GRESHAM INSURANCE COMPANY LIMITED
FINANCIAL STATEMENTS
2005

Gresham Insurance Company Limited

Contents

Gresham Insurance Company Limited

Directors and officer

Directors:

M S Hodges
P C Easter
A Grace
A Seymour-Jackson

Officer:

Company Secretary:
Aviva Company Secretarial Services Limited

Auditors:

Ernst & Young LLP
Registered Auditor
1 More London Place
London
SE1 2AF

Registered office:

8 Surrey Street
Norwich
NR1 3NG

Registered in England : No. 110410

A member of the Association of British Insurers and the Financial Ombudsman Service, and regulated by the Financial Services Authority.

The Company is a member of the Aviva plc group of companies (the Group).

Gresham Insurance Company Limited

Directors' report
for the year ended 31 December 2005

The directors present their annual report and audited financial statements for Gresham Insurance Company Limited (the Company) for the year ended 31 December 2005.

Principal activity and future developments

The principal activity of the Company is the transaction of general insurance business in the United Kingdom through a business partnership arrangement with Barclays Bank plc. The directors consider that this will continue unchanged into the foreseeable future.

Major events

On 31 March 2005 Barclays Bank plc acquired 55,260,000 "A" Ordinary shares from Legal & General Insurance Limted, the Company's parent undertaking, being its entire shareholding in the issued share capital of the Company.

On 4 April 2005 the "A" Ordinary shares of £1 each and the "B" Ordinary shares of £1 each owned by Barclays Bank plc, being the entire issued share capital of the Company, were transferred from Barclays Bank plc to CGU International Insurance plc.

On 18 April 2005 all the authorised, issued and unissued "A" Ordinary shares of £1 each and the "B" Ordinary shares of £1 each were re-classified and re-designated as ordinary shares of £1 each.

Results for the year

Full details of the results for the year are set out on page 13.

Dividends

A final dividend of £ 4,384,775 was paid in 2005 in respect of the 2004 financial year (2004: a final dividend of £3,327,500 in respect of 2003).

Financial instruments

The business of the Company includes use of financial instruments. Details of the Company's risk management objectives and policies and exposures to risk are set out in note 22 to the financial statements.

Payment policy

It is the Company's policy to pay creditors when they fall due for payment. Terms of payment are agreed with suppliers when negotiating each transaction and the policy is to abide by those terms, provided that the suppliers also comply with all relevant terms and conditions.

The amounts due to trade creditors at 31 December 2005 represented approximately 8 days of average daily purchases through the year (2004: 34 days).

Employees

All employees are employed by a fellow subsidiary undertaking of Aviva plc, Aviva Employment Services Limited. Disclosures relating to employees may be found in the consolidated accounts of Aviva plc.

Gresham Insurance Company Limited

Directors' report (continued)

Directors' interests

The names of the present directors of the Company appear on page 1.

R A Phipps, J M A Hughes, P Jackson, L K Penney and I D Viney resigned as directors of the Company on 31 March 2005.

B F McIntyre, M S Hodges, A Grace and P J R Snowball were appointed as directors of the Company on 31 March 2005.

B F McIntyre resigned as a director of the Company on 9 June 2005 and P C Easter was appointed a director on the same date. P J R Snowball resigned as a director on 13 March 2006. A Seymour-Jackson was appointed as a director on 16 March 2006.

The table below shows the interests held by each person who was a director at the end of the financial year in the ordinary shares of 25 pence each in Aviva plc. Details of any options and awards held through Aviva plc's share schemes and incentive plans are shown on pages 3 and 4. All the disclosed interests are beneficial.

	On appointment Number	At 31 December 2005 Number
M S Hodges	18,389	5,437
P C Easter	6,477	6,628

P J R Snowball is a director of the Company's ultimate parent undertaking, Aviva plc, and details of his interests are given in that company's financial statements.

A Grace has no interests in shares of the Company or Aviva plc.

Incentive plans

Details of the directors who held office at the end of the financial year, and hold or held options to subscribe for ordinary shares of Aviva plc or hold or held awards over shares in Aviva plc, pursuant to Aviva plc's share based incentive plans, are set out below.

(i) Share options

	On appointment Number	Options granted during the period Number	Options cancelled during the period Number	At 31 December 2005 Number
M S Hodges				
Savings related options	2,356	-	2,356	-
P C Easter				
Savings related options	4,096	-	-	4,096

(1) *"Savings related options" are options granted under the Inland Revenue approved SAYE Share Option Scheme.* Options granted from 1999 to 2005 are normally exercisable during the six month period following either the third, fifth or seventh anniversary of the relevant savings contract.

(2) During the year no directors exercised any share options.

Gresham Insurance Company Limited

Directors' report (continued)

Directors' interests (continued)

(ii) Share awards

	On appointment	Awards granted during the period	Awards vested during the period	Awards lapsed during the period	At 31 December 2005
	Number	Number	Number	Number	Number
M S Hodges					
Aviva Long Term Incentive Plan	85,597	-	-	-	85,597
Aviva Long Term Incentive Plan 2005	35,046	-	-	-	35,046
Aviva Deferred Bonus Plan	98,594	-	-	-	98,594
P C Easter					
Aviva Long Term Incentive Plan	123,577	-	-	-	123,577
Aviva Long Term Incentive Plan 2005	46,728	-	-	-	46,728
Aviva Deferred Bonus Plan	126,232	-	-	-	126,232

(1) Aviva Long Term Incentive Plan; awards under the Plan are made on an annual basis and the 2005 awards are made in March. Awards are subject to the attainment of performance conditions over a three year period.

(2) Aviva Long Term Incentive Plan 2005; awards under the Plan are made on an annual basis and the 2005 award was made in March. Awards are subject to the attainment of performance conditions over a three year period.

(3) Aviva Deferred Bonus Plan; awards disclosed include those made in lieu of some or all of the cash bonus earned and deferred under Aviva plc's Annual Bonus Plan and also the matching awards granted on a one for one basis. The awards are not subject to performance conditions and vest on the third anniversary of their grant.

Auditors

In accordance with Section 385 of the Companies Act, a resolution is to be proposed at the Annual General Meeting for the reappointment of Ernst & Young LLP as auditor of the Company. A resolution will also be proposed authorising the directors to determine the auditor's remuneration.

Gresham Insurance Company Limited

Directors' report (continued)

Directors' liabilities

Aviva plc, the ultimate parent undertaking, has granted an indemnity to the directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 1985. This indemnity and the provisions in the Company's Articles of Association constitute "qualifying third party indemnities" for the purposes of sections 309A to 309C of the Companies Act 1985. Such qualifying third party indemnity provision remains in force as at the date of approving the directors' report.

Statement of directors' responsibilities

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

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

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

On behalf of the Board

Director

21 March 2006

Gresham Insurance Company Limited

Independent auditors' report

To the shareholders of Gresham Insurance Company Limited

We have audited the Company's financial statements for the year ended 31 December 2005 which comprise the Accounting Policies, the Income Statement, the Balance Sheet, the Statement of Changes in Shareholder's Equity, the Cash Flow Statement and the related notes 1 to 23. These financial statements have been prepared on the basis of the accounting policies set out therein.

