



Providing...
Protection
for business



Contents**Report of the Directors**[03 2010 Highlights](#)[04 Chairman's Statement](#)**Group Overview**[06 Our Structure](#)[08 Our Performance](#)[10 Our Brand](#)[12 Our People](#)**Strategy & Achievements**[15 Chief Executive's Statement](#)[18 Group Strategy](#)[20 Progress against Objectives and Key
Performance Indicators](#)**Business Review**[22 The Business Environment](#)[24 Global Markets](#)[28 Reinsurance](#)[31 UK](#)[34 Claims](#)[35 Operations](#)[36 Risk Management and Risk Factors](#)**Financial Review**[41 Financial Performance](#)[44 Financial Management](#)[47 Investments](#)**Governance**[50 Board of Directors](#)[52 Corporate Governance Report](#)[59 Directors' Remuneration Report](#)[66 Directors' Responsibility Statement](#)[67 Sustainability](#)[71 Investors](#)**Financial Statements**[74 Consolidated Income Statement](#)[75 Consolidated Statement of
Comprehensive Income](#)[76 Consolidated Statement of
Financial Position](#)[77 Consolidated Statement of
Cash Flows](#)[78 Consolidated Statement
of Changes in Equity](#)[80 Notes to the Financial Statements](#)[131 Independent auditor's report
on the Consolidated Financial
Statements](#)[133 Balance Sheet of Brit Insurance
Holdings N.V.](#)[134 Income Statement of Brit Insurance
Holdings N.V.](#)[135 Statement of Changes in Equity
of Brit Insurance Holdings N.V.](#)[136 Notes to the Financial Statements
of Brit Insurance Holdings N.V.](#)[139 Other Information](#)[140 Independent auditor's report
on the Parent Company Financial
Statements](#)**Other Information**[142 Glossary](#)[145 Shareholder and Depositary Interest
Holder Information](#)


Brit Insurance is an international general insurance and reinsurance group specialising in commercial insurance.

Our distribution model is centred on brokers and intermediaries and we aim to deliver an excellent service to them and their clients – through the range of cover we offer, our underwriters' expertise, and our specialist, market-leading claims teams.


Reflecting how and where our customers trade, we are organised into three strategic business units – Global Markets, Reinsurance and UK which have access to our underwriting platforms including Brit Insurance Limited and our Lloyd's syndicate, Syndicate 2987.

Further information


→ Our Structure
See page 06




→ Our Performance
See page 08




→ Our Brand
See page 10




→ Our People
See page 12




→ Chief Executive's Statement
See page 15




→ Progress against Objectives
See page 20



→ Strategic Business Units
See page 24



→ Financial Performance
See page 41



2010 Highlights

Return on equity excluding the effect of foreign exchange on non-monetary items

14.4%

17.4% 2009

Combined ratio excluding the effect of foreign exchange on non-monetary items

97.1%

94.0% 2009

Distributions paid during the year of

60.5p

per share

60.0p 2009

Headline return on equity of

14.2%

12.2% 2009

Profit before tax (PBT) excluding the effect of foreign exchange on non-monetary items

£119.2m

£171.3m 2009

Net tangible assets (NTA) per share of

£11.41

represents growth of 8.5% during 2010

Gross written premium of

£1,530.2m

a reduction of 9.8% or 10.4% at constant currency. The reduction reflects active management of the underwriting portfolio and is in line with the Group's plan

Profit after tax of

£110.5m

£87.5m 2009

up 26.2%, and earnings per share of 142.4p, up 25.8% (2009: 113.2p)

Operational and strategic highlights

Successful first year with new Netherlands-based holding company

Continued active management of the underwriting portfolio throughout the business

Further talent attracted to the Group together with a number of senior appointments from within the business

Significant progress made on driving upper quartile performance throughout the Group as part of the 'Average to Outperform' agenda

Further information



View our website
www.britinsurance.com



Chairman's Statement

Result

I am pleased to announce that the Group recorded profit before tax of £119.2m and a return on equity of 14.4% (both excluding the effect of foreign exchange on non-monetary items). This is a good result given the increased major claim burden faced by the Group and the continued tough economic conditions.

Strategic progress during 2010

2010 was a quieter period in terms of headline strategic activity but underlying this a huge effort has been put in by all staff to build on the 'Average to Outperform' programme established in 2009. This programme is designed to raise performance across the entire Group and develop a culture of outperformance. Major strides have been made during 2010 in terms of managing and optimising the underwriting portfolio, as can be seen in the significant improvement to Global Markets's attritional claims ratio, improving expense efficiency and the continuation of talent management through internal promotions and external recruitment. Managing the underwriting portfolio has constrained growth but has already improved its underlying quality. Much of the benefit from these initiatives will become evident over the coming years.

Recommended cash offer by Achilles Netherlands Holdings B.V.

On 26 October 2010 Brit Insurance announced that the Independent Directors of the Board were recommending a cash offer from Achilles. The per share proposal of 1045p, a Contingent Value Payment (CVP) of up to 25p and the 2010 interim distribution valued each Brit Insurance share at up to 1100p. The acquisition of the Group is expected to close during the first quarter of 2011.

Shareholder distributions

In light of the recommended cash offer from Achilles, the Board is not recommending a final distribution for 2010. Shareholders have, however, received distributions of 60.5p per share during 2010 in the form of reductions in the par value of each share.

Board of Directors

In December 2010, Matthew Scales stepped down from the Board after 15 years with the Group and the last ten years as Group Finance Director. I would like to take this opportunity to once again thank Matthew for his service over the years and his steadfast loyalty to the Group.

In the event that the acquisition of the Group by Achilles is successful, there will be a number of changes to the Board. A number of the non-executive directors including me will step down and be replaced by six new non-executive directors. These appointments were approved by shareholders in December 2010 and will take effect once the offer is declared unconditional. I wish to thank all the Board directors for their service and wisdom, and wish the new directors good luck in steering the Group through the next stage of its development.

John Barton
Chairman
24 February 2011



Group Overview

06 Our Structure

08 Our Performance

10 Our Brand

12 Our People

Our Structure

Brit Insurance Group at a glance

Brit Insurance (the Group) is a general insurance and reinsurance group specialising in commercial insurance.

The Group writes a diverse portfolio of insurance and reinsurance offering protection for businesses worldwide. The scope is wide-ranging: from sole traders to the largest multinational corporations; from manufacturers to professional services; from shops to satellites. The distribution model is centred on brokers and intermediaries.

The Group serves its customers through three strategic business units (SBUs) – Global Markets, Reinsurance and UK. Each SBU underwrites through two regulated underwriting platforms: Lloyd's Syndicate 2987 and Brit Insurance Limited (BIL).

Lloyd's Syndicate 2987

The largest portion of the Group's ongoing business is written by the Group's wholly-aligned Lloyd's syndicate, Syndicate 2987, which as part of Lloyd's is regulated by the FSA. For the 2011 Year of Account, Syndicate 2987 will have an initial capacity of £760m (2010 Year of Account: £745m) and this will be reviewed and monitored throughout the year. Syndicate 2987 has licences, through Lloyd's, to write insurance business in over 65 territories including the US, and licences to write reinsurance business in these and many other territories.

Brit Insurance Limited

Brit Insurance Limited (BIL) is the Group's UK-based insurance company, authorised and regulated by the FSA. In 2010, BIL wrote 41.4% (2009: 47.0%) of the Group's business. BIL benefits from financial strength ratings of A (Strong) with stable outlook from Fitch Ratings and A (Excellent) under review with negative implications from AM Best. It is licensed to write most lines of insurance business in the UK and EEA territories and reinsurance business in these and a number of other territories.

Brit Insurance (Gibraltar) PCC Limited

Brit Insurance (Gibraltar) PCC Limited (BIG) is the Group's wholly-owned intra-group reinsurer, licensed and regulated by the Gibraltar Financial Services Commission. BIG writes a number of intra-group reinsurance contracts on both an excess of loss and a quota share basis. At 31 December 2010, BIG had capital of over £480m.

Group

Brit Insurance Holdings N.V.

Insurers

Brit Insurance Limited

Syndicate 2987

Reinsurer

Brit Insurance (Gibraltar) PCC Limited

SBUs

Global
Markets

Reinsurance

UK

Organised for...

Stability & efficiency

We underwrite a diverse portfolio of risks through three strategic business units and offer clients access to two financially strong underwriting platforms

Our Structure continued

Our office locations

The Group has offices in Chicago, USA, Sydney, Australia and Tokyo, Japan and nine offices throughout the UK. The Group's holding company Brit Insurance Holdings N.V. is located in the Netherlands. Brit Insurance (Gibraltar) PCC Limited (BIG) is the Group's intra-group reinsurer and is located in Gibraltar.



UK office locations



Our Performance

Positioned for...

Sustainable returns

We delivered a return on equity of 14.4% for 2010 and paid distributions of 60.5p per share during the year.

Our performance

In 2010 Brit Insurance produced a return on equity excluding the effect of foreign exchange on non-monetary items of 14.4% (2009: 17.4%). Gross written premium reduced by 10.4% at constant exchange rates reflecting proactive management of the underwriting portfolio and the Group's decision to decline business where margins were no longer adequate. Across the portfolio premium rate increases averaged 1.0% on renewed business. The Group combined ratio excluding the effect of foreign exchange on non-monetary items was 97.1% compared with 94.0% in 2009.

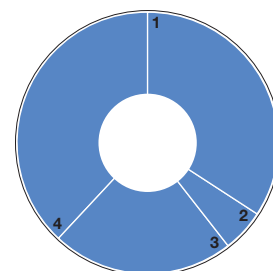
Performance	2010	2009
Gross written premium	£1,530.2m	£1,696.4m
Profit before tax ¹	£119.2m	£171.3m
Combined ratio ¹	97.1%	94.0%
Return on equity ¹	14.4%	17.4%
Net tangible assets per share	£11.41	£10.52

¹ Excluding the effect of foreign exchange on non-monetary items.

Diversity by location of risk

Gross written premium

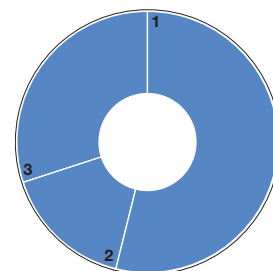
	2010 £m	2010 %	2009 £m	2009 %
1. United Kingdom	523.7	34.2	491.0	29.0
2. Europe (excluding UK)	84.4	5.5	128.7	7.6
3. United States	343.6	22.5	416.2	24.5
4. Worldwide & Other	578.5	37.8	660.5	38.9
	1,530.2	100.0	1,696.4	100.0



Diversity by tail of business

Gross written premium

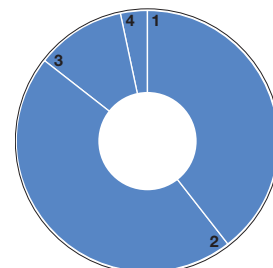
	2010 £m	2010 %	2009 £m	2009 %
1. Short tail (<1.5 years)	825.6	54.0	863.0	50.9
2. Medium tail (1.5 to 3.0 years)	245.8	16.0	274.9	16.2
3. Long tail (>3.0 years)	458.8	30.0	558.5	32.9
	1,530.2	100.0	1,696.4	100.0



Diversity by currency

Gross written premium

	2010 £m	2010 %	2009 £m	2009 %
1. Sterling & Other	603.8	39.5	711.2	41.9
2. US dollar	708.3	46.3	743.1	43.8
3. Euro	168.8	11.0	166.4	9.8
4. Canadian dollar	49.3	3.2	75.7	4.5
	1,530.2	100.0	1,696.4	100.0



Our Performance continued



Global Markets

Seeks to be a highly respected market leader delivering underwriting excellence based on market intelligence and innovation in its chosen fields and disciplines.

The Global Markets SBU has an extensive history of providing a comprehensive range of insurance products for small to medium sized enterprises as well as large corporate customers globally. The SBU is made up of a number of niches which are expert in their respective fields and bring a broad spread to the portfolio. Business is distributed entirely through intermediaries. The SBU accesses business through leading brokers in its main operations in London as well as through delegated authorities with selected coverholders, including the Group's wholly-owned service company, who distribute products into local markets. This underwriting capability is backed up by first class claims handling through specialist staff in London and in overseas claims hubs.

Performance	2010	2009
Gross written premium	£778.3m	£875.3m
Profit before tax ¹	£34.6m	£42.8m
Risks led (by value)	56.0%	59.1%
Retention ratio (by value)	74.0%	71.3%
Combined ratio ¹	97.7%	96.9%

Reinsurance

Aims to build a diverse and high quality multi-class and multi-territory book of business by participating in this potentially high margin but volatile global business.

The Reinsurance SBU writes multi-class and multi-territory reinsurance with a focus on providing excess of loss reinsurance to a broad range of clients globally. The Group transacts reinsurance business exclusively through broker intermediaries with clients ranging from small local mutual insurers to large well-known global insurance groups. It offers the capacity to quote and lead business, whilst aiming to deliver a first class all-round service to customers backed up by its specialist contractual documentation and claims handling teams.

Performance	2010	2009
Gross written premium	£309.6m	£364.2m
Profit before tax ¹	£37.2m	£66.1m
Risks led (by value)	35.9%	36.0%
Retention ratio (by value)	85.6%	87.0%
Combined ratio ¹	88.2%	79.9%

UK

Aims to be a significant player in its chosen market segments. Ease of access, expertise, service and execution skills will differentiate the SBU from its peers.

The UK SBU underwrites a diverse book of UK commercial and specialist personal insurance through a combination of regional, national and international brokers. The SBU's target market focuses on sole traders through to corporates with turnover of up to £300m. Over the last three years the Group has been successful in developing online trading solutions for micro-SME business, underwriting commercial insurance with premium values typically less than £2,000 per policy. The SBU has a carefully targeted distribution strategy with 80% of its commercial business sourced through its top 75 brokers.

Performance	2010	2009
Gross written premium	£441.2m	£455.4m
Profit before tax ¹	£14.3m	£14.2m
Risks led (by value)	92.5%	94.1%
Retention ratio (by value)	66.4%	68.6%
Combined ratio ¹	99.8%	99.7%

¹ Excluding the effect of foreign exchange on non-monetary items.

Our Brand

Brand strategy

Cricket

With effect from January 2010 Brit Insurance became the principal sponsor of the England cricket teams, with Brit Insurance branding on all playing and training kit. With extensive broadcast and print media coverage of the teams, enhanced by victories in the Twenty20 World Cup and in the Ashes series in Australia for the Men's team, awareness of the Group has increased significantly among target audiences.

Investing for...

A strong identity

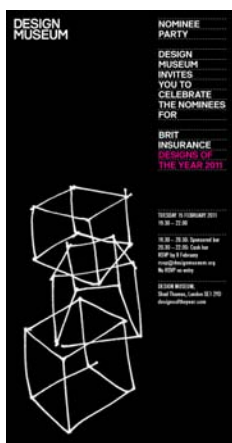
Our strategy focuses on developing a successful and recognisable brand among intermediaries and potential customers.



Our Brand continued

Design

2010 was the third year of the Group's partnership with the Design Museum, the world's foremost museum devoted to contemporary design. The Brit Insurance Design Awards, and supporting exhibition, the Brit Insurance Designs of the Year, continued to increase the visibility of Brit Insurance in the media and with key associated audiences. The winner in 2010, Min Kyu Choi's folding three pin plug, has gone from prototype to production and confirms the importance that good design plays in our every day lives.



In May 2010 we announced a four year partnership with the Cricket Foundation's Chance to Shine programme. Chance to Shine works with state schools, reaching into classrooms by linking into the national curriculum and delivering cricket skills. The programme draws together people from all cultures and backgrounds and gives opportunities to boys and girls including those with special educational needs to acquire important skills, values and attitudes for their future lives.



Our People

Our talented teams

We continue to focus on a culture of achievement to ensure we attract, train and retain talented people, and we pride ourselves on creating a demanding yet rewarding environment that encourages dedicated individuals to outperform.

Our charitable giving and community involvement also ensures our teams play a wider part in the Group's contribution to society.

Insurance Day London Market Awards 2010 – Young Underwriter of the Year

North American Professional Indemnity underwriter Jonathan Mudd was awarded the prestigious Young Underwriter of the Year award.

Richard Banks, editor of Insurance Day, said: "Jonathan was hailed for having an exceptional ability to see opportunities in professional liability risks, frequently finding creative solutions to resolve transactions. His business acumen combined with his significant contribution to developing young talent in the London Market made him an outstanding candidate."



Inspiration for...

Our award-winning team

We continue to focus on a culture of achievement to ensure we attract, train and retain talented people.

Jonathan Mudd Young Underwriter of the Year

Our People continued

Chartered Insurance Institute – Rutter Prize

Alan Groves, Head of Reinsurance Operations, was awarded the Chartered Insurance Institute's Rutter Prize, one of the Institute's highest accolades. The medal is awarded annually to the best new Fellow of the Chartered Insurance Institute (FCII).

Community involvement – Chance to Shine

Peter Grocock, Head of our Bristol office supported the "Chance to Shine" National Cricket Day programme in June 2010 at St Werburgh's Primary School. Peter attended a morning of cricket themed activities in the school playground led by England cricket ambassadors, Alastair Cook and Charlotte Edwards. The purpose of the day was to raise awareness of cricket amongst Year 5 and 6 school pupils and to promote teamwork and leadership. The day was a great success and has since resulted in a request from St Werburgh's for Brit Insurance's Bristol office to become an ongoing partner to the school to work as a role model from the business world.



Alan Groves Head of Reinsurance Operations



Peter Grocock Head of Bristol Office



Strategy & Achievements

15 Chief Executive's Statement

18 Group Strategy

20 Progress Against Objectives and
Key Performance Indicators

Chief Executive's Statement

“Thanks to the dedication of our employees I have no doubt that the Group ended 2010 in a far stronger position than it began the year.”

▼
Return on equity excluding the effect of foreign
exchange on non-monetary items of

14.4%
17.4% 2009



Dane Douetil Chief Executive Officer

Another year of development

2010 has been another key year in the development of Brit Insurance to become a leading international insurance and reinsurance group. Whilst the headlines may have been dominated by the recommended cash offer by Achilles Netherlands Holdings B.V. (Achilles), the real hard work of developing Brit Insurance has continued unabated. Thanks to the dedication of our employees I have no doubt that the Group ended 2010 in a far stronger position than it began the year.

Key highlights for 2010 include:

- ▶ Developing the 'Average to Outperform' programme that aims to take the Group's performance to the top quartile of our peer group
- ▶ Continued active management of the underwriting portfolio, with our underwriters supporting brokers and clients in areas where sustainable returns can be achieved – but willing to walk away where this is no longer the case
- ▶ Managing our expense base so as to allow us the flexibility to reduce top line when it is the right thing to do rather than slavishly following the market cycle
- ▶ Further developing the talent within the organisation through a combination of promotion and advancement for key internal talent, high quality external hires and a more proactive approach to managing poor performance

Each of these developments, discussed in more detail below, is aimed at improving the sustainability and effectiveness of our operations and consequently supporting our relentless focus on improving our return on equity.

Average to Outperform

In late 2009 we set out an agenda which targeted top quartile performance across the Group. This is known internally as 'Average to Outperform'. The focus during 2010 was on putting in place the necessary building blocks for delivering the changes required by this agenda.

Areas of focus have included enhanced external benchmarking, significantly improved underwriting analytical tools and management information, improved training for professional managers and underwriters, including a relaunched underwriters toolkit, and a series of workshops to help all Group staff understand the cultural and behavioural aspects of the change.

Chief Executive's Statement continued

Whilst the framework for 'Average to Outperform' is now in place, delivery will depend on how well we translate this into 'business as usual', a journey that we are only just beginning.

Active management of the underwriting portfolio

Faced with a competitive market, the SBUs have continued to be active in their management of the Group's underwriting portfolio. In 2008 and 2009 the most significant portfolio adjustments came within Global Markets as it reduced weighting to long-tail casualty lines of business that more heavily rely on investment income and towards short-tail property and marine classes. In 2010, this portfolio management approach delivered, with a short-tail combined ratio in Global Markets of 91.5% despite catastrophe claims equivalent to 4.2 percentage points.

For 2010, the UK SBU streamlined its product focus with a significant reduction in the Private Motor account and a withdrawal from Local Authority (Municipal) business. These underwriting decisions were made in response to a combination of changing distribution trends, a prediction of a deteriorating claims environment and current underwriting returns. In each case the Group concluded that it was unlikely to generate a sustainable profit stream into the future. These actions have also enabled the UK to focus on its core client base of small to mid-sized commercial enterprises with a turnover of less than £300m per annum.

Managing our expense base

The key markets in which we operate remain competitive and as such we are prepared in the short-term to walk away from inadequately priced business. In order to achieve this without a significant impact on our expense ratios we remain focused on cost management throughout the business. In 2010 core expenses (excluding commissions, regulatory levies and offer related costs) were stable despite a new holding company in the Netherlands and the high cost of preparing for Solvency II. We will continue to work on managing our cost base such that we can make the required underwriting decisions without having to make short-term expense reductions.

Talent management

Employees remain the lifeblood of an insurer and managing talent appropriately will be key to our success. During 2010 we continued to attract high quality external talent as well as developing internal talent through advancement and promotion. These trends have been experienced at all levels of the organisation. The Executive Management Committee in the UK has made three internal appointments – Ray Cox to CEO of the UK SBU, Baldeep Johal to the newly-created role of Chief Risk Officer and Lorraine Denny continuing her role as Director of Human Resources – as well as welcoming Scott Egan as Chief Financial Officer, who joined in January 2011 from Zurich Financial Services.

At the same time we improved our performance management system and updated our remuneration policy to ensure that we have a greater emphasis on rewarding excellent performance as well as identifying and addressing poor performance in a more proactive manner. We are confident these changes will drive the business forward and help raise the bar across the entire organisation.

2010 results and distribution

The underwriting market in 2010 played out in line with our expectations. The UK market continued its slow grind of positive premium rate increases but against a still competitive backdrop, whilst Reinsurance was broadly stable. Global Markets experienced a mixture of pricing trends across its diverse portfolio with average rate movements ranging from -1% to +1%. Overall, a rate increase of 1.0% was hard-earned by our underwriters and vindicates our policy of walking away from business where price pressure was too great.

▼
Reserve releases for the year

£72.4m
£81.2 2009

Further information



Our Structure
See page 06



Progress against Objectives
See page 20



Strategic Business Units
See page 24



Chief Executive's Statement continued

Overall we delivered another respectable result in a challenging market. Return on equity (excluding the effect of foreign exchange on non-monetary items) was 14.4% compared with 17.4% in 2009. The lower RoE is explained by weaker investment return and higher major claims from the significant earthquake activity during the year. The combined ratio of 97.1% included 4.4 percentage points relating to the earthquakes in Chile and New Zealand. I am pleased that the level of releases from prior years' claims reserves remained significant at £72.4m (2009: £81.2m) demonstrating the robustness of the Group's reserving policy. Growth in net tangible assets per share was 8.5%.

In light of the recommended cash offer from Achilles, the Board is not recommending a final distribution for 2010; however, shareholders have received a total of 60.5p per share in distributions during 2010 (2009: received 60.0p).

Solvency II

We made further good progress in 2010 in preparing for the Solvency II regulatory regime due to come into force in 2013. The Group is working alongside Lloyd's to ensure that the Group is Solvency II ready, as well as engaging directly with the FSA in relation to Brit Insurance Limited (BIL) and the Gibraltar FSC in relation to Brit Insurance (Gibraltar) PCC Limited. In each case the Group has completed the recent QIS5 exercise. In respect of BIL we have received pre-application clearance and have entered BIL into the FSA's Internal Model Approval Process (IMAP).

We fully support the need for consistency in the treatment of policyholders across Europe. We therefore hope that all regulators ensure that their responses to satisfy this aim are proportionate and balance the risks against the cost of implementation.

Outlook

We expect the backdrop of competitive market conditions and modest pressure on premium rates to continue in 2011. In Global Markets we will continue to take a defensive position in longer-tail casualty classes of business until we see rate increases that offset the effect of low interest rates. Within short-tail lines, results have again been good and we will need to focus even more on our core underwriting skills of risk selection to steer us through this point of the underwriting cycle.

The UK market is pushing through rate increases albeit at a slower rate than we believe is required. We remain concerned that the longer this situation continues, the greater the potential market correction will need to be; a situation that is likely to be to the detriment of the market's reputation as a whole. We will continue to support our clients through our regional network of offices during this tough phase of the market.

Within Reinsurance, January 2011 renewals showed continued competitive pressure across most classes of business, most noticeably in our US Property Treaty account. However, despite this and thanks to the spread of our portfolio, rates overall on our renewal book remained broadly flat compared to 2010.

During the first quarter of 2011 above average claims activity has continued in the International Property arena with extensive flooding in Eastern Australia, Cyclone Yasi affecting Queensland, Australia and a major earthquake near Christchurch, New Zealand. Early indications suggest that neither of the Australian events should be major claims for the Group (i.e. more than £10m net to the Group) and in aggregate are estimated not to exceed £15m. The Group expects claims arising from the February 2011 New Zealand quake to be significant for the market. It is too early to assess accurately the Group's exposure to this event.

The Group's focus in 2011 will be on continuing to develop the 'Average to Outperform' agenda and embedding the disciplines required to be an upper quartile performer. The current competitive market means that this journey is not an easy one. However, having seen at first hand the strides made by the Group's staff over the last 18 months I know that we have the ambition, skills and strategic plans to achieve this.

Dane Douetil CBE
Chief Executive Officer
24 February 2011

Group Strategy

Vision

The Group's vision is to be a leading international general insurance and reinsurance group. This will be delivered through size, scale and diversity.

Group long-term goals

Sustainable Business

Delivering sustainable propositions across chosen markets.

The Group aims to move towards business that is less volatile over time. The strategic business units will focus predominantly on the small and medium-sized markets, where loyalty is often greater and price competition less severe.

Multi-Channel Distribution

Creating closer links with customers, developing relationships and distribution channels.

Brit Insurance remains committed to the broker and intermediary model, whilst acknowledging the benefits of technology to support distribution.

Service Excellence

Delivering high quality service to customers, clients and colleagues with speed and consistency.

The Group recognises that a key differentiator is the provision of first class service to customers, brokers and colleagues through speed and quality of service delivery.

Operational Effectiveness

Focusing on the balance between operational effectiveness and efficiency.

To create value for shareholders, it is critical that Brit Insurance demonstrates it can add more value as a group than the businesses do on a stand-alone basis.

Talent Management

Focusing on people, skills, competencies and culture.

The Group will continue to focus on attracting, developing and retaining talented people.

Responsible Growth

Increasing the size of the organisation through sustainable growth through the cycle.

The ambition is that the Group will grow, achieving a return on equity in excess of 15% over the insurance cycle and assuming normalised investment markets, while working within financial return and risk appetite parameters.

Financial Strength and Diversity

Creating diversification of risk income and building fee income to enhance financial strength, stability and flexibility.

Brit Insurance will be known not only for financial strength and stability but also for capital flexibility.

Spread of Reach

Creating scale of market share in horizontal and vertical markets.

The Group will develop businesses that spread its reach into chosen markets. These will range from sectors that use skills to create new products, such as Brit Lite, to regions where market share can be built such as the US and Europe.



Group Strategy continued

Strategic objectives

The Group's short-term strategic priorities are influenced by the market outlook over the next 12-24 months and are aligned to the long-term goals of Sustainability and Operational Effectiveness. The 'Average to Outperform' programme was initiated during 2009 and targets:

- ▶ Developing and measuring top quartile underwriting performance both compared to its Lloyd's peer group and against a wider set of defined peers
- ▶ Reducing claims leakage through a series of targeted actions
- ▶ Embedding risk management and the regulatory requirements of Solvency II
- ▶ Improving delegated underwriting management capabilities
- ▶ Driving operational effectiveness through streamlining the operating model
- ▶ Enhancing technology platforms to improve the effectiveness and efficiency of underwriting, claims and business management processes

The programme is complemented by a continuing focus on developing and motivating talented people with the appropriate technical and managerial skills.

The 'Average to Outperform' programme is expected to be a continued focus through 2011 and 2012, embedding a performance culture and delivering upper quartile underwriting results.

The core insurance competencies for the business are risk origination, risk pricing, loss adjusting, portfolio management and asset management supported by service delivery and communication. These competencies are supported by brand, operational effectiveness and efficiency and a participative approach to business partners.

Further information

→
 Our People
[See page 12](#)



Progress Against Objectives and Key Performance Indicators



Performance metric

Adjusted return on equity (RoE) = profit after tax excluding foreign exchange on non-monetary items and amortisation divided by opening net tangible assets adjusted for capital movements during the year.

Shareholder distribution per share = dividend plus capital return divided by number of shares.

Growth in net tangible assets per share = change in net assets less intangible assets divided by number of shares.

Combined ratio = claims net of reinsurance recoveries plus expenses divided by earned premium net of reinsurance premiums.

No unauthorised breaches of catastrophe risk tolerance matrix (see page 93 for details of matrix).

Staff turnover excluding retirements and redundancies.



Why it is key

The ultimate measure of the Group's value creation for shareholders. Sustainable RoE in excess of the Group's cost of equity demonstrates delivery of long-term economic value added.

Represents the cash payment to shareholders for holding the Group's shares.

Growth in net tangible assets per share is primarily a reflection of RoE less distributions to shareholders and is a key determinant of share price performance.

Demonstrates the Group's underwriting profitability.

An indication of how much risk is being taken to achieve the Group's RoE and combined ratio.

The retention of key talent is vital for the Group to continue to deliver a sustainable business.



2010 (2009) outcome

14.4% (17.4%)

60.5p (60.0p)

8.5% (6.0%)

97.1% (94.0%)

No unauthorised breaches in either year

11.6% (8.2%)



Performance versus Group's target and goals

In line with business plan and ahead of the Group's current estimate of its cost of equity of between 10-11%.

In line with the Group's policy to base the distribution on the 2008 dividend of 60p per share. NB In light of the recommended cash offer by Achilles, no final distribution for 2010 has been recommended.

In line with RoE less shareholder distributions.

Higher than planned combined ratio due to major claims and higher expense ratio. The latter is primarily as a result of lower premium arising from the Group's active management of the underwriting portfolio.

In line with target.

1.9 percentage points lower than the 2009 national average (latest data available).

Return on equity and five year average (%)



The RoE in the five year chart above includes the effect of foreign exchange on non-monetary items.

Over the last five years the Group has on average generated a return on equity of 15.9%.

Business Review

22 The Business Environment

24 Global Markets

28 Reinsurance

31 UK

34 Claims

35 Operations

36 Risk Management and Risk Factors

The Business Environment

Overview

The insurance industry within the developed world continues to operate under competitive conditions. Premium rate movements were broadly unchanged across the wider market and where increases were achieved this was generally in individual markets where specific conditions were prevalent, e.g. UK motor, Gulf of Mexico energy. With a healthy capital position and demand that remains constrained, the industry is likely to see similar competitive conditions in 2011.

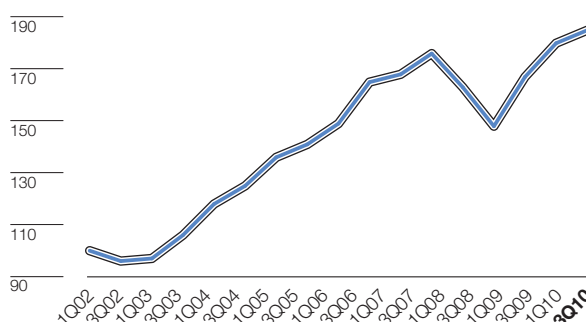
The Group considers the key short to medium-term external drivers of premium rate movements to be capital availability, global growth, claims experience and investment returns. Over the longer term, changes to insurance penetration and distribution methods also have a significant influence.

Capital availability and global GDP

Over the last two years the level of available capital within the global insurance industry has returned to the levels experienced prior to the financial crisis. As an example, the level of capital within the US insurance industry (as measured by ISO) increased by 20% from the start of 2009 to September 2010 and is 4% higher than its previous high in mid-2007. The rebound has primarily resulted from a reversal of unrealised losses on investments over the period.

Over the same period the level of capital in the global reinsurance industry (as measured by Aon Benfield) increased by 38%.

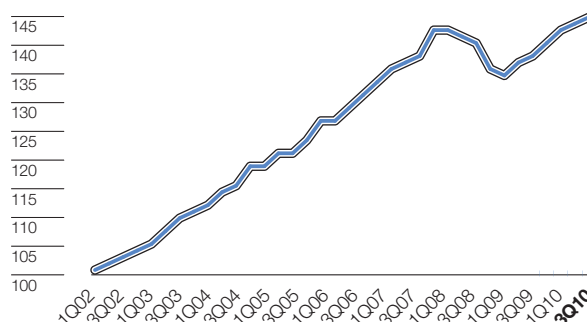
US insurance industry surplus index



Source: ISO

On the demand side, global GDP has corrected (as shown below for the US), thanks in a large part to the US government stimulation programme, but remains behind the trend experienced from 2002 to 2007. In the UK, fourth quarter 2010 real GDP turned negative, once again highlighting the potential risk to economic growth from necessary austerity packages. In this environment the demand for insurance remains constrained.

US nominal GDP index



Source: Bloomberg

The result of high capital levels and constrained demand suggests competitive conditions in most insurance markets will continue into 2011.

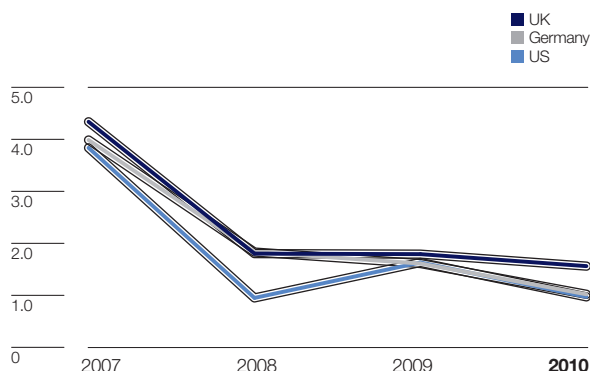
Low fixed income investment returns

Investment returns have historically made an important contribution to the overall profitability of the insurance industry; indeed the US insurance industry has made an underwriting profit in only three of the last nine years. Given solvency requirements, the majority of insurers' assets are fixed income and returns are therefore dependent on government bond yields and credit spreads for high quality corporate instruments.

Since the end of 2007 the returns available on three-year government bonds in the US, the UK and Germany have reduced by 2.2 percentage points in the US, by 2.8 percentage points in the UK and by 3.0 percentage points in Germany. This has materially reduced the level of investment income available to insurers and reinsurers.

The additional spread available to invest in corporate credit, based on a 1-3 year US corporate bond index, has been volatile over this period ranging from close to 6.0 percentage points in late 2008 to less than 1.0 percentage point at the end of 2010. Volatility reduced during 2010 with credit spreads ranging between 1.4 percentage points and 0.9 percentage points.

Three-year government bond yields (%)



Source: Bloomberg

The Business Environment continued

Claims experience

The total cost of claims from natural catastrophes was above average in 2010, but with a different mix when compared against previous years with above average catastrophe claims. Instead of arising from US hurricanes, the year's natural catastrophe activity was dominated by earthquakes and flooding in South America and Australasia. Estimated insured claims from natural catastrophes of US\$33.6bn rose over 50% compared with 2009 and was the fourth highest burden over the last ten years. The largest events were the earthquake in Chile and Winter Storm Xynthia in Continental Europe both in February 2010 and the earthquake in New Zealand in September 2010. In December 2010 and into early 2011, Eastern Australia suffered significant damage from flood and typhoon conditions. In the UK, weather in early and late 2010 was more severe than in recent years.

Estimated at US\$5.0bn, the level of insured property claims from man-made catastrophes was in line with the average since 2002. This includes an estimated US\$1.0bn for the property damage arising from the explosion on the Deepwater Horizon oil platform in April 2010.

Distribution

Distribution trends in 2010 mirrored those experienced in 2009. There was greater stability within the broker/intermediary market with lower levels of consolidation. Reduced business volumes saw certain insurers taking control of distribution through acquisition; and there was a continued shift towards e-trading in an attempt to streamline distribution processes and thereby reduce costs.

Throughout this period the Group has stayed loyal to its core philosophy of a distribution strategy centred on approved brokers and intermediaries. This has led to an increasing depth in relationships particularly with the Group's major producers and a selective engagement with Managing General Agents and Managing General Underwriters (MGAs/MGUs) ensuring a suitable alignment of interests.

The insurance market for micro-SMEs in the UK is also undergoing a significant transformation with e-commerce at its core. Customers, distributors and insurers are all driving the market online, motivated by ease, convenience and reduced frictional costs. With its technological advantage, the Group has played an active role in shaping the transformation of this market.

Rate movements during 2010 and January 2011

Premium rate increases for the year were 1.0% (2009: 4.8%) with either flat or increasing rates in each of the Group's three SBUs. The UK experienced the highest rate increases at 3.0% aided by rate increases of over 10% in Motor. Within Global Markets rate increases mainly fell within the -1% to +1% range with overall rates flat. Reinsurance rates were marginally lower in Property lines and marginally higher in Casualty lines, whilst Marine XL experienced the highest rate increase at 7.6%.

Rate movements in January 2011 were broadly flat overall with stability in Reinsurance and Global Markets and continued modest increases for the UK SBU.

Premium rating increases on renewal business

	Year ended 31 Dec 2010 %	Year ended 31 Dec 2009 %
Global Markets	0.0	4.3
Reinsurance	0.4	7.4
UK	3.0	3.7
Group	1.0	4.8

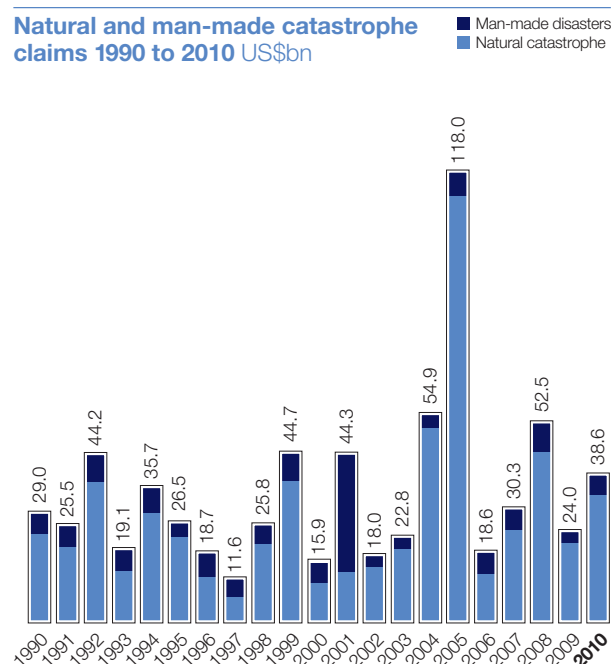
The rate movements should be read with caution. They are based on underwriters' estimates of rate changes, including adjustments to terms and conditions. They relate to renewal business only, since this represents the business for which there is the best year-on-year data.

Conclusion – one global cycle but many sub-cycles

The Group believes the outlook for the global insurance cycle based on the factors described remains competitive. There are, however, a number of variations either by region or by product. The existence of these mini-cycles within the main global insurance cycle allows the Group to manage its underwriting portfolio and to allocate capital to different classes of business that are at different points in their respective cycles. For example, commercial insurance in the UK is close to its cyclical low whereas US catastrophe reinsurance is close to its cyclical peak.

Successful portfolio and cycle management together with continued efforts to support key brokers and intermediaries will contribute to the Group's aim of delivering upper quartile underwriting performance.

Natural and man-made catastrophe claims 1990 to 2010 US\$bn



Source: Swiss Re Sigma, Munich Re NatCatService, Insurance Council of Australia.

Strategic Business Units (SBUs)

Global Markets

Vision

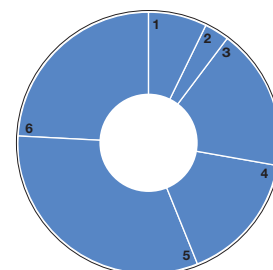
Global Markets seeks to be a highly respected market leader delivering underwriting excellence based on market intelligence and innovation in its chosen fields and disciplines.

Key points

- ▶ 116 employees (2009: 104)
- ▶ 64 underwriters with an average of 17 years' experience
- ▶ London and Chicago based
- ▶ 17.8% of business underwritten by BIL, 82.2% by Syndicate 2987
- ▶ 51% of Group ongoing GWP
- ▶ Tail: short 57.6%; medium 14.8%; long 27.6%

Class of business

	%
1. Accident & Health	7.3
2. Aerospace	3.1
3. Specialty Lines	17.6
4. Professional Lines	15.9
5. Marine	32.2
6. Property	23.9



Providing innovative solutions

Through a new proactive approach to claims management with our service providers, we were able to put over 1,000 North American truckers (comprising a mix of small fleets and single owner operators) back on the road over 50% quicker than in previous years.



Strategic Business Units (SBUs)

Global Markets continued



Matthew Wilson
CEO, Global Markets

About the Global Markets SBU

Global Markets has an extensive history of providing a comprehensive range of insurance products for small-to medium-sized enterprises as well as large corporate customers globally. The SBU is made up of a number of niches which are expert in their respective fields and bring a broad spread to the portfolio. Business is distributed entirely through intermediaries. The SBU accesses business through leading brokers in its main operations in London as well as through delegated authorities with selected coverholders, including the Group's wholly-owned US service company, who distribute products into local markets.

Global Markets' underwriting expertise and local relationships make it a market leader and it is the lead underwriter on 56% of the premium it underwrites. This offers excellent market visibility and enhances its ability to manage the underwriting portfolio through the insurance cycle. This underwriting capability is backed up by first class claims handling through specialist staff in London and in overseas claims hubs.

