products defined within covered business. The total profit recognised over the lifetime of a policy is the same as under the IFRS basis of reporting, but the timing of recognition is different.

Calculation of the embedded value

The shareholders' interest in the life and related businesses is represented by the embedded value. The embedded value is the total of the net worth of the life and related businesses and the value of in-force covered business. Calculations are performed separately for each business and are based on the cash flows of that business, after allowing for both external and intra-group reinsurance. Where one life business has an interest in another life business, the net worth of that business excludes the interest in the dependent company.

The embedded value is calculated on an after-tax basis applying current legislation and practice together with future known changes. Profits are then grossed up for tax at the full rate of corporation tax for the UK and at an appropriate rate for each of the other countries based on opening year tax rates.

EEV methodology continued**Net worth**

The net worth is the market value of the shareholders' funds and the shareholders' interest in the surplus held in the non-profit component of the long-term business funds, determined on a statutory solvency basis and adjusted to add back any non-admissible assets, and consists of the required capital and free surplus. Required capital is reported net of implicit items permitted on a local regulatory basis to cover minimum solvency margins which are assessed at a local entity basis. The level of required capital for each business, which ranges between 100% and 150% of the EU minimum solvency requirement for our main European businesses and 250% of the EU minimum equivalent solvency requirements in the US, reflects the level of capital considered by the Directors to be appropriate to manage the business, allowing for our internal assessment of the level of market, insurance and operating risk inherent in the underlying products. The same definition of required capital is used for both existing and new business. The free surplus comprises the market value of shareholder assets in excess of local statutory reserves and required capital.

Value of in-force covered business

The value of in-force covered business is the present value at the appropriate risk discount rate (which incorporates a risk margin) of the distributable profits to shareholders arising from the in-force covered business projected on a best estimate basis, less a deduction for the cost of holding the required level of capital.

In the UK, shareholders' distributable profits arise when they are released following actuarial valuations. These valuations are carried out in accordance with statutory requirements designed to ensure and demonstrate solvency in long-term business funds. Future distributable profits will depend on experience in a number of areas such as investment return, discontinuance rates, mortality, administration costs, as well as management and policyholder actions. Releases to shareholders arising in future years from the in-force covered business and associated required capital can be projected using best estimate assumptions of future experience. In overseas businesses generally, there are similar requirements restricting payments to shareholders from life businesses.

The value of in-force covered business includes an allowance for the impact of financial options and guarantees arising from best estimate assumptions (the intrinsic value) and from additional costs related to the variability of investment returns (the time value). The intrinsic value is included in the underlying value of the in-force covered business using deterministic assumptions. The time value of financial options and guarantees has been determined using stochastic modelling techniques.

Stochastic modelling typically involves projecting the future cash flows of the business under thousands of economic scenarios that are representative of the possible future outcomes for market variables such as interest rates and equity returns. Allowance is made, where appropriate, for the effect of management and/or policyholder actions in different economic conditions on future assumptions such as asset mix, bonus rates and surrender rates. The time value is determined by deducting the average value of shareholder cash flows under these economic scenarios from the deterministic shareholder value under best estimate assumptions.

The cost of holding required capital is the difference between the required capital and the present value at the appropriate risk discount rate of the projected release of the required capital and investment earnings on the assets deemed to back the required capital. Where the required capital is covered by policyholder assets, for example in the UK with-profit funds, there is no impact of cost of capital on shareholder value. The assets regarded as covering the required capital are those that the operation deems appropriate.

The value of in-force covered business includes the capitalised value of profits and losses arising from subsidiary companies providing administration, investment management and other services to the extent that they relate to covered business. This is referred to as the "look through" into service company expenses. In addition, expenses arising in holding companies that relate directly to acquiring or maintaining covered business have been allowed for. Where external companies provide services to the life and related businesses, their charges have been allowed for in the underlying projected cost base.

Alternative method of reporting long-term business profits continued

EEV methodology continued**Risk discount rates**

Under the EEV methodology, a risk discount rate (RDR) is required to express a stream of expected future distributable profits as a single value at a particular date (the present value). It is the interest rate that an investment equal to the present value would have to earn in order to be able to replicate exactly the stream of future profits. The RDR is a combination of a risk free rate to reflect the time value of money plus a risk margin to make prudent allowance for the risk that experience in future years may differ from that assumed. In particular, a risk margin is added to allow for the risk that expected additional returns on certain asset classes (e.g. equities) are not achieved.

Risk discount rates for our life businesses have been calculated using a risk margin based upon a Group Weighted Average Cost of Capital (WACC). The Group WACC is calculated using a gross risk free interest rate, an equity risk margin, a market assessed risk factor (beta), and an allowance for the gearing impact of debt financing (including subordinated debt) on a market value basis. The market assessed risk factor captures the market's view of the effect of all types of risk on our business, including operational and other non-economic risk.

The RDR is only one component of the overall allowance for risk in EEV calculations. Risk is also allowed for in the cost of holding statutory reserving margins, additional required capital and in the time value of options and guarantees. Hence to derive the RDR the Group WACC is adjusted to reflect the average level of required capital assumed to be held, and to reflect the explicit valuation of the time value of options and guarantees.

In order to derive risk discount rates for each of our life businesses, the adjusted Group WACC is expressed as a risk margin in excess of the gross risk free interest rate used in the WACC calculation as described above. This risk margin is used for all our main businesses including the US. Business-specific discount rates are then calculated as the sum of this risk margin and the appropriate local gross risk free rate at the valuation date, based on returns on government bonds. A common risk free rate, and hence a common RDR, is used for all of our businesses within the Eurozone. Additional country-specific risk margins are applied to smaller businesses to reflect additional economic, political and business-specific risk. For example, risk margins ranging from 3.7% to 8.7% are applied to the Group's eastern European and Asian operations. Within each business, a constant RDR has been applied in all future time periods and in each of the economic scenarios underlying the calculation of the time value of options and guarantees.

At each valuation date, the risk margin is reassessed based on current economic factors and is updated only if a significant change has occurred. In particular, changes in risk profile arising from movements in asset mix are allowed for via the updated risk margin calculation.

Following the review of the risk margin at 31 December 2006, the Directors have decided to leave the life embedded value risk margin unchanged at 2.7%. The market assessed risk factor (beta) has reduced in recent periods, implying a reduction of the risk in the life business. Management will keep the risk margin under review and will make adjustments as necessary to reflect past trends and future expected trends in the riskiness of the life business, based on the beta.

The sensitivity disclosures on page 240 indicate the impact to the embedded value that would arise from a change in the risk discount rate.

Participating business

Future regular bonuses on participating business are projected in a manner consistent with current bonus rates and expected future returns on assets deemed to back the policies.

For with-profit funds in the UK and Ireland, for the purpose of recognising the value of the estate, it is assumed that terminal bonuses are increased to exhaust all of the assets in the fund over the future lifetime of the in-force with-profit policies. However, under stochastic modelling there may be some extreme economic scenarios when the total assets in the Group's with-profit funds are not sufficient to pay all policyholder claims. The average additional shareholder cost arising from this shortfall has been included in the time value of options and guarantees.

For profit sharing business in continental Europe, where policy benefits and shareholder value depend on the timing of realising gains, apportionment of unrealised gains between policyholders' benefits and shareholders reflect contractual requirements as well as existing practice. Where under certain economic scenarios additional shareholder injections are required to meet policyholder payments, the average additional cost has been included in the time value of options and guarantees.

Consolidation adjustments

The effect of transactions between our life companies such as loans and reinsurance arrangements has been included in results split by territory in a consistent manner. No elimination is required on consolidation.

As the EEV methodology incorporates the impact of profits and losses arising from subsidiary companies providing administration, investment management and other services to the Group's life companies, the equivalent profits and losses have been removed from the relevant segment (non insurance or fund management) and are instead included within the results of life and related businesses. In addition, the underlying basis of calculation for these profits has changed from the IFRS basis to the EEV basis.

The capitalised value of the future profits and losses from such service companies are included in the embedded value and new business contribution calculations for the relevant territory, but the net assets (representing historical profits and other amounts) remain under non insurance or fund management. In order to reconcile the profits arising in the financial period within each segment with the assets on the opening and closing balance sheets, a transfer of IFRS profits from life and related business to the appropriate segment is deemed to occur. An equivalent approach has been adopted for expenses within our holding companies.

Components of life EEV return

The life EEV return comprises the following components:

- new business contribution written during the period including value added between the point of sale and end of the period;
- the profit from existing business equal to:
 - the expected return on the value of the in-force covered business at the beginning of the period,
 - experience variances caused by the differences between the actual experience during the period and expected experience based on the operating assumptions used to calculate the start of year value,
 - the impact of changes in operating assumptions including risk margins;
- the expected investment return on the shareholders' net worth, based upon assumptions applying at the start of the year;
- investment return variances caused by differences between the actual return in the period and the expected return based on economic assumptions used to calculate the start of year value; and
- the impact of changes in economic assumptions in the period.