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 financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union as set out in the statement of directors' responsibilities in the Directors' Report.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are 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 financial statements, 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 regarding directors' remuneration and transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements:

- give a true and fair view, in accordance with IRFSs as adopted by the European Union, of the state of the Company's affairs as at 31 December 2005 and of its loss for the year then ended; and
- have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
London
24 March 2006

Gresham Insurance Company Limited

Accounting policies

Gresham Insurance Company Limited (the "Company"), a limited company incorporated and domiciled in the United Kingdom (UK), transacts general insurance business in the UK. The directors consider that this will continue unchanged into the foreseeable future.

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

(A) Basis of presentation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS), as endorsed by the European Union, applicable at 31 December 2005.

The IASB issued amendments to IAS 19, Employee Benefits, and IAS 39, The Fair Value Option, in December 2004 and June 2005 respectively. The requirements are applicable for accounting periods beginning on or after 1 January 2006, but the Company has decided to adopt them early and reflect their impact in these financial statements.

In August 2005, the IASB issued IFRS 7, Financial Instruments: Disclosures, and amendments to IAS 1, Capital Disclosures, and IAS 39/IFRS 4, Financial Guarantee Contracts. Their requirements are applicable for accounting periods beginning on or after 1 January 2007 for the first two and, for the third, 1 January 2006. The Company has decided not to adopt any of them early in these financial statements but the impact of adopting these standards is not expected to have a material effect on the results of the Company. IFRS 7 will result in amendments to the disclosure of financial assets and liabilities, whilst the amendments to IAS 1 bring the capital disclosures into line with IFRS 7. The amendments to IAS 39 and IFRS 4 will not affect the manner in which the Company accounts for financial guarantee business. In addition, IFRS 6 and IFRIC Interpretations 5 and 6 have been issued during 2005 but are not relevant to the activities of the Company.

In accordance with the standard for Phase 1 (IFRS 4), Insurance Contracts, the Company has applied existing accounting practices for insurance, modified as appropriate to comply with the IFRS framework and applicable standards. Further details are given in policy D overleaf.

The Company first adopted IFRS for the year ended 31 December 2005 and has accordingly restated its previously reported 2004 financial statements to comply with IFRS. The principal effects of the adoption of IFRS have been reflected within note 1, on first time adoption of IFRS.

The financial statements are stated in British pounds, which is the Company's functional and presentation currency. Unless otherwise noted, the amounts shown in these financial statements are in thousands of British pounds (£000).

(B) Use of estimates

The preparation of financial statements requires the Company to make estimates and assumptions that affect items reported in the balance sheet and income statement and the disclosure of contingent assets and liabilities at the date of the financial statements. Although these estimates are based on management's best knowledge of current facts, circumstances and, to some extent, future events and actions, actual results ultimately may differ from those estimates, possibly significantly.

(C) Foreign currency translation

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

Translation differences on debt securities and other monetary financial assets measured at fair value are included in foreign exchange gains and losses in the income statement. Translation differences on non-monetary items, such as equities, which are held at fair value through profit or loss as defined in Policy K, are reported as part of the fair value gain or loss.

Accounting policies (continued)

(D) Product classification

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

As noted in policy A above, insurance contracts in general continue to be measured and accounted for under existing accounting practices at the date of the transition to IFRS. Accounting for insurance contracts is determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers in December 2005.

(E) Premiums earned

Insurance premiums written reflect business incepted during the year, and exclude any sales-based taxes, duties or levies. Written premiums include an estimate of pipeline premiums less a provision for anticipated lapses. Unearned premiums are those proportions of the premiums written in a year that relate to periods of risk after the balance sheet date. Unearned premiums are computed principally on either a daily or monthly pro rata basis. Premiums collected by intermediaries, but not yet received, are assessed based on estimates from underwriting or past experience, and are included in premiums written.

(F) Other fee and commission income

Other fee and commission income consists primarily of commission revenue from reinsurance commission and profit participation, which is recognised when earned.

(G) Net investment income

Investment income consists of dividends, interest and rents receivable for the year, movements in amortised cost on debt securities, realised gains and losses, and unrealised gains and losses on FVPL investments (as defined in policy K). Dividends on equity securities are recorded as revenue on the ex-dividend date. Interest income is recognised as it accrues, taking into account the effective yield on the investment.

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

Gresham Insurance Company Limited

Accounting policies (continued)

(H) Insurance contract liabilities

Claims

Insurance claims incurred include all losses occurring during the year, whether reported or not, related loss adjustment expenses, a reduction for the value of salvage and other recoveries, and any adjustments to claims incurred in previous years.

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

Outstanding claims provisions

Insurance outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related loss adjustment expenses. Significant delays are experienced in the notification and settlement of certain types of general insurance claims, particularly in respect of liability business, the ultimate cost of which cannot be known with certainty at the balance sheet date. Any estimate represents a determination within a range of possible outcomes. Further details of estimation techniques are given in note 14.

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

Provision for unearned premiums

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

Liability adequacy

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

Other assessments and levies

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

Accounting policies (continued)

(I) Reinsurance

The Company cedes reinsurance in the normal course of business, with retention limits varying by line of business. The cost of reinsurance is accounted for over the life of the underlying reinsured policies, using assumptions consistent with those used to account for these policies. Gains or losses on buying retroactive reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised.

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

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

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

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

(i) the rights to receive cash flows from the asset have expired;

(ii) the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or

(iii) the Company has transferred its rights to receive cash flows from the asset and either

 (a) has transferred substantially all the risks and rewards of the asset; or

 (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

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

Gresham Insurance Company Limited

Accounting policies (continued)

(K) Financial investments

The Company classifies its investments as either financial assets at fair value through profit or loss (FVPL). The FVPL category is used as, in most cases the Company's strategy is to manage its financial investments on a fair value basis.

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

Purchases and sales of investments are recognised on the trade date, which is the date that the Company commits to purchase or sell the assets, at their fair values less transaction costs. Debt securities are initially recorded at their fair value, which is taken to be amortised cost, with amortisation credited or charged to the income statement. Investments classified as trading and other than trading are subsequently carried at fair value. Changes in the fair value of trading and other than trading investments are included in the income statement in the period in which they arise.

The fair values of investments are based on quoted bid prices or amounts derived from cash flow models. Fair values for unlisted equity securities are estimated using applicable price/earnings or price/cash flow ratios refined to reflect the specific circumstances of the issuer. Equity securities for which fair values cannot be measured reliably are recognised at cost less impairment.

(L) Deferred acquisition costs

The costs directly attributable to the acquisition of new business for insurance contracts are deferred to the extent that they are expected to be recoverable out of future margins in revenues on those contracts.

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

Deferred acquisition costs are amortised over the period in which the related revenues are earned. The reinsurers' share of deferred acquisition costs is amortised in the same manner as the underlying asset.

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

(M) Cash and cash equivalents

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

(N) Contingent liabilities

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

Gresham Insurance Company Limited

Accounting policies (continued)

(O) Income taxes

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

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

The principal temporary differences arise from the equalisation provision, revaluation of certain financial assets and liabilities including derivative contracts and tax losses carried forward; and, in relation to acquisitions, on the difference between the fair values of the net assets acquired and their tax base. The rates enacted or substantively enacted at the balance sheet date are used to determine the deferred tax.