Financial Performance

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m	Year ended 31 December 2006 £m
Gross written premium:					
Accident & Health	56.4	87.4	144.1	143.7	140.2
Aerospace	23.7	22.9	20.3	16.5	23.9
Specialty Lines	137.1	151.9	175.9	188.1	196.8
Professional Lines	124.0	161.6	132.4	88.4	71.0
Marine	250.8	253.8	186.5	165.9	143.4
Property	186.3	197.7	122.1	146.6	131.6
Total	778.3	875.3	781.3	749.2	706.9
Business led (%)	56.0	59.1	57.7	58.8	n/a
Retention ratio (%)	74.0	71.3	76.6	80.1	n/a
Net earned premium	673.0	819.9	665.9	630.4	557.5
Underwriting profit	14.8	22.6	20.7	67.8	81.2
Profit before tax	34.6	42.8	57.6	123.7	127.5
Claims ratio (%)	57.4	62.7	61.2	54.4	46.5
Expense Ratio (%)	40.3	34.2	35.2	34.9	38.9
Combined Ratio (%)	97.7	96.9	96.4	89.3	85.4

Premium rating index (Year 2000 as base year)

	Full year 2010	Full year 2009	Full year 2008	Full year 2007	Full year 2006	Full year 2005	Full year 2004	Full year 2003	Full year 2002	Full year 2001	Full year 2000
Accident & Health	173	172	170	169	164	152	149	142	131	100	n/a
Aerospace	171	188	203	215	254	268	260	237	202	158	100
Specialty Lines	268	266	246	240	246	249	252	246	220	140	100
Professional Lines	288	287	280	294	305	312	302	260	194	120	100
Marine	191	189	177	181	182	171	160	156	144	112	100
Property	158	161	156	168	171	151	152	155	150	112	100

The rate movements should be read with caution. They are based on underwriters' estimates of rate changes, including adjustments to terms and conditions. They relate to renewal business only, since this represents the business for which there is the best year-on-year data.

Strategic Business Units (SBUs)

Global Markets continued

Portfolio

In 2010, Global Markets wrote £778.3m of gross premium across five underwriting divisions (2009: £875.3m). The portfolio is managed in two parts with a short-tail portfolio representing 66% and a long-tail portfolio representing 34%.

The short-tail portfolio consists of the Property & Space, Marine and Accident & Health divisions and underwrote £517.2m of gross premium in 2010, a reduction of 8.9% at constant currency. This reduction arose across all divisions although more than half of the reduction was the delayed effect of the withdrawal from US Medical Expenses in 2008. Property (36% of short-tail) and Marine (48% of short-tail) both saw premiums fall modestly during the year as the SBU managed competitive market conditions.

The Property portfolio consists of a broad-based book of business with particular strengths in the US through Property Financial (Lender Placed Property) and other US binding authority arrangements. Property coverage is offered on an 'all risks' or named peril basis with associated extensions of coverage such as business interruption. Clients range from individual homeowners and small enterprises to Fortune 1000 companies. During the year the Direct and Facultative (D&F) property account, offering coverage for large individual risks, was extended to offer additional balance to the division.

Brit Insurance is recognised as one of the leading insurers in the Space arena and runs the leading London Market Aerospace consortium on behalf of a number of third party insurers. The Space team works closely with one of the world's largest satellite operators, Telesat, who provide valuable technical expertise. With a line size of US\$40m it is a lead market globally for launch and in-orbit risks.

The Marine portfolio offers a broad array of coverages including Hull, Cargo and Energy (upstream and downstream) and Liability. Coverage is provided for both traditional (including nuclear) and renewable energy sources. During the year the SBU experienced growth in the Cargo and the Liability elements of the account, offset by reductions in Hull and Energy – upstream. Overall Hull, Energy and Cargo each account for approximately 25% of the division's premium.

Accident & Health is the smallest division in the short-tail portfolio and writes a selection of diverse classes including Bloodstock, Contingency and Personal Accident. Premium written fell by 35.9% at constant currency reflecting the delayed impact of the withdrawal from US Medical Expenses in 2008 and a significant contraction in the Bloodstock book.

The long-tail portfolio is split into two underwriting divisions – Specialty Lines (53%) and Professional Lines (47%). Since 2007 the SBU has made significant changes to the long-tail portfolio to insulate it from potential claims arising from economic uncertainty and to reflect the effect of lower investment returns on risk adjusted returns on capital.

The Specialty Lines division offers Legal Expenses coverage for adverse legal costs, Directors and Officers (D&O) coverage for individuals and corporations, as well as Financial Institutions insurance which can include crime and professional indemnity as well as D&O. Volumes across the Financial Institutions and D&O accounts reduced during the year as the SBU retained its underwriting discipline in the face of tough trading conditions. Financial Institutions and D&O now account for less than 40% of the division.

Within Professional Lines the SBU underwrites Professional Indemnity on a global basis. Professional Indemnity insurance protects a professional against liability arising from negligent advice. Particular areas of strength include law firms, architects and engineers and technology firms. Professional Lines is written in the open market and through a selected network of coverholders. During 2010 there was a material reduction in the areas of the International PI account which are no longer regarded as core.

The majority of Global Markets's business (82.2%) is written through the Group's Lloyd's Syndicate 2987 with the remainder through Brit Insurance Limited.

Strategic Business Units (SBUs)

Global Markets continued

Brit Insurance Services USA Inc

Brit Insurance Services USA Inc (BISI) was established in Chicago, in May 2009 and represents the SBU's first Group-owned overseas underwriting presence. BISI is a service company which underwrites risks on behalf of Global Markets using Syndicate 2987 as the insurance carrier. Initially, a £20m book of Public Entity and Religious package business previously underwritten in London was transferred to BISI. BISI is part of the Group's wider strategy to get closer to its underlying clients whilst continuing to recognise the importance of, and support for, London's position as a wholesale insurance market.

During 2010 the number of employees in BISI has grown from eight to 15 reflecting the build out of its infrastructure as well as additional underwriting capacity. Premium written by BISI grew by 39.5% in 2010 to US\$43.4m as it expanded both the transferred book and its new Facultative Property offering.

Average to Outperform

As part of the Group's 'Average to Outperform' agenda the SBU has made a number of important strides. In particular the SBU has developed and launched a new underwriting performance management portal which allows for a substantial amount of pre-underwriting ahead of renewals and significantly improves transparency around underwriting decisions.

Furthermore, as a result of the decisive portfolio actions and improved focus over the last two years, a number of previously underperforming classes are now showing profitable results – this includes Accident & Health following the withdrawal from US Medical Expenses.

In order to create further focus within the underwriting divisions, the Property division has been split into separate Open Market and Facilities divisions, each headed up by an internally appointed divisional director. A similar change to the Marine division is planned for 2011 and a separate Energy division will be formed. This new structure should enable more transparency within the underlying operating units within Global Markets and promote additional focus.

2010 financial performance

Operating profit fell 19% to £34.6m as a result of lower premium volume and a higher burden from major claims.

Gross written premium fell by 11.8% at constant currency as the SBU continued its active management of the underwriting portfolio. Gross written premium fell by 36% in Accident & Health reflecting the withdrawal from US Medical Expenses. Specialty Lines premiums reduced by 10% as the Group continued its defensive stance in longer-tail casualty business. Premium reductions in the core short-tail lines of Marine (–2%) and Property (–7%) were lower, reflecting the continuation of better underwriting margins than longer tail lines.

Premium rates on renewed business were on average flat across the portfolio with most classes experiencing movements in the +1% to –1% range.

Global Markets's combined ratio of 97.7% deteriorated by 0.8 percentage points compared with 2009 as a result of higher major claims which offset a significant improvement in the attritional claims ratio. In particular underlying performance from the short-tail portfolio was positive. The SBU continued to reserve conservatively for the long-tail portfolio. Reserve releases of £9.6m were equivalent to 1.4 percentage points compared with £13.8m equivalent to 1.7 percentage points in 2009.

Claims experience during the year was mixed. The accident year attritional claims ratio improved by 8.4 percentage points reflecting the positive results from the portfolio actions taken by the SBU over the last two years. This was, however, partially offset by an increase in major claims arising from the earthquakes in Chile and New Zealand during 2010. Global Markets's share of the Group's major claims was £19.2m. Overall the claims ratio improved by 5.3 percentage points to 57.4%.

The SBU's focus on expense control resulted in a 13% reduction in management expenses, a reduction slightly higher than the move in gross written premium. The reported expense ratio rose to 40.3% as a result of an 18% fall in net earned premium, changes in business mix and higher regulatory levies.

Outlook

The key markets that Global Markets operates in are expected to remain competitive through 2011. In many respects this is similar to the 'finely poised' message in last year's outlook. Consequently the SBU expects modest rate pressure to prevail in 2011 and in particular will continue its defensive position on longer tail casualty lines.

During 2011, the prospect for further growth within BISI will be assessed conservatively; where there are opportunities in London, the SBU will continue to manage its underwriting portfolio on a proactive basis.

Strategic Business Units (SBUs)

Reinsurance

Vision

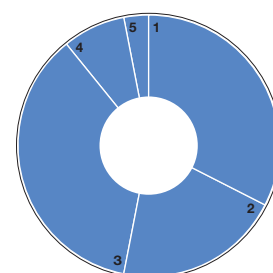
Reinsurance aims to build a diverse and high quality multi-class and multi-territory book of business by participating in this potentially high margin but volatile global business.

Key points

- ▶ 39 employees (2009: 36)
- ▶ 16 underwriters with an average of 21 years' experience
- ▶ London based
- ▶ 35.3% of business underwritten by BIL, 64.7% by Syndicate 2987
- ▶ 20.2% of Group ongoing GWP
- ▶ Tail: short 54.1%; medium 16.0%; long 29.9%

Class of business

	%
1. Property Treaty North America	32.6
2. Property Treaty International	20.6
3. Casualty Treaty	36.1
4. Marine XL	7.8
5. Reinsurance Other	2.9



Providing preparation for the unexpected

Following the destruction of Wadena Deer Creek High School in Minnesota from a multi-vortex tornado in June 2010, our reinsurance programme helped the cedant insurer to resolve the claim quickly. The school has now unveiled the design for its new, environmentally friendly, geothermally heated building.



Strategic Business Units (SBUs)

Reinsurance continued

About the Reinsurance SBU

Reinsurance writes multi-class and multi-territory reinsurance with a focus on providing excess of loss reinsurance to a broad range of clients globally. The SBU transacts reinsurance business exclusively through broker intermediaries with clients ranging from small local mutual insurers to large well known global insurance groups. It offers the capacity to quote and lead business, whilst aiming to deliver a first class all-round service to customers backed up by its specialist contractual documentation and claims handling teams.

The SBU accesses global business through its main underwriting operation in London with representative offices in Japan and Australia and a relationship office in Denmark. This structure is designed to maintain the SBU's profile overseas whilst balancing that with the needs of an efficient operating model in a cyclical market.



Jonathan Turner CEO, Reinsurance

Portfolio

In 2010 the SBU wrote £309.6m of gross premium across its core specialist reinsurance classes of Property, Casualty and Marine.

The largest portfolio is Property Treaty which accounted for 53.1% of the account in 2010 (2009: 49.5%). This is split into two classes – North America (61%) and International (39%). Each offers reinsurance cover against catastrophe events or large individual claims arising from either man-made or natural events. The North America class is a combination of regional and nationwide business, but with a strong bias towards regionally-based clients who write specialised books of business.

The unit's second largest portfolio is Casualty Treaty which accounted for 36.1% of the SBU's premiums in 2010 (2009: 39.0%). The Casualty Treaty account combines a number of sub-classes including Personal Accident catastrophe, clash and individual per risk protection for General Liability, Professional Indemnity and Directors & Officers, as well as whole account coverage. The Casualty Treaty portfolio is almost entirely written on an excess of loss basis with approximately 40% of the book exposed

Financial performance

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m	Year ended 31 December 2006 £m
Gross written premium:					
Property Treaty North America	101.0	116.2	81.5	71.7	–
Property Treaty International	63.5	64.0	55.3	47.8	–
Property Treaty	–	–	–	–	139.5
Casualty Treaty	111.7	142.0	82.6	85.1	95.5
Marine XL	24.3	20.8	17.8	9.1	9.4
Reinsurance Other	9.1	21.2	23.5	25.7	16.5
Total	309.6	364.2	260.7	239.4	260.9
Business led (%)	35.9	36.0	33.9	29.6	n/a
Retention ratio (%)	85.6	87.0	82.8	87.4	n/a
Net earned premium	249.7	297.6	209.9	208.3	237.0
Underwriting profit	28.3	57.6	13.9	35.4	50.3
Profit before tax	37.2	66.1	30.8	61.0	76.5
Claims ratio (%)	59.6	54.9	65.3	56.4	50.0
Expense ratio (%)	28.6	25.0	26.4	26.6	28.8
Combined ratio (%)	88.2	79.9	91.7	83.0	78.8

Premium rating index (Year 2000 as base year)

	Full year 2010	Full year 2009	Full year 2008	Full year 2007	Full year 2006	Full year 2005	Full year 2004	Full year 2003	Full year 2002	Full year 2001	Full year 2000
Property Treaty – NA	234	238	215	234	221	159	155	154	149	110	100
Property Treaty – Int'l	114	113	108	109	107	98	98	100	n/a	n/a	n/a
Casualty Treaty	243	241	226	230	234	228	230	215	182	115	100
Marine XL	356	331	279	288	286	193	183	179	171	115	100

The rate movements should be read with caution. They are based on underwriters' estimates of rate changes, including adjustments to terms and conditions. They relate to renewal business only, since this represents the business for which there is the best year-on-year data.

Strategic Business Units (SBUs)

Reinsurance continued

to catastrophe-type events. Consequently, the portfolio is less exposed to potential attrition-type claims experienced in economic downturns.

Other smaller areas of the reinsurance book include Marine and Agriculture. Both accounts generate high margins albeit with higher than average volatility. 54.1% of the SBU's business is classified as short-tail, with 16.0% medium-tail and 29.9% long-tail.

The Reinsurance SBU utilises each of the Group's insurance carriers with 64.7% written through Syndicate 2987 and 35.3% in Brit Insurance Limited (BIL). The majority of the SBU's North American business is written using Syndicate 2987, making use of the extensive licenses available whereas the majority of the International and European business is written through BIL. The use of two carriers aims to maximise returns on capital and to cater for client wishes where appropriate.

Average to Outperform

In line with the Group's 'Average to Outperform' programme, the SBU has developed enhanced portfolio segmentation tools during the year. These tools have created improved transparency that allows each underwriter to segment his account on a contract by contract basis and has led to a full underwriting review on the worst performing 20% of the Reinsurance portfolio.

Furthermore the SBU has enhanced its management team by recruiting a Reinsurance Underwriting Director who reports directly to the Reinsurance SBU CEO and a new Head of Outwards Reinsurance. Both positions have attracted highly experienced individuals with backgrounds in insurance, reinsurance and broking.

2010 financial performance

In 2010 the Reinsurance SBU's underlying portfolio remained relatively stable. Gross written premium on a constant currency basis fell by 15.8% to £309.6m but this was almost entirely due to the non-recurrence of positive movements on the re-estimation of prior year premium for Casualty Treaty, Property Treaty North America and the Aviation XL run-off portfolio in 2009. Underlying premium growth on a constant currency basis and excluding re-estimates of prior year premium was -1.1% with modest underlying growth in Marine XL being offset by reductions in Property Treaty.

Average premium rates on renewals were up 0.4%. Movements were generally small across all classes with marginal increases in Casualty Treaty and International Property Treaty offsetting reductions in Property Treaty North America.

Reinsurance spend was £61.2m equivalent to 19.8% of gross written premium. Net written premium fell by 19.0% with net earned premium falling by 16.1%.

The SBU's combined ratio of 88.2% was 8.3 percentage points higher than 2009 directly as a result of higher Property Treaty International claims during the year. Major claims of £36.0m contributed 14.4 percentage points to the SBU's combined ratio and arose from earthquakes in Chile and New Zealand. The major claim burden in 2009 of £12.0m arose from the Air France plane crash and contributed 4.0 percentage points to the combined ratio.

Despite the well-publicised Deepwater Horizon event the Marine XL account produced a highly credible financial result for the year with a combined ratio of 86.0%. The circumstances of the loss led to rates hardening notably in the London market segment of the portfolio. The Agriculture XL account has produced another profitable year.

The combined ratio also benefited from reserve releases of £25.0m equivalent to 10.0 percentage points of net earned premium compared with a release of £24.1m (8.1 percentage points of net earned premium) in 2009. Reserve releases arose across all classes but with the highest contribution from Casualty Treaty.

It is a sign of the diverse nature of the Group's Reinsurance portfolio that in a year of heavy claim activity in International Property, the SBU still managed a combined ratio below 90%. This demonstrates the real diversification value of writing Casualty Treaty alongside the two Property Treaty classes.

The expense ratio increased by 3.6 percentage points to 28.6% (2009: 25.0%). Commission costs were stable at 17.5% whereas the non-commission expense ratio rose to 11.1% (2009: 7.6%).

Overall operating profit was £37.2m, a reduction of 43.7% compared with 2009 but still a credible result given the major claim activity during the period.

Outlook

The outlook for 2011 is mixed. A benign US hurricane season (from an insurance perspective) will likely put downward pressure on US pricing; however, if the reinsurance industry continues to behave in a disciplined manner this should be manageable. In 2010 the International Property market has seen claims of more than US\$15bn from earthquakes in Chile and New Zealand as well as floods and hailstorms in Australia; it is expected that this will stabilise pricing generally and increase rates on claim-affected business. Furthermore, a new version of one of the leading catastrophe modelling software programmes launching in late February 2011 is expected to support pricing in the US Property Catastrophe arena.

The Casualty Treaty portfolio remains one of the differentiating factors for the SBU. Within this, pricing for short-tail business remains competitive but there is generally less available capacity than in the Property arena.

The SBU will continue to focus on optimising its portfolio and position the account for the opportunities that will inevitably arise.

Strategic Business Units (SBUs)

UK**Vision**

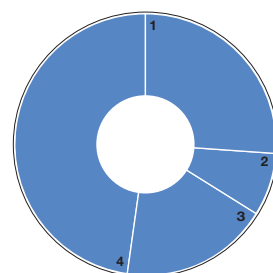
The UK SBU has established itself as a key provider to the regional UK market and aims to be a significant player in its chosen market segments. Ease of access, expertise, service and execution skills will differentiate the SBU from its peers.

Key points

- ▶ 156 employees (2009: 157)
- ▶ 105 underwriters with an average of 15 years' experience
- ▶ Nine UK offices including London
- ▶ 87.4% of business underwritten by BIL, 12.6% by Syndicate 2987
- ▶ 28.8% of Group ongoing GWP
- ▶ Tail: short 47.3%; medium 18.5%; long 34.2%

Class of business

	%
1. Employers'/Public Liability	26.3
2. Professional Indemnity/ D&O	7.6
3. Motor	18.5
4. Property & Commercial Packages	47.6



Providing a proactive approach

Following the devastating floods in the Cumbrian town of Cockermouth, we ensured that 50 residents of a large Housing Association were able to find suitable alternative accommodation. Our proactive approach to claims management ensured that repairs were quickly and efficiently carried out and all residential properties were re-occupied within the agreed timescales.



Strategic Business Units (SBUs)

UK continued

About the UK SBU

The UK SBU underwrites a diverse book of UK commercial insurance through a combination of regional, national and international brokers. The SBU's target market focuses on sole traders through to corporates with turnover of up to £300m. Over the last three years the Group has been successful in developing online trading solutions for micro-SME business, underwriting commercial insurance with premium values typically less than £2,000 per policy. The UK SBU has a carefully targeted distribution strategy with 80% of its commercial business sourced through its top 75 brokers.

Portfolio

In 2010, the UK SBU underwrote £441.2m of gross premium in four main classes of business.



Ray Cox CEO, UK

The UK SBU's largest class of business is Property and Commercial Packages which accounts for 47.6% of the portfolio. The SBU underwrites a wide range of property from shops and offices through to large manufacturing and warehouse risks as well as mid to high net worth home insurance. The portfolio is underwritten directly through brokers, or through specialist coverholders. During 2010 the SBU withdrew from the Local Authority (Municipal) market as pricing levels did not reflect the anticipated outlook for claims.

Liability, which accounts for 26.3% of the portfolio, is split into Employers' Liability insurance, which is a compulsory purchase in the UK, and Public/Products Liability. Within this account the SBU underwrites a specialist book focusing on a number of industries including construction. In addition, the SBU has a strong presence in electronically traded covers and more broadly based risks sourced through its regional network. It also participates on a small number of International programmes.

The Motor insurance portfolio consists of commercial – fleets and haulage, as well as specialist personal motor. Motor insurance accounted for 18.5% of the portfolio in 2010, down from 25.3% in 2009. During 2010 the SBU substantially reduced its exposure to Private Motor as part of its ongoing management of the UK underwriting portfolio.

Financial performance

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m	Year ended 31 December 2008 £m	Year ended 31 December 2007 £m	Year ended 31 December 2006 £m
Gross written premium:					
Employers'/Public Liability	116.0	116.7	103.5	89.8	91.4
Professional Indemnity/D&O	33.5	38.3	34.0	36.3	36.7
Motor	81.6	115.2	87.3	63.8	91.3
Property & Commercial Packages	210.1	185.2	125.8	84.1	60.5
Total	441.2	455.4	350.6	274.0	279.9
Business led (%)	92.5	94.1	91.2	87.1	
Retention ratio (%)	66.4	68.6	78.0	72.3	
Net earned premium	376.2	362.4	259.9	262.8	251.2
Underwriting profit/(loss)	0.3	0.9	1.5	(24.3)	7.7
Profit before tax	14.3	14.2	35.7	15.8	40.4
Claims ratio (%)	64.7	66.7	66.4	76.3	69.6
Expense ratio (%)	35.1	33.0	32.9	33.0	27.3
Combined ratio (%)	99.8	99.7	99.3	109.3	96.9

Premium rating index (Year 2000 as base year)

	Full year 2010	Full year 2009	Full year 2008	Full year 2007	Full year 2006	Full year 2005	Full year 2004	Full year 2003	Full year 2002	Full year 2001	Full year 2000
Employers'/Public Liability	206	205	206	217	237	257	284	286	200	100	n/a
Professional Indemnity/D&O	110	107	105	111	118	130	132	130	100	n/a	n/a
Motor	132	118	108	101	104	111	122	120	115	108	100
Property & Commercial Packages	124	124	121	122	125	130	131	132	123	104	100

The rate movements should be read with caution. They are based on underwriters' estimates of rate changes, including adjustments to terms and conditions. They relate to renewal business only, since this represents the business for which there is the best year-on-year data.

Strategic Business Units (SBUs)

UK continued

The smallest element of the portfolio relates to Professional Lines, which includes Professional Indemnity (PI) and Directors and Officers (D&O) insurance. This accounts for 7.6% of the portfolio, with the vast majority being PI sourced through both London and regional offices. The SBU has also developed a PI product especially tailored for the micro-SME market.

The UK SBU is committed to operating a regional office structure and opened its first office outside London in 2003. It now has nine offices serving the key insurance markets across the UK. The offices outside London experienced further premium growth in 2010 and on an underwriting year basis now represent 30% of the SBU's portfolio, up from 20% three years ago. These offices transact business that is placed locally and does not normally reach the London market. Without an established regional office network, the UK SBU would not be able to access this business.

Consistency in underwriting in the UK SBU is achieved through the use of a matrix approach. Each portfolio class, e.g. Property, Liability, Fleet and Financial Lines, has a Portfolio Manager who is responsible for managing the technical integrity of the portfolio. This includes setting the underwriting and pricing guidelines across each of the distribution platforms.

In 2010 the UK SBU wrote 28.8% of the Group's gross premium which was split 47.3% short-tail, 18.5% medium-tail and 34.2% long-tail. Brit Insurance Limited (BIL) is the carrier for the majority of the SBU's business (87.4%) with Syndicate 2987 (12.6%) primarily used for the international elements of the portfolio.

Micro insurance

During 2010, the SBU continued to develop its distribution edge in the small commercial and micro-SME insurance market.

Brit Lite, which focuses on providing commercial insurance to businesses typically with fewer than ten employees and insurance spend of less than £2,000, has grown to represent 12% of the SBU's portfolio from a standing start in 2007. The success of the proposition has been built on providing a flexible offering to brokers backed up with experienced referrals support, a comprehensive product range, and rapid speed of execution. Customers can access the SBU's suite of products via carefully selected partners either through the traditional broking channel or through e-trading. The SBU's largest e-trading relationship is with Simply Business, an online insurance broker. The Group has a 38.4% shareholding in Simply Business, which is owned by Xbridge Limited.

Average to Outperform

As part of the Group's 'Average to Outperform' agenda, the SBU has been active in managing its UK underwriting portfolio. In particular, in early 2010 the SBU exited Local Authority (Municipal) business as pricing levels did not compensate for the expectation of a more difficult claims environment arising from a squeeze on public sector budgets. Furthermore, the SBU decided to reduce substantially its Private Motor portfolio to concentrate on the commercial elements of its motor portfolio. Private

Motor peaked at 11% of the SBU's premiums but recent structural developments have reduced its attractiveness. It is no longer viewed as a sustainable class of business for the Group.

2010 financial performance

Gross written premium fell by 3.1% to £441.2m. The headline decline in premium was a direct result of the withdrawal from Local Authority (Municipal) business and the substantial reduction in the Private Motor account. The Property account posted healthy growth of 21.2% as a number of contract wins from previous years started to deliver. The Liability account fell by 1.2%, reflecting the tough stance taken by the SBU's underwriters in declining business under the most pricing pressure.

Increases in premium rates on renewed business for 2010 averaged 3.0%. Within this, all lines posted positive rate movements although the Property and Liability accounts have not yet experienced a significant turn in pricing.

Reinsurance spend was similar to 2009 and net earned premium increased by 3.8% as premium written in previous periods was earned.

The combined ratio of 99.8% was in line with 2009 (2009: 99.7%). The claims ratio improved by 2.0 percentage points as recent portfolio actions – together with modestly higher premium rates – began to have an effect. The claims ratio also benefited from a continuation of positive reserve development from prior years with £39.0m of releases during 2010 (2009: £41.2m), equivalent to 10.4 percentage points of net earned premium (2009: 11.4 percentage points). Reserve releases arose predominately from the Liability class of business.

The result includes £8.0m in relation to net claims arising from the UK freeze in December 2010 which added 2.1 percentage points to the claims ratio.

The unit's expense base remained under control with the expense ratio marginally higher at 35.1%. The increase was almost entirely due to a higher commission ratio as business non-renewed as part of the portfolio actions during the year tended to have lower acquisition costs than the ongoing portfolio.

Operating profit for the UK SBU rose by 0.7% to £14.3m.

Outlook

The UK market continues to experience premium rate rises but these remain below the level needed to restore accident year profitability to the wider market. If this situation continues there is a significant risk that, when premium rates do finally turn, the scale of the required rate increases will be detrimental to the reputation of the UK insurance sector.

During this tough phase of the market the UK SBU is determined to continue to deliver first class service and support to its clients, brokers and coverholders. In particular the SBU's regional network of offices enables it to demonstrate commitment to national and regional brokers alike.

Claims

Vision

Brit Insurance claims' vision is to establish the Group as a market leader in its chosen sectors by working closely with insureds and cedants to achieve timely and accurate settlements on all valid claims. At the same time the claims department aims to provide sound claim-based management information and insight to the Group's business partners including underwriters and producers.

2010 progress

At the Group level progress has been made with respect to a number of initiatives including:

- ▶ Audit and control of third party administrators
- ▶ Development of enhanced claim based management information
- ▶ Embedding the 'Average to Outperform' culture throughout the claims department

Within the SBUs, Global Markets has led the market response for a number of high profile claims whilst Reinsurance has been able to complete a number of commutations on favourable economic terms. In the UK SBU, significant progress was made in reducing the inventory of open claims.

2011 outlook

2011 began with two new roles at Group level and a new management structure in Global Markets claims. Each of these changes is intended to position the claims department to make significant progress in 2011.

The Director – Group Claims Operations is driving a number of important initiatives geared at improving performance in some key areas:

- ▶ Through a better understanding of the spend on third party administrators, monitoring counsel, defence and coverage counsel and other experts, the Group will be more effective in purchasing and managing efficiencies from that spend;
- ▶ Through an improved audit mechanism the Group will be able to more effectively drive the technical output and efficiency of its service providers; and
- ▶ Through the development and provision of enhanced management information reports the Group will be in a position to make timely, well informed decisions that drive performance.

Under the direction of the Group Chief Claims Technical Officer the Group is introducing initiatives targeted at ensuring delivery of the most accurate technical result possible:

- ▶ Through the development of a major/complex claim roundtable whereby important matters will see thorough collaboration amongst loss adjusters and the most senior members of the team;
- ▶ Through direct oversight of major/complex issues by the Group Chief Claims Technical Officer or a member of his team;
- ▶ Through involvement of the Group Chief Claims Technical Officer in a review and selection of defence and coverage counsel panels to ensure the Group is receiving the best advice and terms available.

In Global Markets claims a new management structure will see a closer alignment with underwriting counterparts and additional resources dedicated to managing the diverse portfolio.

Finally, with the enhanced management structure the claims department will be an active participant and leader in dealing with market issues. This includes all initiatives geared at improving efficiency, management information and accuracy of outcomes to the benefit of all stakeholders including shareholders, insureds, cedants, and production partners.

Operations

For Group Operations 2010 was a year of consolidation, with the focus on supporting the 'Average to Outperform' agenda. Prioritising where this support would be most effective was key and at the beginning of 2010 the Group agreed on five areas where Operations would play an important role:

- ▶ Underwriting – Continuing the development of technical and analytical tools to support the underwriting process
- ▶ Claims – Supporting the operational management of the Group's claims handling activities particularly in the UK SBU;
- ▶ Management Information – Continuing to invest in the data warehouse and other tools to improve the granularity of data provided to inform pricing decisions;
- ▶ Delegated Underwriting – Building operational capabilities to create greater efficiency within an already effective set of control processes;
- ▶ Solvency II – Supporting the Group's agenda in this critical area.

Key achievements include:

- ▶ Further development and integration into the underwriting process of technical pricing tools for all classes of business;
- ▶ Supporting the Claims teams to define processes to reduce significantly the time taken to settle certain types of claims – with attendant benefits in improved client service and total costs of claims;
- ▶ Completion of the UK Motor data marts and the addition of similar tools for Liability classes of business. A process for delivering the same capability for UK Property lines of business is ongoing;
- ▶ Established a dedicated operational unit in support of the Delegated Underwriting business;
- ▶ Implementation of a new coverholder approval process; a new work flow process has been established which substantially reduces, in some cases to a third, the amount of time taken to approve new coverholder arrangements;
- ▶ Established a corporate data dictionary and related processes in support of data management and control policies.

A variety of improvements have also been made in the day-to-day operations:

- ▶ Risk capture accuracy increased to 90% of data right first time and 96% of risks captured within two days compared to a target of five days;
- ▶ Improved bordereau processing for all the Group's lead relationships;
- ▶ Consolidation of London staff into one headquarters at 55 Bishopsgate;
- ▶ Broadened the credit control capabilities to include a stronger focus on bureau-related business;
- ▶ Delivered £2.5m of savings through commercial procurement activities;
- ▶ Supported the BISI operation with installation of a new Policy Administration platform in Chicago.

Risk Management and Risk Factors

2010 highlights

- ▶ A new position of Group Chief Risk Officer (CRO) was created which sits on the Executive Management Committee (EMC) for the UK-managed operations and reports to the Group CEO. The CRO is responsible for all risk management activities including catastrophe and capital modelling. The risk management function was restructured following the appointment to reflect the additional responsibilities of the department.
- ▶ An Enterprise Risk Management (ERM) framework was designed and approved. This framework recognises that increasing shareholder value comes from seeking risk, while fully managing that risk within agreed risk appetite.
- ▶ An improved process for setting specific risk tolerance and appetite measures for each risk category was designed and implemented.
- ▶ Existing tools and processes the Group uses to manage risk were further developed together with the necessary preparations for Solvency II.

2011 focus

- ▶ Embedding the ERM framework into the Group and collating the current risk management processes into a holistic Group-wide approach. This will lead to better informed decision making and help to optimise the risk and reward relationship and management of the Group's risk exposures.
- ▶ Continue to support the preparations for Solvency II, in particular, to support the development of the Internal Model, the processes supporting the ERM framework and to develop the Own Risk and Solvency Assessment (ORSA) process.

Risk governance

The Brit Insurance Holdings N.V. Board (N.V. Board) is responsible for ensuring the principal risks and uncertainties facing the Group are identified and managed.

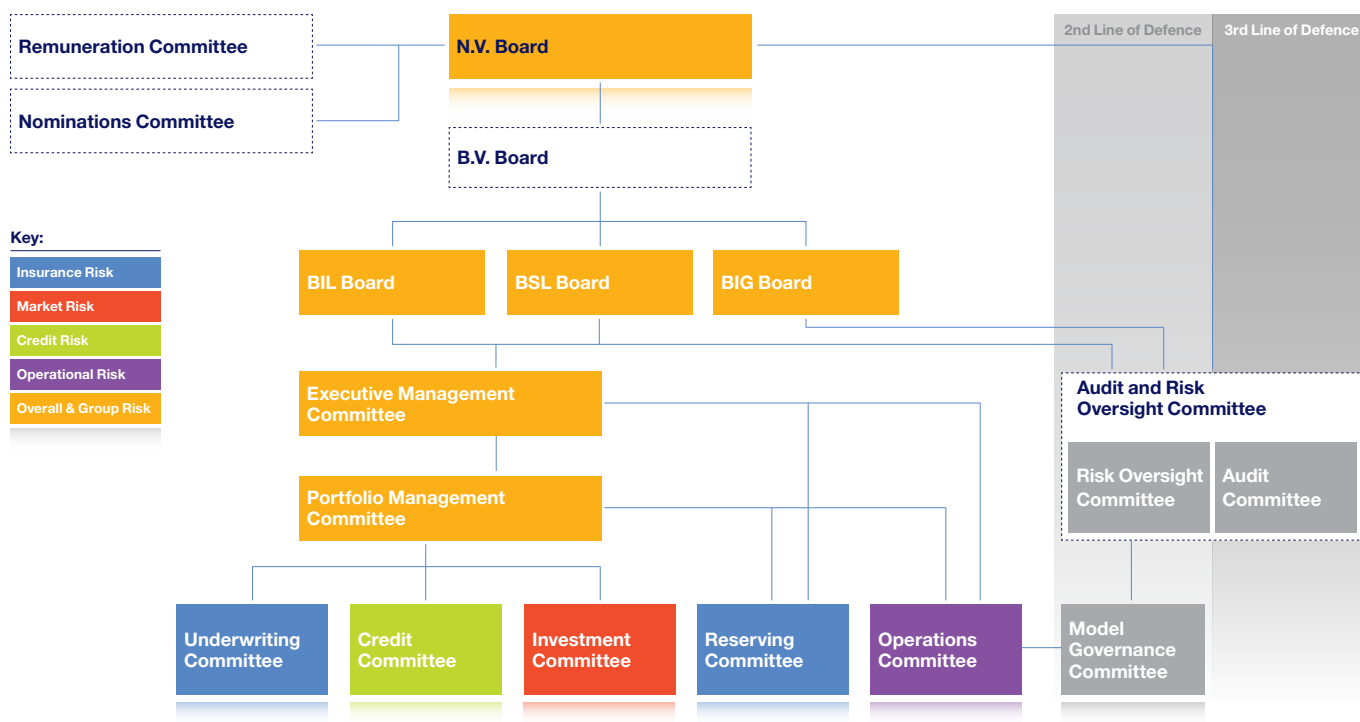
The Executive Management Committee (EMC) has the responsibility for the day-to-day management of the risks within the UK-managed operations. The EMC delegates the management of specific risks to the Chairs of the relevant committees. The EMC reports on the risks within the UK-managed operations to the Boards of the key UK-regulated entities and to the N.V. Board.

The Brit Insurance Gibraltar (PCC) Limited Board (BIG Board) takes responsibility for the management of the risks within the Gibraltar-managed operations. The BIG Board reports on the risks within the Gibraltar-managed operations to the N.V. Board on a regular basis.

The Audit and Risk Oversight Committee (AAROC) ensures the appropriate Risk Management Framework is in place and monitors its usage (including the use of the Internal Model). The AAROC also reviews, challenges and ratifies risk assumptions, parameters and methodology used in the Internal Model. The Model Governance Committee facilitates and oversees the running of the Internal Model in line with guidance issued by the Boards.

The AAROC Committee also provides independent and objective assurance that the risk management process is functioning as designed and identifies improvement opportunities.

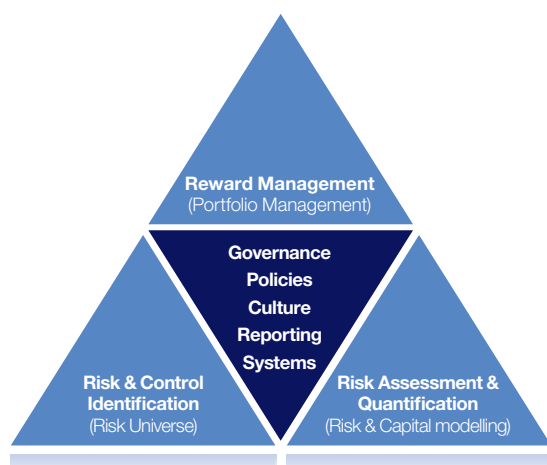
Simplified Group Governance Structure



Risk Management and Risk Factors continued

Enterprise Risk Management framework

The Enterprise Risk Management (ERM) framework encompasses Brit Insurance's approach to the management of risk and the optimisation of the Group's portfolio given specific risk tolerances and appetites. It builds on many existing processes and creates a holistic approach to risk and reward management.



The ERM framework is based on four main components: risk and control identification, risk assessment and quantification, reward management and the supporting elements which allow these three components to work (governance, policies, culture, reporting and systems).

Risk appetite and tolerance

The ERM framework incorporates the setting of risk appetite and tolerances that describe how much risk the Group and each underwriting entity is willing to take in each major risk area. This framework was adopted in 2010 and the monitoring of actual position against appetite is monitored quarterly through the relevant risk committee.

Any breaches of risk appetite for the UK-managed operations are reported to the EMC and for the Gibraltar-managed operations to the BIG Board. If the breach concerns any of the pre-defined key risk measures, the breach is escalated further to the relevant Board. The Risk Oversight Committee oversees the process and ensures that appropriate action is taken to restore the position back within appetite.

Key risks

The Group identifies and manages risk under categories closely aligned with the risk frameworks set out by the Financial Services Authority (FSA) and Solvency II regulations.

Key risks and risk categories

Risk category	Key risks
Insurance	Reserving
	Underwriting
	Catastrophe exposure
	Claims process
	Other processes and systems
Market	Foreign exchange
	Interest rate
	Spread
	Equity and property
	Other processes and systems
Credit	Fixed interest investments
	Reinsurance credit
	Premium debtors
	Other processes and systems
Operational	Systems and IT
	People
	External
	Other processes
Group	Capital
	Programme/projects
	Regulatory/legislative
	Liquidity

Concentration risk is also considered between (and within) these risk categories.

Overview of risk category management

1. Insurance risk

The principal risk that the Group faces is insurance risk. This relates to the inherent uncertainty in the pricing of insurance, the aggregation of underwriting exposures, adverse claims development, reserving inadequacy and the timing of the associated cash flows. Insurance risk can be segmented into three main areas:

- ▶ Reserving: the risk of adverse reserve development impacting the Group's financial position;
- ▶ Underwriting: the risk of unexpected increases in cost of insurance claims;
- ▶ Catastrophe exposure: the risk of claims arising from inherent uncertainties in the occurrence and size of insurance losses from natural and man-made catastrophes.

Reserving

Reserves for unpaid claims represent the largest component of the Group's liabilities. Estimates of these claims reserves are inherently uncertain. Differences between the actual claims and these estimates can have a significant impact on future profitability and the Group's balance sheet.

For the UK-managed operations the Reserving Committee is responsible for reviewing and setting claims reserves. The committee is chaired by the Chief Financial Officer and includes the Group Chief Actuary, the SBU CEOs and representatives from the claims division. The reserves selected by the Reserving Committee are based on quarterly reserve recommendations from the internal actuarial team.

Risk Management and Risk Factors continued

For the Gibraltar-managed operations the claims reserves are selected by the BIG Board.

The Group's reserving policy is to reserve at actuarial best estimates and in addition to retain a margin to allow for uncertainties. Each year the Group claims reserves are also reviewed by external actuarial consultants.

Underwriting

Underwriting risk includes the risks of inappropriate underwriting and inadequate pricing, including ineffective management of underwriting delegated third parties. Underwriting risk for the UK-managed operations is owned by the Underwriting Committee. For the UK-managed operations, appetite and tolerance for underwriting risks are set by the relevant Boards and managed by the Underwriting Committee. Underwriting risk for the Gibraltar-managed operations is owned by the BIG Board. The BIG Board also sets risk appetite and tolerance for underwriting risk for the Gibraltar-managed operations.

In the UK, the Underwriting Committee oversees the underwriting processes ensuring authority limits and peer review processes are followed. The actuarial department conducts quarterly performance reviews with the underwriters, concentrating on historic profitability analysis and technical pricing issues. The Portfolio Management Committee (PMC) oversees the technical pricing process ensuring that risks are fully assessed and documented before being written.

The Underwriting Committee and the PMC oversee the business planning process. Each underwriter is given clear authority relating to line size, aggregate exposure and the classes of business that may be written. The rating environment is continuously monitored and plans are updated to reflect the pricing trends. Following review by the Underwriting Committee and PMC, these plans are presented for consideration to the relevant Boards. This review is carried out in conjunction with an assessment of the appropriateness of the reinsurance programme.

In Gibraltar, underwriting exposure is determined by the BIG Board. It is also responsible for the approval of underwriting guidelines. Underwriting by the Gibraltar-based operation is conducted by the Gibraltar-based underwriting team using these guidelines (supported and reviewed by third-party industry experts).

