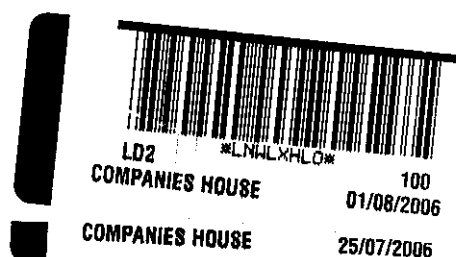


DIRECTORS' REPORT AND FINANCIAL STATEMENTS

HERMES PENSIONS MANAGEMENT LIMITED

31 DECEMBER 2005

Registered No: 1661776



HERMES PENSIONS MANAGEMENT LIMITED

DIRECTORS' REPORT

Directors:	R Bernays	(Chairman – Non executive)
	M Anson	(Chief Executive – appointed 31 January 2006)
	A Watson	(resigned 31 January 2006)
	M G Quirke	
	C M Metcalfe	
	N C W Mustoe	
	Sir Tim Chessells	(Non executive)
	D W Davies	(Non executive)
	D J Pitt-Watson	
	D R Barford	(appointed 1 January 2006 – Non executive)
	J A Biles	(appointed 1 September 2005 – Non executive)

Secretary: M S Green

Registered Office: Lloyds Chambers, 1 Portsoken Street, London E1 8HZ.

The directors who served throughout the year, except as noted, are listed above.

During the year the directors had no interests in the shares of the company or any other group company.

The directors submit their report and the audited financial statements for the year ended 31 December 2005.

PRINCIPAL ACTIVITIES

The principal activity of the company is that of a holding company. That of the group is to act as the principal investment manager of the BT Pension Scheme (BTPS) and the investment manager for other clients.

ELECTIVE RESOLUTIONS

The Board of Hermes Pensions Management Limited has used the written resolution procedures pursuant to S381A of the Companies Act 1985 to pass the following elective resolutions:

- a) that pursuant to S366A of the Companies Act 1985, the company has elected to dispense with the holding of Annual General Meetings (until the election is revoked);

HERMES PENSIONS MANAGEMENT LIMITED

DIRECTORS' REPORT (continued)

- b) that pursuant to S252 of the Companies Act 1985, the company has elected to dispense with the laying of accounts and reports before the company in general meeting; and
- c) That pursuant to S386 of the Companies Act 1985, the company has elected to dispense with the obligation to appoint auditors annually.

FINANCIAL INSTRUMENTS

Group operations are primarily financed from retained earnings and a loan from the BT Pension scheme, the group's ultimate parent.

The Group also has other financial instruments such as debtors, creditors, loans, investments and cash. These mostly arise from the Group's operations. The group has a policy of identifying and controlling the risks associated with such instruments. These risks includes interest rate risk, liquidity risk, currency risk and credit risk. Bearing in mind the nature of the exposure to financial instruments within the group and the limited risks associated, the Directors are satisfied that there is adequate control of the risks.

RESULTS

The results for the year are shown on the attached profit and loss account. The directors do not recommend the payment of a dividend (2004 - £nil).

The directors consider the results of the company to be satisfactory and that the company is well placed to take advantage of future opportunities.

EMPLOYEE INVOLVEMENT

During the year meetings are held to discuss the performance of the group. Opportunity is given at these meetings for senior executives to be questioned about matters which concern the employees.

DISABLED POLICY

Applications for employment by disabled persons are always fully considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled every effort is made to ensure that their employment with the group continues and that appropriate training is arranged. It is the policy of the group that the training, career development and promotion of disabled persons should, as far as possible be identical with that of other employees.

Approved by order of the Board of Directors and signed on behalf of the Board



M. Anson
Director

26 April 2006

HERMES PENSIONS MANAGEMENT LIMITED

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report and the financial statements. The directors have chosen to prepare the accounts for the company and the group in accordance with United Kingdom Generally Accepted Accounting Practice.

Company law requires the directors to prepare such financial statements for each financial year which give a true and fair view in accordance with United Kingdom Generally Accepted Accounting Practice of the state of affairs of the company and of the group and of the profit or loss of the company for that period and comply with UK GAAP and the Companies Act 1985.

In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and the group and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for the system of internal control, for safeguarding the assets of the company and the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF HERMES PENSIONS MANAGEMENT LIMITED

We have audited the financial statements of Hermes Pensions Management Limited for the year ended 31 December 2005 which comprise the consolidated profit and loss account, consolidated statement of total recognised gains and losses, the consolidated balance sheet, the balance sheet, the consolidated cash flow statement, the accounting policies and the related notes 1 to 27. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's member, 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 member those matters we are required to state to it 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 member for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the statement of directors' responsibilities, the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice). Our responsibility is to audit the financial statements in accordance with relevant United Kingdom 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 in accordance with the relevant financial reporting framework, and are properly prepared in accordance with the Companies Act 1985. We also report 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 or material inconsistencies within the financial statements.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland). 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 circumstances of the company and the group, 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.

**INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF
HERMES PENSIONS MANAGEMENT LIMITED (continued)**

Opinion

In our opinion

- the financial statements give a true and fair view in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of affairs of the company and the group as at 31 December 2005 and of the group's profit for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
London

26 April 2006

HERMES PENSIONS MANAGEMENT LIMITED
**CONSOLIDATED PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 2005**

	Notes	2005 £'000	2004 Restated £'000
TURNOVER	1	73,799	57,628
Administrative expenses		<u>(70,619)</u>	<u>(59,685)</u>
OPERATING PROFIT / (LOSS)		3,180	(2,057)
Share of net operating profit of associates	2	2,205	4,673
Dividends receivable		259	207
(Loss) / profit on investments		<u>(6)</u>	<u>16</u>
PROFIT ON ORDINARY ACTIVITIES BEFORE INTEREST AND TAXATION		5,638	2,839
Interest receivable and similar income			
- group		2,055	1,523
- associates		213	354
Other finance income	15	300	200
Interest payable - group	3	(990)	(989)
- associates	3	<u>(4)</u>	<u>(3)</u>
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	4	7,212	3,924
Tax on profit on ordinary activities	6	<u>(1,021)</u>	<u>(1,406)</u>
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION		6,191	2,518
Equity minority interests	24	<u>(8)</u>	<u>(8)</u>
RETAINED PROFIT FOR THE FINANCIAL YEAR	17	<u>6,183</u>	<u>2,510</u>

All of the results are derived from continuing operations.

