GRESHAM INSURANCE COMPANY LIMITED
ANNUAL REPORT AND FINANCIAL STATEMENTS
2012

Gresham Insurance Company Limited

Contents

Gresham Insurance Company Limited

Directors and officer

Directors:

C J Abrahams
P McNamara
A E Middle

Officer - Company Secretary:

R H Spicker
8 Surrey Street
Norwich
NR1 3NG

Auditor:

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
7 More London Riverside
London SE1 2RT

Registered office:

8 Surrey Street
Norwich
NR1 3NG

Company number:

Registered in England and Wales No 110410

Other information:

Gresham Insurance Company Limited ("the Company") is a member of the Association of British Insurers and the Financial Ombudsman Service, and is authorised and regulated by the Financial Services Authority ("FSA")

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

Gresham Insurance Company Limited

Registered in England and Wales: No. 110410

Directors' report

For the year ended 31 December 2012

The directors present their annual report and financial statements for the Company for the year ended 31 December 2012

Directors

The current directors and those in office during the year are as follows

C J Abrahams
P McNamara
A E Middle
A C Winslow resigned 26 November 2012

Principal activity

The principal activity of the Company is the transaction of general insurance business, predominantly household, in the United Kingdom ("UK") through a business arrangement with Barclays Bank plc

Business review

Financial position and performance

The financial position of the Company at 31 December 2012 is shown in the statement of financial position on page 16, with the results shown in the income statement on page 15 and the statement of cash flows on page 18

Premium decreased marginally in 2012, which is due to the continuing tough market conditions The gross combined operating ratio ("COR") worsened in 2012 The principal factor is higher claims costs Claims have worsened in 2012 due to adverse weather conditions, primarily due to the second wettest year on record and an increase in average cost and number of theft claims

Profit before tax for the year is £6 million (2011 £7 million) As described in note 21(a)(i), the Company has a 100% quota share reinsurance arrangement with its parent company, Aviva Insurance Limited The reduction in profit before tax is therefore due primarily to a reduction in non-underwriting profits, relating to commission revenue from successful customer introductions

Gresham Insurance Company Limited

Directors' report (continued)

Business review (continued)

Future outlook

The strategy of the Group ıs determıned by the board of Avıva plc and a summary of these are shown ın ıts financıal statements The strategy of the Company ıs to grow the household book vıa the exıstıng busıness arrangement wıth Barclays Bank plc The dırectors consıder that the Company's prıncıpal actıvıty wıll contınue unchanged ınto the foreseeable future

Prıncıpal rısks and uncertaıntıes

A descrıptıon of the prıncıpal rısks and uncertaıntıes facıng the Company and the Company's rısk management polıcıes are set out ın notes 17 and 19 to the financıal statements

Key performance ındıcators ("KPI")

The dırectors consıder that the Company's key performance ındıcators ("KPIs") that communıcate the financıal performance are as follows

- ıncrease/(decrease) ın gross wrıtten premıums, and
- combıned operatıng ratıo ("COR") - thıs comprıses the sum of the followıng ratıos
  - gross ıncurred claıms to gross earned premıums,
  - gross wrıtten commıssıon to gross wrıtten premıums, and
  - gross wrıtten expenses to gross wrıtten premıums

A summary of the KPIs ıs set out below

	2012	2011
Decrease ın gross wrıtten premıums	(3%)	(2%)
Combıned operatıng ratıo (before corporate costs)	94%	85%
Gross ıncurred claıms ratıo	56%	45%
Gross wrıtten commıssıon ratıo	27%	26%
Gross wrıtten expenses ratıo	11%	14%

The wrıtten expenses ratıo excludes corporate costs of £8 mıllıon (2011 £7 mıllıon)

Gresham Insurance Company Limited

Directors' report (continued)

Dividend

No interim dividend for the year was paid (2011 £8m) The directors do not recommend the payment of a final dividend for the financial year ending 31 December 2012 (2011 £nil)

Going concern

After making enquiries, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future For this reason, they continue to adopt the going concern basis in preparing the financial statements

Financial instruments

The business of the Company includes the use of financial instruments Details of the Company's risk management objectives, policies and exposures to risk relating to financial instruments are set out in note 19 to the financial statements

Employees

All staff are employed by a fellow subsidiary undertaking of Aviva plc, Aviva Employment Services Limited Disclosures relating to employees may be found in the annual report and financial statements of Aviva Employment Services Limited

Disclosure of information to the auditor

Each person who was a director of the Company on the date that this report was approved, confirms that

(a) so far as the director is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing their report, of which the auditor is unaware, and

(b) each director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the auditor is aware of that information

Auditor

Following a competitive tender by the company's ultimate parent company, Aviva plc, Pricewaterhouse Coopers LLP was appointed as auditor to the company, in accordance with the provisions of the Companies Act 2006

It is the intention of the directors to reappoint the auditor under the deemed appointment rules of section 487 of the Companies Act 2006

Directors' liabilities

Aviva plc, the Company's ultimate parent, 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, which continues to apply in relation to any provision made before 1 October 2007

This indemnity was granted in 2004 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 These qualifying third party indemnity provisions remain in force as at the date of approving the Directors' Report by virtue of paragraph 15, Schedule 3 of The Companies Act 2006 (Commencement No 3, Consequential Amendments, Transition Provisions and Savings) Order 2007

Gresham Insurance Company Limited

Directors' report (continued)

Statement of directors' responsibilities

The directors are responsible for preparing the Directors' report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable International Financial Reporting Standards (IFRSs) as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company with continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006 They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

By order of the Board 25 MARCH 2013

R H Spicker
Company Secretary

Gresham Insurance Company Limited

Independent auditor's report

To the members of Gresham Insurance Company Limited

We have audited the financial statements of Gresham Insurance Company Limited for the year ended 31 December 2012, which comprise the Accounting Policies, the Income Statement, the Statement of Changes in Equity, the Statement of Financial Position, the Statement of Cash Flows, and the related notes 1 to 21 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

Respective responsibilities of directors and auditor

As explained more fully in the Directors' responsibilities statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

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

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements In addition we read all the financial and non-financial information in the Annual Report & Financial Statements to identify material inconsistencies with the audited financial statements If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2012 and of its profit and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements

Gresham Insurance Company Limited

Independent auditor's report (continued)

To the members of Gresham Insurance Company Limited

Matters on which we are required to report by exception

We have nothing to report in respect of the following

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit

Lee Clarke

Lee Clarke (Senior statutory auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditor
25 March 2013

Gresham Insurance Company Limited

Accounting policies

The Company is a limited liability company incorporated and domiciled in Great Britain Its principal activity is the transaction of general insurance business in the UK

The principal accounting policies adopted in the preparation of these financial statements are set out below These policies have been consistently applied to all years presented, unless otherwise stated