Catastrophe exposure

Exposure to catastrophic events is managed through the aggregate exposure management process. The Underwriting Committee oversees this process for all inwards business from third-parties, which is currently only written through the UK-managed operations. The Underwriting Committee controls the risk of accumulation for over 50 key Realistic Disaster Scenarios (RDSs). These RDSs reflect the diversity of the underwriting exposures and include specific scenarios for elemental, man-made and economic disasters. The RDSs are reviewed quarterly.

Hypothetical claims in the fourth quarter of 2010 for various RDS events

Event	Industry gross claims US\$m	Brit Insurance gross claims £m	Brit Insurance net claims £m	Comments
► Florida hurricane Tampa Bay	125,000	305	126	Category 4 storm on the SS Scale, landfalling in Tampa. Brit Insurance claims estimates include demand surge, flood associated with the hurricane, and non-property exposures.
► Florida hurricane Miami	125,000	265	95	Category 5 storm on the SS Scale, landfalling in Miami. Brit Insurance claims estimates include demand surge, flood associated with the hurricane, and non-property exposures.
► US north east coast hurricane New York State	78,000	264	125	Category 4 storm on the SS Scale, landfalling in Suffolk County, New York State. Brit Insurance claims estimates include demand surge, flood associated with the hurricane, and non-property exposures.
► California earthquake Los Angeles	78,000	292	91	Magnitude 7.3 earthquake on the MMI scale, on the Elsinore fault in Los Angeles. Brit Insurance claims estimates include demand surge, fire following the earthquake, and non-property exposures.
► California earthquake San Francisco	78,000	295	88	Magnitude 7.5 earthquake on the MMI scale, on the San Andreas fault in San Francisco. Brit Insurance claims estimates include demand surge, fire following the earthquake, and non-property exposures.
► Europe windstorm Western Europe	31,000	218	77	A winter storm with peak gusts in excess of 112mph resulting in a broad swath of damage across southern England, France, Belgium, Netherlands, Luxembourg, Germany and Denmark. Brit Insurance claims estimates include demand surge and UK coastal flood.
► Japan earthquake Tokyo	62,000	183	74	Based on a repeat of the Great Kanto event in 1923, a magnitude 7.9 earthquake in the Tokyo Metropolitan Area.

Further details on insurance risk are provided in Note 4 of the financial statements.

Risk Management and Risk Factors continued

with more frequent reviews of the peak zone natural peril catastrophe RDSs that present the greatest exposure. For the Gibraltar-based operations accumulation risk is monitored by the BIG Board.

The Group's tolerance for catastrophe exposure takes account of expected profitability and available capital. This tolerance is expressed as the maximum net incurred claims acceptable under a number of scenarios. These tolerances are expressed for a number of different perils and numbers of events. The way these tolerances are expressed actively encourages diverse underwriting portfolios and therefore reduces the risk of accumulations.

The N.V., BIL, BSL and BIG Boards review the tolerance annually and may decide to increase or decrease the Group's maximum tolerance based on market conditions and other factors. This review is done in conjunction with an assessment of the appropriateness of the catastrophe reinsurance programme.

As a guide to the level of catastrophe exposure, the table on page 38 shows hypothetical claims in the fourth quarter of 2010 for various RDS events.

2. Market risk

Market risk is the risk that the fair value of investments, other assets and liabilities or future cash flows will fluctuate because of adverse movements in market prices such as exchange rates, interest rates and equity prices. Market risk is owned by the Investment Committee for the UK-managed operations and the BIG Board for the Gibraltar-managed operations.

Market risk for investments is controlled through the use of detailed investment guidelines, supported by our risk tolerance and appetite. The guidelines have been constructed to account for the different requirements of the liability and capital investment portfolios. The liability portfolio is designed to ensure liquidity and safety for the payment of claims to policyholders. The capital portfolio attempts to earn a competitive return and can accept greater volatility. The guidelines, which also cover the investment portfolio as a whole, allow possible combinations of investments. The returns on these investments have been stress-tested using historic data and modelled to analyse the projected Value at Risk.

Interest rate risk is managed through duration limits at the security and portfolio levels within the investment guidelines. In the current environment, the maximum permitted duration of any security in the liability portfolio is seven years. Investments of greater duration are allowed within the capital portfolio, but overall interest rate risk is constrained by asset class and security limits within the whole portfolio section of the guidelines.

The Group has material exposure to insurance business written in foreign currencies. Net assets are retained in foreign currencies as a hedge against solvency and RDS requirements arising from those currencies and to meet Lloyd's Trust Fund requirements. For more detail see Currency Management on page 46.

3. Credit risk

Credit risk is the risk that a counterparty is unable or unwilling to settle their obligations as they fall due. The main sources of credit risk to the Group arise from reinsurance recoveries, premiums due from brokers, coverholders and insureds, and fixed income investments made directly by the Group.

For the UK-managed operations credit risk relating to insurance and reinsurance counterparties is monitored through the Credit Committee with day-to-day management conducted by the Market Security and Ratings (MSR) team and the credit control team. All counterparties must be approved for use by the MSR team who will review published financials and assign a credit exposure limit. The limit is derived using a standard methodology agreed by the Credit Committee. The potential exposure under stressed scenarios is monitored on a monthly basis against these limits by the Credit Committee.

For the UK-managed operations credit risk relating to fixed income investments is monitored through the Investment Committee, with day-to-day management conducted by the investment and treasury teams.

For the Gibraltar-based operations all aspects of credit risk are managed by the BIG Board.

4. Operational risk

Operational risk is the risk of loss of earnings and/or value resulting from inadequate or failed internal processes, people and systems or from external events. It is inherent within all of the above risk categories due to the systems and process risks surrounding their management. Operational risks encompass customer treatment, product development risk, processes and systems risk, change risk, people risk, theft, fraud, legal and regulatory risks and corporate governance risk.

For the UK-managed operations, operational risk is owned by the Operations Committee and is managed by appropriate departments throughout the Group. For the Gibraltar-based operations, operational risk is owned and managed by the BIG Board.

Several processes have workflow management controls in place and the ERM framework includes a feature to assess the effectiveness of the control processes.

Each Group activity has a business continuity plan in place covering all locations, which is regularly tested and enhanced and established policies cover the risks of data protection, financial crime, money laundering, whistle-blowing and disaster recovery.

5. Group risk

Group risk is the risk that an entity faces by being part of an insurance group. These risks include liquidity, capital, project and regulatory and can arise from internal or external factors. Group Risk is owned by the N.V. Board.

Capital and liquidity risk is managed via the Capital Policy. This sets out the principles, defined by the N.V. Board, explaining how capital and liquidity should be managed in the Group. All business plans (and what-if scenarios) are monitored against this policy.

Financial Review

41 Financial Performance

44 Financial Management

47 Investments

Financial Performance

In 2010 Brit Insurance produced a return on equity excluding the effect of foreign exchange on non-monetary items of 14.4% (2009: 17.4%). The lower return reflects lower premium volumes, a higher burden of major claims and lower investment returns, partially offset by a lower tax charge.

Summary income statement

	12 months ended 31 December 2010 £m	12 months ended 31 December 2009 £m
Gross written premium	1,530.2	1,696.4
Net written premium	1,278.4	1,471.4
Net earned premium ¹	1,312.7	1,495.5
Underwriting result ¹	36.9	84.2
Investment return	113.4	137.4
Other expenses	(38.9)	(39.5)
Other foreign exchange	24.1	(3.3)
Other income, finance costs and associates	(16.3)	(7.5)
Profit before tax¹	119.2	171.3
Effect of foreign exchange on non-monetary items	(2.8)	(54.9)
Profit before tax	116.4	116.4
Tax	(5.9)	(28.9)
Profit after tax	110.5	87.5
Combined ratio ¹	97.1%	94.0%
RoE ¹	14.4%	17.4%

¹ Excluding the effect of foreign exchange on non-monetary items

Premiums

Gross written premium (GWP) for the 12 months to 31 December 2010 fell 9.8% to £1,530.2m (2009: £1,696.4m). This reflected the Group's active management of the underwriting portfolio and the non-recurrence of prior year premium adjustments experienced in 2009. At constant exchange rates the reduction was 10.4% (2009: growth of 10.4%) and excluding the movement on the re-estimation of prior year premium, which primarily arose in the Reinsurance SBU, underlying premium fell by 3.8%.

Gross written premium

	12 months ended 31 December 2010 £m	12 months ended 31 December 2009 £m	Movement at constant exchange rates %
Global Markets	778.3	875.3	(11.8)
Reinsurance	309.6	364.2	(15.8)
UK	441.2	455.4	(3.2)
Other ²	1.1	1.5	–
Total Group	1,530.2	1,696.4	(10.4)

² Includes the run-off of historic participations including Life Syndicate 389.

Premium rate increases for the year were 1.0% (2009: 4.8%) with either flat or increasing rates in each of the Group's three SBUs. The UK experienced the highest rate increases at 3.0% aided by rate increases of over 10% in Motor. Within Global Markets rate increases mainly fell within the –1% to +1% range, with overall rates flat. Reinsurance rates were marginally lower in Property lines and marginally higher in Casualty lines, whilst Marine XL experienced the highest rate increase at 7.6%.

Premium rating increases on renewal business

	12 months ended 31 December 2010 %	12 months ended 31 December 2009 %
Global Markets	0.0	4.3
Reinsurance	0.4	7.4
UK	3.0	3.7
Total Group	1.0	4.8

During the year, the Group continued to manage actively its underwriting portfolio. Since 2008, Global Markets has non-renewed over £160m of premium as it exited lines of business that no longer produced acceptable returns. It also increased the weighting in short-tail lines in response to the economic and investment return environment. In 2010, the UK SBU continued this trend by exiting the Local Authority (Municipal) market as pricing levels did not reflect the anticipated outlook for claims. It also substantially reduced its exposure to Private Motor during the period. At the same time the UK SBU continued to expand its micro insurance product offering which maintains its strong growth profile.

Net written premium (NWP) fell by 13.1% to £1,278.4m (2009: £1,471.4m) and net earned premium (NEP) excluding the effect of foreign exchange on non-monetary items reduced by 12.2% to £1,312.7m (2009: £1,495.5m).

Underwriting

The Group combined ratio – excluding the effect of foreign exchange on non-monetary items – increased to 97.1% (2009: 94.0%) with a 1.5 percentage point reduction in the claims ratio offset by a 4.6 percentage point increase in the expense ratio. The combined ratios for Global Markets and UK were broadly stable at 97.7% and 99.8% respectively whereas the combined ratio for Reinsurance increased by 8.3 percentage points to 88.2%.

Financial Performance continued

Combined ratio (excluding the effect of foreign exchange on non-monetary items)

	12 months ended 31 December 2010			12 months ended 31 December 2009		
	Claims ratio %	Expense ratio %	Combined ratio %	Claims ratio %	Expense ratio %	Combined ratio %
Global Markets	57.4	40.3	97.7	62.7	34.2	96.9
Reinsurance	59.6	28.6	88.2	54.9	25.0	79.9
UK	64.7	35.1	99.8	66.7	33.0	99.7
Total Group³	60.7	36.4	97.1	62.2	31.8	94.0

³ Includes the run-off of historic participations including Life Syndicate 389 and specific XL contracts underwritten by BIG.

The reduction in the Group claims ratio reflects a better underlying performance offset by an increase in major claims. Major claims in 2010 were £57.8m, relating to the earthquakes in Chile (£29.9m) and New Zealand (£27.9m). These added 4.4 percentage points to the Group claims ratio (2009: £12m claims from Air France; 0.8 percentage points). Claims estimates for the Chilean earthquake continued to improve from initial estimates in March 2010 of £47m, subsequently revised in June 2010 to £44m.

Excluding the effect of major claims, the accident year attritional claims ratio improved by 5.0 percentage points with each of the three SBUs showing an improvement. Most notable was Global Markets which saw an 8.4 percentage point improvement in its accident year attritional claims ratio, a reflection of the portfolio improvements made over the last two years.

As part of the Group's standard quarterly reserving reviews, the Group released £72.4m of claims reserves from prior years (2009: £81.2m) equivalent to 5.5 percentage points of net earned premium (2009: 5.4 percentage points of net earned premium). The Group experienced reserve releases in the majority of classes of business, particularly in Property (Global Markets and Reinsurance), Casualty Treaty Reinsurance and UK Liability.

Net reserve movements by SBU

	12 months ended 31 December 2010 £m	12 months ended 31 December 2009 £m
Global Markets	9.6	13.8
Reinsurance	25.0	24.1
UK	39.0	41.2
Other	(1.2)	2.1
Total Group	72.4	81.2

The expense ratio of 36.4% was 4.6 percentage points higher than 2009. The increase was due to a number of factors including higher commission levels arising from business mix and premium reductions (2.0 percentage points), the impact of lower earned premium on the direct cost ratio (1.2 percentage points) and higher regulatory levies and other direct costs including bonus accrual (1.4 percentage points).

The Group combined ratio, including the effect of foreign exchange on non-monetary items, was 97.6% (2009: 95.6%). See 'Foreign exchange' for more detail.

Other underwriting related items

The charge relating to the Group's catastrophe swap contract with Fremantle Limited, which is accounted for as a derivative, was £1.8m in 2010 (2009: £4.8m). This contract expired in June 2010.

Investment return

The Group continued to maintain a cautious investment stance during 2010 with the majority of investments in cash and short-dated high quality bonds. Investment return was £113.4m for the period (2009: £137.4m), a return of 3.2% (2009: 4.2%). During the first nine months of 2010 the Group continued to benefit from the impact of falling yields on the mark to market of the fixed income portfolio, whilst equity markets failed to make significant headway. In the last quarter however, this reversed with strong equity markets offsetting weak bond markets as yields on government debt rose. Throughout the period specialised funds made solid returns and yields on cash holdings remained low.

The Investments section of this report contains a detailed breakdown of the investment portfolio and investment return for 2010.

Other corporate expenses

Other non-insurance related expenses, which include Group central costs as well as one-off project costs, decreased by 1.5% compared with 2009 to £38.9m. The decrease arose from a lower number of one-off projects compared with 2009, but still included £2.8m in relation to the recommended cash offer by Achilles Netherlands Holdings B.V. The Group estimates that a further £8.6m of costs would be charged in 2011 if the recommended cash offer is declared wholly unconditional. Group headcount at 31 December 2010 was 746. Headcount has remained broadly constant since 31 December 2009 (741).

	Year ended 31 December 2010		Year ended 31 December 2009	
	Expenses £m	Ratio %	Expenses £m	Ratio %
Acquisition costs – commission ⁴	329.5	25.1	345.1	23.1
Other insurance related expenses	147.9	11.3	130.7	8.7
Underwriting expenses	477.4	36.4	475.8	31.8
Other corporate expenses	38.9	3.0	39.5	2.6
Total expenses	516.3	39.4	515.3	34.4

⁴ Excluding the effect of foreign exchange on non-monetary items.

Financial Performance continued

Foreign exchange

The Group experienced a total net foreign exchange benefit of £21.3m in 2010 (2009: £58.2m charge) made up of the following two elements.

The Group experienced a benefit of £24.1m in the period relating to a real gain on the revaluation of the element of the Group's capital that it holds in non-Sterling currencies. At 31 December 2010, £262.8m of the Group's net tangible assets were denominated in non-Sterling currencies.

Additionally, the Group recognised a charge of £2.8m relating to the IFRS requirement to recognise non-monetary assets and liabilities (DAC and UPR) at historic rather than closing exchange rates. At 31 December 2009, the difference between recognising non-monetary assets and liabilities at historic rather than closing exchange rates was an additional net liability of £0.9m. At 31 December 2010, the difference between recognising non-monetary assets and liabilities at historic rather than closing exchange rates was an additional £3.7m net liability. The charge in 2010 of £2.8m is the movement between the differences at 31 December 2009 and 31 December 2010.

On the basis that exchange rates remain constant, the additional net liability at 31 December 2010 of £3.7m will reverse as a gain to earnings during 2011. Figures relating to this adjustment are disclosed separately in the segmental information in the column 'Effect of foreign exchange on non-monetary items'. The Group considers this purely a timing difference in profit recognition and has therefore presented additional profit before tax and RoE figures excluding its effect.

The total foreign exchange related gain of £21.3m is made up of £29.3m 'Net foreign exchange gain' per the face of the income statement and a reclassification of part of the foreign exchange translation on non-monetary items to premium and acquisition costs. This latter adjustment can be seen in the column 'Effect of foreign exchange on non-monetary items' in Note 5 to the Financial Statements – Segmental information.

Effect of foreign exchange on non-monetary items

	12 months ended 31 December 2010 £m	12 months ended 31 December 2009 £m
UPR/DAC valued at historic rates of exchange	433.6	461.8
UPR/DAC valued at closing rates of exchange	429.9	460.9
Valuation difference in closing balance sheet (A)	(3.7)	(0.9)
Valuation difference in opening balance sheet (B)	(0.9)	54.0
Effect of foreign exchange on non-monetary items (A-B)	(2.8)	(54.9)

Foreign exchange (losses)/gains

	12 months ended 31 December 2010 £m	12 months ended 31 December 2009 £m
Gains/(losses) on exchange	24.1	(3.3)
Effect of FX on non-monetary items (from above)	(2.8)	(54.9)
Total foreign exchange gains/(losses)	21.3	(58.2)
Of which:		
Net FX gains/(losses) (per face of income statement)	29.3	(33.4)
Included within premium and acquisition costs (per segmental)	(8.0)	(24.8)

Associated undertakings

The Group's share of the result of associated undertakings was a loss of £1.8m (2009: loss of £2.3m). £0.8m of the loss relates to the Group's interest in Ri3K which was disposed of in December 2010. The loss on disposal of £0.4m is shown separately. Details of the Group's remaining associated undertakings can be found in Note 19 of the consolidated financial statements.

Profit before tax

The Group's profit before tax excluding the effect of foreign exchange on non-monetary items was £119.2m, a decrease of 30.4% over the prior period (2009: £171.3m). Including the effect of foreign exchange on non-monetary items, the profit before tax was stable at £116.4m (2009: £116.4m).

Tax

The Group's effective tax rate was 5.1% (2009: 24.8%) and benefited from the Group reorganisation, which was completed in late 2009, as well as favourable development relating to prior year provisions.

Net income, EPS and return on equity

Net income for the 12 months to 31 December 2010 was £110.5m compared to £87.5m in 2009. This translates into earnings per share (EPS) of 142.4p (2009: 113.2p) and return on equity of 14.2% (2009: 12.2%).

Excluding the effect of foreign exchange on non-monetary items, the annualised return on equity was 14.4% (2009: 17.4%).

Distributions

Distributions equivalent to 60.5p per share have been paid (2009: 60.0p paid) to shareholders during the year, with £41.1m being settled in cash and £5.9m in the form of new shares via the scrip option. Given the recommended cash offer by Achilles Netherlands Holdings B.V., the Board is not recommending a final distribution for the year ended 31 December 2010.

Net asset value

Net tangible asset value (NTA) of £889.8m was 9.4% higher than at 31 December 2009. This growth reflects the profit after tax for the period of £110.5m less the cash element of the 2009 final and 2010 interim distributions of £41.1m. NTA per share at 31 December 2010 was £11.41 compared with £10.52 at 31 December 2009, a growth of 8.5%.

Financial Management

Overview

Financial management focuses on all areas of the Group's balance sheet from assessing the right level and type of capital to managing the Group's exposure to credit and liquidity risk. The Group continuously responds to developments in the financial environment with the intention to improve risk-adjusted returns. This is especially relevant to the introduction of Solvency II in 2013.

Capital resources

	31 December 2010 £m	31 December 2009 £m	31 December 2008 £m	31 December 2007 £m	31 December 2006 £m
Net tangible assets	889.8	813.4	767.6	768.4	724.3
Long-term subordinated debt*	133.0	132.8	132.7	147.3	147.2
Total capital resources	1,022.8	946.2	900.3	915.7	871.5

* Subordinated borrowings which have at least five years remaining to maturity or call and are of the types which qualify as regulatory capital.

Capital management

The purpose of the capital management strategy is to ensure the capital adequacy of the Group and each underwriting entity whilst optimising return on equity.

Capital adequacy is assessed against three benchmarks: regulatory capital, rating agency capital and management capital. In the event a shortfall is forecast, escalation procedures are in place to address this.

Capital resources and capital adequacy

In assessing the Group's capital adequacy, the principal sources of capital are shareholders' equity net of intangible assets (net tangible assets) and subordinated debt.

The main internal benchmark for assessing capital adequacy is management capital. This is defined as 120% of the Individual Capital Assessment (ICA), plus a capital buffer designed to deal with shock events. Management capital must at all times be covered entirely by net tangible assets and long-term debt. Throughout 2010 this condition was met.

For each regulated entity, capital is maintained at the higher of regulatory, rating agency and management capital requirements. The current ratings for Brit Insurance Limited are A (Strong) with stable outlook from Fitch and A (Excellent) under review with negative implications from AM Best. The Group may decide to use short-term debt to cover timing differences, for example 'trapped' profits in Lloyd's or future dividends from BIL, but this is not permitted to form part of Group-wide management capital.

The Group's capital position is currently in excess of regulatory requirements. On an Enhanced Capital Requirement (ECR) basis the Group's coverage at 31 December 2010 was estimated at 1.32 times. The ECR approach uses a common factor-based model to calculate required capital on a risk-by-risk basis and does not explicitly allow for the potential diversification within an individual company or group.

The Group's ICA requirement, however, is based on the Group's internal model and takes into account the Group's specific portfolio and recent and expected future performance. The Group's coverage of its ICA requirement is estimated at 1.49 times at 31 December 2010.

Further details on capital risk management are given in Note 4 of the financial statements.

Lloyd's regulatory requirements

During 2010, in accordance with the regulatory timetable, the capital requirement for Syndicate 2987 was agreed with Lloyd's. The Lloyd's capital requirement is known as Funds at Lloyd's (FAL). The following table shows the FAL composition for 2010/11.

	2011 Year £m	2010 Year £m
Underwriting Capacity		
at Lloyd's (Syndicate 2987)	760.0	745.0
FAL requirement		
Capital requirement	430.6	397.4
Allowance for open years of account loss/(profit)	25.1	49.8
Total	455.7	447.2
FAL assets at 31 December	2010	2009
Investments	431.3	434.6
Cash	21.2	14.6
Total	452.5	449.2
Of which Sterling denominated	316.7	325.3
Of which US dollar denominated	135.8	123.9

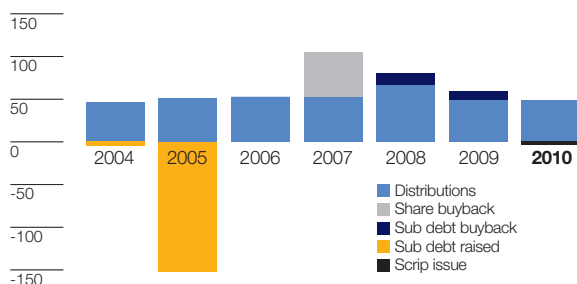
The FAL requirement and FAL assets are brought into line twice a year, in May and November. This is known as the 'coming into line' process. Between these times, asset valuation fluctuations may create a mismatch, which unless material, will not be adjusted for until the following 'coming into line' process. The Group holds its FAL in Sterling and US dollar denominated assets to minimise the effect of exchange rate fluctuations.

Managing the level of capital

Managing the level of capital is a key element in achieving the Group's return on equity target. The Group looks to hold adequate capital to meet its management capital requirements and to ensure rating agency and regulatory requirements are met for each entity. When capital resources are significantly above this level, the Group has a track record of returning excess funds to shareholders. Since it reinstated dividends in 2004, the Group has returned over £350m of equity to shareholders through cash distributions as well as £53m through share buybacks. Over this period the Group has also improved balance sheet efficiency, raising £150m of long-term subordinated debt in December 2005, of which £15m was bought back at a substantial discount in 2008.

Financial Management continued

Returned capital (£m)



Reinsurance and risk transfer

As part of the overall capital management process the Portfolio Management Committee (PMC) is responsible for structuring the reinsurance protection purchased to mitigate that element of the insurance risk the Group does not wish to retain. Different outwards reinsurance strategies are modelled and reviewed to assess the level of balance sheet and earnings volatility protection available. The Group uses a variety of proportional and non-proportional reinsurance contracts written on both a treaty (portfolio) and facultative (individual risk) basis.

In general, proportional reinsurance is used as a capital management tool and enables the Group to leverage its underwriting expertise. Non-proportional reinsurance is used to reduce volatility.

Reinsurance spend as a percentage of gross written premium was 16.4% (2009: 13.3%).

Reinsurance premium ceded

	12 months ended 31 December 2010 £m	12 months ended 31 December 2009 £m
Proportional	113.6	101.2
Non-proportional	138.2	123.8
Total	251.8	225.0

Reinsurance spend in 2010 increased versus 2009 both in absolute terms and as a percentage of gross written premium. The majority of the increase arose in the Global Markets SBU due to an increase in quota shares on the Marine and Legal Expenses accounts.

The financial strength ratings of the reinsurers underlying the Group reinsurance recoverables at 31 December 2010 are set out below. These figures include assumed recoveries in respect of outstanding claims and claims incurred but not reported and are net of impairment provisions at 31 December 2010 of £10.8m (2009: £12.4m).

	AAA £m	AA £m	A £m	BBB & Below £m	Collateralised £m	Not rated £m	Total £m
Reinsurance assets at 31 December 2010	0.6	164.2	197.8	5.7	71.2	13.5	453.0
Reinsurance assets at 31 December 2009	7.7	178.7	176.3	4.0	75.4	18.3	460.4

94% of the Group's reinsurance exposure is with counterparties with credit quality of A or better or is collateralised (2009: 95%).

Solvency II

Following research and assessment of the potential impacts of Solvency II, the Group remains convinced that significant competitive advantage can be gained by those firms who embrace the change and use it to drive improvements within their business.

This approach has already led the Group to consider and implement key changes around its governance, risk processes and organisation, including the recent appointment of the Group Chief Risk Officer. We expect these changes to result in further improvements in how risk and reward are balanced throughout the business.

The Group also made significant progress towards Solvency II compliance including the successful completion of QIS5 for Brit Insurance Limited, Brit Syndicates Limited, Brit Insurance (Gibraltar) PCC Limited and the Brit Insurance Group.

Working closely with regulators resulted in the approval of the FSA to enter the Internal Model Approval Process (IMAP) and positive feedback from Lloyd's and the Gibraltar FSC on progress made to date. A strong dialogue with key regulators will be maintained during 2011 to gain Internal Model approval in line with the start of Solvency II.

The Solvency II framework continues to evolve, and Brit Insurance will continue its work with regulators and trade bodies to ensure a pragmatic and balanced approach continues through its implementation.

Liquidity management

The Group aims to hold a buffer to address the liquidity requirements arising from shock events. This buffer was regularly reviewed and monitored by the Capital Committee during 2010 with responsibility moving to the Portfolio Management Committee for 2011. The liquidity buffer is funded by free cash as well as unutilised credit facilities.

On 9 November 2009 the Group entered into a three-year revolving credit facility agreement for up to £175m with The Royal Bank of Scotland plc, Lloyds TSB Bank plc and Calyon. At 31 December 2010, £37.0m of the facility was drawn down (2009: £107.0m). At 24 February 2011, the facility was undrawn.

On 26 October 2010 the Group agreed to enter into a new £200m four-year revolving credit facility, effective if the acquisition of the Group by Achilles Netherlands Holdings B.V. is declared wholly unconditional, with The Royal Bank of Scotland plc, Lloyds TSB Bank Plc, Bank of America, N.A. and Citibank N.A., London Branch.

The Group gearing ratio at 31 December 2010 was 16.5% (31 December 2009: 25.1%). The Group's current appetite is to retain a gearing ratio below 30%.

Financial Management continued

Currency management

The Group writes a significant amount of its insurance business in currencies other than Sterling, thus necessitating the Group to hold multiple currency balances within its books.

The Group uses two main principles in managing currency exposure. First it matches major non-Sterling liabilities (i.e. net claims reserves) with equivalent financial assets denominated in the same currency. This mitigates the risk that the Group cannot meet its obligations in local currency or that a move in the exchange rate creates a financial loss.

Secondly, the Group holds non-Sterling financial assets in excess of non-Sterling liabilities in order to manage the effect of exchange rate movements on the Group's capital adequacy. As a significant amount of the Group's underwriting exposure (in particular to catastrophe risk) is in non-Sterling currencies, exchange rate fluctuations can affect the amount of Sterling capital required to be held as solvency or against Realistic Disaster Scenarios (RDSs). The equivalent Sterling amount of US dollars, Canadian dollars and Euros at 31 December 2010 was £262.8m (2009: £259.8m). The Group manages currency positions with regular sales of the major non-Sterling currencies, in particular the US dollar.

In addition, the significant movement in exchange rates in recent years has at times caused the exchange rate used by Lloyd's for assessing the FAL solvency requirements to be materially different to the market spot rate. To manage the effect this has on the FAL requirement, surplus net assets denominated in US dollars are now held within FAL. At 31 December 2010 the level of US-denominated assets in FAL was US\$213m, equivalent to 30% of the total FAL requirement.

Claim reserve estimation

The Group evaluates reserves to pay for reported claims and for claims incurred but not reported (IBNR) on a quarterly basis. The process of estimating the right level of reserve is by definition subjective and can significantly affect the accounting result in any one period. The reserves selected each quarter are based on analysis and recommendations from the actuarial department. The Group's reserving policy is to reserve at actuarial best estimate and in addition to retain a margin to allow for uncertainties.

The Group has benefited from consistent net reserve releases over the last five years as claims in the 2002 to 2004 underwriting years have settled materially below initial estimates. Modest releases have also been experienced on the 2005 and 2006 underwriting years. More recent underwriting years are at an earlier stage of development but the Group's reserving process over this period was unchanged from prior years.

The margin retained by the Group to allow for uncertainties over the actuarial best estimate is £40m, which has remained unchanged over the last three years. For many years the Group has had an external actuarial firm review the reserves annually and the internal actuarial best estimate has consistently been higher than the external best estimate, i.e. more conservative.

To aid understanding of the Group's reserving track record, the ultimate net loss ratios on an underwriting year basis are set out below. This table should be read horizontally and shows how over time the ultimate net loss ratio on each underwriting year develops from the level at which it was initially set. These figures are based on premium net of brokerage which is the basis on which the Group sets its claims reserves.

This data is based on an underwriting year approach and hence a significant amount of risk remains in force after one year. The ultimate net loss ratio after one year is therefore not necessarily a good indicator for the ultimate outcome as it can still be affected by new claim events. After two years the majority of risk has expired and consequently the movement in the ultimate net loss ratio from this point offers a better indicator of the reserving track record. For example, the increase in the ultimate net loss ratio for 2009 is partially caused by claims from the Chile earthquake which, although occurring in 2010, relates to risks written in the 2009 (and to a lesser extent 2008) underwriting year.

In the 2005 to 2009 financial years the Group released cumulatively £364m from claims reserves (averaging £73m per annum) and this trend has continued in 2010 with a release of £72.4m. Taken together, the maintenance of a consistent margin and continued reserve releases demonstrates the strength of the Group's reserving position.

Development of Group ultimate net loss ratio by underwriting year

	After 1 year	After 2 years	After 3 years	After 4 years	After 5 years	After 6 years	After 7 years	After 8 years
2003	74%	72%	64%	59%	56%	53%	51%	50%
2004	81%	79%	72%	70%	68%	66%	65%	
2005	106%	110%	107%	104%	102%	96%		
2006	81%	83%	80%	76%	74%			
2007	89%	92%	92%	92%				
2008	95%	99%	100%					
2009	85%	87%						

Investments

Strategy

The Group allocates its investment holdings into one of three internal portfolios – the liability portfolio, the working capital portfolio and the capital portfolio.

The largest portfolio represents funds that are expected to be called upon to pay claims to policyholders (the liability portfolio). These liabilities are segmented by currency and legal entity, and a benchmark is chosen for each segment that matches the characteristics of the liabilities. The investment objective in the liability portfolio is safety, liquidity and return of capital. Assets are primarily allocated to high quality fixed income securities.

The remaining investments, net of cash held in treasury (the working capital portfolio), are allocated to the capital portfolio. The objective of this portfolio is to support the long-term growth of shareholders' funds by earning a competitive return on capital. The current benchmark for the capital fund is LIBOR + 3%, which was comfortably exceeded during 2010. Assets are allocated to all types of fixed income securities (including corporates, mortgages and index-linked bonds), equities and alternative assets.

The Group adheres to a detailed set of investment guidelines that have been approved by the Board. The guidelines have been constructed with the intention of allowing the Group to achieve a competitive investment return while minimising the risk of a meaningful reduction in capital arising from market volatility. All material decisions regarding the allocation of assets within the guidelines are taken by the Investment Committee.

Performance

In 2010 the Group's investments produced a total return for the year of £113.4m (3.2%), compared to a return of £137.4m (4.2%) in 2009.

The fixed income portfolio return of 3.1% was lower than last year's 4.5%. The drivers of performance during 2010 were quite different when compared to 2009. Over 2010, the US Treasury yield curve rallied by between 50 to 70 basis points for two to ten year yields, while in the UK the Gilt curve flattened as it rallied. In the UK, shorter-term two to four year yields rallied by about 20 basis points, while the longer end of the yield curve rallied by about 50 basis points. Within this context higher returns were available for longer durations in both the UK and in US.

The Group continued to hold corporate exposure at the upper end of its guideline limits throughout the year and corporate bonds generally outperformed government bonds as spreads tightened modestly. Over 2010 the Group initiated two new fixed income mandates which helped to maintain and manage its interest rate and credit exposures.

The equities and the specialised investment funds performed well during 2010. The equity portfolio provided a return of 16.5% albeit with periods of volatility, whilst specialised investment funds produced a return of 11.8%. Illiquid equity investments were exited and replaced by high quality dividend yielding companies in the directly managed portfolios together with new long-only equity funds.

Specialised investment funds were further streamlined as a result of redemptions, takeovers and restructurings.

Asset allocation

Brit Insurance entered the year with high cash balances and a high weighting in corporate bonds towards the top of the range established by the Group's investment guidelines. The overweight position in corporate credit was broadly maintained throughout 2010 as non-financial corporate issues were added to the portfolio. Cash balances declined during most of 2010 and were reinvested in debt securities. It is expected that cash holdings will continue to decline during the first half of 2011.

Investment return

	Year ended 31 December 2010		Year ended 31 December 2009	
	£m	%	£m	%
Equity securities	17.6	16.5	13.8	17.5
Debt securities	80.0	3.1	92.5	4.5
Specialised investment funds	11.3	11.8	17.9	19.2
Cash and cash equivalents	4.5	0.5	13.2	1.5
Total portfolio	113.4	3.2	137.4	4.2

Asset allocation by asset class

	31 December 2010		31 December 2009	
	£m	%	£m	%
Equity securities	125.7	3.5	102.0	2.9
Debt securities	2,692.7	76.0	2,282.4	65.7
Specialised investment funds	102.6	2.9	96.7	2.8
Cash and cash equivalents	623.4	17.6	994.2	28.6
Total	3,544.4	100.0	3,475.3	100.0

Investments continued

Breakdown of debt securities at 31 December 2010

	Government	P-1	AAA	AA	A	BBB and lower	Total £m
Government issue*	1,435.5	–	–	–	–	–	1,435.5
Corporate bonds	–	–	21.6	211.6	514.7	87.7	835.6
CDs and CPs	–	279.7	–	–	–	–	279.7
Other	–	–	141.9	–	–	–	141.9
	1,435.5	279.7	163.5	211.6	514.7	87.7	2,692.7

* All government issue bonds are from either the US, Canada, UK or eurozone countries.

Breakdown of debt securities at 31 December 2009

	Government	P-1	AAA	AA	A	BBB and lower	Total £m
Government issue*	1,045.5	–	–	–	–	–	1,045.5
Corporate bonds	–	–	163.3	218.5	282.9	58.1	722.8
CDs and CPs	–	346.9	–	–	–	–	346.9
Other	–	–	111.1	42.7	13.4	–	167.2
	1,045.5	346.9	274.4	261.2	296.3	58.1	2,282.4

* All government issue bonds are from either the US, Canada, UK or eurozone countries.

At 31 December 2010 the Group held £12.5m in debt securities relating to Italy and Spain. The Group had no direct holdings in debt securities relating to Portugal, Greece or Ireland.

During the first half of the year, additional investments were made in asset-backed securities (ABS), residential mortgage-backed securities (RMBS) and commercial mortgage-backed securities (CMBS). Holdings at 31 December 2010 totalled £139.4m and were all rated AAA.

Investments by currency

	31 December 2010		31 December 2009	
	£m	%	£m	%
Sterling	1,787.5	50.4	1,780.1	51.2
US dollar	1,224.1	34.5	1,226.6	35.3
Euro	387.8	11.0	348.2	10.0
Canadian dollar	145.0	4.1	120.4	3.5
Total	3,544.4	100.0	3,475.3	100.0

The Group remained conservatively positioned during 2010 with respect to asset duration although both Sterling and US dollar duration increased slightly during the year. Duration in the US dollar portfolio ended the year at 1.8 years with the duration of the Sterling portfolio also at 1.8 years. The duration of both portfolios is likely to increase further during 2011.

Debt securities (ex CDs/CPs) duration

	31 December 2010 Yrs	31 December 2009 Yrs
Sterling	1.8	1.2
US dollar	1.8	1.5
Euro	2.1	1.4
Canadian dollar	1.8	1.6

Outlook

The outlook for the Group's investment return remains challenging. The macro issues will continue to focus on concerns surrounding peripheral Europe, fears of overheating and inflation in the emerging markets and ultimately a normalisation of monetary policies in the developed world. In markets the search for income will remain a powerful driver and 2011 may see investors seeking it in increasingly unfamiliar places. In such an environment Brit Insurance believes a conservative approach remains appropriate, but will continue to explore new opportunities.

Governance

50	Board of Directors
52	Corporate Governance Report
59	Directors' Remuneration Report
66	Directors' Responsibility Statement
67	Sustainability
71	Investors

Board of Directors

Robert John Orr Barton (John) Chairman

John joined the Board of Brit Insurance Holdings PLC in 2007 as Deputy Chairman and succeeded Clive Coates as Chairman in May 2008. He was appointed to the Board of Brit Insurance Holdings N.V. in October 2009 as Chairman. His contract was renewed with effect from 31 December 2010 for a further term of three years to 31 December 2013. He has a wealth of experience in insurance underwriting and broking as well as the property and consumer retail arena.

John is currently Chairman of Next plc and a non-executive director of WH Smith PLC and Cable & Wireless Worldwide plc. He was Chief Executive of JIB Group plc for 13 years, Chairman of Jardine Lloyd Thompson Group plc for five years and Chairman of Wellington Underwriting plc for five years.

(Born 1944, British nationality, male, Chartered Accountant; appointed in 2009, term subject to terms of the Company's Articles of Association, term expires in 2013).

Joseph Patrick MacHale (Joe) Non-Executive Director

Joe joined the Board of Brit Insurance Holdings PLC in 2005. He was appointed to the Board of Brit Insurance Holdings N.V. in December 2009. He is Chairman of the Remuneration Committee and a member of the Nomination and Audit Committees.

He held a number of senior positions with JP Morgan between 1979 and 2001 and was most recently chief executive of JP Morgan Europe, Middle East and Africa Region.

He is currently a non-executive director of Royal Bank of Scotland Group PLC, chairman of the Prytania Group LLP and a Trustee of Macmillan Cancer Support.

(Born 1951, British nationality, male, Banker; appointed in 2009, term subject to terms of the Company's Articles of Association).

Dane Jonathan Douetil CBE Chief Executive Officer

Dane joined Brit Insurance Limited (BIL) in 1998 and was appointed as BIL's Chief Executive Officer in December of the same year. In 2002 he was appointed Chief Executive Officer of Brit Syndicates Limited and Group Head of Underwriting.

Dane was appointed Chief Executive Officer of Brit Insurance Holdings PLC in 2005 having been Deputy Chief Executive Officer since March 2004 and an Executive Director since 1999. He was latterly appointed Chief Executive Officer of Brit Insurance Holdings N.V. in 2009.

Dane joined the Willis Faber Group in 1982 and was appointed executive director of the Political & Financial Risk Division in 1988. He was a founder shareholder and director of Special Risk Services Limited from 1989-1994. Between 1994 and 1998 he was a consultant on the sale of a number of mortgage operations and a risk consultant to several financial institutions. He was appointed a full time consultant to The Benfield Group in 1997 prior to joining BIL.

He joined the Board of the ABI in 2009, was on the Board of the Lloyd's Market Association from 2004-2006, the last year of which was as chairman, chaired the Market Reform Group until the beginning of 2008 and chaired the industry's Contract Certainty Steering Group from 2005 to 2007.

Dane was made a Commander of the Order of the British Empire in 2007 for services to business.

(Born 1960, British nationality, male, appointed in 2009, term subject to terms of the Company's Articles of Association, has a 12 month rolling contract of employment).

Peter Frank Hazell Non-Executive Director

Peter joined the Board of Brit Insurance Holdings PLC in 2004. He was appointed to the Board of Brit Insurance Holdings N.V. in December 2009. He is Chairman of the Audit Committee and a member of the Remuneration and Nomination Committees.

He was previously UK managing partner of PricewaterhouseCoopers. He spent his early career at Deloitte Haskins & Sells in their Management Consultancy Division, later advising on competition policy, investment appraisal and strategic planning.

He was also involved in founding the Corporate Finance Practice, specialising in privatisation, regulation and mergers and acquisitions.

Peter is chairman of Argent Group PLC, a non-executive director of UK Coal PLC and of Smith & Williamson Holdings Limited. He is a member of the Natural Environment Research Council, a trustee of The Oval Cricket Relief Trust, and was until mid January 2010 a member of the Competition Commission.

(Born 1948, British nationality, male, appointed in 2009, term subject to terms of the Company's Articles of Association).