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

(P) Share capital and dividends

Equity instruments

An equity instrument is a contract that evidences a residual interest in the assets of an equity after deducting all of its liabilities. Accordingly, a financial instrument is treated as equity if:

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

(ii) the instrument will not be settled by delivery of a variable number of shares or is a derivative that can be settled other than for a fixed amount of cash, shares or other financial assets.

Dividends

Interim dividends on ordinary shares are recognised in equity in the period in which they are paid. Final dividends on these shares are recognised when they have been approved by shareholders.

(Q) Equalisation provision

Equalisation provisions are established in accordance with UK company law. These provisions are in addition to the provisions required to meet the anticipated ultimate cost of settlement of outstanding claims at the balance sheet, and in the previously reported balance sheet are included in technical provisions. Under IFRS, the provisions are not reported in the balance sheet or no liability exists but are presented within retained earnings, net of attributable tax relief.

Gresham Insurance Company Limited

Income statement
For the year ended 31 December 2005

	Note	2005	2004
		£000	£000
Income	2		
Gross written premiums		160,674	146,406
Premiums ceded to reinsurers		(5,709)	(8,985)
Premiums written net of reinsurance		154,965	137,421
Net change in provision for unearned premiums		(14,450)	(3,418)
Net premiums earned		140,515	134,003
Fee and commission income		514	180
Net investment income		6,874	6,076
Other operating income		735	-
		148,638	140,259
Expenses	3		
Claims and benefits paid, net of recoveries from reinsurers		85,315	71,422
Change in insurance liabilities, net of reinsurance		1,813	10,353
Fee and commission expense		62,632	51,361
Other operating expenses		9,422	928
		159,182	134,064
(Loss)/Profit before tax		(10,544)	6,195
Tax (credit)/expense	8	(3,131)	1,810
(Loss)/Profit for the year		(7,413)	4,385

The Company has no recognised income and expense other than those included in the results above and therefore a statement of recognised income and expense has not been presented.

The accounting policies on pages 7 to 12 and notes on pages 17 to 40 are an integral part of these financial statements.

Gresham Insurance Company Limited

Balance sheet
As at 31 December 2005

	Note	2005	2004
Assets		£000	£000
Financial investments	10	117,367	113,918
Reinsurance	11	132	6,389
Deferred tax assets	15	-	6
Current tax assets		10,473	-
Receivables and other financial assets	12	95,525	63,082
Deferred acquisition costs	13	22,295	28,940
Prepayments and accrued income		1,220	1,406
Cash and cash equivalents	21 (b)	17,528	10,565
Total assets		264,540	224,306
Liabilities			
Insurance	14	137,675	127,669
Deferred tax	15	6,758	-
Current tax		-	1,045
Payables and other financial liabilities	16	59,864	28,882
Other liabilities	17	6,256	925
Total liabilities		210,553	158,521
Net assets		53,987	65,785
Equity			
Capital			
Ordinary share capital	18	61,400	61,400
Retained earnings	19	(7,413)	4,385
Total equity		53,987	65,785

The accounting policies on pages 7 to 12 and notes on pages 17 to 40 are an integral part of these financial statements.

Approved by the Board on 21 March 2006

Director

Gresham Insurance Company Limited
Statement of changes in shareholder's equity

For the year ended 31 December 2005

	Note	Ordinary share *capital* £000	Retained *earnings* £000	Total *equity* £000
Balance at 1 January 2004		61,400	3,327	64,727
Total recognised income and expense for the year		-	4,385	4,385
Dividends	9	-	(3,327)	(3,327)
Total movements in the year		-	1,058	1,058
Balance at 31 December 2004		61,400	4,385	65,785
Total recognised income and expense for the year		-	(7,413)	(7,413)
Dividends	9	-	(4,385)	(4,385)
Total movements in the year		-	(11,798)	(11,798)
Balance at 31 December 2005		61,400	(7,413)	53,987

The accounting policies on pages 7 to 12 and notes on pages 17 to 40 are an integral part of these financial statements.

Gresham Insurance Company Limited

Cash flow statement
For the year ended 31 December 2005

	Note	2005	2004
		£000	£000
Cash flows from operating activities			
Net cash inflow/(outflow) from continuing operations	21 (a)	11,365	(26,207)
Tax received/(paid)		(1,624)	(3,660)
Net cash from/(used in) operating activities		9,742	(29,867)
Cash flows from financing activities			
Ordinary dividends paid		(4,385)	(3,327)
Net cash used in financing activities		(4,385)	(3,327)
Net increase/(decrease) in cash and cash equivalents		5,357	(33,194)
Cash and cash equivalents at 1 January		10,495	43,689
Cash and cash equivalents at 31 December	21 (b)	15,852	10,495

The accounting policies on pages 7 to 12 and notes on pages 17 to 40 are an integral part of these financial statements.

Gresham Insurance Company Limited

Notes to the financial statements

1. First time adoption of International Financial Reporting Standards

The Company has adopted International Financial Reporting Standards (IFRS) for these financial statements for the year ended 31 December 2005. In order to show comparative balances, the year ended 31 December 2004 is also shown under IFRS. The date of transition to IFRS is 1 January 2004.

In general, a company is required to determine its IFRS accounting policies and apply these retrospectively to determine its opening balance sheet under IFRS. However, International Financial Reporting Standard 1, First time adoption of International Financial Reporting Standards, (IFRS 1) allows a number of exemptions to this general principle upon adoption of IFRS. The Company has taken advantage of the following transitional arrangements.

Estimates

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

Transitional provisions

The Company has not taken advantage of the exemption within IFRS 1 that allows comparative information presented in the first year of adoption of IFRS not to comply with IAS 32, IAS 39 and IFRS 4. It has elected to disclose only five years of data in its loss development tables, as permitted by IFRS 4 in the year of adoption of IFRS. This will be increased in each succeeding additional year, until the full ten years of information is included.

The following tables show the effect of adopting IFRS on the statements that have previously been reported under the former basis for the year ended 31 December 2004.

(i) Reconciliation of equity previously reported under the former basis to equity reported under IFRS

	Note		As at 1 January 2004		As at 31 December 2004
			£000		£000
Equity as previously reported			61,400		61,400
Adjusted for:					
Insurance changes (note 1)		-		-	
Dividend recognition (note 2)		3,327		4,385	
			3,327		4,385
Deferred tax impact of above adjustments (note 3)			-		-
Equity as reported under IFRS			64,727		65,785

Gresham Insurance Company Limited
Notes to the financial statements (continued)

(ii) Reconciliation of profit and loss previously reported to profit and loss reported under IFRS

	For the year ended 31 December 2004
	£000
Profit for the year as previously reported	4,385
Profit for the year as reported under IFRS	4,385

Adjustments between reporting bases

The adjustments between reporting bases are as follows:

(1) Insurance changes	1 January 2004	31 December 2004
The increase in shareholder's funds from insurance changes is as follows:	**£000**	**£000**
Derecognition of equalisation provision, before tax	17,005	19,322
Crystallisation of commission liability, before tax	(17,005)	(19,322)
	-	-

An equalisation provision is recorded in the financial statements of individual general insurance companies in the United Kingdom and in a number of other countries, to eliminate or reduce the volatility in incurred claims arising from exceptional levels of claims in certain classes of business. The provision is required by law even though no actual liability exists at the balance sheet date and was included in the as previously reported balance sheet. The annual change in the equalisation provision was recorded in the profit and loss account. Under IFRS, no equalisation provision is reported as no actual liability exists at the balance sheet date. At 31 December 2004 there is an increase of £13,525 thousand of shareholder's funds as a result of the reclassification of the equalisation provision, net of attributable tax relief, (1 January 2004: £11,903 thousand).