The life EEV operating return comprises the first three of these components and is calculated using economic assumptions as at the start of the year and operating (demographic, expenses and tax) assumptions as at the end of the year.

Life EEV return	2006 £m	2005 £m
New business contribution (after the effect of required capital)	683	612
Profit from existing business		
– expected return	1,011	895
– experience variances	(50)	(39)
– operating assumption changes	44	17
Expected return on shareholders' net worth	345	329
Life EEV operating return before tax	2,033	1,814
Investment return variances	319	2,288
Effect of economic assumption changes	671	(406)
Life EEV return before tax	3,023	3,696
Tax on operating profit	(630)	(566)
Tax charge on other ordinary activities	(295)	(579)
Life EEV return after tax	2,098	2,551

There were no separate development costs reported in these periods.

Alternative method of reporting long-term business profits continued

New business contribution

The following tables set out the premium volumes and contribution from new business written by the life and related businesses, consistent with the definition of new business set out on page 224.

The contribution generated by new business written during the period is the present value of the projected stream of after tax distributable profit from that business. New business contribution before tax is calculated by grossing up the contribution after tax at the full corporation tax rate for UK business and at appropriate rates of tax for other countries. New business contribution has been calculated using the same economic assumptions as those used to determine the embedded value as at the start of the year and operating assumptions used to determine the embedded value as at the end of the year, and is rolled forward to the end of the financial period. New business contribution is shown before and after the effect of required capital, calculated on the same basis as for in-force covered business.

New business sales are expressed on two bases: annual premium equivalent (APE) and the present value of new business premiums (PVNBP). The PVNBP calculation is equal to total single premium sales received in the year plus the discounted value of regular premiums expected to be received over the term of the new contracts, and is expressed at the point of sale. The premium volumes and projection assumptions used to calculate the present value of regular premiums for each product are the same as those used to calculate new business contribution, so the components of the new business margin are on a consistent basis.

	Annual premium equivalent		Present value of new business premiums		New business contribution before the effect of required capital		New business margin before the effect of required capital ¹	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 %	2005 %
Life and pensions								
France	391	384	3,552	3,530	153	135	4.3%	3.8%
Ireland	190	100	1,273	665	15	16	1.2%	2.4%
Italy	323	252	2,768	2,294	70	59	2.5%	2.6%
Netherlands (including Belgium, Germany and Luxembourg)	270	323	2,346	2,739	56	90	2.4%	3.3%
Poland	72	47	534	320	28	16	5.2%	5.0%
Spain	248	240	2,059	2,013	184	175	8.9%	8.7%
Other Europe	63	51	308	240	(4)	(1)	(1.3)%	(0.4)%
Continental Europe	1,557	1,397	12,840	11,801	502	490	3.9%	4.2%
Asia	107	63	685	396	26	20	3.8%	5.1%
Australia	58	64	297	337	17	16	5.7%	4.7%
United States	97	66	884	527	20	13	2.3%	2.5%
Rest of the World	262	193	1,866	1,260	63	49	3.4%	3.9%
International	1,819	1,590	14,706	13,061	565	539	3.8%	4.1%
United Kingdom	1,439	1,155	11,146	9,185	327	269	2.9%	2.9%
Total (before the effect of required capital)	3,258	2,745	25,852	22,246	892	808	3.5%	3.6%

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

1. New business margin represents the ratio of new business contribution before the effect of required capital to PVNBP, expressed as a percentage.

New business contribution continued

New business contribution before the effect of required capital includes minority interests in 2006 of £175 million (2005: £156 million). This comprises minority interests in France of £24 million (2005: £19 million), Ireland £3 million (2005: £nil), Italy £41 million (2005: £35 million), Netherlands £9 million (2005: £10 million), Poland £4 million (2005: £2 million), Spain £93 million (2005: £89 million), Other Europe nil (2005: £1 million) and Asia £1 million (2005: nil).

	Present value of new business premiums		New business contribution after the effect of required capital		New business margin after the effect of required capital ¹	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 %	2005 %
Life and pensions						
France	3,552	3,530	110	91	3.1%	2.6%
Ireland	1,273	665	9	13	0.7%	2.0%
Italy	2,768	2,294	50	36	1.8%	1.6%
Netherlands (including Belgium, Germany and Luxembourg)	2,346	2,739	25	58	1.1%	2.1%
Poland	534	320	25	14	4.7%	4.4%
Spain	2,059	2,013	168	155	8.2%	7.7%
Other Europe	308	240	(6)	(4)	(1.9)%	(1.7)%
Continental Europe	12,840	11,801	381	363	3.0%	3.1%
Asia	685	396	22	16	3.2%	4.0%
Australia	297	337	9	9	3.0%	2.7%
United States	884	527	8	7	0.9%	1.3%
Rest of the World	1,866	1,260	39	32	2.1%	2.5%
International	14,706	13,061	420	395	2.9%	3.0%
United Kingdom	11,146	9,185	263	217	2.4%	2.4%
Total (after the effect of required capital)	25,852	22,246	683	612	2.6%	2.8%

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

1. New business margin represents the ratio of new business contribution after deducting the effect of required capital to PVNBP, expressed as a percentage.

New business contribution after the effect of required capital includes minority interests in 2006 of £142 million (2005: £120 million). This comprises minority interests in France of £15 million (2005: £10 million), Ireland £1 million (2005: £nil), Italy £29 million (2005: £21 million), Netherlands £7 million (2005: £7 million), Poland £3 million (2005: £2 million), Spain £86 million (2005: £79 million), Other Europe nil (2005: £1 million) and Asia £1 million (2005: nil).

EEV basis – new business contribution before the effect of required capital, tax and minority interest

	Annual premium equivalent		Present value of new business premiums		New business contribution ¹		New business margin ²	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 %	2005 %
Analysed between:								
– Bancassurance channels	942	710	7,737	6,075	369	311	4.8%	5.1%
– Other distribution channels	2,316	2,035	18,115	16,171	523	497	2.9%	3.1%
Total	3,258	2,745	25,852	22,246	892	808	3.5%	3.6%

1. Stated before the effect of required capital.

2. New business margin represents the ratio of new business contribution before the effect of required capital to PVNBP, expressed as a percentage.

Alternative method of reporting long-term business profits continued

EEV basis – new business contribution after the effect of required capital, tax and minority interest

	Annual premium equivalent		Present value of new business premiums ¹		New business contribution ²		New business margin ³	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m	2006 %	2005 %
Analysed between:								
– Bancassurance channels	553	387	4,465	3,238	121	93	2.7%	2.9%
– Other distribution channels	2,252	1,997	17,607	15,815	255	248	1.4%	1.6%
Total	2,805	2,384	22,072	19,053	376	341	1.7%	1.8%

1. Stated after deducting minority interests.

2. Contribution stated after deducting the effect of required capital, tax and minority interests.

3. New business margin represents the ratio of new business contribution after deducting the effect of required capital, tax and minority interests to PVNBP after deducting the minority interests, expressed as a percentage.

Experience variances

Experience variances include the impact of the difference between expense, demographic and persistency assumptions, and actual experience incurred in the year. Also included are variances arising from tax, where such variances are due to management action.

	2006 £m	2005 £m
France	71	32
Netherlands (including Belgium, Germany and Luxembourg)	(9)	2
Rest of Europe	29	13
Continental Europe	91	47
United States	(11)	3
Other	10	6
Rest of the World	(1)	9
International	90	56
United Kingdom	(140)	(95)
Total	(50)	(39)

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

Operating assumption changes

Changes in operating assumptions are made when the assumed future levels of expenses, mortality or other operating assumptions are expected to change permanently.

	2006 £m	2005 £m
France	11	14
Netherlands (including Belgium, Germany and Luxembourg)	56	55
Rest of Europe	(83)	2
Continental Europe	(16)	71
United States	(9)	(10)
Other	9	12
Rest of the World	–	2
International	(16)	73
United Kingdom	60	(56)
Total	44	17

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

Further disclosures on experience variances and operating assumption changes on an EEV basis are provided on pages 233 and 234.

Geographical analysis of life EEV operating return

	2006 £m	2005 £m
France	402	321
Ireland	(40)	20
Italy	110	96
Netherlands (including Belgium, Germany and Luxembourg)	329	349
Poland	162	132
Spain	221	214
Other Europe	(13)	(6)
Continental Europe	1,171	1,126
Asia	37	30
Australia	49	44
United States	32	25
Rest of the World	118	99
International	1,289	1,225
United Kingdom	744	589
Total	2,033	1,814

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

Life EEV operating return includes minority interests in 2006 of £247 million (2005: £216 million). This comprises minority interests in France of £33 million (2005: £24 million), Ireland £(11) million (2005: £nil), Italy £60 million (2005: £52 million), Netherlands £30 million (2005: £17 million), Poland £25 million (2005: £18 million), Spain £108 million (2005: £103 million), Other Europe £nil (2005: £2 million) and Asia £2 million (2005: £nil).