(A) Basis of presentation

The financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU) In addition to fulfilling their legal obligation to comply with IFRS as adopted by the EU, the Company have also complied with IFRS as issued by the IASB and applicable at 31 December 2012 The financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through profit and loss

In accordance with IFRS 4, Insurance Contracts, the Company has applied existing accounting practices for insurance contracts, modified as appropriate to comply with the IFRS framework and applicable standards Further details are given in policy C below

New standards, interpretations and amendments to published standards that have been adopted by the Company

The Company has adopted the following new amendments to standards which became effective for financial years beginning on or after 1 January 2012 Neither of these amendments has a material impact on these financial statements
(i) Amendment to IFRS 7, Financial Instruments – Disclosures, relating to the transfer of financial assets
(ii Amendment to IAS 12, Income Taxes, relating to deferred tax

Standards, interpretations and amendments to published standards that are not yet effective and have not been adopted early by the Company

The following new standards, amendments to existing standards and interpretations that are relevant to the company have been issued They are not yet effective and have not been adopted by the Company

Effective for annual periods beginning on or after 1 January 2013

(i) Amendment to IFRS 7, Financial Instruments – Disclosures

The amendment includes enhanced disclosures to enable users of the financial statements to evaluate the effect or potential effect of netting arrangements in the statement of financial position The amendments will not have a significant impact for the Company The amendment has yet to be endorsed by the EU

Gresham Insurance Company Limited

Accounting policies (continued)

(A) Basis of presentation (continued)

(ii) IFRS 13, Fair Value Measurement

IFRS 13 replaces the guidance on fair value measurement in existing IFRS's with a single standard The standard does not include requirements regarding which items should be measured at fair value but provides guidance on how to determine fair value The standard also includes enhanced disclosures about fair value measurement The adoption of IFRS 13 is not expected to have a significant impact on the financial statements The standard has not yet been endorsed by the EU

(iii) Annual Improvements 2011

The Annual Improvements 2011 details amendments to five IFRSs, including IAS 1, Presentation of Financial Statements, IAS 32, Financial Statements – Presentation, and IAS 34, Interim Financial Reporting The amendments clarify existing guidance and do not give rise to a change in existing accounting practice There are no implications for the Company The amendments have been endorsed by the EU

Effective for annual periods beginning on or after 1 January 2014

Amendment to IAS 32, Financial Instruments – Presentation

The amendment to IAS 32 clarifies the requirements for offsetting financial assets and financial liabilities on the statement of financial position The impact of the adoption of the amendment has yet to be fully assessed but is not expected to have significant implications for the Company financial statements The amendment has not yet been endorsed by the EU

Effective for annual periods beginning on or after 1 January 2015

IFRS 9, Financial Instruments

IFRS 9 will replace IAS 39, Financial Instruments – Recognition and Measurement Under IFRS 9, all recognised financial assets that are currently within the scope of IAS 39 will be measured at either amortised cost or fair value The basis of classification will depend on the business model and the contractual cash flow characteristics of the financial asset All equity instruments will be at fair value A debt instrument is measured at amortised cost only if it is held to collect the contractual cash flows and the cash flows represent principal and interest, otherwise it is measured at fair value through profit and loss (FVTPL) Financial liabilities designated as at FVTPL, change in the fair value attributable to changes in the liability's credit risk are recognised in other comprehensive income unless it gives rise to an accounting mismatch in profit or loss

We have not yet completed our assessment of the impact of the adoption of IFRS 9 on the Company which, to a large extent, will need to take account of the interaction of the requirements of IFRS 9 with the IASB's insurance contracts accounting project The standard has not yet been endorsed by the EU

Other external reporting developments continue to be proactively monitored

The financial statements are stated in pounds sterling, which is the Company's functional and presentation currency Unless otherwise noted, the amounts shown in these financial statements are in millions of pounds sterling ("£m")

(B) Use of estimates

The preparation of financial statements requires the Company to make estimates and assumptions that affect items reported in the statement of financial position and income statement and the disclosure of contingent assets and liabilities at the date of the financial statements This is particularly so in the estimation of amounts for insurance liabilities, for which further details are given in policy G overleaf and in note 11 to these financial statements Although these estimates are based on management's best knowledge of current facts, circumstances and, to some extent, future events and actions, actual results ultimately may differ from those estimates, possibly significantly

Gresham Insurance Company Limited

Accounting policies (continued)

(C) Product classification

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

Accounting for insurance contracts, under IFRS 4, is determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers, the most recent version of which was issued in December 2005 and amended in December 2006

(D) Premiums earned

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 Premiums collected by intermediaries, but not yet received, are assessed based on estimates from underwriting or past experience, and are included in premiums written Unearned premiums are those proportions of the premiums written in a year that relate to periods of risk after the statement of financial position date

(E) Other operating income

Other operating income consists primarily of commission revenue for successful customer introductions, which is recognised when earned

(F) Net investment income

Investment income consists of interest for the year, movements in amortised cost on debt securities, realised gains and losses, and unrealised gains and losses on investments held at fair value through profit or loss ("FVPL") Interest income is recognised as it accrues, taking into account the effective yield on the investment

(G) Insurance contract liabilities

Claims

Insurance claims incurred include all losses occurring during the year, whether reported or not, 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 claims handling department and any part of the general administrative costs directly attributable to the loss adjustment function

Gresham Insurance Company Limited

Accounting policies (continued)

(G) Insurance contract liabilities (continued)

Outstanding claims provisions

Insurance outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the statement of financial position 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 statement of financial position date Any estimate represents a determination within a range of possible outcomes Further details of estimation techniques are given in note 11(c)

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

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 statement of financial position

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 statement of financial position

Gresham Insurance Company Limited

Accounting policies (continued)

(H) Reinsurance

The Company cedes reinsurance in the normal course of business The cost of reinsurance is earned over the risk profile 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 and investment contract liabilities Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying contract liabilities, 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 an impact that can be reliably measured on the amounts that the Company will receive from the reinsurer

(I) 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 statement of financial position 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)

(J) Deferred acquisition costs

Costs relating to the acquisition of new business for insurance and participating investment contracts are deferred in line with existing local accounting practices, to the extent that they are expected to be recovered out of future margins in revenues on these 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

(K) 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 that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value Such investments are those with less than three months' maturity from the date of acquisition, or which are redeemable on demand with only an insignificant change in their fair values For the purposes of the statement of cash flows, cash and cash equivalents also include bank overdrafts, which are included within payables and other financial liabilities in the statement of financial position

(L) Operating cash flows

Purchases and sales of loans and financial investments, and related investment income, are included within operating cash flows as the purchases are funded from cash flows associated with the origination of insurance contracts, net of payments of related claims During the year, the net operating cash outflow reflects a number of factors including the level of premium income and the timing of receipts of premiums and the payment of creditors, claims and surrenders It also includes changes in the size and value of consolidated cash investment funds

