



HHG PLC

Full Annual Financial
Report and Accounts

For the year ended 31 December 2004

www.hhg.com



Profit turnaround from a loss of £864million in 2003 to profit before tax* of £41million in 2004.

* Profit before tax represents the profit before tax for the year attributable to shareholders of HHG PLC (the Company).

HHG PLC

Company Registration Number:
2072534

Henderson Global Investors – strong performance

Operating profit up 63%

Cost to income ratio improved to 79%

Assets under management of £69.1billion

Life Services – improved value

Embedded value up 27%

Costs down 30%

Operating profit up 6%

Realising shareholder value

Share price up 49%

Market capitalisation up 64%

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HHG Share Price

CDI v ASX 100

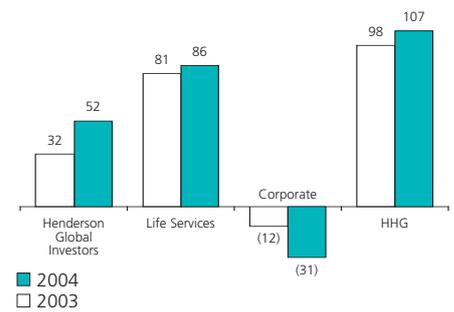


HHG Share Price

Ordinary Shares v FTSE 250



Operating Profit before tax and other items (£m)



During 2004, we made good progress against our business objectives, including solid improvements in operating profit and efficiency.

We further strengthened our financial position and created shareholder value by restructuring the Group and through the turnaround in, and the proposed sale of, the Life Services business.

We took action to improve the capital position and operational structure of the Group. We exited non-core or non-performing businesses through the divestiture of our investment in Virgin Money and the closure of Towry Law International.

We improved the regulatory capital position, increased provisions against risks across the business and reduced costs where we could. In addition, we simplified the Group by buying out the remaining holding in HHG Invest plc from Pearl and in the second half we entered into an agreement to sell the Life Services business and put forward proposals to return the majority of proceeds to shareholders.

All of these actions have helped to create a stronger, more streamlined Group and ensures we are well placed for the future.



The Board is committed to creating shareholder value. We believe the Group is well placed for the future and will, over time, deliver the right returns to shareholders.

Rupert Pennant-Rea, Chairman, HHG

Chairman's Statement

A significant year

I am pleased to report to you as your new Chairman after what has been a challenging and rewarding year for HHG. In 2004, our first 12 months as a listed group, we built a strong independent Group and produced significantly better financial results. The improvement in the businesses has culminated in the proposed sale of the Life Services business, which was overwhelmingly approved at our recent Extraordinary General Meeting. This step has strategic as well as financial significance, and has realised encouraging value for shareholders.

Financial results and Group structure

For the year to 31 December 2004, HHG made a profit before tax of £41 million (compared with a loss of £864 million in 2003). This improvement was due to good growth in profits at Henderson Global Investors and a turnaround in Life Services. Henderson Global Investors' performance reflects the recovery in equity markets and a shift to higher margin business. In Life Services we improved efficiency, embedded value and capital strength – essential steps to increasing the value of this business.

During the year, we simplified the Group structure. The proceeds from an additional placing of ordinary shares enabled us to acquire full ownership of Henderson Global Investors by purchasing the remaining interest of HHG Invest plc from Pearl. We also sold our 50% equity interest in Virgin Money Group Limited in April 2004, and, taking account of difficult market conditions and following a strategic review, we closed the operations of Towry Law International to new business.

Sale of the Life Services business and return of capital to shareholders

When HHG listed in December 2003, the Board said that a key part of HHG's strategy

was to maximise shareholder value from the closed life insurance books. The proposed sale of the Life Services business accelerates the release of capital and also removes exposure to the UK life insurance sector and its associated regulatory, solvency, mortality and surrender risks. The Life Services management and staff have done an excellent job of creating value for shareholders while maintaining the quality of service they provide for policyholders.

Once we receive the cash from the sale of the Life Services business, we intend to return approximately £885 million directly to shareholders in a two-stage process that will reduce issued share capital. The first step involves a pro-rata cancellation of 52 out of every 100 shares held, at a price of 55 pence per share. The remaining organisation will be considerably smaller, and could not sensibly afford to service 875,000 shareholders. So, as a second step, we will cancel smaller holdings in return for a cash payment. This will reduce the number of shareholders to around 150,000.

Looking ahead

Following the expected completion of the sale of the Life Services business, HHG will be renamed Henderson Group plc and its stock ticker code will be changed from HHG to HGI. The Henderson Group will consist of the asset management business of Henderson Global Investors and the smaller financial advisory business of Towry Law. Our central goal is to develop Henderson Global Investors as a leading pan-European investment manager.

Corporate Responsibility Policy

During the year, HHG developed its Corporate Responsibility Policy (outlined on page 16). This sets out the Group's commitment to responsible business conduct with all stakeholders.

The Board

Last year, the Board undertook an evaluation of its own performance to assess its effectiveness and to ensure we have the right blend of experience and skills. The Board is responsible for securing the interests of shareholders, and we need to be sure we are doing that.

During 2004, four new Directors were appointed: John Roques (January 2004), Duncan Ferguson (July 2004), Gerry Aherne and myself (October 2004). Biographies of all the Directors are on pages 12 and 13.

Departures included the two AMP Limited Directors appointed as part of the Demerger, Andrew Mohl, who resigned in February 2004 and Pat Handley in May. Peter Costain, who served the Group for just over 10 years, retired from the Board in February 2005. I thank them all for their support and advice.

The most significant change on the Board was the retirement in February 2005 of Sir Malcolm Bates as HHG's Chairman. He steered the Board through every phase of the Group's evolution to where it now is. The Board and the Group will miss his wealth of experience and constant guidance.

There will be two more changes in the near future. Sir William Wells will retire at the 2005 Annual General Meeting. Ian Laughlin will be staying with the Life Services business, so will retire from the Board when the sale is completed.

From June 2005, the Board will then consist of two Executive Directors and five Non-Executive Directors. This should be the right size and balance for the smaller business, and is in line with the UK's Combined Code and the ASX Corporate Governance Council's Principles of Good Corporate Governance.

The Board operates under formal corporate governance codes, principles and processes. These are described in detail on pages 17 to 20.

Dividends

Your Board knows that shareholders value dividends and we want to provide these in the next year. We aim to ensure that the Henderson Group can sustain a flow of dividends into the future. Assuming the sale of the Life Services business goes through, we expect to pay a final 2005 dividend in early 2006.

Shareholders

Henderson Group will continue to be listed on both the London and Australian Stock Exchanges, and is expected to remain in the FTSE 250 and ASX 200 indices.

In February 2005, 65% of HHG shares were held by investors in Australasia (including the 10% held by AMP as part of the Demerger and some 25% held by retail shareholders). Approximately 30% were held by investors in Europe and the remainder was split across the rest of the world.

Let me end by thanking all employees for their hard work, and particularly for not being distracted during a year of many changes. I would also like to thank all shareholders for their support and encouragement during our first year on the public market.



The Group has a solid platform on which to build further value for shareholders – we look forward to the future with confidence.

Roger Yates, Chief Executive, HHG

Chief Executive's Statement

2004 was the first full year for the Group after its Demerger from AMP and it is satisfying to report a much improved set of results, as well as a simplification of the Group structure. The Chairman's Statement covers the initiatives which we undertook to streamline the Group.

As regards the underlying performance of the businesses, operating profit before tax, exceptionals and other items rose by just over 9% in 2004 to £107 million. This reflected solid performances in both Henderson Global Investors and Life Services, where profits increased by 63% and 6% respectively.

The rise in Henderson Global Investors' operating profit from £32 million in 2003 to £52 million in 2004 was driven by a recovery in equity markets and by improving fee margins. In addition, growth in revenue ensured a significant drop in the cost to income ratio from 84% in 2003 to 79% in 2004. Assets under management remained relatively stable year-on-year at £69.1 billion in 2004, down slightly from £70.6 billion in 2003, as the expected outflows from the closed life books and institutional funds were partly offset by market growth and inflows elsewhere in the business.

Life Services produced a stable operating profit of £86 million, up 6% on 2003. The first half of 2004 was impacted negatively by a necessary adjustment to the annuitant mortality assumptions which was mitigated to some extent by the release of prudential margins. The Service Company turned an £8 million loss in 2003 into an £8 million profit in 2004 as a result

of significant cost reduction initiatives which ensured the cost base fell below £120 million. In relation to our Other Businesses, we exited non-core or non-performing businesses during the period, completing the sales of AMPLE and our 50% equity holding in Virgin Money Group Limited and announcing the closure of Towry Law International. Towry Law UK remains within the Group and open to new business. It reported a breakeven position in 2004.

During the year, Corporate costs were tightly managed, although the overall level increased as a result of the establishment of additional provisions – the majority of which related to Towry Law International. Corporate costs should return to the levels experienced in the first half of 2004. However, from mid-way through 2005, the Group should also start to benefit from the anticipated £4 million annual saving on shareholder servicing costs.

Strategy

When the sale of the Life Services business completes, the new company, Henderson Group plc, will be a simpler organisation comprising Henderson Global Investors and the much smaller financial advisory business, Towry Law. The strategic focus of the Henderson Group will be asset management.

Our objective is to build Henderson Global Investors into a more profitable and more valuable business. This will be based on both our core equities and fixed income capabilities and our range of alternative products such as property, private capital and hedge funds. In particular, we intend to continue to improve

margins measured by revenues as a percentage of funds under management by continuing to reorient the business to higher margin areas such as UK and European mutual funds and the alternative products referred to above. This was demonstrated in 2004 by the rise in total margins on average assets under management to 34 basis points (bps) (2003: 28 bps).

In addition, we remain committed to improving Henderson Global Investors' expense ratio to a target of 75% over the medium term. We expect that this will be achieved principally by revenue growth as opposed to cost cutting – in fact, costs could increase in 2005 as we continue important investment in people and infrastructure. The principal financial measures of success will be the trends in revenues, margins and profits, rather than the growth in assets under management. Given the likely outflows of assets in Life Services (which we will continue to manage under revised investment management agreements) and from the institutional area, it is possible that assets under management could fall while profits rise, as was the case in 2004.

Ultimately, a good financial outcome for Henderson Global Investors must be based upon delivering successful results to its clients. Investment performance remains the lifeblood of any fund management business. We have recently completed a reorganisation of our investment operations to ensure that we deliver on that score. Clearly, longer term investment success will depend on our ability to retain talented investment managers at a time when demand for and rewards to them have never been greater.

As regards Towry Law in the UK, our plan is to develop it as a standalone business. The first task is to generate acceptable margins on revenues and the management of Towry Law has worked hard on cost reduction in 2004 to create a platform for a better business unit result in 2005.

People

As I stated in the 2003 Annual Report, I see great benefit in building share ownership amongst employees. This allows us to align employee interests with those of shareholders. We introduced a number of share incentive schemes, of which more detail is provided on pages 71 to 73. We expect to introduce further share incentive schemes in 2005 which we hope will encourage the delivery of real outperformance.

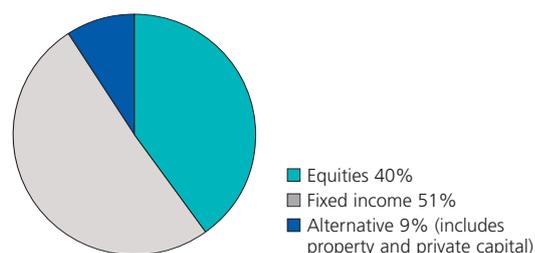
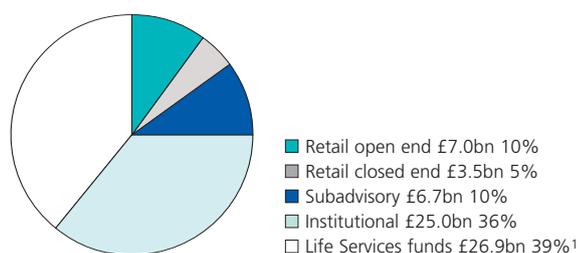
Outlook

The Group has a solid platform on which to build further value for shareholders. Fund management is a growth business with potential for good margins and good returns on capital. The medium and long-term prospects for the business are good and we look forward to the future with confidence.

Henderson Global Investors – Assets Under Management (AUM)

AUM 31 Dec 2004 by line of business

AUM 31 Dec 2004 by asset class



Note 1. This does not include £1.2bn of Life Services assets which are invested into Henderson retail products.

Operational and Financial Review

Henderson Global Investors

Henderson Global Investors is a pan-European investment manager and manufactures a broad range of actively managed investment products for institutional and retail investors, across multiple asset classes including equities, fixed income, private equity and property.

Business strategy

Henderson Global Investors' objective is to build a scaleable, profitable, active investment management business, based on its core equity and fixed interest investment capabilities and emerging alternative products.

To achieve this, Henderson Global Investors will:

- deliver saleable investment performance;
- develop a sustainable entrepreneurial culture to attract and retain the best people;
- leverage market ideas to support a "fast-follower" strategy in core products and a leading edge position in specialist products;
- improve net margin by better co-ordinating marketing, distribution and client servicing activities; and
- deliver a 75% cost to income ratio over the medium term.

Strong 2004 result – 63% up on 2003

The improvement in Henderson Global Investors' result in 2004 (operating profit before tax of £52 million, up 63% from the previous year) reflects the recovery in equity markets from their low in early 2003 and management focus on improving fee margins. Total fee income of £234 million was 21% up on 2003 as a result of stronger investment markets as well as a change and improvement in product mix towards higher margin business.

Focused expenditure, alongside improved revenues, ensured a further reduction in the cost to income ratio to 79% in 2004, well below the 84% cost to income ratio for the full year 2003.

Operating expenses grew 18% to £185 million in 2004 as control over business-as-usual costs was offset by an expected increase of investment in people and infrastructure. The majority of this increase related to variable costs such as incentivisation attached to improved operational performance and charges for pension contributions.

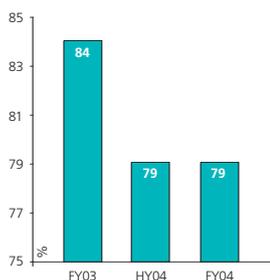
Henderson Global Investors won 19 investment performance awards in 2004. These awards span a range of products, from long equities to hedge funds and property and include six Standard & Poor's first place awards. In addition, Henderson Global Investors won several awards for marketing excellence and property development during the year.

In the second half of 2004, management reorganised investment operations and this included adding two new positions to Henderson Global Investors' senior management team (the Head of Fixed Income and the Head of Equities). In addition, restructuring steps have been taken to revitalise the UK distribution business to ensure we are in a position to regain market share and deliver consistent investment performance in all areas, although it will take time for this to flow through.

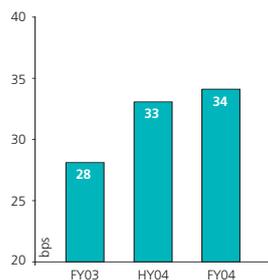
Henderson Global Investors is refreshing its retail product range and optimising its access to wholesale channels in the UK. Servicing institutional clients remains a priority both to minimise outflows and target specialist mandates to replace the margins from outflows in traditional balanced mandates. Outside of the UK, Henderson Global Investors continues to successfully nurture relationships with external distributors, such as MM Warburg & Co. in Germany and Banca Popolare di Lodi (BPL), a 1,000 branch bank in Italy.

Henderson Global Investors

Cost to income ratio

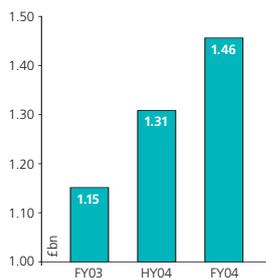


Revenue margins over AUM

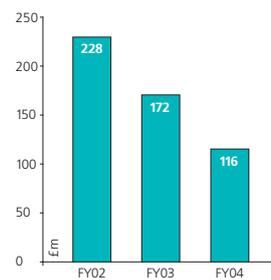


Life Services

Embedded value



Cost base



Total assets under management (AUM) rose in the second half of 2004 from £68.4 billion at 30 June to £69.1 billion by year end. This was slightly below the level for 2003 despite the expected net outflows in external funds and Life Services' funds. Positive market movements and net external fund inflows into higher margin products were the offsetting positives. As part of the agreement to sell the Life Services business, Henderson Global Investors will continue to manage the Life Services' life funds under revised investment management agreements on a ten year term.

Outlook

Henderson Global Investors is a well diversified business and management's objective is to build the operation into a more profitable and valuable business. We plan to improve the total margin, measured by revenue as a percentage of AUM, by continuing to orient the business to higher margin products. In addition, management is focused on improving the cost to income ratio to a target of 75% over the medium term by growing revenue. While investment markets are still likely to present some challenges, the Group has a strong foundation for sustained growth and profitability from the asset management operations of Henderson Global Investors.

Life Services

Life Services comprises the life insurance and pension books of Pearl, National Provident Life, NPI Limited and London Life. Life Services has approximately 4.6 million policies in force and £28 billion of assets under management across annuities, pensions, savings, investment products, industrial branch business and protection policies – all of which are closed to new business.

Stable 2004 result – 6% up on 2003

Life Services produced a relatively stable operational profit year-on-year of £86 million in 2004 compared to £81 million in 2003. However, the second half 2004 profit (£54 million) was significantly above the first half of 2004 (£32 million) which was adversely impacted by strengthening of annuitant mortality assumptions for NPLL and NPIL related business in that period.

During 2004, the Service Company reduced its cost base ahead of lower levels of income, enabling it to deliver an £8 million profit compared to an £8 million loss in 2003.

Life Services continues to receive general insurance profits from the release of margins in technical provisions supporting the run-off of that business. In particular, profits rose due to significant commutations in the second half of 2004 and as a result of the ongoing arrangement with Churchill, which manufactures products under the Pearl brand.

Shareholder interests increased to £14 million in the year compared to a loss of £12 million for 2003. This result largely reflected the benefit of additional capital attributed to the business unit following the sale of Pearl's remaining interest in HHG Invest plc and the sale of the Group's equity interest in Virgin Money Group Limited in the first half of 2004.

The rise in embedded value for the Life Services business during 2004 to £1.46 billion at 31 December included the positive impact of additional capital attributed to the business unit, improved investment return and earnings from the in force book of business offset by the adverse impact of strengthening the annuitant mortality basis.

Operational and Financial Review (continued)

Divestments and exits

Virgin Money Group Limited

In April 2004, the Group completed the sale of its 50% equity interest in Virgin Money Group Limited, resulting in a non-operating exceptional profit of £18 million. In the period to disposal, the Group's share of Virgin Money Group Limited profit was £1 million.

Towry Law International

On 27 May 2004, the Group announced, following a strategic review and in light of difficult market conditions, that it would close the operations of Towry Law International to new business resulting in a non-operating exceptional loss of £8 million, for which provision was made in 2004. As part of a recent review to ensure an orderly exit with no adverse impact on the Group going forward, management made additional provisions for 2004 in respect of Towry Law International legacy issues.

Sale of Life Services business

On 9 December 2004, HHG entered into an agreement to sell the Life Services business to Life Company Investor Group Limited. The 2004 accounts have recognised a £47 million non-operating exceptional loss comprising the impairment of the Life Services business intangible assets of £39 million and committed transaction costs at 31 December 2004 of £8 million.

Towry Law UK

The closure of Towry Law International has no impact on the operations of Towry Law in the UK, which reported a breakeven position

for 2004. The management of Towry Law UK has worked hard on cost reduction during 2004, to create a platform for a better business unit financial result in 2005 – though this is not likely to be material in the context of the overall Group financial results.

Corporate

The Group has a small corporate office which oversees the strategic direction of business. The corporate office undertakes the functions of secretariat, finance and treasury, strategy, investor relations, human resources, legal and regulatory affairs. The Group continues to make inroads in streamlining corporate expenditure. Total costs, however, rose to £31 million in 2004 (£12 million in 2003) as a result of increased provisioning – predominantly in relation to Towry Law International.

Following the proposed sale of the Life Services business and reduction in HHG's investor base, costs associated with shareholder servicing are expected to decrease by approximately £4 million before tax per year progressively from mid year 2005.

Financial reporting

The Group reports its performance on a Modified Statutory Solvency Basis (MSSB). In addition, for Life Services reporting, we also measure the change in embedded value and provide detail on regulatory capital strength through reporting free asset ratios (FARs) and FRS 27 realistic liability positions.

Modified statutory solvency result

The Group operating profit before amortisation of goodwill, exceptionals, interest, tax excluding minority interests was £107 million (2003: £98 million). This reflects solid performances in both Henderson Global Investors and Life Services including improved results in the second half of 2004 of £27 million (first half 2004: £25 million) and £54 million (first half 2004: £32 million) respectively. The Corporate loss of £25 million in second half of 2004 (first half 2004: loss of £6 million) has been impacted by additional provisioning in respect of Towry Law International.

The 2004 profit on ordinary activities before tax includes a number of operating (£10 million) and non-operating (£34 million) exceptional items. The operating exceptionals comprise restructure costs relating to Henderson Global Investors, the UK operations of Towry Law and Corporate Office. The non-operating exceptional items comprise a £47 million loss on the sale of the Life Services business, being impairments of goodwill (£29 million) and PVIF (£10 million) and £8 million of costs associated with the transaction committed at 31 December 2004, and £8 million from costs of closing Towry Law International to new business, offset by an £18 million profit on disposal of the equity interest in Virgin Money Group Limited and £3 million additional profit relating to the sale of Cogent.

Capital allocation and liquidity

On 31 March 2004, the Company issued 246,160,000 new ordinary shares for a net consideration of £115 million. The proceeds from this capital raising, together with internal cash resources, were used by the Company to acquire full ownership of HHG Invest plc from Pearl for a consideration of £119 million. This, together with the disposal of Virgin Money Group Limited, has improved the capital position of the Group.

	31 Dec 2004 £m	31 Dec 2003 £m
Henderson Global Investors	382	373
Life Services	1,483	1,177
Other Businesses	23	73
Corporate	33	68
Net assets	1,921	1,691
Financed by:		
Capital and reserves	1,838	1,689
External loans	–	2
Minority interest ¹	83	–
	1,921	1,691

Note

1. Minority interest represents the equity interests in a Jersey Property Unit Trust (JPUT) not held by the Group. The Group investment in the JPUT is held via the long-term insurance funds of various life insurance companies.

Cash flow improved from a net outflow in 2003 of £18 million to a net inflow in 2004 of £189 million. The liquidity position of the Group has benefited from cash inflows from the 31 March 2004 capital raising and from the sale of Virgin Money Group Limited for £50 million, whereas 2003 cash flow reflected high levels of cash payments associated with restructuring the Life Services businesses.

Life Services embedded value

The Group has provided embedded values on a traditional basis as at 31 December 2004 and has been advised by Tillinghast in this regard. Traditional Embedded Values (TEV) are calculated using a risk margin of 5% above the risk free rate for Pearl and National Provident Life and 3% for London Life, unit linked companies, the Service Company and other companies. Economic assumptions are determined based on appropriate government bond yields at each reporting date.

As a result of movements in bond yields during the period, risk discount rates have decreased in respect of Pearl and National Provident Life from 9.9% p.a. at 31 December 2003 to 9.6% p.a. at 31 December 2004. The corresponding decrease for other Life Services businesses is from 7.9% p.a. to 7.6% p.a.

The embedded value increased further in the second half of 2004 from £1,313 million to £1,456 million at the year end (31 December 2003: £1,145 million). There have been a number of factors impacting on the embedded value during 2004: the expected return reflecting interest on capital and 12 months' worth of unwind on the value of in force business at the discount rate; better than anticipated investment return principally in the second half of 2004; additional capital attributed to the business unit from the capital raising undertaken in March 2004 and from the sale of the equity interest in Virgin Money Group Limited in the first half of 2004; the adverse impact from a strengthening of the annuity mortality basis, again in the first half of 2004; and lower than anticipated expenses offset by more prudent persistency assumptions in the second half of 2004.

The above embedded values do not reflect the additional corporation tax charges that might arise in the event of the future enactment of proposed tax legislation announced in the December 2004 pre budget report and reaffirmed in the 16 March 2005 budget statement in relation to the taxation of surplus amounts held in the long-term insurance funds.

Regulatory capital

Henderson Global Investors

The regulatory environment in Europe (including the UK) is changing, as the European Union (EU) strives to harmonise regulatory practices across both EU member states and different sectors of the financial services industry through implementation of the Capital Requirements Directive (CRD). Neither the legislation nor the timetable for implementation are yet finalised. At the same time countries outside of the EU, including the US and certain Asian states, are considering to what extent they may be willing to convert the CRD into local legislation.

As the legislation is not yet finalised, the full implications of these changes for UK fund managers are not yet clear. However, the Financial Services Authority (FSA) has indicated that it does not anticipate that regulatory capital requirements for the industry as a whole in the UK will rise. It has also indicated, along with the UK Treasury, that it intends to limit the practice of "superequivalent" regulation that is going beyond the minimum necessary to comply with an EU directive, which should go some way to ensuring that UK fund managers are on an even footing with European competitors in future.

Henderson Global Investors continues to monitor regulatory developments to ensure that amendments are factored into its business and financial planning. This includes the conversion of underlying accounting data supporting financial resources requirements from UKGAAP to an IFRS basis, which should not have a material impact on Henderson Global Investors' regulatory capital requirement.

Life Services

The FARs of the main life companies as at 31 December 2004 and 31 December 2003 were for Pearl 3.3% (2.1%), National Provident Life 1.1% (1.4%) and London Life 2.2% (1.7%).

On 13 December 2004, the UK Accounting Standards Board issued the final text of FRS 27 relating to life insurance. This standard applies to all financial statements where the reporting entity includes a business that is a life assurance business and is applicable to accounting periods ending on or after 23 December 2005. Various companies across the industry, but not the Group's Life Services businesses, have entered into a Memorandum of Understanding (MoU), which provides for these entities to disclose key elements of the requirements of FRS 27 within their operating and financial review, for periods ending December 2004.

The Group is not part of the MoU on the basis that, on 9 December 2004, it had entered into an agreement for the sale of its Life Services business. It has, however, chosen to include the following information which is relevant to shareholders. The amount of the excess of realistic assets over realistic liabilities for the main life companies as at 31 December 2004 expressed as a percentage of the risk exposure (including both the risk capital margin and any additional loss absorbency required within contingent loans), was for Pearl 213%, National Provident Life 225% and London Life 500%. The amount of the excess of realistic assets over realistic liabilities is calculated to include shareholder capital available to support these funds after allowing for the additional financial flexibility afforded by both the National Provident Life and London Life contingent loan structures.

Information on guarantees and options given in respect of life assurance products is given in note 22.

Management of risk

Group Treasury operations

Ultimate responsibility for the governance of Group Treasury activities rests with the HHG PLC Board (the Board). Additional, independent oversight of the Group Treasury function is provided by the Board Audit Committee. The Board has established policies for the management of treasury related financial risks within the Group.

The Group's policy on liquidity risk is to ensure that the Group has sufficient cash resources to allow it to meet its obligations, as they arise, in an orderly manner. This is achieved through the maintenance of a sufficient quantum and quality of marketable securities and other short-term financial assets.

The Group's policy on interest rate risk is to minimise the adverse impact of movements in interest rates on the Group's net interest expense or income. Where possible, this is achieved through matching the re-pricing characteristics of its interest bearing assets and liabilities. In addition, where the remaining interest rate risk is material, interest rate derivatives may be used to further reduce the exposure. Derivative financial instruments are only employed in the management of financial risks and are not used for speculative purposes.