Analysis of movement in life and related businesses embedded value

The following tables provide an analysis of the movement in embedded value for the life and related businesses for 2006 and 2005. The analysis is shown separately for net worth and the value of in-force covered business, and includes amounts transferred between these categories. The transfer to life and related businesses from other segments consists of service company profits and losses during the reported period that have emerged from the value of in-force. Since the "look through" into service companies includes only future profits and losses, these amounts must be eliminated from the closing embedded value. All figures are shown net of tax.

	2006		
	Net worth £m	Value of in-force £m	Total £m
Embedded value at the beginning of the year – Free surplus	2,772		
– Required capital ¹	4,448		
Total	7,220	7,893	15,113
New business contribution (after the effect of required capital)	(602)	1,071	469
Expected return on existing business – return on VIF	–	710	710
Expected return on existing business – transfer to net worth	1,023	(1,023)	–
Experience variances and operating assumption changes	400	(415)	(15)
Expected return on shareholders' net worth	239	–	239
Investment return variances and economic assumption changes	355	340	695
Life EEV return after tax	1,415	683	2,098
Exchange rate movements	(189)	(120)	(309)
Embedded value from business acquired	675	759	1,434
Amounts injected into life and related businesses	393	–	393
Amounts released from life and related businesses	(646)	–	(646)
Transfer to life and related businesses from other segments	113	–	113
UK pension fund deficit borne by UK with-profit funds transferred to analysis of net assets on an EEV basis ²	(98)	–	(98)
Embedded value at the end of the year – Free surplus	3,569		
– Required capital ¹	5,314		
Total	8,883	9,215	18,098

1. Required capital is shown net of implicit items permitted by local regulators to cover minimum solvency margins.

2. The impact of the operating assumption change reflecting the UK with-profits funds contribution to the UK pension scheme deficit funding has been removed from the Life EEV analysis as the pension fund deficit notionally allocated to long-term business net assets on an EEV basis is net of the proportion of funding borne by the UK with-profits funds.

Alternative method of reporting long-term business profits continued

Analysis of movement in life and related businesses embedded value continued

The embedded value of business acquired in 2006 of £1,434 million represents the embedded value of Ark Life Assurance Company Limited, Eagle Insurance Company Limited and AmerUs Group Co.

Required capital has increased in the year by £866 million. The movement comprises an increase of £553 million in relation to new business written, a reduction of £188 million in relation to in-force business, £607 million additional in-force required capital relating to acquisitions during the year and a reduction of £106 million in relation to movements in foreign exchange rates. The decrease in the in-force required capital includes the impact of PS06/14 on the amount of shareholder capital required to support the business and the effect of the increase in long-term interest rates, which has decreased statutory reserves and, therefore, capital requirements.

	2005		
	Net worth £m	Value of in-force £m	Total £m
Embedded value at the beginning of the year – Free surplus	1,894		
– Required capital ¹	4,362		
Total	6,256	6,758	13,014
New business contribution (after the effect of required capital)	(536)	955	419
Expected return on existing business – return on VIF	–	624	624
Expected return on existing business – transfer to net worth	929	(929)	–
Experience variances and operating assumption changes	96	(115)	(19)
Expected return on shareholders' net worth	225	–	225
Investment return variances and economic assumption changes	785	517	1,302
Life EEV return after tax	1,499	1,052	2,551
Exchange rate movements	(54)	(45)	(99)
Embedded value from business disposed of	(19)	(19)	(38)
Amounts injected into life and related businesses	266	–	266
Amounts released from life and related businesses	(751)	–	(751)
Transfer to life and related businesses from other segments	23	–	23
UK Life pension fund deficit transferred to analysis of net assets on an EEV basis ²	–	147	147
Embedded value at the end of the year – Free surplus	2,772		
– Required capital ¹	4,448		
Total	7,220	7,893	15,113

1. Required capital is shown net of implicit items permitted by local regulators to cover minimum solvency margins.

2. Reflecting CFO Forum guidance the pension scheme deficit is now being accounted for on an IAS 19 basis. Consequently, the element that had previously been included in the Life EEV analysis, being the present value of agreed deficit funding payments, has been removed from the Life EEV analysis.

Segmental analysis of the components of life EEV operating return

Year ended 31 December 2006	UK £m	France £m	Ireland £m	Italy £m	Netherlands £m	Poland £m	Spain £m	Other Europe £m	United States £m	Other £m	Total £m
New business contribution (after the effect of required capital)	263	110	9	50	25	25	168	(6)	8	31	683
Profit from existing business											
– expected return	474	142	41	26	158	52	53	9	29	27	1,011
– experience variances:											
Maintenance expenses	13	9	4	(1)	(11)	5	(2)	(2)	–	(2)	13
Exceptional expenses ¹	(149)	1	(4)	–	(23)	–	(1)	(2)	–	–	(178)
Mortality/ Morbidity ²	(13)	33	(2)	4	3	16	1	2	–	15	59
Lapses ³	(66)	8	(9)	(8)	2	21	(1)	(2)	(9)	(3)	(67)
Other ⁴	75	20	(9)	6	20	3	11	(1)	(2)	–	123
	(140)	71	(20)	1	(9)	45	8	(5)	(11)	10	(50)
– operating assumption changes:											
Maintenance expenses ⁵	58	–	(3)	–	60	(3)	–	(11)	(12)	(6)	83
Exceptional expenses ⁶	(46)	(2)	(22)	–	(9)	–	–	(3)	–	–	(82)
Mortality/ Morbidity ⁷	57	45	(13)	–	–	17	–	(1)	3	11	119
Lapses ⁸	(224)	(41)	(47)	–	(14)	17	(21)	(1)	–	2	(329)
Other ⁹	215	9	–	2	19	1	2	3	–	2	253
	60	11	(85)	2	56	32	(19)	(13)	(9)	9	44
Expected return on shareholders' net worth	87	68	15	31	99	8	11	2	15	9	345
Life EEV operating return before tax	744	402	(40)	110	329	162	221	(13)	32	86	2,033

1. Exceptional expenses in the UK reflect £32 million relating to the ongoing transformation of the life business and £117 million of other exceptional and project costs associated with strategic initiatives, including developments designed to improve the future new business volumes, and regulatory changes. In the Netherlands, exceptional expenses reflect higher project costs compared to allowances as well as the payment to ABN AMRO in respect of the joint venture operations.

2. Mortality experience continues to be better than the assumptions set across many of our businesses.

3. Lapse experience in the UK has been worse than assumed and primarily relates to bonds and pensions. In Poland, lapses for both life and pension products have been lower than assumed resulting in the favourable experience variances.

4. In the UK, other experience profits include better than assumed default experience on corporate bonds and mortgages and the benefit of higher than expected performance fees in Morley.

5. Maintenance expenses in UK relate to Morley's change in profit margin. The change in Delta Lloyd is driven by improved asset management profitability. The adverse movement in the US is due to a reassessment of expenses in Boston-based operations.

6. In the UK, exceptional expenses relate to short-term project costs and capitalisation of reorganisation costs. Ireland reflects changes in expense assumptions regarding the future attribution of investment income and expenses between policyholders and shareholders.

7. The change in mortality assumptions in the UK includes an alignment in the basis for internal business. Mortality assumptions in France were changed following improvements in mortality experience over the last few years.

8. In the UK, the lapse assumption change relates to bonds and pension business while the change in Ireland relates to the Celebration Bond and unit-linked bonds. In France, lapse assumptions have been changed for non-AFER business in Aviva Vie. In Spain, lapse assumptions have been changed for risk business and some savings products.

9. In the UK, the assumption changes reflect the beneficial impact of the with-profit funds sharing the pension scheme deficit funding (£126 million) and the impact of PS06/14, primarily in reducing the non-profit reserves (£50 million). In Delta Lloyd the impact is due to changes to management fee rebates.