HERMES PENSIONS MANAGEMENT LIMITED
**CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDED 31 DECEMBER 2005**

	Notes	2005 £'000	2004 Restated £'000
Retained profit for the financial year		6,183	2,510
Unrealised surplus on revaluation of investments		126	82
Foreign exchange translation difference on foreign currency investment in associate		(8)	(1)
		<u>6,301</u>	<u>2,591</u>
Defined Benefit Pension Scheme – Actuarial gain on assets	15	6,300	1,500
Defined Benefit Pension Scheme – Actuarial gain on liabilities	15	200	-
Defined Benefit Pension Scheme – Actuarial loss on change in assumptions	15	(7,300)	(1,600)
		<u>5,501</u>	<u>2,491</u>
Total recognised gains relating to the Year	17		
Inclusion of Opening deficit on Defined Benefit Pension Scheme	15 / 26	-	(14,300)
Prior year adjustment FRS 17	15 / 26	-	4,599
		<u>-</u>	<u>(9,701)</u>
Total gains / (losses) recognised since last annual report		<u>5,501</u>	<u>(7,210)</u>

HERMES PENSIONS MANAGEMENT LIMITED**CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 2005**

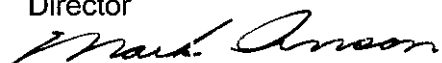
	Notes	2005 £'000	2004 Restated £'000
FIXED ASSETS			
Intangible assets – goodwill	9	5,303	6,097
Tangible assets	10	6,345	6,918
Investments	11	10,756	9,679
		<u>22,404</u>	<u>22,694</u>
CURRENT ASSETS			
Insurance assets attributable to unit-linked policyholders	12	20,334,796	8,506,484
Debtors	13	20,424	16,195
Cash at bank and in hand		64,896	53,408
		<u>20,420,116</u>	<u>8,576,087</u>
CREDITORS - amounts falling due within one year	14	(48,796)	(42,047)
Amounts due to unit-linked policyholders	12	(20,334,796)	(8,506,484)
NET CURRENT ASSETS		<u>36,524</u>	<u>27,556</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		58,928	50,250
CREDITORS - amounts falling due after more than one year	14	(4,296)	(3,027)
		<u>54,632</u>	<u>47,223</u>
Minority interest - equity	24	(135)	(127)
NET ASSETS EXCLUDING PENSION LIABILITIES		54,497	47,096
Pension liabilities	15	(16,600)	(14,700)
NET ASSETS INCLUDING PENSION LIABILITIES		<u>37,897</u>	<u>32,396</u>
CAPITAL AND RESERVES			
Called up share capital	16	30,000	30,000
Revaluation reserves	17	252	126
Non-distributable capital reserves	17	98	98
Profit and loss account	17	7,547	2,172
EQUITY SHAREHOLDER'S FUNDS		<u>37,897</u>	<u>32,396</u>

These financial statements were approved by the Board of Directors on 26 April 2006

Signed on behalf of the Board of Directors

M Anson

Director



HERMES PENSIONS MANAGEMENT LIMITED**BALANCE SHEET AT 31 DECEMBER 2005**

	Notes	2005 £'000	2004 Restated £'000
FIXED ASSETS			
Tangible assets	10	6,345	6,918
Investments	11	25,026	25,126
		<u>31,371</u>	<u>32,044</u>
CURRENT ASSETS			
Debtors	13	23,272	22,892
Cash at bank and in hand		22,019	9,468
		<u>45,291</u>	<u>32,360</u>
CREDITORS - amounts falling due within one year	14	(40,942)	(35,616)
NET CURRENT ASSET/(LIABILITIES)		<u>4,349</u>	<u>(3,256)</u>
TOTAL ASSETS LESS CURRENT LIABILITIES		35,720	28,788
CREDITORS - amounts falling due after more than one year	14	(2,608)	(2,772)
NET ASSETS EXCLUDING PENSION LIABILITIES		<u>33,112</u>	<u>26,016</u>
Pension liabilities	15	(16,600)	(14,700)
NET ASSETS INCLUDING PENSION LIABILITIES		<u>16,512</u>	<u>11,316</u>
CAPITAL AND RESERVES			
Called up share capital	16	30,000	30,000
Profit and loss account	17	(13,488)	(18,684)
EQUITY SHAREHOLDER'S FUNDS		<u>16,512</u>	<u>11,316</u>

These financial statements were approved by the Board of Directors on 26 April 2006

Signed on behalf of the Board of Directors

M Anson
Director



HERMES PENSIONS MANAGEMENT LIMITED**CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2005**

	Notes	2005 £'000	2004 Restated £'000
NET CASH INFLOW FROM OPERATING ACTIVITIES	19	12,947	6,379
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE			
Interest received		2,055	1,507
Interest paid		(990)	(989)
Actuarial gain arising on Pension Fund		200	-
Finance income arising from Pension Fund		300	200
Dividends received from associates		259	207
NET CASH INFLOW FROM RETURNS ON INVESTMENTS AND SERVICING OF FINANCE		1,824	925
TAXATION			
Corporation tax (paid) / received		(1,076)	1,117
TAX (PAID) / RECEIVED		(1,076)	1,117
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT			
Payments to acquire tangible fixed assets	10	(2,007)	(2,861)
Sale of tangible fixed assets		-	3
Purchase of investments		(106)	-
Sale of investments		-	66
NET CASH OUTFLOW FROM CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT		(2,113)	(2,792)
NET CASH INFLOW BEFORE FINANCING FINANCING		11,582	5,629
(Loan to) / Repayment from associate		(94)	137
NET CASH INFLOW FROM FINANCING		(94)	137
INCREASE IN CASH	20	11,488	5,766

HERMES PENSIONS MANAGEMENT LIMITED

NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005

ACCOUNTING POLICIES

The financial statements are prepared in accordance with applicable law and United Kingdom Accounting Standards, with the exception of certain departures from Companies Act requirements as disclosed in note 22. The particular accounting policies adopted by the directors are described below.

a) Accounting convention

The financial statements are prepared under the historical cost convention except for the following:

- i) Fixed asset investments, which are held at a directors' valuation.
- ii) Investments included in life insurance assets, which are revalued to mid-market value.

b) Turnover

Turnover is recognised on an accruals basis.

c) Basis of consolidation

Subsidiary companies of the group include general partners of limited partnerships where the substance of the arrangements is that the group provides investment management services in return for investment management fees. In the prior year certain of these limited partnerships fell within the definition of subsidiary undertakings that were required to be consolidated under the Companies Act 1985 by virtue of the fact they were controlled by the general partner. However, the group's beneficial interest in the limited partnerships is restricted to the fees it earns from managing the partnerships. Furthermore, the limited partnerships were set up for the beneficial interest of external parties who collectively own the entire equity of the partnerships. In the prior year the directors departed from the Companies Act 1985 requirements and accounted for the interests in such partnerships at cost on the basis that this reflected the substance of the arrangements and to consolidate would not give a true and fair view. The effect of this departure is quantified in note 22. Due to changes in the structure in 2005 the limited partnerships no longer meet the definition of subsidiary undertakings.

d) Goodwill

Goodwill arising in respect of acquisitions is capitalised in the year in which it arises within intangible fixed assets and amortised over its estimated useful life up to a maximum of 20 years with a full year's charge for amortisation in the year of acquisition. The directors regard the following as the estimated useful lives of goodwill arising in those acquisitions.