The Group's policy on foreign exchange risk is to protect the long-term sterling value of the business's foreign currency denominated net assets and to manage shorter term transactional exposures. Wherever practicable, these exposures are managed through natural hedging methods, but derivative instruments, such as forward foreign exchange contracts, currency options and cross currency swaps, may also be used to manage residual risks in relation to specific transactions.

The Group's exposure to credit risk is managed through the use of formal counterparty credit limits, which reflect the Group's view of the credit standing of each approved counterparty. All credit limits are regularly monitored and reviewed. Where appropriate, credit limits are revised or removed to reflect changes in the perceived underlying creditworthiness of a counterparty or business needs. Investments are diversified among approved credit counterparties within the established credit limits.

Contingent liabilities, in the form of financial guarantees and other off balance sheet instruments, are controlled through formal policies and approval processes.

Henderson Global Investors

The Henderson Global Investors risk management policy addresses how operational, market, credit and financial risks are managed within the business. Management is responsible for implementing the policies and risk management framework. Management is accountable to the Board for monitoring the systems of internal controls and for providing assurance to the Board and its delegated committees that it has done so.

The effectiveness of the system of internal control is reviewed by separate risk management and compliance functions. In addition, the Henderson Risk Committee provides oversight of risk management issues within the business and the Henderson Credit and Derivatives Risk Committee monitors adherence to credit and derivative risk policies.

Life Services

During 2004, Life Services management focused on understanding and managing the risks associated with the life companies and their balance sheets.

Investment risk

The investment policies for long-term business and other businesses have due regard to the nature of the liabilities and the guarantees and other embedded options given to policyholders. Investment policy is reviewed regularly by the relevant Investment Committee or Board of each of the life companies and senior management, with particular attention paid to management of credit risk, market risk and interest rate risk. Investment policy is further managed by setting a risk budget to ensure that there is sufficient capital in the business to manage the consequence of a mismatch under a number of adverse scenarios or through the use of derivatives. Asset and liability management for all insurance subsidiaries is especially important when regulatory capital is finite.

Insurance risk

Insurance risk is controlled using delegated authorities for the limited existing product pricing and underwriting arrangements in place. Prudent reserves are held, based on assumptions for example relating to expenses, persistency and mortality, that reflect past experience and anticipated future trends.

Pension scheme

A full triennial valuation of the staff pension scheme was conducted at 31 December 2003 and revealed a small surplus of £9 million on a funding basis. Details of this valuation are provided at note 33 to the accounts. On a FRS 17 basis, the pension scheme showed a deficit of £66 million (before tax) at 31 December 2004 (31 December 2003: deficit £69 million). Employer contributions recommenced with effect from 1 January 2004 at an average of 19.9% of pensionable earnings. From 1 January 2005, this rate was replaced by contributions of 27.0%, 20.8% and 13.8% of pensionable earnings for final salary section members, hybrid (a mix of final salary and money purchase) members and pure money purchase members respectively.

On the sale of the Life Services business, an estimated £1.5 billion in employee pension assets and liabilities will be transferred, thereby leaving the Henderson Group with pension assets and liabilities only in respect of its past and present employees. A further formal valuation of the Henderson Global Investors' scheme will be completed as at 31 December 2005.

Tax

The effective rate of tax in the Group consolidated profit and loss account for 2004 of 11% shows a favourable variance to the expected rate. This was due to realised gains on the disposal of investments not subject to tax. The 2003 effective tax rate on the loss for the period of 2.0% reflected the non tax-deductibility of exceptional costs and impairments arising during the period.

Dividend

No ordinary dividends are proposed for the year 2004 (2003: £nil). If the sale of the Life Services business proceeds in full, the Henderson Group expects to pay a final 2005 dividend in early 2006.

International Financial Reporting Standards (IFRS)

The Group adopted IFRS from 1 January 2005. The project that is in place to ensure that the Group meets the requirements of IFRS is progressing well. Work is underway to restate the 31 December 2004 balance sheet, set out on pages 36 and 37, on an IFRS basis. The Group expects to communicate the impact of IFRS on the future business in June 2005.

Board of Directors

Board members

At 23 March 2005, the Board consists of the Non-Executive Chairman, three Executive Directors (being the Chief Executive, the Chief Financial Officer and the Managing Director, Life Services) and five other Non-Executive Directors.

The Board is responsible for all strategic decisions regarding the Group's businesses, including approval of commercial strategy, annual budgets, interim and full year financial statements and reports, and dividend and accounting policies. It is also responsible for approving all significant capital projects, investments and disposals.



Chairman
Rupert Pennant-Rea
BA (Econ), MA (Econ), age 57 – Chairman and Non-Executive Director since October 2004 and Chairman since March 2005. Chairman of the Board Nomination Committee since March 2005.

Experience:
Deputy Governor of the Bank of England from 1993 to 1995, prior to which he spent 16 years with *The Economist*, where he was editor from 1986 to 1993. Mr Pennant-Rea has been Chairman of The Stationery Office since 1996 and non-executive Chairman of Plantation & General Investments plc since 1997. Amongst his other directorships are British American Tobacco plc, Go-Ahead Group plc and Gold Fields Limited (South Africa).



Executive Director
Roger Yates
BA (Hons) (Oxon), age 47 – Chief Executive. Executive Director since June 2003 and Managing Director of Henderson Global Investors since 1999.

Experience:
Joined AMP in October 1999 to lead the integration of Henderson Investors and AMP Asset Management Australia to form Henderson Global Investors. Mr Yates has 23 years' experience in the fund management industry as an investment professional and business manager. Previously, he was Chief Investment Officer of Invesco Global and held senior roles for fund management companies LGT and Morgan Grenfell. He was an executive Director of AMP Limited from December 2002 until the Demerger of AMP's UK and Australian operations in December 2003.



Executive Director
Toby Hiscock
BA (Hons) (Oxon), MA (Oxon), FCA, age 45 – Chief Financial Officer. Executive Director since August 2003.

Experience:
Chief Financial Officer of HHG PLC since May 2003. Mr Hiscock is also Director of Finance and Strategy for Henderson Global Investors and was Director of Finance for Henderson Investors from July 1998, having held senior internal audit and finance roles since joining Henderson Investors in 1992. A qualified chartered accountant with 24 years' experience in the accounting profession. Prior to joining Henderson Investors, Mr Hiscock was Senior Audit Manager at Midland Bank, London for three years. From 1981 to 1988 he worked for Binder Hamlyn, Chartered Accountants in London.



Executive Director
Ian Laughlin
BSc, FIA, FIAA, age 54 – Managing Director, Life Services. Executive Director since January 2003.

Experience:
Appointed Managing Director, UK Life Services in October 2002. In the five months prior to his current appointment, Mr Laughlin was Director, Managing Director's Office of the former UK Financial Services business. Prior to that, he held a similar role in AMP's Australian Financial Services for over two years. He has over 30 years' financial services experience and joined AMP in 1996 as Chief Manager, Life and Risk Insurance Services. He later became General Manager, Customer Solutions. Prior to joining AMP, Mr Laughlin was General Manager Retail Customer Services at Suncorp (Australia) and previously held various senior management roles in Suncorp and National Mutual (Australia). He is a qualified actuary.



Non-Executive Director
Gerald Aherne
BSc, AIA, age 59 – Non-Executive Director since October 2004. Member of the Board Remuneration Committee.

Experience:
Mr Aherne spent 16 years, to September 2002, with Schroder Investment Management, as Investment Director. Prior to this, he spent 18 years with Equity & Law in various actuarial and investment management roles. He is currently managing partner of Javelin Capital Partners LLP and a Director of Electric and General Investment Trust plc. He was also a founding Director of PRI Group plc from August 2002 until June 2003, when it was acquired by BRIT.



**Non-Executive Director
Duncan Ferguson**

MA (Cantab), FIA, Dip Ag Sci, age 62 – Non-Executive Director since July 2004. Chairman and Non-Executive Director of London Life Limited and a Non-Executive Director of Pearl Assurance plc, National Provident Life Limited and NPI Limited.

Experience:

Non-Executive Chairman of both Alba Life and the life assurance companies of the Phoenix Group owned by Resolution Life. Mr Ferguson is also a Non-Executive Director of HBOS Financial Services and Illium Insurance. His full-time career was part senior management of insurance companies and part consulting actuary. He was Senior Partner of Bacon & Woodrow, then B&W Deloitte, from 1994 to 2003. Mr Ferguson is a fellow of the Institute of Actuaries and served on the Council of the Institute from 1989 to 2000 and as President from 1996 to 1998. He was also a Member of Council of the International Actuarial Association from 1996 to 2002.



**Non-Executive Director
Anthony Hotson**

M.Phil (Oxon), MA (Oxon), MA (London), age 51 – Non-Executive Director since November 2002. Non-Executive Director of Henderson Global Investors (Holdings) plc. Chairman of Towry Law plc since October 2003. Member of the Board Audit Committee since August 2003, Board Remuneration Committee since August 2003 and Board Nomination Committee since March 2005.

Experience:

Mr Hotson was formerly at the Bank of England, McKinsey & Company and Warburg. He was a Director of S.G.Warburg & Co. Ltd from 1992 to 1995 and subsequently Managing Director and Head of Financial Institutions Group, Warburg Dillon Read, the investment banking division of UBS AG.



**Non-Executive Director
John Roques**

CA, age 65. Joined the HHG PLC Board as Non-Executive Director in January 2004. Chairman of the Board Audit Committee and a Non-Executive Director of Henderson Global Investors (Holdings) plc and Towry Law plc.

Experience:

Currently Chairman of the Portman Building Society. Mr Roques is also a Non-Executive Director of BBA Group PLC, Premier Farnell PLC and is a Governor of the Health Foundation. He was previously a Director of Chubb PLC and a Director of British Nuclear Fuels PLC. A member of the Institute of Chartered Accountants of Scotland, Mr Roques spent 42 years with Deloitte & Touche (formerly Touche Ross & Co.) where he served from 1990-1999 as Senior Partner and Chief Executive. He was a Member of the Financial Reporting Review Panel (1991-1994) and a Member of the Financial Reporting Council (1996-2001).



**Non-Executive Director
Sir William Wells**

BA, FRICS, age 64 – Non-Executive Director since April 1994 and Chairman of the Board Remuneration Committee since August 2003. Member of the Board Audit Committee and the Board Nomination Committee. Appointed Senior Independent Director March 2004. Chairman and Non-Executive Director of Pearl Assurance plc, National Provident Life Limited and NPI Limited.

Experience:

Sir William is currently President of international property group Chesterton International PLC, having joined Chesterton Property Consultants in 1959 and becoming a partner in 1965. In addition he is a Non-Executive Director of Exel plc. He received a Knighthood in 1997 for his services in a non-executive capacity to the National Health Service. In April 2001 he was appointed Chairman of the NHS Appointments Commission, which is responsible for all non-executive National Health Service appointments in England and in October 2003 became Chairman of the Department of Health's Commercial Advisory Board.

Resignations

Since the last Full Annual Financial Report and Accounts, the following Directors have resigned from the Board:

Sir Malcolm Bates, Chairman and Non-Executive Director (resigned February 2005);

Peter Costain, Non-Executive Director (resigned February 2005);

Pat Handley, Non-Executive Director (resigned May 2004).

Sir William Wells will retire at the 2005 Annual General Meeting (AGM). If the sale of the Life Services business completes, Ian Laughlin will retire from the Board as part of his transfer with the Life Services business.

Directors' Report

The Directors present their report to the shareholders for the year ended 31 December 2004.

Principal activities

The principal activities of the Group in 2004 were the provision of investment management services and the transaction of various classes of insurance business. The investment management business is undertaken through Henderson Global Investors headquartered in London. Life Services undertakes insurance business and comprises principally the life insurance and pension books of Pearl, National Provident Life, NPIL and London Life which are effectively closed to new business. Other businesses include Towry Law which provides independent financial advice and insurance broking services. The Group continues to operate a number of overseas Henderson Global Investors and Towry Law branches.

Review of the year and future developments

The Group's results for the financial period are shown in the Consolidated Profit and Loss Accounts on pages 31 to 34. A review of the financial year and future developments are covered in the Chairman's and Chief Executive's Statements and the Operational and Financial Review that precede this report.

Results and dividends

The Group made a profit for the year attributable to members of the parent company of £38m in 2004 (2003: loss of £847m). The Directors do not recommend the payment of any dividends in respect of 2004 (2003: £nil).

Reporting

HHG PLC is listed on both the London Stock Exchange and the Australian Stock Exchange and as such is required to comply with both sets of disclosure requirements.

Post balance sheet events

At an Extraordinary General Meeting held on 21 February 2005, shareholders approved an agreement that the Company and its subsidiary companies entered into on 9 December 2004, to sell the Life Services business owned by Pearl Group Limited (a direct subsidiary of the Company) to Life Company Investor Group Limited. It is anticipated that regulatory approval by the FSA and satisfaction of conditions relating to the HHG Staff Pension Scheme will be obtained to enable completion of the sale in April 2005.

Following completion of the sale of the Life Services business, it is proposed that the majority of the proceeds be returned to shareholders in cash in exchange for cancellation of shares, that the investor base is reduced and that the remaining group, which will comprise Henderson Global Investors and Towry Law, be renamed Henderson Group plc. Further details are provided in note 38 to the accounts.

Substantial shareholdings

At 18 March 2005, in accordance with the provisions of Sections 198 to 208 of the Companies Act 1985, the Company had received notification from AMP, Aviva plc, Legal & General Group plc and Perennial Investment Partners Limited of holdings in the Company's issued share capital amounting to 12.65%, 3.17%, 3.01% and 5.01% respectively.

Employees

During 2004, the Group continued its policy of informing and involving employees in matters which concern them and in the achievement of its business goals. The Group has comprehensive processes for consultation and communication involving regular meetings between management and employees, team briefings

and the issue of various bulletins. Employee development within the Group is promoted by encouraging staff to gain appropriate professional qualifications and assisting with wider personal development. Specific human resources initiatives vary by business unit to reflect business needs and their competitive environment.

The Group is committed to providing equal opportunities to all employees irrespective of their sex, sexual orientation, marital status, religion, race, or disability. It is the Group's policy to give positive consideration to disabled persons with respect to applications for employment, training, career development and promotion, having regard to each individual's particular aptitudes and abilities.

Supplier payment policy

It is the policy throughout the Group that payments to suppliers are made in accordance with those terms and conditions agreed between the Group companies and their suppliers, provided that all trading terms and conditions have been complied with. In respect of Group activities, the amounts due to trade creditors at 31 December 2004 represents approximately 31 days of average daily purchases through the year (2003: 31 days). The Company has no trade creditors.

Corporate Governance

A statement on Corporate Governance appears on pages 17 to 20.

Share capital

Details of movements in authorised and allotted share capital during the year are given in note 18 to the accounts.

Directors

Details of the Board members at the date of this report are set out on pages 12 and 13. Gerald Aherne, Duncan Ferguson, Rupert Pennant-Rea and Anthony Hotson will all seek re-election at the 2005 Annual General Meeting.

Directors' remuneration and interests

A Report on Directors' remuneration appears on pages 21 to 27, including details of their interests in shares and share options.

International Financial Reporting Standards (IFRS)

The Group will adopt IFRS from 1 January 2005. The Group's financial position after the proposed sale of the Life Services business will be impacted under IFRS primarily by the accounting for pensions and goodwill. Under IAS 19 "Employee benefits", the Group will recognise the HHG Staff Pension Scheme deficit in the Consolidated Group Balance Sheet and actuarial gains and losses will be recognised in full in the period in which they occur in the Consolidated Statement of Recognised Income and Expense. On prospective application of IFRS 3 "Business combinations", from 1 January 2005 the Group will no longer incur an amortisation charge on goodwill carried in its balance sheet, but will instead conduct an annual impairment review of this intangible asset. The Group's financial position will also be affected on adoption of other IFRS including those relating to accounting for deferred taxation and leases.

The 2004 comparatives included within the Group's IFRS accounts for the year ending 31 December 2005 will include the presentation of the results of Life Services as discontinued operations. This item will also include the anticipated loss at 31 December 2004 from the sale of the Life Services business based on the difference between the sale proceeds less transaction costs and the IFRS net assets of the Life Services business at 31 December 2004. In 2005, the results of Life Services up until the effective date of the completion of the sale of Life Services business will again be reported as part of discontinued operations. A further offsetting loss or profit on disposal will also be reported in this period.

The project that is in place to ensure that the Group meets the requirements of IFRS is progressing well. Work is underway to restate the 31 December 2004 balance sheet set out on pages 36 and 37 on an IFRS basis. The Group expects to communicate the impact of IFRS on the future business in June 2005.

Indemnification and insurance of Directors and officers

The Company provides a Deed of Indemnity to Directors to the extent permitted by UK law whereby the Company is able to indemnify a Director against any liability incurred in proceedings in which he is successful, and against the costs of successfully applying to the Court to be excused for breach of duty where the Director acted honestly and reasonably.

In addition, the Deed of Indemnity provides that Directors will have access to the board/committee papers of the Company for the period of their office and for seven years after ceasing to be a Director for the purpose of defending legal proceedings, and that the Company will maintain Directors' and officers' insurance cover for the Directors to the extent permitted by law for the period of their office.

During or since the end of the financial year, the Company has paid or agreed to pay premiums in respect of a contract insuring all of the officers (including all Directors) of the Group against certain liabilities. The insurance policy prohibits disclosure of the nature of the liability, the amount of the premium and the limit of liability.

Rounding

In accordance with the Australian Securities and Investments Commission Class Order 98/0100, amounts in this Directors' Report and other sections of this Full Annual Financial Report and Accounts have been rounded off to the nearest million pounds sterling, unless stated otherwise.

Donations

Donations by the Group for community and charitable purposes amounted to £38,000 (2003: £44,000) which comprises medical and other £11,000 (2003: £19,000); social and welfare £22,000 (2003: £17,000); and arts and heritage £5,000 (2003: £8,000). The Group made no political donations.

Annual General Meeting

A separate document, the Notice of Annual General Meeting 2005, covering the Annual General Meeting of the Company to be held on 9 June 2005, will be sent to all shareholders and contains an explanation of the business before that meeting.

Auditors

Ernst & Young LLP have intimated their willingness to continue in office and a resolution that they be re-appointed will be proposed at the Annual General Meeting.

Signed in accordance with a resolution of the Directors



Roger Yates
Chief Executive
22 March 2005

Corporate Responsibility Policy

The Corporate Responsibility Policy details the Group-wide commitment to responsible business conduct with all our stakeholder groups.

Business standards

Corporate governance

The Group supports the high standards of corporate governance contained in the Combined Code on Corporate Governance issued by the Financial Reporting Council in July 2003 and annexed to the Listing Rules of the UK Listing Authority (the Combined Code) and the Principles of Good Corporate Governance and Best Practice Recommendations issued by the Australian Stock Exchange Corporate Governance Council (the ASX Principles). Further details can be found within the Corporate Governance section of the Full Annual Financial Report and Accounts on page 17 to 20 and on the Company's website at www.hhg.com

Code of conduct

All employees are bound by the Code of Conduct, detailed on the Company's website, which sets out standards expected by the Group. The Code underscores the Company's commitment to maintaining its reputation and also provides a framework for employee conduct in line with that commitment.

Investment management

In today's world social, environmental and ethical factors can influence the value of investments. The Group has a responsibility to seek to ensure that companies and other assets in which it invests have appropriate standards in these areas. The Group therefore seeks to take account of relevant social, environmental and ethical factors in our investment operations.

Human rights

The Group agrees with the principles of the Universal Declaration of Human Rights and is guided by its provisions in the conduct of its business.

Suppliers and service providers

The Group regards its suppliers as partners and seeks suppliers that match the Group's corporate responsibility aspirations in the delivery of their products and services. The Group is committed to ensuring that external contractors who provide services work in a suitable environment and under appropriate terms and conditions.

Customers

The Group's businesses seek to provide their clients with a service characterised by integrity, quality and care.

Environment

The Group is committed to responsible environmental management practices. These include the adoption of systems to limit the use of non-renewable resources and minimise the impact of its operations on the environment.

Workplace

Equal opportunities

The Group has an Equal Employment Opportunities (EEO) policy and code of conduct committing it to promote non-discrimination and equal opportunities.

Health and safety

The Group is committed to providing a working environment which is both safe and fit for the intended purpose.

Employee relations

The Group aims to provide all employees with a workplace free from all forms of discrimination and harassment and which is conducive to the health, confidence, morale and effective performance of all employees. The Group also aims to ensure that no employee feels discriminated against because of their religious belief or political opinion.

Employee reward

The Group's remuneration framework is designed to be market competitive and specifically to motivate employees to improve individual and corporate performance, retain key employees and align employee behaviour with the interests of clients and shareholders.

Community

The Group recognises its impact on local communities and is committed to building partnerships with the communities in which it operates.

Corporate Governance Statement

Codes and principles

The Directors support the high standards of corporate governance contained in the Combined Code and the ASX Principles as referred to in the Corporate Responsibility Policy section. This Statement, together with the Report on Directors' Remuneration, describes the Company's corporate governance arrangements. Further details can be found within the corporate governance section of the Company's website.

In its 2003 Full Annual Financial Report and Accounts, the Company disclosed a number of exceptions to compliance with either the Combined Code or the ASX Principles since its listing on 23 December 2003. Apart from the first three items listed below, these exceptions have been addressed during 2004:

- An annual evaluation of the Board was undertaken in the latter part of 2004. Performance evaluation of the direct reports of the Chief Executive was undertaken by the Chief Executive and the Remuneration Committee. Due to the significant number of changes in Directors and the Board Committees in 2004 and early 2005, no evaluation of the Board Committees or of individual Non-Executive Directors (including the Chairman) was undertaken in 2004. It is the Board's intention to undertake these in 2005 (Combined Code and ASX Principles).
- The documents required to meet the recommendations of the Combined Code were placed on the Company's website on 31 March 2004. However, as no evaluation of the Board Committees or individual Non-Executive Directors was undertaken in 2004, a description of the process for performance evaluation of the Board, its Committees and individual Non-Executive Directors has not been placed on the Company website (ASX Principles).
- Details of the remuneration of the five highest paid (non-Director) executives are not disclosed, as proposed by ASX best practice recommendation 9.1, for the reasons stated in the Additional Remuneration Information (page 28).
- The terms of reference for the Audit Committee did not include a responsibility to review the Company's whistleblowing arrangements (Combined Code). This was amended on 19 February 2004.
- The number of independent Non-Executive Directors did not comprise at least half of the Board (excluding the Chairman) until 2 February 2004 (Combined Code). Although the Chairman, on appointment, met the independence criteria, the Combined Code provides that the test of independence is not appropriate thereafter. However, the Chairman is an independent Director in accordance with the ASX Principles and, following those Principles, a majority of the Board were independent Non-Executive Directors from 2 February 2004.
- The Board did not appoint a Senior Independent Director until 25 March 2004 (Combined Code).
- As a result of his previous arrangements with AMP Limited (the Group's parent prior to 23 December 2003), Roger Yates, Chief Executive, has a contract that allows the Company to terminate his appointment by paying a liquidated sum equivalent to 24 months' basic salary, reducing from 1 January 2004 on a sliding scale on a monthly basis, to 12 months' basic salary from 1 January 2005 (Combined Code).

The Board

Following the retirement of the Board's Chairman, Sir Malcolm Bates, and Peter Costain on 28 February 2005, the Board comprises a Non-Executive Chairman, a Chief Executive, two other Executive Directors and five Non-Executive Directors, all of whom the Board consider to be independent. The Board has appointed Sir William Wells as the Senior Independent Director. The Directors consider that each of the Non-Executive Directors is independent on the basis that they do not have any interest or business or other relationship which could, or could reasonably be perceived to, materially interfere with their ability to act in the best interests of the Company. In addition,

the Board has considered the criteria proposed by the Combined Code and the ASX Principles in assessing the independence of the Directors. Materiality, as referred to in the ASX Principles, is assessed on a case-by-case basis by reference to each Director's individual circumstances rather than general materiality thresholds. However, the Board is satisfied that the independent Directors meet a quantitative materiality threshold for independence that no Director has a relationship with the Group which generates or accounts for more than 5% of the Group's revenue or expenses. Biographical details of the Directors are given on pages 12 and 13.

Sir William Wells has served on the Board since April 1994 and is to retire from the Board at the 2005 AGM. The Board decided that, given his other interests (see Board of Directors section, pages 12 and 13), and the fact that he meets the other independence criteria of the Combined Code and ASX Principles, he should be considered independent in character and judgement notwithstanding his length of service. The Board considered Peter Costain, who had also served on the Board since April 1994 and retired from the Board on 28 February 2005, to be independent for the same reasons. In reaching these views, the Board considered that these Directors were independent of management and free of any business or other relationship that could materially interfere with the exercise of their independent judgement or could otherwise affect their ability to act in the Group's best interests.

There is a division of responsibility between the Chairman, Rupert Pennant-Rea, who is responsible for the effective operation of the Board, and the Chief Executive, Roger Yates, who is responsible to the Board for the overall management and performance of the Group. Rupert Pennant-Rea's other significant commitments are as non-executive Chairman of The Stationery Office, Plantation & General Investments plc and Electra Kingsway VCT. He is also a Non-Executive Director of several other companies in the UK and abroad. Further details are shown in the Board of Directors section on pages 12 and 13.

Non-Executive Directors are appointed for a fixed term, normally of three years, and any subsequent terms are subject to review. A summary of the remuneration payable to the Non-Executive Directors is set out in the Report on Directors' Remuneration (see pages 21 to 27). The terms and conditions of appointment of the Non-Executive Directors may be viewed on the Company's website.

All newly-appointed Directors receive induction on joining the Board. Thereafter, the Company provides the necessary resources for developing and updating the knowledge and capabilities of its Directors.

In 2004, the Institute of Chartered Secretaries and Administrators conducted an independent evaluation of the performance of the Board. The evaluation looked at the operation of the Board, including its corporate governance and decision-making framework and the operation and content of its meetings. The evaluation process, on the basis of private interviews with each of the Directors, was considered to have been thorough. The Board was satisfied that the process showed that the Board worked effectively. During 2005, the Chairman intends to facilitate discussions on, and evaluation of, the performance of the Board, of the Board Committees and of individual Directors. The Non-Executive Directors will appraise the Chairman's performance, after taking into account the views of the Executive Directors.

At the AGM held on 10 June 2004, being the first as a listed company, all Directors at that time were re-appointed by shareholders. At subsequent AGMs, approximately one third of the Directors, and any Director who has served for more than three years without being proposed for re-appointment at an AGM, will retire by rotation and may seek re-appointment.