The Company has an obligation to pay profit commission arising out of distributable profits prior to 31 March 2005 to Barclays Bank plc. As the equalisation reserve has been transferred to equity under IFRS a compensating adjustment has been made to establish this obligation to pay profit commission since the liabilities of the Company remain the same whether the equalisation reserve is a liability or equity.

(2) Dividend recognition

Under IFRS, the Company accounts for final dividends as a liability when they have been approved by shareholders. These financial statements have been adjusted where approval was obtained post year-end.

(ii) Reconciliation of profit and loss previously reported to profit and loss reported under IFRS (continued)

(3) Deferred tax

As previously reported, provision was made for deferred tax assets and liabilities, using the liability method, arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation. Deferred tax was recognised as a liability or asset if the transactions or events that gave the entity an obligation to pay more tax in future or a right to pay less tax in future had occurred by the balance sheet date. The Company's policy was to discount its deferred tax balances.

Under IAS 12 Income Taxes, deferred taxes are provided under the liability method for all relevant temporary differences, being the difference between the carrying amount of an asset or liability in the balance sheet and its value for tax purposes. Deferred tax assets are recognised for unused tax losses and other deductible temporary differences to the extent that it is probable that future taxable profit will be utilised against the unused tax losses and credits. Discounting is prohibited under IAS 12.

The changes to deferred tax arise from changes to the valuation of the Company's assets and liabilities under IFRS and presentational changes to disclosure of tax assets and liabilities. The main net increases in deferred tax at 1 January 2004 and 31 December 2004 that reduce shareholder's funds are:

The decrease in shareholder's funds is as follows:	1 January 2004	31 December 2004
	£000	£000
Deferred tax impact of the removal of the equalisation provision (refer note 1)	5,101	5,797
Deferred tax impact of the removal of commission liability (refer note 1)	(5,101)	(5,797)
	-	-

(4) Cash

At 31 December 2004, £10,545 thousands of the Company's investments meet the definition of cash equivalents and so have been reclassified to "cash and cash equivalents" (1 January 2004: £43,678 thousands).

Gresham Insurance Company Limited
Notes to the financial statements (continued)

2. Details of income

	2005	2004
	£000	£000
Premiums earned		
Gross written premiums	160,674	146,406
Less: premiums ceded to reinsurers	(5,709)	(8,985)
Gross change in provision for unearned premiums	(8,189)	(3,135)
Reinsurers' share of change in provision for unearned premiums	(6,261)	(283)
Net change in provision for unearned premiums	(14,450)	(3,418)
Net premiums earned	140,515	134,003
Fee and commission income		
Reinsurance commissions receivable	514	180
Other operating income	735	-
Total revenue	141,764	134,183
Net investment income		
Interest and similar income	6,563	7,253
Realised gains and losses	(836)	(962)
Unrealised gains and losses	2,162	(81)
Movement in amortised cost on debt securities	(946)	-
Gains/(Losses) on investments	380	(1,043)
Other investment expense	(69)	(134)
Net investment income	6,874	6,076
Total income	148,638	140,259

3. Details of expenses

	2005	2004
	£000	£000
Claims and benefits paid, net of recoveries from reinsurers		
Claims and benefits paid to policyholders	85,892	71,598
Less: Claim recoveries from reinsurers	(577)	(176)
	85,315	71,422
Change in insurance liabilities, net of reinsurance		
Change in insurance liabilities	1,817	10,409
Less: Change in reinsurance asset for insurance provisions	(4)	(56)
	1,813	10,353
Fee and commission expense		
Acquisition costs		
Commission expenses	47,738	56,049
Other acquisition costs for insurance	8,249	-
Change in deferred acquisition costs	6,645	(4,688)
	62,632	51,361
Other operating expenses	9,422	928
Total expenses	159,182	134,064

4. Analysis of investment return

Effective interest rates

The table below summarises the average effective interest rate by major currency for monetary financial instruments:

	2005	2004
	%	%
Monetary assets in British pounds		
Debt securities	4.7	5.4
Cash and cash equivalents	5.4	4.4

5. Employee information

Since 4 April 2005, all employees are employed by a fellow subsidiary undertaking of Aviva plc, Aviva Employment Services Limited. Disclosures relating to employees may be found in the consolidated accounts of Aviva plc.

Previously all staff had been employed by Legal & General Group plc.

Gresham Insurance Company Limited
Notes to the financial statements (continued)

6. Directors' emoluments

Since 4 April 2005, the emoluments of the executive directors have been borne by the parent undertaking, CGU International Insurance plc. Those of the non-executive director, Mr A Grace, have been borne by Barclays Bank plc.

Previously, emoluments of the directors were:-

	2005	2004
In respect of services as directors:	£ 000	£ 000
Aggregrate emoluments	13	49

Retirement benefits accrued to one (2004: one) director under a defined benefit pension scheme of Legal & General Group plc, the Company's former ultimate parent undertaking.

7. Auditors' remuneration

The remuneration of the auditors has been borne by the parent undertaking, CGU International Insurance plc for the 2005 financial year. Fees paid to the auditors in relation to the audit of the 2004 financial statements amounted to £27,500. Other fees for 2004 paid to the auditors amounted to £6,400.

8. Tax

(a) Tax charged to the income statement

	2005	2004
	£000	£000
Current tax:		
For this year	(9,933)	1,831
Prior year adjustments	38	-
Total current tax	(9,895)	1,831
Deferred tax:		
Origination and reversal of temporary differences	6,770	(21)
Prior year adjustments	(6)	-
Total deferred tax	6,764	(21)
Total tax (credited) / charged to income statement	(3,131)	1,810

(b) Tax reconciliation

The tax on the Company's profit / (loss) before tax differs from the theoretical amount that would arise using the tax rate in the United Kingdom as follows:

	2005	2004
	£000	£000
Profit/(loss) before tax	(10,544)	6,195
Tax calculated at standard UK corporation tax rate of 30% (2004: 30%)	(3,163)	1,859
Adjustment to tax charge in respect of prior years	32	-
Disallowable expenses	-	14
Other	-	(63)
Tax charged for the period (note 8a)	(3,131)	1,810

Gresham Insurance Company Limited
Notes to the financial statements (continued)

9. Dividends

	2005	2004
	£000	£000
Ordinary dividends declared and charged to equity in the year		
Final 2003 - 5.42p per share declared and paid in 2004	-	3,327
Final 2004 - 7.14p per share declared and paid in 2005	4,385	-
	4,385	3,327

10. Financial investments

(a) Financial investments comprised:

	Other than trading at fair value through profit or loss	
	2005	2004
	£000	£000
Debt securities		
UK Government - listed	117,367	113,918

Of the above total £115,651 (2004: £112,252) is expected to be recovered in more than one year after the balance sheet date.