Hermes Focus Asset Management Ltd	- 20 years
Hermes Assured Ltd	- 5 years

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****ACCOUNTING POLICIES (continued)****e) Tangible fixed assets**

Depreciation is provided on cost in equal annual instalments over the estimated useful lives of the assets. The expected useful lives are as follows:

Fixtures, fittings and equipment	- 4 years
Leasehold improvements	- Period of the lease

f) Fixed asset investments

Investments held as fixed assets are stated at directors' valuation. For quoted investments, this is taken to be mid-market value. For unquoted investments this is based upon the latest available information and reports.

g) Operating leases

Rentals in respect of operating leases are charged to the profit and loss account on a straight-line basis over the period of the lease.

h) Pension benefits

Pension benefits under the group's defined benefit scheme are funded over the employees' periods of service. The company's contributions are based on the most recent actuarial valuation of the fund on 31 December 2003. Pension benefits are accounted for in accordance with FRS17 as disclosed in note 15.

i) Investment income

Income from investments is accounted for on an accruals basis.

j) Bonus costs

Provision is made for bonuses attributable to performance prior to the balance sheet date.

k) Deferred taxation

Deferred taxation is provided in full on timing differences that result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax balances are not discounted.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****ACCOUNTING POLICIES (continued)****l) Long-term life insurance business**

Assets attributable to unit-linked policyholders are valued at mid-market value. Amounts due to unit-linked policyholders represent the value of in force units at the balance sheet date.

Expenses incurred in the operation and establishment of the Life business are deducted in arriving at operating profit.

1. TURNOVER

Turnover comprises the value of services provided in the UK by the group exclusive of VAT and is analysed as follows:

	2005	2004
	£'000	£'000
Continuing operations:		
Investment management services	64,617	51,560
Miscellaneous fees	2,388	905
Recharge to associate	1,790	1,608
Recharges to Focus Funds	864	750
Management fees from assurance activities	4,140	2,805
	<u>73,799</u>	<u>57,628</u>

Investment management services include performance fees based upon rolling three year performance periods and are recognised in the year the performance period ends.

2. ASSOCIATES**Share of Net Operating Profit of Associates**

	2005	2004
	£'000	£'000
49% share of HFAME operating profit	-	697
45.7% share of HFAME operating profit	1,818	651
35.9% share of Innisfree operating profit	260	3,050
25% share of Activa operating profit	129	277
Amorisation of goodwill	(2)	(2)
	<u>2,205</u>	<u>4,673</u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****2. ASSOCIATES (continued)**

The company had the following interests in the performance and position of its associates at 31 December 2005.

HFAME	2005	2004
	£'000	£'000
Turnover	5,580	4,552
Profit before tax	1,948	1,407
Tax	(578)	(422)
Profit after tax	1,371	985
Current assets	6,144	4,179
Current liabilities	(3,364)	(2,327)
Long term liabilities	(539)	(526)

Innisfree	2005	2004
	£'000	£'000
Turnover	4,670	6,547
Profit before tax	660	3,829
Tax	(159)	(788)
Profit after tax	501	3,041
Fixed assets	37	65
Current assets	6,627	6,215
Current liabilities	(2,560)	(3,328)
Long term liabilities	(1,080)	(555)

Activa	2005	2004
	£'000	£'000
Turnover	668	715
Profit before tax	131	345
Tax	(29)	(26)
Profit after tax	102	319
Fixed assets	43	47
Current assets	318	519
Current liabilities	(176)	(301)

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****3. INTEREST PAYABLE**

	2005	2004
	£'000	£'000
Interest payable or similar charges in respect of:		
Bank loans and overdrafts (excluding group loans)	2	1
Interest on loans from group companies	988	988
Other	4	3
	<u>994</u>	<u>992</u>

4. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

	2005	2004
	£'000	Restated £'000
Profit on ordinary activities before taxation is stated after charging:		
Depreciation of tangible fixed assets	2,580	3,151
Amortisation of goodwill	794	794
Rentals under operating leases:		
- Charges	741	1,446
- Receipts	(216)	(216)
Auditors' remuneration:		
Audit fees - group	217	150
- company	22	36
Other services	232	46
	<u>232</u>	<u>46</u>

HERMES PENSIONS MANAGEMENT LIMITED

NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)

5. INFORMATION REGARDING DIRECTORS AND EMPLOYEES

Total emoluments of directors excluding pension contributions were:

Directors	Salary £	Annual bonus £	Benefits £	Long term		Fees £	Total 2005 £	Total 2004 £
				incentive scheme £				
A Watson	288,430	419,291	16,356	1,046,505	-	-	1,770,582	1,305,942
N C W Mustoe	204,687	255,138	9,497	500,569	-	-	969,891	852,329
C M Metcalfe	183,625	215,515	10,028	448,995	-	-	858,163	801,738
M G Quirke	181,625	216,979	9,763	57,096	-	-	465,463	253,186
D W Davies	40,000	-	-	-	-	-	40,000	30,000
D Pitt-Watson	143,750	535,713	7,800	631,828	-	-	1,319,091	-
R Bernays	-	-	-	-	50,000	-	50,000	-
J A Biles	-	-	-	-	11,666	-	11,666	-
P R Butler	-	-	-	-	-	-	-	538,777
A H M White	-	-	-	-	-	-	-	532,567
R A Selkirk	-	-	-	-	-	-	-	518,576
S P Brown	-	-	-	-	-	-	-	437,930
P Bisping	-	-	-	-	-	-	-	437,845
M L Carter	-	-	-	-	-	-	-	413,273
R J Clarke	-	-	-	-	-	-	-	363,591
J H C Walsh	-	-	-	-	-	-	-	341,869
A M Cook	-	-	-	-	-	-	-	265,463
C C Hartridge-Price	-	-	-	-	-	-	-	213,720
I A Kirby	-	-	-	-	-	-	-	190,799
A Orriss	-	-	-	-	-	-	-	145,637
R A Harrold	-	-	-	-	-	-	-	114,840
TOTAL	1,042,117	1,642,636	53,444	2,684,993	61,666	5,484,856	7,758,082	

As at 31 December 2005 one director (2004 - 1) had investments of £650,081 (2004 - £574,731) in the three Hermes UK Focus Funds and one director (2004 - 1) had an investment of £162,344 (2004 - £137,061) in the UK Small Companies Focus Fund.