Operation of the Board

The Directors met as a Board 14 times in 2004. Attendance by each of the Directors was:

Director's name	Date appointed	Date resigned	Number of meetings held in 2004 while a Director	Number of meetings attended in 2004 while a Director	Percentage of meetings attended in 2004 while a Director
Sir Malcolm Bates	12/03/1996	28/02/2005	14	13	93%
Gerald Aherne	01/10/2004		6	6	100%
Peter Costain	12/05/1994	28/02/2005	14	13	93%
Duncan Ferguson	01/07/2004		8	7	88%
Pat Handley	16/06/2003	21/05/2004	5	4	80%
Toby Hiscock	11/08/2003		14	14	100%
Anthony Hotson	29/11/2002		14	14	100%
Ian Laughlin	28/01/2003		14	14	100%
Andrew Mohl	17/10/2002	02/02/2004	1	0	0%
Rupert Pennant-Rea	01/10/2004		6	4	67%
John Roques	14/01/2004		14	13	93%
Sir William Wells	12/05/1994		14	13	93%
Roger Yates	16/06/2003		14	14	100%

The Directors are scheduled to meet as a Board at least seven times in 2005 (2004: scheduled eight times). Additional meetings will be held as required or at the request of a Director. During 2004, the Non-Executive Directors met the Chairman without executives being present, and it is the intention that this should happen again during 2005.

To enable the Directors to perform their role effectively, they are given the means and information necessary for them to make informed decisions and to follow best corporate governance practice. At each of its meetings, the Board receives detailed reports on the various aspects of the business and of any major issues affecting it.

The Board is responsible for all strategic decisions regarding the Company's business, including approval of commercial strategy, annual budgets, interim and full year financial statements and reports, dividend and accounting policies, and the approval of all significant capital projects, investments and disposals. There is a schedule of matters reserved for approval by the Board that is reviewed annually and which may be viewed on the Company's website.

The Board has approved corporate governance policies including a policy on trading in the shares of the Company by Directors and employees, a market disclosure policy and a code of conduct which, together, set a framework within which the Directors and other employees are expected to behave to protect the interests of shareholders, customers, employees and suppliers. A summary of the three documents may be viewed on the Company's website.

The Directors are entitled to seek independent professional advice at the Company's expense where they judge it necessary to discharge their responsibilities as Directors.

Board Committees

The Board has delegated specific responsibilities to three standing Committees of the Board. The membership of the Board Committees and a summary of their main duties under their terms of reference are set out on pages 19 and 20. The full terms of reference may be viewed on the Company's website.

Audit Committee

John Roques succeeded Peter Costain as Chairman of the Audit Committee on 11 June 2004. Peter Costain remained on the Committee until his retirement from the Board on 28 February 2005. Its other current members are Anthony Hotson and Sir William Wells (see Board of Directors, pages 12 and 13, for details of the qualifications of the Committee members). The Committee met seven times in 2004. Attendance by each of the members was:

Director's name	Date appointed	Date resigned	Number of meetings held in 2004 while a member	Number of meetings attended in 2004 while a member	Percentage of meetings attended in 2004 while a member
Peter Costain	28/07/1998	28/02/2005	7	7	100%
Anthony Hotson	28/08/2003		7	7	100%
John Roques	11/06/2004		3	3	100%
Sir William Wells	28/07/1998		7	7	100%

The Audit Committee is responsible for making recommendations to the Board on the appointment of the external auditors, the terms of engagement (including audit fees) and for reviewing the performance, independence and objectivity of the external auditors. It receives and reviews reports from management and the external auditors relating to the Company's Annual Report and Accounts and interim reports, although ultimate responsibility for reviewing and approving the Annual Report and Accounts and interim reports remains with the Board. The Audit Committee also receives formal reports from the internal auditor, who attends meetings as required.

The Audit Committee reviews compliance with legal and regulatory requirements, accounting standards and the form of the statutory accounts and accounting policies. It particularly focuses on assessing the effectiveness of the Group's systems of internal controls and risk management procedures, as well as the internal audit function. The Audit Committee also reviews arrangements for whistleblowing.

Information on the procedures for the selection and appointment of the external auditors and for the rotation of the external audit engagement partner is provided on the Company's website. The Company has adopted a Charter of Statutory Auditor Independence, which requires both the Company and the external auditors to take measures to safeguard the objectivity and independence of the external auditors.

Nomination Committee

Rupert Pennant-Rea succeeded Sir Malcolm Bates as Chairman of the Nomination Committee on 1 March 2005 following Sir Malcolm's retirement from the Board. Its other current members are Sir William Wells and Anthony Hotson. Peter Costain was a member of the Committee until his retirement from the Board on 28 February 2005. The Committee met five times in 2004. Attendance by each of the members was:

Director's name	Date appointed	Date resigned	Number of meetings held in 2004 while a member	Number of meetings attended in 2004 while a member	Percentage of meetings attended in 2004 while a member
Sir Malcolm Bates	28/08/2003	28/02/2005	5	5	100%
Peter Costain	28/08/2003	28/02/2005	5	5	100%
Sir William Wells	28/08/2003		5	5	100%
Rupert Pennant-Rea	01/03/2005				
Anthony Hotson	01/03/2005				

The Nomination Committee has responsibility for considering the size, composition and balance of the Board, retirement and appointment of additional and replacement Directors and making appropriate recommendations to the Board on these matters.

In identifying suitable candidates for recommendation for appointment to the Board, the Nomination Committee is concerned to ensure that the Board has available to it Directors with an appropriate mix of expertise and experience.

It is the Company's practice to use an external search consultancy to assist the Committee in identifying suitable candidates for non-executive Board positions.

Remuneration Committee

Sir William Wells chairs the Remuneration Committee and its other current members are Gerald Aherne and Anthony Hotson. The Committee met seven times in 2004. Attendance by each of the members was:

Director's name	Date appointed	Date resigned	Number of meetings held in 2004 while a member	Number of meetings attended in 2004 while a member	Percentage of meetings attended in 2004 while a member
Sir William Wells	28/08/2003		7	7	100%
Gerald Aherne	01/10/2004		3	3	100%
Peter Costain	28/10/2003	28/02/2005	7	7	100%
Anthony Hotson	28/08/2003		7	7	100%

The Remuneration Committee has responsibility for making recommendations to the Board on the Company's policy for the remuneration and performance of Executive Directors and for determining, within agreed terms of reference, specific remuneration packages for each of the Executive Directors. These include pension rights, any compensation payments and the implementation of executive incentive schemes. The Chairman and the Executive Directors determine the remuneration of Non-Executive Directors, except for the Chairman whose remuneration is determined by the Chairman of the Remuneration Committee and the other Non-Executive Directors. The Remuneration Committee operates on the principle that members of the executive management should be provided with appropriate incentives to encourage superior performance and should, in a fair and responsible manner, be rewarded for their individual contributions to the success of the Group.

The Report on Directors' Remuneration (see pages 21 to 27) provides details on how the Remuneration Committee exercises these duties. Towers Perrin, acting as remuneration consultants, advises the Remuneration Committee. Towers Perrin does not have any other connection with the Company other than providing compensation data and information on remuneration developments and as consulting actuaries to the Group's life companies subsidiaries through its sister company, Tillinghast.

Investor Relations

The Company values its interaction with shareholders and welcomes the views of both retail and institutional investors and their representative bodies. The Company utilises its regularly updated website (www.hhg.com) to communicate a wide range of information about the Group and to provide online services to help shareholders manage their holding and engage with the Company. In addition, the Company offers a variety of information and feedback channels including the shareholder call centre, email access and shareholder meetings. A programme, including monthly reporting, to ensure feedback to the Executive and Non-Executive Directors from shareholders and market participants is in place. Additionally, the Board is briefed regularly on shareholder issues and Investor Relations makes publicly available (on the Company website) archives of biannual market briefings. In line with the Combined Code, during the year substantial shareholders were offered meetings with Non-Executive Directors.

The Company's commitment to communicating with its shareholders was recognised by being awarded the 2004 ProShare award for Best Website for Individual Shareholders for a Non-FTSE 100 Company.

The Company publishes its results biannually and sends a Concise Annual Report to all shareholders (unless they have elected to receive a copy of the Full Annual Financial Report and Accounts).

All shareholders and CHES Depositary Interest (CDI) holders were invited to the 2004 AGM, held on 10 June 2004. The AGM was held in London and, to allow Australian shareholders to attend and participate, was simultaneously broadcast as a satellite meeting to Sydney. All Directors were present, either in London or Sydney. After the meeting, the Company provided, on its website, a summary of the questions asked at the AGM and the answers given, together with the results of resolutions put to the AGM.

Financial reporting and going concern

The Directors have acknowledged their responsibilities in relation to the financial statements in the Statement of Directors' Responsibilities in Respect of the Accounts (see page 29). After making appropriate enquiries, the Directors consider that the Company has adequate resources to continue in operational existence for the foreseeable future and therefore have continued to adopt the going concern basis in preparing the accounts.

Oversight of internal controls and risk management

The Board has overall responsibility for the Group's system of internal controls and for reviewing its effectiveness. The system of internal controls is 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 misstatement or loss. The Board considers risk assessment and controls to be fundamental to achieving its corporate objectives within an acceptable risk/reward profile. Throughout 2004, and up until the date of this report, there has been in place an ongoing process for identifying, evaluating and managing significant risks within the Group's control which accords with the guidance set out in the "Turnbull Report" – Internal Control: Guidance for Directors on the Combined Code Annexed to the Combined Code. The effectiveness of the Group's system of internal controls is reviewed at least annually by the Board.

Below Board level, the management of risk within the Group is governed by two audit committees (the HHG Audit Committee, the role of which is described earlier, and the Henderson Audit Committee, which is chaired by John Roques, a Non-Executive Director, and focuses specifically on Henderson Global Investors' internal control issues), and Business Unit Risk Committees, which are management committees, chaired by and consisting of senior managers. The Henderson Audit Committee has recently been discontinued so that the HHG Audit Committee is now the only Board audit committee within the Group.

The purpose of the Business Unit Risk Committees, which normally meet monthly, is to provide leadership and oversight of risk management, to maintain effective governance structures and to advise the relevant Board on risk management policies and risk appetite. They maintain a forum for the management and resolution of all significant regulatory and compliance issues and constructively challenge the relevant business to demonstrate that risks have been identified, prioritised and appropriately addressed and to recommend improvements as required. Their activities are overseen by the HHG Risk Committee, a management committee chaired by and consisting of senior managers, which meets at least quarterly.

Day-to-day management of risk is the responsibility of the Group's line management. The risk management function works closely with management to maintain a risk and control self-assessment process, an incident reporting process and the provision of management information to the Audit Committee and the Business Unit Risk Committees. The compliance function works with the risk management function and the business units to ensure that all regulatory risks have been understood and are being effectively managed.

Additional assurance is provided by the internal audit function, which operates and reports independently of the governance functions.

Report on Directors' Remuneration

Introduction

The Directors' Remuneration Report of the Company contains the following information:

- a description of the role of the Company's Remuneration Committee;
- a summary of the remuneration policy of the Group including a statement of the Company's policy on Directors' remuneration;
- details of the terms of the service contracts and the remuneration of each Director for the preceding financial year;
- details of the share options and awards under long-term incentive schemes held by the Directors; and
- details of each Director's interest in ordinary shares in the Company.

The Company's remuneration policy and remuneration arrangements for its Executive Directors have applied since the Demerger from AMP and the Company's listing on 23 December 2003 and were disclosed in the Listing Particulars dated 27 November 2003.

Corporate Governance

This Report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002 (the Regulations) under the UK Companies Act 1985. The report also meets the requirements of the Listing Rules of the UK Listing Authority and the relevant provisions of the Companies Act 1985. It also sets out how the principles of the Combined Code relating to Executive Directors' remuneration are applied by the Group.

A resolution will be put at the AGM on 9 June 2005 inviting shareholders to consider and approve this Report.

Membership and responsibilities of the Remuneration Committee

Role of the Remuneration Committee

The Remuneration Committee reviews and approves, where appropriate, the Group's remuneration and compensation plans, policies and practices. Its duties are to:

- review and recommend to the Board the Company's remuneration protocols and practices, which are performance based and aligned with the Company's vision, values and overall business objectives;
- determine annually the remuneration of the Board Chairman, the Chief Executive and his direct reports, including Executive Directors;
- approve the terms and conditions of employment and other contractual matters relating to the Group's executive management team; and
- approve the policy and terms of the Group's employee and executive share incentive plans.

The full terms of reference of the Remuneration Committee are available at www.hhg.com and on request from the Company Secretary.

No Director or member of the Group's executive management team is involved in any decision as to his own remuneration.

Membership

The Remuneration Committee consists entirely of independent Non-Executive Directors. In 2004, it comprised Sir William Wells (Committee Chairman), Peter Costain, Anthony Hotson and Gerald Aherne. The Board Chairman and the Chief Executive may attend meetings of the Remuneration Committee at the Remuneration Committee's invitation, save that they may not attend if their own remuneration is under consideration.

Meetings

The Remuneration Committee meets regularly and takes advice from both inside and outside the Group on a range of matters, including the scale and composition of the total remuneration package payable in comparable financial institutions to people with similar qualifications, skills and experience.

Internal support is provided to the Remuneration Committee by the Company Secretary and also by the Director of Human Resources, who is invited to attend and speak at meetings, except when his own remuneration is under consideration.

The Committee Chairman and the Chief Executive make recommendations on matters relating to the remuneration of the Executive Directors, who report to the Chief Executive. The Board Chairman is consulted in relation to the remuneration of all Executive Directors.

The Committee met seven times in 2004. Those meetings were fully attended by committee members.

Advisers

During the year, where considered appropriate, the Remuneration Committee took advice on technical aspects of compensation policy from independent external consultants appointed by the Remuneration Committee. These were Towers Perrin, a specialist remuneration consulting firm who provided advice on executive pay and share plan issues, and Watson Wyatt LLP, who provided advice on pensions issues to the Group. Tillinghast, a sister company of Towers Perrin, provided general management consulting and valuation advice to the Group.

Additional remuneration survey data published by McLagan Partners was presented to the Remuneration Committee and advice on bonus arrangements was taken from MM&K Limited.

Policy Statement

Reward policy

The Remuneration Committee considers that a successful remuneration policy needs to be sufficiently flexible to take account of future changes in the Company's business environment and in remuneration practice and so the policy is subject to change. The Remuneration Committee has instructed Towers Perrin to advise on remuneration policy for the Company assuming the Life Services business is sold but as it is necessary to have incentive schemes in place for the current year it has decided to retain the existing arrangements for 2005.

The Company's remuneration framework is designed to be market competitive and specifically to motivate employees to improve individual and corporate performance, retain key employees and align employee actions with the interests of shareholders.

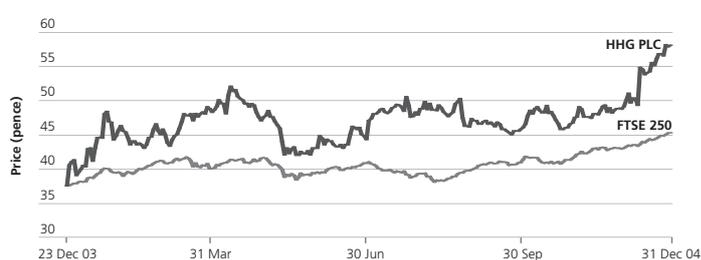
It is based on a total reward approach designed to deliver top quartile pay for top performance. There are three key components:

- basic salary – within appropriate market range;
- annual bonus – paid under a short-term incentive (STI) plan where individuals have the opportunity to receive a bonus based on business and individual performance against targets; and
- long-term incentive – performance-based for senior executives and certain professionals such as key senior fund managers.

Performance graph

The Companies Act 1985 requires the report to include a performance graph comparing the Group's total shareholder return (TSR) performance against that of a broad market index. The graph below shows the Company's ordinary share price movement and compares this against the movement in the FTSE 250 index. The graph starts from 23 December 2003, being the date on which the Company's shares were admitted to trading on the London Stock Exchange (LSE), and ends on 31 December 2004. The FTSE 250 was selected as the most appropriate broad market index since the Company is a constituent member and because it is a widely recognised performance benchmark for UK companies of a similar market capitalisation to that of the Group. The graph shows that the Company outperformed the FTSE 250 index over this period.

HHG PLC relative to FTSE 250



Executive Directors' Remuneration: individual elements

Overall structure

Executive Directors' remuneration comprises: basic salary, annual bonus, pension benefits, benefits in kind and the opportunity to participate in Group-wide incentive schemes, such as the HHG PLC Long-Term Incentive Plan (LTIP), the HHG PLC Restricted Share Plan (RSP) and the HHG PLC Sharesave Scheme. The LTIP and the annual bonus are performance related and the Remuneration Committee regards them as key elements in the Executive Directors' remuneration packages. The Scheme is available to all employees and is not performance related. As set out in the UK Listing Particulars, awards to Executive Directors under the RSP will only be made in exceptional circumstances and may be subject to performance conditions.

Performance linkage

Each element of the Executive Directors' reward package supports the achievement of key business measures as illustrated in the table below:

Element	Structure	Purpose	Performance measure
Basic salary	Fixed	Reflects the competitive market rate for the job, the individual's contribution and prior contractual arrangements	Individual performance
Annual bonus	Variable	Rewards the delivery of operational goals and financial targets	Return on capital, operating profit, pre-tax and corporate cash flow against target and other operational objectives
Long-term incentive	Variable	Supports superior business performance in relation to competitor companies; aligns executives with shareholders' interests	Relative TSR

The Remuneration Committee intends that, for target levels of performance, at least 60% of total compensation (excluding pension) should be performance related. The expected value of awards made under the LTIP was calculated by our advisers, Towers Perrin, using a proprietary methodology. Its methodology considers TSR rank at which payment begins, the payment level at this threshold, the maximum payment under the plan and the rank at which this maximum is achieved. The methodology also takes into account the correlation of the Company's stock with those companies in the peer group, starting from the premise that the value of the shares awarded at the end of the performance period is correlated with the TSR ranking. The Committee is satisfied that this structure constitutes a well considered overall plan for Executive Directors' remuneration. It is kept under regular review to take account of changing circumstances. Incentive payments are not taken into account for pension purposes.

In 2004, remuneration arrangements had a higher proportion of fixed pay than for other investment management companies, reflecting the fact that the Group was not a pure fund management business and included the Life Services businesses, Towry Law and other interests. These arrangements were unchanged from 2003. The Remuneration Committee, using independent external advisers, has recently reviewed the levels of remuneration for the Executive Directors pending the proposed sale of the Life Services business and the resultant organisational changes, to ensure the remuneration continues to reflect the market in which the Group will operate.

Basic salary

The Remuneration Committee's objective is that Executive Directors' basic salaries should be paid at an appropriate level to take account of both salaries within a comparator group of financial institutions based on external independent advice and of individual performance. The Remuneration Committee considers that exceptional performance, whether individual or corporate, should be rewarded through bonus and incentive schemes rather than basic salary.

Salaries are reviewed annually for each Executive Director, with effect from 1 April. Current salaries, which are unchanged since the Demerger on 23 December 2003, are as follows:

R.P. Yates	Chief Executive	£600,000 per annum
N.T. Hiscock	Chief Financial Officer	£300,000 per annum
I.W. Laughlin	Managing Director, Life Services	£275,000 per annum

Annual bonus

At the discretion of the Remuneration Committee, each Executive Director may receive a cash bonus subject to the achievement of individual and corporate performance targets established by the Remuneration Committee. Payment of bonuses (if any) will be made to the relevant Executive Director annually, usually in March, conditional upon achievement of the performance targets in the preceding calendar year. The bonus range is zero to a specified maximum with target being the midpoint. The maximum bonus entitlement is based on a percentage of annual basic salary. Maximum entitlements for 2005 performance are unchanged from 2004 and are 200% of salary for the Chief Executive, 150% of salary for the Chief Financial Officer and 150% of salary for the Managing Director, Life Services.

For each Executive Director, the corporate performance targets relate to both Company performance measures as set out in the Performance linkage section and performance measures for individual businesses. The Henderson Global Investors' performance measures were operating profit pre-tax, net external fund flow and investment performance. The Life Services performance measures were operating profit pre-tax, embedded value, expenses and realistic free assets.

In 2004, for each of the Executive Directors, the individual component was based on achievement against individual performance agreements approved by the Remuneration Committee. These agreements set out objectives relating to factors such as achievement of strategic milestones; relationships with the Board, regulators and investors; customer management; employees and risk management.

The Remuneration Committee will review the performance of each Executive Director on an annual basis against these corporate targets.

The Remuneration Committee has examined proposals to introduce a deferral to part of the annual STI bonus paid to Executive Directors. Such deferred amounts would be held in trust, normally for a minimum fixed period, before being released. Such proposals are expected to be introduced during 2005.

Long-term incentives

Under the LTIP, the Remuneration Committee may make awards to Executive Directors up to a maximum number of ordinary shares determined by the Remuneration Committee at the date of grant. Vesting of awards is conditional on the achievement of a performance target (see below) measured over a three year period and the Executive Director's continued employment during the performance period. The primary performance measure is TSR, which the Committee believes provides executives with a strong alignment to shareholders' interests. However, for all awards, the Remuneration Committee must be satisfied that the Company's TSR performance reasonably reflects its underlying financial performance over the performance period.

The Company made awards under the LTIP to Executive Directors in April 2004. The aggregate market value of the ordinary shares (averaged over the three month period immediately prior to the date of grant) capable of being acquired under these awards was equivalent to 250% of salary in the case of the Chief Executive and 160% of salary in the cases of the Chief Financial Officer and the Managing Director, Life Services.

Awards granted to the Life Services business employees (including the Managing Director) will become exercisable on completion of the sale of the Life Services business, subject to meeting performance targets.

Whilst the awards would normally be exercisable at the end of a three year performance period, the Remuneration Committee considered it appropriate, in the circumstances of the sale of the Life Services business and the return of capital to shareholders, to allow part of the awards granted to employees of the remaining group after the sale of

the Life Services business to vest. They took into account the fact that the return of capital achieves an accelerated release of capital from the Life Services business and that after completion of the sale of the Life Services business the remaining group will be smaller, with a different business to that which it had been when the awards were granted. Therefore, the Remuneration Committee determined that two thirds of the 2004 LTIP awards will become exercisable for these employees if the sale of the Life Services business completes and the return of capital is approved by the court. This part of the award will be subject to the application of the TSR performance condition up to the completion of the sale which will determine how many of the shares comprised in the two thirds part can be acquired on exercise. The remaining one third of the 2004 LTIP awards will continue to be held subject to the balance of the three year performance period and subject to the satisfaction of the TSR performance condition over that period.

In the case of both the Life Services business and other employees, the awards will be exercisable for six months from the date of vesting, and if not exercised in this period, will lapse.

The proportion of the 2004 LTIP awards that will be exercisable following the sale of the Life Services business and return of capital will be determined by reference to the growth in the Company's TSR over the period commencing 1 January 2004, compared to that achieved over the same period by the companies in the FTSE 250 index at the date of grant. If the Company's TSR performance at the vesting date is below the 50th percentile, none of the shares awarded will vest. If the Company's TSR performance is at the 50th percentile, 35% of the shares awarded will vest and if it is at the 75th percentile, 100% of the shares awarded will vest. Vesting between these two points will be calculated on a straight line basis. An independent adviser will verify relative TSR performance. Similarly, the one third of the 2004 LTIP awards that do not vest as a result of the completion of the sale of the Life Services business and the return of capital will continue to be subject to the TSR performance measure. In this case, performance will be measured over the three year period commencing 1 January 2004.

The Remuneration Committee intends to make annual awards under the LTIP for Executive Directors in 2005.

The Committee has also determined that, over time, each Executive Director should be required to maintain a target shareholding of ordinary shares in the Company, equivalent to 100% of base salary, in order to align the interests of Executive Directors more closely with those of shareholders. This is expected to be achieved mainly through vesting of awards under the LTIP.

All-employee share schemes

Executive Directors are eligible to participate in the Company's all-employee Sharesave Scheme on the same terms as other employees.

The Sharesave Scheme, a savings related share option scheme, is available to all employees. This Sharesave Scheme operates within specific UK tax legislation (including a requirement to finance exercise of the option using the proceeds of a monthly savings contract) and exercise of the option is not subject to satisfaction of a performance target since this is an all-employee scheme.

The Henderson Share Incentive Plan (SIP) is an all-employee scheme that operates within specific UK tax legislation and was established following shareholder approval at the 2004 AGM. The SIP represents a further opportunity for Henderson Global Investors employees to increase their share ownership, which is an important tool in attracting and retaining staff in the asset management industry. Executive Directors are not eligible to participate in the SIP.

The SIP enables participants to acquire ordinary shares out of deductions from gross salary, for which the Company may provide matching shares. The SIP also allows for annual awards of free shares.

Pensions

Retirement benefits are designed to be both market competitive and cost effective. The Company is the sponsoring employer of the HHG Staff Pension Scheme (the Scheme), which has both defined benefit sections (closed to new members) and defined contribution sections. As a result of the statutory cap on earnings, the Company also has unapproved pension arrangements, which apply to certain current and former Group employees. In addition, the Group has pension arrangements in place for its non-UK-based employees, which are in line with market conditions in those regions.

The Executive Directors participate in non-contributory sections of the Scheme providing Scheme benefits on either a defined benefit or defined contribution basis, depending on the date the Executive Director joined the Scheme. The Chief Executive is entitled to a pension accruing at 1/30th of uncapped pensionable salary, being the greater of £750,000 or his basic salary at the time of leaving pensionable service with the Company, for each year of pensionable service. The Scheme will provide the Chief Executive with a pension of 1/30th of pensionable salary in respect of pensionable salary below the earnings cap imposed by the Finance Act 1989 for each year of pensionable service. The earnings cap for 2004/2005 is £102,000. In addition, the Chief Executive participates in an unfunded unapproved retirement benefits scheme which will provide the balance of his pension entitlement. The Chief Financial Officer is entitled to a pension accruing at 1/45th of pensionable salary up to the earnings cap for each year of pensionable service under the Scheme. Since 23 December 2003, the Chief Financial Officer has participated in an unfunded unapproved pension arrangement to provide benefits in respect of his pensionable earnings above the earnings cap. The Managing Director, Life Services has participated in the money purchase section of the Scheme from 23 December 2003. He receives a credit to his money purchase account of 51% of the earnings cap which Watson Wyatt LLP has confirmed is in line with current Inland Revenue limits and broadly comparable to the contribution rate required to fund a pension accruing at 1/30th of the earnings cap for each year of service.

Other benefits and benefits in kind

The Executive Directors are contractually entitled to a lump-sum life assurance benefit of four times salary, permanent health insurance and medical insurance. The Chief Financial Officer and the Managing Director, Life Services are each entitled to a car allowance of £11,000 per annum.

The Executive Directors also benefit from indemnity arrangements in respect of their services as Directors, and Directors and officers' insurance, under separate Deeds of Indemnity.

Contracts and termination provisions

The Company's policy is to employ Executive Directors on one year rolling contracts although, in exceptional circumstances on recruitment, longer initial terms may be approved by the Remuneration Committee. To date, it has not exercised this right. The Remuneration Committee will, consistent with the best interests of the Company, seek to minimise termination payments.

The Executive Directors have service agreements terminable on not less than 12 months' written notice by the Company or on not less than six months' written notice by the relevant Executive Director.

The service agreements allow the Company to suspend the Executive Directors from their duties at any time after notice has been given by either party provided they continue to receive full pay. Under certain circumstances (e.g. serious misconduct), the Company may terminate employment immediately with no liability to make any further payment (other than amounts accrued to the date of termination).

There are no other provisions for compensation payable on early termination in the above contracts. In relation to their participation in incentive related pay, Executive Directors are subject to the rules of the LTIP in the same manner as other participants.