(b) The following is a summary of the cost/amortised cost, gross unrealised gains and losses and fair value of financial investments:

				2005
	Cost/amortised cost	Unrealised gains	Unrealised losses	Fair value
	£000	£000	£000	£000
Debt securities	117,032	335	-	117,367

				2004
	Cost/amortised cost	Unrealised gains	Unrealised losses	Fair value
	£000	*£000*	*£000*	*£000*
Debt securities	115,706	-	(1,788)	113,918

Gresham Insurance Company Limited
Notes to the financial statements (continued)

11. Reinsurance

(a) Carrying amounts

The following is a summary of the reinsurance assets and related insurance reserves as at 31 December.

	2005			2004		
	Gross insurance provisions	Reinsurance assets	Net	Gross insurance provisions	Reinsurance assets	Net
	£000	£000	£000	£000	£000	£000
Outstanding claims provisions	45,411	132	45,279	33,791	128	33,663
Provisions for claims incurred but not reported	5,411	-	5,411	15,214	-	15,214
	50,822	132	50,690	49,005	128	48,877
Provision for unearned premiums	86,854	-	86,854	78,664	6,261	72,403
Total	137,676	132	137,544	127,669	6,389	121,280

(b) Assumptions

The assumptions used for reinsurance contracts follow those used for insurance contracts, shown in note 14 (c).

Reinsurance assets are valued net of any provisions for their recoverability.

(c) Movements

(i) Reinsurance asset

	2005	2004
	£000	£000
Carrying amount at 1 January	128	72
Reinsurers' share of claims losses and expenses incurred in current year	-	289
Reinsurers' share of claims losses and expenses incurred in prior years	581	(57)
Reinsurers' share of incurred claims losses and expenses	581	232
Less:		
Reinsurance recoveries received on claims incurred in current year	-	(161)
Reinsurance recoveries received on claims incurred in prior years	(577)	(15)
Reinsurance recoveries received in the year	(577)	(176)
Change in reinsurance asset recognised as income	4	56
Carrying amount at 31 December	132	128

(ii) Reinsurers' share of the provision for unearned premiums ("UPP")

	2005	2004
	£000	£000
Carrying amount at 1 January	6,261	6,544
Premiums ceded to reinsurers in the year	5,709	8,985
Less:		
Reinsurers' share of premiums earned during the year	11,970	9,268
Change in reinsurance asset recognised as income	(6,261)	(283)
Carrying amount at 31 December	-	6,261

12. Receivables and other financial assets

	2005 £000	2004 £000
Amounts due from insurance contract holders	74,257	-
Amounts due from intermediaries	16,969	61,993
Amounts due from reinsurers	471	-
Other financial assets	3,828	1,089
Total	95,525	63,082
Expected to be recovered in less than one year	95,525	63,082

Concentrations of credit risk with respect to receivables are limited due to the size and spread of the Company's trading base. No further credit risk provision is therefore required in excess of the normal provision for doubtful receivables.

13. Deferred acquisition costs

(a) The carrying amount comprised:

	2005 £000	2004 £000
Deferred acquisition costs	22,295	28,940

(b) The movements in deferred acquisition costs during the year were:

	2005 £000	2004 £000
Carrying amount at 1 January	28,940	24,252
Acquisition costs written during the year	52,367	53,732
Amortisation	(59,012)	(49,044)
Carrying amount at 31 December	22,295	28,940

Deferred acquisition costs are generally recoverable within one year of the balance sheet date.

Gresham Insurance Company Limited
Notes to the financial statements (continued)

14. Insurance liabilities

(a) Carrying amount

Gross insurance liabilities at 31 December comprised:

	2005 £000	2004 £000
Outstanding claims provisions	45,411	33,791
Provision for claims incurred but not reported	5,411	15,214
Technical provisions	50,822	49,005
Provision for unearned premiums	86,853	78,664
Total	137,675	127,669

(b) Provisions for outstanding claims

Significant delays occur in the notification and settlement of claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the balance sheet date. The reserves are based on information currently available. However, it is inherent in the nature of the business written that the ultimate liabilities may vary as a result of subsequent developments.

Provisions for outstanding claims are established to cover the outstanding expected ultimate liability for losses and loss adjustment expenses ("LAE") in respect of all claims that have already occurred. The provisions established cover reported claims and associated LAE, as well as claims incurred but not yet reported, and associated LAE.

Outstanding claims provisions are based on undiscounted estimates of future claim payments.

No equalisation or catastrophe reserves have been recognised. This treatment differs from the former basis and is explained in note 1 on the first time adoption of IFRS.

Gresham Insurance Company Limited
Notes to the financial statements (continued)

14. Insurance liabilities (continued)

(c) Assumptions

Outstanding claims provisions are estimated based on known facts at the date of estimation. Case estimates are generally set by skilled claims technicians applying their experience and knowledge to the circumstances of individual claims. The ultimate cost of outstanding claims is then estimated by using a range of standard actuarial claims projection techniques, such as the Chain Ladder and Bornhuetter-Ferguson methods. The main assumption underlying these techniques is that the Company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios.

Historical claims development is mainly analysed by accident period, although underwriting or notification period is also used where this is considered appropriate. Claims development by each line of business. Certain lines of business are also further analysed by claim type or type of coverage. In addition, large claims are usually separately assessed, either by being reserved at the face value of loss adjuster estimates, or separately projected in order to reflect their future development.

In most cases no explicit assumptions are made regarding future rates of claims inflation or loss ratios. Instead, the assumptions used are those implicit in the historic claims development data on which the projections are based. Additional qualitative judgement is used to assess the extent to which past trends may not apply in the future, for example, to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy conditions and loss adjustment procedures, in order to arrive at the estimated ultimate cost of claims.

(d) Movements

The following changes have occurred in the technical provisions during the year:

	2005 £000	2004 £000
Carrying amount at 1 January	49,005	38,596
Claims losses and expenses incurred in the current year	89,970	83,659
Decrease in estimated claims losses and expenses incurred in prior years	(2,261)	(1,652)
Incurred claims losses and expenses	87,709	82,007
Less:		
Payments made on claims incurred in the current year	56,663	50,397
Payments made on claims incurred in prior years	29,229	21,201
Claims payments made in the year, net of recoveries	85,892	71,598
Changes in claims provisions reserve recognised as an expense	1,817	10,409
Carrying amount at 31 December	50,822	49,005

14. Insurance liabilities (continued)

(e) Loss development tables

The table that follows presents the development of claim payments and the estimated ultimate cost of claims for the accident years 2001 to 2005. The upper half of the table shows the cumulative amounts paid during successive years related to each accident year. For example, with respect to the accident year 2001, by the end of 2005 £38,479 thousand had actually been paid in settlement of claims. In addition, as reflected in the lower section of the table, the original estimated ultimate cost of claims of £41,476 thousand was re-estimated to be £39,107 thousand at 31 December 2005. This decrease from the original estimate would generally be a combination of a number of factors, including claims being settled for larger or smaller amounts than originally estimated. The original estimates will also be increased or decreased, as more information becomes known about the individual claims and overall claim frequency and severity.