Alternative method of reporting long-term business profits continued

Segmental analysis of the components of life EEV operating return

Year ended 31 December 2005	UK £m	France £m	Ireland £m	Italy £m	Netherlands £m	Poland £m	Spain £m	Other Europe £m	United States £m	Other £m	Total £m
New business contribution (after the effect of required capital) 217		91	13	36	58	14	155	(4)	7	25	612
Profit from existing business											
– expected return	425	122	29	30	148	50	48	10	13	20	895
– experience variances:											
Maintenance expenses	12	3	(2)	(2)	3	5	(2)	1	(1)	(3)	14
Exceptional expenses ¹	(151)	–	(5)	–	(12)	–	(2)	–	–	–	(170)
Mortality/Morbidity ²	86	29	(1)	2	16	16	5	–	(1)	6	158
Lapses ³	(78)	(4)	(9)	(4)	2	5	1	(5)	5	4	(83)
Other ⁴	36	4	(4)	4	(7)	10	2	(2)	–	(1)	42
	(95)	32	(21)	–	2	36	4	(6)	3	6	(39)
– operating assumption changes:											
Maintenance expenses	(20)	–	1	(3)	25	3	1	(6)	(12)	3	(8)
Exceptional expenses	(4)	(3)	–	–	(2)	–	–	1	–	–	(8)
Mortality/Morbidity ⁵	19	1	(4)	4	(25)	8	–	1	–	5	9
Lapses ⁶	(130)	–	(8)	–	(10)	–	(2)	(2)	–	4	(148)
Other ⁷	79	16	–	–	67	11	(2)	(1)	2	–	172
	(56)	14	(11)	1	55	22	(3)	(7)	(10)	12	17
Expected return on shareholders' net worth	98	62	10	29	86	10	10	1	12	11	329
Life EEV operating return before tax	589	321	20	96	349	132	214	(6)	25	74	1,814

1. Exceptional expenses in the UK reflect £47 million relating to ongoing transformation of the life business and £101 million of other exceptional and project costs associated with regulatory change and strategic initiatives.

2. Mortality experience continues to be better than assumed across most of our businesses, and particularly for protection business in the UK, AFER and unit-linked business in France and group business in the Netherlands.

3. Lapse experience in the UK has been worse than assumed and mainly relates to bonds and pension business. In Ireland, the adverse persistency has mainly arisen on unit-linked pensions business.

4. In the UK, other experience profits includes better than assumed default experience on corporate bonds and commercial mortgages.

5. Mortality assumptions have been revised in the Netherlands following the publication of new annuitant mortality tables used for group business.

6. In the UK, the adverse lapse assumption change reflects a more prudent allowance for future persistency experience in the UK following recent experience. In Ireland, the lapse assumption change mainly relates to unit-linked pension business. Lapse assumption changes in the Netherlands largely relate to group business in the intermediary division.

7. Other operating assumption changes in the UK primarily relate to the change in annuitant required capital to 150% of required minimum margins which results in a £110 million one-off benefit. In France other operating assumptions represent an allowance for further tax benefits arising from dividends from subsidiaries. In the Netherlands, they reflect a variety of changes including increased annual management fees on unit-linked contracts, favourable change in asset mix, and the reduction of future guaranteed returns on group pensions business in Belgium. In Poland it was previously assumed that the introduction of new individual pension products would lead to significant conversion of existing policies. The prudent allowance made for this is no longer required.

Segmental analysis of life and related businesses embedded value

	Net worth		Value of in-force covered business		Total
	Required capital ¹ £m	Free surplus £m	Present value of in-force £m	Cost of required capital £m	Embedded value £m
31 December 2006					
France	1,143	250	1,142	(244)	2,291
Ireland	254	143	535	(40)	892
Italy	320	329	206	(63)	792
Netherlands (including Belgium, Germany and Luxembourg)	1,067	1,701	1,461	(362)	3,867
Poland	105	107	540	(33)	719
Spain	273	37	606	(59)	857
Other Europe	18	25	75	(12)	106
Continental Europe	3,180	2,592	4,565	(813)	9,524
United States ²	618	211	794	(145)	1,478
Other	182	125	204	(51)	460
Rest of the World	800	336	998	(196)	1,938
International	3,980	2,928	5,563	(1,009)	11,462
United Kingdom	1,334	641	5,103	(442)	6,636
Total	5,314	3,569	10,666	(1,451)	18,098

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

1. Required capital is shown net of implicit items permitted by local regulators to cover minimum solvency margins.
2. AmerUs holding company debt amounting to £362 million at 31 December 2006 has been included with non-insurance.

	Net worth		Value of in-force covered business		Embedded value	
	2006 £m	2005 £m	2006 £m	2005 £m	2006 £m	2005 £m
As at 31 December 2006						
France	1,393	1,264	898	803	2,291	2,067
Ireland	397	286	495	353	892	639
Italy	649	602	143	114	792	716
Netherlands (including Belgium, Germany and Luxembourg)	2,768	2,204	1,099	933	3,867	3,137
Poland	212	214	507	445	719	659
Spain	310	262	547	463	857	725
Other Europe	43	42	63	54	106	96
Continental Europe	5,772	4,874	3,752	3,165	9,524	8,039
United States	829	254	649	77	1,478	331
Other	307	289	153	106	460	395
Rest of the World	1,136	543	802	183	1,938	726
International	6,908	5,417	4,554	3,348	11,462	8,765
United Kingdom	1,975	1,803	4,661	4,545	6,636	6,348
Total	8,883	7,220	9,215	7,893	18,098	15,113

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

The shareholders' net worth is the market value of the shareholders' funds and the shareholders' interest in the surplus held in the non-profit component of the long-term business funds, determined on a statutory solvency basis and adjusted to add back any non-admissible assets. Required capital, net of implicit items, of £5,314 million at 31 December 2006 (31 December 2005: £4,448 million) is included within the net worth.

The value of in-force covered business includes the effect of holding shareholders' capital to support the level of required capital and allowing for projected future releases. This impact reduces the value of in-force covered business at 31 December 2006 by £1,451 million (31 December 2005: £1,187 million).

The embedded value at the end of 2006 includes minority interests of £1,387 million (2005: £1,000 million). This comprises minority interests in France of £162 million (2005: £148 million), Ireland £216 million (2005: nil), Italy £413 million (2005: £365 million), Netherlands £102 million (2005: £70 million), Poland £118 million (2005: £107 million), Spain £366 million (2005: £310 million) and Other £10 million (2005: nil).

Alternative method of reporting long-term business profits continued

Time value of options and guarantees

The following table sets out the time value of options and guarantees relating to covered business by territory at 31 December 2006 and 31 December 2005.

	2006 £m	2005 £m
France	77	84
Ireland	2	3
Italy	17	19
Netherlands (including Belgium, Germany and Luxembourg)	146	118
Poland	4	5
Spain	4	8
Other Europe	–	2
Continental Europe	250	239
United States	68	11
Other	4	5
Rest of the World	72	16
International	322	255
United Kingdom	50	48
Total	372	303

Germany has been reclassified from Other Europe to the Netherlands, Lithuania has been reclassified from Other Europe to Poland and Norwich Union's Dublin-based offshore life and savings business has been reclassified from Other Europe to the United Kingdom.

The time value of options and guarantees (TVOG) is most significant in the United Kingdom, France, the Netherlands and the United States. In the United Kingdom, this relates mainly to non-market value adjustment (MVA) guarantees on unitised with-profit business and guaranteed annuity rates. In France, this relates mainly to guaranteed crediting rates and surrender values on traditional business including the AFER fund. In the Netherlands, this relates mainly to maturity guarantees on unit-linked products and interest rate guarantees on traditional individual and Group profit sharing business. In the United States, this relates to crediting rate, death benefit and surrender on life business.

The TVOG has increased to £372 million reflecting acquired TVOG from AmerUs of £56 million.

Minority interest in life and related businesses' EEV results

	Shareholders' interest £m	Minority interest £m	2006 Group £m	2005 Group £m
New business contribution before effect of required capital	717	175	892	808
Effect of required capital	(176)	(33)	(209)	(196)
New business contribution including effect of required capital	541	142	683	612
Life EEV operating return before tax	1,786	247	2,033	1,814
Life EEV return before tax	2,744	279	3,023	3,696
Attributed tax	(830)	(95)	(925)	(1,145)
Life EEV return after tax	1,914	184	2,098	2,551
Closing life and related businesses' embedded value	16,711	1,387	18,098	15,113

Principal economic assumptions – deterministic calculations

Economic assumptions are derived actively, based on market yields on risk-free fixed interest assets at the end of each reporting period. The same margins are applied on a consistent basis across the Group to gross risk-free yields to obtain investment return assumptions for ordinary shares and property and to produce risk discount rates. Additional country-specific risk margins are applied to smaller businesses to reflect additional economic, political and business-specific risk, which result in the application of risk margins ranging from 3.7% to 8.7% in our eastern European and Asian business operations. Expense inflation is derived as a fixed margin above a local measure of long-term price inflation. Risk free rates and price inflation have been harmonised across territories within the Euro currency zone, except for expense inflation in Ireland where significant differences remain. Required capital is shown as a multiple of the EU statutory minimum solvency margin or equivalent.