Chairman and Non-Executive Directors

The remuneration of the Board Chairman is determined by the Chairman of the Remuneration Committee and the other Non-Executive Directors, and for other Non-Executive Directors is determined by the Chairman and the Executive Directors on the basis of external independent advice. The Board Chairman and Non-Executive Directors serve the Company under letters of appointment which are terminable by the Company on one month's notice without liability for compensation; they do not have service agreements. It is the Company's policy that the Board Chairman and Non-Executive Directors do not participate in any of the Group's bonus, incentive or pension schemes, nor are they entitled to any retirement benefits. Under their respective letters of appointment:

- (a) the annual fee payable to each Non-Executive Director (other than the Board Chairman and the Audit and Remuneration Committee Chairmen) is £40,000;
- (b) the Board Chairman's annual fee is £150,000. He is also entitled to a fee of £1,000 for travel expenses;
- (c) Rupert Pennant-Rea was appointed as Non-Executive Chairman of the Company with effect from 1 March 2005. His fees are £150,000 per annum (inclusive of all other fees as a director or officer);
- (d) Duncan Ferguson is entitled to additional fees of £7,500 as Chairman of London Life. He is also entitled to fees of £500 per half day and £1,000 per whole day for attendance at meetings of various subsidiary boards and committees of which he is a director or member, where such attendance is required on days other than Board meeting days;
- (e) John Roques is entitled to additional fees of £5,000 per annum as Chairman of the Audit Committee and £2,500 per annum as Chairman of the Henderson Board Audit Committee. He is also entitled to fees of £500 per half day and £1,000 per whole day for attendance at the meetings of the boards of Towry Law plc and Henderson Global Investors (Holdings) plc of which he is a director, where such attendance is required on days other than Board meeting days;
- (f) Anthony Hotson's appointment letter has been varied to confirm the cessation of his appointment as Chairman of London Life with the corresponding reduction in fees, with effect from 10 September 2004. He is entitled to additional fees of £7,500 as Chairman of Towry Law plc. He is also entitled to fees of £500 per half day and £1,000 per whole day for attendance at meetings of various subsidiary boards and committees of which he is a director/committee member; and
- (g) Sir William Wells' appointment letter has been varied to confirm that he will remain as a Non-Executive Director until a date on or before the 2005 AGM on an annual fee of £50,000 including £5,000 per annum for his role as Senior Independent Director from 25 March 2004.

Tables

The following tables on pages 25 to 27 provide greater detail in respect of each of the Directors' and former Directors' emoluments, pension entitlements and share interests, which have been audited by the Company's auditors.

Directors' emoluments in 2004

The emoluments (cash payments and benefits in kind, but not including any pension and equity incentive award) of the Directors of the Company in respect of the period for which they were in office in the relevant year, including their remuneration in respect of subsidiary undertakings, comprised:

	Salary and fees £'000 ^{1,2}	Benefits in kind £'000 ³	Annual cash bonus £'000	Current employment arrangement £'000	Legacy arrangements ⁴ £'000	2004 Total £'000	2003 Total from appointment £'000	2003 Annualised £'000
Chairman								
Sir Malcolm Bates (Chairman and Non-Executive Director)	151	–	–	151	–	151	110	110
Executive Directors								
R.P. Yates (Chief Executive)	601	25	800	1,426	1,363	2,789	590	1,096
N.T. Hiscock	314	2	306	622	375	997	136	350
I.W. Laughlin	286	6	412	704	301	1,005	537	547
Non-Executive Directors								
P.J. Costain	44	–	–	44	–	44	44	44
A.C. Hotson	73	–	–	73	–	73	55	55
Sir William Wells	50	–	–	50	–	50	42	42
J. Roques (appointed 14 January 2004)	46	–	–	46	–	46	–	–
D. Ferguson (appointed 1 July 2004)	24	–	–	24	–	24	–	–
G. Aherne (appointed 1 October 2004)	10	–	–	10	–	10	–	–
R. Pennant-Rea (appointed 1 October 2004)	10	–	–	10	–	10	–	–
Former Non-Executive Directors								
R.P. Handley (resigned 21 May 2004)	13	–	–	13	–	13	14	14
A.M. Mohl (resigned 2 February 2004)	4	–	–	4	–	4	1	1
Total	1,626	33	1,518	3,177	2,039	5,216	1,529	2,259

Notes

- There were no amounts paid to the Executive Directors in respect of their qualifying services by way of expenses allowance that was chargeable to UK income tax.
- Emoluments of all Directors are stated with effect from 1 January 2004 or the date of appointment, if later. The final column in the table above represents the annualised cost for 2003.
- The non-cash elements of the Executive Directors' remuneration packages (disclosed in the table above as benefits in kind) consist of the provision of life assurance and private medical insurance.
- Executive Directors received retention payments in respect of the Demerger. The cost of these payments was met by AMP. For the Chief Executive, Chief Financial Officer and Managing Director, Life Services, these were £1,100,001, £300,000 and £213,320 respectively.

From 23 December 2003, the Executive Directors ceased to be eligible for further awards under the Henderson Long-Term Value Sharing Incentive Plan (HLTVSIP). Under the HLTVSIP, the Chief Executive and the Chief Financial Officer received awards of phantom equity units in substitution for part of their bonus for the year ended 31 December 2000, together with matching units entitling them to receive cash payments on satisfaction of various performance targets relating to return on capital and continued employment, payable over three years with the first payment having been made in January 2004 (in respect of 2000 performance). For the Chief Executive and Chief Financial Officer these were £262,686 and £74,720 respectively.

The Managing Director, Life Services, received a one-off payment of £50,000 and other miscellaneous payments of £37,554 in respect of the cessation of certain expatriate benefits to which he was previously entitled when employed by AMP.

Report on Directors' Remuneration (continued)
Tables (continued)

Long-term incentives

(a) Pensions

In accordance with the Regulations, the tables below show the Company's and members' contributions, the increase in accrued entitlement during the year and the accrued entitlement at the end of the year.

(b) Directors' pension entitlements

(i) Defined benefit

The following table gives details of the accrued pension benefit at 31 December 2004 (or retirement, if earlier) for Directors who have participated in the defined benefits section of the UK Scheme during the year to 31 December 2004. The final column represents the Company's funding obligations for 2004.

	Service at 31/12/2004	Accrued benefit at 31/12/2004 £'000	Additional pension earned during year to 31/12/2004 £'000	Transfer value of accrued benefit at 31/12/2004 ('A') £'000	Transfer value of accrued benefit at 31/12/2003 ('B') £'000	The amount of (A-B) less contributions made by Directors during 2004 £'000
Executive Directors						
R.P. Yates (Chief Executive)	5 years 3 months	131	53	1,305	724	581
N.T. Hiscock	12 years 8 months	33	7	352	266	86
Total		164	60	1,657	990	667

(ii) Defined contribution

The following table gives details of the pension contributions paid or payable by the Company into defined contribution arrangements for the year to 31 December 2004.

	2004 Employer contributions £'000 ¹	2003 Employer contributions £'000 ¹
Executive Director		
I.W. Laughlin	51	30
Total	51	30

Note

1. The pension contributions and accrued benefits shown are for the full calendar year 2004 and 2003 respectively.

(iii) Directors' share interests

At 31 December 2004 (or date of resignation, if earlier) and at 31 December 2003 (or date of appointment, if later) the Directors had the following beneficial interests in shares in the Company:

	23 March 2005 or retirement	31 December 2004 or resignation	31 December 2003 or appointment
Chairman			
Sir Malcolm Bates (Chairman and Non-Executive Director – retired 28 February 2005)	107,649	107,649	107,649
Executive Directors			
R.P. Yates (Chief Executive)	600,692	600,692	400,692
N.T. Hiscock	70,954	70,954	10,891
I.W. Laughlin	60,291	60,291	60,291
Non-Executive Directors			
P.J. Costain (retired 28 February 2005)	102,431	102,431	102,431
A.C. Hotson	45,700	45,700	45,700
Sir William Wells	104,077	104,077	104,077
J. Roques (appointed 14 January 2004)	25,000	25,000	–
D. Ferguson (appointed 1 July 2004)	25,000	25,000	–
G. Aherne (appointed 1 October 2004)	50,000	50,000	–
R. Pennant-Rea (appointed 1 October 2004)	–	–	–
Former Non-Executive Directors			
R.P. Handley (resigned 21 May 2004)	N/a	106,294	6,294
A.M. Mohl (resigned 2 February 2004)	N/a	478,799	478,799
Total	1,191,794	1,776,887	1,316,824

(c) Directors' interests in share awards

The following table shows the Executive Directors' interests in the LTIP:

	Interests at 31 December 2003			Awards made during year			Interests at 31 December 2004
	Sharesave	Maximum LTIP award	Target LTIP award	Sharesave ¹	Maximum LTIP award ^{2,3}	Target LTIP award ⁴	
R.P. Yates (Chief Executive)	–	–	–	22,656	3,288,031	1,377,685	3,310,687
N.T. Hiscock	–	–	–	22,656	1,052,170	440,859	1,074,826
I.W. Laughlin	–	–	–	22,656	964,489	404,121	987,145
Total	–	–	–	67,968	5,304,690	2,222,665	5,372,658

Notes

- Under the Sharesave, after 36 monthly contributions of up to £250, Sharesave participants may exercise their options to acquire HHG shares at an issue price of 41.6 pence per share. The option price was set at a 20% discount to the closing mid market value on 2 April 2004.
- This is the number of shares initially awarded. The number of shares was based on the three month average market value of the shares prior to the date of award, 2 April 2004. The average market price on which the awards were based was 45.62 pence.
- Although the award was granted with a three year cycle (1 January 2004 – 31 December 2006), as discussed in the Long-term incentives section for Remaining Group employees, two thirds will vest on the sale of the Life Services business, with the remaining one third award subject to the three year cycle. Awards granted to Life Services employees (including the Managing Director, Life Services) will become exercisable on completion of the sale of the Life Services business. All vesting is subject to meeting performance targets. On exercise, awards will be satisfied by the transfer to participants of shares purchased on market by the LTIP trustee.
- This number reflects the number of shares to be exercisable on the vesting date, based on an expected level of achievement of the TSR performance target (41.9%) at the time of award.

Additional Remuneration Information

Disclosure of non-Director executive remuneration is not required either by UK laws that apply to the Company or by UK corporate governance or best practice guidelines, nor is it market practice in the UK for this information to be disclosed. The Principles of Good Corporate Governance and Best Practice Recommendations issued by the Australian Stock Exchange Corporate Governance Council in Australia recommend certain information to be disclosed about the remuneration of the five highest paid non-Director executives. Details of the remuneration of each individual and the value of the component parts of their remuneration have not been disclosed, to ensure that these details do not become available to the Company's competitors in the UK as the Company considers this information to be commercially sensitive.

The five highest paid non-Director executives during 2004 were:

Name	Position
Ian Buckley	Chief Investment Officer – Henderson Global Investors
Mike Clare	Henderson Global Investors Managing Director, UK and Asia
Jonathan Moss	Finance Director – Life Services
Steven O'Brien	Group General Counsel
Simon Smith	HHG Director of Finance and Tax

Together with the three Executive Directors, Messrs Clare, Moss and O'Brien form the HHG Executive management team. The aggregate annual remuneration for the five executives listed above was £3,982,009, of which £1,373,700 was for retention bonuses paid by AMP as part of the terms of the Demerger and £2,608,309 relates to their normal remuneration package made up of the following:

- basic salary;
- a discretionary annual bonus, which is dependent on stipulated Company, business unit and individual performance measures;
- Company non-contributory (i.e. the employee does not contribute and the company bears all the costs) pension plan in either a defined benefit or defined contribution section of the plan; and
- other benefits including private medical insurance, permanent health insurance, car allowance, season ticket loans and life assurance.

During 2004, the role of Chief Investment Officer was made redundant and Ian Buckley will leave the Group in 2005.

In April 2004, the Remuneration Committee made awards to non-Director executives under the LTIP as described on page 23. In 2004, the aggregate market value of the ordinary shares (averaged over the three month period immediately prior to the date of grant) capable of being acquired by any non-Director executive under these awards is a maximum of 125% of salary depending on the role and responsibilities of the relevant executive. The vesting criteria set out on page 23 will apply to these awards. The executives were awarded 2,433,688 shares under the LTIP in April 2004, the vesting of which is described in the Long-term incentives section. Jonathan Moss is an employee of Life Services and the whole of his LTIP award (subject to the performance criteria being met) will vest on completion of the sale of the Life Services business.

Non-Director executives are entitled to participate in the Sharesave Scheme. Executives employed by Henderson Global Investors are also able to participate in the SIP as described on page 23.

Non-Director Executives may also be invited to participate in the Deferred Equity Plan under which participants receive part of their annual bonus in the form of the Company's shares or an interest in an investment fund at the end of a specified restricted period, subject to the executive continuing to be employed with the Group. The restricted period will normally be two or three years, but cannot be less than one year or more than five years. The investment fund will be units in a UK authorised unit trust, ordinary shares in an investment trust company, shares in the capital of an open-ended investment company or shares in the capital of a société d'investissement (in all cases the assets of which are managed by a company in the Group).

The structure of the remuneration packages for non-Director executives is designed to support the achievement of the same key measures as for Executive Directors (as set out on page 22), and to ensure that executive pay complies with the Board's remuneration policy (as described on page 21).

Statement of Directors' Responsibilities in Respect of the Accounts

Company law requires the Directors to prepare accounts for each financial year, which give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that year. In preparing those accounts, the Directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts; and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group and to enable them to ensure that the accounts comply with the Companies Act 1985. The Directors are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent Auditors' Report

We have audited the Group's accounts for the year ended 31 December 2004 which comprise the Consolidated Profit and Loss Account, Consolidated Statement of Total Recognised Gains and Losses, Reconciliation of Group Operating Profit to Profit on Ordinary Activities Before Taxation, Consolidated Balance Sheet, Company Balance Sheet, Consolidated Cash Flow Statement, Accounting Policies and the related notes 1 to 38. These accounts have been prepared on the basis of the accounting policies set out therein. We have also audited the information in the Report on Directors' Remuneration 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 are responsible for preparing the Annual Report, including the accounts, which are required to be prepared in accordance with applicable United Kingdom law and accounting standards as set out in the Statement of Directors' Responsibilities in relation to the accounts.

Our responsibility is to audit the accounts and the part of the Report on Directors' Remuneration to be audited in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the accounts give a true and fair view and whether the accounts and the part of the Report on Directors' Remuneration to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the accounts, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding Directors' remuneration and transactions with the Group is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 FRC 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 accounts. This other information comprises the Financial Highlights, Chairman's Statement, Chief Executive's Statement, Operational and Financial Review, Board of Directors, Directors' Report, Corporate Governance Statement and the unaudited part of the Report on Directors' Remuneration, Additional Remuneration Information and Shareholder Information. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board.

An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts and the part of the Report on Directors' Remuneration to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the accounts, 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 accounts and the part of the Report on Directors' Remuneration 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 accounts and the part of the Report on Directors' Remuneration to be audited.

Opinion

In our opinion:

- the accounts give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2004 and of the profit of the Group for the year then ended; and
- the accounts and the part of the Report on Directors' Remuneration to be audited have been properly prepared in accordance with the Companies Act 1985.



Ernst & Young LLP
Registered Auditor
London
22 March 2005

Consolidated Profit and Loss Account

Technical account for general insurance business

For the year ended 31 December 2004

	Notes	31 Dec 04 £m	31 Dec 03 £m
Allocated investment return transferred from the non-technical account	5.2	4	3
Total technical income		4	3
Claims paid:			
Gross amount		(65)	(45)
Reinsurers' share		40	39
Net claims paid		(25)	(6)
Change in the provision for claims:			
Gross amount	24.2	72	59
Reinsurers' share	24.2	(45)	(54)
Change in the net provision for claims		27	5
Claims incurred, net of reinsurance		2	(1)
Net operating expenses	2.1	2	5
Change in equalisation provision	1.1	3	2
		5	7
Total technical credits		7	6
Balance on the technical account – general business		11	9

All activities relate to discontinued operations.

Consolidated Profit and Loss Account (continued)

Technical account for long-term business

For the year ended 31 December 2004

	Notes	31 Dec 04 £m	Restated 31 Dec 03 £m
Gross premiums written	4.1	972	1,664
Outward reinsurance premiums		(5)	(6)
Earned premiums, net of reinsurance	4.2	967	1,658
Investment income	5.1	1,412	1,405
Unrealised gains on investments	5.1	799	979
Other technical income		2	13
Total technical income		3,180	4,055
Gross claims paid		(3,504)	(4,210)
Reinsurers' share		13	41
Net claims paid		(3,491)	(4,169)
Change in the gross and net provision for claims	24.3	36	(42)
Claims incurred, net of reinsurance		(3,455)	(4,211)
Change in gross long-term business provision (note 22.10)		485	2,008
Change in reinsurers' share		(3)	(34)
Change in long-term business provision, net of reinsurance		482	1,974
Change in technical provision for linked liabilities, net of reinsurance		134	(440)
Change in other technical provisions, net of reinsurance		616	1,534
Net operating expenses	2.1	(190)	(305)
Investment expenses and charges	5.1	(64)	(1,006)
Other technical charges	2.2	–	(23)
Taxation charge attributable to the long-term business	6.1	(57)	(71)
Allocated investment return transferred (to)/from the non-technical account	5.2	(2)	8
Transfer from/(to) the fund for future appropriations	21	10	(182)
		(303)	(1,579)
Total technical charges		(3,142)	(4,256)
Balance on the technical account – long-term business	4.8	38	(201)
Taxation attributable to the balance on long-term business technical account	6.1	19	(13)
Profit/(loss) on long-term business operations before taxation		57	(214)

All activities relate to continuing operations.

The table below provides a reconciliation between the analysis used in the segmental information in the Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation and in note 3 of this report and the Profit/(loss) on long-term business operations before taxation above:

	Notes	31 Dec 04 £m	31 Dec 03 £m
Operating profit before taxation excluding minority interests, based on longer term investment return before operating exceptionals, amortisation of goodwill and acquired PVIF – Life Services	3.2	51	89
Operating profit before taxation attributable to minority interests		6	–
Amortisation of acquired PVIF ¹	2.2	–	(6)
Impairment of acquired PVIF ¹	2.2	–	(27)
Other operating exceptional costs ¹	22.10	–	(270)
Profit/(loss) on long-term business operations before taxation		57	(214)

Note

1. In 2003, amortisation and impairment of acquired PVIF and other operating exceptional costs were grossed up at the longer term effective tax rate attributable to the balance on the long-term business technical account for the purpose of the Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation and segmental information in note 3.

Consolidated Profit and Loss Account (continued)

Non-technical account

For the year ended 31 December 2004

	Notes	31 Dec 04 £m	31 Dec 03 £m
Balance on the general insurance business technical account			
Discontinued operations		11	9
Balance on the long-term business technical account			
Continuing operations	4.8	38	(201)
Tax credit/(charge) attributable to balance on long-term business technical account	6.1	19	(13)
Shareholders' pre-tax profit/(loss) from long-term business			
Investment income	5.1	57	(214)
Allocated investment return transferred from/(to) the long-term business technical account – continuing operations	5.2	53	27
Unrealised gains/(losses) on investments – continuing operations	5.1	2	(8)
	5.1	2	(148)
Share of operating profit in associates	13.4	1	2
Impairment of goodwill arising on acquisition of associates		–	(9)
Profit/(loss) from interest in associates – discontinued operations		1	(7)
Investment expenses and charges	5.1	(8)	(78)
Allocated investment return transferred to the general business technical account – discontinued operations	5.2	(4)	(3)
Other income (note 8)		80	85
Other charges	2.2	(113)	(530)
Group operating profit/(loss) based on longer term investment return		82	(847)
Short-term fluctuation in investment return	5.2	(2)	(13)
Profit/(loss) from interest in associates		1	(7)
Profit/(loss) on ordinary activities before non-operating exceptional items and taxation			
Continuing operations		109	(862)
Discontinued operations:			
General insurance business		7	6
Other businesses		(35)	(11)
		81	(867)
Non-operating exceptional items – (losses)/profits on disposal/termination of businesses	9	(34)	3
Profit/(loss) on ordinary activities before taxation			
Taxation (charge)/credit on profit/(loss) on ordinary activities	6.1	47	(864)
		(5)	17
Profit/(loss) on ordinary activities after taxation			
Minority interests		42	(847)
		(4)	–
Profit/(loss) for the year attributable to members of the parent company			
Preference dividend on non-equity shares	11	38	(847)
		–	(1)
Retained profit/(loss) for the year			
	19.1	38	(848)
Basic and diluted earnings per share			
	7	1.4p	(119.7p)

A further analysis of operating profit items between continuing and discontinued operations is provided in note 1.2.

Consolidated Statement of Total Recognised Gains and Losses

For the year ended 31 December 2004

	31 Dec 04 £m	31 Dec 03 £m
Profit/(loss) for the year attributable to members of the parent company	38	(847)
Foreign exchange losses	(2)	(3)
Total recognised gains/(losses) arising in the year	36	(850)

Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation

For the year ended 31 December 2004

	Notes	31 Dec 04 £m	31 Dec 03 £m
Henderson Global Investors (Henderson)	3.1	52	32
Life Services	3.2	86	81
Other Businesses	3.3	–	(3)
Business unit operating profit		138	110
Corporate costs		(31)	(12)
Operating profit		107	98
Unallocated interest costs		–	(60)
Operating profit before taxation excluding minority interests, based on longer term investment return before other operating exceptional costs, amortisation of goodwill and acquired PVIF		107	38
Other operating exceptional costs, excluding impairment of goodwill and acquired PVIF ¹	2.3	(10)	(543)
Amortisation and impairment of goodwill	2.2	(20)	(307)
Impairment of goodwill arising on acquisition of associates	2.3	–	(9)
Amortisation and impairment of acquired PVIF ¹	2.2	–	(33)
Short-term fluctuation in investment return	5.2	(2)	(13)
(Losses)/profits on disposal/termination of businesses	9	(34)	3
Profit/(loss) on ordinary activities before taxation excluding minority interests		41	(864)
Operating profit before taxation attributable to minority interests		6	–
Profit/(loss) on ordinary activities before taxation		47	(864)

Note

1. In 2003, amortisation and impairment of acquired PVIF and other operating exceptional costs were grossed up at the longer term effective taxation rate attributable to the balance on the long-term business technical account for the purpose of the Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation and segmental information in note 3.

Consolidated Balance Sheet

Assets

At 31 December 2004

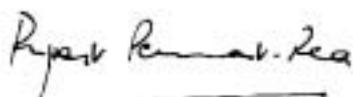
	Notes	31 Dec 04 £m	Restated 31 Dec 03 £m
Intangible assets			
Goodwill	12	233	280
Investments			
Land and buildings	13.1	779	1,632
Investments in joint ventures			
Share of gross assets		40	343
Share of gross liabilities		-	(179)
Loans		-	67
	13.3	40	231
Investments in associates	13.4	537	411
Other financial investments	13.5	22,279	21,506
		23,635	23,780
Assets held to cover linked liabilities	13.5	4,215	4,349
Reinsurers' share of technical provisions			
Long-term business provision (note 22)		78	81
Claims outstanding	24.2	199	244
		277	325
Debtors			
Debtors arising out of direct insurance operations	14.1	18	31
Other debtors	14.2	308	426
		326	457
Other assets			
Tangible assets	15	13	27
Cash at bank and in hand		330	395
Present value of acquired in force long-term business	16	-	10
		343	432
Prepayments and accrued income			
Accrued interest and rent		306	321
Deferred acquisition costs	17	115	151
Other prepayments and accrued income		10	12
		431	484
Total assets		29,460	30,107

Liabilities

At 31 December 2004

	Notes	31 Dec 04 £m	Restated 31 Dec 03 £m
Capital and reserves			
Called up share capital	18.2	271	246
Share premium	19.1	1,081	1,081
Own shares held	19.1	(4)	–
Capital reserve	19.1	2	292
Profit and loss account	19.1	488	70
Equity shareholders' funds	20.1	1,838	1,689
Minority interests		83	–
Fund for future appropriations	21	602	612
Gross technical provisions			
Long-term business provision (note 22)		20,962	21,447
Claims outstanding	24.1	321	429
Equalisation provision	1.1	2	5
Technical provisions for linked liabilities		21,285 4,215	21,881 4,349
		25,500	26,230
Provision for other risks and charges			
Deferred taxation	23.1	36	11
Other provisions	28.1	217	243
		253	254
Creditors			
Creditors arising out of direct insurance operations		3	2
Debenture loans	27.1	348	357
Amounts owed to credit institutions	27.1	296	257
Other creditors including taxation and social security	29	404	534
		1,051	1,150
Accruals and deferred income		133	172
Total liabilities		29,460	30,107

The accounts were approved by the Board of Directors on 22 March 2005 and signed on its behalf by:



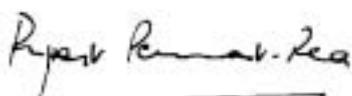
Rupert Pennant-Rea
Chairman

Company Balance Sheet

At 31 December 2004

	Notes	31 Dec 04 £m	31 Dec 03 £m
Fixed assets			
Investments	13.6	3,502	3,129
Current assets			
Debtors	14.2	9	42
Investments	13.6	–	67
Cash at bank		103	11
		112	120
Creditors: amounts falling due within one year	25	(1,849)	(1,206)
Net current liabilities		(1,737)	(1,086)
Total assets less current liabilities			
Creditors: amounts falling due after more than one year	26	(47)	(337)
Provisions for liabilities and charges	28.2	(39)	–
		1,679	1,706
Capital and reserves			
Called up share capital	18.2	271	246
Share premium	19.2	1,081	1,081
Own shares held	19.2	(2)	–
Capital reserve	19.2	–	290
Profit and loss account	19.2	329	89
Equity shareholders' funds	20.2	1,679	1,706

The accounts were approved by the Board of Directors on 22 March 2005 and signed on its behalf by:



Rupert Pennant-Rea
Chairman

Consolidated Cash Flow Statement

For the year ended 31 December 2004

	Notes	31 Dec 04 £m	31 Dec 03 £m
Operating activities			
Net cash inflow/(outflow) from operating activities	32.1	32	(362)
Returns on investments and servicing of finance			
Interest paid		(1)	(73)
Dividends paid to preference shareholders		–	(1)
Net cash outflow from servicing of finance		(1)	(74)
Tax			
Corporation tax received/(paid)		2	(3)
Capital expenditure			
Payments to acquire tangible fixed assets		(4)	(4)
Receipts from sales of tangible fixed assets		1	8
Net cash (outflow)/inflow from capital expenditure		(3)	4
Acquisitions and disposals			
Net cash inflow from acquisitions and disposals	32.2	50	3
Financing activities			
Issue of share capital		118	479
Share issue costs		(3)	(6)
Purchase of own shares held		(4)	–
Proceeds from close out of swaps		–	90
New loans		–	70
Repayment of loans		(2)	(219)
Net cash inflow from financing activities		109	414
Net cash flows available for investment		189	(18)
Cash flows were invested as follows:			
Increase/(decrease) in cash holdings	32.6	6	(99)
Net purchases of investments	32.5	183	81
Net investment of cash flows		189	(18)

The Consolidated Cash Flow Statement does not include any amounts relating to long-term business except cash transactions between the long-term business and shareholder funds and movements in cash held by the Pacific fund.