(M) Contingent liabilities

Contingent liabilities are disclosed if there is a possible future obligation as a result of a past event, or if there is a present obligation as a result of a past event but either a payment is not probable yet still possible or the amount cannot be reliably estimated

Gresham Insurance Company Limited

Accounting policies (continued)

(N) Income taxes

The current tax expense is based on the taxable results 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 rates enacted or substantively enacted at the statement of financial position 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

(O) Share capital and dividends

Equity instruments

An equity instrument is a contract that evidences a residual interest in the assets of an entity 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

Gresham Insurance Company Limited

Income statement
For the year ended 31 December 2012

	Note	2012	2011
		£m	£m
Income	1		
Gross written premiums		232	238
Premiums ceded to reinsurers		(230)	(236)
Premiums written and earned, net of reinsurance		2	2
Other operating income		4	7
		6	9
Expenses	2		
Claims paid, net of reinsurance		2	3
Change in claims provisions, net of reinsurance		(3)	(1)
Other operating expenses		1	-
		-	2
Profit before tax		6	7
Tax expense	6	(2)	(2)
Profit for the year		4	5

The Company has no recognised income and expenses other than that included in the results above and therefore a separate statement of comprehensive income has not been presented

The accounting policies on pages 8 to 14 and notes on pages 19 to 43 are an integral part of these financial statements

Gresham Insurance Company Limited

Statement of financial position
As at 31 December 2012

	Note	2012	2011
ASSETS		**£m**	**£m**
Reinsurance assets	8	197	185
Receivables	9	129	140
Deferred acquisition costs	10	36	34
Cash and cash equivalents	18(b)	23	22
Total assets		385	381
LIABILITIES			
Insurance liabilities	11	199	190
Current tax liabilities	12(a)	2	2
Payables and other financial liabilities	13	35	57
Other liabilities	14	68	55
Total liabilities		304	304
Net assets		81	77
EQUITY			
Ordinary share capital	15	61	61
Retained earnings	16	20	16
Total equity		81	77

The accounting policies on pages 8 to 14 and notes on pages 19 to 43 are an integral part of these financial statements

The financial statements on pages 8 to 43 were approved by the Board of Directors on 25 March 2013 and signed on its behalf by

C J Abrahams
Director

Gresham Insurance Company Limited

Statement of changes in equity
For the year ended 31 December 2012

	Note	Ordinary share capital	Retained earnings	Total equity
		£m	£m	£m
Balance at 1 January 2011		61	19	80
Total comprehensive income for the year		-	5	5
Dividend	7	-	(8)	(8)
Total movements in the year	16	-	(3)	(3)
Balance at 31 December 2011		61	16	77
Total comprehensive income for the year		-	4	4
Total movements in the year	16	-	4	4
Balance at 31 December 2012		61	20	81

The accounting policies on pages 8 to 14 and notes on pages 19 to 43 are an integral part of these financial statements

Gresham Insurance Company Limited

Statement of cash flows
For the year ended 31 December 2012

	Note	2012	2011
		£m	£m
Cash flows from operating activities			
Net cash inflow from/(outflow to) continuing operations	18(a)	5	(4)
Net cash generated by/(used in) operating activities		5	(4)
Net increase/(decrease) in cash and cash equivalents		5	(4)
Cash and cash equivalents at 1 January		15	19
Cash and cash equivalents at 31 December	18(b)	20	15

The accounting policies on pages 8 to 14 and notes on pages 19 to 43 are an integral part of these financial statements

Gresham Insurance Company Limited

Notes to the financial statements

1. Details of income

	2012	2011
	£m	£m
Premiums earned		
Gross written premiums	232	238
Less premiums ceded to reinsurers	(230)	(236)
Gross change in provision for unearned premiums	4	8
Reinsurers' share of change in provision for unearned premiums	(4)	(8)
Net change in provision for unearned premiums	-	-
Net earned premiums	2	2
Other operating income	4	7
Total income	6	9

2. Details of expenses

	2012	2011
	£m	£m
Claims paid, net of reinsurance		
Claims paid to policyholders	118	153
Less Claims recoveries from reinsurers	(116)	(150)
	2	3
Change in claims provisions, net of reinsurance		
Change in gross claims provisions	13	(43)
Change in reinsurance asset for claims provisions	(16)	42
	(3)	(1)
Other operating expense	1	-
Total expenses	-	2

The Company has no fee and commission expense or other operating expense net of reinsurance (with the exception of levy expenses) due to a 100% quota share reinsurance agreement

3. Employee information

All staff are employed by a fellow subsidiary undertaking of Aviva plc, Aviva Employment Services Limited, and a recharge is made to the Company Disclosures relating to employees may be found in the annual report and financial statements of Aviva Employment Services Limited

4. Directors

Mr Abrahams is remunerated for his role as a Director of Aviva Insurance Limited and his emoluments are disclosed in the financial statements of that entity Mr Abrahams is not remunerated directly for his services as a Director of this Company and the amount of time spent performing his duties is incidental to his role across the Group

Messrs Middle and Winslow are remunerated for their roles as employees across the Group They are not remunerated directly for their services as Directors of this Company and the amount of time spent performing their duties is incidental to their role across the Group

No cost is borne by the Company for these services

Mr McNamara is remunerated by a Company outside of the Group No recharge is made to the Company for his services

5. Auditor's remuneration

The total remuneration payable by the Company, excluding VAT, to its auditor, PricewaterhouseCoopers LLP and its associates (2011 Ernst and Young LLP), in respect of the audit of these financial statements, is shown below

	2012 £000	2011 £000
Fees payable to the Company's auditor for the audit of the Company's financial statements	36	60

Fees paid to PricewaterhouseCoopers LLP and its associates for services other than the statutory audit of the Company are not disclosed in these accounts since the consolidated accounts of the Company's parent company, Aviva plc (see note 21(c)), are required to disclose other (non-audit) services on a consolidated basis

Audit fees are paid by Aviva Central Services UK Limited, a fellow Group company, and recharged as appropriate to the Company and fellow Group companies

Gresham Insurance Company Limited

Notes to the financial statements (continued)

6. Tax

(a) Tax charged to the income statement

(i) The total tax charge comprises

	2012	2011
	£m	£m
Current tax:		
For this year	2	2
Total tax charged to income statement	2	2

(b) Tax reconciliation

The tax on the Company's profit before tax is equal to the amount that would be expected to arise using the tax rate in the UK as follows

	2012	2011
	£m	£m
Profit before tax	6	7
Tax charge calculated at standard UK corporation tax rate of 24 5% (2011 26 5%)	2	2
Tax charged for the period (note 6(a)(i))	2	2

The UK corporation tax rate reduced to 24% from 1 April 2012 A subsequent reduction in the UK corporation tax rate to 23% was substantively enacted on 3 July 2012 and will apply from 1 April 2013 The substantively enacted rate of 23% has been used in the calculation of the UK's deferred tax liabilities

As announced in the 2012 Autumn Statement, the rate is expected to reduce further to 21% from 1 April 2014 The impact on the company's net assets from the further 2% reduction in the rate from 23% to 21% is not material

Gresham Insurance Company Limited

Notes to the financial statements (continued)

7. Dividends

	2012 £m	2011 £m
Ordinary dividends declared and charged to equity in the year		
Interim 2011 - 13 029p per share paid in November 2011	-	8

The 2011 dividend was settled by a reduction in the intercompany receivable due from the then immediate parent company, Aviva International Insurance Limited.