Board of Directors continued

Cornelis Antonius Carolus Maria Schrauwers (Cees)

Senior Independent Director

Cees joined the Board of Brit Insurance Holdings PLC in 2005. He was appointed to the Board of Brit Insurance Holdings N.V. in October 2009 and is the Senior Independent Director. He is a member of the Audit, Nomination and Remuneration Committees.

Cees was appointed as a Non-Executive Director of Brit Insurance Limited and Brit Syndicates Limited in 2007.

He has some 30 years' industry experience, most recently as managing director of Aviva International and managing director of CGU Insurance. He previously held a number of senior positions in Commercial Union. Prior to this Cees was a partner with Coopers & Lybrand in charge of insurance consultancy.

He is chairman of Drive Assist Holdings Limited, Senior Independent Director of Record plc and, a Commissioner of the Guernsey Financial Services Commission.

(Born 1947, Dutch nationality, male, appointed in 2009, term subject to terms of the Company's Articles of Association).

Maarten Joannes Hulshoff

Non-Executive Director

Maarten joined the Board of Brit Insurance Holdings N.V. in December 2010.

Maarten, a Dutch national, holds a master's degree in economics from the Erasmus university in the Netherlands.

He has held various management positions with Citigroup in Europe and Asia and has been chairman of the managing board of NCM (renamed Atradius), Rabobank International and Rodamco Europe (merged into Unibail-Rodamco).

He currently holds a number of senior board positions within a number of major companies, including chairman of the supervisory boards of Credit Europe Bank and Goedland, member of the board of Damen Shipyards Group and a member of the board of HB Reavis.

(Born 1947, Dutch nationality, male, Company director; appointed in 2010, term subject to terms of the Company's Articles of Association).

Willem Frans Casimir Stevens

Non-Executive Director

Willem was appointed to the Board in December 2009. He is an independent counsel on legal, tax and corporate governance issues.

Willem is a member of the supervisory board of AZL N.V., Goedland N.V., N.V. Luchthaven Schiphol, Stichting Exploitatie Nederlandse Staatsloterij, and Stichting Holland Casino.

He is a chairman of the supervisory council of the Stichting Onderzoek Diabetes Nederland.

He is a managing director on the board of Michelin Finance BV, chairman of Foundation Preferred Shares WAVIN N.V., vice-chairman of Het Concertgebouw Fonds, and a director of Foundation Priority Shares ANTEA Participaties.

He is a board member of Chamber of Commerce Nederland-Israel and a governor of Harvard Law School Association of Europe.

(Born 1938, Dutch nationality, male, Attorney at Law; appointed in 2009, term subject to terms of the Company's Articles of Association).

Corporate Governance Report

Brit Insurance has a strong ethos of corporate governance and is committed to business integrity, ethics and professionalism. The Board fully supports the need for good corporate governance and, following its change of domicile to the Netherlands in December 2009, promotes the highest standards by complying with both the applicable provisions of the Dutch Corporate Governance Code ('Dutch Code') as well as the UK Corporate Governance Code (the 'UK Code'). (The Dutch Code and the UK Code are hereinafter referred to as the 'Codes').

The Company has a one-tier board and, in accordance with the Codes, the Non-Executive Directors are able to provide proper and independent supervision. The best practice provisions of the Dutch Code applying to a one-tier board are all complied with and there are no exceptions.

The full text of the Dutch Code and the UK Code can be viewed on www.commissiecorporategovernance.nl/ www.frc.org.uk respectively.

The Board

The Board operates a single-tier management structure and is responsible for creating and sustaining shareholder value through the management and control of the Group's businesses. It is the decision making body for all matters material to the Group in strategic, financial and reputational terms and ensures that management maintain a system of internal control that provides assurance of effective and efficient operations, internal financial controls and compliance with regulation and laws. The schedule of matters reserved to the Board is reviewed annually and includes approval of the financial results, strategy and corporate objectives, significant transactions and matters affecting share capital. Subject to this schedule, the Board delegates certain powers to a number of committees within written terms of reference as detailed below.

During the period up to 17 December 2010 the Company held eight scheduled Board meetings, including a two day meeting to consider the Group's ongoing strategy. The Board considered, amongst other items, the 2009 full-year and 2010 half-year results, distributions, annual business plan and budget. At each scheduled meeting, the Board received a report on the Group's performance and other relevant matters from the Chief Executive Officer and Finance Director. In addition, a further two unscheduled Board meetings were held to consider the offer from Achilles Netherlands Holdings B.V. (the Offer).

In addition to considering the full-year, half-year results and Interim Management Statements the Board considered amongst other matters:

- ▶ Strategy
- ▶ Business plans
- ▶ Group performance
- ▶ Board performance
- ▶ Terms of reference
- ▶ Tax and treasury policies
- ▶ Investor relations
- ▶ Group policies

▶ Committee and subsidiary updates

▶ Governance and compliance

In addition, in response to the approach from Apollo Management VII, L.P., the Board formed the Board Response Sub Committee (BRSC) to conduct any bid processes in relation to approaches by third parties with a view to them making, or announcing an intention to make, an offer for all or part of the share capital of the Company. The BRSC held six Committee meetings during the year for this purpose.

Board composition

The Board should have an appropriate balance of skills, knowledge and experience to support its strategy and the effective management of the Company and its investments. The Nomination Committee reviews the balance and composition of the Board and its principal Committees and considers the issue of independence on an annual basis. The Nomination Committee reviewed the Non-Executive Directors' independence against the UK Code criteria, which was regarded as the most comprehensive and considered each Non-Executive Director to be independent. At least half the Board, excluding the Chairman, are independent Non-Executive Directors. The Chairman was deemed to be independent at his date of appointment.

At the date of this report, the Board comprised the Chairman, one Executive Director and five independent Non-Executive Directors whose biographies are on pages 50 and 51. Ken Culley and Michael Smith retired from the Board on 6 May 2010 and Matthew Scales stepped down from the Board on 20 December 2010. Maarten Hulshoff was appointed a Non-Executive Director of the Company on 17 December 2010. The Executive Director is permitted to maintain one non-executive appointment at any one time.

Chairman and CEO

The roles of the Chairman and Chief Executive Officer (CEO) are separate and each has clearly defined responsibilities within their terms of reference. The Chairman's main role is to lead and manage the work of the Board to ensure that it operates effectively and provides appropriate challenge and support to the executive management. The Chairman also ensures, with support from the Company Secretariat, that Directors receive accurate, timely and clear information about the Group's performance to enable the Board to take sound decisions, monitor effectively and provide advice to promote the success of the Group. He also ensures effective communication with the shareholders. There have been no additional significant commitments taken on by the Chairman in 2010. The CEO is responsible for the day-to-day management of the Group, recommending strategy to the Board and making and implementing operational decisions.

Senior Independent Director

Cees Schraauwers continued in this role during the year. If shareholders or investors do not wish to follow the usual methods of communication through the Chairman, Chief Executive Officer or Finance Director, the Board's Senior Independent Director is available to meet with shareholders or investors. The role of the Senior Independent Director is clearly established and agreed by the Board as detailed within their terms of reference.

Corporate Governance Report continued

Appointment, retirement and re-election

The Company's shareholders may appoint a Director by ordinary resolution. The UK Code and the Company's Articles of Association require one third of the Directors to retire from office at every Annual General Meeting (AGM) and each Director must offer himself for re-election at least once every three years. Details of the Directors retiring and offering themselves for re-election at this year's AGM may be in the 2011 AGM notice of meeting. The Company's Nomination Committee has considered the effectiveness of each Director offering himself for re-election at the AGM and has advised the Board that each Director has continued to make an effective contribution to the Group and each Director has committed sufficient time to the Group.

Directors' interest

The interests of the Directors who held office at 31 December 2010 and their connected persons in the ordinary shares or other securities of the Company are disclosed in the Directors' Remuneration Report on pages 59 to 65.

Conflicts of interest

The Company's Articles of Association and the Dutch Code permit the Board to consider, and if thought fit, to authorise situations where a Director has an interest that conflicts, or may possibly conflict, with the interest of the Company. In deciding whether to authorise a conflict of interest, the conflicting Director will not take part in any discussion or decision making. The Board will consider if approving a conflict of interest promotes the success of the Company and whether authorisation should be contingent on factors including: the type of company involved, the nature of the conflict and the position of the Director. Any notified conflicts of interest considered or approved will be recorded in the minutes of that meeting and included on the Register of Conflicts of Interest.

Joe MacHale is a Non-Executive Director of Royal Bank of Scotland Group PLC (RBS Group) and is consequently deemed to be interested in the Group's current £175m Revolving Credit Agreement as well as a proposed £200m Revolving Credit Facility agreement with an RBS Group company, which acts as an arranger, facility agent and participant on both facilities. Joe MacHale has been a director of companies in the JP Morgan group in recent years and the Company appointed JP Morgan Securities Limited as the Company's joint corporate broker and financial adviser in January 2010. The potential conflict of interest for this Director was disclosed prior to his appointment and authorised at that time. These conflicts have been reviewed by the Company's Board and remain authorised. At no time during the year did any Director hold a material interest in any contract of significance with the Company or any of its subsidiary undertakings other than service contracts between each Executive Director and a Group company, details of which are disclosed in the Director's Remuneration Report.

Dane Douetil was deemed not to be independent in respect of the Offer negotiations following the start of the discussions relating to the Management Agreement. This was due to the natural conflict of interest that arises in such negotiations. Dane Douetil took no part in any Board or

BRSC decisions relating to the Offer from Achilles following his loss of independence. The Board has adopted an appropriate policy to ensure that its powers of authorisation of conflicts of interest operate effectively.

Directors and Officers insurance

Throughout 2010, directors and officers liability insurance has been available for the benefit of Directors and Officers. In addition, each Director had a deed of indemnity with the Company. This deed of indemnity was in accordance with the provisions of the Company's Articles of Association.

Induction and professional development

On appointment, Directors receive a comprehensive induction programme tailored to their individual requirements. This covers the Group's operations, activities and risks, responsibilities of a Director, role of the Board and Committees and governance policies and procedures. In addition, they meet key business and function heads and receive ongoing training and updates to improve their knowledge and skills to discharge their duties effectively. A log of all Directors' training and development is maintained which is reviewed as part of the annual performance appraisal process. Directors may request independent professional advice at the Company's expense. No such requests were received during the year except in relation to the Offer and the Management Agreement.

Board effectiveness

Following the Board's recommendation of the Offer from Achilles in November 2010, it was clear that significant changes to the Board's composition would occur on the Offer becoming wholly unconditional. Under these circumstances the Nomination Committee recommended, and the Board approved, that the annual Board/Committee performance evaluations be deferred. It was further agreed that in the event that the Offer was not declared wholly unconditional, the Board would appoint external consultants to undertake a formal performance evaluation in early 2011. In this respect the Board did not comply with UK Code provision B.6.1.

Following the 2009 Board performance evaluation, improvements were made to the provision and quality of management information to Board members. In addition, changes were made to the Board's annual strategy review process to improve its effectiveness.

Communication with shareholders

The Board regards communication with shareholders as a high priority and uses general meetings and meetings with institutional shareholders to ensure there is a mutual understanding of the Group's strategy and performance. Directors are regularly updated on shareholder and market matters at Board meetings and through the provision of analyst reports.

The Company's website provides access to information about the Company, including its results and press releases.

Corporate Governance Report continued

Governance

During the year the Group's UK regulated entities commissioned an extensive study of their governance structure using an external consultant. The scope of the study was restricted to the governance of the UK regulated entities and their committees. The study resulted in a number of recommendations that have been adopted and lessons learnt have been applied across the Group. This study has resulted in:

- ▶ The formation of joint Audit and Risk Oversight Committees to replace the previous Audit Committees, overseeing Group activities and those in the UK and Gibraltar
- ▶ The revision of the UK and Gibraltar governance structures to improve their effectiveness
- ▶ The revision and implementation of new terms of reference for the Company, its regulated entities and all their committees

The Board believes the new Group governance structure will, in future, provide for a more efficient and effective management of the Group's activities.

Board Committees

The Audit and Risk Oversight Committee

The Audit and Risk Oversight Committee (previously known as the Audit Committee) is composed of Independent Non-Executive Directors, with, in accordance with its Terms of Reference, a minimum of three such members and a maximum of seven such members. The Board is satisfied that each member is competent in financial matters and Peter Hazell, Joe MacHale and Cees Schraauwers have recent and relevant financial experience. The Chairman and Finance Director (2010)/Chief Financial Officer (2011) attend the Committee meetings by invitation. The Committee reviews the financial and internal reporting process and financial statements, the system of internal control, risk management and the external and internal audit process. The Committee meets the external auditors without management present at least once a year.

The Committee met on seven scheduled occasions (eight in total) to consider the full-year, half-year results and Interim Management Statements. In addition, it considered:

- ▶ Annual audit and interim review planning
- ▶ Monitoring the integrity of the financial statements and financial reporting processes
- ▶ The effectiveness of financial controls
- ▶ Risk management
- ▶ Internal control
- ▶ Tax and treasury planning policies
- ▶ Governance, including its own Terms of Reference
- ▶ Capital management
- ▶ Regulatory matters
- ▶ Provision of non-audit services

- ▶ Relationship with auditors and their independence
- ▶ The performance, qualifications and independence of the external auditors
- ▶ Presentations from the business regarding progress following audits and on significant ongoing projects

The Nomination Committee

The Nomination Committee is composed of independent Non-Executive Directors. The Committee reviews the structure, size and composition of the Board and recommends appointees to the Board, as well as establishing, approving and monitoring the succession plan for the Board and senior management.

The Nomination Committee met on three scheduled occasions (five in total) to consider amongst other matters:

- ▶ The search for a Non-Executive Director and Chief Financial Officer
- ▶ Board balance and Non-Executive Director independence
- ▶ Executive succession planning
- ▶ Training and development programme for directors
- ▶ Committee performance evaluation
- ▶ Review of balance of skills, knowledge and experience of the Board
- ▶ Retirement and re-election of Directors

The identification of Maarten Hulshoff as new Non-Executive Director and Scott Egan as Chief Financial Officer were two of the Committee's key activities. The Nomination Committee appointed an independent search agency to identify a further Dutch resident Non-Executive Director. The Committee evaluated the skills and requirements of the Board and developed the required profile for the new Director. The Senior Independent Director managed the selection process on behalf of the Committee in respect of the new Non-Executive Director. All Directors were given the opportunity to meet prospective candidates. As a result Maarten Hulshoff was recommended to the Board and in due course was appointed by shareholders on 17 December 2010. Maarten Hulshoff's biography may be found on page 51.

The Board and the Committee participated in the search, selection and appointment of Scott Egan as Chief Financial Officer. Scott joined the Group on 7 January 2011 following Matthew Scales stepping down as Finance Director on 20 December 2010.

Upon assessment, the Nomination Committee deemed all Non-Executive Directors who served during 2010 to be independent in accordance with the criteria detailed in the UK Code and in judgement and character.

Corporate Governance Report continued

The Remuneration Committee

The Remuneration Committee is comprised only of independent Non-Executive Directors, with a minimum requirement of two such members.

The principal responsibilities of the Committee are:

- ▶ To recommend the remuneration policy for the Executive Directors and members of the Executive Management Committee (EMC) to the Board;
- ▶ To review the design of all share incentive plans for approval by the Board and shareholders;
- ▶ To set and assess the achievement of performance conditions for share incentive schemes; and
- ▶ To determine the total remuneration package for each Executive Director and EMC member

The Chairman, Chief Executive Officer (CEO) and HR Director are usually invited to attend all or part of Committee meetings but are excluded from any discussion on their own remuneration.

Deloitte LLP (Deloitte) is the Committee's appointed independent remuneration consultants. During the year Deloitte also provided unrelated tax services to the Company, and also provided market data to the Company on Non-Executive Directors remuneration.

Committee membership and attendance at meetings

The table below sets out the membership of the Audit and Risk Oversight, Nomination and Remuneration Committees as at 31 December 2010:

Current Directors	Audit and Risk Oversight Committee	Nomination Committee	Remuneration Committee
John Barton	–	C	–
Dane Douetil	–	–	–
Peter Hazell	C	M	M
Joe MacHale	M	M	C
Cees Schrauwens	M	M	M
Willem Stevens	M	–	–
Maarten Hulshoff	–	–	–

Key: C = Chairman M= Member

All Directors of the Company invested the time required in 2010 to discharge their responsibilities and their attendance at meetings is disclosed below. Directors unable to attend a meeting provide feedback on the papers and their comments are then communicated to the meeting. All Directors must report any material change in their circumstances and potential conflict situations to the Board before any change occurs. The other commitments of the Directors are reported in their biographies on pages 50 and 51.

Directors	Board	Audit and Risk Oversight Committee	Nomination Committee	Remuneration Committee
No. of scheduled meetings held	8	7	3	5
John Barton	8	n/a	3	n/a
Ken Culley*	3	4	1	2
Dane Douetil	8	n/a	n/a	n/a
Peter Hazell	8	7	3	5
Maarten Hulshoff**	1	n/a	n/a	n/a
Joe MacHale	8	6	2	5
Matthew Scales	8	n/a	n/a	n/a
Cees Schrauwens	8	7	3	5
Michael Smith*	3	4	1	2
Willem Stevens***	7	4	n/a	n/a

Notes:

* Ken Culley and Michael Smith resigned from the Board on 6 May 2010 and the maximum number of scheduled Board meetings they could have attended was three, the maximum number of scheduled Audit and Risk Oversight Committee meetings they could have attended was four, the maximum number of scheduled Nomination Committee meetings they could have attended was one and the maximum number of scheduled Remuneration Committee meetings they could have attended was two.

** Maarten Hulshoff's appointment was effective on 17 December 2010 and the maximum number of scheduled Board meetings he could have attended was one.

*** Willem Stevens' appointment on the Audit and Risk Oversight Committee was effective on 6 May 2010 and the maximum number of scheduled Audit and Risk Oversight Committee meetings he could have attended was four.

The above table indicates the number of scheduled meetings held in the year. Further meetings were held to consider such matters as the Offer. The total number of unscheduled Board and Committee meetings held during the year was as follows:

Board: two, Audit and Risk Oversight Committee: one, Nomination Committee: two, Remuneration Committee: zero. These unscheduled Board and Committee meetings were fully attended, except for Peter Hazell who was unable to attend one Board meeting, Willem Stevens who was unable to attend one Board meeting, Joe MacHale and Michael Smith who were unable to attend the Audit and Risk Oversight Committee meeting.

Corporate Governance Report continued

Risk management

It is necessary to understand and manage the risks which may impact on the Group's performance. To ensure this is achieved in an effective manner, the Audit and Risk Oversight Committee, on behalf of the Board, oversaw the operation of the Group's Risk Management function. During the year, the Group appointed a Chief Risk Officer to assume overall control and manage the Group's risk management activities. In conjunction with other support functions the Risk Management department regularly evaluated risks facing the business and implemented plans to mitigate these risks. These plans take into account the Group's long-term strategy and immediate business objectives. In particular, risk management activities are interlinked with the Group's key performance indicators, which can be found on page 20. Regular risk management updates are presented to the Audit and Risk Oversight Committee by the Chief Risk Officer and Group Risk Manager and to the Board. The Audit and Risk Oversight Committee believes that the Group's risk management plans and processes are appropriate and effective for operation of the business. Further details are provided under 'Risk Management and Risk Factors' on page 36.

Internal control

The Board has overall responsibility for the Group's systems of internal control and for reviewing their effectiveness. However, the Board delegates responsibility for the operation review and effectiveness of the systems of internal control to executive management. Neither the Board nor its Audit and Risk Oversight Committee has made any material changes to the Group's internal control systems during the year.

The Group's system of control cover all material controls including operational, financial, risk management and compliance and are in compliance with latest UK and Dutch best practise. The internal control systems are designed to manage risk and not eliminate it and cannot be expected to provide absolute assurance against material loss, error or fraud.

The Group's system of internal control has been in place throughout 2010 and up to the date of this Report and accords with the UK Turnbull Guidance on Internal Control.

Internal Audit

Internal Audit provides independent assurance to management and the Audit and Risk Oversight Committee that major risks affecting the Group are being managed appropriately by means of a controls network, which is operating effectively. Audit and Risk Oversight Committee members had regular meetings with the Head of Internal Audit during the year to review work plans and findings. The Audit and Risk Oversight Committee approves the Internal Audit programme each year. The results of audits and opinions on controls effectiveness and operation are communicated to the relevant business unit with Internal Audit conducting follow up reviews where appropriate.

External auditors

The Group's external auditors, Ernst and Young Accountants LLP (Ernst and Young), provide an independent, supplementary perspective on the Group's internal control systems. In the course of their work they assess the Group's internal control systems relating to financial reporting and report their findings to the Audit and Risk Oversight Committee. To ensure auditor objectivity and independence there is a process in place to seek approval for any non-audit work. This requires the Chairman of the Audit and Risk Oversight Committee or Finance Director (2010)/Chief Financial Officer (2011) to approve any such work. The general meeting of shareholders appoints the external auditor. After review the Board proposes the re-appointment of Ernst and Young as the Company's auditors at the 2011 annual general meeting.

Each person who is a Director at the date of preparation of this Report confirms that:

- ▶ So far as the Director is aware, there is no relevant audit information of which the Company's auditor's are unaware; and
- ▶ He has taken all the steps that ought to have been taken in order to make himself aware of any relevant audit information and to establish the Company's Auditors are aware of that information.

Creditors payment policy

It is the policy of the Company to settle all expenses on a timely basis in the ordinary course of business. It is the Group's policy to agree appropriate terms and conditions in advance with its suppliers and to make payment in accordance with those terms and conditions, provided that the supplier has complied with them. During 2010 the Company aimed to settle invoices in an average of five days (2009: five days).

Share capital

As of 31 December 2010 the Company's authorised share capital was eight hundred twenty million Euros, divided into two hundred fifty million (250,000,000) ordinary shares of three euro and twenty eight eurocents (Euro 3.28) each. The issued share capital was 79,162,725 ordinary shares of three euro and twenty eight eurocents (Euro 3.28) each.

Major shareholders

The Company is not directly or indirectly owned or controlled by another corporation or by any other government. This will change in the event the Offer becoming wholly unconditional, which will result in a change of control.

Corporate Governance Report continued

Substantial equity investors

The Dutch Financial Supervision Act provides that any person, who acquires, directly or indirectly, or disposes of an interest in the Company's share capital or voting rights must without delay give written notice to the AFM, if, as a result of such acquisition or disposal, the percentage of capital interest or voting rights held by such person, directly or indirectly, reaches, exceeds or falls below the following thresholds: 5%, 10%, 15%, 20%, 25%, 30%, 40%, 50%, 60%, 75% and 95%.

In addition, the obligation to notify the AFM also applies when a person's direct or indirect interest in the Company's share capital or voting rights passively reaches, exceeds or falls below the above mentioned thresholds as a result of a change in the share capital or voting rights of the Company.

The following table lists the shareholders on record in the AFM register on 24 February 2011.

Shareholder	Date of disclosure	Capital interest	Voting interest
Deutsche Bank AG	24 December 2010	5,983,079	5,983,079
Halcyon Asset Management LLC	26 October 2010	5,400,000	5,400,000
UBS AG	23 December 2010	5,147,080	5,147,080
Credit Suisse Group AG	26 October 2010	4,713,053	4,713,053

General meeting of shareholders

The annual general meeting of shareholders will be held in Amsterdam (see AGM notice for full details). All Directors are expected to be in attendance at the meeting to answer any shareholders' questions. To ensure shareholders' views are reflected proportionately, all resolutions will be voted on a poll.

Further general meetings of shareholders shall be held whenever the Board deems necessary or in case one or more shareholders who jointly or severally represent at least five percent (5%) of the Company's issued capital so request the Board in writing, stating the subjects to be discussed.

General meetings of shareholders may only be held in Amsterdam, Rotterdam, The Hague and Utrecht.

During 2010 the Company held three extraordinary general meetings to change the Company's articles of association, to approve interim and final distributions, to appoint Maarten Hulshoff and to discuss the Offer in accordance with article 18 of the Dutch Public Takeover Bids. Full details, including results can be found on the Company's website.

One or more shareholders who jointly or severally represent at least one per cent of the Company's issued capital or representing a value of €50 million in market value, have the right to request to submit subjects on the agenda of a general meeting of shareholders.

The agenda for the annual general meeting shall, among other things, include the adoption of the annual accounts, the discharge of the Directors for their management of the Company and the discussion of the allocation of profits.

Each shareholder has the right to attend a general meeting to exercise their rights to attend and address a general meeting and to vote at such meeting in person, and, if so resolved by the Board, by means of electronic communication equipment. The Board may designate one or more satellite meeting places anywhere in the world where the exercise of rights to attend and address a general meeting, and to vote at such a meeting, shall be facilitated by the use of electronic communication equipment. The Board may set a record date for the entitlement to attend or vote at a certain general meeting.

Voting rights

Each share confers the right to cast one vote at a general meeting. All resolutions shall be passed by an absolute majority of the votes cast, unless required otherwise by Dutch law or the Company's articles of association. The Company's articles of association do not provide for special voting rights attached to shares in the capital of the Company.

Although the Depositary Interests themselves do not formally have voting rights, holders of Depositary Interests are in practice equated with shareholders. They can attend all of the Company's general meetings, either personally or by proxy, and also have right of speech, subject to obtaining a valid letter of representation. The holders of the Depositary Interests will then automatically, without limitation and under all circumstances, receive a voting proxy from the Depositary, managed by Computershare Investor Services PLC (CIS), to vote on the underlying shares. Under the terms of the Poll Deed, CIS is obliged to follow voting instructions of holders of Depositary Interests.

Acquisition of own shares

The Company may acquire shares or Depositary Interests in its own capital subject to the provisions of Dutch law and only following authorisation by the general meeting of shareholders. Such authorisation shall be valid for no more than 18 months and shall state the number of shares and/or Depositary Interest which may be acquired, the manner in which they may be acquired and the limits within which the acquisition price must be set.

The Board has been authorised by the shareholders to acquire such a number of shares in its own capital as permitted within the limits of law and the articles of association. This authority will expire at the conclusion of the 2011 annual general meeting of the Company or on 5 August 2011, whichever is the earlier.

Issue of additional shares and pre-emptive rights

Shares may be issued pursuant to a resolution by the general meeting of shareholders. The general meeting of shareholders may delegate this authority to the Board for a period not exceeding five years. The Board has been granted the authority to issue shares and to grant rights to subscribe for shares in the capital of the Company by resolution of the shareholders passed in the 2010 annual general meeting of shareholders. This authority will expire at the conclusion of the 2011 annual general meeting of the Company or on 5 August 2011, whichever is the earlier.

The general meeting of shareholders may resolve to restrict or exclude the pre-emptive rights or to confer this authority to the same body upon which it conferred the authority to issue shares and to grant rights to subscribe

Corporate Governance Report continued

for shares in the capital of the Company. The Board has been granted this authority by resolution of the shareholders passed in the 2010 annual general meeting of shareholders. This authority will expire at the conclusion of the 2011 annual general meeting of the Company or on 5 August 2011, whichever is the earlier.

Changes to rights of shareholders

Shareholders' rights may be changed pursuant to an amendment of the Company's articles of association, a merger or demerger as referred to in Book 2 of the Dutch Civil Code or a dissolution of the Company. A resolution of the general meeting of shareholders to dissolve the Company may only be passed with a majority of at least three quarters of the votes cast. A resolution to merge or demerge requires a majority of at least two thirds, in case less than half the issued share capital is represented at the meeting.

Articles of association

Amendments to the Company's articles of association require a resolution of the general meeting of shareholders to be passed with a majority of at least three quarters of the votes cast, except where the amendment to the articles of association concerns article 4 (authorised share capital) or article 101.1 (financial year), in which instances the resolution shall be adopted by an absolute majority of the votes cast.

The current text of the articles of association is available at the Trade Register of the Chamber of Commerce for Amsterdam and on the Company's website. The Company's articles of association have been amended twice in 2010 on 14 July 2010 and 6 December 2010. Both amendments concerned a change of the authorised share capital of the Company in view of a decrease of the nominal value of the shares in the capital of the Company.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Director's Report on pages 1 to 72. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Financial Review on pages 40 to 48. In addition, Note 4 to the financial statements includes the Group's objectives, policies and processes for managing its capital, its insurance risk management procedures, risk concentrations, reinsurance protections, aggregate exposure management and sensitivities, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit risk and liquidity risk.

The Group has sufficient financial resources together with sufficient renewing income from customers across different geographic areas and industries. As highlighted in Notes 22 and 25 to the financial statements, the Group meets its day to day working capital requirements through maintaining a proportion of its investment portfolio in cash, cash equivalents and short dated fixed income securities. The continuing economic conditions and exchange rate fluctuations create a degree of uncertainty over the exchange rate between Sterling and the US dollar and Euro and the level of capital required to support this planned premium income. As disclosed in Note 26,

the Group also has access to a three year revolving credit facility dated 9 November 2009.

The Directors believe that the Group has adequate resources to manage its business risks successfully despite the continuing uncertain economic outlook. After making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operation existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

Board support

The Company Secretariat provides advice and administrative support to the Board. All Directors have access to the advice of the Company Secretariat and procedures are in place for Directors to seek independent professional advice at the Company's expense. No such advice was sought by any Director during the year.

Corporate governance statement

This corporate governance statement concerns the statement as referred to in the Dutch Decree implementing further accounting standards for the content of annual reports (*Vaststellingsbesluit nadere voorschriften inhoud jaarverslag*) dated 23 December 2004 (as amended on 20 March 2009) (the Decree). The information required to be included in this corporate governance statement as described in articles 3, 3a and 3b of the Decree is incorporated in this Annual Report and can be found in the following sections of the Annual Report:

- The information required by article 3, paragraph 1 and paragraph 2 of the Decree, concerning compliance with the Dutch Code and the UK Code (voluntarily applied code), can be found under 'Corporate Governance Report' in this Annual Report;
- The information required by article 3a, paragraph a of the Decree, concerning the main elements of the Company's risk management and control frameworks relating to the financial reporting process, can be found under 'Risk Management and Risk Factors' in this Annual Report;
- The information required by article 3a, paragraph b of the Decree, concerning the functioning of the Company's meeting of shareholders and the authority and rights of shareholders can be found under 'Corporate Governance Report' in this Annual Report;
- The information required by article 3a, paragraph c, concerning the composition and functioning of the Board and its committees can be found under 'Corporate Governance Report' in this Annual Report;
- The information required by article 3b, concerning the inclusion of the information required by the Decree Article 10 Takeover Directive, can be found under 'Corporate Governance Report' and 'Investors' in this Annual Report.

Directors' Remuneration Report

The principal responsibilities of the Remuneration Committee are:

- ▶ To recommend the remuneration policy for the Executive Directors and members of the Executive Management Committee (EMC) to the Board
- ▶ To review the design of all share incentive plans for approval by the Board and shareholders
- ▶ To set and assess the achievement of performance conditions for share incentive schemes
- ▶ To determine the total remuneration package for each Executive Director and EMC member

The Chairman, Chief Executive Officer (CEO) and HR Director are usually invited to attend all or part of Committee meetings but are excluded from any discussion on their own remuneration.

Deloitte LLP (Deloitte) is the Committee's appointed independent remuneration consultants. During the year Deloitte also provided unrelated tax services to the Company, and also provided market data to the Company on Non-Executive Directors remuneration.

Brit Insurance Holdings N.V. is a Dutch incorporated company and therefore has no UK statutory requirement to prepare a Directors' Remuneration Report. Nevertheless, on a voluntary basis, the requirements of the UK Companies Act and Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 have been taken into account in preparing this report. The report also meets the requirements of the Listing Rules and the UK Listing Authority. In addition, the report meets the Dutch statutory disclosure requirements as set out in Title 9 of Book 2 of the Dutch Civil Code.

Remuneration policy

In summary, the Remuneration Policy adopted by the Company is as follows:

- ▶ The Group operates in personnel-orientated markets and its performance is dependent on the skill and experience of motivated employees.
- ▶ The remuneration policy aims to attract, retain and motivate high calibre executives, rewarding outstanding performance with packages that are aligned with the interests of shareholders.
- ▶ The level of Executive Directors' remuneration takes into account market practice and Executive Directors are rewarded on the basis of responsibility, competence and contribution.
- ▶ Components of these packages include salary, on which pension and other benefits are calculated, an annual bonus and long-term incentives.
- ▶ The Remuneration Committee will assess whether the reward strategies are achieving their objectives. It reviews independent market data regularly and assesses whether any adjustments to policy and practices are necessary.
- ▶ In respect of Non-Executive Directors, arrangements shall consist of a fixed fee and where appropriate this may include an additional element to reflect areas of responsibility (e.g. Chairmanship of individual Board Committees), which may be payable in the form of cash and/or shares.

The current remuneration package adopted by the Company is closely linked to the performance of the Group. Under the existing package it would be anticipated that c.60% of remuneration (excluding pensions) for Executive Directors and EMC members would be performance related.

Directors' Remuneration Report continued

Components of remuneration

The Company is currently subject to an offer by Achilles Netherlands Holdings B.V. This Remuneration Report therefore details the arrangements that applied in respect of 2010. In the event that a takeover of the Company does not occur, the Committee will review and agree arrangements for 2011 based on the corporate strategy and the needs of business over the medium and long term. In this situation it would be envisaged that for 2011, the remuneration structure would be operated on terms substantially similar to previous years.

The table below shows the principal elements of executive remuneration:

	Objective	Participation	Performance period	Performance conditions
► Base salary	To reflect the value of the individual, their role and their skills.	All employees.	Not applicable but salaries are reviewed annually.	Not applicable but salaries are determined by taking a number of factors into account including individual performance, level of experience, scope of responsibility and market benchmarks.
► Pension	To provide post-retirement remuneration.	All employees.	Not applicable	Not applicable
► Annual bonus	To reward strong performance and incentivise delivery of short-term objectives. A proportion of the annual bonus earned by senior executives may be deferred under the BSMP (see below).	All employees are eligible to be considered for a non-contractual bonus.	1 year	Achievement of Group profit and reflecting individual performance.
► Bonus Share Matching Plan (BSMP)	To encourage executives to invest in Brit Insurance shares and incentivise generation of strong Return on Equity.	Generally targeted at senior executives.	3 years	Subject to Return on Equity performance.
► Performance Share Plan (PSP)	To encourage a share ownership culture and to incentivise generation of (i) long-term shareholder returns; and (ii) strong Return on Equity.	Generally targeted at senior executives.	3 years	One half subject to the achievement of Total Shareholder Return ('TSR') conditions using a sector based comparator group. One half subject to Return on Equity performance.
► All employee share rewards	To develop wider share ownership amongst employees to align their interests with those of shareholders. Since 2010, the Company operates the Brit Insurance Holdings N.V. Savings Related Share Option Scheme. Previously the Company operated the HMRC approved Brit Employee Share Ownership Plan 2001 ('ESOP').	All employees are eligible to participate subject to a minimum employment period.	Not applicable	Not applicable

Directors' Remuneration Report continued

Base salary

Base salaries are reviewed annually and take into account the individual's responsibilities, skills and experience and are set against a benchmark determined by reference to other insurance companies and FTSE 250 organisations. Any changes are usually effective from 1 April each year.

The Chief Executive Officer has been awarded a salary increase of 3.5%. Given that the Chief Executive Officer's salary has remained unchanged since April 2008, the Committee felt that the increase was appropriate.

The table below sets out his revised salary.

	Base salary from 1 April 2011
D J Douetil	£530,000

Matthew Scales left the Company in December 2010. His salary for the period 1 January 2010 to 13 November 2010 was £345,000. On 14 November 2010 Matthew returned his company car and his salary was subsequently increased by £15,674 to £360,674 until his departure.

Annual bonuses

In 2010, all Group employees were eligible to participate within the Group's annual bonus scheme. The scheme aims to reinforce the relationship between individual and Group performance and reward. For the most senior executives within the Company, including Executive Directors and EMC members, bonuses are primarily dependent on profit which funds a bonus pool.

For Executive Directors and other senior executives, allocations are based on personal performance and contribution to the Group's performance and achievements during the year. The Chairman sets the CEO's objectives and reviews his performance against objectives following the year-end. The Committee then determines the bonus payable to the CEO. The CEO makes recommendations to the Committee regarding the performance of the other Executive Management team against their objectives and the Committee considers these recommendations when setting their bonuses.

Given the potential interest from Achilles, in the summer of 2010 the Committee considered the bonus performance measures for the Chief Executive Officer in order to ensure ongoing alignment with Shareholder interests. The Committee determined that in the event the bid was recommended by the Board and the acquisition was successful, CEO's bonus for 2010 would be based on the aggregate consideration received from Achilles over and above a threshold level. If the acquisition were to be unsuccessful, the bonus amount would be determined on the normal basis as outlined above. On the basis that the deal is declared wholly unconditional, the Board agreed the bonus that would become payable would be £701,000, reflecting the value delivered to shareholders.

As indicated in last year's report, bonuses may exceed 100% of salary for superior levels of performance. Although there is no formal cap, it is extremely unlikely that bonuses will exceed 200% of salary, even in exceptional circumstances. The Committee believe that this structure will appropriately incentivise participants and ensures that the Company remains in line with market practice in the sector.

Long-term incentives

Executive Directors are eligible for annual long-term incentive awards along with senior employees. The awards are designed to attract and retain talented employees and have stretching performance conditions that aim to encourage participants to work for the long-term benefit of the Group. The Company currently grants awards under two discretionary share incentive schemes, the BSMP and the PSP. Details of the performance conditions attaching to the outstanding awards of each Director are summarised below. Deloitte provides the information on the extent to which the TSR performance conditions are met and the Committee review this alongside the ROE performance to determine the extent to which the award will vest in accordance with the terms of the Performance Condition.

All permanent employees of the Group (subject to a minimum service requirement) are now able to participate in the Brit Insurance Holdings N.V. Savings Related Share Option Scheme. This includes Executive Directors. In previous years the employees were previously eligible to join the ESOP, which has now ceased.

As noted above, in light of the offer from Achilles, it was not appropriate for the Committee to consider the structure of long term incentive awards for 2011. As such, the section below sets out details of awards made in 2010 only. In the event of a successful takeover of the Company, the Committee will treat all outstanding awards in accordance with the rules of the plans and any vesting would suitably reflect both time since grant and performance achieved.

BSMP

Participation in the BSMP is restricted to the most senior executives.

Under the BSMP an individual may choose to receive up to 50% of their post-tax annual bonus in the form of ordinary shares (Investment Shares). The Company may then grant Matching Awards over shares with a market value worth up to three times the pre-tax value of the Investment Shares. Matching Awards may vest on the third anniversary of grant subject to the achievement of a sliding scale of average annual Return on Equity (ROE) targets as follows:

The performance targets for 2010 awards were:

Average annual ROE during the Performance Period	Portion of matching award subject to the ROE condition that will vest
Equal to 10%	One-sixth
Between 10% and 20%	Between one-sixth and the whole award vesting on a straight-line basis
Equal to or greater than 20%	The whole award

Any part of an award that does not vest at the end of the Performance Period will lapse and cannot be retested.

Directors' Remuneration Report continued

PSP

Under the PSP, awards may be granted each year over shares with a value of up to 100% of basic salary (or 200% of salary in exceptional circumstances). The vesting of awards is determined by the extent to which Performance Conditions are satisfied over a three-year Performance Period.

The ROE targets for awards granted in 2010 were as follows:

Average annual ROE during the Performance Period	Percentage of one half of the total number of shares subject to the award that will vest
Equal to 10%	20%
Between 10% and 20%	Pro-rata on a straight-line basis between 20% and 100%
Equal to or greater than 20%	100%

The other half of an award is subject to the Company's Total Shareholder Return (TSR) against a bespoke industry comparator group chosen as a representative peer group against which the Company's performance can be measured. The portion of the award subject to the TSR performance condition will vest as follows:

Position at which the Company is ranked against the comparator group at the end of the Performance Period	Percentage of one half of the total number of shares subject to the award that vests
Below median	0%
Median	20%
Between median and upper quartile	Between 20% and 100% (interpolated based on Brit Insurance's TSR relative to the TSR of the companies ranked above and below Brit Insurance)
Upper quartile	100%

Any part of an award that does not vest at the end of the Performance Period will lapse and cannot be retested.

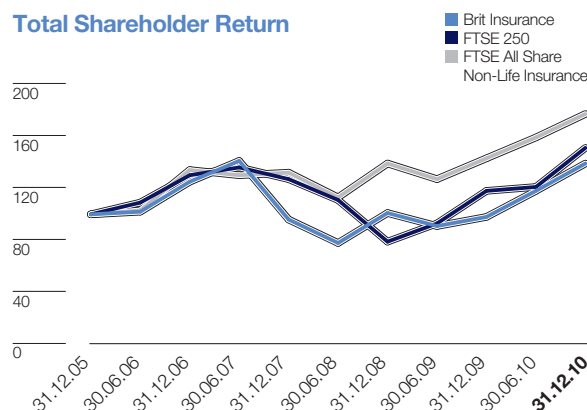
The current comparator group for awards since 2007 comprises:

- ▶ Amlin plc
- ▶ Beazley plc
- ▶ Catlin Group Limited
- ▶ Chaucer Holdings PLC
- ▶ Hardy Underwriting Bermuda Limited
- ▶ Hiscox Limited
- ▶ Novae Group plc

Performance graph

The following graph illustrates the total shareholder return performance of Brit Insurance against (i) the FTSE Mid 250 Index and (ii) the FTSE All Share Non-Life Insurance Sector, over the past five years to indicate performance against the broader market and industry comparators. Performance by TSR represents growth plus reinvested dividends.

Total Shareholder Return



Options and awards outstanding

As at 31 December 2010, there were a total of 3,953,572 options outstanding under all executive option schemes, and the employee share participation trust held 1,122,667 shares. The Executive Directors are deemed to have an interest in the shares held in the employee benefit trust. If all outstanding awards in excess of the shares held in trust were satisfied by the issue of ordinary shares, potential dilution would be 3.6% of the issued share capital of the Company (excluding Treasury Shares). The current intention of the Company is to use a combination of new issue and shares held in the employee share participation trust in order to satisfy any vested awards.