Notes to the Accounts

Accounting Policies

Basis of presentation and consolidation

The consolidated accounts of the Company and its subsidiary undertakings have been prepared in accordance with the special provisions for insurance groups of Section 255A of, and Schedule 9A to, the Companies Act 1985 except as noted for investment properties (see accounting policy on investments below). The consolidated accounts have also been prepared in accordance with applicable UK accounting standards and under the historical cost accounting rules, modified to include the revaluation of investments, and comply with the UK Statement of Recommended Practice on Accounting for Insurance Business (SORP) issued by the Association of British Insurers in 2003.

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year using consistent accounting policies. No profit and loss account is presented for the Company as permitted by Section 230 of the Companies Act 1985. The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal as appropriate. Where there is a loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting year during which the Group has control. Minority interests represent the equity interests in subsidiaries not held by the Group.

Principal associated undertakings (both associates and joint ventures) are accounted for by the equity method in the consolidated accounts. The profit or loss in respect of interests in associated undertakings attributable to the long-term business fund are treated as unrealised gains or losses within the technical account for long-term business. The profit or loss in respect of other investments in associated undertakings are included in the non-technical account.

Changes in accounting policy

The provisions of the SORP, issued in November 2003, have been adopted in these financial statements. Prior to the adoption of the SORP, the present value of the future margins expected to finance the repayment of limited recourse bonds was classified as an asset in the balance sheet and included within other prepayments and accrued income. This asset was amortised in accordance with the repayment term. Following adoption of the SORP, this accounting treatment is no longer permitted. In the 31 December 2003 balance sheet this has resulted in the recognition of a £111m securitised asset, the recognition of £45m additional deferred acquisition costs (note 17) and a reduction of £66m in the long-term business provision. The 2003 technical account for long-term business has been restated to recognise a £97m increased transfer from the fund for future appropriations (note 21), a £69m change in gross long-term business provision and reductions in net operating expenses and other technical charges of £45m and £121m respectively. This has had no impact on the profit/(loss) for the year attributable to members of the parent company for either 2004 or 2003.

The Group has chosen to early adopt FRS 20 "Share-based payments" in accounting for share-based payment schemes. No prior period adjustments were required. The charge for share-based payments in 2004 is £2m and further information is provided in note 34.

General business

Basis of accounting

All classes of business have been discontinued. Provision has been made for obligations that have been incurred that are not expected to be covered by the future profits of the operation, including the expected future investment return on the related assets and their disposal.

Claims

Full provision is made for the estimated cost of claims, including claims incurred but not reported after taking into account handling costs, anticipated inflation and settlement trends. Any difference between the estimated provision and subsequent settlement is dealt with in the technical accounts of later years.

Equalisation provisions

Equalisation provisions have been established in accordance with the requirements of the Integrated Prudential Sourcebook to mitigate exceptional high loss ratios for classes of business displaying a high degree of claims volatility.

Long-term business

Premiums

Premiums and annuity considerations are credited when they become due. Premiums in respect of linked long-term business are recognised when liabilities arising from these premiums are created. Reinsurance premiums are charged when they are payable.

Funds at retirement under individual pension contracts left with the Group are classified as new business single premiums and for accounting purposes are included in both claims incurred and as single premiums within gross premiums written.

Claims

Claims payable on maturity are recognised when the claim becomes due for payment and on death are accounted for on notification. Surrenders are accounted for at the earlier of the payment date or when the policy ceases to be included within the provision for unit-linked liabilities or the long-term business provision. Where claims are payable and the contract remains in force, the claim instalment is accounted for when due for payment. Claims payable include the costs of settlement.

Long-term business provision and technical provision for linked liabilities

The long-term business provision for non-linked business is determined by the Pearl, NPLL, NPIL and London Life Boards of Directors following their annual investigations of the long-term businesses. This provision is calculated initially to comply with the reporting requirements under the Integrated Prudential Sourcebook using a gross premium valuation method or a method at least as prudent as a gross premium method. The principal assumptions are given in note 22. It includes explicit provision for vested annual bonuses including those relating to the current declaration and makes no provision for future annual or final bonuses. The statutory solvency basis of valuation is then adjusted by eliminating the undistributed surplus carried forward together with general contingency reserves and reserves required under the Integrated Prudential Sourcebook. The provision, which is initially calculated on a statutory solvency basis, is adjusted to remove excessively prudent margins required for statutory solvency purposes.

The technical provision in respect of linked business is equal to the value of the assets to which the contracts are linked. An additional provision in respect of mortality and other risks on linked business is included in the long-term business provision, calculated initially to comply with the reporting requirements under the Integrated Prudential Sourcebook. This is then adjusted to eliminate any undistributed surplus carried forward together with general contingency reserves and reserves required under the Integrated Prudential Sourcebook.

Deferred acquisition costs

Acquisition costs, comprising all direct and indirect costs arising from the conclusion of insurance contracts, are deferred as an explicit acquisition cost asset, gross of tax, and amortised over the period in which the costs are expected to be recoverable out of margins from matching revenues from related policies and in accordance with the pattern of such margins. At the end of each accounting period, deferred acquisition costs are reviewed for recoverability, by category, against future margins from the related policies in force at the balance sheet date.

Profit recognition and the fund for future appropriations

The Group has adopted the modified statutory solvency basis approach in the determination of profit.

Surpluses arising from the participating long-term business, as a result of the annual actuarial valuation of the related assets and liabilities, are subject to appropriation by the directors of the relevant life company subsidiaries to participating policyholders, by way of bonuses, and to shareholders. This determines the profit attributable to shareholders reported in respect of participating business.

Any unappropriated surplus arising in long-term funds is carried forward in the fund for future appropriations. All surplus in other business is attributable to shareholders and included in profit.

The fund for future appropriations represents all funds the allocation of which to participating policyholders and shareholders has not been determined at the balance sheet date. Transfers between the fund for future appropriations and the long-term business technical account represent the changes in these unallocated amounts between balance sheet dates.

Pacific fund

During the mid-1990s, Pearl undertook an exercise to identify the extent to which unattributed surplus assets held within its with-profits fund could be attributed to shareholder contributions or historical shareholder entitlements which had not been withdrawn from the fund. As a result of this exercise, £960m of assets were identified as being shareholder assets. £42m of this capital was paid to the 90:10 fund in order to acquire the rights to expected profit from the newly formed 0:100 fund. The remaining £918m of assets was formally attributed to shareholders with the agreement of the UK regulator. A component of the agreement with the regulator was the formal segmentation of the Pearl long-term fund into separate with-profits (90:10) and non-profit (0:100) components. The attributed assets, known as the Pacific fund, are an earmarked segment of the Pearl 0:100 long-term fund. Under the terms of the agreement with the FSA, the attributed assets were required to remain within Pearl's long-term fund for a period of five years and could then be withdrawn subject to Pearl's governing body confirming that policyholder reasonable expectations would not be affected by the withdrawal. The net assets of the Pacific fund at 31 December 2004 were £569m.

The Consolidated Cash Flow Statement includes movements in cash held by the Pacific fund.

Fees and commissions

Asset management fees are credited on an accruals basis and commissions are credited as earned. Performance fees, which include all incentive fees and gains/losses on investments that the Group holds in the funds that it manages, are only recognised once they have been "locked in" and cannot subsequently be reversed.

Investments

Company balance sheet

Investments consist of investments in subsidiary undertakings, authorised collective investment schemes and short-term deposits. Investments in subsidiary undertakings are included at cost less any provision for impairment where circumstances indicate that the carrying value may not be recoverable. Investments in authorised collective investment schemes are included at middle market value. Short-term deposits are included at cost.

Group balance sheet

Investments are stated at current value at the balance sheet date, calculated as follows:

- freehold and leased properties have been valued at open market value. Other than for leasehold properties where the lease has less than 20 years unexpired term, no provision is made for depreciation of investment properties. The Directors consider that as these properties are held for investment, to depreciate them would not give a true and fair view. Depreciation is only one of many factors considered in the independent valuation of such properties. It is the Group's practice to maintain properties occupied by the Group in a continual state of sound repair. Accordingly, the Directors consider that the economic lives of these properties and their residual values, based on prices prevailing at time of acquisition or subsequent valuation, are such that any depreciation is insignificant and is thus not provided. No depreciation is provided on properties held for own use since such depreciation is immaterial;
- listed investments are stated at the middle market value;
- investments in authorised collective investment schemes are included at middle market value;
- short-term deposits are included at cost;
- other investments are shown at Directors' estimates of market value; and
- interests in property limited partnerships and Jersey Property Unit Trusts (JPUTs) within the long-term business which affect or establish policyholders' rights or are otherwise held as part of the Group's investment portfolio are accounted for as subsidiaries, joint ventures, associates or investments in land and buildings depending on the holdings of the Group and on the level of influence and control that the Group exercises. Where the interest is managed by a contractual agreement such that no one party exerts control, notwithstanding the Group's share, both direct and indirect, may be greater than 50%, such interests have been accounted for as joint ventures. The Group's share of the respective interests' gross assets and gross liabilities are shown on the face of the consolidated balance sheet, in accordance with the requirements of FRS 9 "Associates and joint ventures". Where the interest is managed by a contractual agreement, such that the Group can exercise a significant influence, but one other party controls the partnership, such interests have been accounted for as associates. The Group's share of the respective interests' net assets and liabilities are shown on the face of the consolidated balance sheet, in accordance with the requirements of FRS 9 "Associates and joint ventures". Where the Group holds minority stakes, with no disproportionate influence, the relevant investments are included in land and buildings at their market value.

Notes to the Accounts (continued) Accounting Policies (continued)

Investment income, realised and unrealised gains and losses on investments

Dividends are included as investment income on the date that shares become quoted ex-dividend. Interest and rents are included on an earned basis.

Realised gains and losses on investments are calculated as the difference between the net sales proceeds and original cost. Unrealised gains and losses on investments represent the difference between the valuation of investments at the balance sheet date and their original cost, or if they have been previously revalued, the valuation at the last balance sheet date. The movement in unrealised gains and losses recognised in the period also includes the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

Long-term business investment income and unrealised gains and losses are included in the technical account – long-term business. Investment return is allocated from the technical account – long-term business to the non-technical account so as to reflect the longer term investment return on investments directly attributable to shareholders in the balance on the technical account.

An allocation of investment return from the non-technical account to the general business technical account is made based upon the level of technical provisions and capital allocated to back these provisions.

Goodwill

Goodwill arising on acquisitions, being the difference between the fair value of the purchase consideration and the fair value of net assets acquired, is capitalised in the balance sheet and amortised over its useful economic life or 20 years if shorter. The carrying value of goodwill is tested annually for indicators of impairment.

Present value of acquired in force business

Acquired PVIF is recognised in the balance sheet as an asset. To the extent that the acquired PVIF will be recognised as profit over the remaining lifetime of the related in force policies, it is amortised on a systematic basis, and the discount unwound, over the anticipated lives of the related contracts of the portfolios. The carrying value of the asset is tested annually for indicators of impairment. Any amortisation or impairment charge is recorded in the long-term business technical account in "Other technical charges".

Fixed assets and depreciation

All items of capital expenditure are capitalised and depreciated on a straight-line basis over their useful economic life of between two and ten years.

Guarantee fund levies

Provision is made at the balance sheet date for levies declared by the Financial Services Compensation Scheme before completion of the financial statements. Provision is also made if it is more likely than not that a levy will be raised based on premium income, which has already been recognised in the financial statements.

Taxation

The Group recognises deferred tax assets and liabilities on a discounted basis to reflect the time value of money. A discount rate has been selected that reflects the yield on government bonds which have a maturity date similar to the likely average period for assets upon which deferred tax liabilities and assets arise. Deferred tax is recognised in respect of all timing differences that have originated but not reversed by the balance sheet date with the following exceptions:

- provision is made for deferred tax that would arise on remittance of the retained earnings of overseas subsidiaries, associates and joint ventures only to the extent that, at the balance sheet date, dividends have been accrued as receivable; and
- deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax on changes in the fair value of investments is recognised in the profit and loss account.

The transfer from the long-term business account to the non-technical account is grossed up at the longer term effective rate of corporation tax.

Pension costs

In accordance with SSAP 24, defined benefit pension costs are recognised on a systematic basis so that the cost of providing retirement benefits to employees is evenly spread over the service lives of the employees concerned. Variations arising from actuarial surpluses are spread over the average remaining service lives of members to the extent that the resulting credit does not exceed the regular cost. The Group also operates a defined contribution scheme. Contributions are charged in the profit and loss account as they become payable in accordance with the rules of the scheme.

Operating and finance leases

Assets used by the Group which have been funded through finance leases are capitalised and the resulting lease obligations are included in creditors. Rental payments under operating leases are charged to the profit and loss account as incurred.

Borrowings

Borrowings issued at a discount are included in the balance sheet at their proceeds, net of expenses, together with any unamortised discount and issue expenses at the balance sheet date. The discount and expenses are charged to loan interest in the profit and loss account over the term of the borrowings. Interest payable and receivable related to interest rate swaps on the Group's borrowings is included within investment expenses and charges in the profit and loss account.

Limited recourse bonds

Expenditure incurred in the issue of limited recourse bonds is amortised at a constant rate over the term of the loan and the carrying value of the liability represents the par value less unamortised issue expenses. Some such liabilities are secured on a block of existing policies. The limited recourse bonds currently in issue are detailed in note 27.

Foreign currencies

Transactions in currencies other than the functional currency of the undertaking concerned are recorded at the rate appropriate at the time of accounting for the transaction. Currency balances at the year end are converted at the rate ruling at that date except where covered by an open foreign exchange contract in which case the rate specified in the contract is used. Assets and liabilities of those subsidiaries and associates which prepare accounts in currencies other than the Group's reporting currency are translated at year end rates. The results and cash flows of these undertakings are translated at average rates for the year.

Differences on exchange arising from the translation of opening balance sheets of those subsidiaries and associates whose reporting currency is not sterling, together with the differences between the results of these undertakings translated at average rates for the year and year end rates, are taken directly to reserves, together with differences on non-sterling borrowings used to hedge those investments.

All other gains and losses are taken to the profit and loss account.

Share-based payment transactions

The Group issues equity-settled and cash-settled share-based payments to certain employees.

Equity-settled share-based payments are measured at fair value at the date of grant and expensed, together with a corresponding increase in equity, on a straight line basis over the vesting period, based on the Group's estimate of shares that will eventually vest. Details of the measurement of fair values are set out in note 34 to the accounts. The expected life used in the determination of fair value has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

A liability equal to the portion of the goods or services received is recognised at the current fair value determined at each balance sheet date for cash-settled, share-based payments.

Own shares held

Own shares held by the Group, including those held by employee benefit trusts, are recorded at cost and deducted from equity shareholders' funds.

1. Analysis of profit/(loss) items between continuing and discontinued operations

1.1 General business – Equalisation provisions

Equalisation provisions are established in accordance with the requirements of the Integrated Prudential Sourcebook to mitigate exceptional high loss ratios for classes of business displaying a high degree of claims volatility. These provisions, which are in addition to the provisions required to meet the anticipated ultimate cost of settlement of outstanding claims at the balance sheet date, are required by Schedule 9A to the Companies Act 1985 to be included within technical provisions in the balance sheet notwithstanding that they do not represent liabilities at the balance sheet date. This has had the effect of reducing shareholders' funds by £2m as at 31 December 2004 (2003: £5m). The movement in equalisation provisions during the year resulted in an increase in the general business technical account result and the profit before taxation of £3m in 2004 (2003: £2m).

1.2 Non-technical consolidated profit and loss account

Included below is an analysis of profit/(loss) items in the non-technical consolidated profit and loss account between continuing and discontinued operations:

	31 Dec 04		31 Dec 03	
	Continuing £m	Discontinued £m	Continuing £m	Discontinued £m
Investment income	53	–	25	2
Investment expenses and charges	8	–	76	2
Other income	76	4	83	2
Other charges	73	40	524	6
Non-operating exceptional items – (losses)/profits on disposal/termination of businesses	(47)	13	–	3

Discontinued operations comprise AMPLE, Cogent, Henderson private client asset management business, Towry Law International and Virgin Money Group Limited.

2. Net operating expenses and other charges

2.1 Net operating expenses

	Technical account General business		Technical account Long-term business	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	Restated 31 Dec 03 £m
Acquisition costs:				
Commission	–	–	8	12
Other	–	–	3	19
Change in deferred acquisition costs (note 17)	–	–	36	92
Administrative expense (release)/charge	(2)	(5)	143	182
	(2)	(5)	190	305

2.2 Other technical charges and other charges

	Technical account Long-term business		Non-technical account	
	31 Dec 04 £m	Restated 31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Amortisation of goodwill (note 12)	–	–	18	35
Impairment of goodwill (note 12)	–	–	2	272
Amortisation of acquired PVIF	–	4	–	–
Impairment of acquired PVIF	–	19	–	–
Other expenditure/charges	–	–	93	223
	–	23	113	530
Operating exceptional charges included above	–	19	10	415

Included in other expenditure above in 2004 is £10m of exceptional costs, associated with the restructure of Henderson, the UK operations of Towry Law, and Corporate Office.

Other expenditure in 2003 included exceptional costs of £143m in respect of the changes to the Life Services businesses required as a result of the Group's Demerger from AMP and the subsequent decision to close all life companies to new business. This was in respect of £87m of restructuring costs, £41m relating to the vacation of leasehold properties and £15m of sundry other costs associated with the Demerger.

Also included in the table above are £272m exceptional charges in respect of the impairment of the Group's purchased goodwill arising from reviews by management at 31 December 2003. The discount rate used to calculate the impairment of goodwill was a risk free rate of 4.37%, plus a risk factor of 6%.

In 2003, amortisation and impairment of acquired PVIF were grossed up at the longer term effective tax rate attributable to the balance on the long-term business technical account for the purpose of the Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation and segmental information in note 3. The tax attributable to the amortisation of acquired PVIF was £2m and to the impairment of acquired PVIF was £8m.

2.3 Analysis of operating exceptional charges

	Technical account Long-term business		Non-technical account	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Impairment of goodwill	–	–	–	272
Impairment of goodwill arising on acquisition of associates	–	–	–	9
Impairment of acquired PVIF	–	19	–	–
Restructuring costs (note 2.2)	–	–	10	143
Impairment of contingent loans (note 5.1)	–	–	–	130
Charges arising from changes in actuarial assumptions (note 22.10)	–	242	–	–
	–	261	10	554

In 2003, impairment of acquired PVIF and other operating exceptional costs were grossed up at the longer term effective tax rate attributable to the balance on the long-term business technical account for the purpose of the Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation and segmental information in note 3. The tax attributable to the impairment of acquired PVIF was £8m and to the charges arising from changes in actuarial assumptions was £28m.

2.4 Depreciation

Net operating expenses include:

	31 Dec 04 £m	31 Dec 03 £m
Depreciation of tangible fixed assets (note 15)	17	9

2.5 Analysis of staff costs

Staff costs comprise:

	31 Dec 04 £m	31 Dec 03 £m
Salaries and wages	124	204
Social security costs	12	16
Pension costs (note 33.1)	15	2
Total	151	222

Included within 2003 wages and salaries above are £38m of operating exceptional charges relating to the restructure of the Life Services businesses referred to in notes 2.2 and 2.3. Social security costs for 2003 also include operating exceptional restructuring costs of £2m. Pension costs for 2003 of £2m comprise operating exceptional restructuring costs for pension augmentations.

2.6 Average employee numbers

The average number of employees of the Group was as follows:

	31 Dec 04 No.	31 Dec 03 No.
Henderson	853	796
Life Services	1,457	3,404
Other Businesses	790	793
Total employees	3,100	4,993

Notes to the Accounts (continued)

2. Net operating expenses and other charges (continued)

2.7 Auditors' remuneration

	31 Dec 04 £m	31 Dec 03 £m
Statutory audit services	1.7	1.4
Statutory regulatory reporting	0.3	0.3
Non-statutory audit of half year financial information	–	0.3
Further assurance services	0.5	0.1
Tax advisory services	0.3	0.2
Other non-audit services	0.5	2.9
Total services	3.3	5.2

Included within further assurance services in 2004 is £0.3m relating to assurance work on the Group's IFRS project.

Other non-audit services remuneration in 2004 includes £0.4m in relation to the sale of the Life Services business (note 9). In 2003, other non-audit services remuneration included £2.7m on work related to the Demerger of the Group from AMP.

3. Segmental information – Group operating profit and net assets

3.1 Operating profit – Henderson

	31 Dec 04 £m	31 Dec 03 £m
Revenue		
Total fee income	234	193
Investment income	8	3
Total revenue	242	196
Expenses		
Operating expenses	(185)	(157)
Depreciation	(5)	(7)
Total expenses	(190)	(164)
Operating profit	52	32

Total fee income includes £45m (2003: £44m) relating to insurance companies within the Group.

3.2 Operating profit before taxation, exceptional costs, amortisation of goodwill and acquired PVIF, and excluding minority interests – Life Services

	31 Dec 04 £m	Restated 31 Dec 03 £m
Earned premiums, net of reinsurance	967	1,658
Claims incurred, net of reinsurance	(3,455)	(4,211)
Net investment return	2,141	1,399
Operating expenses and other technical charges	(190)	(305)
Changes in other technical provisions, net of reinsurance	616	1,776
Taxation	(38)	(46)
Transfer from/(to) the fund for future appropriations	10	(182)
Total from the long-term technical account	51	89
General insurance	13	12
Service Company	8	(8)
Other shareholders' interests	14	(12)
Operating profit	86	81

3.3 Operating profit/(loss) – Other Businesses

	31 Dec 04 £m	31 Dec 03 £m
Towry Law	(1)	1
Virgin Money	1	2
AMPLE	–	(6)
Operating profit/(loss)	–	(3)

	31 Dec 04 £m	31 Dec 03 £m
Towry Law		
Revenue	42	48
Expenses	(43)	(47)
Operating (loss)/profit	(1)	1

3.4 Geographical analysis of operating profit/(loss)

	31 Dec 04 £m	31 Dec 03 £m
Henderson		
United Kingdom	56	37
Europe	(2)	(2)
United States	(3)	(5)
Other overseas	1	2
Operating profit	52	32

	31 Dec 04 £m	31 Dec 03 £m
Towry Law		
United Kingdom	–	1
International	(1)	–
Total	(1)	1

All other operating profit/(loss) arises in the United Kingdom.

3.5 Net assets by business and geographical segment

	31 Dec 04 £m	31 Dec 03 £m
Henderson		
United Kingdom	296	288
Europe	65	64
United States	11	12
Other overseas	10	9
Total Henderson	382	373
Life Services	1,483	1,177
Other Businesses	23	73
Corporate	33	68
Net assets	1,921	1,691
Financed by:		
Capital and reserves	1,838	1,689
External loans	–	2
Minority interests	83	–
	1,921	1,691

The net assets of Life Services, Other Businesses and Corporate are employed in the United Kingdom.

4. Segmental information – Long-term business

Almost all business is direct and written in the UK in respect of continuing operations.

4.1 Analysis of gross premiums written

	31 Dec 04 £m	31 Dec 03 £m
Premiums from individuals	912	1,494
Premiums from group contracts	60	170
	972	1,664
Life business	253	353
Annuity business	98	193
Pension business	621	1,118
	972	1,664

4.2 Analysis of earned premiums, net of reinsurance

	31 Dec 04 £m	31 Dec 03 £m
Premiums from individuals	907	1,488
Premiums from group contracts	60	170
	967	1,658
Life business	249	347
Annuity business	98	193
Pension business	620	1,118
	967	1,658

4.3 Analysis of gross premiums written by way of direct insurance split by premium type

	31 Dec 04 £m	31 Dec 03 £m
Regular premiums	545	754
Single premiums	427	910
	972	1,664

4.4 Analysis of gross premiums written by way of direct insurance split by contract type

	31 Dec 04 £m	31 Dec 03 £m
Non-profit contracts	324	469
With-profits contracts	446	686
Linked contracts	202	509
	972	1,664

4.5 Analysis of new gross written premiums

	31 Dec 04 £m	31 Dec 03 £m
Life business	1	35
Annuity business	7	87
Pension business	421	823
	429	945

Industrial branch premiums of £23m in 2004 (2003: £36m) are classified as regular premium with-profits life business in the above analysis.

4.6 New business annual premium equivalent

	31 Dec 04 £m	31 Dec 03 £m
Annual premium equivalent	45	126

4.7 Analysis of new gross premiums written by way of direct insurance

	31 Dec 04 £m	31 Dec 03 £m
Regular premiums (annualised)	2	35
Single premiums	427	910
	429	945
Non-profit contracts	272	426
With-profits contracts	65	206
Linked contracts	92	313
	429	945

In classifying new business premiums, the basis of recognition adopted is as follows:

- incremental increases on existing policies are classified as new business premiums;
- rebates from the Department of Social Security are classified as new single premiums; and
- funds at retirement under individual pension contracts left with the Group are classified as new business single premiums and for accounting purposes are included in both claims incurred and as single premiums within gross written premiums.

4.8 Analysis of balance on technical account

	31 Dec 04 £m	31 Dec 03 £m
Non-linked:		
Life and annuity business	26	20
Pension business	42	(52)
Shareholders' attributable assets	(35)	(173)
	33	(205)
Linked:		
Life business	1	1
Pension business	4	3
	5	4
Balance on technical account – long-term business	38	(201)

5. Investment return

5.1 Actual investment income

	Technical account Long-term business		Non-technical account	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Income from land and buildings	40	100	–	–
Income from other investments	1,229	1,305	52	27
Gains on realisation of investments	143	–	1	–
Investment income	1,412	1,405	53	27
Unrealised gains/(losses)	799	979	2	(148)
Investment management expenses and charges	(20)	(27)	–	–
Interest on bank loans and overdrafts	–	(1)	–	–
Other loan interest	(44)	(53)	(8)	(74)
Losses on realisation of investments	–	(925)	–	(4)
Investment expenses and charges	(64)	(1,006)	(8)	(78)
Total investment return	2,147	1,378	47	(199)

Included in unrealised losses in the non-technical account for the year ended 31 December 2003 is an operating exceptional charge of £130m in respect of the impairment of the contingent loan to the long-term fund of London Life (note 31), which was caused by changes arising from the restructuring of Life Services resulting from the proposed Demerger of the Group from AMP announced on 1 May 2003.

Notes to the Accounts (continued)
5. Investment return (continued)

5.2 Longer term investment return

The longer term investment return, net of expenses, allocated to the general business technical account in 2004 was £4m (2003: £3m). The longer term investment return transferred (from)/to the long-term business technical account in 2004 was £(2)m (2003: £8m).

The longer term investment return and short-term fluctuations are as follows:

	Shareholders' interest in long-term business		Non long-term business	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Total investment return before taxation	26	42	47	(199)
Less: investment return not supporting general insurance	–	–	(47)	197
	26	42	–	(2)
Longer term investment return	24	50	4	3
Short-term fluctuation in investment return	2	(8)	(4)	(5)
Total investment return	26	42	–	(2)

(i) The longer term return is calculated separately for general insurance business and certain long-term business operations. In respect of equities, gilts and cash, the return is calculated by multiplying the opening market value of the investments by the longer term rate of investment return. The longer term rate of investment return is set by reference to the market redemption yields at the measurement date. The allocated longer term return for other investments is the actual income receivable for the year.

(ii) The principal assumptions underlying the longer term investment return are:

	31 Dec 04 %	31 Dec 03 %
Equities	8.6	8.0
Gilts	5.1	5.0
Cash	3.9	3.7

(iii) Comparison of longer term investment return with actual returns

The actual return on investments, before deducting investment management expenses and charges, is compared below with the aggregate longer term return over a five year period.