8. Reinsurance assets

(a) Carrying amounts

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

	2012			2011		
	Gross insurance liabilities £m	Reinsurance assets £m	Net £m	Gross insurance liabilities £m	Reinsurance assets £m	Net £m
Outstanding claims provisions	72	70	2	59	54	5
Provisions for claims incurred but not reported	6	6	-	6	6	-
	78	76	2	65	60	5
Provision for unearned premiums	121	121	-	125	125	-
Total	199	197	2	190	185	5

Of the above total, £63 million (2011 £47 million) of the reinsurance assets is expected to be recovered in more than one year after the statement of financial position date

The reinsurers' share of outstanding claims provisions and provisions for claims incurred but not reported is reduced by £1 million (2011 £nil) as a result of the discounting of structured settlements

(b) Assumptions

The assumptions used for reinsurance contracts follow those used for insurance contracts, shown in note 11(c)

Reinsurance assets are valued net of any provisions for their recoverability

Notes to the financial statements (continued)

8. Reinsurance assets (continued)

(c) Movements

(i) Reinsurers' share of claims provisions	2012	2011
	£m	£m
Carrying amount at 1 January	60	102
Reinsurers' share of claims losses and expenses incurred in current year	128	107
Reinsurers' share of claims losses and expenses incurred in prior years	4	1
Reinsurers' share of incurred claims losses and expenses	132	108
Less		
Reinsurance recoveries received on claims incurred in current year	(76)	(72)
Reinsurance recoveries received on claims incurred in prior years	(40)	(78)
Reinsurance recoveries received in the year	(116)	(150)
Change in reinsurance asset	16	(42)
Carrying amount at 31 December	76	60

(ii) Reinsurers' share of the provision for unearned premiums	2012	2011
	£m	£m
Carrying amount at 1 January	125	133
Premiums ceded to reinsurers in the year	230	236
Less		
Reinsurers' share of premiums earned during the year	(234)	(244)
Change in reinsurance asset	(4)	(8)
Carrying amount at 31 December	121	125

9. Receivables

	2012	2011
	£m	£m
Amounts due from insurance contract holders	123	130
Amounts due from reinsurers	-	8
Amounts due from related parties (note 21(a)(iii))	6	-
Other receivables	-	2
Total	129	140
Expected to be recovered in less than one year	129	140

All receivables are carried at amortised cost, which approximates to fair value

Gresham Insurance Company Limited

Notes to the financial statements (continued)

10. Deferred acquisition costs

The movements in deferred acquisition costs during the year are

	2012	2011
	£m	£m
Carrying amount at 1 January	34	35
Acquisition costs written during the year, gross of reinsurance	84	79
Amortisation	(82)	(80)
Carrying amount at 31 December	36	34

Deferred acquisition costs are generally amortised within one year of the statement of financial position date

11. Insurance liabilities

(a) Carrying amount

Gross insurance liabilities at 31 December comprise

	2012	2011
	£m	£m
Provisions for outstanding claims	72	59
Provisions for claims incurred but not reported	6	6
	78	65
Provision for unearned premiums	121	125
Total	199	190

(b) Provisions for outstanding claims

Delays occur in the notification and settlement of claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the statement of financial position 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

Gresham Insurance Company Limited

Notes to the financial statements (continued)

11. Insurance liabilities (continued)

(b) Provisions for outstanding claims (continued)

Outstanding claims provisions are based on undiscounted estimates of future claims payments, except for the following classes of business for which discounted provisions are held

	Discount rate	Mean term of liabilities
	2012	2012
Structured settlements	0 57% - 3 33%	27

During 2012, the first bodily injury claim to be settled by a periodic payment order (PPO) by the Company, was awarded by the Courts PPOs are reserved for on a discounted basis The period of time which will elapse before the liability is settled has been estimated by modelling the settlement pattern of the underlying claim The gross outstanding claims provisions before discounting are £79 million

Loss reserves are only established for losses that have already occurred

(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, taking into account all available information and correspondence regarding the circumstances of the claim, such as medical reports, investigations and inspections Claims technicians set case estimates according to documented claims department policies and specialise in setting estimates for certain lines of business or types of claim Claims above certain limits are referred to senior claims handlers for authorisation

No adjustments are made to the claims technicians' case estimates included in booked claims provisions, except for rare occasions when the estimated ultimate cost of a large or unusual claim may be adjusted, subject to internal reserve committee approval, to allow for uncertainty regarding, for example, the outcome of a court case 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 claims 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 is separately analysed by each line of business Certain lines of business are also further analysed by claims type or type of coverage In addition, large claims are usually separately assessed, either by being reserved at the face value of loss adjusted 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, that represent the most likely outcome, from the range of possible outcomes, taking account of all the uncertainties involved The range of possible outcomes does not, however, result in the quantification of a reserve range Where discount rate assumptions are based on current market yields on fixed interest securities, allowance is made for default risk implicit in the yields on the underlying assets

Gresham Insurance Company Limited

Notes to the financial statements (continued)

11. Insurance liabilities (continued)

(d) Movements

The followmg changes have occurred in the claims provisions during the year

	2012 £m	2011 £m
Carrying amount at 1 January	65	108
Claims losses and expenses incurred related to the current year	128	107
Claims losses and expenses incurred related to prior years	3	3
Incurred claims losses and expenses	131	110
Less		
Payments made on claims incurred in the current year	(76)	(72)
Payments made on claims incurred in prior years	(42)	(81)
Claims payments made in the year	(118)	(153)
Change in gross claims	13	(43)
Carrying amount at 31 December	78	65

Effect of changes in estimates during the year

During the year, gross prior years' claims provisions of £3 million (£1 million credit net of reinsurance) were charged to the income statement (2011 £3 million, £2 million net of reinsurance) The main reason is the reassessment of the levels of provision for household and motor claims