Share ownership guidelines

Executive Directors and EMC members are expected to build up their holding in Brit Insurance ordinary shares to 100% of salary within five years of the introduction of the BSMP (2007) or later date of appointment through their own investment and the retention of all the vested BSMP shares (other than those sold to cover any income tax and national insurance liability) until they have reached the target.

The current shareholdings of Executive Directors are set out on page 64.

Fees of the Chairman and Non-Executive Directors

The Company Chairman and Chief Executive set the fees of the Non-Executive Directors and review their fees annually. Any change in fees is effective from 1 April each year. Non-Executive Directors are not entitled to participate in any of the Group's short and long-term incentive and pension arrangements. Fees are not set by reference to the number of meetings held.

Non-Executive Directors receive a basic fee and additional fees for chairmanship of the Audit, Remuneration and Nomination Committees and for the duties associated with the Senior Independent Director role. Non-Executive Directors do not receive any additional fees for membership of individual Board Committees. The Chairman receives an all-inclusive fee for his role.

Directors' Remuneration Report continued

Since 1 April 2008, the fees paid to Non-Executive Directors are as follows:

Role	Fee per annum (£)
Chairman	£175,000
Non-Executive Director	£55,000
Nomination or Remuneration Committees Chairman	£12,000
Audit Committee Chairman	£18,000
Senior Independent Director	£18,000

Non-Executive Directors serving on the Board of Brit Insurance Limited and Brit Syndicates Limited are paid an additional fee of £12,000 per annum.

The fees were not increased during 2010.

Directors' Remuneration

Emoluments and compensation

	Fees & salaries £'000	Benefits in kind £'000	Bonus* £'000	Pension £'000	Other £'000	12 months ended 31 December 2010 Total £'000	12 months ended 31 December 2009 Total £'000
John Barton	175	–	–	–	–	175	175
Kenneth Culley	73	–	–	–	–	73	66
Dane Douetil	512	2	701	128	–	1,343	969
Peter Hazell	74	–	–	–	–	74	73
Joe MacHale	67	–	–	–	–	67	67
Matthew Scales	349	18	–	86	600**	1,053	628
Cees Schrauwers	86	–	–	–	–	86	86
Michael Smith	23	–	–	–	–	23	67
Willem Stevens	55	–	–	–	–	55	0
Maarten Hulshoff	2	–	–	–	–	2	–
Total for the year	1,416	20	701	214	600	2,951	2,286

* Bonuses are based on Company targets and individual performance.

** In accordance with the terms of his service contract and the obligations entered into by Mr Scales at the request of the Company.

Executive Directors are offered a number of benefits namely private medical insurance, permanent health insurance and life assurance. Matthew Scales who left the Company on 31 December 2010 had a company car until November 2010. All Executive Directors have a death in service benefit which is subject to the terms and conditions of the insurer.

Share-based incentives

In all instances the details of share options and share awards shown below reflect the position following the share consolidation approved by shareholders on 25 February 2010.

Share options

Directors had the following interests in share options in the Company at 31 December 2010:

	Scheme	1 January 2010	No. options granted in year	No. options exercised in year	No. options lapsed in year	31 December 2010	Exercise price	Exercisable from	Expiry date	Market price at 31 December 2010
Dane Douetil	A	17,250	–	–	–	17,250	942.00p	18/10/07	17/10/14	1042.00p
	B	–	1,488	–	–	1,488	609.60p	01/06/13	01/12/13	1042.00p
	Total	17,250	1,488			18,738				
Matthew Scales	A	15,923	–	–	–	15,923	942.00p	18/10/07	17/10/14	1042.00p
	B	–	1,488	–	–	1,488	609.60p	01/06/13	01/12/13	1042.00p
	Total	15,923	1,488			17,411				

A Options granted to Directors under the ESOS.

B Options granted to Directors under the Savings Related Share Option Scheme.

Directors' Remuneration Report continued

Share awards

Directors had the following interests in awards over shares in the Company at 31 December 2010:

	Scheme	Performance period ending	Award date	Share price on award date	1 January 2010	Awarded	Exercised	Lapsed	31 December 2010	Value vested 2010	Vesting date	Expiry date
Dane Douetil												
	C	2012	24/03/2010	762.50p	–	62,950	–	–	62,950	–	24/03/2013	23/09/2013
	C	2011	05/08/2009	780.00p	1,844	–	–	–	1,844	–	05/08/2012	04/02/2013
	C	2011	26/06/2009	740.00p	50,260	–	–	–	50,260	–	26/06/2012	25/12/2012
	C	2010	09/04/2008	1,040.04p	62,997	–	–	–	62,997	–	09/04/2011	08/10/2011
	C	2009	31/05/2007	1,387.00p	41,115	–	41,115	–	–	£306,307	–	–
	D	2012	10/03/2010	747.00p	–	51,405	–	–	51,405	–	10/03/2013	09/09/2013
	D	2011	05/08/2009	780.00p	234	–	–	–	234	–	05/08/2012	04/02/2013
	D	2011	26/06/2009	740.00p	41,871	–	–	–	41,871	–	26/06/2012	25/12/2012
	D	2010	10/03/2008	864.00p	30,525	–	–	–	30,525	–	10/03/2011	09/09/2011
	D	2009	16/10/2007	1,338.20p	35,709	–	17,854	17,855	–	£133,036	–	–
Total					264,555	114,355	58,969	17,855	302,086			
Matthew Scales												
	C	2012	24/03/2010	762.50p	–	37,343	–	–	37,343	–	24/03/2013	23/09/2013
	C	2011	26/06/2009	740.00p	35,287	–	–	–	35,287	–	26/06/2012	25/12/2012
	C	2010	09/04/2008	1,040.04p	40,305	–	–	–	40,305	–	09/04/2011	08/10/2011
	C	2009	31/05/2007	1,387.00p	17,385	–	17,385	–	–	£129,541	–	–
	D	2012	10/03/2010	747.00p	–	34,638	–	–	34,638	–	10/03/2013	09/09/2013
	D	2011	26/06/2009	740.00p	28,214	–	–	–	28,214	–	26/06/2012	25/12/2012
	D	2010	10/03/2008	864.00p	20,678	–	–	–	20,678	–	10/03/2011	09/09/2011
	D	2009	16/10/2007	1,338.20p	24,190	–	12,095	12,095	–	£90,123	–	–
Total					166,059	71,981	29,480	12,095	196,465			

C Awards granted to Directors under the BSMP.
D Awards granted to Directors under the PSP.

As at 31 December 2010 there were no outstanding vested and exercisable awards under the BSMP or PSP.

The share price at 31 December 2010 was 1042.0p (31 December 2009: 788.4p). The highest and lowest closing prices during the financial year were 1045.0p and 728.0p respectively.

Brit Employee Share Ownership Plan (ESOP)

The ESOP was available to all Group employees. The Plan was not operated in 2010. The Directors' interests in the ESOP at 31 December 2010 are below:

	1 January 2010	31 December 2010
Dane Douetil	2,440	2,440
Matthew Scales	2,440	2,440

As at 31 December 2010, the ESOP trust held 344,389 shares.

Interests in Shares

The interests of Directors in the Shares of the Company during 31 December 2010, including BSMP Investment Shares, were as follows:

	1 January 2010	31 December 2010*
John Barton	17,500	17,500
Ken Culley	5,853	7,500
Dane Douetil	157,878	204,943
Joe MacHale	15,000	15,000
Matthew Scales	67,622	92,299
Cees Schrauwers	2,916	16,916
Michael Smith	2,500	2,500
Willem Stevens	–	–
Maarten Hulshoff	–	–
Peter Hazell	–	–

*or earlier retirement date.

No Director's interest in the share capital of the Company has changed between 31 December 2010 and 24 February 2011.

Directors' Remuneration Report continued

Directors' pension benefits

No Director who held office during 2010 was a member of a defined benefit pension scheme.

Dane Douetil has a personal pension, into which the Group makes contributions as detailed in the emoluments and the compensation table above. Matthew Scales was a member of the Brit Insurance Limited Retirement Benefits Scheme (BIL Scheme) and the defined contribution Brit Group Services Limited Group Personal Pension Plan (GPPP). The Chairman and Non-Executive Directors do not have any pension benefits.

External appointments

Dane Douetil is a member of the ABI Board. Any fees receivable in respect of this directorship is paid directly to the Group and are not passed on to the Director.

Service contracts

Copies of the Executive Directors' service contracts and Chairman and Non-Executive Directors' letters of appointment are available for inspection at the registered office of the Company. The Committee's policy on the length of notice periods is that they should be set so as to reflect appropriately the interests of the Company and the Executive Director, while also reflecting best practice. Consequently, the Executive Directors have notice periods of twelve months, which can be given by either party.

In the event of early termination, when determining the amount of compensation that is paid, the Committee will take into account the departing Executive Director's duty to mitigate his loss. Compensation payments will be based on 12 months' basic salary and benefits.

Subject to prior consent by the Company, Executive Directors may be permitted to accept appointments on external boards or committees provided these are not deemed to interfere with the business of the Group. Any fees received in respect of these appointments are remitted to the Group and any such fees are reflected in the remuneration package of the individual Director concerned.

Matthew Scales stepped down from the Board and ceased employment with the Company in December 2010. In accordance with the terms of his service contract as outlined above, he received an amount equivalent to 12 months' basic salary in lieu of his notice period as well as other contractual benefits. A payment was also made to reflect the obligations agreed by Mr Scales, as requested by the Company. It is expected that Mr Scales will be treated as a good leaver for the purpose of his outstanding share awards, and awards shall vest in due course, in accordance with the plan rules and taking into account time pro-rating and performance.

Chairman and Non-Executive Directors

The Non-Executive Directors have letters of appointment with the Company for an initial three year term and provide for a notice period of three months but with no provision for compensation for loss of office save for John Barton whose contract was renewed with effect from 31 December 2010 for a further term of three year to 31 December 2013 with no provision for compensation for loss of office. The date of appointment to the Board and the date of the last re-appointment at an AGM for each Non-Executive Director on the Board at 31 December 2010 is shown below:

Name	Date of appointment to the Board	Date of last re-appointment at an AGM
John Barton	28 October 2009*	n/a
Peter Hazell	21 December 2009*	6 May 2010
Maarten Hulshoff	17 December 2010	n/a
Joe MacHale	21 December 2009*	n/a
Cees Schrauwers	28 October 2009*	n/a
Willem Stevens	21 December 2009	n/a

* These directors were on the board of Brit Insurance Holdings PLC prior to the restructuring in November 2009.

Approved by the Board and signed on its behalf by

Joe MacHale

Chairman of the Remuneration Committee
24 February 2011

Directors' Responsibility Statement

The members of the Board as required by section 5:25c, paragraph 2, under c of the Dutch Act on Financial Supervision (Wet of het Financieel Toezicht) confirm that to the best of their knowledge

- ▶ These 2010 financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- ▶ This Annual Report gives a true and fair view of the Company's position and the undertakings included in the consolidation taken as a whole as of 31 December 2010 and of the development and performance of the business for the financial year then ended;
- ▶ This Annual Report includes a description of the principal risks and uncertainties that the Company faces.

This Annual Report and the 2010 financial statements, audited by Ernst and Young Accountants LLP, have been presented to the Board. The 2010 financial statements and the external auditor's report relating to the audit of the 2010 financial statements were discussed with the Audit and Risk Oversight Committee in the presence of the Executive Board and the external auditor. The Board recommends that the General Meeting of Shareholders adopts the 2010 financial statements included in this Annual Report.

All members of the Board have signed a copy of the Annual Report pursuant to their obligations under section 2, article 101, paragraph 2 of the Dutch Civil Code.

Amsterdam
24 February 2011

Robert John Orr Barton

Dane Jonathan Douetil

Joseph Patrick MacHale

Peter Frank Hazell

Maarten Joannes Hulshoff

Cornelis Antonius Carolus Maria Schrauwers

Willem Frans Casimir Stevens

Sustainability

Introduction

Whilst the main focus of the Group is to generate value for its investors, that value must be sustainable and aligned to the interests of the Group. Brit Insurance seeks both to make a positive contribution to society and to be aware of the long-term consequences of its actions.

The responsibility to build a sustainable business means recognising and respecting the connections between customers, investors, business partners, the marketplace, the workplace, the environment and society at large. Sustainability means the Group seeks to generate new commercial opportunities by developing stronger stakeholder relationships and by recruiting and retaining a highly skilled, engaged and motivated workforce.

Brit Insurance in the marketplace

The Group's strategy focuses on developing a successful and recognisable brand among intermediaries and potential customers wherever it trades internationally. The core elements of brand development include specific sponsorships, promotional campaigns and expert editorial contributions in key publications. Of these, sponsorships in cricket and design make up the largest components.

Cricket

There is a good match between the characteristics of cricket followers and the key audience of insurance buyers and intermediaries. Cricket also creates excellent all-round media coverage.

With effect from January 2010 Brit Insurance became the principal sponsor of the England cricket teams, with Brit Insurance branding on all playing and training kit. During the year, the Men's team enjoyed an unbeaten run, most notably winning the ICC Twenty20 World Championship and the Ashes in Australia for the first time in 24 years. With extensive broadcast and print media coverage of the teams' matches, awareness of the Group has increased significantly among target audiences.

The Group's successful seven-year sponsorship of Surrey County Cricket Club and the Brit Insurance Oval, which were the original platforms that took the Group into cricket sponsorship, came to an end in December 2010.

The Design Museum

In January 2008 the Group entered into a four-year partnership with the Design Museum, the world's foremost museum devoted to contemporary design. The partnership involves title sponsorship of the Brit Insurance Design Awards, and a supporting exhibition, the Brit Insurance Designs of the Year. These celebrate the most innovative and progressive international design over the previous 12 months and span the seven major design disciplines: Architecture, Graphics, Fashion, Product, Furniture, Interactive and Transport.

In 2010 the Awards continued to increase the visibility of Brit Insurance in the media and with key associated audiences, in particular breaking through into mainstream broadcast on BBC2's Culture Show and Radio 4's Today programme. The winner in 2010, Min Kyu Choi's folding three pin plug, has gone from prototype to production and confirms the importance of good design in our everyday lives.

Society – charitable giving and community involvement

The Group is committed to supporting the local communities in which it operates. Its strategy is to select charitable giving and community projects based on three criteria:

- ▶ Projects should be for a good cause and operate in an area relevant to Brit Insurance
- ▶ Financial involvement should be capable of being leveraged for the benefit of the good cause, such as sponsored charity cricket matches
- ▶ Projects should offer alignment with the Group's vision

Brit Insurance's main aims in 2010 were to:

- ▶ Support the multi-year partnership with Chance to Shine and the community activities of Brit Insurance's sponsorship partners: Surrey County Cricket Club, the Design Museum, Lloyd's Community Programme
- ▶ Match money raised by staff for their chosen charities

The Group promotes staff involvement by matching the charitable fund raising activities of its employees and by operating an employee volunteering scheme. This grants every employee two additional days of paid leave a year to volunteer their time through schemes offered by charity partners.

Sustainability continued

Chance to Shine

In 2010, the Group entered a long term partnership with Chance to Shine: an initiative run by the Cricket Foundation. This programme works with state schools, reaching into classrooms by linking into the national curriculum and delivering cricket skills. The programme draws together people from all cultures and backgrounds and gives children including those with special educational needs the chance to acquire important skills, values and attitudes.

Our existing global profile and involvement in the game supported the logic of choosing a partnership that uses cricket as the catalyst to make a positive difference in our local communities.

In 2010, our funding contributed to the programme having a significant positive impact on the lives of children across England and Wales. During the year through Chance to Shine cricket was delivered to 2,507 primary schools, 554 secondary schools and 156 special needs schools, with 345,356 children benefiting.

Lloyd's Community Programme

A day of play at the Brit Insurance Oval was again donated to the Lloyd's Community Programme to enable 190 children from Tower Hamlets to enjoy cricket coaching and a tournament.

Design Museum

During 2010 the Group supported a number of educational programmes at the Design Museum which drew on the Brit Insurance Designs of the Year 2010. This included the Design Museum's Design Factory project for students in Higher Education, Family Workshops and the Discover Design online resource. Our funding of the Design Factory allowed 314 undergraduate students from 17 different educational establishments to enter the competition which is aligned with the Brit Insurance Design Awards. In addition, a total of 95 children benefited from the family workshops and the Discover Design online resource received 13,000 hits during the year.

Political donations

No donations were made to any political organisation during 2010 (2009: nil).

The environment

Brit Insurance is committed to managing and reducing its environmental impact in a cost effective and responsible way. During 2010, employees' individual waste bins were replaced with larger, centrally located bins with improved waste sorting. As a result our capacity to recycle materials has increased substantially. Timers have also been installed on all TVs and lights to minimise our energy consumption.

'FTSE4GOOD'

During 2010, Brit Insurance was independently assessed and again satisfied the requirements of the 'FTSE4Good Index Series'. Created by the global index company FTSE Group, FTSE4Good is an equity index series designed to facilitate investment in companies that meet globally recognised corporate responsibility standards. Companies selected have to meet stringent social, ethical and environmental criteria and are positioned to capitalise on the benefits of responsible business practice.

Distributors, partners and suppliers

The Group distributes its products through a carefully selected group of brokers and intermediaries. These relationships are managed by each of the strategic business units, working together where appropriate, to ensure that development and performance objectives are met. This approach helps to ensure that the needs of the ultimate customer are consistently met, enabling the Group to achieve sustainable and profitable growth.

Commercial Services seeks to establish professional third party agreements that recognise and value the contribution made by Group suppliers. Commercial Services is also involved in all major purchasing and contract decisions to ensure positive supplier relationship management throughout the life of the contract. Brit Insurance seeks to pay all valid supplier invoices in a timely manner. Brit Insurance also complies with The Late Payment of Commercial Debts (Interest) Act 1998. A copy of the regulations can be obtained from www.opsi.gov.uk

Sustainability continued

Customers

The Group's customer service objective focuses on delivering sustainable value through

- ▶ Providing efficient claims management and funds settlement
- ▶ Delivering a quality range of products tailored to customers' business risks
- ▶ Challenging and improving service standards for each major process and business unit
- ▶ Regularly re-evaluating processes to promote an efficient and customer friendly operational environment
- ▶ Facilitating ease of access to key decision makers

The Group embraces fully the FSA's 'Treating Customers Fairly' principle to assist in achieving these objectives.

Complaint handling

Developments in 2010

In 2010, the Financial Services Authority required all insurers with more than 500 regulated complaints in a six month period to publish complaints data. Brit Insurance receives fewer than this and is therefore not required to publish these figures.

Performance

Brit Insurance tracks and monitors customer treatment using the number of complaints escalated to the Financial Ombudsman Service and the outcome of those referrals.

The Group also monitors the proportion of complaints that are resolved informally without the need for a formal complaint investigation. During 2010, 29% of all complaints logged were resolved in this way (2009: 30%). This demonstrates that staff are keen to help customers resolve matters and is a more economical way of resolving issues that might otherwise escalate to formal complaints.

The number of formal complaints has increased between 2009 and 2010 as a result of growth in Domestic Emergency business. Of the formal complaints logged in 2010, 256 (32%) were for Domestic Emergency – in 2009 only 94 were logged.

In 2010 797 formal complaints were received (2009: 658) of which 11% have been escalated to the Financial Ombudsman Service. Of the Brit Insurance cases reviewed by the Financial Ombudsman Service in 2010, 31% were subject to some change in outcome.

People

Culture and environment

Brit Insurance is committed to creating a demanding yet rewarding environment that encourages individuals to outperform. The Group aspires to be the insurer that is best able to attract, train and retain talented people. Achieving this is fundamental to the Group's financial and operational objectives and strategy. The newly implemented 'Achievement Culture' and 'Average to Outperform' programme is pivotal to ensuring successful delivery of the Group's objectives,

The Achievement Culture encourages individuals to outperform across four areas:

- ▶ Living our distinctive ethos
- ▶ Delivering on commitments and ensuring the same from others
- ▶ Managing risk actively to optimise rewards
- ▶ Focusing efforts to maximize results

HR initiatives in 2010 have focused on embedding this culture.

Headcount

The total headcount of the Group in 2010 increased marginally to 746 (2009: 741).

Employees by activity

	As at 31 December 2010		As at 31 December 2009	
	No.	%	No.	%
Underwriting	295	39.5	297	40.1
Claims	109	14.6	101	13.6
Operations and IT	177	23.7	190	25.6
Finance and Actuarial	78	10.5	91	12.3
Other	87	11.7	62	8.4
Total	746	100.0	741	100.0

The above figures exclude Non-Executive Directors (2010: six; 2009: seven).

Sustainability continued

Staff retention

The 2010 staff turnover rate excluding retirements and redundancies was 11.6% (2009: 8.2%), compared with the national average of 13.5% for 2009. At 31 December 2010, 35% (2009: 23%) of staff had completed at least five years' service and 10% (2009: 9%) had served at least ten years.

The Sunday Times 'Best Companies to Work For' survey

In 2010 Brit Insurance was again awarded a 'one to watch' accreditation in The Sunday Times 'Best Companies to Work For' survey. The data from the survey provided valuable insight into the Group and how it compares to other companies. Employee focus groups have been established to examine further the key issues identified.

Policies

The Group's policies on recruitment, learning and development and reward are continuously reviewed. They are designed to evolve whilst maintaining the objective of attracting and retaining high calibre personnel and supporting the 'Average to Outperform' Programme.

The Group considers itself an equal opportunities employer with policies and procedures that are free from discrimination in relation to all employment matters. The Group does not discriminate against current or prospective employees because of any disability. Should any employee become disabled, Brit Insurance works with the individual and provides specialised training where necessary to enable their employment within the Group to continue.

Brit Insurance's employee handbooks explain the systems and procedures that all individuals must follow in their relevant location. A copy is provided to all employees when they join the Group.

The Group is pleased to consider applications for flexible working from eligible staff with children aged under 17, disabled children under 18 or dependants over 18 for whom the employee is the main carer. Others may work from home where this is appropriate to their role and the needs of the business.

All employees are expected to treat each other with dignity and respect. Any form of harassment or bullying will not be tolerated and staff are encouraged to report any such occurrences to management.

The Group provides a healthy and safe working environment ensuring, insofar as is reasonably practicable, any machinery, systems or equipment provided for the use of employees is safe in its operations and that maintenance methods do not present a risk to health and safety.

Staff are encouraged to speak up on any unlawful or unethical activities and behaviour in the business. This is in accordance with policies on whistle-blowing, ethics and conflicts of interest. Brit Insurance also has an employee assistance programme whereby individuals can contact independent counsellors and other specialist advisers via a 24-hour helpline.

Management, leadership and development programmes

During 2010 Brit Insurance continued to operate a three-tier management development programme which identified a pool of talented leaders to meet future business challenges and maintain Brit Insurance's competitive edge. The 'Executive Development Programme' assists senior managers to develop as leaders and enhance their expertise and personal performance in the pursuit of excellence. The programme involves in-depth assessment, a tailored development plan and executive coaching. The 'Accelerated Leadership Programme' helps grow future leaders and involves self assessment, a development centre and a leadership event, culminating in a tailored development plan. The 'Manager's Toolkit' builds the skills of managers, enabling them to manage effectively their teams.

The management, learning and development programmes identify and develop the next generation of leaders and embed a consistent approach to management across the Group.

In 2011 management development programmes will be aligned to the 'Achievement Culture' and support the 'Average to Outperform' Programme.

Rewards and incentives

The reward structure provides a competitive package which includes incentive schemes, non-contractual bonus, health insurance and pension arrangements. These are regularly reviewed to ensure that they continue to attract, retain and motivate whilst supporting the Group's objectives and values.

Information relating to staff numbers and costs are included in Note 11 to the Financial Statements.

Employee involvement and communication

Brit Insurance encourages employee involvement and feedback is sought on all aspects of how the Group works. Consultation methods used include the intranet, employee surveys, briefings, electronic newsletters and lunches attended by Directors, members of the Executive Management Committee for the Group's UK operations and selected staff. These methods foster the development of a common awareness of the financial and strategic factors affecting business performance.

Investors

Over the last year Brit Insurance maintained its commitment to communicating with and understanding the needs of current and potential investors. The Group has had an ongoing programme of dialogue and meetings between senior management (including the Executive Directors) and institutional investors, fund managers and analysts. The investment community has been encouraged to interact with the Chairman and Non-Executive Directors. Reports and market feedback have been regularly circulated to the Board, enabling any issues to be addressed as well as providing investor views on strategic direction.

	Year ended 31 December 2010	Year ended 31 December 2009
Number of investor/analyst meetings	94	141

In the first half of the year the number of shareholder meetings remained high and roadshows were carried out in London, Edinburgh, Canada and the United States. Following the initial confirmation in June 2010 that a potential offer had been made for the Group, restrictions were placed on investor relations activity. This led to the overall decrease in the number of meetings during the year.

During 2010 management presented at three investor conferences giving exposure to numerous investors. A number of site visits were also arranged for the buy and sell side at locations including Lloyd's and Simply Business (previously known as Xbridge).

In addition to the regular presentations that follow financial results announcements the Group held its sixth 'Analysts' Event' in July 2010. Hosted at the Brit Insurance Oval, analysts had the opportunity to meet senior management and underwriters from across the Group.

Analyst coverage

The Group is aware of 17 analysts who have published notes on Brit Insurance during 2010 (2009: 20) and the Group provides the names of analysts and their firms on its website.

Share consolidation

On 25 February 2010 shareholder approval was given to consolidate the shares of Brit Insurance Holdings N.V. on the basis of one share for each four shares held.

Listing

The principal trading market for the ordinary shares (which are traded in the form of depositary interests (DIs)) is the London Stock Exchange, on which 113,699,129 ordinary shares/DIs were traded during 2010 (2009: 77,177,894 adjusted for 1 for 4 share consolidation). At 31 December 2010, the Group had a market capitalisation of £824.9m (2009: £618.8m) and a 0.352% weighting in the FTSE 250 (2009: 0.327%).

Distribution of equity investors

31 December 2010	Number of holders	% of total	Number of DIs ¹	% of total
Up to 1,000 shares	1,540	69.4	537,473	0.7
1,001 – 10,000	420	18.9	1,231,664	1.6
10,001 – 100,000	177	8.0	5,983,140	7.5
100,001 – 1,000,000	61	2.8	21,060,588	26.6
1,000,001 and over	20	0.9	50,349,860	63.6
Total	2,218	100.0	79,162,725	100.0

¹ Each DI represents one share in Brit Insurance Holdings N.V.
Source: Computershare

Analysis of equity investors by type

	31 December 2010 %	31 December 2009 %
Mutual funds	26.3	46.0
Pension schemes	7.4	15.5
Retail sector	5.0	5.6
Insurance sector	3.5	4.5
Other	57.8	28.4
Total	100.0	100.0

Source: JP Morgan Cazenove

The number of shares held by 'Other' increased during the year as a result of the recommended cash offer from Achilles Netherlands Holdings B.V.

Analysis of equity investors by geography

	31 December 2010 %	31 December 2009 %
United Kingdom	45.7	51.1
North America	38.6	33.9
Europe (excluding UK)	7.6	4.8
Miscellaneous	7.8	9.8
Asia/Oceania	0.3	0.4
Total	100.0	100.0

Source: JP Morgan Cazenove

Investors continued

Substantial equity investors

At 24 February 2010 the Directors had been advised of the following interests in 3% or more in the Company's issued share capital:

Holders of DIs

	Number of DIs ¹	% of issued share capital
Deutsche Bank AG	5,983,079	7.6%
Halcyon Asset Management LLC	5,618,397	7.1%
UBS AG	5,147,080	6.5%
Credit Suisse Group AG	4,713,053	6.0%
Jupiter Asset Management Limited	4,530,729	5.7%
Dimensional Fund Advisors Ltd	4,166,751	5.3%
Gruss Asset Management LLP	3,855,487	4.9%
Artisan Partners Limited Partnership	3,662,450	4.6%
Mediobanca S.p.A.	3,200,000	4.0%
LSV Asset Management	3,118,735	3.9%
Legal and General Investment Management Ltd	3,066,602	3.9%
Centaurus Capital Limited	2,494,219	3.2%

¹ Each DI represents one share in Brit Insurance Holdings N.V.

Source: Disclosures to Brit Insurance under Disclosure and Transparency Rule 5 and Rule 8.3 announcements

Investor return statistics

Cumulative total investor returns to 31 December 2010, assuming reinvestment of distributions, were as follows:

Period

	Brit Insurance %	FTSE Insurance Index (non-life) %	FTSE 250 %
1 year	41.9	23.2	27.4
3 years	45.7	35.8	18.7
5 years	39.4	77.0	50.7

Source: JP Morgan Cazenove

During the 12 months ended 31 December 2010, the Group's total investor return on the basis of the calculation set out above was comprised entirely of capital gain with distributions in the form of return of capital contributing 8.2% (2009: 6.8% yield and 10.0% capital loss).

During 2010 the share price reached a high of 1045p on 26 October and a low of 728p on 8 June.

Distributions

At the time of the Group reorganisation in December 2009, it was announced that for an initial period the Group would make distributions to shareholders by way of reductions of the par value of Brit Insurance Holdings N.V. shares (i.e. in the form of a capital distribution). Currently distributions are free from Dutch dividend withholding tax. The Group has been advised that for UK and Dutch shareholders the distribution is treated as capital for tax purposes. The Group has also been advised that it would be appropriate for UK funds to account for the distribution as income. Shareholders should seek independent advice on their own tax and accounting affairs.

During 2010 shareholders received 60.5p per share in distributions relating to the final distribution from 2009 and the interim distribution from 2010. Shareholders were able to elect to receive the final 2009 distribution in the form of a scrip distribution. The scrip alternative was taken up by 25% of shareholders (by number of shares).

Given the recommended cash offer by Achilles Netherlands Holdings B.V., the Board is not recommending a final distribution for 2010.

The following table below sets out the Sterling amounts of interim, final and total distributions paid per ordinary share.

Year ended 31 December

	Pence per ordinary share		Total
	Interim	Final	
2006 [∞]	30.0	38.0*	68.0*
2007 [∞]	30.0	58.0^	88.0^
2008 [∞]	30.0	30.0	60.0
2009 [∞]	30.0	30.1	60.1
2010	30.4	–	30.4

Source: Brit Insurance

* Includes special dividend of 8.0p per share

^ Includes special dividend of 28.0p per share

[∞] Adjusted for 1 for 4 share consolidation in February 2010

Debt particulars

The Group's debt securities at 31 December 2010 comprise £135m Subordinated Notes due 2030 which were first issued in 2005.

6.625% Subordinated Notes due 2030

Nominal Outstanding	£135.0m
Call	9 December 2020
Maturity	9 December 2030
Credit ratings	BBB Fitch
	BBB– AM Best
LSE Code	32 OW
SEDOL	B0SRM51

Consolidated Financial Statements

74 Consolidated Income Statement

75 Consolidated Statement of Comprehensive
Income

76 Consolidated Statement of Financial Position

77 Consolidated Statement of Cash Flows

78 Consolidated Statement of Changes in Equity

80 Notes to the Financial Statements

131 Independent auditor's report on the
Consolidated Financial Statements

Consolidated Income Statement

for the year ended 31 December 2010

	Note	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Revenue			
Gross premiums written	5	1,530.2	1,696.4
Less premiums ceded to reinsurers	5	(251.8)	(225.0)
Premiums written, net of reinsurance		1,278.4	1,471.4
Gross amount of change in provision for unearned premiums		20.5	(0.3)
Reinsurers' share of change in provision for unearned premiums		3.4	(7.2)
Net change in provision for unearned premiums		23.9	(7.5)
Earned premiums, net of reinsurance		1,302.3	1,463.9
Investment return	6	113.4	137.4
Return on derivative contracts	7	(1.9)	(4.1)
Disposal of associated undertakings	8	(0.4)	4.2
Net foreign exchange gains	9	29.3	–
Other income		–	1.4
Total revenue		1,442.7	1,602.8
Expenses			
Claims incurred:			
Claims paid:			
Gross amount		(926.2)	(792.2)
Reinsurers' share		181.6	110.8
Claims paid, net of reinsurance		(744.6)	(681.4)
Change in the provision for claims:			
Gross amount		(38.5)	(262.1)
Reinsurers' share		(13.5)	12.8
Net change in the provision for claims		(52.0)	(249.3)
Claims incurred, net of reinsurance	5	(796.6)	(930.7)
Acquisition costs	10	(396.1)	(396.9)
Other operating expenses	10	(117.8)	(111.6)
Net foreign exchange losses	9	–	(33.4)
Total expenses excluding finance costs		(1,310.5)	(1,472.6)
Operating profit		132.2	130.2
Finance costs	12	(14.0)	(11.5)
Share of loss after tax of associated undertakings	19	(1.8)	(2.3)
Profit on ordinary activities before tax		116.4	116.4
Tax expense	14(i)	(5.9)	(28.9)
Profit attributable to owners of the parent		110.5	87.5
Basic earnings per share (pence per share) (restated for 25 February 2010 share consolidation)	15	142.4p	113.2p
Diluted earnings per share (pence per share) (restated for 25 February 2010 share consolidation)	15	142.4p	113.2p

Consolidated Statement of Comprehensive Income

for the year ended 31 December 2010

	Note	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Profit for the year		110.5	87.5
Other comprehensive income			
Actuarial gains/(losses) on defined benefit pension scheme	21	8.1	(2.5)
Tax relating to actuarial gains/(losses) on defined benefit pension scheme	14(ii)	(2.2)	0.7
Foreign exchange differences arising on the revaluation of foreign operations	19	–	0.1
Reversal of foreign exchange translation differences resulting from the disposal of foreign operations		–	(4.2)
Effect of associates' capital movements	19	0.3	–
Other comprehensive income for the year net of tax		6.2	(5.9)
Total comprehensive income for the year attributable to owners of the parent		116.7	81.6

Consolidated Statement of Financial Position

at 31 December 2010

	Note	31 December 2010 £m	31 December 2009 £m
Assets			
Property, plant and equipment	16	6.5	6.0
Intangible assets	17	81.8	81.2
Deferred acquisition costs	18	166.7	162.4
Investments in associated undertakings	19	15.3	15.3
Current taxation		19.5	–
Reinsurance contracts	20	519.5	523.5
Employee benefits	21	9.6	–
Financial investments	22	2,921.0	2,481.1
Derivative contracts	23	0.4	0.6
Insurance and other receivables	24	540.8	537.0
Cash and cash equivalents	25	623.4	994.2
Total assets		4,904.5	4,801.3
Liabilities and equity			
Liabilities			
Insurance contracts	20	3,485.3	3,439.4
Employee benefits	21	–	4.1
Borrowings	26	168.4	237.6
Current taxation		10.3	4.7
Deferred taxation	27	15.6	19.0
Provisions	28	1.6	0.3
Derivative contracts	23	–	0.9
Insurance and other payables	29	251.7	200.7
Total liabilities		3,932.9	3,906.7
Equity			
Called up share capital	32	221.9	277.9
Share premium account		615.9	612.0
Own shares	33	(9.8)	(10.7)
Retained earnings		143.6	15.4
Total equity attributable to owners of the parent		971.6	894.6
Total liabilities and equity		4,904.5	4,801.3
Net assets per share (pence per share) (restated for 25 February 2010 share consolidation)	15	1,245.6p	1,156.8p
Net tangible assets per share (pence per share) (restated for 25 February 2010 share consolidation)	15	1,140.8p	1,052.0p

Consolidated Statement of Cash Flows

for the year ended 31 December 2010

	Note	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Cash generated from operations			
Cash flows provided by operating activities	35	(317.7)	73.5
Tax paid		(25.4)	(32.1)
Interest paid		(13.2)	(11.3)
Interest received		98.6	116.0
Dividends received		7.1	2.4
Net cash (outflows)/inflows from operating activities		(250.6)	148.5
Cash flows from investing activities			
Purchase of property, plant and equipment	16	(4.3)	(1.0)
Purchase of intangible assets	17	(5.4)	(5.5)
Net proceeds from disposals of associated undertakings	8	0.7	15.4
Movements in associated undertaking loan and preference share balances	19	(2.6)	(3.8)
Net cash (outflows)/inflows from investing activities		(11.6)	5.1
Cash flows from financing activities			
Equity dividends paid	30	–	(46.4)
Capital distributions paid	31	(41.1)	–
Proceeds from exercised share options		0.1	–
(Repayment)/draw down on revolving credit facility		(70.0)	104.8
Repurchase of US dollar floating rate unsecured subordinated loan notes		–	(9.1)
Acquisition of own shares for employee incentive schemes		(6.4)	(0.4)
Net cash (outflows)/inflows from financing activities		(117.4)	48.9
Net (decrease)/increase in cash and cash equivalents		(379.6)	202.5
Cash and cash equivalents at beginning of the year		994.2	840.7
Effect of exchange rate fluctuations on cash and cash equivalents		8.8	(49.0)
Cash and cash equivalents at the end of the year	25	623.4	994.2

Consolidated Statement of Changes in Equity

for the year ended 31 December 2010

	Note	Called up share capital £m	Share premium account £m	Capital redemption reserve £m	Translation reserve £m	Own shares £m	Retained earnings £m	Total equity attributable to owners of the parent £m
At 1 January 2010		277.9	612.0	–	–	(10.7)	15.4	894.6
Total comprehensive income for the year		–	–	–	–	–	116.7	116.7
Capital distributions	31	(45.7)	3.9	–	–	–	0.7	(41.1)
Exchange difference on retranslation of share capital		(10.3)	–	–	–	–	10.3	–
Acquisition of own shares for share schemes		–	–	–	–	(6.4)	–	(6.4)
Vesting of own shares		–	–	–	–	7.3	(7.2)	0.1
Share-based payments	36	–	–	–	–	–	7.7	7.7
At 31 December 2010		221.9	615.9	–	–	(9.8)	143.6	971.6

	Note	Called up share capital £m	Share premium account £m	Capital redemption reserve £m	Translation reserve £m	Own shares £m	Retained earnings £m	Total equity attributable to owners of the parent £m
At 1 January 2009		247.3	–	–	4.1	(64.2)	662.5	849.7
Total comprehensive income for the year		–	–	–	(4.1)	–	85.7	81.6
Cancellation of treasury shares		(11.9)	–	11.9	–	53.4	(53.4)	–
Equity dividends	30	–	–	–	–	–	(46.4)	(46.4)
Corporate reorganisation		(235.4)	–	(11.9)	–	–	247.3	–
Establishment of Brit Insurance Holdings N.V.		278.7	612.0	–	–	–	(890.7)	–
Exchange difference on retranslation of share capital		(0.8)	–	–	–	–	0.8	–
Acquisition of own shares for share schemes		–	–	–	–	(0.4)	–	(0.4)
Vesting of own shares		–	–	–	–	0.5	(0.5)	–
Share-based payments	36	–	–	–	–	–	10.1	10.1
At 31 December 2009		277.9	612.0	–	–	(10.7)	15.4	894.6

Consolidated Statement of Changes in Equity continued

for the year ended 31 December 2010

Nature and purpose of Group reserves

Share premium account

The share premium account represents the difference between the price at which shares are issued and their nominal value.

As a result of the corporate reorganisation on 21 December 2009, the balance as at that date has been cleared. On the same date, an amount equal to the difference between the issue price of Brit Insurance Holdings N.V. shares and their nominal value has been recognised in the share premium account.

Capital redemption reserve

The capital redemption reserve is used to maintain the Company's capital where, under certain circumstances, the Company's shares are cancelled.

Translation reserve

The translation reserve arises on the revaluation of overseas associated undertakings.

Own shares

Own shares represents the cost of shares held in trust for settling share-based payments and shares held in treasury.

Retained earnings

Retained earnings represents the cumulative comprehensive income retained by the Group after taxation and dividends.

Notes to the Financial Statements

1 General information

Brit Insurance Holdings N.V. (the Company) was incorporated and registered in the Netherlands on 22 June 2009 as a public company limited by shares with registered number 24464323. The address of the registered office is provided in the Shareholder and Depositary Interest Holder Information page. The nature of the Group's operations and its principal activities are included in the Report of the Directors.

2 Accounting policies

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union (EU).

During the year the Group has adopted IFRS 3R: 'Business Combinations', IAS 27R: 'Consolidated and Separate Financial Statements', IFRIC 17: 'Distributions of Non-Cash assets to Owners' and IFRIC 18: 'Transfers of Assets from Customers'. The adoption of these standards has had no effect on the consolidated financial statements for the year ended 31 December 2010.

The solus accounts of the parent company are prepared in accordance with the Dutch Civil Code and presented in a separate section of the annual report.

Corporate reorganisation

On 12 November 2009, the former ultimate holding company of the Brit Insurance Group, Brit Insurance Holdings PLC, announced proposals for the establishment of a Netherlands holding company for the Group.

Following approval by the shareholders of Brit Insurance Holdings PLC, the approval by the High Court of Justice of a scheme of arrangement under sections 895 to 899 of the UK Companies Act 2006 (the 'Scheme') and the Scheme becoming effective on 21 December 2009, the Company became the new holding company of the Group.

Under the Scheme, all of the shares of Brit Insurance Holdings PLC were cancelled. In consideration of the cancellation of these shares, the holders received one share in Brit Insurance Holdings N.V. in return for each share in Brit Insurance Holdings PLC.

The Company's ordinary shares were admitted to trading on the London Stock Exchange on 21 December 2009.

Share consolidation

On 25 February 2010, the Company undertook a consolidation of its share capital, such that the shareholders received one ordinary €4 share for every four ordinary €1 shares owned as at that date. All comparatives have been restated for the share consolidation.

Basis of preparation

The Group's consolidated opening and closing statement of financial position, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of cash flows and the consolidated statement of changes in equity, have been prepared in accordance with IFRS and Part 9 of Book 2 of the Dutch Civil Code. IFRS comprises standards issued by the International Accounting Standards Board (IASB) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) and as endorsed by the EU.