Also at 31 December 2005, one director (2004 - 1) had an investment in European Focus Fund I of £78,407 (2004 - £60,148), managed by associate company Hermes Focus Asset Management Europe Limited.

The annual bonus and long term incentive scheme rewards together comprise 80% (2004 - 71%) of total emoluments. These rewards are based on the results of the group, investment performance and the successful completion of individual management objectives.

HERMES PENSIONS MANAGEMENT LIMITED

NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)

5. INFORMATION REGARDING DIRECTORS AND EMPLOYEES (continued)

Amounts awarded to all excluding D Pitt-Watson under the Hermes Group long-term incentive plan are payable in two tranches. 50% is payable in March 2006 and the remaining 50% is payable in March 2008. The amount awarded to D Pitt-Watson relates to the HFAM long term incentive plan which represents the value of options vesting in 2005 under the five year Shadow Option Scheme. This also rewards participating executives for the growth in the value of the business.

Sir Tim Chessells did not receive any emoluments relating to his services to the group but received fees from the Hermes Group on behalf of the BT Pension Scheme in respect of Trustees' services to the BT Pension Scheme as described in Note 23.

D W Davies also received fees from the BT Pension Scheme in respect of Trustees' services to the BT Pension Scheme as described in Note 23.

The unfunded pension cost relates to the increase in the year in the company's liability to pay a pension in excess of that provided by the Hermes Group Pension Scheme.

The company's pension scheme is a defined benefit scheme and the accrued benefit as at 31 December 2005 for the highest paid director was £34,260 (2004 - £28,779). The total number of directors who accrue benefits under the scheme is 4 (2004 - 11).

	2005	2004
	No.	No.
Average number of persons employed by the group and company in the year:		
Investment management	164	143
Administration	134	143
	<u>298</u>	<u>286</u>

	2005	2004
	£'000	RESTATED £'000
Staff costs during the year in respect of these directors and employees were:		
Wages and salaries	35,117	31,280
Social security costs	3,830	3,727
Pension cost related to group scheme (see Note 15)	3,400	3,000
Unfunded pension costs	84	78
	<u>42,431</u>	<u>38,085</u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****6. TAX ON PROFIT ON ORDINARY ACTIVITIES**

	2005	2004
	£'000	£'000
a) Profit and loss account		
UK corporation tax at 30%	9	21
Share of tax charge in associate	764	449
Adjustment in respect of prior periods	111	(10)
	<u>884</u>	<u>460</u>
Deferred tax:		
Share of deferred tax charge in associate	-	788
Time differences, origination and reversal	163	112
Adjustment in respect of prior periods	(26)	46
Tax on profit on ordinary activities	<u>1,021</u>	<u>1,406</u>

- b) The tax charged in the period is lower than the standard rate of corporation tax in the UK (30%). The differences are explained below:

	2005	2004
	£'000	£'000
Profit on ordinary activities multiplied by the standard rate of corporation tax in the UK of 30% (2004 - 30%)	2,164	1,177
Non-taxable income	(2,431)	(2,440)
Drawings not subject to tax	-	(777)
Capital allowances in excess of depreciation not provided for in deferred tax	149	905
Short term timing differences not provided for in deferred tax	1,014	567
Tax losses	(123)	1,038
Adjustment in respect of prior periods	111	(10)
	<u>884</u>	<u>460</u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****6. TAX ON PROFIT ON ORDINARY ACTIVITIES (continued)**

	2005 Provided £'000	2005 Unprovided £'000	2004 Provided £'000	2004 Unprovided £'000
c) The Group				
Deferred tax asset				
Accelerated capital allowances	-	(3,182)	-	(3,016)
Tax losses	(227)	-	(226)	-
Short term timing differences	301	(9,094)	163	(4,937)
	<u>74</u>	<u>(12,276)</u>	<u>(63)</u>	<u>(7,953)</u>
The Company				
Deferred tax asset				
Accelerated capital allowances	-	(3,179)	-	(3,012)
Short term timing differences	-	(6,454)	-	(2,779)
	<u>-</u>	<u>(9,633)</u>	<u>-</u>	<u>(5,791)</u>

Deferred tax assets totalling £12,276,129 (2004: £7,952,509) have not been recognised in respect of depreciation in excess of capital allowances and short term timing differences as the Group is not sufficiently certain that it will be able to recover those assets within a relatively short period of time.

Movement on Deferred Tax

	Group £'000
d)	
1 January 2005	(63)
Inadmissible assets	138
Tax losses	(1)
31 December 2005	<u>(74)</u>

HERMES PENSIONS MANAGEMENT LIMITED

NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)

7. CAPITAL STATEMENTS

The Capital statements shown below relate to Insurance business within Hermes Assured Limited, a wholly owned subsidiary.

Available capital

	UK Non-participating	Life Business Shareholders Funds	Total Life Business
	£'000	£'000	£'000
Shareholders: funds outside fund	-	4,828	4,828
Shareholders: funds held in fund	4,498	-	4,498
Total shareholders funds	4,498	4,828	9,326
Adjustments onto regulatory basis:			
Assets inadmissible for regulatory purposes	(1,003)	(702)	(1,705)
Total available capital resources	3,495	4,126	7,621

There is no other qualifying capital within the Company.

Capital movements

	UK Non-participating	Life Business Shareholders Funds	Total Life Business
	£'000	£'000	£'000
Total available capital resources 01 January 2005	2,530	4,807	7,337
New business and other factors	965	(681)	284
Total available capital resources 31 December 2005	3,495	4,126	7,621

The Company operates a non-participating fund within the United Kingdom. It does not have any with profit funds and it does not have any overseas operations.

The total available capital resources for each section of the statement shows the capital on a regulatory basis that is available to meet the regulatory capital requirements of that part of the business.

The available surplus held in the non-participating fund is attributable to shareholders, and, subject to meeting the regulatory requirements of this business this capital is available to meet requirements elsewhere in the Company. Any transfer of surplus may give rise to a tax charge.