	01 Jan 00 to 31 Dec 04 £m	01 Jan 99 to 31 Dec 03 £m
Actual return attributable to shareholders:		
Long-term business	96	197
Non long-term business	20	32
Longer term return credited to operating results:		
Long-term business	(265)	(308)
Non long-term business	(40)	(47)
Shortfall of actual returns over longer term returns	(189)	(126)

(iv) The table below shows the sensitivity to changes in the longer term rates of returns:

Movement in investment return	By	Change in	By
Equities	1% higher/lower	Group operating profit before taxation	£nil
Gilts	1% higher/lower	Group operating profit before taxation	£2m
Cash	1% higher/lower	Group operating profit before taxation	£3m

6. Taxation

6.1 Taxation

	Technical account Long-term business		Non-technical account	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
United Kingdom corporation taxation				
Current tax charge/(credit) for the year	74	56	1	(14)
Adjustments for previous years	(44)	(4)	(15)	7
	30	52	(14)	(7)
Overseas taxation	1	2	1	–
Tax attributable to the balance on long-term business technical account	–	–	19	(13)
Total current taxation	31	54	6	(20)
Deferred taxation				
Origination and reversal of timing differences	19	(2)	(9)	3
Adjustment to the estimated recoverable amount of deferred tax assets arising in previous periods	10	20	8	–
Decrease in discount	(3)	(1)	–	–
Total deferred taxation	26	17	(1)	3
Total tax charge/(credit)	57	71	5	(17)

After taking into account reliefs to which the Group is entitled, UK corporation tax on taxable profits attributable to shareholders has been accounted for at the rate of 30% (2003: 30%). The tax rate for the life policyholders is 20% (2003: 22% and 20%).

6.2 Factors affecting tax charge for year

The tax assessed in the year is lower than the standard rate of corporation tax in the UK and the differences are explained below.

The standard rate of tax has been determined by using the UK rate enacted for the year for which the profits/(losses) will be taxed.

	31 Dec 04 £m	31 Dec 03 £m
Profit/(loss) on ordinary activities before taxation	47	(864)
Profit/(loss) on ordinary activities multiplied by the standard rate of corporation tax in the UK of 30% (2003: 30%)	14	(259)
Effects of:		
Non-taxable book gains on sales of subsidiaries and associates	–	(5)
Non-taxable goodwill amortisation and impairment	7	187
Other disallowable expenses	20	6
Timing differences other than on long-term business	(18)	30
Adjustment to taxation charge in prior years	(15)	7
Lower tax rates on overseas earnings	(2)	(1)
Non-taxable income	–	6
Current taxation losses surrendered for £nil value	–	9
Current taxation charge/(credit) for the year	6	(20)

7. Earnings per share

7.1 Basic earnings per share

	Profit/(loss)		Basic earnings per share	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 pence	31 Dec 03 pence
Profit/(loss) on ordinary activities after taxation	42	(847)	1.6	(119.6)
Minority interests	(4)	–	(0.2)	–
Profit/(loss) for the year attributable to members of the parent company	38	(847)	1.4	(119.6)
Preference dividend on non-equity shares	–	(1)	–	(0.1)
Basic earnings/earnings per share	38	(848)	1.4	(119.7)
Basic weighted average number of 10 pence shares (millions)	2,646	708		

7.2 Diluted earnings per share

	Profit/(loss)		Diluted earnings per share	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 pence	31 Dec 03 pence
Profit/(loss) on ordinary activities after taxation	42	(847)	1.6	(119.6)
Minority interests	(4)	–	(0.2)	–
Profit/(loss) for the year attributable to members of the parent company	38	(847)	1.4	(119.6)
Preference dividend on non-equity shares	–	(1)	–	(0.1)
Diluted earnings/earnings per share	38	(848)	1.4	(119.7)
Diluted weighted average number of 10 pence shares (millions)	2,654	708		

Basic and diluted earnings per share have been calculated on the profit/(loss) attributable to equity shareholders. The difference of 8 million 10 pence shares between the weighted average number of shares used in the basic earnings per share and the diluted earnings per share calculations reflects the dilutive impact of the Group's share-based payment schemes (note 34).

On 26 November 2003, the High Court of Justice in England confirmed a reduction in the authorised share capital of the Company from £2,350m to £27m and as part of this arrangement, 759,870,000 ordinary shares of £1, all of the 16,770,000 'A' redeemable preference shares of £1 and all of the 1,350,704,312 preferred ordinary shares of £1 in issue were cancelled and extinguished. Subsequently, on the Demerger of the Group from AMP on 12 December 2003, the remaining ordinary shares of £1 were sub-divided into ordinary shares of 10 pence. To enable fair comparison, the weighted average numbers of shares has been calculated on the basis that the number of 10 pence ordinary shares that were in issue on 12 December 2003 was equivalent to the total number of £1 ordinary shares and £1 ordinary preferred shares on 26 November 2003.

8. Other income

Other income includes elements of the profit before tax on the investment management business and commission on sales made by Towry Law.

9. Exceptional items

The non-operating exceptional items have arisen from the disposal/termination of the following businesses:

	31 Dec 04 £m	31 Dec 03 £m
Virgin Money Group Limited	18	–
Towry Law International	(8)	–
Life Services	(47)	–
Cogent	3	(5)
Henderson private client asset management business	–	8
Total (losses)/profits on disposal/termination of businesses	(34)	3

Interactive Investor Trading Limited

On 27 February 2004, 100% of the issued shares in Interactive Investor Trading Limited, which represented the AMPLE business, were sold to Carruthers and Associates Limited which resulted in a profit on disposal of £nil.

Virgin Money Group Limited

On 27 April 2004, HHG Virgin Holdings Limited (subsequently renamed HHG (VH) Limited) sold its equity interest in Virgin Money Group Limited to Virgin Group Investments Limited. Also on this date, the loan from Pearl to Virgin Money Group Limited was sold to Virgin Management Limited for £90m. £50m of this consideration was received on completion of the deal, £20m will become due 12 months after the date of completion and the final £20m will be payable 24 months after the date of completion. The net consideration was £75m, reflecting the discounting of amounts receivable in future years, provisions in respect of certain indemnities given under the transaction and transaction expenses. A profit of £18m was recorded on the disposal.

Towry Law International

On 27 May 2004, Towry Law announced that it would close its international operations to new business resulting in a loss of £8m arising from costs of terminating those operations. A cash outflow of £6m arose in respect of this in 2004.

Life Services

On 9 December 2004, the Company and its wholly owned subsidiary undertaking, Pearl Group Limited, entered into an agreement to sell the Life Services business owned by Pearl Group Limited to Life Company Investor Group Limited (see note 38). The agreed consideration of £1.070bn for this transaction indicated an impairment had occurred in both the goodwill and PVIF of the Life Services business. As a consequence, these assets were written down to their net realisable value of £nil and impairments of £29m and £10m were reported for goodwill and PVIF respectively. £8m of associated committed transaction costs have also been recognised and a cash outflow of £3m arose in respect of this in 2004.

Cogent

On 2 September 2002, the Group completed the sale of Cogent Investment Operations Limited, a subsidiary undertaking. In 2003, a loss on disposal of £5m was reported in the profit and loss account in respect of this sale, consisting of additional sales proceeds of £6m offset by further disposal costs and increases in provisions for related contractual obligations of £11m. During 2004, £3m of unutilised provisions for related contract obligations were released. Contract obligations relating to the sale cease by June 2008.

Henderson private client asset management business

During 2002, the Group disposed of its private client asset management business to Newton Investment Management. A further £8m of profit arose during 2003 on receipt of a tranche of proceeds from this disposal not recognised during 2002 since it was contingent.

10. Directors' emoluments

The information is included in the Report on Directors' Remuneration on pages 21 to 27.

11. Dividends

	31 Dec 04		31 Dec 03	
	Per share pence	Total £m	Per share pence	Total £m
Non-equity dividends on 'A' preference shares	–	–	4.6	1

12. Goodwill

	Total £m
Cost	
At 1 January 2004	1,809
Acquisition of Towry Law Mortgage Services Limited	2
At 31 December 2004	1,811
Amortisation and impairment	
At 1 January 2004	1,529
Amortisation charge for the year	18
Impairment charge for the year – Life Services non-operating exceptional item (note 9)	29
Other impairment charges for the year	2
At 31 December 2004	1,578
Net book value	
At 31 December 2004	233
At 31 December 2003	280

On 14 October 2004, one of the Group's principal subsidiaries, Towry Law plc, purchased the remaining 50% stake in Towry Law Mortgage Services Limited. This resulted in goodwill of £2m which was immediately impaired.

13. Investments**13.1 Investments – land and buildings**

	Freehold £m	Long leasehold £m	Short leasehold £m	Total £m
Group				
At 1 January 2004	1,165	466	1	1,632
Additions	7	343	–	350
Disposals	(1,045)	(166)	(1)	(1,212)
Surplus on revaluation	6	3	–	9
At 31 December 2004	133	646	–	779
Land and buildings at cost:				
At 31 December 2004	145	623	–	768
At 31 December 2003	1,059	444	–	1,503

As part of the Group's ongoing review of its investment strategy, a significant number of property holdings were moved into more liquid investments in the form of JPUTs and cash during 2004.

All properties held by the Group were valued as at 31 December 2004 and 31 December 2003 by qualified professional valuers working for the companies DTZ Debenham Thorpe, Knight Frank LLP or CB Richard Ellis Limited.

Investment properties were valued on the basis of open market value. The properties in owner occupation for the purposes of the Group's business were valued on the basis of existing use value. All valuations were carried out in accordance with the Royal Institution of Chartered Surveyors (RICS) Appraisal and Valuation Manual. All such valuers are Chartered Surveyors, being members of the RICS.

Other than for leasehold properties, where the lease has less than 20 years' unexpired term, no provision is made for depreciation of investment properties.

Leasehold properties include £264m (2003: £267m) property reversions arising from sales of the NPI Extra Income Plan. The reversionary interest is valued as the NPIL and NPLL proportion of the current market value, projected for the lifetime of the policyholder at the assumed future increase in house prices, then discounted back by the valuation rate of interest.

Included in the figures shown for current value is £30m (2003: £36m) in respect of buildings which are owned and occupied by the Group.

13.2 Investments in participating interests

	Cost		Carrying value	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Group				
Investments in joint ventures (note 13.3)	40	137	40	231
Investments in associates (note 13.4)	460	405	537	411
Total	500	542	577	642

13.3 Investments in joint ventures

	Long-term business £m
Group	
Share of result for the year after taxation	9
Disposals	(200)
Movements in investments in joint ventures	(191)
At 1 January 2004	231
At 31 December 2004	40

13.4 Investments in associates

	Long-term business		Non long-term business		Total carrying value £m
	Share of capital and reserves £m	Loan £m	Share of capital and reserves £m	Loan £m	
Group					
At 1 January 2004	315	39	(34)	91	411
Operating profit for the year after taxation	71	–	1	–	72
Additions/(disposals)	160	(48)	33	(91)	54
Movements in year	231	(48)	34	(91)	126
At 31 December 2004	546	(9)	–	–	537

Long-term business additions include investments made in the period in Henderson Caspar Property Fund, Henderson Central London Office Fund, Henderson (UK) Retail Warehouse Fund and Henderson UK Shop Fund.

13.5 Other financial investments

	31 Dec 04		31 Dec 03	
	Market value £m	Cost £m	Market value £m	Cost £m
Group				
Shares and other variable yield securities and units in unit trusts	3,615	3,143	3,330	2,638
Debt securities and other fixed income securities	16,980	16,415	14,345	13,738
Loans secured by mortgage	87	87	85	73
Other loans	21	21	19	19
Deposits with credit institutions	1,576	1,576	3,727	3,727
	22,279	21,242	21,506	20,195
Listed investments included above	19,904	18,965	17,210	16,449
Assets held to cover linked liabilities	4,215	4,210	4,349	5,064

Deposits with credit institutions include a collateral fund of £128m (2003: £113m) (note 27.1 (b)).

Notes to the Accounts (continued)
13. Investments (continued)

13.6 Investments of the Company

	Shares in subsidiary undertakings £m	Loans to subsidiary undertakings £m	Total fixed asset investments £m
Cost			
At 1 January 2004	5,251	298	5,549
Additions	2,098	145	2,243
Disposals	(1,992)	(236)	(2,228)
At 31 December 2004	5,357	207	5,564
Provision for impairment			
At 1 January 2004	(2,367)	(53)	(2,420)
Charge for the year	(141)	–	(141)
Disposals	446	53	499
At 31 December 2004	(2,062)	–	(2,062)
Net book value			
At 31 December 2004	3,295	207	3,502
At 31 December 2003	2,884	245	3,129
			Units in unit trusts £m
Cost			
At 1 January 2004			67
Disposals			(67)
At 31 December 2004			–
Net book value			
At 31 December 2004			–
At 31 December 2003			67

The impairment charge for the year includes an impairment of £107m in the Company's investment in its direct subsidiary, Pearl Group Limited, as a result of the sale of the Life Services business to Life Company Investor Group Limited (note 38) based on the expected consideration to be received from Life Company Investor Group Limited less expected disposal costs. The Company's other shares in subsidiary undertakings were impaired to their net asset values.

During the year, the Company transferred the ownership of a number of subsidiaries within the Group as part of a Group restructure. The net book value of these shares in the subsidiary undertakings was £207m and the aggregate consideration was £220m. In addition to this, subsidiary undertakings with a net book value of £1,339m were liquidated.

14. Debtors

14.1 Debtors arising out of direct insurance operations

	31 Dec 04 £m	31 Dec 03 £m
Group		
Amounts owed by policyholders	18	31

14.2 Other debtors

	Group		Company	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Outstanding sale of investments	118	138	–	–
Amounts due from Group undertakings	–	–	7	25
Other debtors	190	288	2	4
Corporation tax recoverable	–	–	–	13
	308	426	9	42

15. Tangible assets

	Total £m
Cost	
At 1 January 2004	42
Additions	4
Disposals	(8)
At 31 December 2004	38
Depreciation	
At 1 January 2004	15
Charge for the year	17
On disposals	(7)
At 31 December 2004	25
Net book value	
At 31 December 2004	13
At 31 December 2003	27

16. Present value of acquired in force long-term business

	Total £m
Cost	
At 1 January and 31 December 2004	101
Amortisation and impairment	
At 1 January 2004	91
Impairment charge – Life Services non-operating exceptional item (note 9)	10
At 31 December 2004	101
Net book value	
At 31 December 2004	–
At 31 December 2003	10

The principal assumptions used to calculate the acquired PVIF are the same as those used to calculate the long-term business provision (note 22).

17. Deferred acquisition costs

	Long-term business £m
At 1 January 2004 as previously reported	106
Prior year adjustment	45
At 1 January 2004 restated	151
Decrease in year	(36)
At 31 December 2004	115

18. Share capital**18.1 Share capital authorised**

	31 Dec 04 £m	31 Dec 03 £m
4,250,000,000 ordinary shares of 10 pence each	425	425

18.2 Share capital allotted

	31 Dec 04 £m	31 Dec 03 £m
Allotted, called up and fully paid equity shares: 2,710,562,634 (2003: 2,464,049,470) ordinary shares of 10 pence each	271	246

On 31 March 2004, as part of an institutional capital raising, the Company issued 246,160,000 ordinary shares of 10 pence each at a price of 48 pence for consideration of £115m (net of expenses of £3m) through HHG Capital (Jersey) Limited, a special purpose entity. £25m was taken to share capital and the balance of £90m was initially taken to a merger reserve but then transferred to the profit and loss account reserve following the redemption of shares in HHG Capital (Jersey) Limited.

During the year, the Company issued 55,517 shares of 10 pence each to certain employees leaving the group participating in the Sharesave Scheme (see note 34) for an aggregate consideration of £23,095.

During the year, the Company also issued 297,647 shares of 10 pence each to the employee benefit trust administering the Share Incentive Plan (see note 34) for an aggregate consideration of £144,949.

19. Reserves**19.1 Group**

	Share premium £m	Own shares held £m	Capital reserve £m	Profit and loss account £m
At 1 January 2004	1,081	–	292	70
Proceeds from capital raising (note 18.2)	–	–	–	90
Increase in own shares held	–	(4)	–	–
Transfer of capital reserve	–	–	(290)	290
Movement in equity settled share scheme expenses (note 34.2)	–	–	–	2
Retained profit for the year ended 31 December 2004	–	–	–	38
Foreign exchange rate movements	–	–	–	(2)
At 31 December 2004	1,081	(4)	2	488

The own shares held reserve includes 7,836,224 shares owned by employee benefit trusts and constituted 0.3% of the Company's allotted share capital at 31 December 2004. The shares held in the reserve at 31 December 2004 were the maximum number held during the year. These shares had a nominal value of £4m and a market value of £5m. Of the shares held by the employee benefit trusts, 4,046,191 are under option to employees and 3,790,033 have been conditionally gifted to them.

The HHG PLC Employee Trust 2004, Henderson Share Incentive Plan and Henderson Employee Share Trust 2000 are used by the Group to operate the LTIP, SIP and DEP share-based payment schemes respectively. Shares are distributed to employees as and when they vest in line with the terms of each scheme under the administration of Computershare Trustees Limited, Towers Perrin Share Plan Services Limited and Ogier Trustees Limited Jersey who act as trustees respectively.

On 27 October 2004, £290m was transferred from the capital reserve to the profit and loss account following the liquidation of NPI Finances Limited, a subsidiary undertaking of the Company.

19.2 Company

	Share premium £m	Own shares held £m	Capital reserve £m	Profit and loss account £m
At 1 January 2004	1,081	–	290	89
Retained loss for the financial year	–	–	–	(141)
Proceeds from capital raising (note 18.2)	–	–	–	90
Transfer of capital reserve	–	–	(290)	290
Movement in equity settled share scheme expenses (note 34.2)	–	–	–	1
Increase in own shares held	–	(2)	–	–
At 31 December 2004	1,081	(2)	–	329

The own shares held reserve includes 4,046,191 shares owned by HHG PLC Employee Trust 2004 and constituted 0.1% of the Company's allotted share capital at 31 December 2004. The shares held in the reserve at 31 December 2004 were the maximum number held during the year. These shares had a nominal value of £2m and a market value of £2m. All of the shares are under option to employees. A further £2m of the Company profit and loss account reserve is non distributable reflecting the impact of own shares issued and purchased by the Group.

On 27 October 2004, £290m was transferred from the capital reserve to the profit and loss account following the liquidation of NPI Finances Limited, a subsidiary undertaking of the Company. The £290m is now considered distributable.

20. Reconciliation of movement in shareholders' funds

20.1 Group

	31 Dec 04 £m	31 Dec 03 £m
Shareholders' funds at 1 January	1,689	1,045
Total recognised gains/(losses) arising in the year	36	(850)
Dividend on non-equity shares	–	(1)
Redemption of £249m 'C' preference shares	–	(249)
Issue of £249m ordinary shares	–	249
Consideration for acquisition of Henderson Global Investors (Jersey) Limited and its subsidiaries from AMP	–	(28)
Issue of £27m preferred ordinary shares	–	27
Issue of £1,323m preferred ordinary shares	–	1,323
Application of capital reserve to repay preference shares	–	(17)
Issue of £65m ordinary 10 pence shares at a premium of £125m	–	190
Increase in own shares held (note 19.1)	(4)	–
Proceeds from capital raising (note 18.2)	115	–
Movements in equity settled scheme expenses (note 34.2)	2	–
Shareholders' funds at 31 December	1,838	1,689

On 30 June 2003, the Company issued 248,930,000 ordinary shares with a par value of £1 each for a total consideration of £249m. On the same day the Company redeemed the 'C' class redeemable preference shares with a par value of £1 each, for a total redemption value of £249m.

On 14 November 2003, the Company issued 27,657,688 preferred ordinary shares with a par value of £1 each for a consideration of £27m and on 21 November 2003, a further 1,323,046,626 preferred ordinary shares with a par value of £1 each for a consideration of £1,323m.

On 26 November 2003, as an integral step in the Demerger of the Group from AMP, the High Court of Justice confirmed that the 16,770,000 'A' redeemable preference shares of £1 were cancelled and extinguished and the resulting capital reduction reserve was utilised to repay an amount equal to the amount paid up on these 'A' preference shares plus any arrears of dividend thereon down to the effective date of the capital reduction.

On 23 December 2003, as part of an institutional capital raising, the Company issued 652,920,962 ordinary shares of 10 pence each for an aggregate consideration of £190m (net of expenses of £6m) with the balance of £125m being taken to share premium account.

Notes to the Accounts (continued)

20. Reconciliation of movement in shareholders' funds (continued)

20.2 Company

	31 Dec 04 £m	31 Dec 03 £m
Shareholders' funds at 1 January	1,706	1,528
Total recognised losses arising in the year	(141)	(1,359)
Dividend on non-equity shares	–	(1)
Redemption of £249m 'C' preference shares (note 20.1)	–	(249)
Issue of £249m ordinary shares (note 20.1)	–	249
Issue of £15m preferred ordinary shares	–	15
Issue of £27m preferred ordinary shares (note 20.1)	–	27
Issue of £1,323m preferred ordinary shares (note 20.1)	–	1,323
Application of capital reserve to repay preference shares (note 20.1)	–	(17)
Issue of £65m ordinary 10 pence shares at a premium of £125m (note 20.1)	–	190
Proceeds from capital raising (note 18.2)	115	–
Movements in equity settled scheme expenses (note 34.2)	1	–
Increase in own shares held (note 19.2)	(2)	–
Shareholders' funds at 31 December	1,679	1,706

On 30 June 2003, the Company issued 10 million ordinary shares with a par value of £1 each in exchange for AMP Financial Services Holdings Limited's minority interest in Pearl Group Limited, which was deemed to have a value of £15m. The balance of £5m was taken to the share premium account.

21. Fund for future appropriations

	31 Dec 04 £m	Restated 31 Dec 03 £m
At 1 January as previously reported	612	527
Prior year adjustment	–	(97)
At 1 January restated	612	430
Transfer (to)/from the technical account	(10)	182
At 31 December	602	612

22. Policyholder liabilities

Long-term business provision

Material judgement is required in calculating the long-term business provision. In particular, there is discretion over the choice of assumptions used. The long-term business provision is sensitive to changes in assumptions, with some having a greater effect than others. Changes in annuitant mortality, for example, can have a significant impact, as can the interest rates used.

The principal assumptions used to calculate the long-term business provision for the main classes of business, excluding linked business liabilities, are:

22.1 Interest rates

	Valuation interest rates			
	With-profits		Non-profit	
	31 Dec 04 %	31 Dec 03 %	31 Dec 04 %	31 Dec 03 %
Basic life assurance	3.0 – 4.5	3.7 – 4.4	3.2 – 4.5	2.5 – 4.1
Pension business	3.0 – 5.03	3.3 – 5.45	3.9 – 4.7	3.3 – 5.0
Pension annuity in payment	4.15	4.7	4.24 – 5.0	4.75 – 4.9
General annuities	4.5	4.7	3.25 – 4.75	4.1 – 5.1
Unitised with-profits (life)	2.9 – 4.5	3.0 – 4.26	N/a	N/a
Unitised with-profits (pension)	3.6 – 5.03	3.9 – 5.45	N/a	N/a
Private Health Insurance (PHI)	N/a	N/a	3.25 – 4.82	2.3 – 3.3

Valuation interest rate assumptions are set with regard to actual yields on the supporting assets. These yields are adjusted downwards to allow for credit risk, investment expenses, tax and reinvestment of future income. A further margin for risk is then deducted for all asset classes.

22.2 Mortality rates

	31 Dec 04	31 Dec 03
Basic life assurance	85% AM/F80 Ult, 100% A67/70 Ult, 65%-100% AM/F92 and 70% ELT 14 (M) all with adjustments	100% AM 80 Ult, 80%-100% A67/70 Ult, 100% AM/F92 and 80% ELT 14 (M) all with adjustments
Pension business	65% AM/F80 Ult, 100% A67/70 Ult, 70% AM/F92 and 100% PM/FA92MC (2025) all with adjustments	100% A67/70 Ult, 100% AM/F92 and 70%-100% IM/F80 all with adjustments
Pension annuity in payment	72% IML/IFL92, 78%-95% RMV/RFV92 Year of use and 100% PM/FA92MC (2025) all with adjustments	70%-72% IM/F80 C2014/16, 72% IML/IFL 92 and 78%-88% RMV/RFV92 Year of use all with adjustments
Unitised with-profits	65%-89% AM/F80 Ult, 100% A67/70 Ult, 95%-100% AM/F92 and 100% PM/FA92MC (2025) all with adjustments	60%-100% A67/70 Ult and 95%-100% AM/F92 all with adjustments
Private Health Insurance	100% CMIR 12 with adjustments	100% CMIR 12 with adjustments

The abbreviations above represent standard industry mortality tables as published by the Continuous Mortality Investigation (CMI) Bureau of the Institute of Actuaries. Adjustments are made by the Group to the standard tables to reflect the experience of the relevant company relative to the industry standard.

22.3 Persistency

Recent experience is used to form a view of future persistency. A prudent margin for adverse deviation is added to arrive at prudent persistency rates.

22.4 Methodology

In 2004, conventional non-profit liabilities and conventional with-profits liabilities were valued using a gross premium method allowing for a prudent level of discontinuances. In 2003, certain conventional with-profits liabilities were valued using a net premium method. The changes in methodology reflect the changes made to the prudential rules. Overall, the change has not had a significant effect as the benefit of using a gross premium valuation method and allowing for a prudent level of discontinuances has been offset by a reduction in the valuation rate of interest for certain classes of business.

The long-term business provision for linked liabilities is calculated using a gross premium cash flow method.

22.5 Provision for bonuses

The provision includes £37m (2003: £180m) in respect of bonuses added following the valuation at the end of each year.

The total bonuses attributable to the year are as follows:

	31 Dec 04 £m	31 Dec 03 £m
Provided declared bonuses, included in the movement in the long-term business provision	37	180
Interim and terminal bonuses, included in claims paid	104	81
	141	261

22.6 Review of mortgage endowments

The FSA carried out a review of mortgage endowments in 1999. As a result, all mortgage endowment policyholders were provided with information on the performance of their policy. These accounts include provision for the estimated costs of investigating and settling complaints associated with mortgage endowments and for the estimated cost of meeting promises given to specific policyholders. The total amount provided for at 31 December 2004 was £211m (2003: £231m).

22.7 Guaranteed annuity options

The provisions held in respect of guaranteed annuity options are a prudent assessment of the additional liabilities incurred in respect of options on a basis and method consistent with that used to value basic policy liabilities, and include a prudent assessment of the proportion of policyholders who will choose to exercise options. The total amount provided for at 31 December 2004 was £652m (2003: £525m).

22.8 Pension transfers and opt outs

Group companies have set up provisions for the review and possible redress relating to personal pension policies. These provisions, which have been calculated using data derived both from detailed file reviews of specific cases and from a statistical review of other outstanding cases, are included in the long-term business provision. The provision for possible redress included in the long-term business provision for Phase 1 cases is £521m (2003: £344m) and for Phase 2 cases is £10m (2003: £12m). Included in the long-term business provision are provisions for additional costs associated with the misselling of pensions policies of £16m (2003: £18m).