(e) Loss development tables

The table that follows presents the development of claims payments and the estimated ultimate cost of claims for the accident years 2003 to 2012 The upper half of the table shows the cumulative amounts paid during successive years relating to each accident year For example, with respect to the accident year 2003, by the end of 2012 £61 million had actually been paid in settlement of claims In addition, as reflected in the lower section of the table, the original estimated ultimate cost of claims of £64 million was re-estimated to be £61 million at 31 December 2012 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 claims frequency and severity patterns

The Company aims to maintain prudent reserves in order to protect against adverse future claims experience and development As claims develop and the ultimate cost of claims becomes more certain, the absence of adverse claims experience will generally result in a release of reserves from earlier accident years However, in order to maintain strong reserves, the Company transfers some of this release to current accident year reserves where the development of claims is less mature and there is much greater uncertainty attaching to the ultimate cost of claims

Notes to the financial statements (continued)

11. Insurance liabilities (continued)

(e) Loss development tables (continued)

Accident Year	Prior years	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Gross cumulative claims payments												
At end of accident year		(35)	(50)	(57)	(83)	(150)	(113)	(99)	(81)	(72)	(76)	
One year later		(52)	(74)	(94)	(151)	(233)	(169)	(145)	(145)	(97)		
Two years later		(56)	(79)	(101)	(159)	(246)	(175)	(150)	(152)			
Three years later		(58)	(82)	(105)	(161)	(250)	(179)	(153)				
Four years later		(60)	(82)	(105)	(164)	(254)	(181)					
Five years later		(60)	(83)	(105)	(166)	(256)						
Six years later		(60)	(84)	(106)	(168)							
Seven years later		(60)	(84)	(107)								
Eight years later		(61)	(84)									
Nine years later		(61)										
Estimate of gross ultimate claims												
At end of accident year		64	84	90	138	239	182	166	153	107	128	
One year later		63	83	101	162	247	181	156	152	101		
Two years later		62	82	104	167	255	182	155	155			
Three years later		61	84	107	168	257	183	156				
Four years later		62	84	107	169	261	184					
Five years later		61	85	109	169	262						
Six years later		61	85	109	171							
Seven years later		61	85	111								
Eight years later		61	85									
Nine years later		61										
Estimate of ultimate claims		61	85	111	171	262	184	156	155	101	128	
Cumulative payments		(61)	(84)	(107)	(168)	(256)	(181)	(153)	(152)	(97)	(76)	
Undiscounted gross outstanding claims provisions	-	-	1	4	3	6	3	3	3	4	52	79
Effect of discounting	-	-	-	(1)	-	-	-	-	-	-	-	(1)
Discounted gross outstanding claims provisions recognised in the statement of financial position	-	-	1	3	3	6	3	3	3	4	52	78

Gresham Insurance Company Limited

Notes to the financial statements (continued)

11. Insurance liabilities (continued)

(e) Loss development tables (continued)

After the effect of reinsurance, the loss development table is

Accident Year	Prior years	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Net cumulative claims payments												
At end of accident year		(35)	(50)	(57)	(46)	-	-	-	-	-	-	
One year later		(52)	(73)	(94)	(51)	-	-	-	-	-		
Two years later		(56)	(78)	(101)	(52)	-	-	-	-			
Three years later		(58)	(81)	(103)	(55)	-	-	-				
Four years later		(60)	(82)	(103)	(57)	-	-					
Five years later		(60)	(82)	(103)	(58)	-						
Six years later		(60)	(82)	(104)	(59)							
Seven years later		(60)	(82)	(106)								
Eight years later		(61)	(82)									
Nine years later		(61)										
Estimate of net ultimate claims												
At end of accident year		64	83	90	61	-	-	-	-	-	-	
One year later		63	82	100	59	-	-	-	-	-		
Two years later		62	82	104	59	-	-	-	-			
Three years later		61	83	104	59	-	-	-				
Four years later		62	83	105	57	-	-					
Five years later		61	83	107	59	-						
Six years later		61	83	107	59							
Seven years later		61	83	107								
Eight years later		61	83									
Nine years later		61										
Estimate of ultimate claims		61	83	107	59	-	-	-	-	-	-	
Cumulative payments		(61)	(82)	(106)	(59)	-	-	-	-	-	-	
Net outstanding claims provisions recognised in the statement of financial position	-	-	1	1	-	-	-	-	-	-	-	2

Gresham Insurance Company Limited

Notes to the financial statements (continued)

11. Insurance liabilities (continued)

(f). Provision for unearned premiums

The following changes have occurred in the provision for unearned premiums during the year

	2012	2011
	£m	£m
Carrying amount at 1 January	125	133
Premiums written during the year	232	238
Less Premiums earned during the year	(236)	(246)
Change in year	(4)	(8)
Carrying amount at 31 December	121	125

12. Tax assets and liabilities

(a) Current tax

	2012	2011
	£m	£m
Tax liability		
Expected to be payable in more than one year	2	2
Tax liability recognised in statement of financial position	2	2

Liabilities for prior years' tax settled by group relief of £2 million (2011 £3 million) are included within payables and other financial liabilities (note 13) and within the related party transactions (note 21(a)(iii)) and are payable in less than one year

Gresham Insurance Company Limited

Notes to the financial statements (continued)

13. Payables and other financial liabilities

	2012	2011
	£m	£m
Payables arising out of direct insurance and assumed reinsurance	1	1
Reinsurance creditors	14	-
Bank overdrafts (note 18(b))	3	7
Amounts due to related parties (note 21(a)(iii))	-	37
Other financial liabilities	17	12
Total	35	57
Expected to be settled within one year	35	57

All payables and other financial liabilities are carried at amortised cost, which approximates to fair value

14. Other liabilities

	2012	2011
	£m	£m
Reinsurers' share of deferred acquisition costs	36	34
Deferred income	1	4
Accruals	31	17
Total	68	55
Expected to be settled within one year	68	55

Gresham Insurance Company Limited

Notes to the financial statements (continued)

15. Ordinary share capital

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

	2012	2011
	£m	£m
Authorised		
100,000,000 (2010 100,000,000) Ordinary shares of £1 each	100	100
Allotted, called up and fully paid		
61,400,000 (2010 61,400,000) Ordinary shares of £1 each	61	61

16. Retained earnings

	2012	2011
	£m	£m
Balance at 1 January	16	19
Profit for the year	4	5
Dividend	-	(8)
Balance at 31 December	20	16

17. Contingent liabilities and other risk factors

Uncertainty over claims provisions

Note 11(c) 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

Levy schemes

The Company pays contributions into levy schemes in the UK in which it operates Given the economic environment, there is a heightened risk that the levy contributions will need to be increased to protect policyholders if an insurance company falls into financial difficulties The directors continue to monitor the situation but are not aware of any need to increase provisions at the statement of financial position date

Gresham Insurance Company Limited

Notes to the financial statements (continued)