In the year of adoption of IFRS, only five years are required to be disclosed. This will be increased in each succeeding additional year, until ten years' information is included.

The Company aims to maintain strong reserves in order to protect against adverse future claim experience and development. As claims develop and the ultimate cost of claims become more certain, the absence of adverse claims experience will then result in a release of reserves from earlier accident years, as shown in the loss development tables below.

Accident Year	All prior years	2001	2002	2003	2004	2005	Total
	£000	£000	£000	£000	£000	£000	£000
Gross cumulative claim payments							
At end of accident year		(24,066)	(28,359)	(34,855)	(50,397)	(56,663)	
One year later		(35,395)	(43,293)	(51,772)	(74,060)		
Two years later		(37,190)	(45,150)	(55,754)			
Three years later		(38,005)	(46,007)				
Four years later		(38,479)					
Estimate of gross ultimate claims							
At end of accident year		41,476	46,334	64,253	83,659	89,970	
One year later		40,065	47,410	62,751	82,534		
Two years later		39,083	47,095	62,165			
Three years later		39,089	47,290				
Four years later		39,107					
Estimate of ultimate claims		39,107	47,290	62,165	82,534	89,970	
Cumulative payments		(38,479)	(46,007)	(55,754)	(74,060)	(56,663)	
Outstanding claims provisions recognised in the balance sheet	719	628	1,283	6,411	8,474	33,307	50,822

Gresham Insurance Company Limited
Notes to the financial statements (continued)

14. Insurance liabilities (continued)

(e) Loss development tables (continued)

After the effect of reinsurance, the loss development table is:

Accident Year	All prior years	2001	2002	2003	2004	2005	Total
	£000	*£000*	*£000*	*£000*	*£000*	*£000*	*£000*
Net cumulative claim payments							
At end of accident year		(24,066)	(28,359)	(34,855)	(50,236)	(56,663)	
One year later		(35,395)	(43,293)	(51,772)	(73,483)		
Two years later		(37,190)	(45,150)	(55,754)			
Three years later		(38,005)	(46,007)				
Four years later		(38,479)					
Estimate of net ultimate claims							
At end of accident year		41,476	46,334	64,253	83,370	89,970	
One year later		40,065	47,410	62,751	81,825		
Two years later		39,083	47,095	62,165			
Three years later		39,089	47,290				
Four years later		39,107					
Estimate of ultimate claims		39,107	47,290	62,165	81,825	89,970	
Cumulative payments		(38,479)	(46,007)	(55,754)	(73,483)	(56,663)	
Net outstanding claims provisions recognised in the balance sheet	719	628	1,283	6,411	8,342	33,307	50,690

(f) Provision for unearned premiums

Movements

The following changes have occurred in the provision for unearned premiums ("UPP") during the year:

	2005	2004
	£000	£000
Carrying amount at 1 January	78,664	75,529
Premiums written during the year	160,674	146,406
Less:		
Premiums earned during the year	(152,485)	(143,271)
Changes in year	*8,189*	*3,135*
Carrying amount at 31 December	86,853	78,664

Gresham Insurance Company Limited
Notes to the financial statements (continued)

15. Tax assets and liabilities

(a) General

Current tax assets and liabilities recoverable or payable in more than one year are £8,063 thousand and £nil (2004: £nil and £nil) respectively.

(b) Deferred taxes

(i) The balance at the period end comprises:	2005 £000	2004 £000
Temporary difference arising on other insurance items	(6,770)	(5,797)
Other temporary differences	12	5,803
Net deferred tax (liability)/asset	(6,758)	6

(ii) The movement in the net deferred tax (liability)/asset was as follows:

Net asset/(liability) at 1 January	6	(15)
Amounts (charged)/ credited to profit (note 8a)	(6,764)	21
Net (liability)/asset at 31 December	(6,758)	6

16. Payables and other financial liabilities

	2005 £000	2004 £000
Payables arising out of direct insurance and assumed reinsurance	10,259	14
Payables arising out of ceded reinsurance	1,969	3,944
Bank overdrafts	1,676	70
Other financial liabilities	45,960	24,854
	59,864	28,882
Expected to be settled within one year	59,864	28,882

The profit commission (included in other financial liabilities) is payable when the equalisation reserve within equity becomes distributable (see note 1 on page 18). The directors consider the book value approximates to fair value.

17. Other liabilities

	2005	2004
	£000	£000
Reinsurers' share of deferred acquisition costs	-	513
Other liabilities	6,256	412
	6,256	925
Expected to be settled within one year	6,256	925

18. Ordinary share capital

Details of the Company's ordinary share capital are as follows:

	2005	2004
	£000	£000
Authorised		
90,000,000 "A" Ordinary shares of £1 each	-	90,000
10,000,000 "B" Ordinary shares of £1 each	-	10,000
100,000,000 Ordinary shares of £1 each	100,000	-
	100,000	100,000
Allotted, called up and fully paid:		
55,260,000 "A" Ordinary shares of £1 each	-	55,260
6,140,000 "B" Ordinary shares of £1 each	-	6,140
61,400,000 Ordinary shares of £1 each	61,400	-
	61,400	61,400

As detailed in the Directors' Report, the share capital of the Company was re-classified, following the acquisition by CGU International Insurance plc.

19. Retained earnings

	2005	2004
	£000	£000
Balance at 1 January	4,385	3,327
(Loss)/profit for the year	(7,413)	4,385
Dividends (note 9)	(4,385)	(3,327)
Balance at 31 December	(7,413)	4,385

In accordance with accounting policy Q, retained earnings includes £22,567 thousand (2004: £19,322 thousand) relating to equalisation provisions, net of attributable tax relief which are not distributable.

20. Contingent liabilities and other risk factors

Uncertainty over claims provisions

Note 14 gives details of the estimation techniques used in determining the outstanding claims provisions which are designed to allow for prudence. These are estimated to give a result within the normal range of outcomes. To the extent that the ultimate cost falls outside this range, for example where future claims inflation differs from that expected, there is uncertainty in respect of this liability.

21. Cash flow statement

	2005 £000	2004 £000
(a) The reconciliation of (loss)/profit before tax to the net cash inflow from operating activities is:		
(Loss)/Profit before tax	(10,544)	6,195
Adjustments for:		
Fair value (gains)/ losses on investments (note 2)	(380)	1,043
Changes in working capital:		
Decrease in reinsurance assets	6,257	227
Decrease/(Increase) in deferred acquisition costs	6,645	(4,688)
Increase in receivables and other financial assets	(32,443)	(11,854)
Decrease in prepayments and accrued income	186	129
Increase in insurance liabilities	10,006	13,544
Increase in payables and other financial liabilities	29,376	4,772
Increase/(Decrease) in other liabilities	5,331	(516)
Net (purchases)/sales of operating assets:		
Financial investments	(3,069)	(35,059)
Net cash inflow/(outflow) from operating activities	11,365	(26,207)

Purchases and sales of financial investments are included in operating cash flows as the purchases are funded from cash flows associated with the orignation of insurance contracts, net of repayments of claims.