The non-participating fund must meet the minimum solvency requirements determined in accordance with Financial Services Authority (FSA) regulations. At 31 December 2005 the available capital was 375% of the capital requirement of £2,030k.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****8. PROFIT OF THE PARENT COMPANY**

As permitted by Section 230 of the Companies Act, the profit and loss account of the parent company is not presented as part of these accounts. The parent company's profit for the year amounted to £5,196,170 (2004 - loss of £1,335,818 as restated).

9. INTANGIBLE FIXED ASSETS

	Goodwill £'000
The Group	
Cost	
At 1 January 2005 and 31 December 2005	<u>8,614</u>
Accumulated amortisation	
At 1 January 2005	2,517
Charge for the year	<u>794</u>
At 31 December 2005	<u>3,311</u>
Net book value	
At 31 December 2005	<u><u>5,303</u></u>
At 31 December 2004	<u><u>6,097</u></u>

10. TANGIBLE FIXED ASSETS

	Leasehold improvements £'000	Fixtures, Fittings and equipment £'000	Total £'000
The Group and the Company			
Cost			
At 1 January 2005	5,773	11,569	17,342
Additions	199	1,808	2,007
Disposals	<u>-</u>	<u>(4,266)</u>	<u>(4,266)</u>
At 31 December 2005	<u>5,972</u>	<u>9,111</u>	<u>15,083</u>
Accumulated depreciation			
At 1 January 2005	2,153	8,271	10,424
Charge for the year	258	2,322	2,580
Disposals	<u>-</u>	<u>(4,266)</u>	<u>(4,266)</u>
At 31 December 2005	<u>2,411</u>	<u>6,327</u>	<u>8,738</u>
Net book value			
At 31 December 2005	<u><u>3,561</u></u>	<u><u>2,784</u></u>	<u><u>6,345</u></u>
At 31 December 2004	<u><u>3,620</u></u>	<u><u>3,298</u></u>	<u><u>6,918</u></u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****11. INVESTMENTS HELD AS FIXED ASSETS**

	Investment in associates £'000	Listed investments £'000	Unlisted investments £'000	Total £'000
The Group				
At 1 January 2005 – Restated	4,956	4,702	21	9,679
Share of retained profit for the year	843	-	-	843
Revaluation	20	106	-	126
Additional investment	106	-	-	106
Share of associate reserves	8	-	-	8
Disposal	-	-	(4)	(4)
Goodwill amortisation	(2)	-	-	(2)
At 31 December 2005	<u>5,931</u>	<u>4,808</u>	<u>17</u>	<u>10,756</u>

**Shares in subsidiary
undertakings
£'000**

The Company

At 1 January 2005	25,126
Purchase of shares	(350)
Sale of shares	250
31 December 2005	<u>25,026</u>

The investment in associates is the share of net assets in Hermes Focus Asset Management Europe Limited (HFAME) of £2,235,632, Activa Capital of £291,788 and Innisfree Limited of £3,404,363. The investment in Activa Capital includes £23,552 of goodwill (2004 - £24,909).

On 10 April 2006 the directors of Hermes Investment Management Ltd agreed to sell the company's holding of 107,600 shares in Innisfree Ltd.

Listed investments are short dated gilts held at market value by subsidiary companies and their total market value at 31 December 2005 was £4,807,650 (2004 - £4,701,903). The gilts were revalued at the end of the year and a total unrealised gain of £105,747 was transferred to revaluation reserves.

Information on subsidiaries and associates is disclosed in note 21.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****12. INSURANCE ASSETS ATTRIBUTABLE TO UNIT-LINKED POLICYHOLDERS**

All insurance assets and liabilities relate to Hermes Assured Limited, a wholly owned subsidiary of the Company and are as follows:

- a) At 31 December 2005, the insurance assets attributable to unit-linked policyholders comprised:

	2005	2004
	£'000	£'000
Equities and unit trusts	13,914,474	5,659,642
Overseas investments	5,553,784	2,457,548
Fixed interest stocks	720,084	335,962
Cash unit trusts	10,553	16,193
Cash	82,433	12,390
Derivatives	910	523
Dividends and accrued interest	52,558	24,226
	<u>20,334,796</u>	<u>8,506,484</u>
Amounts due to unit-linked policyholders	<u>20,334,796</u>	<u>8,506,484</u>

- b) At 31 December, the summarised income and expenditure account of the Life business comprised:

	2005	2004
	£'000	£'000
Gross premiums written	9,550,839	1,265,185
Net claims incurred	(1,040,412)	(99,841)
Unrealised gains	2,481,876	635,555
Realised gains	344,703	11,828
Investment income receivable	491,306	212,652
Other technical income	4,340	2,973
Change in technical provisions for linked liabilities	(11,828,312)	(2,025,379)
Net operating expenses	<u>(3,684)</u>	<u>(2,866)</u>
	<u>656</u>	<u>107</u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****13. DEBTORS**

	2005		2004	
	Group £'000	Company £'000	Group £'000	Company £'000
Due within one year				
Owed by subsidiaries	-	12,871	-	12,602
Owed by associates	917	730	554	400
Owed by parent	1,536	298	2,100	60
Trade debtors	13,811	370	9,078	705
Taxation	2,155	1,343	2,043	1,343
Other debtors	511	1,178	465	940
Prepayments and accrued income	1,399	1,332	1,891	1,841
	<u>20,329</u>	<u>18,122</u>	<u>16,131</u>	<u>17,891</u>
Due after one year				
Subordinated loan – subsidiary	-	5,000	-	5,000
Loan to associate	95	150	-	-
Deferred tax	-	-	63	-
Prepayments and accrued income	-	-	1	1
	<u>20,424</u>	<u>23,272</u>	<u>16,195</u>	<u>22,892</u>

14. CREDITORS

	2005		2004	
	Group £'000	Company £'000	Group £'000	Company £'000
Amounts falling due within one year				
Owed to parent	18,430	17,830	17,830	17,830
Other creditors	654	310	381	200
Unfunded pension liability	758	758	673	673
Accruals and prepaid income	28,954	22,044	23,163	16,913
	<u>48,796</u>	<u>40,942</u>	<u>42,047</u>	<u>35,616</u>
Amounts falling due after more than one year				
Other creditors	4,222	2,608	3,027	2,772
Deferred Taxation	74	-	-	-
	<u>4,296</u>	<u>2,608</u>	<u>3,027</u>	<u>2,772</u>

The amount owed to parent represents a loan from the BT Pension Scheme which is repayable on demand. The interest on the loan is calculated and paid quarterly at LIBOR + 1%.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****15. PENSION COMMITMENTS**

The group operates a defined benefit scheme, Hermes Group Pension Scheme (the "Scheme"), funded by the payment of contributions to a separately administered trust fund.