Investment return assumptions are generally derived by major product class, based on hypothecating the assets at the valuation date. Future assumed reinvestment rates are consistent with implied market returns at 31 December 2006. Rates have been derived using rates from the current yield curve at a duration based on the term of the liabilities, or directly from forward yield curves where considered appropriate. Assumptions about future investment mix are consistent with long-term plans. In most cases, the investment mix is assumed to continue unchanged throughout the projection period. The changes in assumptions between reporting dates reflect the actual movements in risk free yields in the United Kingdom, the Eurozone and other territories. The principal economic assumptions used are as follows:

	UK			France		
	2006	2005	2004	2006	2005	2004
Risk discount rate	7.3%	6.8%	7.3%	6.7%	6.0%	6.4%
Pre-tax investment returns:						
Base government fixed interest	4.6%	4.1%	4.6%	4.0%	3.3%	3.7%
Ordinary shares	7.6%	7.1%	7.6%	7.0%	6.3%	6.7%
Property	6.6%	6.1%	6.6%	6.0%	5.3%	5.7%
Future expense inflation	3.4%	3.2%	3.3%	2.5%	2.5%	2.5%
Tax rate	30.0%	30.0%	30.0%	34.4%	34.4%	34.9%
Required Capital (% EU minimum)	150%/100%	150%/100%	200%/100%	115%	115%	115%

	Ireland			Italy		
	2006	2005	2004	2006	2005	2004
Risk discount rate	6.7%	6.0%	6.4%	6.7%	6.0%	6.4%
Pre-tax investment returns:						
Base government fixed interest	4.0%	3.3%	3.7%	4.0%	3.3%	3.7%
Ordinary shares	7.0%	6.3%	6.7%	7.0%	6.3%	6.7%
Property	6.0%	5.3%	5.7%	6.0%	5.3%	5.7%
Future expense inflation	4.0%	4.0%	4.0%	2.5%	2.5%	2.5%
Tax rate	12.5%	12.5%	12.5%	38.3%	38.3%	38.3%
Required Capital (% EU minimum)	150%	150%	150%	115%	115%	115%

	Netherlands			Poland		
	2006	2005	2004	2006	2005	2004
Risk discount rate	6.7%	6.0%	6.4%	8.7%	8.6%	9.7%
Pre-tax investment returns:						
Base government fixed interest	4.0%	3.3%	3.7%	5.0%	4.9%	6.0%
Ordinary shares	7.0%	6.3%	6.7%	8.0%	7.9%	9.0%
Property	6.0%	5.3%	5.7%	n/a	n/a	n/a
Future expense inflation	2.5%	2.5%	2.5%	3.4%	3.3%	3.4%
Tax rate	25.5%	29.1%	31.5%	19.0%	19.0%	19.0%
Required Capital (% EU minimum)	150%	150%	150%	150%	150%	150%

Alternative method of reporting long-term business profits continued

Principal economic assumptions – deterministic calculations continued

	Spain			US		
	2006	2005	2004	2006*	2005	2004
Risk discount rate	6.7%	6.0%	6.4%	7.4%	7.2%	7.1%
Pre-tax investment returns:						
Base government fixed interest	4.0%	3.3%	3.7%	4.7%	4.5%	4.4%
Ordinary shares	7.0%	6.3%	6.7%	n/a	n/a	n/a
Property	6.0%	5.3%	5.7%	n/a	n/a	n/a
Future expense inflation	2.5%	2.5%	2.5%	3.0%	3.0%	3.0%
Tax rate	30.0%	35.0%	35.0%	35.0%	35.0%	35.0%
Required Capital (% EU minimum or equivalent)	125%/110%	125%/110%	125%/110%	250%	200%	200%

* The principal economic assumptions used for AmerUs Group Co. at the date of acquisition were as follows: risk discount rate of 7.2%, pre-tax investment returns of 4.6% for base government fixed interest and required capital of 250%.

For service companies, expense inflation relates to the underlying expenses rather than the fees charged to the life company. Future returns on corporate fixed interest investments are calculated from prospective yields less an adjustment for credit risk. Required capital in the United Kingdom is 150% EU minimum for Norwich Union Annuity Limited and 100% for other companies. Required capital in Spain is 125% EU minimum for Aviva Vida y Pensiones and 110% for bancassurance companies. The level of required capital for the US business is 250% of the risk based capital at the company action level set by the National Association of Insurance Commissioners. The required capital is equivalent to 5% of the insurance liabilities on a local regulatory basis which is broadly equivalent to the required capital we hold for our main European businesses.

Other economic assumptions

Required capital relating to with-profit business is assumed to be covered by the surplus within the with-profit funds and no effect has been attributed to shareholders.

Bonus rates on participating business have been set at levels consistent with the economic assumptions and Aviva's medium-term bonus plans. The distribution of profit between policyholders and shareholders within the with-profit funds assumes that the shareholder interest in conventional with-profit business in the United Kingdom and Ireland continues at the current rate of one ninth of the cost of bonus.

Principal economic assumptions – stochastic calculations

The time value of options and guarantees calculation allows for expected management and policyholder actions in response to varying future investment conditions. The management actions modelled include changes to asset mix and bonus rates. Modelled policyholder actions are described under "Other assumptions".

This section describes the models used to generate future investment simulations, and gives some sample statistics for the simulations used. Two separate models have been used, for the UK businesses and for International businesses, as each of these models better reflect the characteristics of the businesses.

United Kingdom

Model

Overall asset returns have been generated assuming that the portfolio total return has a lognormal distribution. The mean and standard deviation of the overall asset return have been calculated using the evolving asset mix of the fund and assumptions over the mean and standard deviation of each asset class, together with correlations between them.

Asset Classes

The significant asset classes for UK participating business are equities, property and long-term fixed rate bonds. The most significant assumption is the distribution of future long-term interest rates, since this is the most important factor in the cost of guaranteed annuity options.

Summary Statistics

The following table sets out the means and standard deviations (StDev) of future returns at 31 December 2006 for the three most significant asset classes. Interest rates are assumed to have a lognormal distribution with an annualised standard deviation of 12.5% p.a. for the natural logarithm of the interest rate.

	Mean ¹	StDev ²
Equities	7.6%	20%
Property	6.6%	15%
Government Bonds	4.6%	3.25-4.5% ³

1. Means have been calculated by accumulating a unit investment for the required number of years in each simulation, averaging the accumulation across all simulations, and converting the result to an equivalent annual rate (by taking the nth root of the average accumulation minus 1).

2. Standard deviations have been calculated by accumulating a unit investment for the required number of years in each simulation, taking the natural logarithm of the result, calculating the variance of this statistic, dividing by the projection period (n years) and taking the square root. This makes the result comparable to implied volatilities quoted in investment markets.

3. Depending on the duration of the portfolio.

Principal economic assumptions – deterministic calculations continued

For the UK, the statistics are the same over all projection horizons. Assumptions are also required for correlations between asset classes. These have been set based on an assessment of historical data. Returns for corporate fixed interest investments in each scenario are equal to the return on Government bonds plus a fixed additional amount, based on current spreads less a margin for credit risk.

**International
Model**

Government nominal interest rates are generated by a model that projects a full yield curve at annual intervals. The model assumes that the logarithm of the short rate follows a mean reverting process subject to two normally distributed random shocks. This ensures that nominal interest rates are always positive, the distribution of future interest rates remains credible, and the model can be calibrated to give a good fit to the initial yield curve.

The total annual return on equities is calculated as the return on 1-year bonds plus an excess return. The excess return is assumed to have a lognormal distribution. The model also generates property total returns and real yield curves, although these are not significant asset classes for Aviva outside the UK.

Asset Classes

The most important assets are fixed rate bonds of various durations. In some businesses equities are also an important asset class.

Summary Statistics

The following table sets out the means and standard deviations of future euro and US dollars returns at 31 December 2006 for the three most significant asset classes: equities (in the case of Euro), short-term bonds (defined to be of 1-year duration) and long-term bonds (defined to be 10-year zero coupon bonds). In the accumulation of 10-year bonds, it is assumed that these are held for one year, sold as 9-year bonds then the proceeds are reinvested in 10-year bonds, although in practice businesses follow more complex asset strategies or tend to adopt a buy and hold strategy. Correlations between asset classes have been set using the same approach as described for the United Kingdom.

	5-year return		10-year return		20-year return	
	Mean ¹	StDev ²	Mean ¹	StDev ²	Mean ¹	StDev ²
Euro						
Short Government Bonds	3.7%	1.7%	3.7%	3.0%	3.8%	5.3%
Long Government Bonds	4.2%	3.8%	4.1%	2.9%	4.1%	3.3%
Equities	7.0%	19.5%	6.9%	19.3%	6.9%	19.0%
US dollar						
Short Government Bonds	4.5%	2.0%	4.4%	3.5%	4.7%	6.7%
Long Government Bonds	5.0%	4.5%	4.8%	3.7%	5.0%	4.4%

1. Means have been calculated by accumulating a unit investment for the required number of years in each simulation, averaging the accumulation across all simulations, and converting the result to an equivalent annual rate (by taking the nth root of the average accumulation minus 1).