	2005 £000	2004 £000
(b) Cash and cash equivalents in the cash flow statement at 31 December comprised		
Cash at bank and in hand	228	20
Cash equivalents	17,300	10,545
	17,528	10,565
Bank overdrafts	(1,676)	(70)
	15,852	10,495

22. Risk management policies

(a) The Company's approach to financial risk and capital management

On 4 April 2005, the Company was acquired by CGU International Insurance plc. Since then the Company manages financial risk and capital within an overall risk and financial management framework operated by a group of companies (the NUI Group), within the Aviva plc group, that are engaged in writing general insurance business in the United Kingdom.

The primary objective of the NUI Group risk and financial management framework is to protect against events that hinder the sustainable achievement of the Company's performance objectives, including failing to exploit opportunities. The NUI Group recognises the critical importance of having efficient and effective risk management systems in place. To this end, the NUI Group has an established governance framework, including:-

- Clear terms of reference for the legal entity Boards and the associated executive management and other committees within the NUI Group:
- A clear organisational structure with documented delegated authorities and responsibilities from the legal entity Boards to executive management committees and senior management within the NUI Group and;
- Adoption of the Group policy framework which sets out risk appetite, risk management, control and business conduct standards for the Group's worldwide operations. Each policy has a member of senior management who is charged with overseeing compliance with the policy throughout the NUI Group.

This governance structure and policy set is regularly reviewed to reflect the changing commercial and regulatory requirement. For example, following the regulatory changes brought about by the FSA's Prudential Sourcebook, which came into effect on 1 January 2004, the NUI Group has placed a greater emphasis on assessment and documentation of risks and controls, including the development of an articulation of risk appetite. As a result the NUI Group has clearly articulated its risk appetite for financial risks (insurance, market, credit and liquidity risks) and where appropriate, non financial risks (operational, group and strategic risks).

The NUI Group has adopted Group established policies focusing on the management of financial and non-financial risks. The NUI Group also monitors risks on an ongoing basis and prepares quarterly reports identifying all material risks, along with information on likelihood, severity and mitigating actions taken or planned.

The NUI Group and the Company has developed a framework using the Internal Capital Assessment (ICA) principles for identifying the risks to which it is exposed, quantifying their impact on economic capital. The ICA estimates how much capital is needed to mitigate the risk of insolvency to a selected remote level of risk applied to a number of tests (both financial and non-financial) on the capital position of the business. The ICA works to a 99.5% confidence level of economic solvency over one year, in line with UK FSA regulatory requirements. The ICA combines the results of financial and operating experience tests. Although the ICA is an internal process, from 2005 the FSA can use ICA information in discussing the target capital levels it believes the Company must have available.

In addition, the NUI Group has developed a risk-based capital model for its businesses which provides a more detailed assessment of the economic capital needs of the business.

22. Risk management policies (continued)

The NUI Group also provides a Financial Condition Report (FCR) to inform decisions on capital management issues. The FCR is a medium term projection of the overall financial position of the business under a variety of economic and operating scenarios, allowing for new business. The FCR considers a number of key performance indicators in addition to solvency and capital requirements. The FCR enables the NUI Group to assess the range of risks to which the business is exposed, their evolution over time, and the impact of mitigating actions which might be taken.

(b) Management of financial and non-financial risks

General insurance risk
The NUI Group considers insurance risk within its general insurance activity to be comprised of the following:

- The assessment and pricing of risk,
- The adequacy of exposure management through the use of accumulation management techniques and reinsurance tools,
- Catastrophe risk,
- The management of claims, and
- The adequacy of reserving

The majority of the general insurance business underwritten by the Company is of a short tail nature such as motor and household insurances. The Group's underwriting strategy and appetite is agreed by the Group Executive Committee and communicated via specific policy statements and guidelines.

The vast majority of the Company's general insurance business is managed and priced within the same country as the domicile of the customer, predominantly in the United Kingdom.

The ICA framework is used to identify the risks to which the Company is exposed, quantifying their impact and calculating appropriate capital requirements. In due course risk-based capital (RBC) models will become the primary driver of ICA risk quantification. The NUI Group undertakes a quarterly review of its insurance risks, the output from which is a key input into the ICA and RBC assessments. The NUI Group has implemented Group policies for underwriting, claims, reinsurance and reserving.

The NUI Group has developed mechanisms which identify and manage accumulated insurance exposures to contain them within the limits of the appetite of the Group. The NUI Group has pioneered various developments, such as the Norwich Union Digital Flood Map to effectively manage exposure from specific perils.

22. Risk management policies (continued)

Reinsurance purchases are reviewed annually, to verify that the levels of protection being bought are commensurate with any developments in exposure and equate with the risk appetite of the NUI Group and the Company. The basis of these arrangements is underpinned by extensive financial modelling and actuarial analysis to optimise the cost and risk management benefits of these arrangements. This involves utilising externally sourced probablistic models to verify the accumulations and loss probabilites based on the Company's specific portfolios of business. Where external models are not available, scenarios are developed and tested using the Company's data to determine potential losses and appropriate levels of reinsurance protection. The reinsurance is placed with providers who meet the Group's counterparty security requirements.

Processes are in place to manage catastrophe risk. The Company purchases reinsurance to protect against significant natural hazard events such as a windstorm or flood event. For a single realistic catastrophic event the Company's maximum retention is approximately £25 million plus any losses in excess of £165 million.

Actuarial claims reserving is conducted by the NUI Group's actuaries in compliance with the Group General Insurance Reserving Policy and reviewed by the NUI Group's Reserving Committee. There are periodic external reviews by consultant actuaries.

Asset/liability management (ALM)

The Company has adopted Group policy on asset/liability management. The Company matches liabilities with appropriate assets for all classes of business in order to minimise the financial risk from mismatching of assets and liabilities as investment markets change. Application of the Group asset and liability framework covers a number of areas which are discussed in more detail below.

Liquidity risk

The Company has a strong liquidity position and through the application of a Group liquidity management policy seeks to ensure that it has sufficient financial resources available to meet its obligations as they fall due.

22. Risk management policies (continued)

The following table provides an analysis of investment into their relevant maturity groups based on the remaining period at the balance sheet date to their contractual maturities.

	Total	Within 1 year	1-5 years	5-15 years	Over 15 years
	£ 000	£ 000	£ 000	£ 000	£ 000
31 December 2005					
Debt securities	117,367	1,716	85,191	6,936	23,524
31 December 2004					
Debt securities	113,918	1,666	82,687	6,732	22,833

The following table shows the gross insurance liabilities analysed by duration.

	Total	Within 1 year	1-5 years	5-15 years	Over 15 years
	£ 000	£ 000	£ 000	£ 000	£ 000
31 December 2005					
Gross insurance liabilities	137,676	101,451	35,414	811	-
31 December 2004					
Gross insurance liabilities	127,669	94,291	31,763	1,615	-

Market risk

Market risk is the risk of adverse financial impact due to changes in fair values of financial instruments arising from fluctuations in interest rates. Market risk arises due to fluctuations in the value of insurance liabilities and the value of investments, including those backing shareholder's funds. The Company manages market risk within its ALM framework and within local regulatory constraints. For each of the major components of market risk, described in more detail below, the Company has put in place policies and procedures to set out how each risk should be managed and monitored, and the approach to setting an appropriate risk appetite.