The financial statements provide for full adoption of FRS 17 – Retirement Benefits. The information required under FRS 17 for the year ended 31 December 2005 has also been provided for the year ended 31 December 2004.

Contributions to the Scheme are determined with the advice of independent qualified actuaries on the basis of triennial valuations using the Projected Unit method.

The actuarial valuation was updated at 31 December 2003 by a qualified actuary using assumptions that are consistent with the requirements of FRS 17. The next full valuation will take place on 31 December 2006. Investments have been valued, for this purpose, at fair value.

The contributions of the company throughout the year were 13.8% of pensionable payroll, in line with the Schedule of Contributions. Members of the scheme contribute 5% of pensionable earnings.

The major assumptions used for the actuarial valuation were:

	2005	2004	2003
	%	%	%
Rate of increase in salaries	2.8	2.8	2.8
Rate of increase in pensions in payment	2.8	2.8	2.8
Discount rate	4.75	5.3	5.4
Inflation assumption	2.8	2.8	2.8

The fair value of the assets in the Scheme, the present value of the liabilities in the Scheme and the expected rate of return at each balance sheet date were:

	2005	2005	2004	2004	2003	2003
	%	£m	%	£m	%	£m
Equities	7.70	40.5	8.25	32.0	8.25	28.3
Bonds	4.20	5.2	4.70	3.9	4.80	1.6
Other	5.60	5.1	6.60	4.0	6.40	3.3
Total fair value of assets		50.8		39.9		33.2
Present value of Scheme Liabilities		(67.4)		(54.6)		(47.5)
Deficit in the Scheme		(16.6)		(14.7)		(14.3)

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****15. PENSION COMMITMENTS (continued)**

Analysis of the amount that has been charged to operating profit:

	2005 £m	2004 £m
Current service cost	3.4	3.0
Total operating charge	<u>3.4</u>	<u>3.0</u>

Analysis of amounts included in Other finance income:

	2005 £m	2004 £m
Expected return on scheme assets	(3.2)	(2.7)
Interest on pension scheme liabilities	<u>2.9</u>	<u>2.5</u>
Net return	<u>(0.3)</u>	<u>(0.2)</u>

Analysis of the actuarial loss recognised in the statement of total recognised gains and losses:

	2005 £m	2004 £m
Actual return less expected return on pension Scheme assets, i.e. gain	6.3	1.5
Experience gains and losses arising on the Scheme liabilities, i.e. gain	0.2	-
Changes in assumptions underlying the present value of the Scheme liabilities, i.e. (loss)	<u>(7.3)</u>	<u>(1.6)</u>
Actuarial loss	<u>(0.8)</u>	<u>(0.1)</u>

Balance Sheet reconciliation:

	2005 £m	2004 £m
Fair value of Scheme assets	50.8	39.9
Present actuarial value of Scheme liabilities	<u>(67.4)</u>	<u>(54.6)</u>
Deficit in Scheme	(16.6)	(14.7)
Related deferred tax	-	-
Net pension liability	<u>(16.6)</u>	<u>(14.7)</u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****15. PENSION COMMITMENTS (continued)**

Analysis of the movement in the Scheme deficit during the year:

	2005 £m	2004 £m
Movement in deficit during the year:		
Deficit in Scheme at 1 January	(14.7)	(14.3)
Current service cost	(3.4)	(3.0)
Contributions paid	2.0	2.5
Other finance income	0.3	0.2
Actuarial loss	(0.8)	(0.1)
Deficit in Scheme at 31 December	<u>(16.6)</u>	<u>(14.7)</u>

History of experience gains and losses:

	2005 £m	2004 £m	2003 £m	2002 £m
Difference between the expected and actual return on Scheme assets:				
Amount (gain) / loss	(6.3)	(1.5)	3.4	(7.8)
Percentage of Scheme assets	12.40%	3.76%	10.24%	30.23%
Experience gains and losses on Scheme liabilities:				
Amount (gain) / loss	(0.2)	0.0	2.3	(6.2)
Percentage of the present value of Scheme liabilities	0.30%	0.0%	4.84%	14.09%
Total actuarial gain recognised in the statement of total recognised gains and losses:				
Amount (gain) / loss	0.8	0.1	4.8	(14.5)
Percentage of the present value of Scheme liabilities	1.19%	0.18%	10.11%	32.95%

A deferred tax asset has not been recognised in respect of the pension provision calculated as the Group is not sufficiently certain that it will be able to recover this asset within a relatively short period of time.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****16. CALLED UP SHARE CAPITAL**

	2005 £'000	2004 £'000
Authorised:		
100,000 (2004: 100,000) ordinary shares of £1 each	<u>100,000</u>	<u>100,000</u>
Called up, allotted and fully paid:		
30,000 (2004: 30,000) ordinary shares of £1 each	<u>30,000</u>	<u>30,000</u>

17. COMBINED STATEMENT OF MOVEMENTS IN SHAREHOLDER'S FUNDS AND STATEMENT OF MOVEMENTS ON RESERVES

The Group	2005 Called up Share Capital £'000	2005 Revaluation reserves £'000	2005 Non- distributable capital reserves £'000	2005 Profit and loss account £'000	2005 Total £'000	2004 RESTATED Total £'000
At 1 January	30,000	126	98	2,172	32,396	39,606
Profit/(loss) for the financial year	-	-	-	6,183	6,183	2,510
Foreign exchange differences	-	-	-	(8)	(8)	(1)
Defined Benefit Pension Scheme						
- Actuarial gain on liabilities	-	-	-	200	200	-
Defined Benefit Pension Scheme						
- Actuarial gain on assets	-	-	-	6,300	6,300	1,500
Defined Benefit Pension Scheme						
- Actuarial loss on change in assumptions	-	-	-	(7,300)	(7,300)	(1,600)
Inclusion of Opening Deficit Defined Benefit Pension Scheme	-	-	-	-	-	(14,300)
Prior year FR&S 17 Adjustment	-	-	-	-	-	4,599
Revaluation of investments	-	126	-	-	126	82
At 31 December	<u>30,000</u>	<u>252</u>	<u>98</u>	<u>7,547</u>	<u>37,897</u>	<u>32,396</u>