2. Standard deviations have been calculated by accumulating a unit investment for the required number of years in each simulation, taking the natural logarithm of the result, calculating the variance of this statistic, dividing by the projection period (n years) and taking the square root. This makes the result comparable to implied volatilities quoted in investment markets.

Other assumptions**Taxation**

Current tax legislation and rates have been assumed to continue unaltered, except where changes in future tax rates have been announced.

Demographic assumptions

Assumed future mortality, morbidity and lapse rates have been derived from an analysis of Aviva's recent operating experience. Where appropriate, surrender and option take up rate assumptions that vary according to the investment scenario under consideration have been used in the calculation of the time value of options and guarantees, based on our assessment of likely policyholder behaviour in different investment scenarios.

Expense assumptions

Management expenses and operating expenses of holding companies attributed to life and related businesses have been included in the EEV calculations and split between expenses relating to the acquisition of new business, the maintenance of business in-force and project expenses. Future expense assumptions include an allowance for maintenance expenses and a proportion of recurring project expenses. Certain expenses of an exceptional nature, when they occur, are identified separately and are generally charged as incurred. No future productivity gains have been anticipated.

Where subsidiary companies provide administration, investment management or other services to businesses included in the European Embedded Value calculations, the value of profits or losses arising from these services have been included in the embedded value and new business contribution.

Valuation of debt

Borrowings in the EEV consolidated balance sheet are valued on an IFRS basis, consistent with the primary financial statements.

At 31 December 2006 the market value of the Group's external debt, subordinated debt, preference shares including General Accident plc preference shares of £250 million (classified as minority interests) and direct capital instrument was £5,991 million (31 December 2005: £5,868 million).

Alternative method of reporting long-term business profits continued

Principal economic assumptions – deterministic calculations continued

	2006 £m	2005 £m
Borrowings per summarised consolidated balance sheet – EEV basis	12,137	11,013
Less: Securitised mortgage funding	(7,068)	(6,303)
Borrowings excluding non-recourse funding – EEV basis	5,069	4,710
Less: Operational financing by businesses	(874)	(900)
External debt and subordinated debt – EEV basis	4,195	3,810
Add: Preference shares (including General Accident plc) and direct capital instrument	1,440	1,440
External debt, subordinated debt, preference shares and direct capital instrument – EEV basis	5,635	5,250
Effect of marking these instruments to market	356	618
Market value of external debt, subordinated debt, preference shares and direct capital instrument	5,991	5,868

Other

It has been assumed that there will be no changes to the methods and bases used to calculate the statutory technical provisions and current surrender values, except where driven by varying future investment conditions under stochastic economic scenarios.

Sensitivity analysis – economic assumptions

The tables below show the sensitivity of the embedded value as at 31 December 2006 and the new business contribution before the effect of required capital for 2006 to:

- one percentage point increase and decrease in the discount rates;
- one percentage point increase and decrease in interest rates, including all consequential changes (including assumed investment returns for all asset classes, market values of fixed interest assets, risk discount rates);
- one percentage point increase and decrease in the assumed investment returns for equity and property investments, excluding any consequential changes to the risk discount rate;
- 10% rise and fall in market value of equity and property assets (not applicable for new business contribution); and
- decrease in the level of required capital to 100% EU minimum (or equivalent) (not applicable for new business contribution).

In each sensitivity calculation, all other assumptions remain unchanged except where they are directly affected by the revised economic conditions. For example, future bonus rates are automatically adjusted to reflect sensitivity changes to future investment returns. Some of the sensitivity scenarios may have consequential effects on valuation bases, where the basis for certain blocks of business is actively updated to reflect current economic circumstances. Consequential valuation impacts on the sensitivities are allowed for where an active valuation basis is used. Where businesses have a target asset mix, the portfolio is re-balanced after a significant market movement otherwise no re-balancing is assumed.

Embedded value (net of tax) 31 December 2006	As reported on page 235 £m	1% increase in discount rates £m	1% decrease in discount rates £m	1% increase in interest rates £m	1% decrease in interest rates £m
France	2,291	(135)	155	(90)	85
Ireland	892	(40)	40	(30)	30
Italy	792	(20)	25	(5)	(60)
Netherlands (including Belgium, Germany and Luxembourg)	3,867	(165)	195	50	(210)
Poland	719	(35)	40	(5)	5
Spain	857	(45)	50	(25)	25
Other Europe	106	(5)	5	–	–
Continental Europe	9,524	(445)	510	(105)	(125)
United States	1,478	(80)	85	(85)	85
Other	460	(15)	20	–	–
Rest of the World	1,938	(95)	105	(85)	85
International	11,462	(540)	615	(190)	(40)
United Kingdom	6,636	(470)	560	(310)	350
Total	18,098	(1,010)	1,175	(500)	310

Sensitivity analysis – economic assumptions continued

Embedded value (net of tax) 31 December 2006	As reported on page 235 £m	1% increase in equity/ property returns £m	1% decrease in equity/ property returns £m	10% rise in equity/ property market values £m	10% fall in equity/ property market values £m	EU minimum capital (or equivalent) £m
France	2,291	75	(75)	115	(135)	40
Ireland	892	20	(20)	30	(30)	15
Italy	792	10	(10)	10	(10)	10
Netherlands (including Belgium, Germany and Luxembourg)	3,867	225	(225)	405	(415)	95
Poland	719	10	(10)	10	(10)	10
Spain	857	15	(15)	15	(15)	5
Other Europe	106	–	–	–	–	5
Continental Europe	9,524	355	(355)	585	(615)	180
United States	1,478	25	(10)	5	(5)	80
Other	460	5	(5)	10	(10)	5
Rest of the World	1,938	30	(15)	15	(15)	85
International	11,462	385	(370)	600	(630)	265
United Kingdom	6,636	220	(230)	435	(435)	95
Total	18,098	605	(600)	1,035	(1,065)	360

In general, the magnitude of the sensitivities will reflect the size of the embedded values, though this will vary as the sensitivities have different impacts on the different components of the embedded value. In addition, other factors can have a material impact, such as the nature of the options and guarantees, as well as the types of investments held. The interest rate sensitivity will vary significantly by territory, depending on the type of business written: for example, where non-profit business is well matched by backing assets, the favourable impact of reducing the risk discount rate is the dominant factor.

Sensitivities will also vary according to the current economic assumptions, mainly due to the impact of changes to both the intrinsic cost and time value of options and guarantees. Options and guarantees are the main reason for the asymmetry of the sensitivities where the guarantee impacts to different extents under the different scenarios. This can be seen in the sensitivity of a 1% movement in the interest rate for the Netherlands, where there is a significant amount of business with investment return guarantees. The increase of 70 basis points to the assumed pre-tax investment returns at 31 December 2006 has significantly decreased this sensitivity, reflecting the level of the guarantees relative to the interest rate assumption.

Sensitivities to a 1% movement in the equity/property return will only impact the value of the in-force covered business, whereas a 10% movement in equity/property values may impact both the net worth and the value of in-force, depending on the allocation of assets.

New business contribution before required capital (gross of tax) 31 December 2006	As reported on page 228 £m	1% increase in discount rates £m	1% decrease in discount rates £m	1% increase in interest rates £m	1% decrease in interest rates £m
France	153	(13)	15	(1)	(2)
Ireland	15	(4)	4	(2)	1
Italy	70	(4)	5	2	(12)
Netherlands (including Belgium, Germany and Luxembourg)	56	(10)	11	43	(39)
Poland	28	(2)	3	–	1
Spain	184	(12)	14	(5)	5
Other Europe	(4)	(2)	2	(1)	–
Continental Europe	502	(47)	54	36	(46)
United States	20	(3)	3	(1)	(2)
Other	43	(8)	9	3	(4)
Rest of the World	63	(11)	12	2	(6)
International	565	(58)	66	38	(52)
United Kingdom	327	(55)	65	(20)	23
Total	892	(113)	131	18	(29)

Alternative method of reporting long-term business profits continued

Sensitivity analysis – economic assumptions continued

New business contribution before required capital (gross of tax) 2006	As reported on page 228 £m	1% increase in equity/ property returns £m	1% decrease in equity/ property returns £m
France	153	6	(6)
Ireland	15	2	(2)
Italy	70	1	(1)
Netherlands (including Belgium, Germany and Luxembourg)	56	16	(21)
Poland	28	1	(1)
Spain	184	2	(1)
Other Europe	(4)	1	(1)
Continental Europe	502	29	(33)
United States	20	1	(1)
Other	43	1	(1)
Rest of the World	63	2	(2)
International	565	31	(35)
United Kingdom	327	31	(31)
Total	892	62	(66)

Sensitivity analysis – non-economic assumptions

The tables below show the sensitivity of the embedded value as at 31 December 2006 and the new business contribution before the effect of required capital for 2006 to the following changes in non-economic assumptions:

- 10% decrease in maintenance expenses (a 10% sensitivity on a base expense assumption of £10pa would represent an expense assumption of £9pa). Where there is a “look through” into service company expenses, the fee charged by the service company is unchanged while the underlying expense decreases;
- 10% decrease in lapse rates (a 10% sensitivity on a base assumption of 5% pa would represent a lapse rate of 4.5%pa);
- 5% decrease in both mortality and morbidity rates disclosed separately for life assurance and annuity business.