18. Statement of cash flows

	2012	2011
	£m	£m
(a) The reconciliation of profit before tax to the net cash inflow from/(outflow to) operating activities is:		
Profit before tax	6	7
Adjustments for		
Changes in working capital		
(Increase)/decrease in reinsurance assets	(12)	50
(Increase)/decrease in deferred acquisition costs	(2)	1
(Increase)/decrease in receivables	11	(15)
(Increase)/decrease in prepayments and accrued income	-	1
Increase/(decrease) in insurance liabilities	9	(51)
Increase/(decrease) in payables and other financial liabilities	(20)	(7)
Increase/(decrease) in other liabilities	13	10
Net cash inflow from/(outflow to) operating activities	5	(4)

Increase/(decrease) in payables and other financial liabilities" is stated after eliminating £2 million (2011 £3 million) of corporation tax settled or to be settled by group relief

	2012	2011
(b) Cash and cash equivalents in the statement of cash flows at 31 December comprise:	£m	£m
Cash equivalents	23	22
Bank overdrafts (note 13)	(3)	(7)
	20	15

Notes to the financial statements (continued)

19. Risk management

The ultimate parent company, Aviva plc, and its subsidiaries, joint ventures and associates, collectively known as "the Group", operate a risk management framework ("RMF"), which is the collection of processes and tools that have been put in place to ensure that the risks to which it is exposed are identified, measured, managed, monitored and reported on a continuous basis The RMF is designed to facilitate a common approach to, and language regarding, the management of risk across the Group The key instruments of the RMF include the risk management policies, risk reports, risk models, the governance and oversight infrastructure and the risk appetite framework The RMF has been adopted in the Aviva businesses collectively referred to as "UK&I GI" (including this company and the UK and Ireland general insurance businesses carried out primarily within Aviva Insurance Limited)

Risks are grouped by risk type market, credit, general insurance, liquidity and operational risk Risk falling within these types may affect a number of key metrics including those relating to strength within the statement of financial position, liquidity and profit They may affect the performance of the products that the Company delivers to customers and the service to customers and distributors, which can be categorised as risks to the Company's franchise

The Group has a set of formal risk policies that facilitate a consistent approach to the management of all the Group's risks across all businesses and locations in which the Group operates These risk policies define the Group's appetite for different, specific risk types and set out risk management and control standards for the Group's worldwide operations

UK&I GI sets limits to manage material risks to ensure the risks stay within risk appetite (the amount of risk UK&I GI is willing to accept) UK&I GI assesses the size and scale of a risk by considering how likely it is that the risk will materialise and the potential impact the risk could have on its business customers and other stakeholders Where risks are outside of appetite, actions are agreed to mitigate the exposure Impact assessments are considered against financial, operational and reputational criteria and take into account underlying factors such as economic conditions, for example, UK economic growth and inflation

UK&I GI has an established governance framework, which has the following key elements

- defined terms of reference for the legal entity Boards and the associated Board and management committees,
- a clear organisational structure with documented delegated authorities and responsibilities from the legal entity Boards to management, and
- adoption of the Group risk management framework that defines risk appetite measures and sets out risk management and control standards for the Group's worldwide operations The risk management framework also set out the roles and responsibilities of businesses, policy owners, and risk oversight committees

UK&I GI operates a three lines of defence risk management model Primary responsibility for risk identification and management lies with business management (the first line of defence) Support for and challenge on the completeness and accuracy of risk assessment, risk reporting and adequacy of mitigation plans are performed by specialist risk functions (the second line of defence) Independent and objective assurance on the robustness of the risk management framework and the appropriateness and effectiveness of internal control is provided by Internal Audit (the third line of defence)

Notes to the financial statements (continued)

19. Risk management (continued)

Risk models are an important tool in UK&I GI's measurement of risk and are used to support the monitoring and reporting of the risk profile and in the evaluation of alternative risk management actions UK&I GI carries out a range of stress (where one risk factor is assumed to vary) and scenario (where combinations of risk factors are assumed to vary) tests to evaluate their impact on the business and the management actions available to respond to the conditions envisaged Monthly assessments are made of the economic capital available within the business and the economic capital required to cover the current risk profile of the business and these assessments are included in the regular reporting to the appropriate committees

In addition to monitoring regulatory solvency under applicable FSA regulations, the FSA also requires UK&I GI to assess its economic capital requirements to ensure that it adequately reflects the risks facing the business

UK&I GI has developed economic capital models that support the measurement, comparison and further understanding of its risks The results of the modelling are incorporated into key strategic planning and decision-making processes These models show the relative impact to economic capital from the risks faced In turn this supports the assessment of appropriate and effective mitigating strategies where risks are outside of agreed risk limits

(a) Financial risk management

(i) Market risk

Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments due to fluctuations in interest rates, equity prices, property prices and foreign currency exchange rates Market risk arises due to fluctuations in both the value of liabilities and the value of investments held

UK&I GI manages market risk locally within its market risk framework, within local regulatory constraints and in line with established Group policy, including minimum principles for matching liabilities with appropriate assets

Interest rate risk arises primarily from the Company's investments, which are exposed to fluctuations in interest rates UK&I GI maintains a close matching of assets and the economic value of its technical liabilities, by duration, using derivative instruments if necessary, to minimise this risk

The Company operates predominantly within the UK and there is no material exposure to foreign currency exchange rates

Derivatives are used within policy guidelines agreed by the Aviva plc Board of Directors Derivatives are only used for efficient portfolio management or risk hedging purposes The Company did not have any derivatives during the year or at the year-end

The management of market risk is overseen by the UK&I GI Asset Liability Committee

(ii) 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 UK&I GI's management of credit risk is carried out in accordance with Group credit risk processes, which include setting exposure limits and monitoring exposures in accordance with ratings set by credit ratings agencies such as Standard & Poor's Exposure levels are reported to, and reviewed by, the UK&I GI Asset Liability Committee

Gresham Insurance Company Limited

Notes to the financial statements (continued)

19. Risk management (continued)

(a) Financial risk management (continued)

(ii) Credit risk (continued)

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 and the type of exposure

The following table provides information regarding the aggregated credit risk exposure of the Company "Non-rated" captures assets not rated by external ratings agencies

	Credit rating						
31 December 2012	**AAA**	**AA**	**A**	**BBB**	**Speculative grade**	**Non-rated**	**Carrying value in the statement of financial position**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Reinsurance assets	-	-	197	-	-	-	197
Cash and cash equivalents	-	7	16	-	-	-	23

	Credit rating						
31 December 2011	**AAA**	**AA**	**A**	**BBB**	**Speculative grade**	**Non-rated**	**Carrying value in the statement of financial position**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Reinsurance assets	-	185	-	-	-	-	185
Cash and cash equivalents	-	1	21	-	-	-	22

The Company is not generally exposed to significant concentrations of credit risk to third parties