22.9 Other specific matters

The FSA raises matters from time to time that impact the Group and many others in the industry. These accounts reflect those that the Group considers require provisioning based on current regulatory requirements.

Notes to the Accounts (continued)
22. Policyholder liabilities (continued)

22.10 Operating exceptional charge

	31 Dec 04 £m	31 Dec 03 £m
Operating exceptional charges included in change in long-term business provision	–	242

The change in long-term business provision for the 2003 financial year included the following exceptional charges:

- (a) increases in technical provisions in NPLL due to the changes in equity backing ratios and other actuarial assumption changes arising from the decision to close all Life Services' life companies to new business, which have led to the impairment of the contingent loans made by Pearl (note 31). The shareholders' share of the write-downs was £171m; and
- (b) increases in technical provisions of £71m in Pearl resulting from the changes referred to in (a) above.

Other operating exceptional charges of £242m in 2003 have been grossed up by £28m, being the longer term effective tax rate attributable to the balance on the long-term business technical account for the purpose of the Reconciliation of Group Operating Profit to Profit/(Loss) on Ordinary Activities Before Taxation and segmental information in note 3.

23. Deferred taxation

23.1 Provisions for taxation

Reconciliation of movements in deferred tax:

	31 Dec 04 £m	31 Dec 03 £m
At 1 January	11	(9)
Charge/(release) for the year:		
Technical account – long-term business	26	17
Non-technical account	(1)	3
At 31 December	36	11

23.2 Deferred taxation provisions

The components of the net deferred tax liability are as follows:

	31 Dec 04 £m	31 Dec 03 £m
Unrealised gains in investments	60	42
Deferred acquisition costs	(27)	(40)
Capital allowances	5	9
Total undiscounted	38	11
Total on a discounted basis	36	11

A deferred tax asset has been recognised in respect of long-term business acquisition expenses where relief is deferred under corporation tax legislation. It has been determined that taxable income of future periods will be sufficient to enable relief for these expenses as they fall due to be deductible. Due to the uncertainty of the quantum, source and timing of future taxable profits or chargeable gains, no provision has been made for the assets listed in note 23.3.

23.3 Factors that may affect future taxation charges

The deferred taxation assets, which have not been recognised due to the uncertainty of their recoverability in the foreseeable future, comprise:

	Long-term business		Non long-term business	
	31 Dec 04 £m	31 Dec 03 £m	31 Dec 04 £m	31 Dec 03 £m
Provisions and other timing differences	4	6	29	46
Capital and trading losses	141	177	49	32
	145	183	78	78

The unrecognised assets have not been discounted. Further analysis is as follows:

- £40m (2003: £44m) arises on realised capital losses on chargeable securities and will be available to offset against realised chargeable gains of future years;
- £150m (2003: £165m) in respect of trading losses arising from ongoing activities will be available to offset against taxable profits for future years;
- £5m (2003: £10m) arises from three year funded general insurance business and will be available to offset against the Group's taxable profits in future periods when claims are paid; and
- £28m (2003: £34m) in respect of provisions and other timing differences will be available to offset against taxable profits in future periods when the timing differences reverse or provisions are utilised.

24. Claims outstanding

24.1 Claims outstanding

	31 Dec 04 £m	31 Dec 03 £m
General business (note 24.2)	229	301
Life business (note 24.3)	92	128
	321	429

24.2 General business

	Gross £m	Reinsurance £m	Net £m
2004			
Notified outstandings	49	39	10
Incurred but not reported	178	160	18
	227	199	28
Claims handling expenses	2	–	2
	229	199	30
2003			
Notified outstandings	84	64	20
Incurred but not reported	212	180	32
	296	244	52
Claims handling expenses	5	–	5
	301	244	57

The technical provisions for future claims payments have primarily been assessed using chain ladder methods. Where there is a notable exposure to long-term asbestos, pollution and health hazard liabilities, external independent actuaries provide best estimate benchmarks. An appropriate prudential margin is applied to all lines of business, as it is recognised that the estimation of certain future claims payments is an inherently uncertain exercise and future experience could be adverse.

In calculating the technical provisions in respect of certain long-term marine, aviation and reinsurance business, the future investment income on the assets held to cover the related provisions has been taken into account by discounting future cash flows. The average period before the liability will be settled has been estimated at 6.7 years for 2004 (2003: 10.8 years). The provision has been discounted at an interest rate of 3.5% for 2004 (2003: 4.00%).

The overall effect is to reduce the net technical provisions for those classes of business referred to above at 31 December 2004 by £4m from £17m to £13m (2003: by £14m from £50m to £36m). The total amount of the investment return which corresponds to the unwinding of the discount is £1m (2003: £1m).

The overall effect is to reduce the gross technical provisions for those classes of business referred to above at 31 December 2004 by £5m from £21m to £16m (2003: by £18m from £66m to £48m). The total amount of the investment return which corresponds to the unwinding of the discount is £1m (2003: £2m).

24.3 Life business

	Gross and net	
	31 Dec 04 £m	31 Dec 03 £m
At 1 January	128	86
(Decrease)/increase in the year	(36)	42
At 31 December	92	128

25. Creditors: amounts falling due within one year

	31 Dec 04 £m	31 Dec 03 £m
Company		
Loans due to Group undertakings (note 27.2)	126	138
Amount owed to Group undertakings	1,711	1,058
Other creditors	–	4
Accruals and deferred income	9	6
Corporation tax	3	–
	1,849	1,206

26. Creditors: amounts falling due after more than one year

	31 Dec 04 £m	31 Dec 03 £m
Company		
Loans due to Group undertakings (note 27.2)	47	337

27. Debenture loans and amounts owed to credit institutions**27.1 Debenture loans and amounts owed to credit institutions**

	31 Dec 04 £m	31 Dec 03 £m
Group		
Floating rate guaranteed unsecured loan notes due 2004 and 2006	–	2
Debenture loans, external	–	2
Subordinated guaranteed bonds undated (note a) ¹	130	130
Limited recourse bonds 2012 7.39% (note b) ¹	101	108
Limited recourse bonds 2022 7.59% (note b) ¹	117	117
Total debenture loans	348	357
Refinancing loan (note c) ¹	296	257
Total amounts owed to credit institutions	296	257
Total borrowings	644	614

Notes

1. Borrowings of NPLL long-term fund.

- (a) A £100m 9.625% subordinated guaranteed bond and a £30m 9.6257% subordinated guaranteed bond were both issued at par in 1996 by a wholly owned subsidiary of NPI. On 1 January 2000, NPI demutualised and these bonds, along with the net proceeds of their issue, were transferred to NPLL. The bonds are repayable on a non-installment basis, on 30 June 2006 and each fifth anniversary thereafter, so long as the bonds are outstanding.
- (b) Prior to its acquisition by the Group, NPI raised £260m of capital through the securitisation of embedded value on a block of existing unit-linked and unitised with-profit life and pension policies in 1998. On demutualisation of NPI, these were transferred to NPLL. The bonds are split between two classes, which rank pari passu. The £140m 7.39169% class A1 limited recourse bonds have an average life of eight years maturing in 2012 and the £120m 7.5873% limited recourse bonds have an average life of 18 years maturing in 2022. Amounts relating to the securitisation included within loans represent the principal outstanding less unamortised deferred issued costs. The bonds are repaid out of margins emerging from the securitised block of business and from a collateral fund of £128m (2003: £113m).
- (c) The refinancing loan from Abbey National plc relates to the sale of Extra-Income Plan policies that Abbey National plc finances to the value of the associated property reversions. As part of the arrangement, NPLL and NPIL have undertaken to indemnify Abbey National plc against profits or losses arising from mortality or surrender experience which differs from the basis used to calculate the reversion amount. Repayment will be on a policy-by-policy basis and is expected to occur over the next 10 to 20 years.

27.2 Time period for payment

Payable as follows:

	31 Dec 04 £m	31 Dec 03 £m
Group		
In one year or less, or on demand	9	1
Between one and two years	141	–
Between two and five years	39	131
In five years or more	455	482
	644	614
Company		
In one year or less, or on demand	126	138
Between one and two years	–	290
In five years or more	47	47
	173	475

27.3 Nature of borrowings

After taking account of the various interest rate and currency rate swaps entered into by the Group, the currency exposure of Group borrowings is all in sterling and the interest rate exposure is as follows:

	31 Dec 04 £m	31 Dec 03 £m
Fixed rate borrowings	348	355
Floating rate borrowings	–	2
Interest free borrowings	296	257
Total borrowings	644	614

28. Provisions

28.1 Group

	Restructure £m	Leasehold properties £m	Product misselling £m	Staff related £m	Other £m	Total £m
At 1 January 2004	57	96	14	34	42	243
Amounts utilised	(36)	(23)	(9)	(8)	(34)	(110)
Increase in provision	18	–	44	5	39	106
Unutilised amount reversed	(5)	(5)	–	–	(12)	(22)
At 31 December 2004	34	68	49	31	35	217

The restructure provision of £34m (2003: £57m) has been made for costs of restructuring management and staffing across the Group and to complete the closure of Towry Law International. It is expected that most of the expenditure will be incurred in 2005.

The leasehold properties provision has been made for amounts in respect of the excess of lease rentals and other payments on properties that are currently vacant or expected to become vacant over the amounts to be recovered from subletting these properties on a discounted basis at 4.1% (2003: 4.1%). The provision is expected to be utilised over the next 15 years.

Product misselling provisions include a £43m provision relating to possible claims arising from inappropriate advice given to certain Towry Law International customers. The matters relating to these provisions are expected to be settled within the next five years.

Staff related provisions include £17m (2003: £18m) held in respect of healthcare costs for former employees and £3m (2003: £9m) relating to long-term staff incentives.

Other provisions include £20m (2003: £11m) for obligations relating to various sale contracts which are expected to be utilised within the next three years.

Notes to the Accounts (continued)
28. Provisions (continued)

28.2 Company

	Restructure £m	Product misselling £m	Other £m	Total £m
At 1 January 2004	–	–	–	–
Amounts utilised	(1)	–	(9)	(10)
Increase in provision	3	35	23	61
Unutilised amount reversed	–	–	(12)	(12)
At 31 December 2004	2	35	2	39

The restructure provision relates to the restructure of the Corporate Office (note 2.2).

The product misselling provision has been established for possible claims arising from inappropriate advice given to certain Towry Law International customers. The matters relating to this provision are expected to be settled within the next five years. To the extent that further capital needs to be provided to Towry Law International to enable settlement of legacy product issues, this will be funded by the Company.

The increase in other provisions in the year comprises the cost of settling certain intra-Group matters relating to investments made by the asset management business, the settlement of Group-wide issues with AMP and settlements relating to the Demerger of the Group from AMP.

29. Other creditors including taxation and social security

	31 Dec 04 £m	31 Dec 03 £m
Group		
Corporation tax	64	77
Obligations under finance leases (note 30.2)	–	1
Other creditors	340	456
	404	534

30. Capital commitments

30.1 Capital commitments

	31 Dec 04 £m	31 Dec 03 £m
Other capital commitments for settlement after 31 December	4	32
Securities commitments	239	345

Securities commitments comprise commitments of Pearl to subscribe to private equity funds.

30.2 Obligations under finance leases

The obligations under finance leases fall due:

	31 Dec 04 £m	31 Dec 03 £m
In the second to fifth years inclusive	–	1

30.3 Annual commitments under non-cancellable land and building operating leases

The obligations under non-cancellable land and building operating leases fall due:

	31 Dec 04 £m	Restated 31 Dec 03 £m
Within one year	4	–
In the second to fifth years inclusive	1	5
In more than five years	16	20
Total	21	25

The comparatives for obligations under non-cancellable land and building operating leases have been restated following a reanalysis of capital commitments at 31 December 2003.

31. Contingent loans

Both NPLL and London Life have received contingent loans from their respective parent undertakings, NP Life Holdings Limited and London Life Holdings Limited. The assets backing the loans are utilised to provide additional regulatory capital for the long-term funds. A full impairment review of the value of the loans made to the policyholder funds of London Life and NPLL was carried out as at 31 December 2004. The amounts below represent the best estimate of the Directors of the amounts that will be recoverable from the long-term funds following the settlement of policyholder claims by those funds and were valued at a market consistent embedded value (MCEV). MCEV allows explicitly for the cost of market-related risk, by reference to the pricing of similar risks observed in the financial markets. The most important of these are risks associated with the provision of policyholder financial guarantees and options and the risks associated with mismatches between assets and liabilities and revenues and expenses.

The intra-Group contingent loans cancel on consolidation. However, since they are loans between shareholder and policyholder funds any impairment in the shareholder asset, recognising non-recoverability, will reduce Group profit.

The Group long-term business provision is adjusted for the difference arising on consolidation between the carrying value of the contingent loan liability in the relevant life companies (which is in part determined by the approach to setting the long-term business provision in those companies, as disclosed in note 22) and the valuation of the contingent loans by the shareholder on the basis described above.

The loans provided to NPLL are repayable in accordance with the Schedule 2c Scheme under which the business of NPI was transferred to NPLL. The loan to London Life is repayable in accordance with the Schedule 2c Scheme under which the business of AMP UK Branch was transferred to London Life. The balances at 31 December are as follows:

	31 Dec 04 £m	31 Dec 03 £m
NP Life Holdings Limited	260	303
London Life Holdings Limited	76	85
	336	388

32. Notes to the cash flow statement

32.1 Reconciliation of profit/(loss) on ordinary activities to net cash inflow/(outflow) from operating activities:

	31 Dec 04 £m	31 Dec 03 £m
Profit/(loss) on ordinary activities before non-operating exceptional items and taxation	81	(867)
Adjustments for financing expenses and items not involving movements of cash:		
Depreciation of tangible fixed assets	13	9
Amortisation and impairment of goodwill (note 12)	20	307
Amortisation and write-off of deferred issue costs	–	11
Decrease in creditors arising out of direct insurance operations	–	(10)
Decrease in technical provisions	(30)	(7)
Decrease in present value of acquired in force business	–	23
Unrealised losses on investments	66	379
(Profit)/loss from interest in associates	(1)	7
Movement in other assets	29	(355)
Movement in other liabilities	(50)	96
Profits relating to long-term business funds, excluding Pacific fund	(88)	(19)
Loan interest expense	1	64
Cash outflow from termination of Towry Law International (note 9)	(6)	–
Cash outflow from proposed sale of Life Services businesses (note 9)	(3)	–
Net cash inflow/(outflow) from operating activities	32	(362)

32.2 Analysis of cash flows in respect of acquisitions and disposals

	31 Dec 04 £m	31 Dec 03 £m
Cash proceeds received on disposal of associate, including loans sold	50	1
Cash proceeds received on disposal of subsidiary undertakings	–	14
Costs associated with disposal of subsidiary undertakings	–	(12)
Net cash inflow from acquisitions and disposals	50	3

Notes to the Accounts (continued)
32. Notes to the cash flow statement (continued)

32.3 Analysis of cash holdings included in the Consolidated Balance Sheet

	31 Dec 04 £m	31 Dec 03 £m
Cash at bank and in hand	330	395
Less: Cash on deposit not repayable on demand	(21)	(191)
Add: Deposits with credit institutions repayable on demand included within other financial investments	45	26
Total cash holdings (note 32.6)	354	230

32.4 Analysis of portfolio investments included in the Consolidated Balance Sheet

	31 Dec 04 £m	31 Dec 03 £m
Other financial investments	22,279	21,506
Add: Cash on deposit not repayable on demand (note 32.3)	21	191
Less: Deposits with credit institutions repayable on demand included within other financial investments (note 32.3)	(45)	(26)
Total portfolio investments (note 32.6)	22,255	21,671

32.5 Net portfolio investments (excluding long-term business)

	31 Dec 04 £m	31 Dec 03 £m
Purchase of portfolio investments	480	664
Sale of portfolio investments	(297)	(583)
	183	81

32.6 Movements in cash, portfolio investments and financing

	At 01 Jan £m	Cash flow £m	Changes in long-term business £m	Changes in market value and exchange rate effects £m	Non-cash movements £m	At 31 Dec £m
2004						
Portfolio investments	21,671	183	467	(66)	–	22,255
Cash holdings	230	6	118	–	–	354
	21,901	189	585	(66)	–	22,609
Borrowings	(614)	2	(32)	–	–	(644)
Total	21,287	191	553	(66)	–	21,965
2003						
Portfolio investments	23,072	81	(1,103)	(379)	–	21,671
Cash holdings	201	(99)	128	–	–	230
	23,273	(18)	(975)	(379)	–	21,901
Borrowings	(1,776)	59	74	–	1,029	(614)
Total	21,497	41	(901)	(379)	1,029	21,287

33. Staff pension schemes

The Group has continued to account for pensions in accordance with SSAP 24 and the disclosures given under the SSAP 24 disclosures below are those required by that Standard. FRS 17 "Retirement benefits" was issued in November 2000 requiring phased transitional disclosures. These are set out under FRS 17 disclosures below to the extent not already provided under SSAP 24 disclosures.

33.1 SSAP 24 disclosures

As at 31 December 2004 the Group operated one pension scheme, the HHG Staff Pension Scheme (formerly AMP UK Staff Pension Scheme) (the Scheme), for its employees. The Scheme is funded by payment of contributions to a separately administered trust fund. The Scheme's appointed investment managers are Henderson Global Investors, Fidelity Investments and Standard Life. The Scheme is subject to regular valuations by an independent qualified actuary.

Up until 15 November 1999, the Scheme operated on a defined benefit basis for all members. From that date, a new money purchase section was established for new members of the Scheme. Pearl and London Life final salary members were offered membership of this new section, on special terms, in respect of future service in April 2000 and NPI and Henderson final salary members in June 2001. If they declined they remained members of the defined benefit scheme.

At the date of the last actuarial investigation (31 December 2003) the market value of the assets of the Scheme was £1.705bn and on the basis of the assumptions set out below this was sufficient to cover 101% of the value of the benefits which had accrued to members after allowing for future increases in pensionable remuneration. Following a suspension of contributions, employer contributions to the Scheme recommenced with effect from 1 January 2004 at an average rate of 19.9% of pensionable earnings. From 1 January 2005, this rate will be replaced by contributions of 27.0%, 20.8% and 13.8% of pensionable earnings for final salary section members, hybrid (a mix of final salary and money purchase) members and pure money purchase members respectively. Contributions are paid annually at the end of the year.

With effect from 31 March 2005, the trustees have agreed to split the pension scheme assets and liabilities between those relating to the Life Services business and the group remaining after the sale of the Life Services business (the Remaining Group). This was done on the basis of a valuation as at the date of agreement to sell the Life Services business which revealed that the market value of the assets of the Scheme at that date was sufficient to cover 103% of the value of the benefits accrued to members.

The principal assumptions used for the purpose of assessing pensions costs before retirement under SSAP 24 for the Scheme were that the annual return on investments, after allowing for investment expenses, would be 2.5% higher than the annual increase in members' pensionable remuneration before retirement and 2.6% higher than the expected annual increase in future pensions after retirement. The costs were assessed using the projected unit method.

The 2004 pension cost is £15m which comprises £8m in relation to defined benefit members and £7m in relation to money purchase members (2003: £2m (see note 2.5)). A £3m prepayment is carried in the balance sheet at 31 December 2004 (2003: £nil) reflecting contributions prepaid at that date.

33.2 FRS 17 disclosures

The valuation used for the 2004 FRS 17 disclosures has been based on the most recent actuarial valuation at 31 December 2003 updated by Watson Wyatt to take account of the requirements of FRS 17 in order to assess the liabilities of the Scheme at 31 December 2004. The 2003 FRS 17 disclosures were based on the actuarial valuation at 31 December 2001 updated by Watson Wyatt to take account of the requirements of FRS 17. The Scheme assets are stated at their market value at 31 December 2004 and 31 December 2003.

- (i) The effect on the Group's net assets and retained profits substituting the relevant FRS 17 pensions assets and liabilities for the corresponding SSAP 24 balance sheet items would be as follows:

	31 Dec 04 £m	31 Dec 03 £m
Net assets		
Total net assets excluding pension liability	1,835	1,689
Pension liability	(46)	(48)
Total net assets including pension liability	1,789	1,641
Reserves		
Profit and loss reserve excluding pension liability	485	70
Pension liability	(46)	(48)
Profit and loss reserve including pension liability	439	22

Total net assets excluding pension liability includes a £17m (2003: £18m) provision held in respect of healthcare costs for former employees. This provision has been calculated on the assumption of medical expense inflation of 9.5% (2003: 10.25%) and a valuation interest rate of 4.5% (2003: 4.5%).

- (ii) The financial assumptions used to calculate Scheme liabilities under FRS 17 are:

	31 Dec 04 Projected unit	31 Dec 03 Projected unit	31 Dec 02 Projected unit
Valuation method			
Discount rate	5.30%	5.50%	5.70%
Inflation rate	2.80%	2.80%	2.00%
Rate of increase in pensionable salaries (aged related scale in addition)	4.30%	4.30%	3.50%
Rate of increase in pensions in payment (in excess of GMPs)	2.80%	2.80%	2.00%
Rate of increase in deferred pensions	2.80%	2.80%	2.00%

Notes to the Accounts (continued)
33. Staff pension schemes (continued)

(iii) The assets in the Scheme and the expected rate of return are:

	Long-term rate of return expected at			Value		
	31 Dec 04 %	31 Dec 03 %	31 Dec 02 %	31 Dec 04 £m	31 Dec 03 £m	31 Dec 02 £m
Equities	8.2	8.5	7.9	842	975	1,061
Property	6.9	7.1	6.6	172	136	150
Bonds	4.7	4.9	5.0	734	541	298
Cash and other	3.6	3.8	3.5	37	24	21
Total market value of defined benefit assets	6.5	7.2	7.1	1,785	1,676	1,530
Money purchase assets				37	28	20
Total value of assets				1,822	1,704	1,550
Present value of Scheme liabilities				(1,888)	(1,773)	(1,558)
Deficit in the Scheme				(66)	(69)	(8)
Related deferred tax asset				20	21	2
Net pension liability				(46)	(48)	(6)

(iv) The components of the pensions cost are:

	31 Dec 04 £m	31 Dec 03 £m
Analysis of the amount charged to operating profit:		
Current service cost – final salary	14	18
Current service cost – money purchase	7	8
Past service cost	–	1
Total operating charge	21	27

	31 Dec 04 £m	31 Dec 03 £m
Analysis of the amount charged to the profit and loss account:		
Loss on settlements	–	1
Gain on curtailments	(5)	(37)
Net gain to profit and loss account	(5)	(36)

The gain on curtailments in 2003 relates to the restructuring of Life Services in that year.

	31 Dec 04 £m	31 Dec 03 £m
Analysis of the amount charged to other finance income:		
Interest cost	93	84
Expected return on pension scheme assets	(117)	(106)
Net return	(24)	(22)
Total operating credit	(8)	(31)

Analysis of the amount recognised in the Statement of Total Recognised Gains and Losses (STRGL):

	31 Dec 04 £m	31 Dec 03 £m
Actual gain less expected return on pension Scheme assets	(54)	(140)
Experience losses arising on Scheme liabilities	18	5
Changes in assumptions underlying the present value of the Scheme liabilities	61	229
Actuarial loss recognised in the STRGL	25	94

(v) The movement in the Scheme deficit during the year is as follows:

	31 Dec 04 £m	31 Dec 03 £m
Deficit in Scheme at 1 January	(69)	(8)
Movement during the year:		
Contributions paid	13	2
Total operating charge	(14)	(27)
Settlement cost	–	(1)
Curtailment gain	5	37
Net expected return on pension asset	24	22
Actuarial loss	(25)	(94)
Deficit in Scheme at 31 December	(66)	(69)

(vi) Scheme experience gains and losses are as follows:

	31 Dec 04	31 Dec 03	31 Dec 02
(Gain)/loss on Scheme assets			
Amount (£m)	(54)	(140)	377
Percentage of present value of Scheme assets	(3.0%)	(8.4%)	24.6%
Experience losses on Scheme liabilities			
Amount (£m)	18	5	14
Percentage of present value of Scheme liabilities	1.0%	0.3%	0.9%
Total loss recognised in Statement of Total Recognised Gains and Losses			
Amount (£m)	25	94	338
Percentage of present value of Scheme liabilities	1.4%	5.4%	22.0%

34. Share-based payments

34.1 Group share-based compensation plans

The following share-based compensation plans were launched by the Group in 2004:

Sharesave Scheme

Eligible employees who wish to purchase shares in HHG PLC contribute a monthly amount to a savings account up to a maximum of £250 after tax per month. At the expiration of 36 months contribution, the employees have the option to use the funds in the account (plus interest and bonus) to subscribe for shares at a previously agreed price. The price was set at £0.416 per share, a 20% discount to the share price on 2 April 2004.

Employees have up to six months after the 36 month period to exercise their options and subscribe for shares.

Share Incentive Plan (SIP)

Eligible employees who wish to purchase shares in HHG PLC invest a monthly amount up to a maximum of £125 per month, which is deducted from their gross salary. Each participating employee received for no additional payment one share for each share purchased through to December 2004. From January 2005, the matching share ratio increased from 1:1 to 2:1. Matching shares will be forfeited if purchased shares are withdrawn from the Trust within two years.

Long-Term Incentive Plan (LTIP)

Under the LTIP, a number of executives were granted performance shares.

These awards of £nil priced options are granted on condition that the executives remain with the Company for three years and that the Total Shareholder Return (TSR) of the Company (HHG TSR) shares compares favourably to the median of companies that make up the FTSE 250 index as at 1 January 2004. A proportion of the shares will vest if the HHG TSR is at the 50th percentile of the FTSE 250 companies with the full amount of shares granted vesting if HHG TSR is at or above the 75th percentile of the FTSE 250 companies. No vesting will occur if the HHG TSR is below the 50th percentile of the FTSE 250 companies. The executives are not entitled to vote or receive dividends in respect of these awards until the vesting conditions are met.

100% of awards granted to Life Services employees will become exercisable on completion of the sale of the Life Services business, subject to performance hurdles being met, whereas two thirds of the awards granted to the remaining Henderson and Towry Law employees will vest on the Court approval date for the return of capital, subject to the extent performance hurdles have been met on completion of the sale of the Life Services business. The remaining one third of the 2004 awards held by Henderson and Towry Law employees will be subject to the normal three year performance period and the satisfaction of the TSR performance conditions over that period. On exercise, awards will be satisfied by the transfer to participants of shares purchased on market by the LTIP trustee.

A phantom LTIP scheme has been set up for non-UK resident executives, which is the same in all respects except that it will be settled in cash.

Notes to the Accounts (continued)

34. Share-based payments (continued)

Deferred Equity Plan (DEP)

Under the Henderson remuneration policy, there is a requirement for some executives to defer an element of their Short-Term Incentive (STI) awards, Growth Equity Bonus Scheme (GEBS) and performance fees. A mandatory deferral applies above certain levels of award and is administered via the DEP. Under DEP, executives can defer their awards into the Company's shares and/or Henderson products. The deferred monies are paid directly to a trustee, who purchases the nominated investments and holds them in trust. Under the two year DEP (which applies to STI and performance fee deferrals), 50% of the investment units/shares are released to employees at the end of the first year, the other 50% at the end of year two.

In March 2004, a number of executives were given the opportunity to invest an amount equivalent to their 2003 annual cash bonus into the Company's shares at the market price. Each participating executive will receive for no additional payment one share for every three shares held in the plan for a minimum of three years.