No future management actions are modelled in reaction to the changing non-economic assumptions. In each sensitivity calculation, all other assumptions remain unchanged. No changes to valuation bases have been included.

Embedded value (net of tax) 31 December 2006	As reported on page 235 £m	10% decrease in maintenance expenses £m	10% decrease in lapse rates £m	5% decrease in in mortality/ morbidity rates – life insurance £m	5% decrease in in mortality/ morbidity rates – annuity business £m
France	2,291	35	35	20	(5)
Ireland	892	20	20	5	(5)
Italy	792	5	–	–	–
Netherlands (including Belgium, Germany and Luxembourg)	3,867	75	15	15	(45)
Poland	719	20	35	10	–
Spain	857	10	40	15	(5)
Other Europe	106	5	5	–	–
Continental Europe	9,524	170	150	65	(60)
United States	1,478	25	15	15	(5)
Other	460	10	10	10	–
Rest of the World	1,938	35	25	25	(5)
International	11,462	205	175	90	(65)
United Kingdom	6,636	180	85	75	(120)
Total	18,098	385	260	165	(185)

New business contribution before required capital (gross of tax) 31 December 2006	As reported on page 228 £m	10% decrease in maintenance expenses £m	10% decrease in lapse rates £m	5% decrease in in mortality/ morbidity rates – life insurance £m	5% decrease in in mortality/ morbidity rates – annuity business £m
France	153	5	7	6	–
Ireland	15	2	4	1	–
Italy	70	2	2	1	–
Netherlands (including Belgium, Germany and Luxembourg)	56	10	9	5	(2)
Poland	28	2	3	2	–
Spain	184	4	19	5	–
Other Europe	(4)	–	1	–	(1)
Continental Europe	502	25	45	20	(3)
United States	20	1	(1)	–	(1)
Other	43	3	4	1	–
Rest of the World	63	4	3	1	(1)
International	565	29	48	21	(4)
United Kingdom	327	21	25	23	(4)
Total	892	50	73	44	(8)

The demographic sensitivities shown above represent a standard change to the assumptions for all products. Different products will be more or less sensitive to the change, and impacts may partially offset.

Aviva Group of companies

Parent Company

Aviva plc

Subsidiaries

The principal subsidiaries of the Company are listed below by country of incorporation. All are wholly-owned, directly or indirectly, and transact insurance or reinsurance business, fund management or services in connection therewith, unless otherwise stated.

United Kingdom

Aviva Employment Services Limited
Aviva Insurance Limited
Aviva International Insurance Limited
CGNU Life Assurance Limited
CGU Bonus Limited
CGU Underwriting Limited
Commercial Union Life Assurance Company Limited
Gresham Insurance Company Limited
HPI Limited
Lifetime Group Limited
London & Edinburgh Insurance Group Limited
Morley Fund Management Limited
Morley Pooled Pensions Limited
Norwich Union Annuity Limited
Norwich Union Central Services Limited
Norwich Union Collective Investments Limited
Norwich Union Consumer Products Limited
Norwich Union Equity Release Limited
Norwich Union Healthcare Limited
Norwich Union Insurance Limited
Norwich Union Insurance Services Limited
Norwich Union Investment Funds Limited
Norwich Union Life (RBS) Limited
Norwich Union Life & Pensions Limited
Norwich Union Life Services Limited
Norwich Union Risk Services Limited
NUI Investments Limited
RAC Auto Windscreens Limited
RAC Insurance Limited
RAC Motoring Services
RAC plc
The British School of Motoring Limited

Australia

Aviva Australia Holdings Limited and its principal subsidiaries:
Norwich Union Life Australia Limited
Navigator Australia Limited
Portfolio Partners Limited

Belgium

Delta Lloyd Life N.V.

Bermuda

Aviva Re Limited

Canada

Aviva Canada Inc and its principal operating subsidiaries:
Aviva Insurance Company of Canada
Pilot Insurance Company
Traders General Insurance Company

Czech Republic

Aviva zivotni pojist'ovna, a.s.

France

Aviva Participations SA and its principal subsidiaries:

Antarius S.A. (50.0%)
Aviva Assurances S.A.
Aviva Courtage S.A.
Aviva France SA
Aviva Gestion d'Actifs S.A.
Aviva Vie SA
Eurofil S.A.
Société d'Epargne Viagère SA (75.0%)
Union Financière de France Banque (Banking) (76.3%)

Germany

Delta Lloyd Deutschland AG and its principal subsidiary:
Delta Lloyd Lebensversicherung AG (99.5%)

Hong Kong

Aviva Life Insurance Company Limited

Hungary

Aviva Életbiztosító Részvénytársaság

Ireland

Hibernian Group plc and its principal subsidiaries:

Ark Life Assurance Company Limited
Hibernian General Insurance Limited
Hibernian Life & Pensions Limited
Hibernian Investment Managers Limited

Italy

Aviva Italia Holding S.p.A and its principal subsidiaries:

Aviva Assicurazioni S.p.A (50.0%)
Aviva Italia S.p.A
Aviva Life SpA (50.0%)
Aviva Previdenza S.p.A (50.0%)
Aviva Vita S.p.A (25.5%)
Eurovita Assicurazioni S.p.A (41.5%)

Lithuania

UAB Commercial Union Lietuva Gyvybes draudimas

Luxembourg

Commercial Union International Life SA

Netherlands

Delta Lloyd N.V. and its principal subsidiaries:

Delta Lloyd ABN AMRO Verzekeringen Holding BV (51.0%)
Delta Lloyd Asset Management N.V.
Delta Lloyd Bankengroep N.V. (Banking)
Delta Lloyd Levensverzekering N.V.
Delta Lloyd Schadeverzekering N.V.
Delta Lloyd Zorgverzekering NV
OHRA Schadeverzekeringen N.V.
OHRA Levensverzekeringen N.V.

Poland

Commercial Union Polska – Towarzystwo Ubezpieczen
Ogolnych SA (90.0%)
Commercial Union Polska – Towarzystwo Ubezpieczen Na
Zycie SA (90.0%)
Commercial Union Powszechnie Towarzystwo Emerytalne
BPH CU WBK S.A. (75.0%)

Romania

Aviva Asigurari de Viata SA

Singapore

Aviva Limited

Spain

Aseguradora Valenciana SA, de Seguros y

Reaseguros (Aseval) (50.0%)

Aviva Vida y Pensiones, Sociedad Anonima de

Seguros y Reaseguros

Bia Galicia, de Seguros y Reaseguros SA (50.0%)

Caja Espana Vida, Compania de Seguros y Reaseguros (50.0%)

General Vida, Sociedad Agencia de Seguros, S.L. (25.0%)

Unicorp Vida, Compania de Seguros y Reaseguros (50.0%)

Sri Lanka

Eagle Insurance Company Limited (51.0%)

Turkey

Aviva Hayat ve Emeklilik A.S

Aviva Sigorta A.S. (98.6%)

United States

AmerUs Group Co and its principal subsidiaries:

American Investors Life Insurance Company, Inc.

AmerUs Annuity Group Co. (AAG)

AmerUs Life Insurance Company

Aviva Capital Management

Bankers Life Insurance Company of New York

ILICO Holdings, Inc.

Indianapolis Life Insurance Company Limited

Aviva USA Corporation and its principal operating subsidiaries:

Aviva Life Insurance Company

Aviva Life Insurance Company of New York

Associates and joint ventures

The Group has ongoing interests in the following operations that are classified as associates or joint ventures. Further details of those operations that were most significant in 2006 are set out in notes 17 and 18

United Kingdom

RBS Life Investments Limited (49.99%)

RBSG Collective Investments Limited (49.99%)

British Aviation Insurance Company Limited (38.1%)

The Group also has interests in several property limited partnerships. Further details are provided in note 17

China

AVIVA – COFCO Life Insurance Co. Limited (50.0%)

India

Aviva Life Insurance Company India Private Limited (26.0%)

Shareholder services

Managing your shareholding:

The Company's Register of members is maintained by the Company's Registrar, Lloyds TSB Registrars. Shareholders who have any queries in respect of their shareholding should refer to them via the contact details provided below. In addition to assisting with general queries the Registrar can also help with the following:

Amalgamating different share accounts

If shareholders received more than one copy of this Annual Report, it could be because there is more than one record for the shareholder on the share register. To ensure that duplicate mailings are avoided the Registrar can arrange for accounts to be amalgamated.