The management of credit risk is overseen by the UK&I GI Asset Liability Committee

UK&I GI manages exposure to reinsurance counterparties in accordance with Group policy Exposure limits are set by Aviva Group Centre which maintains a list of reinsurers that have acceptable credit standing Reinsurer exposure and the impact of any reinsurer default are monitored regularly by the Group Asset Liability Committee

The Company has a significant exposure to its parent company, Aviva Insurance Limited, arising from the quota share reinsurance agreement transferred from Aviva International Insurance Limited on 14 November 2011 Further details are set out in note 21 on related party transactions

Reinsurance assets of £197 million (2011 £185 million) are neither past due nor impaired

At 31 December 2012, receivables are £129 million (2011 £140 million)

Gresham Insurance Company Limited

Notes to the financial statements (continued)

19. Risk management (continued)

(a) Financial risk management (continued)

(iii) General insurance risk

UK&I GI considers insurance risk within its general insurance activity to comprise

- fluctuations in the timing, frequency and severity of insured events, relative to expectations when the business was underwritten This includes inaccurate pricing and selection of risks, unexpected claims arising from a single source and inadequate reinsurance protection or other risk transfer techniques,
- fluctuations in the timing and amount of claims settlements This includes the risk of inadequate reserves

The majority of the general insurance business underwritten by the Company is of a short-tail nature such as household insurance

The Group's underwriting strategy and appetite is agreed by the Aviva Group Executive Committee and communicated via specific policy statements and guidelines UK&I GI sets its own underwriting strategy, consistent with the Group strategy Underwriting strategy is communicated to underwriters, with underwriting licences granted to individual underwriters according to competence and experience The vast majority of the Company's general insurance business is managed and priced in the same country as the domicile of the customer, predominantly in the UK

UK&I GI has developed mechanisms that identify, quantify and manage accumulated exposures to contain them within the limits of the appetite of UK&I GI UK&I GI has in place various methodologies to manage effectively exposures arising from specific perils UK&I GI analyses accumulations of insurance risk under various headings, including type of business, location, profile of customers and type of claim and uses these analyses to inform underwriting and reserving

Reinsurance purchases are reviewed to verify that the levels of protection being bought reflect any developments in exposure and the risk appetite of UK&I GI The basis of these purchases is underpinned by extensive financial and capital modelling and actuarial analyses which consider the cost and capital efficiency benefits This involves utilising externally sourced probabilistic models to verify the accumulations and loss probabilities based on UK&I GI's specific portfolios of business In addition to external models, scenarios are developed and tested using UK&I GI's data to determine potential losses and appropriate levels of reinsurance protection Reinsurance covers single large exposures and concentrations of exposures UK&I GI has processes in place to manage catastrophe risk It purchases catastrophe reinsurance to protect against significant natural hazard events

The adequacy of UK&I GI's general insurance claims provisions is overseen by the UK&I GI Reserve Committee Actuarial claims reserving is conducted by UK&I GI's actuaries, with periodic independent external reviews by consulting actuaries

Risk-based capital models are being used to support the quantification of risk under the Individual Capital Assessment ("ICA") framework UK&I GI undertakes a quarterly review of insurance risks, the output from which is a key input into the ICA and risk-based capital assessments

The management of insurance risk is overseen by specific UK&I GI senior management committees, namely the Underwriting Pricing and Costing Committee, the Reserve Committee and the Projections Committee

Gresham Insurance Company Limited

Notes to the financial statements (continued)

19. Risk management (continued)

(a) Financial risk management (continued)

(iv) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations as they fall due

UK&I GI has set its investment strategy to ensure it has sufficient liquid funds to meet its expected obligations on an expected basis and under adverse circumstances In extreme circumstances, the Company would approach the Group for additional short-term borrowing whilst the Company liquidated other assets The Group maintains significant committed borrowing facilities from a range of highly rated banks to mitigate this risk further

The following table provides an analysis, by maturity date of the principal, of the carrying value of financial assets and reinsurers' share of the unearned premium provision which are available to fund the repayment of liabilities as they crystallise

31 December 2012	Within 1 year	1 to 5 years	5 to 15 years	Over 15 years	Total
	£m	£m	£m	£m	£m
Reinsurers' share of claims provisions	41	32	3	-	76
Reinsurers' share of unearned premium provision	93	27	1	-	121
Receivables	129	-	-	-	129
Cash and cash equivalents	23	-	-	-	23
	286	59	4	-	349

31 December 2011	Within 1 year	1 to 5 years	5 to 15 years	Over 15 years	Total
	£m	£m	£m	£m	£m
Reinsurers' share of claims provisions	35	23	2	-	60
Reinsurers' share of unearned premium provision	103	21	1	-	125
Receivables	140	-	-	-	140
Cash and cash equivalents	22	-	-	-	22
	300	44	3	-	347

The assets above are analysed in accordance with the earliest possible redemption date of the instrument at the initiation of the Company

The following table shows the Company's financial liabilities and the provision for unearned premiums analysed by duration

31 December 2012	Within 1 year	1 to 5 years	5 to 15 years	Over 15 years	Total
	£m	£m	£m	£m	£m
Provisions for outstanding claims	42	33	3	-	78
Provision for unearned premiums	93	27	1	-	121
Payables and other financial liabilities	35	-	-	-	35
	170	60	4	-	234

31 December 2011	Within 1 year	1 to 5 years	5 to 15 years	Over 15 years	Total
	£m	£m	£m	£m	£m
Provisions for outstanding claims	40	23	2	-	65
Provision for unearned premiums	103	21	1	-	125
Payables and other financial liabilities	57	-	-	-	57
	200	44	3	-	247

For insurance contracts, the analysis of liabilities above is based on the estimated timing of future cash flows, in respect of claims incurred and unearned premiums

The management of liquidity risk is overseen by the UK&I GI Asset Liability Committee

Gresham Insurance Company Limited

Notes to the financial statements (continued)

19. Risk management (continued)

(b) Strategic risks

UK&I GI is exposed to a number of strategic risks UK&I GI's strategy supports its vision, purpose and objectives and is responsive to both the external and internal environment, for example, changes in the competitive landscape arising from economic conditions, customer demands and competitor activity, regulatory changes, merger and acquisition opportunities and emerging trends (such as climate change and pandemic events)

Strategic risk is explicitly considered throughout UK&I GI's strategic review and planning process Developments are assessed during the quarterly performance management process where all aspects of the risk profile are considered UK&I GI actively engages with external bodies to share the benefit of its expertise in supporting responses to emerging risks as well as challenging developments that could be damaging to the business and the industry as a whole

(c) Operational risk management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events Operational risks include taxation, reputation and regulatory risks, such as compliance Only financial instrument risk requires quantification under IFRS and consequently no quantification of operational risk is provided