34.2 Share-based payments through the profit and loss account

	31 Dec 04 £m
Sharesave Scheme	1
SIP	–
LTIP	1
DEP	–
Total expense	2

This total expense can be analysed between:

	31 Dec 04 £m
Amount which is expected to be settled with equity	2
Amount which is expected to be settled in cash	–
	2

Amounts recorded as liabilities for option grants expected to be settled in cash, based on the fair value of the options granted, totalled £nil at 31 December 2004. The intrinsic value of liabilities for which the counterparty's right to cash had vested by 31 December 2004 was £nil.

£1m of the above amount which is expected to be settled with equity, arose in the Company.

34.3 Share options outstanding

Share options outstanding under the Group's share-based compensation plans during 2004 were as follows:

	2004	Weighted average exercise price £
	Number of options	
At 1 January	–	–
Granted	11,518,112	0.416
Exercised (note 18.2)	(55,517)	0.416
Expired, cancelled or lapsed	(962,090)	0.416
At 31 December	10,500,505	0.416

The weighted average share price on the date options were exercised during 2004 was £0.53.

The weighted average fair value of options granted during 2004 was £0.20.

At 31 December 2004, the weighted average remaining expected life and remaining contractual life of outstanding awards was 2.4 years.

These disclosures are applicable only to the Sharesave Scheme.

34.4 Fair values of share-based compensation plans

The fair value amounts for the options granted under the Sharesave Scheme were determined using the Black Scholes option-pricing method using the following assumptions:

Dividend yield	Zero
Expected volatility	47.4%
Risk free interest rate	4.6%
Expected life	3 years
Weighted average share price	£0.475
Exercise price	£0.416

The Company listed in December 2003 and does not have a sufficient history of price movements for its own volatility calculation to be made. Therefore volatility has been calculated by taking the average of the volatility of nine of the Company's quoted peers over the preceding three year period. Peers selected were publicly quoted life insurance and fund management companies who were considered to offer suitable coverage in terms of business mix to be a reasonable proxy for volatility for the Company at the time that the options were granted.

Fair value of the Sharesave Scheme was adjusted for dividends. No other factors were taken into account in calculating the fair value of the Sharesave Scheme.

Other share schemes involve the grant of shares for £nil consideration. The fair value for these schemes is calculated using the share price at grant date, which is set out in the following table. No adjustments have been made for dividends.

Scheme	Shares granted	Average share price
SIP	297,647	£0.47
LTIP	19,708,570	£0.52
DEP	1,948,535	£0.44

The fair value calculation for the LTIP includes a statistical assessment of the likelihood of the Company achieving performance targets set out in the Scheme. These performance targets are in respect of TSR over three years and are as follows:

Criteria	Amount vesting
HHG TSR less than the 50th percentile of the FTSE 250 companies	nil%
HHG TSR at the 50th percentile of the FTSE 250 companies	35%
HHG TSR at or above the 75th percentile of the FTSE 250 companies	100%

For a TSR between the 50th and 75th percentiles the amount vesting will increase on a linear basis.

No goods or services have been received in respect of share-based payments other than the employee transactions identified above.

35. Subsidiary and associated undertakings

The principal subsidiaries and associated undertakings of the Group are as follows:

	Country of incorporation and principal place of operation	Class of shares held (wholly-owned unless otherwise indicated)
(a) Insurance companies:		
London Life Limited	UK ‡ *	Ordinary shares of £1
London Life Linked Assurances Limited	UK ‡ *	Ordinary shares of £1
National Provident Life Limited	UK ‡ *	Ordinary shares of £1
NPI Limited	UK ‡ *	Ordinary shares of £1
Pearl Assurance plc	UK ‡ *	'A' ordinary shares of 5 pence 'B' ordinary shares of £1
Pearl Assurance (Unit Funds) Limited	UK ‡ *	Ordinary shares of £1
Pearl Assurance (Unit Linked Pensions) Limited	UK ‡ *	Ordinary shares of £1
(b) Non-insurance companies:		
All held by the Company unless indicated		
Henderson Global Investors (Holdings) plc (holding company)	UK	Ordinary shares of 25 pence
HHG Capital (Jersey) Limited (special purpose entity)	Jersey	Ordinary shares of £1
HHG International Holdings Limited UK (holding company)	UK	Ordinary shares of £1
HHG Invest plc (holding company)	UK	Ordinary shares of £1
NPI Asset Management Limited (investment management company)	UK	Ordinary shares of £1
NPI Investment Managers Limited (unit trust company)	UK	Ordinary shares of £1
NPI Portfolio Managers Limited (unit trust company)	UK	Ordinary shares of £1
Pearl Group Limited (holding company)	UK	'A' ordinary shares of 5 pence

Notes

‡ Held by a subsidiary undertaking.

* Life Services business to be disposed of under agreement with Life Company Investor Group Limited (note 38).

Notes to the Accounts (continued)
35. Subsidiary and associated undertakings (continued)

	Country of incorporation and principal place of operation	Class of shares held (wholly-owned unless otherwise indicated)
UKLS Financial Planning Limited (holding company)	UK	Ordinary shares of £1
Henderson Administration Limited (service company)	UK ‡	Ordinary shares of £1
Henderson Fund Management plc (investment management)	UK ‡	Ordinary shares of £1
Henderson Global Investors (International Holdings) BV (holding company)	Netherlands ‡	Ordinary shares of 45 cents (€)
Henderson Global Investors (Jersey) Limited (holding company)	Jersey ‡	Ordinary shares of £1
		'A' and 'B' ordinary shares of £1
		Fixed rate preference shares of £1
Henderson Global Investors Limited (investment management)	UK ‡	Ordinary shares of £1
Henderson Holdings Limited (holding company)	UK ‡	Ordinary shares of 25 pence
		Participating preference shares of £1
Henderson International Holdings Limited (holding company)	UK ‡	Ordinary shares of £1
Henderson Investment Funds Limited (unit trusts/OEIC management)	UK ‡	Ordinary shares of £1
Henderson Investment Management Limited (investment management)	UK ‡	Ordinary shares of £1
Henderson Management SA (fund management)	Luxembourg ‡	Ordinary shares of US\$1
Henderson Private Capital Limited (investment management)	UK ‡	Ordinary shares of £1
Henderson Technology Ventures Limited (holding company)	UK ‡	Ordinary shares of £1
Henderson UK Shopping Centre Fund (Jersey property unit trust)	Jersey ‡ *	79% of units owned
HHG Private Capital Portfolio No. 1 (private equity partnership)	UK ‡	–
HHG Private Capital Portfolio No. 2 (private equity partnership)	UK ‡	–
HHG Private Capital Portfolio No. 3 (private equity partnership)	UK ‡	–
HHG Private Capital Portfolio No. 4 (private equity partnership)	UK ‡	–
HHG Private Capital Portfolio No. 5 (private equity partnership)	UK ‡	–
HHG Services Limited (service company)	UK ‡ *	Ordinary shares of £1
London Life Group Services Limited (service company)	UK ‡ *	Ordinary shares of £1
London Life Holdings Limited (holding company)	UK ‡ *	Ordinary shares of £1
Mutual Securitisation plc (finance company)	ROI ‡ *	–
NP Life Holdings Limited (holding company)	UK ‡ *	'A' and 'B' ordinary shares of £1
NPI Finance plc (finance company)	UK ‡ *	Ordinary shares of £1
NPI Holdings Limited (holding company)	UK ‡ *	'A' ordinary shares of £1
NPI Payments Limited (disbursing NPI policyholders' demutualisation benefits)	UK ‡ *	Ordinary shares of £1
NPI Self Invested Personal Pensions Limited (pension management)	UK ‡ *	'B' ordinary shares of £1
Pearl Assurance Group Holdings Limited (holding company)	UK ‡ *	Ordinary shares of £1
Pearl GI Limited (general insurance agent)	UK ‡ *	Ordinary shares of £1
Pearl Invest Limited (financial services company)	UK ‡ *	Ordinary shares of £1
Pearl ISA Limited (ISA management)	UK ‡ *	Ordinary shares of £1
Pearl Unit Trusts Limited (unit trust management)	UK ‡	Ordinary shares of £1
Premier Pension Trustees Limited (pensioner trustee services)	UK ‡ *	Ordinary shares of £1
Towry Law (Asia) HK Limited (financial services company)	China ‡	Ordinary shares of HK\$1
Towry Law Financial Services Limited (financial services)	UK ‡	Ordinary shares of £1
Towry Law Insurance Brokers Limited (insurance brokers)	UK ‡	Ordinary shares of £1
Towry Law plc (financial services company)	UK ‡	Ordinary shares of £1
UKLS Financial Services Limited (finance company)	UK ‡ *	Ordinary shares of £1
(c) Joint venture undertaking:		
The Printworks Leisure Scheme Trust (property trust)	UK ‡ *	50%
(d) Associate undertakings:		
Henderson Caspar Property Fund (property fund)	Jersey ‡ *	50%
Henderson Central London Office Fund (property fund)	Jersey ‡ *	40%
Henderson French Property Fund BV (property fund)	UK ‡ *	41%
Henderson (UK) Retail Warehouse Fund (property fund)	UK ‡ *	22%
Henderson UK Shop Fund (property fund)	Jersey ‡	50%
Moor House Limited Partnership (property partnership)	UK ‡ *	33%
The Covent Garden Limited Partnership (property partnership)	UK ‡ *	37%

Notes

‡ Held by a subsidiary undertaking.

* Life Services business to be disposed of under agreement with Life Company Investor Group Limited (note 38).

The information disclosed above is only in respect of those undertakings which principally affect the figures shown in the Group's accounts. There are a number of other subsidiary and associated undertakings whose business does not materially affect the Group's profits or the amount of its assets and particulars of these have been omitted in view of their excessive length.

As part of the Group's ongoing review of its investment strategy, a significant number of property holdings were moved into more liquid investments in the form of JPUTs and cash during 2004. This has resulted in the Group owning a 79% equity interest in the Henderson UK Shopping Centre Fund at 31 December 2004 and a corresponding minority interest of £83m has been recognised in the Consolidated Group Balance Sheet at that date.

36. Related party transactions

The Group's pension scheme is charged on an arm's length basis with the costs of administration and investment management services, which amounted to £0.6m in 2004 (2003: £0.3m).

At 31 December 2004, one director held a life assurance policy issued by Pearl in the normal course of business. The sum assured under this policy is £1,406,004 (2003: £1,176,000).

During the year, Henderson Fund Management plc has agreed to make a loan facility available to seven employees who are limited partners in the Henderson PFI Secondary Co-Investment Fund 'A' LP to assist in meeting an agreed proportion of their commitment to the partnership from time to time. The gross facility is £1.25m and £0.2m has been utilised at 31 December 2004.

All related party transactions with AMP are conducted on normal commercial terms.

	31 Dec 04 £m	31 Dec 03 £m
Management services fee expense	–	(9)
Interest paid	–	(33)
Interest received	–	6
Investment management fee income	5	7
Service fee income	–	6
Other income	–	2
	5	(21)

Balances with AMP are as follows:

	31 Dec 04 £m	31 Dec 03 £m
Debtors less creditors	4	9

In 2004, the 31 December 2003 net debtor balance with AMP of £9m and £1m of the 2004 investment management fee income were settled for cash.

During 2003, the Group also had related party transactions with AMP in relation to share capital and other financing.

37. Contingent liabilities

The following contingent liabilities existed at 31 December 2004:

- (a) in the normal course of business, the Group is exposed to certain legal issues, which involve litigation and arbitration;
- (b) in the normal course of business, the Group enters into various types of investment contracts that can give rise to contingent liabilities. These include foreign exchange contracts, financial futures, interest rate derivatives and exchange traded options. These contracts are entered into in the normal management of the investment portfolio;
- (c) provision for liabilities arising under contracts with policyholders is based on certain assumptions. The variance of actual experience from that assumed may result in such liabilities differing from the provisions made for them. Liabilities may also arise in respect of claims relating to the interpretation of such contracts, or the circumstances in which policyholders have entered into them. The extent of such liabilities is influenced by the actions and requirements of the FSA, the Ombudsman rulings, by industry compensation and by court judgements; and
- (d) the provision for costs in respect of Towry Law International legacy products is based on a number of assumptions. The variance of actual experience from that assumed may result in such liabilities differing from the provisions made for them.

38. Post Balance Sheet events

At an Extraordinary General Meeting held on 21 February 2005, shareholders approved an agreement that the Company and its subsidiary companies entered into on 9 December 2004, to sell the Life Services business owned by Pearl Group Limited (a direct subsidiary of the Company) to Life Company Investor Group Limited. It is anticipated that regulatory approval by the FSA and satisfaction of conditions relating to the HHG Staff Pension Scheme will be obtained to enable completion of the sale in April 2005.

The Life Services business comprises principally the life insurance and pensions books of Pearl, London Life, NPLL and NPIL, which are effectively closed to new business, various unit-linked life insurance companies and the Service Company which provides administrative services to these businesses. All of these are directly or indirectly owned by Pearl Assurance Group Holdings Limited, 100% of whose issued share capital is being sold by Pearl Group Limited.

The consideration payable to Pearl Group Limited for the sale of the Life Services business will be satisfied by cash payment on Completion of £1.070bn. In addition, Life Company Investor Group Limited will transfer to Pearl Group Limited at Completion the benefit of a receivable of £34m representing the value of the stake in BPL together with related entities held in Pearl. Based on net assets of the Life Services business at 31 December 2004 of £1.409bn, expected associated professional fees and transaction costs of £28m and £7m loss arising from the settlement of the net outstanding loans between Life Services and the Remaining Group, this is expected to result in a loss on disposal of approximately £340m. The actual loss on disposal will be calculated using net assets at the Completion date and will be reported in 2005 under IFRS.

Following Completion it is proposed that the majority of the proceeds be returned to shareholders in cash, that the investor base be reduced and that the Remaining Group will be renamed Henderson Group plc. The table below sets out the consolidated balance sheet of the Group after adjustments to reflect these transactions as if they had occurred at 31 December 2004.

	Group consolidated Balance Sheet at 31 Dec 2004 £m	Life Services consolidated Balance Sheet at 31 Dec 2004 £m	Adjustments Other adjustments £m	Pro-forma Remaining Group £m
Assets				
Intangible assets	233	–	–	233
Investments	23,635	(23,540)	454 ¹	549
Assets held to cover linked liabilities	4,215	(4,215)	–	–
Reinsurers' share of technical provisions	277	(277)	–	–
Debtors	326	(240)	–	86
Other assets	343	(274)	–	69
Prepayments and accrued income	431	(421)	–	10
Total assets	29,460	(28,967)	454	947
Liabilities				
Minority interests	83	(83)	–	–
Fund for future appropriations	602	(602)	–	–
Gross technical provisions	21,285	(21,285)	–	–
Technical provisions for linked liabilities	4,215	(4,215)	–	–
Provision for other risks and charges	253	(157)	28 ²	124
Debenture loans	348	(556)	242 ³	34
Amounts owed to credit institutions	296	(296)	–	–
Creditors, accruals and deferred income	540	(364)	–	176
Total liabilities	27,622	(27,558)	270	334
Net assets	1,838	(1,409)	184	613
Capital and reserves				
Called up share capital	271	–	(158) ⁴	113
Share premium	1081	–	(727) ⁵	354
Own shares held	(4)	–	–	(4)
Capital reserve	2	–	–	2
Profit and loss account	488	(1,409)	1,069 ⁶	148
	1,838	(1,409)	184	613

The reduction in pro-forma capital and reserves from £1,838m to £613m comprises the return of capital to shareholders following the intended sale of the Life Services business (£885m) together with the loss on disposal (£340m).

Notes to the adjustments

	£m
1 This adjustment comprises the following components and reflects management's best estimate of the return of cash to shareholders, based on the number of shares in issue at 26 November 2004:	
• Purchase by the Remaining Group of investments in BPL at fair value for cash from the Pearl with-profits fund;	–
• Transfer of investments in BPL at fair value from the shareholder fund of Pearl;	34
• Novation of loans due to the Life Services business in settlement of assignment of loan receivables and accrued interest due to the Remaining Group;	201
• Creation of new loan receivable from Pearl Assurance Group Holdings Limited, a Life Services entity;	34
• Cash consideration received;	1,070
• Cash paid to shareholders in respect of the capital reduction of 52 out of 100 shares at a price of 55 pence per share; and	(775)
• Cash paid to shareholders for the fractional entitlements created on the consolidation of 500 10 pence shares into one £50 share. This assumes that all fractional entitlements created on the consolidation will be aggregated into as many whole consolidated shares as possible and such consolidated shares will be cancelled and the proceeds repaid to shareholders. It has been assumed that 330,000 consolidated shares will be cancelled at a price equivalent to 66 pence per ordinary share.	(110)
	454
2 This adjustment comprises a provision for transaction and separation related expenses including warranty insurance premium.	28
3 This adjustment comprises the following components:	
• Assignment of loans currently classified as intra-Group due from the Life Services business to Life Company Investor Group Limited in settlement of novation of loans payable, together with accrued interest due from the Remaining Group; and	208
• Creation of new loan payable to Pearl in settlement of transfer of investments from the shareholder fund in BPL at fair value.	34
	242
4 This adjustment reflects management's best estimate of the effect on share capital of the return of cash to shareholders, based on the number of shares in issue at 26 November 2004:	
• Court confirmed reduction of share capital under section 135 of the Companies Act 1985 of 1.409bn 10 pence shares, i.e. the cancellation of 52 out of 100 shares of 10 pence each at 55 pence per share;	141
• Cancellation of £50 shares as a result of the fractional entitlements created on the consolidation of 500 10 pence shares into one £50 share, on the basis that all fractional entitlements are aggregated and cancelled, with the proceeds paid to shareholders. It has been assumed that 330,000 consolidated shares will be cancelled at a price equivalent to 66 pence per ordinary share; and	17
• Share division of one £50 share into 500 10 pence shares.	–
	158
5 This adjustment reflects management's best estimate of the effect on share premium of the return of cash to shareholders, based on the number of shares in issue at 26 November 2004:	
• Court confirmed reduction of share capital under section 135 of the Companies Act 1985 of 1.409bn 10 pence shares, i.e. the cancellation of 52 out of 100 shares of 10 pence each at 55 pence per share;	634
• Cancellation of £50 shares as a result of the fractional entitlements created on the consolidation of 500 10p shares into one £50 share, on the basis that all fractional entitlements are aggregated and cancelled, with the proceeds paid to shareholders. It has been assumed that 330,000 consolidated shares will be cancelled at a price equivalent to 66 pence per ordinary share; and	93
• Share division of one £50 share into 500 10 pence shares.	–
	727
6 This adjustment reflects the following components:	
• Cash consideration received;	1,070
• Gain arising on transfer of investments in BPL at fair value;	34
• Provision for transaction and separation related expenses including warranty insurance premium; and	(28)
• Loss arising from the settlement of the net outstanding loans between the Life Services business and the Remaining Group at 31 December 2004.	(7)
	1,069

Shareholder Information

As at 18 March 2005

Total number of holders of ordinary shares and their voting rights

The share capital of HHG PLC consisted of 2,710,772,247 ordinary shares held by 858,915 security holders. This included 1,687,783,107 shares, held by CHES Depository Nominees (CDN), quoted on the ASX in the form of CHES Depository Interests (CDIs) and held by 804,030 CDI holders. Each registered holder of shares present in person (or by proxy, attorney or representative) at a meeting of shareholders has one vote on a vote taken by a show of hands, and one vote for each fully paid share held on a vote taken on a poll. CDI holders can instruct CDN to appoint a proxy on their behalf and can direct the proxy how to vote on the basis of one vote per person taken by a show of hands, and one vote per CDI on a vote taken on a poll.

Twenty largest share/CDI holders

	Ordinary shares/CDIs	% of issued Capital
1 AMP Financial Services Holdings Limited	272,000,000	10.03
2 RBC Global Services Australia Nominees Pty Limited	193,849,525	7.15
3 Chase Nominees Ltd	185,142,794	6.83
4 Citicorp Nominees Pty Limited	146,696,466	5.41
5 Westpac Custodian Nominees Limited	146,104,204	5.39
6 National Nominees Limited	123,972,347	4.57
7 J P Morgan Nominees Australia Limited	115,984,405	4.28
8 HSBC Global Custody Nominee (UK) Ltd	109,134,640	4.03
9 Cogent Nominees Pty Limited	58,085,402	2.14
10 CUIM Nominee Ltd	53,866,900	1.99
11 State Street Nominees Ltd	41,506,102	1.53
12 IOOF Investment Management Limited	39,850,716	1.47
13 Chase (GA Group) Nominees Limited	33,528,648	1.24
14 Vidacos Nominees Ltd	31,624,622	1.17
15 BNY Norwich Union Nominees Ltd	31,444,684	1.16
16 AMP Life Limited	30,271,393	1.12
17 Queensland Investment Corporation	28,227,683	1.04
18 Westpac Financial Services Limited	25,074,653	0.93
19 ANZ Nominees Limited	22,401,643	0.83
20 Nortrust Nominees Limited	22,093,256	0.82
Top 20 Total	1,710,860,083	63.11
Total Shares	2,710,772,247	100.00

Distribution of share/CDI holdings

Categories	Number of holders	% of issued Capital
1 – 1,000	716,017	9.74
1,001 – 5,000	131,861	8.76
5,001 – 10,000	6,550	1.72
10,001 – 100,000	4,028	3.60
100,001 and over	459	76.18
Total	858,915	100.00

384,572 share/CDI holders held less than A\$500 worth of shares/CDIs, i.e. fewer than 329 shares/CDIs.

Stock exchange listings

HHG PLC shares are listed on the London Stock Exchange and HHG CDIs are quoted on the Australian Stock Exchange.

Substantial shareholders

HHG had received substantial shareholding notices, sent in accordance with Australian regulatory requirements, from the following:

- AMP Limited and its associates held 342,930,210 shares/CDIs or 12.65% of HHG's issued capital, as detailed in its substantial shareholding notice sent on 14 December 2004;
- Perpetual Trustees Australia Limited held 245,749,190 shares/CDIs or 9.07% of HHG's issued capital, as detailed in its substantial shareholding notice sent on 17 February 2005;
- Perennial Value Management Limited held 135,826,601 shares/CDIs or 5.01% of HHG's issued capital, as detailed in its substantial shareholding notice sent on 23 February 2005.

Total number of options over unissued shares and option holders

There were 9,859,803 options over unissued ordinary shares in HHG PLC held by 791 option holders.

Restricted securities

There are no restricted securities on issue.

Buy-back

There is no current on-market buy-back.

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Glossary

AMP

AMP Limited and its controlled entities

annuity

a periodic payment made for an agreed period of time (usually up to the death of the recipient) in return for a cash sum. The cash sum can be paid as one amount or as a series of premiums

CDI

a CHES Depositary Interest representing one ordinary share. These are quoted on the Australian Stock Exchange

CDO

Collateralised Debt Obligations

closed or closed book

a book of business with no new customers, although there are limited volumes of new business, for example, to meet contractual obligations to existing policyholders or to cater for new members to certain group schemes

commutation

an agreement negotiated between an insured and insurer, usually involving the payment of a lump sum which relieves the insurer of the obligation to meet all current debts and anticipated future liabilities under one or more than one specific insurance contract

Companies Act 1985

the UK Companies Act 1985, as amended

Completion

the completion of the sale of the Life Services business to Life Company Investor Group Limited pursuant to the terms of the sale agreement

Corporations Act 2001

the Australian Corporations Act 2001

CRR

the Capital Resources Requirement, i.e. the excess of available capital resources to cover long-term insurance business

embedded value

an actuarially determined estimate of the economic value of the shareholder capital in the Life Services businesses and the profits expected to emerge from the business in force

FRC

Financial Reporting Council

free assets

the excess of available assets (admissible assets less total liabilities) over and above the CRR

Free Asset Ratio or FAR

this has been calculated in this document as the free assets divided by total liabilities; this is one of the key regulatory capital measures for UK life insurers. Note that the calculation for the 2004 FARs are not directly comparable with 2003 due to changes in the rules for assessing capital adequacy. In particular, the asset figures are calculated on a twin peaks basis

general insurance

non-life insurance covering risks such as motor vehicle liability, fire and damage to property

Group

HHG PLC and its controlled entities

Henderson Group plc

the remaining group (after the sale of the Life Services business) which will comprise Henderson Global Investors (Henderson) and Towry Law

in force business

long-term business which has been written before a specified date and which has not terminated before that date

ISA

Individual Savings Accounts

Life Services

comprises principally the life insurance and pension books of Pearl, London Life, NPLL and NPIL, which are effectively closed to new business; Life Services also includes the closed general insurance books of Pearl, the pension trustee business of Premier Pension Trustees Limited and the retirement services business operated by NPIL

Life Services business

the legal entities of the life business of the Group which comprise principally (i) the life insurance and pension books of Pearl, London Life, NPLL and NPIL, which are effectively closed to new business, (ii) the unit-linked companies and (iii) the Service Company which provides administrative services to these businesses, all of which are owned (directly or indirectly) by Pearl Assurance Group Holdings Limited, the shares of which are being sold to Life Company Investor Group Limited

liquidity

net cash flows available for investment in the Consolidated Cash Flow Statement

London Life

London Life Limited

long-term fund

a segregated fund of assets and liabilities established and maintained by a life insurance company for the purpose of supporting a long-term business

non-profit policy

a policy where the value of the policy or product is either linked directly to the performance of the underlying assets (such as a unit-linked policy), or is guaranteed by the insurer. Also known as a non-participating policy

NPI

National Provident Institution

NPIL

NPI Limited

NPLL/National Provident Life

National Provident Life Limited

OEIC

Open-Ended Investment Company

profit before tax

profit before tax represents the profit before tax for the year attributable to shareholders of HHG PLC (the Company)

Pearl

Pearl Assurance plc

PVIF

Present Value of In Force Business. This represents the discounted future margins on an in force portfolio of long-term business. It is only recognised on the balance sheet when it has been acquired for value and is then amortised over its expected life

reinsurance

the insuring again by an insurer of the whole or part of a risk that it has already insured for a customer with another insurer called a reinsurer. The expression "reassurance" is sometimes used to describe the same arrangements when made by a life insurance company

Remaining Group

Henderson Group plc

run-off

the administration of insurance portfolios that have been closed to new business

Service Company

HHG Services Limited

traditional

when used in respect of an embedded value or value of new business, an approach which allows for risk and uncertainty in a relatively simple way, through the choice of the rate used to discount expected profits and flows of supporting capital back to the present

TSR

Total Shareholder Return

underwriting

the insurer's process of reviewing applications for insurance cover and the decision whether to accept all or part of the risk and determination of the applicable premiums; also refers to the acceptance of such risk

unitised with-profits

a policy under which the value of the benefits is measured in whole or in part by reference to the with-profits units allocated to that policy

unit trust

a trust in which investors (unit holders) obtain an interest. Unlisted trusts often permit investors to exit their investment by having their units purchased or redeemed at a price closely reflecting the underlying market value of the trust's investments

with-profits policy or participating policy

a policy under which (in addition to guaranteed benefits specified in the policy) additional bonuses may be payable. The declaration of such bonuses (usually annually) reflects, amongst other things, the overall investment performance of the fund of which the policy forms part; "without-profits policy" or "non-participating policy" means a policy where no such additional bonuses are payable

with-profits units

notional units whose value or number varies by reference to premiums paid, to bonuses declared or surpluses otherwise distributed for the purposes of calculating benefits payable under policies



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