The income statement of the holding company, Brit Insurance Holdings N.V., has been drawn up in accordance with Section 402, Book 2, of the Dutch Civil Code, allowing a simplified format.

At the date of authorisation of these financial statements, the following standards which have not been applied in these financial statements were in issue but not yet effective:

Standard	Effective
IFRS 9 Financial Instruments	Periods commencing on or after 1 January 2013
IAS 24R Related Party Disclosures	Periods commencing on or after 1 January 2011
Amendments to IAS 32 Classification of a Rights Issue	Periods commencing on or after 1 February 2010
IFRIC 14 Prepayments of a Minimum Funding Requirement	Periods commencing on or after 1 January 2011
IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments	Periods commencing on or after 1 July 2010

The impact of IFRS 9 is still being evaluated. The Directors anticipate that the adoption of the other standards in future periods will have no material impact on the financial statements of the Group.

In accordance with IFRS 4, 'Insurance Contracts', the Group continues to comply with the recommendations of the Statement of Recommended Practice on Accounting for Insurance Businesses issued by the Association of British Insurers in December 2005 (as revised in December 2006). However the Group has the option to make improvements to its policies if the changes make the financial statements more relevant and no less reliable to the decision making needs of the users.

Certain amounts recorded in the financial information include estimates and assumptions made by management, particularly about insurance liability reserves, investment valuations, interest rates and other factors. Actual results may differ from the estimates made. For further information on the use of estimates and judgements, refer to Note 3.

Notes to the Financial Statements continued

2 Accounting policies continued

Basis of consolidation

The consolidated financial statements include the accounts of the Company, its subsidiaries and the Group's participation in Lloyd's syndicates' assets, liabilities, revenues and expenses. Subsidiaries are those entities in which the Group directly or indirectly has the power to exercise control over the operating and financial policies in order to gain economic benefits. Also consolidated as if they were subsidiaries are special purpose entities. The financial statements of subsidiaries are prepared up to 31 December each year. Consolidation adjustments are made to convert subsidiary accounts from local GAAP into IFRS so as to remove any dissimilar accounting policies that may exist. Subsidiaries are consolidated from the date control is transferred to the Group and cease to be consolidated from the date control is transferred from the Group. All inter-company balances, profits and transactions are eliminated.

Associated undertakings are those entities over which the Group has the power to exercise significant influence but not control. The Group's investment in associated undertakings is accounted for under the equity method of accounting whereby associated undertakings are carried in the statement of financial position at cost plus post-acquisition changes in the Group's share of net assets of the associate, less any impairment in value. The Group's investment in associated undertakings also includes goodwill identified on acquisition less any accumulated impairment loss. The income statement reflects the Group's share of the post-acquisition results of operations of the associated undertaking and the statement of comprehensive income reflects the Group's share of the comprehensive income of the associated undertaking. The financial statements of associated undertakings are prepared up to 31 December each year.

Product classification

Insurance contracts are those contracts that transfer significant insurance risk. Insurance risk is transferred when an insurer agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder. The significance of insurance risk is dependent on both the probability of an insured event and the magnitude of its potential effect.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period.

Where the Group has issued financial guarantee contracts these have been regarded as insurance contracts and have been accounted for in accordance with IFRS 4, 'Insurance Contracts'.

Other accounting policies

(i) Insurance contracts

a) Premiums

Premiums written relate to business incepted during the year, together with any differences between booked premiums for prior years and those previously accrued, and include estimates of premiums due but not yet receivable or notified, less an allowance for cancellations. Premiums are accreted to the income statement on a pro rata basis over the term of the related policy, except for those contracts where the period of risk differs significantly from the contract period. In these circumstances, premiums are recognised over the period of risk in proportion to the amount of insurance protection provided. Reinstatement premiums are accreted to the income statement on a pro rata basis over the term of the original policy to which it relates.

Premiums are shown net of premium taxes and other levies on premiums.

b) Deferred acquisition costs

Commission and other acquisition costs incurred during the financial period that are related to securing new insurance contracts and/or renewing existing insurance contracts, but which relate to subsequent financial periods, are deferred to the extent that they are recoverable out of future revenue margins. Deferred acquisition costs are capitalised and amortised over the life of the policy to which they relate on a basis consistent with the earnings pattern of that policy.

c) Claims incurred

Claims incurred comprise claims and claims handling costs paid in the year and changes in the outstanding claims provisions, including provisions for claims incurred but not reported and related expenses, together with any adjustments to claims from prior years. Claims handling costs are mainly those external costs related to the negotiation and settlement of claims.

d) Outstanding claims provisions

Outstanding claims represent the estimated ultimate cost of settling all claims (including direct and indirect claims settlement costs) arising from events which have occurred up to the date of the statement of financial position, including provision for claims incurred but not reported, less any amounts paid in respect of those claims. The Group does not discount its liabilities for unpaid claims, the ultimate cost of which cannot be known with certainty at the date of the statement of financial position.

e) Provision for unearned premiums

The proportion of written premiums that relate to unexpired terms of policies in force at the date of the statement of financial position is deferred as a provision for unearned premiums, generally calculated on a time apportioned basis. The movement in the provision is taken to the income statement in order that revenue is recognised over the period of the risk.

f) Liability adequacy tests

At the date of each statement of financial position, liability adequacy tests are performed, to ensure the adequacy of unearned premiums net of related deferred acquisition costs, employing the current estimates of future cash flows under its insurance contracts. If as a result of these tests, the carrying amount of the Group's insurance liabilities is found to be inadequate in comparison to the value of these future cash flows, the deficiency is charged to the income statement for the period by establishing an unexpired risk provision.

g) Reinsurance

The Group assumes and cedes reinsurance in the normal course of business. Premiums and claims on reinsurance assumed are recognised in the income statement along the same basis as direct business, taking into account the product classification. Reinsurance premiums ceded and reinsurance recoveries on claims incurred are included in the respective expense and income accounts. Reinsurance outwards premiums are earned according to the nature of the cover. 'Losses occurring during' policies are earned evenly over the policy period. 'Risks attaching' policies are expensed on the same basis as the inwards business being protected. Reinstatement premiums on both inwards and outwards business are accreted to the income statement on a pro rata basis over the term of the original policy to which they relate.

Notes to the Financial Statements continued

2 Accounting policies continued

Reinsurance assets include amounts recoverable from reinsurance companies for paid and unpaid losses and loss adjustment expenses, and ceded unearned premiums. Amounts recoverable from reinsurers are calculated with reference to the claims liability associated with the reinsured risks. Revenues and expenses arising from reinsurance agreements are therefore recognised in accordance with the underlying risk of the business reinsured.

Gains or losses on buying reinsurance are recognised immediately in the income statement.

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

h) Syndicate assets and liabilities

For each managed syndicate on which the Group participates, the Group's proportion of the syndicate's assets and liabilities has been reflected in its consolidated statement of financial position. Syndicate assets are held subject to trust deeds for the benefit of the Syndicate's insurance creditors.

(ii) Revenue recognition

a) Fee and commission income

Fee and commission income consists mainly of administration and broking fees charged to third parties. It is recognised in the accounting period in which the service is rendered by reference to completion of the specific transaction, assessed on the basis of the actual service provided as a proportion of the total services to be provided.

b) Investment return

Investment income comprises all interest and dividend income. Interest income is recognised using the effective interest method. Dividend income is recognised when the shareholders' right to receive the payment is established.

Realised gains and losses on investments are calculated as the difference between net sales proceeds and cost and are recognised when the sale transaction occurs.

Unrealised gains and losses on investments are calculated as the difference between the valuation at the date of the statement of financial position and the valuation at the last statement of financial position or purchase price, if acquired during the year. Unrealised investment gains and losses include adjustments in respect of unrealised gains and losses recorded in prior years which have been realised during the year and are reported as realised gains and losses in the current year's income statement.

(iii) Recognition and derecognition of financial assets and financial liabilities

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the contract.

A financial asset is derecognised when either the contractual rights to the asset's cash flows expire, or the asset is transferred and the transfer qualifies for derecognition under a combination of risks and rewards and control tests.

A financial liability is derecognised when it is extinguished which is when the obligation in the contract is discharged, cancelled or expired.

All 'regular way purchases and sales' of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset. Regular way purchases and sales are purchases and sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the marketplace.

(iv) Investments

The Group has designated on initial recognition its financial assets held for investment purposes (investments) at fair value through profit or loss (FVTPL). This is in accordance with the Group's documented investment strategy and consistent with investment risk being assessed on a portfolio basis. Information relating to investments is provided internally to the Group's Directors and key managers on a fair value basis.

The fair values of quoted financial investments are based on current bid prices. If the market for an investment is not active, the Group establishes fair value by using valuation techniques such as recent arm's length transactions, reference to similar listed investments, discounted cash flow models or option pricing models.

Unquoted equity investments are initially carried at fair value where this can be reliably determined. Where fair value cannot be reliably determined, cost is used as the best estimate of fair value. This is subsequently adjusted whenever events or changes in circumstances indicate that cost may not approximate to fair value. The fair value of an unquoted equity is calculated using the most appropriate valuation technique, such as reference to current fair values of another instrument that is substantially the same, discounted cash flow analysis or option pricing models.

Gains and losses on investments designated as FVTPL are recognised through the income statement. Investments are held on the statement of financial position at fair value.

(v) Derivatives

Derivative financial instruments include foreign exchange contracts, forward rate agreements, catastrophe swap contracts and other financial instruments that derive their value mainly from underlying interest rates, foreign exchange rates, catastrophe risk, commodity values or equity instruments. All derivatives are initially and subsequently measured at their fair value with movements in the fair value being immediately recognised in the income statement. Fair values are obtained from quoted market prices, discounted cash flow models, risk models and option pricing models as appropriate.

Where the risks and characteristics of derivatives embedded in financial instruments are not closely related to those of the host contract and the combined instrument is not measured at fair value with changes in fair value recognised in profit or loss, the derivative is separated from that host contract and measured at fair value.

(vi) Intangible assets

a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets, liabilities and reliably measured contingent liabilities of the acquired subsidiary or associated undertaking at the date of the acquisition. Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investments in associates. Goodwill is treated as an indefinite life asset and is carried at cost less any accumulated impairment losses.

Notes to the Financial Statements continued

2 Accounting policies continued

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units expected to benefit from the combination's synergies.

All goodwill created prior to 1 January 2003 is recorded at UK GAAP carrying amount at 1 January 2004 less any subsequent impairments.

b) Syndicate participation rights

Where the Group has purchased the right to participate on managed syndicates, the cost is capitalised and amortised in equal annual instalments over their estimated useful economic lives of three years. Amortisation commences from the date the underwriting results are first recognised in the income statement.

c) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring into use the specific software. Internal development costs that are directly associated with the production of identifiable and unique software products controlled by the Group are also capitalised where the cost can be measured reliably, the Group intends to and has adequate resources to complete development and the computer software will generate future economic benefits.

All computer software costs are finite life assets and amortised on a straight-line basis over their expected useful lives, not exceeding a period of five years.

(vii) Property, plant and equipment

Property, plant and equipment are carried at cost, less accumulated depreciation and any impairment in value. Depreciation is calculated so as to write-off the cost over their estimated useful economic lives on a straight-line basis having regard to the residual value of each asset, as follows:

Office refurbishment costs, computers (except personal computers), office machinery, furniture and equipment	20% per annum
Personal computers	33% per annum

The assets' residual values and useful lives are reviewed at the date of each statement of financial position and adjusted if appropriate.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Gains and losses on the disposal of property, plant and equipment are determined by comparing proceeds with the carrying amount of the asset and are included in the income statement. Costs for repairs and maintenance are expensed as incurred.

(viii) Impairment

Goodwill is not subjected to amortisation but is tested annually for impairment as it is an asset with an indefinite useful life. Other assets, except for assets arising from insurance contracts, are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

If the carrying value of an asset is impaired, it is reduced to the recoverable amount by an immediate charge to the income statement. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Value in use is based on discounting cash flows at the Group's weighted average cost of capital which is loaded where significant uncertainties exist.

Assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

Impairment reviews are made by comparing carrying value to recoverable amount.

(ix) Cash and cash equivalents

Cash and cash equivalents in the statement of financial position include cash in hand, deposits held at call with banks and other short-term highly liquid investments with a maturity of three months or less at the date of placement or acquisition, free of encumbrances.

For the purpose of the consolidated cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(x) Income taxes

Income tax comprises current and deferred tax. Income tax is recognised in the income statement except where it relates to an item which is recognised in equity.

a) Current income tax

Current income tax is the expected tax payable on the taxable profit for the period using tax rates (and laws) enacted or substantively enacted at the date of the statement of financial position and any adjustment to the tax payable in respect of previous periods. The Group calculates current income tax using the current income tax rate.

b) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not recognised. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the date of the statement of financial position and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income 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.

Deferred income tax relating to items recognised in other comprehensive income is also recognised in other comprehensive income.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the Group controls the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.

Deferred tax assets and liabilities are not discounted.

Notes to the Financial Statements continued

2 Accounting policies continued

(xi) Post-retirement employee benefits

The Group operates a defined contribution group personal pension plan and several other defined contribution schemes. It also makes payments into a number of personal money purchase pension plans. Contributions in respect of these schemes are charged to the income statement in the period to which they relate.

The Group also operates a defined benefit pension scheme. The liability recognised in the statement of financial position in respect of the defined benefit scheme is the present value of the defined benefit obligation at the date of the statement of financial position less the fair value of plan assets. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows. The discount rate is based on market yields of high-quality corporate bonds that have terms to maturity which approximate to those of the related pension liability.

Actuarial gains and losses are recognised immediately through other comprehensive income.

Past service costs arising in the period are recognised immediately in the income statement, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortised on a straight-line basis over the vesting period.

(xii) Share-based payments

The Group operates a number of equity-settled share-based payment plans. The fair value of the equity instrument granted is recognised as an expense, spread over the vesting period of the instrument. The total amount to be expensed is determined by reference to the fair value of the awards made at the grant date, excluding the impact of any non-market vesting conditions. At the date of each statement of financial position, the Group revises its estimate of the number of equity instruments that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment is made to equity over the remaining vesting period. The fair value of the awards and ultimate expense are not adjusted on a change in market vesting conditions during the vesting period.

Where the Group operates cash-settled share-based payment plans, the treatment is similar except that at the date of each financial statement the fair value of the awards is remeasured. The impact of the resulting adjustment is recognised in the income statement and a corresponding adjustment is made to liabilities.

(xiii) Own shares

Where the Company purchases the Company's own share capital, the consideration paid is shown as a deduction from total shareholders' equity. No gain or loss is recognised in the income statement on the purchase, sale, issue or cancellation of own shares and any consideration paid or received is recognised directly in equity.

(xiv) Provisions

Provisions are liabilities with uncertainties in the amount or timing of payments. Provisions are recognised if there is a present obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made at the date of the statement of financial position.

(xv) Leased assets

Where the Group enters into an operating lease, the payments (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the lease term. An operating lease is one in which the risks and rewards remain with the lessor.

(xvi) Foreign currency translation

The consolidated financial statements are presented in Sterling. Items included in the financial statements of each of the Group's entities are measured using the functional currency which is the primary economic environment in which the entity operates.

Foreign currency transactions are recorded in the functional currency for each entity using the exchange rates prevailing at the dates of the transactions or at the average rate for the period when this is a reasonable approximation. Substantially all of the Group's operations have Sterling as their functional currency. Monetary assets and liabilities denominated in foreign currencies are translated at period end exchange rates. Non-monetary assets and liabilities that are measured at historical cost denominated in a foreign currency are not retranslated. The resulting exchange differences on translation are recorded in the income statement.

Exchange differences arising on monetary items which form part of the Group's net investment in a foreign operation are initially recognised in other comprehensive income until the disposal of the investment.

(xvii) Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred and subsequently stated at amortised cost. Fair value is normally determined by reference to the fair value of the proceeds received. Any difference between the initial carrying amount and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

(xviii) Segmental reporting

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the entity's chief operating decision maker and for which discrete financial information is available.

(xix) Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments. Loans and receivables are measured at amortised cost, using the effective interest method.

(xx) Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously.

(xxi) Dividend and capital distributions

Dividend and capital distributions to the Company's shareholders are recognised in the Group's financial statements in the period in which they are declared and appropriately approved.

Notes to the Financial Statements continued

2 Accounting policies continued

(xxii) Collateral

The Group receives collateral from certain reinsurers and pledges collateral where required for regulatory purposes.

Collateral received in the form of cash is recognised as an asset on the statement of financial position with a corresponding liability for the repayment. Non-cash collateral received is not recognised on the statement of financial position.

Collateral pledged is not derecognised from the statement of financial position unless the Group defaults on its obligations under the relevant agreement.

3 Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities. Estimates and judgements are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

(i) The ultimate liability arising from claims made under insurance contracts

The estimation of the ultimate liability arising from claims made under insurance contracts is the Group's most critical accounting estimate. There are several sources of uncertainty that need to be considered in the estimate of the amounts that the Group will ultimately pay to settle such claims.

Significant areas requiring estimation and judgement include:

- a) Estimates of the amount of any liability in respect of claims notified but not settled and incurred but not reported claims provisions (IBNR) included within provisions for insurance and reinsurance contracts.
- b) The corresponding estimate of the amount of reinsurance recoveries which will become due as a result of these estimated claims.
- c) The recoverability of amounts due from reinsurers.
- d) Estimates of the proportion of exposure which has expired in the period as represented by the earned proportion of premiums written.

The assumptions used and the manner in which these estimates and judgements are made are set out below:

- a) Quarterly statistical data is produced in respect of gross and net premiums and claims (paid and incurred).
- b) Projections are produced by an internal actuarial department, with appropriate adjustment for specific claims made by management where deemed appropriate.
- c) The resulting projections are discussed with experienced underwriting and claims personnel and claims provision recommendations made to an internal reserving committee consisting of senior underwriters, claims managers and finance staff.
- d) Claims provisions are subject to independent external actuarial review at least annually.

- e) Some classes of business have characteristics which do not necessarily lend themselves easily to statistical estimation techniques. These classes would include Financial Risk, Casualty Treaty, Catastrophe Retrocessional and Mortgage Indemnity Guarantee business. In these cases review is carried out on a policy-by-policy basis to support statistical estimates.

- f) In the event of catastrophe losses and prior to detailed claims information becoming available, claims provision estimates are compiled using a combination of specific recognised modelling software and reviews of material contracts exposed to the event in question.

Overall the objectives of the estimates and judgements applied to claims provisions seek to state such provisions on a best estimate, undiscounted basis.

In addition to claims provisions, the reserve for future loss adjustment expenses is also subject to estimation. In arriving at this estimate, regard is had to the levels of internal and third party loss adjusting expenses incurred annually. The estimated loss adjustment expenses are expressed as a percentage of net claims reserves and are benchmarked to assess the reasonableness of the estimate.

Further judgements are made as to the recoverability of amounts due from reinsurers. Provisions for bad debts are made specifically, based on the solvency of reinsurers, internal and external ratings, payment experience with them and any disputes of which the Group is aware.

The carrying value at the date of the statement of financial position of gross claims reported and loss adjustment expenses and claims incurred but not reported were £2,818.5m (2009: £2,752.1m) as set out in Note 20 to the accounts. The amount of reinsurance recoveries estimated at that date is £453.0m (2009: £460.4m).

(ii) Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value, both of which are material sources of uncertainty.

The carrying amount of goodwill at the date of the statement of financial position was £63.7m (2009: £63.7m) as set out in Note 17 to the accounts.

(iii) Financial investments

Financial investments are carried in the statement of financial position at fair value. The carrying amount of financial investments at the date of the statement of financial position was £2,921.0m (2009: £2,481.1m). Determining the fair value of certain investments requires estimation.

For further information, refer to Note 22.

Notes to the Financial Statements continued

4 Risk management policies

The Group's activities expose the business to a number of key risks which have the potential to affect its ability to achieve its business objectives. The following describes the Group's financial and insurance risk management from a quantitative and qualitative perspective.

The Board is responsible for the Group's systems of internal control and for reviewing their effectiveness. The systems of internal control are designed to manage rather than eliminate risk and aim to provide reasonable and not absolute assurance. Group underwriting activities are co-ordinated through a system of strategic business unit management committees as well as the Executive Management Committee and the Boards for the regulated entities. Investment risk is managed in accordance with investment frameworks which are set by the Investment Committee which meets monthly.

Financial risk

(i) Credit risk

This is the risk that one party to a financial arrangement will fail to discharge an obligation and cause the other party to incur a financial loss. The following is an overview of how the Group manages its significant credit risk exposures.

Reinsurance assets

Reinsurance is placed in line with policy guidelines and concentration of risk is managed by reference to counterparties' limits that are set each year and are subject to regular reviews. On a regular basis management performs assessments of creditworthiness of reinsurers to update reinsurance purchase strategy and to ascertain suitable allowance for impairment of reinsurance assets.

Financial investments and cash and cash equivalents

Credit risk relating to financial investments and cash and cash equivalents is monitored by the Investment Committee. The Group's investment guidelines specify the maximum

percentage of the portfolios that can be invested in or with any single counterparty – these limits are determined using the Moody's or other recognised credit rating of each asset. In addition the Group's Investment Committee will from time to time impose special limits on assets that are deemed more at risk than the rating agencies currently imply.

Derivative contracts

The Group may use derivatives from time to time, with prior approval from the Investment Committee. The four main derivative classes are credit derivatives, foreign exchange forwards and options, interest rate derivatives and equity index options. Derivatives are only used for the purposes of efficient portfolio management, reduction in investment risk and to mitigate the credit risk of certain reinsurance counterparties. Credit risk with respect to derivatives, where deemed necessary, is controlled with the implementation of collateral agreements with derivative counterparties that put a finite limit on the credit risk of each transaction.

Insurance receivables

The Group credit risk is in respect of balances with customers, intermediaries and reinsurers. The Group seeks to reduce its credit exposure to intermediaries through application of its internal credit vetting processes and its active credit control procedures. Wherever possible, the Group includes premium payment warranties in its terms and conditions which gives it the right to cancel policies in the event of non-payment. Insurance receivables are made up of debtors arising out of direct and reinsurance operations.

The following credit risk table in respect of monetary assets and derivatives provides information regarding the credit risk exposure of the Group by classifying the assets according to credit ratings of the counterparties. Ratings in respect of financial investments and cash and cash equivalents are from the Moody's rating scale and ratings in respect of reinsurance assets are from the Standard and Poor's rating scale. These amounts represent the maximum credit risk exposure.

31 December 2010

	Government £m	AAA £m	AA £m	A £m	P-1 £m	BBB and below £m	Collateralised £m	Equities £m	Not rated £m	Total £m
Reinsurance assets (a)	–	0.6	164.2	197.8	–	5.7	71.2	–	13.5	453.0
Financial investments (b)	1,435.5	163.5	211.6	514.7	279.7	87.7	–	125.7	102.6	2,921.0
Derivative contracts	–	–	–	–	–	–	–	–	0.4	0.4
Insurance receivables (c) (d)	–	–	–	–	–	–	–	–	498.0	498.0
Cash and cash equivalents	–	356.8	96.0	11.2	88.2	71.2	–	–	–	623.4
	1,435.5	520.9	471.8	723.7	367.9	164.6	71.2	125.7	614.5	4,495.8

Notes to the Financial Statements continued

4 Risk management policies continued

31 December 2009

	Government £m	AAA £m	AA £m	A £m	P-1 £m	BBB and below £m	Collateralised £m	Equities £m	Not rated £m	Total £m
Reinsurance assets (a)	–	7.7	178.7	176.3	–	4.0	75.4	–	18.3	460.4
Financial investments (b)	1,045.5	274.4	261.2	296.3	346.9	58.1	–	102.0	96.7	2,481.1
Derivative contracts	–	–	–	–	–	–	–	–	0.6	0.6
Insurance receivables (c) (d)	–	–	–	–	–	–	–	–	493.4	493.4
Cash and cash equivalents	–	613.3	63.1	138.7	33.6	145.5	–	–	–	994.2
	1,045.5	895.4	503.0	611.3	380.5	207.6	75.4	102.0	609.0	4,429.7

a Amounts recoverable from reinsurers on claims reported and loss adjustment expenses and claims incurred.

b Financial investments categorised as government, are bonds issued by the governments of Eurozone countries, the UK, Canada and the US.

c Insurance receivables arising out of direct and reinsurance operations.

d Insurance receivables are generally due from customers and intermediaries who are unlikely to seek ratings as part of their normal course of business.

At 31 December 2010, the Group held £12.5m in debt securities relating to Italy and Spain. The Group had no direct holdings in debt securities relating to Portugal, Greece or Ireland.

Impairment

The Group considers reinsurer ratings, notified disputes and collection experience in determining which assets should be impaired.

The following table shows the movements in impairment provisions during the year.

	Impairment provision against reinsurance assets		Impairment provision against insurance receivables	
	31 December 2010 £m	31 December 2009 £m	31 December 2010 £m	31 December 2009 £m
1 January	12.4	15.5	6.3	5.1
(Release)/strengthening for the year	(1.8)	(2.2)	(3.4)	1.2
Net foreign exchange differences	0.2	(0.9)	–	–
31 December	10.8	12.4	2.9	6.3

The following table shows a breakdown of the impairment provision against reinsurance assets.

	31 December 2010 £m	31 December 2009 £m
AAA	–	0.2
AA	4.6	5.8
A	5.6	5.7
BBB and below	0.2	0.1
Not rated	0.4	0.6
Total	10.8	12.4

The following table shows the amount of insurance receivables that were past due but not impaired at the end of the year.

	31 December 2010 £m	31 December 2009 £m
0-3 months past due	26.4	20.3
4-6 months past due	3.3	2.7
7-9 months past due	0.4	0.5
10-12 months past due	1.0	0.3
More than 12 months past due	0.6	1.9
Total	31.7	25.7

Notes to the Financial Statements continued

4 Risk management policies continued

(ii) Liquidity risk

This is the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities that are settled by cash or another financial asset.

The most significant liquidity risk confronting the Group is the daily calls on its available cash resources in respect of claims arising from insurance contracts. This liquidity risk is increased by the requirement to ring fence funds in respect of US and Canadian regulated business.

The Group manages this risk by maintaining sufficient liquid assets or assets that can be translated into liquid assets at short notice to meet the expected cash flow requirements. The Group's Investment Guidelines also set out various short term cash balances to be held by external fund managers.

The Group has determined the minimum amount of funds required to ensure that the Group has sufficient liquid assets to withstand claim scenarios at the extreme end of business plan projections by reference to modelled Realistic Disaster Scenario events.

The table below analyses the fair value of monetary assets and the undiscounted value of monetary liabilities of the Group into their relevant maturing groups based on the remaining period at the end of the year to their contractual maturities or expected repayment dates.

31 December 2010

Assets	Statement of Financial Position £m						Fair values
		Up to a year £m	1-3 years £m	3-5 years £m	Over 5 years £m	Equities £m	Total £m
Reinsurance assets	453.0	150.8	171.8	73.7	56.7	–	453.0
Financial investments	2,921.0	558.7	1,316.4	641.8	278.4	125.7	2,921.0
Derivative contracts	0.4	–	–	–	–	–	–
Insurance receivables	498.0	498.0	–	–	–	–	498.0
Cash and cash equivalents	623.4	623.4	–	–	–	–	623.4
	4,495.8	1,830.9	1,488.2	715.5	335.1	125.7	4,495.4

Liabilities	Statement of Financial Position £m						Undiscounted values
		Up to a year £m	1-3 years £m	3-5 years £m	Over 5 years £m		Total £m
Insurance contract liabilities	2,818.5	884.1	1,020.9	485.8	427.7		2,818.5
Derivative contracts	–	–	–	–	–		–
Borrowings	168.4	10.4	57.5	17.9	179.7		265.5
Insurance and other payables	251.7	251.7	–	–	–		251.7
	3,238.6	1,146.2	1,078.4	503.7	607.4		3,335.7

31 December 2009

Assets	Statement of Financial Position £m						Fair values
		Up to a year £m	1-3 years £m	3-5 years £m	Over 5 years £m	Equities £m	Total £m
Reinsurance assets	460.4	164.0	122.2	74.0	100.2	–	460.4
Financial investments	2,481.1	767.4	1,194.2	242.3	175.2	102.0	2,481.1
Derivative contracts	0.6	–	–	–	–	–	–
Insurance receivables	493.4	493.4	–	–	–	–	493.4
Cash and cash equivalents	994.2	994.2	–	–	–	–	994.2
	4,429.7	2,419.0	1,316.4	316.3	275.4	102.0	4,429.1

Notes to the Financial Statements continued

4 Risk management policies continued

Liabilities	Undiscounted values					
	Statement of Financial Position £m	Up to a year £m	1-3 years £m	3-5 years £m	Over 5 years £m	Total £m
Insurance contract liabilities	2,752.1	980.1	730.2	442.5	599.3	2,752.1
Derivative contracts	0.9	2.4	–	–	–	2.4
Borrowings	237.6	13.1	132.4	17.9	188.7	352.1
Insurance and other payables	200.7	200.7	–	–	–	200.7
	3,191.3	1,196.3	862.6	460.4	788.0	3,307.3

The nature of insurance is that the requirements of funding cannot be predicted with absolute certainty and therefore the theory of probability is applied to insurance contracts to ascertain the likely provision and the time period when such liabilities will require settlement. The amounts and maturities in respect of insurance liabilities are thus based on management's best estimate based on statistical techniques and past experience.

(iii) Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and price risk.

Market risk can be caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

a) Currency risk

The Group writes a significant proportion of its insurance business in currencies other than Sterling.

Currency risk is mitigated by the Group mainly maintaining financial assets denominated in the same currencies as its liabilities which is demonstrated in the table below. This is monitored by reviewing the Group's currency statement of financial position on a quarterly basis.

31 December 2010

Assets	Sterling equivalent				
	US dollars £m	Canadian dollars £m	Euros £m	Sterling and others £m	Total £m
Reinsurance assets	244.6	9.1	31.2	168.1	453.0
Financial investments	995.2	121.3	236.4	1,568.1	2,921.0
Derivative contracts	–	–	–	0.4	0.4
Insurance receivables	242.7	13.8	36.6	204.9	498.0
Cash and cash equivalents	228.9	23.7	151.4	219.4	623.4
Total monetary assets	1,711.4	167.9	455.6	2,160.9	4,495.8
Non-monetary assets	95.3	23.8	18.6	271.0	408.7
Total assets	1,806.7	191.7	474.2	2,431.9	4,904.5

Notes to the Financial Statements continued

4 Risk management policies continued

31 December 2010

	Sterling equivalent				
	US dollars £m	Canadian dollars £m	Euros £m	Sterling and others £m	Total £m
Liabilities					
Insurance contract liabilities	1,242.9	108.0	394.2	1,073.4	2,818.5
Borrowings	–	–	–	168.4	168.4
Insurance and other payables	75.4	3.1	19.3	153.9	251.7
Total monetary liabilities	1,318.3	111.1	413.5	1,395.7	3,238.6
Non-monetary liabilities	305.8	25.7	35.4	327.4	694.3
Total liabilities	1,624.1	136.8	448.9	1,723.1	3,932.9
Net assets and liabilities	182.6	54.9	25.3	708.8	971.6

31 December 2009

	Sterling equivalent				
	US dollars £m	Canadian dollars £m	Euros £m	Sterling and others £m	Total £m
Assets					
Reinsurance assets	248.4	7.6	31.1	173.3	460.4
Financial investments	827.4	93.4	242.4	1,317.9	2,481.1
Derivative contracts	(0.6)	–	–	1.2	0.6
Insurance receivables	226.0	25.8	32.6	209.0	493.4
Cash and cash equivalents	399.2	27.0	105.8	462.2	994.2
Total monetary assets	1,700.4	153.8	411.9	2,163.6	4,429.7
Non-monetary assets	88.4	14.6	22.1	246.5	371.6
Total assets	1,788.8	168.4	434.0	2,410.1	4,801.3

	Sterling equivalent				
	US dollars £m	Canadian dollars £m	Euros £m	Sterling and others £m	Total £m
Liabilities					
Insurance contract liabilities	1,246.5	95.8	359.0	1,050.8	2,752.1
Derivative contracts	–	–	–	0.9	0.9
Borrowings	–	–	–	237.6	237.6
Insurance and other payables	65.5	2.1	12.3	120.8	200.7
Total monetary liabilities	1,312.0	97.9	371.3	1,410.1	3,191.3
Non-monetary liabilities	275.2	17.4	57.6	365.2	715.4
Total liabilities	1,587.2	115.3	428.9	1,775.3	3,906.7
Net assets and liabilities	201.6	53.1	5.1	634.8	894.6

The matching of assets and liabilities prevents economic exposure to currency risk but it does not prevent exposure to exchange gains or losses recorded in the income statement created as a result of the IFRS accounting treatment of certain assets and liabilities. IFRS requires that gross and reinsurers share of unearned premium reserves and deferred acquisition costs are translated at historical transaction rate rather than closing rate. This means that these amounts in the statement of financial position are carried at a different exchange rate to the remaining assets and liabilities with the resulting exchange differences that are created being recognised in the income statement.

Notes to the Financial Statements continued

4 Risk management policies continued

A strengthening of the following currencies relative to Sterling by 10% would have resulted in an additional net foreign exchange gain/(loss) before tax in the income statement as set out below.

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
US dollars	44.5	44.8
Canadian dollars	8.1	8.1
Euros	5.5	5.2

b) Interest rate risk and price risk

The Group is exposed to interest rate and price risk on its investment portfolio. Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Price risk is the risk that the value of investments decreases due to market factors.

In order to manage interest rate and price risk the Group uses Value at Risk (VaR) methodology with the objective of minimising the risk taken on the investment portfolio in targeting a desired return. This is performed by examining the asset allocation of the portfolio and modelling the portfolio's expected return and associated risk. Different asset combinations are then modelled to examine the effect of the changes on risk, determining which combination of changes is expected to minimise risk.

The model uses assumptions of risks, correlations and expected returns for each asset class. Interest rate risk, price risk and currency risk are all included in the model both independently and in their interaction with each other. Assumptions for future market returns, volatilities and correlations are provided by independent investment consultants.

A principal measure of risk produced by the model is one year VaR. One year VaR measures the minimum amount by which the assets should be expected to underperform the expected annual return of the portfolio with a 1 in 20 probability.

The model used by the Group estimates the VaR and the tracking error. The tracking error measures annual volatility as the standard deviation of the asset returns relative to the expected return. Whereas VaR expresses a 1 in 20 probability of the portfolio returns being reduced by at least that amount in one year, the tracking error is the expected deviation above or below the expected return.

	31 December 2010	31 December 2009
Value at Risk 95%	3.55%	2.01%
Tracking Error	2.08%	1.33%

As an illustration of the above information, if the expected return as at 31 December 2010 for the following year was 5.0%, then there would be a 1 in 20 probability that if the asset portfolio remained unaltered, the actual return for the following year would underperform the 5.0% expected return by at least 3.55% i.e. a 1.45% return or less.

The model is designed to illustrate the future range of returns stemming from different asset classes and their inter-relationship. The assumptions have incorporated a degree of subjective judgement to complement the information provided by historical returns and current conditions.

(iv) Capital risk management

The total amount of capital of the Group is £1,022.8m (2009: £946.2m) consisting of net tangible assets amounting to £889.8m (2009: £813.4m) and long-term subordinated debt amounting to £133.0m (2009: £132.8m).

The capital policy, which is set by the Board, requires that the Group always holds long-term capital in excess of the Management Capital requirement (derived from a risk-based internal stochastic model) and that the appropriate level of capital is held at individual insurance entity level with reference to the various regulatory or rating agency requirements.

The capital policy also requires that the appropriate mix of debt and equity is used to fund the Group and that adequate liquidity is available at all times.

The most significant entities within the Group subject to externally imposed capital requirements are Brit Insurance Limited, Brit Insurance (Gibraltar) PCC Ltd and the Lloyd's corporate member, Brit UW Limited, which provides the entire capacity of Syndicate 2987.

Brit Insurance Limited is regulated by the Financial Services Authority (FSA) in the UK which has provided the Company with individual capital guidance based on the Enhanced Capital Requirements return (ECR). The ECR, which takes into account the premiums written and outstanding reserves on a class of business basis, seeks to ensure that the Company has at least the minimum amount and type of capital to meet future expected claims obligations. Brit Insurance Limited holds capital in excess of the FSA requirement in order to maintain a strong 'A' credit rating.

The Group holds capital at Lloyd's which is held in trust and known as Funds at Lloyd's (FAL). These funds are intended primarily to cover circumstances where syndicate assets prove insufficient to meet participating members' underwriting liabilities. FAL is determined by a risk based capital assessment based upon the syndicate's specific circumstances and results in an individual capital assessment (ICA).

Brit Insurance (Gibraltar) PCC Ltd is regulated by the Financial Services Commission of Gibraltar which sets a capital requirement based on the Solvency I Minimum Capital Requirement (MCR). The MCR is a factor based calculation based on premiums written and earned during the year.

All externally imposed capital requirements have been complied with during the year.

Insurance risk

(i) Introduction

The risk under any one insurance contract is the possibility that an insured event occurs and a claim results. By the very nature of an insurance contract, risk is based on fortuity and is therefore unpredictable.

The principal risks that the Group faces under its insurance contracts are that the business will be under-priced, under-reserved or subject to catastrophe claims.

Notes to the Financial Statements continued

4 Risk management policies continued

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. In addition, a more diversified portfolio is less likely to be affected across the board by a change in any subset of the portfolio. The Group has developed its insurance underwriting strategy to diversify the type of insurance risks accepted to achieve a sufficiently large population of risks to reduce the variability of the expected outcome.

The Group has developed underwriting guidelines, limits of authority and business plans which are binding upon all staff authorised to underwrite. These are detailed and specific to underwriters and classes of business as well as establishing more general principles and conditions. A proportion of the Group's insurance risks are written by third parties under delegated underwriting authorities. The third parties are closely vetted in advance and are subject to tight reporting requirements. In addition the performance of these contracts is closely monitored by underwriters and regular audits are carried out.

Compliance is checked through both a peer review process and, periodically, by the Group's internal audit department which is entirely independent of the underwriting units.

In order to limit risk, the number of reinstatements per policy is limited, deductibles are imposed, policy exclusions are applied and whenever allowed by statute, maximum indemnity limits are put in place per insured event.

The Group carries out an annual business planning process for each of its underwriting units. The resulting plans set out premium, territorial and aggregate limits for all classes of business. Performance against the plans is monitored on a regular basis through a system of underwriting committees as well as regularly by the Executive Management Committee and the Boards for the regulated entities.

(ii) Concentrations of risk

The concentration of insurance risk before and after reinsurance by the location of the underlying risk is summarised below:

Year ended 31 December 2010

	Gross premiums written £m	Premium ceded to reinsurers £m	Net premiums written £m
United Kingdom	523.7	(105.8)	417.9
Europe (excluding UK)	84.4	(18.6)	65.8
United States	343.6	(60.6)	283.0
Other (including worldwide)	578.5	(66.8)	511.7
	1,530.2	(251.8)	1,278.4

Year ended 31 December 2009

	Gross premiums written £m	Premium ceded to reinsurers £m	Net premiums written £m
United Kingdom	491.0	(77.5)	413.5
Europe (excluding UK)	128.7	(15.4)	113.3
United States	416.2	(64.2)	352.0
Other (including worldwide)	660.5	(67.9)	592.6
	1,696.4	(225.0)	1,471.4

The Group is organised into three Strategic Business Units, details of which are set out in Note 5.

(iii) Reinsurance

The Group purchases reinsurance to limit its exposure to individual risks and aggregation of risks arising from individual large claims and catastrophe events. The types of reinsurance purchased were as follows:

- ▶ facultative reinsurance purchased to reduce risk relating to an individual specific inwards contract
- ▶ risk excess of loss reinsurance purchased to protect a range of individual inwards contracts which could give rise to individual large claims
- ▶ general excess of loss reinsurance purchased to provide protection from the aggregation of claims, possibly arising from catastrophe events
- ▶ pro rata reinsurance purchased to provide protection against claims arising either from individual large claims or aggregations.

All of the Group's reinsurance purchasing is approved by the Portfolio Management Committee, a sub-committee of the Executive Management Committee. Decisions are supported by historical underwriting experience and actuarial analysis.

(iv) Aggregate exposure management

The Group monitors and controls the accumulation of risk for over 50 key Realistic Disaster Scenario (RDS) events. These RDSs reflect the diversity of the Group's exposures. There are specific scenarios for elemental, man-made and economic disasters, and for different business classes such as marine, aerospace, casualty and property. The RDSs are regularly reviewed in light of Group exposures and environmental factors.

Each scenario is reviewed quarterly, with more frequent reviews of the peak zone natural peril catastrophe RDSs which present the greatest exposure to the Group.

Aggregate claims tolerance

The Group's tolerance for catastrophe risk is a function of expected profitability and available capital. This tolerance is expressed as the maximum net claims acceptable under a number of scenarios.

Exposure and compliance with a severity band matrix is formally reviewed on a quarterly basis, with informal reviews being conducted more frequently. The Board may decide to increase or decrease the maximum tolerances based on market conditions and other factors.

Notes to the Financial Statements continued

4 Risk management policies continued

The tolerance for catastrophe risk is set using industry claims bandings. For example for US Windstorm, tolerance is set for seven separate industry claims bands increasing from a 'US\$20bn-US\$30bn' band to a 'US\$200bn-US\$350bn' band. The underlying frequency and severity of catastrophe events varies by peril and territory. For instance, a US\$20bn US windstorm is expected to occur much more frequently than a US\$20bn Japanese earthquake. Therefore, in terms of risk appetite and claims tolerance, it is not appropriate to treat these events equally.

The severity bands show the industry claims for each peril which are probabilistically equivalent. An example band is shown below.