Operational risk is managed in accordance with control standards set out in Group risk management framework

The management of operational risk is overseen by the UK&I GI Operational Risk & Reputation Committee

Gresham Insurance Company Limited

Notes to the financial statements (continued)

19. Risk management (continued)

(d) Risk and capital management

UK&I GI uses a number of risk management tools to understand the volatility of earnings, the volatility of its capital requirements, and to manage its capital more efficiently Primarily, risk-based capital models and scenario tests are used Sensitivities to economic and operating experience are regularly produced on all of UK&I GI's financial performance measurements to inform UK&I GI's decision-making and planning processes, and as part of the framework for identifying and quantifying the risks to which UK&I GI is exposed

General insurance claims liabilities are estimated by using standard actuarial claims projection techniques In general, these methods extrapolate the claims development for each accident year based on the observed development of earlier years As such, in the analysis overleaf, the sensitivity of general insurance claims 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
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 by 5%

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

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 2012

	Increase/(decrease) in shareholder's equity (£m)		Increase/(decrease) in profit before tax (£m)	
	Gross of reinsurance	Net of reinsurance	Gross of reinsurance	Net of reinsurance
Expenses +10%	(4)	-	(4)	-
Gross loss ratios + 5%	(7)	-	(7)	-

Gresham Insurance Company Limited

Notes to the financial statements (continued)

19. Risk management (continued)

(d) Risk and capital management (continued)

The tables shown earlier in this note demonstrate the effect of a change in a key assumption while other assumptions remain unchanged In reality, there is a correlation between the assumptions and other factors It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results

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

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

20. Capital structure

The Company maintains an efficient capital structure from equity shareholder's funds, consistent with the Company's overall risk profile and the regulatory and market requirements of the business This note describes the way the Company manages capital and shows where this is employed

(a) General

IFRS underpins the Company's capital structure and, accordingly, the capital structure is analysed on this basis UK&I GI uses risk management tools to assess its internal economic capital requirements

The Company as a regulated company is required to hold sufficient capital to meet acceptable solvency levels based on applicable FSA regulations The Company's ability to declare dividends from distributable profits to its parent company is therefore restricted to the extent that these amounts form part of UK regulatory capital

(b) Capital management

In managing its capital, the Company seeks to

(i) match the expected cash flows from its assets with the expected cash outflows from the Company's insurance liabilities as they fall due,
(ii) maintain financial strength to support new business growth and satisfy the requirements of its policyholders and regulators,
(iii) retain financial flexibility by maintaining strong liquidity, and
(iv) allocate capital efficiently to support growth and repatriate excess capital where appropriate

The Company considers not only the traditional sources of capital funding but the alternative sources of capital including reinsurance, as appropriate, when assessing its deployment and usage of capital

Gresham Insurance Company Limited

Notes to the financial statements (continued)

20. Capital structure (continued)

(c) Different measures of capital

The Company measures its capital on a number of different bases These include measures which comply with the regulatory regime within which the Company operates and those which the directors consider appropriate for the management of the business The measures which the Company uses are

(i) Accounting basis

The Company is required to report its results on an IFRS basis

(ii) Regulatory bases

Relevant capital and solvency regulations are used to measure and report the Company's financial strength These measures are based on the FSA's current regulatory requirements under Solvency I and the ICA regime The regulatory capital tests verify that the Company retains an excess of solvency capital above the required minimum level calculated using a series of prudent assumptions about the type of business that is underwritten

The Company fully complied with these regulatory requirements during the year

(iii) Economic bases

Notwithstanding the required levels of capital laid out by the FSA, UK&I GI also measures its capital using various risk-based management tools that take into account a more realistic set of financial and non-financial assumptions Note 19, Risk management, gives further details

(d) Capital structure

	IFRS net assets 2012 £m	IFRS net assets 2011 £m
General insurance	81	77
Total capital employed	81	77
Financed by		
Equity shareholder's funds	81	77

Gresham Insurance Company Limited

Notes to the financial statements (continued)

21. Related party transactions

(a) The Company had the following related party transactions in 2012 and 2011

(i) Quota share arrangement

The Company entered into a quota share reinsurance arrangement with Aviva International Insurance Limited, with effect from 1 January 2006 On 14 November 2011, this contract was transferred to the Company's current parent company, Aviva Insurance Limited by way of an insurance business transfer under part VII of the Financial Services and Markets Act 2000

The key terms of the agreement remain

- a 100% cession rate on premiums, claims costs and underwriting expense costs is applied in respect of the underwriting year, and
- a requirement for the Company to retain a percentage in relation to the Financial Services Compensation Scheme levy

The premiums, claims and expenses which were reinsured to Aviva International Insurance Limited under the previous arrangement to 14 November 2011 were

Quota share	2011
	£m
Premiums earned	185
Claims incurred	(89)
Fee and commission expenses and operating expenses	(86)
Profit ceded	10

No material balances relating to this arrangement were included in the statement of financial position in 2011

The premiums, claims and expenses which have been reinsured to Aviva Insurance Limited under the arrangement from 14 November 2011 are

Quota share	2012	2011
	£m	£m
Premiums earned	218	45
Claims incurred	(128)	(19)
Fee and commission expenses and operating expenses	(96)	(15)
Profit/(loss) ceded	(6)	11

The material balances in the statement of financial position relating to this arrangement are

	2012	2011
	£m	£m
Reinsurance assets	197	185
Receivable arising out of ceded reinsurance	-	8
Payable arising out of ceded reinsurance	(14)	-
Reinsurers' share of deferred acquisition costs	(36)	(34)

Gresham Insurance Company Limited

Notes to the financial statements (continued)

21. Related party transactions (continued)

(ii) Structured settlements arrangement

In 2012, the Company entered into an arrangement with Aviva Annuity UK Limited, a fellow Group company, for the reinsurance of its obligations in respect of structured settlements, also known as periodic payment orders During the year, the Company paid Aviva Annuity UK Limited £1 million under this arrangement to reinsure new structured settlements arising during the year

(iii) Other services provided by related parties

	2012		2011	
	Expense incurred in year	Receivable/ (payable) at year end	Expense incurred in year	Receivable/ (payable) at year end
	£m	£m	£m	£m
Parent	39	6	5	(37)
Other Group companies	-	-	43	-
	39	6	48	(37)

Expense incurred in the year of £39 million (2011 £48 million) represents recharges of costs payable to Aviva Insurance Limited, the Company's parent

Transactions with Group companies for settlement of corporation tax assets and liabilities by group relief are described in note 12(a)

(iv) Key management compensation

The key management of the Company are considered to be the statutory directors of the Company Note 4, Directors, gives details of their compensation as directors of the Company

(b) Immediate parent company

The Company's immediate parent company is Aviva Insurance Limited, registered in Scotland

(c) Ultimate controlling entity

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