Dividend payments direct to your bank account

As an alternative to having dividends paid by cheque, shareholders can, if they wish, have them credited directly into their bank or building society account on the dividend payment date. Having the dividend paid directly into their bank account offers shareholders the benefits of avoiding the risk of cheques being lost in the post, and is more convenient as payment is credited automatically on the payment date. The tax voucher is sent to the shareholder's registered address as usual. Shareholders wishing to set up a dividend mandate can do so on the Company's website www.aviva.com/dividendmandate. For overseas shareholders, a TAPS (Transcontinental Automated Payment Service) is available, which allows shareholders in many countries to have dividends credited direct to their bank accounts in local currencies.

Consolidated Tax Vouchers

Private shareholders who currently receive dividends paid directly into their bank or building society account receive one consolidated tax voucher each year instead of a voucher with each dividend payment, unless they request otherwise.

Scrip Dividend

The Aviva Scrip Dividend Scheme (the "Scheme") provides shareholders with the opportunity to receive their dividends in the form of new ordinary shares in the Company instead of cash. Shareholders who have not joined the Scheme but wish to do so should contact Lloyds TSB Registrars and request a mandate form. The completed mandate form will need to be received by Lloyds TSB Registrars no later than 18 April 2007 in order to be effective for the 2006 final dividend. Further details are included on the Company's website www.aviva.com/scripdividend.

A range of shareholder frequently asked questions and practical help on transferring shares and updating details is available online at www.aviva.com/shareholders.

Annual General Meeting

The 2007 Annual General Meeting of the Company will be held at the Barbican Centre, Silk Street, London EC2Y 8DS on Thursday, 26 April 2007 at 11.00am. The Notice of Meeting, together with details of the business to be conducted at the Meeting, is being circulated to shareholders with this Annual Report, and can also be viewed on the Company's website www.aviva.com/agm.

Share dealing

The Company has arranged the following services that can be used to buy or sell Aviva shares. Alternatively, if shareholders hold a share certificate they can also use any bank, building society or stockbroker offering share dealing facilities to sell their shares. Shareholders in any doubt about buying or selling their shares should seek professional financial advice.

Share dealing facilities for UK shareholders/share account members

- You can buy or sell shares via the internet or by telephone through Shareview Dealing, a share dealing service provided by Lloyds TSB Registrars. For internet purchases and sales log on to www.shareview.co.uk/dealing and for telephone purchases and sales call 0870 850 0852 between 8.00am and 4.30pm, Monday to Friday. All 0870 numbers are charged at national rates, and are only available if you are calling from the UK. Lloyds TSB Registrars is authorised and regulated by the Financial Services Authority, registered number 119278.
- To buy or sell shares over the telephone, shareholders can contact Barclays Stockbrokers on 0870 549 3002 (for shareholders with a share certificate) or 0870 549 3001 (for shareholders with a share account statement). To check instructions and maintain high quality service standards, Barclays Stockbrokers may record and monitor calls. New Business Development hours are 8.00am and 6.00pm Monday to Friday, excluding Bank Holidays. Barclays Stockbrokers is authorised and regulated by the Financial Services Authority, registered number 124247.
- NatWest Stockbrokers provide a Share Dealing Service either over the telephone or at certain NatWest branches for Aviva Share Account holders only. For more information contact NatWest Stockbrokers on 0845 122 0689. NatWest Stockbrokers Limited (NWS) is a member of the London Stock Exchange and PLUS. NWS is authorised and regulated by the Financial Services Authority, registered number 124395. Registered Office: Waterhouse Square, 138-142 Holborn, London EC1N 2TH. Registered Number 1959479, England. NWS is operated by a joint venture between The Royal Bank of Scotland Group plc and The Toronto-Dominion Bank.

Share dealing facilities for overseas shareholders

To sell Aviva shares over the telephone, shareholders can contact Barclays Stockbrokers on +44 (0)141 352 3959. Non-UK residents will need to provide various documentation in order to use this service and details will be provided on registration. Please note that regulations prevent this service from being offered to US, Canadian and Australian residents. Settlement proceeds will be sent to either a UK sterling bank account or by sterling cheque.

ShareGift

The Orr Mackintosh Foundation operates a purely voluntary charity share donation scheme for shareholders who wish to dispose of small numbers of shares when the dealing costs or minimum fee makes it uneconomical to sell them. Details of the scheme are available from ShareGift at www.sharegift.org or can be obtained from the Company's Registrar.

Share price

Shareholders can access the current share price of Aviva plc ordinary shares at www.aviva.com or alternatively can call 0906 843 2197. Calls are currently charged at 60 pence per minute at all times. The average time to access the share price is approximately one minute.

Shareholder information**Shareholder profile**

The categories of ordinary shareholders and the range and size of shareholdings as at 31 December 2006 are set out below:

Analysis of shareholders	No. of shareholders	%	No. of shares	%
Individuals	635,178	97.3	247,766,201	9.66
Banks and nominee companies	13,395	2.05	2,199,002,281	85.71
Pension fund managers and insurance companies	97	0.02	114,546	0
Other corporate bodies	4,093	0.63	118,870,403	4.63
Total	652,763	100	2,565,753,431	100

Range of shareholdings	No. of shareholders	%	No. of shares	%
1 – 1,000	605,297	92.73	161,544,158	6.29
1,001 – 5,000	42,844	6.56	77,809,156	3.03
5,001 – 10,000	2,126	0.33	14,545,784	0.57
10,001 – 250,000	1,841	0.28	100,615,743	3.92
250,001 – 500,000	186	0.03	66,136,616	2.58
500,001 and above	469	0.07	2,145,101,974	83.61
Total	652,763	100	2,565,753,431	100

Group financial calendar for 2007

Announcement of first quarter long-term savings new business figures	24 April
Annual General Meeting	26 April
Announcement of unaudited six months' interim results	9 August
Announcement of third quarter long-term savings new business figures	25 October

Ordinary shares

Ex-dividend date	7 March
Record date	9 March
Scrip dividend price available	14 March
Dividend payment date	17 May

Preference shares

First dividend payment for 8%% cumulative irredeemable preference shares	31 March
First dividend payment for 8%% cumulative irredeemable preference shares	30 June
Second dividend payment for 8%% cumulative irredeemable preference shares	30 September
Second dividend payment for 8%% cumulative irredeemable preference shares	31 December

Shareholder services continued

Useful contact details

Detailed below are the contact details that shareholders may find useful if they have a query in respect of their shareholding.

Please quote Aviva plc, as well as the name and address in which the shares are held, in all correspondence. If you have a shareholder reference, please have this available as well.

General shareholding, administration queries and Aviva share account queries	Lloyds TSB Registrars www.shareview.co.uk e-mail: aviva@lloydstsb-registrars.co.uk	The Causeway Worthing West Sussex BN99 6DA	0870 600 3952
Corporate and single company Peps	Barclays Stockbrokers Limited www.stockbrokers.barclays.co.uk	Tay House 300 Bath Street Glasgow G2 4LH	0870 514 3263
Individual Savings Accounts (ISAs)	Lloyds TSB Registrars (ISA Manager)	The Causeway Worthing West Sussex BN99 6DA	0870 242 4244

Internet sites

Aviva owns various internet sites, most of which interlink with each other.

Aviva Group	www.aviva.com
UK long-term savings and general insurance	www.norwichunion.com
Fund management	www.morleyfm.com
Aviva worldwide internet sites	www.aviva.com/websites

Aviva plc

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We are committed to caring for the environment and looking for sustainable ways to minimise our impact on it.

This year our annual report and accounts has been printed by Burlington. We choose Burlington because not only do they have the important environmental certification by SGS for the FSC standards, but also they take innovative steps to minimise their impact on the environment even further. A great example of this is where they plan to use naturally cooled water from their well to supply the existing air conditioning system.

Based in Foxton in Cambridgeshire, Burlington are a privately owned business employing over 100 local people, as a rural employer they play a significant part in supporting the community.

Also we take care to minimise the impact on the environment in the paper we use, the paper we have used, 9lives 55™, is produced using 55% recycled fibre from both pre- and post consumer sources using an elemental chlorine free process and the remaining virgin fibre using a totally chlorine free process. The virgin fibre is sourced from well managed forests. The paper is FSC certified and manufactured at an ISO 14001 accredited mill.



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forests, controlled sources and
recycled wood or fiber
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FSC – Forest Stewardship Council. This ensures there is an audited chain of custody from the tree in the well managed forest through to the finished document in the printing factory.

ISO 14001 – A pattern of control for an environmental management system against which an organisation can be credited by a third party.

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