US windstorm	US\$70bn-US\$100bn
California earthquake	US\$30bn-US\$40bn
European windstorm	US\$10bn-US\$15bn
Japanese earthquake	US\$20bn-US\$30bn
Japanese typhoon	US\$10bn-US\$15bn

The portfolio contains a mix of business and therefore given an industry event there will be a large range of possible aggregate claims to the Group. To capture this claim distribution whilst being able to measure compliance, the measure used is a weighted 75th percentile of the claim distribution within a particular band. Ultimately, the size of a probable maximum loss (PML) arising from an event or series of events will always remain judgemental for Brit Insurance and others in the industry.

The Group uses its own and commercially available proprietary risk management software. However, there is always a risk that the assumptions and techniques used in these models are unreliable or that claims arising from an unmodelled event are greater than those arising from a modelled event.

As a further guide to the level of catastrophe exposure written by the Group, the table below shows hypothetical claims in the fourth quarter of 2010 for various RDS events.

Event	Modelled industry claims US\$m	Brit Insurance gross claims £m	Brit Insurance net claims £m	Comments
► Florida hurricane Tampa Bay	125,000	305	126	Category 4 storm on the Saffir-Simpson Hurricane Wind Scale, landfalling in Tampa. Brit Insurance claims estimates include demand surge, flood associated with the hurricane, and non-property exposures.
► Florida hurricane Miami	125,000	265	95	Category 5 storm on the Saffir-Simpson Hurricane Wind Scale, landfalling in Miami. Brit Insurance claims estimates include demand surge, flood associated with the hurricane, and non-property exposures.
► US north east coast hurricane New York State	78,000	264	125	Category 4 storm on the Saffir-Simpson Hurricane Wind Scale, landfalling in Suffolk County, New York State. Brit Insurance claims estimates include demand surge, flood associated with the hurricane, and non-property exposures.
► California earthquake Los Angeles	78,000	292	91	Magnitude 7.3 earthquake on the Modified Mercalli Intensity Scale for Earthquakes, on the Elsinore fault in Los Angeles. Brit Insurance claims estimates include demand surge, fire following the earthquake, and non-property exposures.
► California earthquake San Francisco	78,000	295	88	Magnitude 7.5 earthquake on the Modified Mercalli Intensity Scale for Earthquakes, on the San Andreas Fault in San Francisco. Brit Insurance claims estimates include demand surge, fire following the earthquake, and non-property exposures.
► Europe windstorm Western Europe	31,000	218	77	A winter storm with peak gusts in excess of 112mph resulting in a broad swathe of damage across southern England, France, Belgium, Netherlands, Luxembourg, Germany and Denmark. Brit Insurance claims estimates include demand surge and UK coastal flood.
► Japan earthquake Tokyo	62,000	183	74	Based on a repeat of the Great Kanto event in 1923, a magnitude 7.9 earthquake in the Tokyo Metropolitan Area.

Source: RMS/Lloyd's/Brit Insurance

Notes to the Financial Statements continued

4 Risk management policies continued

(v) Sensitivity

The Group profit on ordinary activities before tax is sensitive to an independent 1% change in the net claims ratio (excluding the effect of foreign exchange on non-monetary items) for each class of business as follows:

Strategic business unit	Class	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
		£m	
Global Markets	Accident & Health	0.6	1.1
	Aerospace	0.2	0.2
	Specialty lines	1.0	1.6
	Professional lines	1.1	1.3
	Marine	2.3	2.3
	Property	1.5	1.7
		6.7	8.2
Reinsurance	Property Treaty NA	0.8	0.9
	Property Treaty INT	0.4	0.5
	Casualty Treaty	1.1	1.3
	Marine XL	0.2	0.2
	Aviation XL	0.0	0.1
		2.5	3.0
UK	Employers'/Public Liability	1.1	1.0
	Professional Indemnity/D&O	0.3	0.3
	Motor	0.7	0.7
	Property and Commercial Combined (Packages)	1.7	1.6
		3.8	3.6
Other underwriting		0.1	0.2
Total		13.1	15.0

Subject to taxation, the impact on equity would be the same as that on profit following a change in the net claims ratio.

5 Segmental information

The reportable segments have been identified as follows:

The Global Markets strategic business unit which underwrites the Group's international and US business other than reinsurance. In the main, Global Markets deals with wholesale buyers of insurance, not individuals. Risks are large and usually syndicated by several underwriters – the subscription market.

The Reinsurance strategic business unit which underwrites reinsurance business which is essentially the insurance of insurance and reinsurance companies and includes providing non-proportional cover for major events such as earthquakes or hurricanes. These insurance and reinsurance companies calculate how much risk they want to bear and pass on the remaining exposure to reinsurers in return for a premium.

The UK strategic business unit which is developing business opportunities within the UK general commercial insurance markets through both wholesale and retail brokers and has opened offices in key locations across the UK.

'Other underwriting' which is made up of Excess of Loss reinsurance ceded from the strategic business units to a cell of Brit Insurance (Gibraltar) PCC Limited, Syndicate 389 (Life – final year of account 2003) and historic participations on external managed syndicates in run-off (final year of account 2000).

'Other corporate' which is made up of residual income and expenditure not allocated to other segments.

Foreign exchange differences on non-monetary items are separately disclosed. This provides a fairer representation of the claims ratios and financial performance of the SBUs which would otherwise be distorted by the mismatch arising from IFRSs whereby unearned premium, reinsurers share of unearned premium and deferred acquisition costs are treated as non-monetary items and the majority of other assets and liabilities are treated as monetary items. Non-monetary items are carried at historic exchange rates, while monetary items are translated at closing rates.

The Group investment return is managed centrally and an allocation is made to each of the strategic business units based on the average risk free interest rate for the period being applied to the insurance funds of each strategic business unit. The annualised average risk free rate applied to insurance funds was 1.65% for the year ended 31 December 2010 (31 December 2009: 1.66%).

Information regarding the Group's reportable segments is presented below.

Notes to the Financial Statements continued

5 Segmental information continued

a) Income statement by segment

12 months ended 31 December 2010

	Global Markets £m	Reinsurance £m	UK £m	Other underwriting £m	Intra Group £m	Total underwriting excluding the effect of foreign exchange on non-monetary items £m	Effect of foreign exchange on non-monetary items £m	Total underwriting after the effect of foreign exchange on non-monetary items £m	Other corporate £m	Total £m
Gross premiums written	778.3	309.6	441.2	12.2	(11.1)	1,530.2	–	1,530.2	–	1,530.2
Less premiums ceded to reinsurers	(143.2)	(61.2)	(58.1)	(0.4)	11.1	(251.8)	–	(251.8)	–	(251.8)
Premiums written, net of reinsurance	635.1	248.4	383.1	11.8	–	1,278.4	–	1,278.4	–	1,278.4
Gross earned premiums	809.7	311.6	439.5	14.2	(13.1)	1,561.9	(11.2)	1,550.7	–	1,550.7
Reinsurers' share	(136.7)	(61.9)	(63.3)	(0.4)	13.1	(249.2)	0.8	(248.4)	–	(248.4)
Earned premiums, net of reinsurance	673.0	249.7	376.2	13.8	–	1,312.7	(10.4)	1,302.3	–	1,302.3
Investment return	19.8	8.9	14.0	0.5	–	43.2	–	43.2	70.2	113.4
Return on derivative contracts	(0.1)	(1.2)	(0.5)	–	–	(1.8)	–	(1.8)	(0.1)	(1.9)
Loss on disposal of associated undertaking	–	–	–	–	–	–	–	–	(0.4)	(0.4)
Net foreign exchange gains	–	–	–	–	–	–	5.2	5.2	24.1	29.3
Total revenue	692.7	257.4	389.7	14.3	–	1,354.1	(5.2)	1,348.9	93.8	1,442.7
Gross claims incurred	(491.0)	(188.7)	(284.6)	(17.2)	16.8	(964.7)	–	(964.7)	–	(964.7)
Reinsurers' share	104.2	40.0	41.1	(0.4)	(16.8)	168.1	–	168.1	–	168.1
Claims incurred, net of reinsurance	(386.8)	(148.7)	(243.5)	(17.6)	–	(796.6)	–	(796.6)	–	(796.6)
Acquisition costs – commission	(203.7)	(43.7)	(82.0)	(0.1)	–	(329.5)	2.4	(327.1)	–	(327.1)
Acquisition costs – other	(33.7)	(11.5)	(22.7)	(1.1)	–	(69.0)	–	(69.0)	–	(69.0)
Other insurance related expenses	(33.9)	(16.3)	(27.2)	(1.5)	–	(78.9)	–	(78.9)	–	(78.9)
Other expenses	–	–	–	–	–	–	–	–	(38.9)	(38.9)
Total expenses excluding finance costs	(658.1)	(220.2)	(375.4)	(20.3)	–	(1,274.0)	2.4	(1,271.6)	(38.9)	(1,310.5)
Operating profit/(loss)	34.6	37.2	14.3	(6.0)	–	80.1	(2.8)	77.3	54.9	132.2
Finance costs										(14.0)
Share of loss of associated undertakings										(1.8)
Profit on ordinary activities before tax										116.4
Tax expense										(5.9)
Profit attributable to owners of the parent										110.5
Claims ratio	57.4%	59.6%	64.7%	127.6%		60.7%		61.2%		
Expense ratio	40.3%	28.6%	35.1%	19.6%		36.4%		36.4%		
Combined ratio	97.7%	88.2%	99.8%	147.2%		97.1%		97.6%		

Notes to the Financial Statements continued

5 Segmental information continued

12 months ended 31 December 2009

	Global Markets £m	Reinsurance £m	UK £m	Other underwriting £m	Intra Group £m	Total underwriting excluding the effect of foreign exchange on non-monetary items £m	Effect of foreign exchange on non-monetary items £m	Total underwriting after the effect of foreign exchange on non-monetary items £m	Other corporate £m	Total £m
Gross premiums written	875.3	364.2	455.4	16.5	(15.0)	1,696.4	–	1,696.4	–	1,696.4
Less premiums ceded to reinsurers	(116.8)	(57.4)	(64.9)	(0.9)	15.0	(225.0)	–	(225.0)	–	(225.0)
Premiums written, net of reinsurance	758.5	306.8	390.5	15.6	–	1,471.4	–	1,471.4	–	1,471.4
Gross earned premiums	944.4	354.5	430.1	16.4	(15.0)	1,730.4	(34.3)	1,696.1	–	1,696.1
Reinsurers' share	(124.5)	(56.9)	(67.7)	(0.8)	15.0	(234.9)	2.7	(232.2)	–	(232.2)
Earned premiums, net of reinsurance	819.9	297.6	362.4	15.6	–	1,495.5	(31.6)	1,463.9	–	1,463.9
Investment return	20.2	8.5	13.3	0.1	–	42.1	–	42.1	95.3	137.4
Return on derivative contracts	(2.3)	(2.2)	(0.3)	–	–	(4.8)	–	(4.8)	0.7	(4.1)
Disposal and partial disposal of associated undertaking	–	–	–	–	–	–	–	–	4.2	4.2
Other income	–	–	–	–	–	–	–	–	1.4	1.4
Total revenue	837.8	303.9	375.4	15.7	–	1,532.8	(31.6)	1,501.2	101.6	1,602.8
Gross claims incurred	(582.7)	(180.5)	(290.8)	(13.0)	12.7	(1,054.3)	–	(1,054.3)	–	(1,054.3)
Reinsurers' share	68.5	17.1	49.2	1.5	(12.7)	123.6	–	123.6	–	123.6
Claims incurred, net of reinsurance	(514.2)	(163.4)	(241.6)	(11.5)	–	(930.7)	–	(930.7)	–	(930.7)
Acquisition costs – commission	(220.2)	(51.6)	(73.9)	0.6	–	(345.1)	6.8	(338.3)	–	(338.3)
Acquisition costs – other	(29.6)	(9.3)	(18.1)	(1.6)	–	(58.6)	–	(58.6)	–	(58.6)
Other insurance related expenses	(31.0)	(13.5)	(27.6)	–	–	(72.1)	–	(72.1)	–	(72.1)
Other expenses	–	–	–	–	–	–	–	–	(39.5)	(39.5)
Net foreign exchange losses	–	–	–	–	–	–	(30.1)	(30.1)	(3.3)	(33.4)
Total expenses excluding finance costs	(795.0)	(237.8)	(361.2)	(12.5)	–	(1,406.5)	(23.3)	(1,429.8)	(42.8)	(1,472.6)
Operating profit/(loss)	42.8	66.1	14.2	3.2	–	126.3	(54.9)	71.4	58.8	130.2
Finance costs										(11.5)
Share of loss of associated undertakings										(2.3)
Profit on ordinary activities before tax										116.4
Tax expense										(28.9)
Profit attributable to owners of the parent										87.5
Claims ratio	62.7%	54.9%	66.7%	73.7%		62.2%		63.6%		
Expense ratio	34.2%	25.0%	33.0%	6.4%		31.8%		32.0%		
Combined ratio	96.9%	79.9%	99.7%	80.1%		94.0%		95.6%		

Notes to the Financial Statements continued

5 Segmental information continued

b) Statement of financial position by segment

As at 31 December 2010

	Global Markets £m	Reinsurance £m	UK £m	Other underwriting £m	Intra Group £m	Total underwriting excluding the effect of foreign exchange on non-monetary items £m	Effect of foreign exchange on non-monetary items £m	Total underwriting after the effect of foreign exchange on non-monetary items £m	Other corporate £m	Total £m
Reinsurance contracts	360.3	79.1	112.9	0.4	(33.5)	519.2	0.3	519.5	–	519.5
Intangible assets	19.1	2.1	55.1	–	–	76.3	–	76.3	5.5	81.8
Other assets	2,129.2	919.0	1,180.4	42.5	–	4,271.1	1.1	4,272.2	31.0	4,303.2
Total assets	2,508.6	1,000.2	1,384.4	42.9	(33.5)	4,866.6	1.4	4,868.0	36.5	4,904.5
Insurance contracts	1,751.3	756.2	971.2	35.0	(33.5)	3,480.2	5.1	3,485.3	–	3,485.3
Other liabilities	125.4	54.2	69.6	2.5	–	251.7	–	251.7	195.9	447.6
Total liabilities	1,876.7	810.4	1,040.8	37.5	(33.5)	3,731.9	5.1	3,737.0	195.9	3,932.9

As at 31 December 2009

	Global Markets £m	Reinsurance £m	UK £m	Other underwriting £m	Intra Group £m	Total underwriting excluding the effect of foreign exchange on non-monetary items £m	Effect of foreign exchange on non-monetary items £m	Total underwriting after the effect of foreign exchange on non-monetary items £m	Other corporate £m	Total £m
Reinsurance contracts	363.9	68.0	116.0	1.5	(26.0)	523.4	0.1	523.5	–	523.5
Intangible assets	18.8	2.1	55.1	–	–	76.0	–	76.0	5.2	81.2
Other assets	2,160.5	828.5	1,170.5	35.1	–	4,194.6	0.2	4,198.8	1.8	4,196.6
Total assets	2,543.2	898.6	1,341.6	36.6	(26.0)	4,794.0	0.3	4,794.3	7.0	4,801.3
Insurance contracts	1,784.2	684.3	966.8	28.9	(26.0)	3,438.2	1.2	3,439.4	–	3,439.4
Other liabilities	103.8	39.8	56.3	1.7	–	201.6	–	201.6	265.7	467.3
Total liabilities	1,888.0	724.1	1,023.1	30.6	(26.0)	3,639.8	1.2	3,641.0	265.7	3,906.7

c) Depreciation, amortisation, impairment and capital expenditure by segment

Year ended 31 December 2010

	Global Markets £m	Reinsurance £m	UK £m	Other corporate £m	Total £m
Depreciation of property, plant and equipment	1.4	0.4	0.6	1.1	3.5
Amortisation of intangibles	1.7	0.5	0.7	1.2	4.1
Impairment of property, plant and equipment	0.1	–	0.1	0.1	0.3
Impairment of intangibles	0.3	0.1	0.1	0.2	0.7
Capital expenditure	4.0	0.6	3.5	1.6	9.7

Year ended 31 December 2009

	Global Markets £m	Reinsurance £m	UK £m	Other corporate £m	Total £m
Depreciation of property, plant and equipment	1.2	0.3	0.5	0.9	2.9
Amortisation of intangibles	1.7	0.5	0.7	1.3	4.2
Impairment of intangibles	0.9	0.3	0.4	0.6	2.2
Capital expenditure	1.6	0.5	3.3	1.1	6.5

Notes to the Financial Statements continued

5 Segmental information continued

d) Geographical information

The Group's strategic business units operate mainly in four geographical areas, though the business is managed on a worldwide basis.

The segmental split shown below is based on the location of the underlying risk.

Gross premiums written

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
United Kingdom	523.7	491.0
Europe (excluding UK)	84.4	128.7
United States	343.6	416.2
Other (including worldwide)	578.5	660.5
	1,530.2	1,696.4

All non-current assets of the Group are located in the United Kingdom.

6 Investment return

	Year ended 31 December 2010				Year ended 31 December 2009			
	Investment income £m	Net realised gains/(losses) £m	Net unrealised gains £m	Total investment return £m	Investment income £m	Net realised gains £m	Net unrealised gains/(losses) £m	Total investment return £m
Equity securities	3.6	7.0	7.0	17.6	2.4	6.7	4.7	13.8
Debt securities	93.3	(13.3)	–	80.0	81.2	6.6	4.7	92.5
Specialised investment funds	4.1	(16.1)	23.3	11.3	2.6	(12.3)	27.6	17.9
Cash and cash equivalents	4.5	–	–	4.5	13.2	–	–	13.2
	105.5	(22.4)	30.3	113.4	99.4	1.0	37.0	137.4

7 Return on derivative contracts

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Currency forwards	0.1	1.1
Catastrophe swap contracts	(1.8)	(4.8)
Credit derivatives, warrants and weather derivatives	(0.2)	(0.4)
	(1.9)	(4.1)

Notes to the Financial Statements continued

8 Disposal of associated undertakings

On 7 December 2010, the Group sold its 20.3% holding of ordinary shares and 21.6% holding of preference shares in RI3K Limited.

Assets disposed of and related sales proceeds during 2010 were as follows:

	RI3K Limited £m
Proceeds	0.7
Carrying value of Group holding in associated undertaking	(1.1)
Loss on disposal	(0.4)

On 26 March 2009, Norton II Holdings Limited was placed in members' voluntary liquidation in order to return capital to investors.

Assets disposed of and related sales proceeds during 2009 were as follows:

	Norton II Holdings Limited £m
Proceeds	15.4
Carrying value of Group holding in associated undertaking	(15.4)
Reversal of translation reserve	4.2
Profit on disposal	4.2

9 Net foreign exchange gains/(losses)

The Group recognised foreign exchange gains of £29.3m (31 December 2009: loss of £33.4m) in the income statement in the period.

Foreign exchange gains and losses result from the translation of the balance sheet to closing exchange rates and the income statement to average exchange rates. However, as an exception to this, International Accounting Standard 21 'The Effects of Changes in Foreign Exchange Rates' requires that net unearned premiums

and deferred acquisition costs (UPR/DAC), being non-monetary items, remain at historic exchange rates. This creates a foreign exchange mismatch, the financial effects of which are shown in the table below.

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Gains/(losses) on foreign exchange arising from:		
Translation of the balance sheet and income statement	24.1	(3.3)
Maintaining UPR/DAC items in the balance sheet at historic rates	(2.8)	(54.9)
Maintaining UPR/DAC items in the income statement at historic rates	8.0	24.8
Net foreign exchange gains/(losses)	29.3	(33.4)

Included within foreign exchange gains/(losses) are exchange gains of £20.6m (2009: losses of £103.6m) arising on the retranslation of monetary items that are classified as fair value through profit or loss.

Principal exchange rates applied are set out in the table below.

	Year ended 31 December 2010		Year ended 31 December 2009	
	Average	Closing	Average	Closing
US dollar	1.55	1.57	1.57	1.61
Canadian dollar	1.59	1.56	1.78	1.69
Euro	1.17	1.17	1.12	1.13

In accordance with International Accounting Standard 1 'Presentation of Financial Statements', exchange gains and losses are presented on a net basis.

They are reported within revenue where they result in a net gain and within expenses where they result in a net loss.

Notes to the Financial Statements continued

10 Acquisition costs and other operating expenses

	Year ended 31 December 2010			Year ended 31 December 2009		
	Acquisition costs £m	Other operating expenses £m	Total £m	Acquisition costs £m	Other operating expenses £m	Total £m
Staff costs (Note 11)	28.2	52.7	80.9	27.6	45.3	72.9
Other staff related costs	0.4	15.2	15.6	0.5	15.9	16.4
Accommodation costs	4.5	5.0	9.5	4.3	4.2	8.5
Legal and professional charges	4.3	9.0	13.3	4.1	12.0	16.1
Investment management expenses	–	3.8	3.8	–	3.5	3.5
IT costs	–	8.3	8.3	–	8.3	8.3
Travel and entertaining	2.1	1.3	3.4	2.2	0.8	3.0
Marketing and communications	0.1	6.2	6.3	0.2	3.9	4.1
Amortisation and impairment of intangible assets	–	4.8	4.8	–	6.4	6.4
Depreciation and impairment of property, plant and equipment	–	3.8	3.8	–	2.9	2.9
Regulatory levies and charges	27.8	–	27.8	18.9	–	18.9
Other	1.2	7.7	8.9	1.3	8.4	9.7
Movement on insurance related acquisition cost deferral	0.4	–	0.4	(0.5)	–	(0.5)
Expenses before commissions	69.0	117.8	186.8	58.6	111.6	170.2
Commission costs	327.1	–	327.1	338.3	–	338.3
Total expenses	396.1	117.8	513.9	396.9	111.6	508.5

11 Staff costs

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Wages and salaries	65.9	57.8
Social security costs	7.4	6.0
Pension costs	7.6	9.1
	80.9	72.9

The average monthly number of employees during the year, including Executive Directors, was as follows:

	Year ended 31 December 2010 Number	Year ended 31 December 2009 Number
Management	32	32
Administration	319	311
Underwriting and claims	410	391
	761	734

The majority of employees work outside of the Netherlands.

12 Finance costs

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Revolving credit facility and other bank borrowings	4.9	2.0
US dollar floating rate unsecured subordinated loan notes	–	0.4
Lower Tier Two subordinated debt	9.1	9.1
Total finance costs	14.0	11.5

Notes to the Financial Statements continued

13 Auditor's remuneration

	Year ended 31 December 2010				
	Audit of the financial statements £m	Audit related fees £m	Tax advisory £m	All other services £m	Total £m
Fees payable to the Group's auditor for the audit of the Group's annual accounts	0.3	–	–	–	0.3
Fees payable to the Group's auditor and its associates for other services:					
The audit of the Group's subsidiaries pursuant to legislation	0.6	–	–	–	0.6
	0.9	–	–	–	0.9
Other services pursuant to legislation	–	0.2	–	–	0.2
Other services relating to taxation	–	–	0.1	–	0.1
Valuation and actuarial services	–	–	–	0.3	0.3
	0.9	0.2	0.1	0.3	1.5
	Year ended 31 December 2009				
	Audit of the financial statements £m	Audit related fees £m	Tax advisory £m	All other services £m	Total £m
Fees payable to the Group's auditor for the audit of the Group's annual accounts	0.3	–	–	–	0.3
Fees payable to the Group's auditor and its associates for other services:					
The audit of the Group's subsidiaries pursuant to legislation	0.4	–	–	–	0.4
	0.7	–	–	–	0.7
Other services pursuant to legislation	–	1.1	–	–	1.1
Other services relating to taxation	–	–	0.1	–	0.1
Valuation and actuarial services	–	–	–	0.2	0.2
Services relating to corporate finance transactions entered into or proposed to be entered into by or on behalf of the Company or any of its associates	–	0.2	–	–	0.2
Other	–	0.2	–	–	0.2
	0.7	1.5	0.1	0.2	2.5

Of the other services pursuant to legislation, £nil (2009: £0.9m) relates to services provided to the Group as required by the Listing Rules and Prospectus Rules.

Notes to the Financial Statements continued

14 Tax expense

(i) Tax (charged)/credited to income statement

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Current tax:		
Current taxes on income for the year		
United Kingdom	(19.4)	(37.9)
United States	(10.2)	(6.6)
	(29.6)	(44.5)
Double tax relief	8.1	–
Adjustments in respect of prior years	10.0	5.8
Total current tax	(11.5)	(38.7)
Deferred tax:		
Relating to the origination and reversal of temporary differences	3.2	9.9
Relating to changes in tax rates	0.6	–
Adjustments in respect of prior years	1.8	(0.1)
Total deferred tax (Note 27)	5.6	9.8
Total tax charged to income statement	(5.9)	(28.9)

Tax relating to associated companies of £0.3m (2009: £nil) has been credited to the income statement within the Group's share of loss after tax of associated undertakings.

United States tax and the double tax relief principally arise from taxes suffered as a result of the Group's operations at Lloyd's. Double tax relief is effectively limited to an amount equal to the tax due at the UK tax rate on the same source of income.

(ii) Tax (charged)/credited to other comprehensive income

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Deferred tax on actuarial gains/(losses) on defined benefit pension scheme	(2.2)	0.7

(iii) Tax reconciliation

Based on the analysis of Group profits the weighted average rate of tax is 10.88% (2009: 25.6%). The tax on the Group's profits before tax differs from the theoretical amount that would arise based on the weighted average rate of tax as follows:

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Profit on ordinary activities before tax	116.4	116.4
Tax calculated at weighted average rate of tax on income	(12.7)	(29.8)
Expenses not deductible for tax purposes	(2.4)	(2.4)
Equity dividends not subject to corporation tax	1.7	0.1
Taxes on income at rates in excess of the domestic rate and where credit is unavailable	(2.2)	(5.3)
Profit on sale and unrealised gain on substantial shareholdings	–	0.4
Effect of temporary differences not recognised	(2.1)	3.0
Tax effect of share of results of associated undertakings	(0.5)	(0.6)
Deferred tax effect of change in the rate of tax	0.5	–
Other adjustments to tax charge in respect of prior years	11.8	5.7
	(5.9)	(28.9)

The weighted average rate of tax is based on the geographic split of Group profit across entities in jurisdictions with differing tax rates. As the mix of taxable profits changes so will the weighted average rate of tax.

The adjustment to tax charge in respect of prior years relates to the finalisation of some outstanding matters with Revenue authorities.

(iv) Effect of post balance sheet rate changes

The UK Government has announced proposals to reduce the rate of corporate taxation over the next five years. The proposals are as yet not fully enacted. The Group estimates the long-term benefit of the reduction in tax rate in respect of future taxes already provided for (deferred tax) will be no more than £1.0m.

The Government of Gibraltar has enacted a range of measures reforming the tax legislation in the territory the result of which will be to broaden the tax base of companies incorporated in Gibraltar and enacting a rate of 10% from 1 January 2011. This rate change will have no effect on the profits of the Group for 2010 or prior.

Notes to the Financial Statements continued

15 Earnings and net assets per share

Basic and diluted earnings per share are as follows:

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Profit on ordinary activities after tax	110.5	87.5
	Year ended 31 December 2010 Number in millions	Year ended 31 December 2009 Number in millions (restated)
Basic weighted average number of shares	77.6	77.3
Employee share options	–	–
Diluted weighted average number of shares	77.6	77.3
Basic earnings per share (pence per share)	142.4	113.2
Diluted earnings per share (pence per share)	142.4	113.2
Net assets and net tangible assets per share are as follows:		
	31 December 2010 £m	31 December 2009 £m
Net assets	971.6	894.6
Intangible assets	(81.8)	(81.2)
Net tangible assets	889.8	813.4
	31 December 2010 Number in millions	31 December 2009 Number in millions (restated)
Number of shares in issue at end of period	79.2	78.5
Own shares	(1.2)	(1.2)
Number of shares in issue less own shares	78.0	77.3
Net assets per share (pence per share)	1,245.6	1,156.8
Net tangible assets per share (pence per share)	1,140.8	1,052.0

16 Property, plant and equipment

	Office refurbishment £m	Computers and office machinery, furniture and equipment £m	Total £m
Cost:			
At 1 January 2009	9.8	6.9	16.7
Additions	0.1	0.9	1.0
Disposals	–	(0.1)	(0.1)
At 31 December 2009	9.9	7.7	17.6
At 1 January 2010	9.9	7.7	17.6
Additions	2.9	1.4	4.3
Disposals	(0.3)	(0.9)	(1.2)
At 31 December 2010	12.5	8.2	20.7
Depreciation:			
At 1 January 2009	4.4	4.3	8.7
Charge for the year	1.8	1.1	2.9
At 31 December 2009	6.2	5.4	11.6
At 1 January 2010	6.2	5.4	11.6
Charge for the year	2.4	1.1	3.5
Impairment	0.1	0.2	0.3
Disposals	(0.3)	(0.9)	(1.2)
At 31 December 2010	8.4	5.8	14.2
Carrying amount:			
At 31 December 2009	3.7	2.3	6.0
At 31 December 2010	4.1	2.4	6.5

The gross cost of property, plant and equipment fully depreciated but still in use is £3.8m (2009: £2.3m).

The depreciation charge for the year is included in 'Other operating expenses' in the income statement.

During the year, various items of property, plant and equipment were impaired down to a recoverable amount of £nil. This was mainly due to a regional support office relocating to new offices and resulted in a charge of £0.3m. Further information is given in Note 5c.

Notes to the Financial Statements continued

17 Intangible assets

	Goodwill £m	Syndicate participations £m	Software £m	Total £m
Cost:				
At 1 January 2009	72.3	9.0	29.7	111.0
Additions	–	–	5.5	5.5
Disposals	–	–	(2.5)	(2.5)
At 31 December 2009	72.3	9.0	32.7	114.0
At 1 January 2010	72.3	9.0	32.7	114.0
Additions	–	–	5.4	5.4
Disposals	–	–	(0.9)	(0.9)
At 31 December 2010	72.3	9.0	37.2	118.5
Amortisation:				
At 1 January 2009	8.6	9.0	11.3	28.9
Charge for the year	–	–	4.2	4.2
Impairment	–	–	2.2	2.2
Disposals	–	–	(2.5)	(2.5)
At 31 December 2009	8.6	9.0	15.2	32.8
At 1 January 2010	8.6	9.0	15.2	32.8
Charge for the year	–	–	4.1	4.1
Impairment	–	–	0.7	0.7
Disposals	–	–	(0.9)	(0.9)
At 31 December 2010	8.6	9.0	19.1	36.7
Carrying amount:				
At 31 December 2009	63.7	–	17.5	81.2
At 31 December 2010	63.7	–	18.1	81.8

The gross cost of software fully amortised but still in use is £9.1m (2009: £6.4m).

All software additions in 2010 and 2009 are internally developed.

The amortisation charge for the year is included in 'Other operating expenses' in the income statement.

During the year, various software systems were impaired down to a recoverable amount of £nil. This was due to those software systems not being put into service and resulted in a charge of £0.7m. Further information is given in Note 5c.

Impairment tests for goodwill

Goodwill is reviewed annually for impairment and has been allocated to individual cash-generating units (CGUs) as follows:

	31 December 2010 £m	31 December 2009 £m
UK strategic business unit	52.0	52.0
Global Markets strategic business unit	11.7	11.7
	63.7	63.7

The recoverable amount of each CGU has been determined using a value in use calculation.

Notes to the Financial Statements continued

17 Intangible assets continued

Each value in use calculation uses cash flow projections based on business plans approved by senior management covering a three year period and subsequent cash flows which assume a nil growth rate. These cash flows have been discounted using a risk adjusted discount rate of 11.3% (2009: 11.3%). In each goodwill impairment review, the recoverable amount significantly exceeds the carrying value of the CGU including its associated goodwill and it is considered that a reasonably possible change in key assumptions will not cause the carrying value of the CGU to exceed its recoverable amount.

The key assumptions used for the impairment calculations were:

Cash flows and profit levels will mainly depend on the level of premiums written by each strategic business unit, the rates at which these premiums are written and the claims activity on both prior and future underwriting years. The business plans reflect senior management's best estimates based on historical experience, growth rates for the respective insurance industry sector, the insurance pricing cycle and expected results from ongoing and future strategic business unit product and distribution strategies.

Forecast investment returns are based on risk free interest rates being applied to strategic business unit insurance funds which is the method of allocating investment returns to strategic business units.

Commissions and other insurance related expenses are assumed to remain materially in line with current amounts relative to premium levels.

18 Deferred acquisition costs

	31 December 2010 £m	31 December 2009 £m
At 1 January	162.4	152.1
Costs deferred during the year	165.3	164.5
Amortisation charge for the year	(161.0)	(154.2)
At 31 December	166.7	162.4

19 Investments in associated undertakings

The following companies have been designated as associated undertakings due to the significant influence resulting from a combination of shareholding and board representation.

RI3K Limited

RI3K Limited ceased to be an associated undertaking during the year. For further information see Note 8.

Xbridge Limited

The Group owns 38.4% of the ordinary share capital of Xbridge Limited and has a Director on its Board.

The Group has granted Xbridge Limited a five year loan facility of up to £6.0m. As at 31 December 2010, £5.2m of this amount had been drawn down.

Xbridge Limited is an unlisted company registered in England and Wales. Its accounting reference date is 31 December.

The company's principal activity is online insurance and finance technology.

Verex Limited

The Group owns 35.3% of the ordinary share capital of Verex Limited.

The Group has entered into a contract to subscribe for up to £6.0m of Verex Limited loan notes. As at 31 December 2010, £6.0m of these loan notes had been subscribed for.

Verex Limited is an unlisted company registered in England and Wales. Its accounting reference date is 31 December.

The company provides vehicle manufacturer affinity motor insurance, accident management, network management and related products and services, back office support and administration to vehicle manufacturers, their dealers and associated body shops.

Notes to the Financial Statements continued

19 Investments in associated undertakings continued

The movements in the Group's investments in associated undertakings were as follows:

	RI3K Limited 2010 £m	Xbridge Limited 2010 £m	Verex Limited 2010 £m	Total 2010 £m	Total 2009 £m
At 1 January	1.7	10.9	2.7	15.3	29.1
Share of (loss)/profit after tax in the year	(0.8)	0.2	(1.2)	(1.8)	(2.3)
Effect of associates' capital movements	0.2	0.1	–	0.3	–
Movements in loan and preference share balances	–	0.2	2.4	2.6	3.8
Foreign exchange revaluation	–	–	–	–	0.1
Disposal of associated undertaking	(1.1)	–	–	(1.1)	(15.4)
At 31 December	–	11.4	3.9	15.3	15.3

The carrying value is made up as follows:

	Xbridge Limited 2010 £m	Verex Limited 2010 £m	Total 2010 £m	Total 2009 £m
Share of net liabilities	(2.1)	(2.7)	(4.8)	(6.3)
Goodwill arising on acquisition	8.5	–	8.5	10.2
Preference shares and loans	5.0	6.6	11.6	11.4
	11.4	3.9	15.3	15.3

The summary income statement and statement of financial position of the companies which were associated undertakings as at 31 December 2010 were as follows:

	Xbridge Limited 2010 £m	Verex Limited 2010 £m
Income statement		
Income	4.4	1.5
Profit/(loss) on ordinary activities before tax	0.4	(4.2)
Tax credit on loss	–	0.9
Profit/(loss) on ordinary activities after tax	0.4	(3.3)
Statement of financial position		
Current assets	7.6	1.0
Non-current assets	0.6	3.0
Total assets	8.2	4.0
Current liabilities	(6.8)	(0.9)
Non-current liabilities	(6.8)	(10.7)
Total liabilities	(13.6)	(11.6)
Net liabilities	(5.4)	(7.6)

Notes to the Financial Statements continued

20 Insurance and reinsurance contracts

(i) Balances on insurance and reinsurance contracts

	31 December 2010 £m	31 December 2009 £m
Gross		
Insurance contracts		
Claims reported and loss adjustment expenses	1,585.1	1,511.7
Claims incurred but not reported	1,233.4	1,240.4
	2,818.5	2,752.1
Unearned premiums	666.8	687.3
Total insurance contracts	3,485.3	3,439.4
Recoverable from reinsurers		
Reinsurance contracts		
Claims reported and loss adjustment expenses	265.8	284.5
Claims incurred but not reported	198.0	188.3
Impairment provision	(10.8)	(12.4)
	453.0	460.4
Unearned premiums	66.5	63.1
Total reinsurance contracts	519.5	523.5
Net		
Claims reported and loss adjustment expenses	1,319.3	1,227.2
Claims incurred but not reported	1,035.4	1,052.1
Impairment provision	10.8	12.4
	2,365.5	2,291.7
Unearned premiums	600.3	624.2
Net insurance and reinsurance contracts	2,965.8	2,915.9

Insurance contracts – assumptions and changes in assumptions

Process used to decide on assumptions required

The risks associated with these insurance contracts and in particular with casualty insurance contracts are complex and subject to a number of variables that complicate quantitative sensitivity analysis.

The Group uses several statistical methods to incorporate the various assumptions made in order to estimate the ultimate costs of claims. The two methods more commonly used are the chain-ladder and the Bornhuetter-Ferguson methods.

Notes to the Financial Statements continued

20 Insurance and reinsurance contracts continued

Chain-ladder methods may be applied to premiums, paid claims or incurred claims (i.e. paid claims plus case estimates). The basic technique involves the analysis of historical claims development factors and the selection of estimated development factors based on this historical pattern. The selected development factors are then applied to cumulative claims data for each underwriting year that is not yet fully developed to produce an estimated ultimate claims cost for each underwriting year.

Chain-ladder techniques are most appropriate for mature classes of business that have a relatively stable development pattern. Chain-ladder techniques are less suitable in cases in which the insurer does not have a developed claims history for a particular class of business.

The Bornhuetter-Ferguson method uses a combination of a benchmark or market-based estimate and an estimate based on claims experience. The former is based on a measure of exposure such as premiums; the latter is based on the paid or incurred claims to date. The two estimates are combined using a formula that gives more weight to the experience-based estimate as time passes. This technique is used in situations in which developed claims experience is not available for the projection (recent underwriting years or new classes of business).

The choice of selected results for each year of each class of business depends on an assessment of the technique that has been most appropriate to observed historical developments. In certain instances, this has meant that different techniques or combination of techniques have been selected for the individual underwriting year or groups of underwriting years within the same class of business.

Claims for a number of classes of business, including Financial Risk, Mortgage Indemnity Guarantee, Catastrophe Retrocession and Casualty Treaty, do not always conform to the statistical distribution expected. For these classes claims reserves are additionally reviewed on a policy by policy basis by underwriters and claims managers and these reviews take account of market intelligence in addition to notified claims.

In addition to the estimation of claims reserves certain estimates are produced for unearned premiums. For open market business earned premium is calculated at policy level. However, premium derived from delegated underwriting authorities is calculated by applying the 1/144ths method to estimated premiums applied to the master policy. This assumes that attachments to master policies arise evenly throughout the period of that master policy.

Reinsurance outwards premiums are earned according to the nature of the cover. 'Losses occurring during' policies are earned evenly over the policy period. 'Risks attaching' policies are earned on the same basis as the inwards business being protected.

Changes in assumptions

The Group did not change its estimation techniques for the insurance contracts disclosed in this note during the year.

Claims development tables

The tables below show the development of claims over a period of time on a gross and net of reinsurance basis.

The claims development tables have been presented on an underwriting year basis.

The tables show the cumulative incurred claims, including both notified and IBNR claims, for each successive underwriting year at the end of each year, together with cumulative paid claims as at the end of the current year.

The claims have been adjusted to make them comparable on a year by year basis.

They have been grossed up to include 100% of the managed syndicate claims rather than the claims that reflects the Brit Insurance percentage ownership of each syndicate's capacity during the respective underwriting years.

In addition, claims in currencies other than Sterling have been retranslated at 31 December 2010 exchange rates.