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****17. COMBINED STATEMENT OF MOVEMENTS IN SHAREHOLDER'S FUNDS AND STATEMENT OF MOVEMENTS ON RESERVES (continued)**

The Company	2005 Issued share capital £'000	2005 Profit and Loss Account £'000	2005 Total £'000	2004 Total £'000
At 1 January restated	30,000	(18,684)	11,316	21,772
Profit / (Loss) for the financial year	-	6,004	6,004	(654)
Foreign exchange differences	-	(8)	(8)	(1)
Defined Benefit Pension Scheme - Actuarial gain or liabilities	-	200	200	-
Defined Benefit Pension Scheme - Actuarial gain on assets	-	6,300	6,300	1,500
Defined Benefit Pension Scheme - Actuarial loss on charge in assumptions	-	(7,300)	(7,300)	(1,600)
Inclusion of Opening Deficit Defined Benefit Pension Scheme	-	-	-	(14,300)
Prior year FRS 17 Adjustment	-	-	-	4,599
At 31 December	<u>30,000</u>	<u>(13,488)</u>	<u>16,512</u>	<u>11,316</u>

18. COMMITMENTS UNDER OPERATING LEASES

The Group and Company annual commitments for the year to 31 December 2006 under operating leases are as follows:

	2005 Land and buildings £'000	2005 Other £'000	2004 Land and buildings £'000	2004 Other £'000
Operating Leases which expire within:				
1 year	-	20	-	19
2 - 5 years	-	95	-	93
Over 5 years	1,803	-	1,226	-
	<u>1,803</u>	<u>115</u>	<u>1,226</u>	<u>112</u>

All operating leases which are related to land and buildings are subject to five yearly upward only rent reviews.

The company has sub-let part of the buildings and expects to receive £288,310 in rent during 2006.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****19. RECONCILIATION OF OPERATING PROFIT / (LOSS) TO NET CASH INFLOW FROM OPERATING ACTIVITIES**

	2005	2004
	£'000	Restated £'000
Operating profit / (loss)	3,180	(2,057)
Depreciation charges	2,580	3,151
Amortisation charges	794	794
Increase in debtors	(11,831,371)	(2,019,962)
Increase in creditors	11,837,764	2,024,453
Net cash inflow from operating activities	<u>12,947</u>	<u>6,379</u>

20. RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	2005	2004
	£'000	£'000
Increase in cash in year	<u>11,488</u>	<u>5,766</u>
Movement in net funds in year	11,488	5,766
Net funds at beginning of year	<u>53,408</u>	<u>47,642</u>
Net funds at end of year	<u>64,896</u>	<u>53,408</u>

Net funds at 31 December 2005 comprised cash of £64,895,875 (2004 - £53,407,926).

21. ADDITIONAL INFORMATION ON SUBSIDIARIES AND ASSOCIATES

SUBSIDIARY UNDERTAKINGS	ACTIVITY
Hermes Focus Asset Management Limited	Investment management company
Hermes Investment Management Limited	Investment management company
Hermes Real Estate Investment Management Limited	Investment management company
Hermes Administration Services Limited	Administration company
Hermes Assured Limited	Life Assurance company
Hermes SLP Limited	Special limited partner to Hermes UK Focus Funds
Hermes UOB Capital Management Limited	Investment management company
Hermes Equity Ownership Services Limited	Investment management company
Hermes Private Equity Limited	Investment management company
Hermes UOB GP Limited	General partner to limited partnership of Hermes UOB European Private Equity Fund
Hermes UOB SLP GP Limited	Special limited partner to special limited partnership of Hermes UOB European Private Equity Fund
Hermes Private Equity GP Ltd	General partner to Hermes Equity LP investor in Apax Europe V Private Equity Fund

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****21. ADDITIONAL INFORMATION ON SUBSIDIARIES AND ASSOCIATES (continued)**

Hermes Asset Management Limited	General Partner to Hermes Private Equity Partners I LP and Hermes Private Equity Partners II LP
HPEP GP Limited	General Partner to Hermes Private Equity Partners I LP and Hermes Equity Partners II LP
Hermes Secretariat Ltd	Dormant
Hermes Lens Asset Management Ltd	Dormant
Hermes X-Leisure (Nominees) Ltd	Dormant
Hermes Shelf Company No 1 Ltd	Dormant
Hermes Investment Management (Nominees) Ltd	Dormant
Hermes Focus Fund Co-Investment Trustee Ltd	Dormant
ASSOCIATES AND JOINT VENTURES	
	ACTIVITY
Hermes Focus Asset Management Europe Limited	Investment management company
Activa Capital	Investment management company
UOB Hermes Asia Management Pte Ltd	Investment management company
Innisfree Limited	Investment management company

Subsidiary undertakings are owned as to 100% of ordinary share capital except for Hermes UOB Capital Management Limited, Hermes UOB GP Limited and Hermes UOB SLP GP Limited are owned as to 60% of ordinary share capital.

All subsidiaries have been consolidated in the accounts. All are incorporated in Great Britain and registered and operate in England and Wales apart from Hermes UOB GP Limited and Hermes UOB SLP GP Limited, which are incorporated, registered and operate in Scotland.

Hermes Focus Asset Management Europe Limited is 45.7% owned and is incorporated in Great Britain and registered and operates in England and Wales. Activa Capital is 25% owned and is incorporated, registered and operates in France. Innisfree Limited is 35.9% owned and is incorporated in Great Britain and registered and operates in England and Wales. Investments in associates relate to ordinary share capital. UOB Hermes Asia Management Pte Ltd is owned as to 40% of ordinary share capital and is incorporated, registered and operates in Singapore.

On 30 January 2006 the Company acquired 33.3% of the issued share capital of NLI Investments Europe Limited. This transaction had no impact on the results for the year ended 31 December 2005.

On 10 April 2006, the directors of Hermes Investment Management Ltd agreed to sell the company's holding of 107,600 shares in Innisfree Ltd.

HERMES PENSIONS MANAGEMENT LIMITED

NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)

22. LIMITED PARTNERSHIPS

As described in accounting policy c), the results of certain limited partnership were not consolidated in 2004. Had these been consolidated, the effect on the consolidated 2004 balance sheet would have been to increase fixed assets by £561.8 million, decrease net current assets by £2.3 million and increase associated minority interests by £559.5 million. In the consolidated profit and loss account, investment income would have increased by £11 million, expenses by £563,000 and associated minority interests by £14 million. In the consolidated statement of total recognised gains and losses, the revaluation of investments would have increased by £80 million along with an increase in associated minority interests of the same amount. Consequently, the effect on net assets, retained profit and total recognised gains and losses was nil.