The Company operates within the UK so has no material exposure to foreign exchange rates.

The fair value of the Company's investments and technical liabilities is exposed to potential fluctuations in interest rates. The Company ensures a close matching of assets and technical liabilities by duration to minimise this risk.

The Company has no derivatives.

22. Risk management policies (continued)

Credit risk

Credit risk is the risk of loss in the value of financial assets due to counterparties failing to meet all or part of their obligations.

The Company's management of credit risk is carried out in accordance with the NUI Group's Credit Risk Policy, which includes the monitoring of exposure levels and setting exposure limits in accordance with rating categories devised by credit rating agencies such as Standard & Poor's.

Financial assets are graded according to current credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. Financial assets which fall outside this range are classified as speculative grade. Credit limits for each counterparty are set based on default probabilities that are in turn based on the rating of the counterparty concerned.

The following table provides information regarding the aggregated credit risk exposure at 31 December 2005 of certain financial assets.

	Credit rating						
	AAA	AA	A	BBB	Speculative grade	Non-rated	Total
	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000
Debt securities	100,123	4,406	7,741	-	-	5,097	117,367

The Company is not individually exposed to significant concentrations of credit risk due to the regulations limiting investments in individual assets and classes. The aggregation of credit risk is monitored as above. The monitoring of reinsurance security is undertaken in conjunction with the Group reinsurance function.

At 31 December 2005, receivables are £99,144 thousand. Concentration of credit risk with respect to receivables are limited due to the size and spread of the Company's trading base. Exposure by counter-party is monitored for the NUI Group for all expenses greater that £20 million.

Operational risk

Operational risk arises as a result of inadequate or failed internal processes, people or systems, or from external events. Operational risks include, for example, IT infrastructure and systems, business interruption, information security, project, outsourcing, legal, fraud and compliance risks. As with other risk categories, line management of business areas have primary responsibility for how risks are assessed according to the potential impact and probability of the event concerned. These impact assessments are made against financial, operational and reputational criteria. Operational risks are reported, as with other risks, on a quarterly basis to Group.

Gresham Insurance Company Limited
Notes to the financial statements (continued)

22. Risk management policies (continued)

(c) Sensitivity analysis and capital management

The NUI Group uses a number of sensitivity test based risk management tools to understand the volatility of earnings, the volatility of its capital requirements, and to manage capital more efficiently. Primarily, the NUI Group uses financial condition reporting and increasingly ICA. However sensitivities to economic and operating experience are regularly produced on all of our key financial performance indicators (KPIs) as part of our decision making and planning processes and set the framework for identifying and quantifying the risks to which the NUI Group is exposed.

General insurance claim liabilities are estimated by using standard actuarial claims projection techniques. These methods extrapolate the claims development for each accident year based on the observed development of earlier years. In most cases, no explicit assumptions are made as projections are based on assumptions implicit in the historic claims development on which the projections are based. As such, in the analysis below, the sensitivity of general insurance claim liabilities is primarily based on the financial impact of changes to the reported loss ratio.

Some results of sensitivity testing for general insurance business are set out below. For each sensitivity test the impact of a change in a single factor is shown, with other assumptions left unchanged.

Sensitivity factor	Description of sensitivity factor applied
Interest rate & investment return	The impact of a change in market interest rates by +/- 1% (eg. If a current interest rate of 5%, the impact of an immediate change to 4% and 6%). The test allows consistently for similar changes to investment returns and movements in the market value of backing fixed securities.
Expenses	The impact of an increase in expenses by 10%.
Gross loss ratios	The impact of an increase in gross loss ratios for general insurance business by 5%.

The above sensitivity factors are applied using actuarial and statistical models, with the following pre-tax impacts on profit and shareholder's equity at 31 December 2005.

22. Risk management policies (continued)

General insurance business - impact on profit before tax

	Interest rates +1% £ 000	Interest rates -1% £ 000	Expenses +10% £ 000	Gross loss ratios +5% £ 000
Gross of reinsurance	(2,990)	2,990	(6,844)	(7,624)
Net of reinsurance	(2,990)	2,990	(6,844)	(7,624)

General insurance business - impact on shareholder's equity

	Interest rates +1% £ 000	Interest rates -1% £ 000	Expenses +10% £ 000	Gross loss ratios +5% £ 000
Gross of reinsurance	(2,093)	2,093	(4,790)	(5,337)
Net of reinsurance	(2,093)	2,093	(4,790)	(5,337)

Due to the importance of reinsurance for general insurance, the impact of the sensitivities on profit and equity are shown both gross and net of reinsurance. The impact of the expense sensitivity on profit also includes the increase in ongoing administration expenses, in addition to the increase in the loss adjustment expense provision.

The above table demonstrates the effect of a change in a key assumption whilst other assumptions remain unaffected. In reality, such an occurrence is unlikely, due to correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impact should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that assets and liabilities are actively managed and may vary at the time that any actual market movement occurs. For example, the Company's financial risk management strategy aims to manage the exposure to market fluctuations, including selling investments, changing investment portfolio allocation and taking other protective action, as investment markets move past various trigger levels.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Company's view of reasonably possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

23. Related party transactions

(a) The Company had the following related party transactions in 2005 and 2004.

The Company was a subsidiary undertaking of Legal & General Insurance Limited, a subsidary undertaking of Legal & General Group plc, throughout 2004 and until 31 March 2005. On this date, the entire shareholding in the Company of Legal & General Insurance Limited was acquired by a minority shareholder, Barclays Bank plc. On 4 April 2005, the entire share capital of the Company was transferred to CGU International Insurance plc, part of the Aviva plc group.

(i) Services provided by related parties

	2005		2004	
	Expense incurred in year	Payable at year end	Expense incurred in year	Payable at year end
	£000	£000	£000	£000
Parent	-	41,407	-	45
Fellow subsidiaries	20,784	-	309	86
	20,784	41,407	309	131

(ii) Services provided to related parties

	2005		2004	
	Income earned in year	Receivable at year end	Income earned in year	Receivable at year end
Fellow subsidiaries	-	267	-	10,122

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms.

(ii) Reinsurance arrangements
The Company paid premiums of £482 thousands to a fellow Group undertaking, Curepool Limited, in respect of reinsurance arrangements, in 2005.

(iii) Compensation to those employees classified as key management

The total compensation to those employees classified as key management, including the directors, is as follows:

	2005	2004
	£000	£000
Salary and other short-term benefits	2,985	49
Post-employment benefits	134	-
Equity compensation plans	1,216	-
Total	4,335	49

Compensation for key management for 2005, includes compensation for the directors and, for the period since 4 April 2005, compensation of management of the business unit within the Aviva plc group that has responsibility for managing the Company.

(b) Immediate parent undertaking

The Company's immediate parent undertaking is CGU International Insurance plc, registered in England.

(c) Ultimate controlling entity

The ultimate controlling entity is Aviva plc. Its Group Accounts are available on application to the Group Company Secretary, Aviva plc, St Helen's, 1 Undershaft, London EC3P 3DQ.