23. RELATED PARTY TRANSACTIONS

During the year there were transactions with the following related parties:

The Trustees of the BT Pension Scheme

The following fees were paid by the Hermes group on behalf of the BT Pension Scheme in respect of the Trustees' services to the BT Pension Scheme.

	2005 £'000	2004 £'000
Sir Tim Chessells (Chairman)	75	75
S B Birkenhead	28	24
D W Davies	18	25
C N J Long	23	23
D M MacDonald	21	18
H Marchant	24	24
W McClory	21	21
Total fees	<u>210</u>	<u>210</u>

Hermes Group Pension Scheme

Certain activities of the Scheme are carried out by the Hermes group, all of the costs of which are borne by Hermes Pensions Management Limited. These costs have not been apportioned for accounting purposes between those attributable to the Scheme and those attributable to the Hermes group as functions maintained for both entities cannot be divided meaningfully between them.

Parent Undertaking

The company is a wholly owned subsidiary and consolidated into the accounts of the BT Pension Scheme, which are available to the public. As such, the company has not disclosed related party transactions with the BT Pension Scheme, as it is taking advantage of the exemption in FRS8 available to wholly owned subsidiaries.

HERMES PENSIONS MANAGEMENT LIMITED

NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)

23. RELATED PARTY TRANSACTIONS (continued)

Subsidiaries

The company prepares group accounts into which all of its subsidiaries are consolidated, save as disclosed in note 21. The company has not disclosed related party transactions with subsidiaries as it is taking advantage of the exemption in FRS8.

Associated Undertakings

Hermes Focus Asset Management Europe Ltd

HFAME is an associate of Hermes Focus Asset Management Ltd which is a 100% subsidiary of Hermes Pensions Management Ltd. During the period HPML recharged £1,789,702 (2004 - £1,607,516) of expenditure to HFAME. At 31 December 2005 £494,460 (2004 - £339,776) of this amount was included in debtors.

Activa Capital

Activa is an associate of Hermes Private Equity Management (HPEM) which is a 100% subsidiary of Hermes Pensions Management Ltd. During the period HPEM received dividends of £201,430 from Activa. HPEM purchased shares in Activa totalling £107,674. HPEM also made a loan of £94,894 to Activa.

Hermes UK Focus Funds

The Hermes UK Focus Funds are partnerships investing in UK equities. Hermes Focus Asset Management Limited (HFAM) is the General Partner. During the year there were the following transactions between the UK Focus Funds and HFAM:

- HFAM received £3,132,461 (2004 - £2,862,188) from the Hermes UK Focus Fund, £1,033,826 (2004 - £893,094) from the Second Hermes UK Focus Fund and £2,186,446 (2004 - £2,194,207) from the Third Hermes UK Focus Fund as profit share.
- HFAM recharged £73,640 (2004 - £80,443) of expenditure to the Hermes UK Focus Fund, £31,017 (2004 - £33,989) to the Second Hermes UK Focus Fund and £48,685 (2004 - £60,034) to the Third Hermes UK Focus Fund. This expenditure represented the direct costs of the partnership.

Hermes UK Small Companies Focus Fund

The Hermes UK Small Companies Focus Fund (UKSCFF) is a partnership investing in UK Small Company equities. HFAM is the general partner. During the year there were the following transactions between UKSCFF and HFAM:

- HFAM received £1,761,673 (2004 - £1,112,201) from UKSCFF as profit share.
- HFAM recharged £29,423 (2004 - £28,700) of expenditure to UKSCFF. This expenditure represented the direct costs of the partnership.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****24. MINORITY INTEREST - EQUITY**

The minority interest of £135,065 (2004 - £126,808) included within the consolidated balance sheet relates to the 40% shareholding of Hermes UOB Capital Management Limited (HUCM) owned by UOB Global Capital LLC.

25. ULTIMATE PARENT UNDERTAKING

The directors regard the BT Pension Scheme as the company's immediate and ultimate parent and controlling entity. It is also the parent of the largest and smallest group to prepare group accounts into which the results of the company are consolidated. The accounts of the BT Pension Scheme can be obtained at Lloyds Chambers, 1 Portsoken Street, London E1 8HZ.

26. PRIOR YEAR ADJUSTMENT

The Group has, as required, implemented the disclosure requirements included in FRS 17 relating to Retirement Benefits. The assets and liabilities under the revised reporting structure are included in financial statements for the year ended 31 December 2005. A prior year adjustment has been included to present the adjustments that would have been required in the year ended 31 December 2004 and the correct opening position for the current year.

A further prior year adjustment has been made to reflect a loss of £20,000 relating to the sale of the investment in ECROSSNET.

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****26. PRIOR YEAR ADJUSTMENT (continued)**

The effects of this revised reporting, and the investment sale adjustment, are summarised as follows:-

	2004 £'000
Profit and loss account	
Removal of Pension Contributions under SSAP 24 – Administrative expenses	2,500
Inclusion of Current Service Cost FRS 17 – Administrative expenses	(3,000)
Add back of excess contributions over SSAP 24 required amount – Other finance income	(375)
Realised Loss on sale of Investment	(20)
Expected Return on Scheme Assets – Other finance income	2,700
Interest Payable on Scheme Liabilities – Other finance income	(2,500)
Decrease in profit for the financial year	(695)
Statement of Total recognised gains and losses	
Actual return less expected return on Pension Scheme assets - gain	1,500
Changes in assumptions underlying the present value of Pension Scheme liabilities – loss	(1,600)
Adjustment to prior year Profit and loss account for SSAP 24 Pension provisions	4,599
Inclusion of Pension Scheme assets as at 1 January 2004	33,200
Inclusion of Pension Scheme liabilities as at 1 January 2004	(47,500)
Decrease in total recognised gains / losses in the financial year	(10,496)
Balance Sheet	
Investments	(20)
Provisions	4,224
Pension Scheme Reserve	(14,700)
Decrease in net assets	(10,496)

HERMES PENSIONS MANAGEMENT LIMITED**NOTES TO THE ACCOUNTS - YEAR ENDED 31 DECEMBER 2005 (continued)****27. LITIGATION**

An action has been brought against Hermes Investment Management Limited (HIML), a company within the Group, in South Korea in respect of the actions of a former fund manager and alleged breaches of the South Korean Securities and Exchange Act. The company has been advised that it has not breached the relevant legislation and will be strongly defending the action. Accordingly no provision has been made in the accounts of the group for any costs associated with the case apart from those costs incurred up to the financial year end.