Notes to the Financial Statements continued

20 Insurance and reinsurance contracts continued

Ultimate gross claims

	2001 and prior years £m	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m	Intra Group and other underwriting adjustments £m	Total £m
At end of underwriting year	2,144.0	358.2	601.0	841.6	1,341.2	826.8	1,022.1	1,072.6	972.2	922.8		
One year later	2,202.1	356.6	568.6	797.8	1,376.5	840.2	1,091.5	1,177.2	1,011.5			
Two years later	2,227.4	343.8	512.9	758.4	1,390.7	836.5	1,101.4	1,207.5				
Three years later	2,229.3	342.9	487.0	740.3	1,363.8	805.0	1,117.3					
Four years later	2,236.3	327.3	476.3	721.3	1,334.7	774.9						
Five years later	2,192.6	321.2	465.1	707.0	1,303.6							
Six years later	2,205.9	318.9	451.2	688.8								
Seven years later	2,198.5	318.6	435.8									
Eight years later	2,196.5	314.5										
Nine years later	2,170.9											
Total ultimate gross claims at 31 December 2010	2,170.9	314.5	435.8	688.8	1,303.6	774.9	1,117.3	1,207.5	1,011.5	922.8	–	9,947.6
Less accumulated gross paid claims	(2,041.3)	(289.6)	(375.5)	(603.6)	(1,163.9)	(538.6)	(649.7)	(586.0)	(340.0)	(67.4)	–	(6,655.6)
Unearned portion of gross ultimate claims	0.0	0.0	0.0	(0.1)	(1.5)	(3.4)	(4.3)	(2.8)	(40.4)	(466.7)	–	(519.2)
Claims handling provision	1.6	0.3	0.9	1.4	2.4	4.0	7.2	10.4	10.1	5.8	–	44.1
Outstanding gross claims at 31 December 2010	131.2	25.2	61.2	86.5	140.6	236.9	470.5	629.1	641.2	394.5	–	2,816.9
Other corporate adjustments	–	–	–	–	–	–	–	–	–	–	1.6	1.6
Total outstanding gross claims at 31 December 2010	131.2	25.2	61.2	86.5	140.6	236.9	470.5	629.1	641.2	394.5	1.6	2,818.5
Ultimate movement in gross claims during 2010 calendar year	(25.6)	(4.1)	(15.4)	(18.2)	(31.1)	(30.1)	15.9	30.3	39.3	–	–	(39.0)
of which relates to re-estimation of ultimate premium	1.7	0.0	0.2	(1.3)	(0.6)	0.1	(1.3)	5.9	(1.3)	–	–	3.4
of which relates to re-estimation of gross ultimate claims	(27.3)	(4.1)	(15.6)	(16.9)	(30.5)	(30.2)	17.2	24.4	40.6	–	–	(42.4)

Notes to the Financial Statements continued

20 Insurance and reinsurance contracts continued

Ultimate net claims

	2001 and prior years £m	2002 £m	2003 £m	2004 £m	2005 £m	2006 £m	2007 £m	2008 £m	2009 £m	2010 £m	Intra Group and other underwriting adjustments £m	Total £m
At end of underwriting year	1,417.6	302.2	545.6	711.6	945.4	738.3	882.4	912.3	835.3	780.4		
One year later	1,494.6	297.1	503.4	626.7	944.0	765.3	930.1	1,011.6	844.9			
Two years later	1,512.3	279.1	443.8	592.1	951.7	741.2	949.5	1,025.2				
Three years later	1,504.1	262.2	422.6	582.9	926.4	714.3	945.1					
Four years later	1,507.7	254.5	401.4	568.0	900.5	692.2						
Five years later	1,484.0	248.9	384.3	553.8	873.2							
Six years later	1,491.8	242.8	370.7	540.4								
Seven years later	1,478.9	242.0	358.8									
Eight years later	1,470.3	237.8										
Nine years later	1,454.8											
Total ultimate net claims at 31 December 2010	1,454.8	237.8	358.8	540.4	873.2	692.2	945.1	1,025.2	844.9	780.4	–	7,752.8
Less accumulated net paid claims	(1,373.7)	(218.2)	(314.3)	(472.7)	(750.5)	(489.6)	(567.4)	(494.8)	(290.4)	(57.4)	–	(5,029.0)
Unearned portion of net ultimate claims	0.0	0.0	0.0	(0.1)	(1.5)	(3.4)	(4.3)	(2.8)	(34.8)	(398.1)	–	(445.0)
Claims handling provision	1.6	0.3	0.9	1.4	2.4	4.0	7.2	10.4	10.1	5.8	–	44.1
Bad debt provision	1.3	0.2	0.4	0.4	1.2	0.9	2.6	1.7	1.4	0.7	–	10.8
Outstanding net claims at 31 December 2010	84.0	20.1	45.8	69.4	124.8	204.1	383.2	539.7	531.2	331.4	–	2,333.7
Other corporate adjustments	–	–	–	–	–	–	–	–	–	–	31.8	31.8
Total outstanding net claims at 31 December 2010	84.0	20.1	45.8	69.4	124.8	204.1	383.2	539.7	531.2	331.4	31.8	2,365.5
Ultimate movement in net claims during 2010 calendar year	(15.5)	(4.2)	(11.9)	(13.4)	(27.3)	(22.1)	(4.4)	13.6	9.6	–	–	(75.6)
of which relates to re-estimation of ultimate premium	(4.3)	0.0	0.4	(0.7)	(0.7)	(0.6)	(3.9)	3.2	(12.6)	–	–	(19.2)
of which relates to re-estimation of ultimate net claims	(11.2)	(4.2)	(12.3)	(12.7)	(26.6)	(21.5)	(0.5)	10.4	22.2	–	–	(56.4)

Notes to the Financial Statements continued

20 Insurance and reinsurance contracts continued

Material surpluses released

The net aggregate reserve releases from prior years amounted to £72.4m (2009: £81.2m). In part this arises from the Group's reserving philosophy which aims to make the most recent years, with the greatest uncertainty of result, prudently reserved leaving a potential for subsequent release.

This differs from the £56.4m stated in the table above as the table above is on an underwriting year basis and the surpluses in this narrative are on an annually accounted basis. The reconciling items are the 2009 underwriting year not being fully earned and the Chile and New Zealand earthquake losses which are 2010 accident year losses but relate to 2008 to 2010 underwriting year policies.

Releases have been made in the Global Markets strategic business unit of £9.6m (2009: £13.8m), Reinsurance strategic business unit of £25.0m (2009: £24.1m) and UK strategic business unit of £39.0m (2009: £41.2m) and a strengthening has been made in Other Underwriting of £1.2m (2009: release of £2.1m).

(ii) Movements in insurance and reinsurance contracts

a) Claims and loss adjustment expenses

	31 December 2010			31 December 2009		
	Gross £m	Reinsurance £m	Net £m	Gross £m	Reinsurance £m	Net £m
As at 1 January	2,752.1	(460.4)	2,291.7	2,657.7	(479.2)	2,178.5
Cash paid for claims settled in the year	(926.2)	181.6	(744.6)	(792.2)	110.8	(681.4)
Increase in liabilities	964.7	(168.1)	796.6	1,054.3	(123.6)	930.7
Net foreign exchange differences	27.9	(6.1)	21.8	(167.7)	31.6	(136.1)
As at 31 December	2,818.5	(453.0)	2,365.5	2,752.1	(460.4)	2,291.7

b) Unearned premiums

	31 December 2010			31 December 2009		
	Gross £m	Reinsurance £m	Net £m	Gross £m	Reinsurance £m	Net £m
As at 1 January	687.3	(63.2)	624.1	687.0	(70.4)	616.6
Premiums written in the year	1,530.2	(251.8)	1,278.4	1,696.4	(225.0)	1,471.4
Premiums earned during the year	(1,550.7)	248.5	(1,302.2)	(1,696.1)	232.2	(1,463.9)
As at 31 December	666.8	(66.5)	600.3	687.3	(63.2)	624.1

21 Employee benefits

The Group has the following pension schemes in operation:

(i) Brit Group Services Limited – Defined Benefit Pension Scheme

The Group operates a funded pension plan providing benefits for its employees based on final pensionable salaries.

The assets of the scheme are held in a separate trustee administered fund. This scheme closed to new entrants on 4 October 2001.

In July 2010, the UK Government announced its intention that future statutory minimum pension indexation would be measured by the Consumer Prices Index, rather than the Retail Prices Index. This has been reflected in the Group's assumptions and a gain of £1.1m has been recognised as a result, included in 'actuarial gains/(losses)' on assumptions in the figures below.

The scheme is subject to a formal actuarial valuation every three years and the results of the valuation carried out as at 31 July 2009 were updated to the accounting date by an independent qualified actuary in accordance with International Accounting Standard 19 'Employee Benefits' (IAS 19). As required by IAS 19, the value of the defined benefit obligations and current service cost have been measured using the projected unit credit method.

Notes to the Financial Statements continued

21 Employee benefits continued

The following table sets out the key IAS 19 assumptions used for the scheme.

	31 December 2010 %	31 December 2009 %	31 December 2008 %
Retail price inflation	3.50	3.60	2.90
Consumer price inflation	3.00	n/a	n/a
Discount rate	5.40	5.60	6.40
Pension increases in payment	3.40	3.50	2.90
General salary increases	5.00	5.10	4.90
Life expectancy of a pensioner aged 60 at the date of the statement of financial position			
Male	26.3 years	26.2 years	26.8 years
Female	28.6 years	28.5 years	29.2 years
Life expectancy of a member retiring at age 60 in 20 years' time			
Male	28.4 years	28.3 years	28.1 years
Female	29.8 years	29.8 years	30.3 years

The expected rate of return on assets has been derived by taking the weighted average of the long-term expected rate of return on each of the asset classes at the start of each year.

The expected returns for individual asset classes at the start of each year were as follows:

	31 December 2010 %	31 December 2009 %	31 December 2008 %
Equities	8.00	7.40	7.60
Corporate Bonds	5.30	5.00	5.00
Gilts	4.20	3.60	4.20
Cash	4.40	3.80	4.40
Weighted average expected return	6.80	6.00	6.60

The amount included in the statement of financial position arising from the Group's defined benefit pension scheme is as follows:

	31 December 2010 %	31 December 2009 %	31 December 2008 %
Present value of defined benefit obligations	(105.2)	(100.7)	(84.1)
Fair value of scheme assets	114.8	96.6	82.7
Net employee benefit assets/(obligations)	9.6	(4.1)	(1.4)

The amounts recognised in the income statement were as follows:

	31 December 2010 £m	31 December 2009 £m
Current service cost	1.2	1.2
Interest cost	5.6	5.3
Past service cost	—	0.1
Expected return on scheme assets	(6.6)	(4.9)
Total expense recognised in the income statement	0.2	1.7

The above charges have been recognised in the acquisition costs and other operating expenses lines of the income statement.

The actual return on the scheme's assets over the year was a gain of £15.9m (2009: £16.3m).

Notes to the Financial Statements continued

21 Employee benefits continued

The allocation of the scheme's assets was as follows:

	31 December 2010		31 December 2009		31 December 2008	
	Allocation %	Fair value £m	Allocation %	Fair value £m	Allocation %	Fair value £m
Equity securities	61	70.0	66	63.8	57	46.8
Debt securities	9	44.3	23	22.2	27	22.6
Other	30	0.5	11	10.6	16	13.3
	100	114.8	100	96.6	100	82.7

A reconciliation of the present value of the defined benefit obligation is as follows:

	31 December 2010 £m	31 December 2009 £m
Opening defined benefit obligations	100.7	84.1
Current service cost	1.2	1.2
Interest cost	5.6	5.3
Past service cost	–	0.1
Actuarial losses	1.2	13.9
Benefits paid	(3.5)	(3.9)
Closing defined benefit obligations	105.2	100.7

A reconciliation of the fair value of the scheme assets is as follows:

	31 December 2010 £m	31 December 2009 £m
Opening fair value of scheme assets	96.6	82.7
Expected return on scheme assets	6.6	4.9
Difference between expected and actual return on scheme assets	9.3	11.4
Contributions by the employer	5.8	1.5
Benefits paid	(3.5)	(3.9)
Closing fair value of scheme assets	114.8	96.6

The Group paid regular contributions of 33.7% of eligible salaries from 1 January 2010 to 31 August 2010 and regular contributions of 32.5% of eligible salaries from 1 September 2010 to 31 December 2010 (1 January 2009 to 31 December 2009: 33.7%). The Group made an additional lump sum contribution during 2010 of £4.5m (2009: £nil).

The contributions expected to be paid during 2011 are 32.5% of eligible salaries and an additional lump sum contribution of £4.5m.

Notes to the Financial Statements continued

21 Employee benefits continued

A summary of the scheme's experience was as follows:

	31 December 2010 £m	31 December 2009 £m	31 December 2008 £m	31 December 2007 £m	31 December 2006 £m
Defined benefit obligation	(105.2)	(100.7)	(84.1)	(93.5)	(89.7)
Scheme assets	114.8	96.6	82.7	88.4	77.3
Surplus/(deficit)	9.6	(4.1)	(1.4)	(5.1)	(12.4)

The recent history of experience gains and losses is as follows:

	31 December 2010 £m	31 December 2009 £m	31 December 2008 £m	31 December 2007 £m	31 December 2006 £m
Difference between expected and actual return on scheme assets:					
Amount – gain/(loss)	9.3	11.4	(22.3)	2.7	(0.3)
Experience gains and losses on obligations:					
Amount – (loss)/gain	(0.4)	4.8	(0.6)	(0.7)	4.1

Total amount recognised outside income statement:

Actuarial gain/(loss) on defined benefit pension scheme	8.1	(2.5)	(10.1)	1.9	8.8
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The cumulative amount recognised in the Consolidated Statement of Comprehensive Income since 1 January 2004 is a loss of £0.5m (2009: £8.6m).

(ii) Brit Group Services Limited – Defined Contribution Group Personal Pension Plan

From 5 October 2001, Brit Group Services Limited has operated a defined contribution group personal pension plan. The assets of the scheme are held separately from those of the Group in an independently administered fund.

The pension cost charge represents contributions payable by Brit Group Services Limited to the fund and amounted to £7.1m (2009: £7.3m).

At 31 December 2010 no contributions were payable to the fund (2009: £nil).

(iii) Brit Insurance Limited – Defined Contribution Scheme

For Brit Insurance Limited, the Group operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the Group in an independently administered fund.

The pension cost charge represents contributions payable by Brit Insurance Limited to the fund and amounted to £0.1m (2009: £0.0m).

At 31 December 2010, no contributions were payable to the fund (2009: £nil).

22 Financial investments

	31 December 2010 £m	31 December 2009 £m
Equity securities	125.7	102.0
Debt securities	2,692.7	2,282.4
Specialised investment funds	102.6	96.7
	2,921.0	2,481.1

All financial investments have been designated as held at fair value through profit or loss.

Disclosures of fair values in accordance with the fair value hierarchy

The Group has classified fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements.

The fair value hierarchy includes the following levels:

(a) quoted prices (unadjusted) in active markets for identical assets (Level 1);

(b) inputs other than quoted prices included within Level 1 that are observable for the asset, either directly (i.e. as prices) or indirectly (i.e. derived from prices) (Level 2); and

(c) inputs for the asset that are not based on observable market data (unobservable inputs) (Level 3).

The level in the fair value hierarchy within which the fair value measurement is categorised in its entirety shall be determined on the basis of the lowest level input that is significant to the fair value measurement. The significance of an input is assessed against the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a Level 3 measurement. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgement, considering factors specific to the asset.

Level 3 financial investments are valued using techniques appropriate to the specific investment. The techniques used, amongst others, include fair value by reference to NAVs issued by fund managers based on their knowledge of underlying investments and credit spreads of counterparties.

Notes to the Financial Statements continued

22 Financial investments continued

	31 December 2010			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Equity securities	116.9	7.5	1.3	125.7
Debt securities	805.1	1,870.2	17.4	2,692.7
Specialised investment funds	43.2	–	59.4	102.6
	965.2	1,877.7	78.1	2,921.0

	31 December 2009			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Equity securities	84.9	5.7	11.4	102.0
Debt securities	634.2	1,601.0	47.2	2,282.4
Specialised investment funds	41.9	–	54.8	96.7
	761.0	1,606.7	113.4	2,481.1

Reconciliation of movements in Level 3 financial investments measured at fair value

	Equity securities £m	Debt securities £m	Specialised investment funds £m	Total £m
At 1 January 2010	11.4	47.2	54.8	113.4
Total gains recognised in the income statement	0.1	13.2	4.5	17.8
Purchases	–	14.0	14.3	28.3
Sales	(10.2)	(59.2)	(14.9)	(84.3)
Foreign exchange gains	–	2.2	0.7	2.9
At 31 December 2010	1.3	17.4	59.4	78.1

	Equity securities £m	Debt securities £m	Specialised investment funds £m	Total £m
At 1 January 2009	45.0	46.9	61.9	153.8
Total gains recognised in the income statement	2.2	1.8	7.8	11.8
Purchases	–	5.7	8.9	14.6
Sales	(35.7)	(2.7)	(19.5)	(57.9)
Foreign exchange losses	(0.1)	(4.5)	(4.3)	(8.9)
At 31 December 2009	11.4	47.2	54.8	113.4

All unrealised gains of £30.6m (2009: £36.2m) and realised losses of £12.8m (2009: £24.4m) on Level 3 financial investments are presented in investment return in the income statement.

Total unrealised gains of £5.2m are included in the income statement in respect of Level 3 financial investments held at the end of the year.

There were no transfers between Level 3 and Levels 1 or 2 in the year.

Transfers between Level 1 and Level 2

There were no transfers between Levels 1 and 2 during the year.

Sensitivity of Level 3 financial investments measured at fair value to changes in key assumptions

The following table shows the sensitivity of the fair value of Level 3 financial investments to changes in key assumptions.

	31 December 2010	
	Carrying amount £m	Effect of possible alternative assumptions (+/-) £m
Equity securities	1.3	0.0
Debt securities	17.4	0.2
Specialised investment funds	59.4	7.5
	78.1	

	31 December 2009	
	Carrying amount £m	Effect of possible alternative assumptions (+/-) £m
Equity securities	11.4	0.5
Debt securities	47.2	2.0
Specialised investment funds	54.8	7.1
	113.4	

In order to determine reasonably possible alternative assumptions, the Group adjusted key unobservable model inputs as follows:

- For equity securities, based on a review of the composition and investment strategy of the fund, the price was recalculated assuming movements in prices of the underlying investments.
- For debt securities, the Group adjusted, dependant on the type and valuation methodology of the investment, key variables including the probability of spread movements, leverage ratio changes and changes in mortgage default rates used in the models.
- For specialised investment funds, the assumptions have been adjusted by between 5–20% which has been determined by historic movements in valuations or price changes in the underlying investments.

Notes to the Financial Statements continued

23 Derivative contracts

	31 December 2010 £m	31 December 2009 £m
Derivative contract assets		
Warrants and weather derivatives	0.4	0.6
	0.4	0.6

	31 December 2010 £m	31 December 2009 £m
Derivative contract liabilities		
Currency forwards	—	0.3
Catastrophe swap contracts	—	0.6
	—	0.9

Disclosures of fair values in accordance with the fair value hierarchy

	31 December 2010			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Derivative contract assets	—	—	0.4	0.4

	31 December 2009			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Derivative contract assets	—	—	0.6	0.6
Derivative contract liabilities	—	0.3	0.6	0.9

For further information regarding the fair value hierarchy, see Note 22.

24 Insurance and other receivables

	31 December 2010 £m	31 December 2009 £m
Arising out of direct insurance operations	259.6	302.9
Arising out of reinsurance operations	238.4	190.5
Prepayments	4.6	5.9
Accrued income	31.2	31.4
Other debtors	7.0	6.3
	540.8	537.0

The carrying amounts disclosed above reasonably approximate fair values as all material amounts are due within one year of the date of the statement of financial position.

Notes to the Financial Statements continued

25 Cash and cash equivalents

	31 December 2010 £m	31 December 2009 £m
Cash at bank and on deposit	601.8	949.2
Cash equivalents	21.6	45.0
	623.4	994.2

The carrying amounts disclosed above reasonably approximate fair values.

Included in cash and cash equivalents are amounts totalling £150.1m (2009: £357.8m) not available for use by the Group which are held within the Lloyd's syndicates or as Funds at Lloyd's.

26 Borrowings

				31 December 2010			31 December 2009	
	Maturity	Call	Effective interest rate %	Initial capitalised borrowing costs £m	Amortised cost £m	Fair value £m	Amortised cost £m	Fair value £m
Non-current								
Lower Tier Two subordinated debt	2030	2020	6.84	1.8	133.0	89.4	132.8	95.6
			LIBOR +					
Revolving credit facility	2012	–	3.25	2.2	35.4	37.0	104.8	107.0
				4.0	168.4	126.4	237.6	202.6

The fair value of the Lower Tier Two subordinated debt represents trading market values on recognised exchanges.

Lower Tier Two subordinated debt

The Lower Tier Two subordinated debt is callable in whole by the Group on 9 December 2020. Following this date the interest rate resets to 3.4% above the 10-year gilt rate prevailing at the time. The effective interest rate method of accounting has been applied over the term up to the call date.

Revolving credit facility

The Group has access to a three-year £175.0m revolving credit facility effective from 9 November 2009.

Notes to the Financial Statements continued

27 Deferred taxation

	Unrealised (profits)/losses on investments £m	Pensions £m	Foreign exchange (profits)/losses on non-monetary items £m	Underwriting £m	Other £m	Total £m
As at 1 January 2009	–	0.4	(1.3)	(30.7)	2.1	(29.5)
Movements in the year:						
(Charged)/credited to income statement (Note 14)	(0.5)	0.1	0.5	7.1	2.6	9.8
Tax relating to components of other comprehensive income (Note 14)	–	0.7	–	–	–	0.7
At 31 December 2009	(0.5)	1.2	(0.8)	(23.6)	4.7	(19.0)
As at 1 January 2010	(0.5)	1.2	(0.8)	(23.6)	4.7	(19.0)
Movements in the year:						
Credited/(charged) to income statement (Note 14)	0.1	(1.6)	0.8	6.1	0.2	5.6
Tax relating to components of other comprehensive income (Note 14)	–	(2.2)	–	–	–	(2.2)
At 31 December 2010	(0.4)	(2.6)	–	(17.5)	4.9	(15.6)

Deferred tax has not been set up in respect of losses carried forward of £6.3m (2009: £1.2m) as it is not considered probable that they can be utilised in the foreseeable future.

Deferred tax has not been provided in respect of the profits of subsidiaries in the Group as tax exemptions, for example the participation exemption, are expected to apply.

Notes to the Financial Statements continued

28 Provisions

	Onerous lease provision £m	Dilapidation provision £m	Total £m
At 1 January 2009	0.4	–	0.4
Amounts utilised during the year	(0.1)	–	(0.1)
At 31 December 2009	0.3	–	0.3
At 1 January 2010	0.3	–	0.3
New provisions	–	1.2	1.2
Unwinding of discount	–	0.1	0.1
At 31 December 2010	0.3	1.3	1.6

29 Insurance and other payables

	31 December 2010 £m	31 December 2009 £m
Arising out of direct insurance operations	23.3	24.7
Arising out of reinsurance operations	191.0	147.6
Other taxes and social security costs	2.1	1.6
Accruals and deferred income	32.0	24.1
Other creditors	3.3	2.7
	251.7	200.7

The carrying amounts disclosed above reasonably approximate fair values as all amounts are payable within one year of the date of the statement of financial position.

30 Equity dividends

	Amount (pence per ordinary share) (restated)	31 December 2010 £m	31 December 2009 £m
Dividend paid			
Final 2008	30.0	–	23.2
Interim 2009	30.0	–	23.2
		–	46.4

31 Capital distributions

At the time of the Group reorganisation in December 2009, it was announced that for an initial period the Group would make distributions to shareholders by way of reductions of the par value of Brit Insurance Holdings N.V. shares.

	Amount (pence per ordinary share)	Settled with cash 31 December 2010 £m	Settled with shares 31 December 2010 £m	Total 31 December 2010 £m	Total 31 December 2009 £m
Distribution paid					
Final 2009	30.1	17.4	5.9	23.3	–
Interim 2010	30.4	23.7	–	23.7	–
		41.1	5.9	47.0	–

A final distribution of 30.1p per ordinary share for the year ended 31 December 2009 was approved by the Annual General Meeting on 6 May 2010 and paid on 15 July 2010. This was satisfied in the form of 675,217 newly issued shares for shareholders who elected to take the distribution in the form of a scrip and £17.4m in cash for the remaining shareholders. As a result of the distribution, the nominal value of the share capital was reduced by 36 eurocents from €4.00 to €3.64 in respect of each registered share.

An interim distribution of 30.4p per ordinary share for the period ended 30 June 2010 was approved by the General Meeting on 23 September 2010 and paid on 7 December 2010. As a result of the distribution, the nominal value of the share capital was reduced by 36 eurocents from €3.64 to €3.28 in respect of each registered share.

Notes to the Financial Statements continued

31 Capital distributions continued

The amounts stated above do not include distributions amounting to £0.7m paid in respect of own shares held by the Group's Employee Share Participation Trust as these are eliminated on consolidation of the Trust.

No final distribution has been recommended for the year ended 31 December 2010.

32 Share capital

	31 December 2010 £m	31 December 2009 £m	31 December 2010 €m	31 December 2009 €m	31 December 2010 Number in millions	31 December 2009 Number in millions (restated)
Authorised:						
Ordinary shares	700.9	885.0	820.0	1,000.0	250.0	250.0
Allotted, issued and fully paid:						
Ordinary shares	221.9	277.9	259.6	314.0	79.2	78.5

As at 31 December 2010, the nominal value per ordinary share was €3.28 (2009: €4.00) (restated).

Share capital has been translated from Euros into Sterling using an exchange rate of 1.17 as at the end of the year (2009: 1.13).

	31 December 2010 Number in millions	31 December 2009 Number in millions (restated)
Ordinary shares in issue		
At 1 January/on incorporation	78.5	—
Issue of ordinary shares on corporate reorganisation	—	78.5
Issued in respect of capital distribution	0.7	—
At 31 December	79.2	78.5

There were no shares reserved for issue under options as at 31 December 2010 or 31 December 2009.

On 25 February 2010, the Company undertook a consolidation of its share capital, such that the shareholders received one ordinary €4 share for every four ordinary €1 shares owned as at that date. The comparatives have been restated to reflect this share consolidation.

33 Own shares

The trustees of the All Employee Share Ownership Plan hold Brit Insurance Holdings N.V. shares in accordance with the terms of that trust. The number of unvested shares held at 31 December 2010 was 116,668 (2009: 164,317) (restated).

The trustees of the Employee Share Participation Trust acquire Brit Insurance Holdings N.V. shares in accordance with the terms of that trust. The number of shares held at 31 December 2010 was 1,122,667 (2009: 1,017,196) (restated).

For further information refer to Note 36.

	31 December 2010 £m	31 December 2009 £m
All Employee Share Ownership Plan	1.0	1.5
Employee Share Participation Trust	8.8	9.2
	9.8	10.7

34 Commitments

Operating lease commitments

The Group has entered into a number of operating lease arrangements to lease properties, motor vehicles and office equipment.

Property leases typically have rent reviews every five years where the lease payments could be increased to reflect market rates.

Operating lease payments recognised in the income statement were £4.0m (2009: £4.8m).

Notes to the Financial Statements continued

34 Commitments continued

The future minimum lease payments under non-cancellable operating leases were as follows:

	31 December 2010 £m	31 December 2009 £m
Not later than one year	4.3	4.0
Later than one year and not later than five years	14.1	12.5
Later than five years	0.2	2.5
	18.6	19.0

The Group has sublet one of the properties at a rental of £55,000 per year until 2014 and therefore the future minimum sublease receipts expected to be received under this sublease as at 31 December 2010 were £0.2m (2009: £0.3m). Sublease receipts recognised in the income statement during the year were £0.1m (2009: £0.1m).

35 Cash flows provided by operating activities

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Profit on ordinary activities before tax	116.4	116.4
Adjustments for non-cash movements:		
Realised and unrealised gains on investments	(7.9)	(38.0)
Realised and unrealised losses on derivatives	1.9	4.1
Loss on sale of property, plant and equipment	–	0.1
Amortisation of software	4.1	4.2
Impairment of software	0.7	2.2
Depreciation of property, plant and equipment	3.5	2.9
Impairment of property, plant and equipment	0.3	–
Foreign exchange gains on financing items	–	(1.4)
Foreign exchange (gains)/losses on cash and cash equivalents	(8.8)	49.0
Share of loss after tax of associated undertakings	1.8	2.3
Charges in respect of employee share schemes	7.7	10.1
Cash contributions (in excess of)/lower than defined benefit pension scheme charges	(5.6)	0.2
Interest income	(98.4)	(97.1)
Dividend income	(7.1)	(2.4)
Finance costs on borrowing	14.0	11.5
Loss/(profit) on disposal of associated undertakings	0.4	(4.2)
Changes in working capital:		
Deferred acquisition costs	(4.3)	(10.3)
Insurance and other receivables excluding accrued income	(4.0)	(37.5)
Insurance and reinsurance contracts	49.9	120.8
Financial investments	(432.0)	(50.1)
Derivative contracts	(2.6)	(7.8)
Insurance and other payables	51.0	(1.4)
Provisions	1.3	(0.1)
Cash flows provided by operating activities	(317.7)	73.5

Notes to the Financial Statements continued

36 Share-based payments

During the year ended 31 December 2010, the Group had a number of long-term employee incentive schemes. With the exception of one cash-settled award made under terms similar to the Bonus Share Matching Plan all awards have been classified as equity-settled. These schemes are described below and further information is available in the Directors' Remuneration Report.

The compensation cost recognised in the income statement under International Financial Reporting Standard 2 'Share-based payments' (IFRS 2) for the Group's share-based payment arrangements is shown below:

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
All Employee Share Ownership Plan (ESOP)	0.3	0.3
Savings Related Share Option Scheme (SRSOS)	0.1	—
Performance Share Plan (PSP)	4.5	5.3
Bonus Share Matching Plan (BSMP)	3.6	4.5
	8.5	10.1

The amount recognised in equity is shown below:

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Compensation cost	8.5	10.1
BSMP dividend equivalents settled in cash	(0.8)	—
	7.7	10.1

Share consolidation

All prior year comparatives for numbers of shares and prices per share in this Note have been restated to reflect the share consolidation on 25 February 2010.

Measurement of fair value

PSP share awards with vesting based on Total Shareholder Return (TSR) performance

The fair value of the PSP share awards with a TSR performance condition is calculated at the date of grant using a Monte Carlo simulation. This valuation process simulates the future TSRs for the Group and each stock in the comparator group over the three calendar years beginning with the year in which the awards are granted. The TSR for each stock is simulated by assuming a log-normal model of share returns. The inputs to that model are: the risk-free interest rate and the expected volatility of share returns over the life of the awards.

The uncertainty of share returns is generated for each simulation of future TSRs by randomly sampling from the weekly share returns which have been observed over recent periods of history. The correlation between the stocks in the comparator group is allowed for automatically (without the need for separate assumptions) because the simulation is sampling from the observed share returns which include the stocks' relative weekly returns. Dividends are not deducted in the calculation of fair value because it has been assumed that any dividends will be accumulated over the vesting period and repaid in equivalent shares. Many thousands of simulations of the future TSRs are calculated and these are used to determine the average fair value of the PSP share award.

For PSP share awards granted during the year, the following assumptions have been made:

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Risk-free interest rate	1.5%–1.9%	1.7%–2.4%
Expected volatility	33.3%–33.6%	32.9%–33.9%

Expected volatility is based on the historical volatility of the Group's share returns over the most recent period that is commensurate with the expected term of the performance shares and also the long-term trend observed. The risk-free rate used in both the valuation models is equal to the yields available on zero-coupon UK government bonds at the date of grant with a term equal to the expected term of the awards.

Notes to the Financial Statements continued

36 Share-based payments continued

SRSOS share awards

The fair value of each award on the day of grant was estimated using a binomial option valuation model, including allowance for the exercise price being at a discount to market price. There are no performance conditions for the vesting of these awards. The key assumptions used for the valuation of awards granted during the year are as follows.

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Expected volatility	35%	n/a
Risk-free interest rate	2.2%	n/a
Assumed future dividend yield	7.5%	n/a
Ongoing cancellation rate	5.0%	n/a

Expected volatility is based on the historical volatility of the Group's share returns over the most recent period that is commensurate with the expected term of the performance shares and also the long-term trend observed. The risk-free rate used in the valuation model is equal to the yield available on zero-coupon UK government bonds at the date of grant with a term equal to the expected term of the awards.

In addition to the ongoing cancellation rate above it is assumed that on the anniversary of date of grant a proportion of employees will cancel their awards in favour of new awards if the then share price is less than the exercise price. The proportion assumed is a sliding scale from 20% cancelling if the current share price equals the exercise price to 100% cancelling if the current share price is 75% of the exercise price or less. It is assumed that participants in the SRSOS will exercise their options halfway through the six month exercise window, provided they are in 'in-the-money'.

BSMP and PSP share awards with vesting based on non-market conditions

The fair values of the BSMP and PSP share awards with vesting based on non-market conditions are set to equal the share price on date of grant. Dividends are not deducted in the calculation of fair value because it has been assumed that any dividends will be accumulated over the vesting period and repaid in equivalent shares on the BSMP and PSP schemes.

(i) All Employee Share Ownership Plan

Following the corporate reorganisation, no further purchases or awards have been made under the ESOP since 31 December 2009. All participating employees had the opportunity to make contributions from their pre-tax salary each month (to a maximum of £125 per month), to buy shares in the Group at the prevailing market price (partnership shares). The Group provided one share for each two shares purchased by the employee (matching shares). Free shares were awarded depending on Group performance over the previous year. If the participant leaves within three years of the award of free shares and within five years of the award of matching shares, except under specified circumstances, the rights to these shares are forfeited. There are no performance criteria that must be satisfied before the Plan shares may be sold or transferred.

A reconciliation of the free and matching shares awards which had not yet vested unconditionally by 31 December 2010 is shown in the table below. All of these shares have been conditionally gifted to employees, subject to reaching the relevant qualifying period.

	Year ended 31 December 2010 Number of shares	Year ended 31 December 2009 Number of shares
Outstanding and unvested at start of year	164,317	148,915
Granted	–	65,222
Forfeited	(23,534)	(29,035)
Vested	(24,115)	(20,785)
Outstanding and unvested at end of year	116,668	164,317

The weighted average share price at date of vesting during 2010 was 987.6p (2009: 802.8p).

The weighted average fair value at date of grant for awards granted during 2010 was nil (2009: 800.4p).

The calculation of the compensation cost recognised in the income statement in respect of these awards assumes forfeitures due to employee turnover of 10% per annum prior to vesting, with subsequent adjustments to reflect actual experience.

Notes to the Financial Statements continued

36 Share-based payments continued

(ii) Savings Related Share Option Scheme

All employees have the opportunity to participate in this Scheme. Participating employees contribute a fixed monthly amount into the Scheme from their pre-tax salary. Contributions receive interest and a potential bonus upon completion of the three year participation period. At the end of the participation period participants have six months in which to elect to use their savings to purchase Company shares at the stated exercise price. If a participant leaves within three years of the award, except under specified circumstances, the right to the share options is forfeited. There are no performance criteria that must be satisfied before the options can be exercised. Participants do not receive dividends until they exercise the options so the expected value of future dividends is removed from the fair value calculations.

The calculation of the compensation cost recognised in the income statement in respect of these awards assumes forfeitures due to employee turnover of 10% per annum prior to vesting, with subsequent adjustments to reflect actual experience.

A summary of the status of the SRSOS as at 31 December 2010 and changes during the year is presented below:

	31 December 2010		31 December 2009	
	Number of options	Weighted average exercise price (pence)	Number of options	Weighted average exercise price (pence)
Outstanding at start of year	–	n/a	–	n/a
Granted	338,887	609.6	–	n/a
Forfeited	(15,251)	609.6	–	n/a
Cancellations	(6,961)	609.6	–	n/a
Exercised	(520)	609.6	–	n/a
Outstanding at end of year	316,155	609.6	–	n/a

There were 956 shares (2009: n/a) exercisable at the end of the year.

The weighted average share price at date of exercise during the year was 937.3p (2009: n/a).

The weighted average remaining contractual life at the end of the year was 2.9 years (2009: n/a).

The exercise price for outstanding options at the end of the year was 609.6p (2009: n/a).

(iii) Performance Share Plan

Selected employees are awarded the right to acquire a defined number of shares in the Group at no cost to the employee. Subject to the satisfaction of prescribed criteria, the right to acquire shares may be exercised on or after the third anniversary of the grant date. The performance condition that applied prior to 24 April 2007 was that the Group's TSR had to exceed the median TSR of the other FTSE Actuaries Insurance sector companies on the grant date over a period of three years from that date. After 24 April 2007 the performance condition was changed so that:

- one half of an award is subject to the Company's TSR against a bespoke industry comparator group; and
- one half of an award is subject to conditions on the average annual Return on Equity over a fixed three-year performance period.

For awards granted prior to 1 January 2010, the Return on Equity performance condition was based on the Company's Return on Equity compared with the UK Bank of England Base Rate, underpinned by further conditions based on growth in Gross Premiums and the delivery of positive Return on Equity to shareholders.

For awards granted from 1 January 2010 onwards the Remuneration Committee changed the Return on Equity performance condition so that it is instead based on the Company's Return on Equity subject to the delivery of positive Return on Equity to shareholders.

For awards granted prior to 1 January 2010, the right must be exercised within six months of the award becoming exercisable.

For awards granted from 1 January 2010 onwards, in general, the right must be exercised within 18 months of the award becoming exercisable. Participants do not receive any dividends until after the shares have been received. However, the Remuneration Committee may decide to award the value of accrued dividends in the vesting period, for options granted after 24 April 2007.

For awards granted after 24 April 2007 it has been assumed that the participants will receive the value of any dividends accrued between date of grant and date of vest at the date of vesting of the awards and in proportion to the number of awards that vest. The calculation of the compensation cost recognised in the income statement in respect of these awards assumes forfeitures due to employee turnover of 5% per annum prior to vesting, with subsequent adjustments to reflect actual experience.

Notes to the Financial Statements continued

36 Share-based payments continued

Outstanding PSP awards granted at nil cost were as follows as at 31 December 2010:

Year of grant	Number of shares	Latest vesting year
2008	560,760	2011
2009	816,786	2012
2010	814,394	2013
	2,191,940	

A reconciliation of the PSP share awards which had not been exercised by 31 December 2010 is presented below. All of these shares have been conditionally gifted to employees, subject to reaching the relevant qualifying period and meeting the relevant performance criteria.

	31 December 2010 Number of shares	31 December 2009 Number of shares
Outstanding and unexercised at start of year	2,141,967	1,996,420
Granted	859,576	983,873
Forfeited	(159,121)	(261,577)
Failed performance conditions and lapsed	(325,241)	(567,734)
Exercised	(325,241)	(9,015)
Outstanding and unexercised at end of year	2,191,940	2,141,967

The weighted average share price at date of exercise during the year was 768.9p (2009: 813.2p).

The weighted average fair value at date of grant for awards granted during 2010 was 536.6p (2009: 573.6p).

(iv) Bonus Share Matching Plan

Selected employees are invited to purchase a number of Investment Shares in the Group using up to 50% of their post tax bonus. Each participant is awarded the right to acquire Matching Shares to match the investment at no cost to the employee. Subject to retaining the Investment Shares for three years and subject to the satisfaction of performance conditions, the Matching Shares will vest on the third anniversary of the grant date. For awards granted before 1 January 2010 the right must be exercised within six months of the award becoming exercisable. For awards granted beyond 1 January 2010 the right must be exercised within 18 months of the award becoming exercisable.

For awards granted prior to 1 January 2010, the performance conditions included targets for the Group's return on equity relative to the UK Bank of England Base Rate, growth in gross written premiums and volatility of ROE. For awards granted from 1 January 2010 onwards the Remuneration Committee changed the performance conditions so that they are instead based on the Company's Return on Equity subject to the delivery of positive Return on Equity to shareholders.

The Remuneration Committee may decide to award the participants the value of the accrued dividends in the vesting period. It has been assumed in the calculation of fair value for IFRS2 purposes that the participants will receive the value of any dividends accrued between date of grant and date of vest at the date of vesting of the awards and in proportion to the number of awards that vest. The calculation of the compensation cost recognised in the income statement in respect of these awards assumes forfeitures due to employee turnover of 5% per annum prior to vesting, with subsequent adjustments to reflect actual experience.

Notes to the Financial Statements continued

36 Share-based payments continued

Outstanding BSMP awards granted at nil cost were as follows as at 31 December 2010:

Year of grant	Number of matching shares	Latest vesting year
2008	529,813	2011
2009	439,490	2012
2010	586,873	2013
	1,556,176	

A reconciliation of the BSMP share awards which had not been exercised by 31 December 2010 is presented below. All of these shares have been conditionally gifted to employees, subject to reaching the relevant qualifying period and meeting the relevant performance criteria.

	31 December 2010 Number of shares	31 December 2009 Number of shares
Outstanding and unexercised at start of year	1,473,970	1,120,500
Granted	591,679	471,223
Forfeited	(88,424)	(117,753)
Exercised	(421,049)	—
Outstanding and unexercised at end of year	1,556,176	1,473,970

The weighted average share price at date of exercise during the year was 751.2p (2009: nil).

The weighted average fair value at date of grant for awards granted during 2010 was 761.5p (2009: 731.2p).

In addition to the amounts referred to above, during 2008, a senior consultant was granted the right to receive a further 23,521 Matching Shares on terms similar to the BSMP scheme but with the exception that the award should be settled with cash instead of equity. The fair value of this award was £0.2m which is based on the share price on the date of grant. As at 31 December 2010 all of the consultant's matching shares were outstanding and unexercised.

(v) Executive Share Option Scheme

Under the terms of the ESOS, selected employees were offered a defined number of options at an exercise price no less than the average market price of the shares on the three dealing days preceding date of grant. Subject to a prescribed performance criterion, the options may be exercised in a period commencing three years after the date of grant and ending ten years after the date of grant. The performance criterion was for the Group's TSR to exceed the median TSR of the companies in the FTSE Mid 250 over a period of at least three years from grant. The proportion of options that will become exercisable depends on the level of outperformance. If an employee leaves the Group before the beginning of the exercise period, he forfeits his options. All outstanding options expire at the end of the exercise period. Following shareholder approval of the BSMP in 2007, no further grants of options have been made under this scheme.

The calculation of the compensation cost recognised in the income statement in respect of these options assumes forfeitures due to employee turnover of 5% per annum prior to vesting, with subsequent adjustments to reflect actual experience.

A summary of the status of the ESOS as at 31 December 2010 and changes during the year is presented below:

	31 December 2010		31 December 2009	
	Number of options	Weighted average exercise price (pence)	Number of options	Weighted average exercise price (pence)
Outstanding at start of year	193,155	942.0	208,746	942.0
Exercised	(5,229)	942.0	—	n/a
Expired or lapsed after vesting	(2,405)	942.0	(15,591)	942.0
Outstanding at end of year	185,521	942.0	193,155	942.0

There were 185,521 shares (2009: 193,155) exercisable at the end of the year.

The weighted average exercise price of options exercisable at the end of the year was 942.0p (2009: 942.0p).

The weighted average share price at date of exercise during the year was 1,017.9p (2009: nil exercises)

The weighted average remaining contractual life at the end of the year was 3.8 years (2009: 4.8 years).

The exercise price for outstanding options at the end of the year was 942.0p (2009: 942.0p).

Notes to the Financial Statements continued

36 Share-based payments continued

(vi) Executive Share Option Schemes

Prior to the introduction of the ESOS, share options were granted under a number of share option schemes which have subsequently been closed.

A summary of the status of the Executive Share Option Schemes as at 31 December 2010 and changes during the year is presented below:

	31 December 2010		31 December 2009	
	Number of options	Weighted average exercise price (pence)	Number of options	Weighted average exercise price (pence)
Outstanding at start of year	111,420	980.4	120,071	973.6
Exercised	(3,941)	888.0	–	n/a
Expired or lapsed after vesting	(87,544)	917.2	(8,651)	889.6
Outstanding at end of year	19,935	1275.4	111,420	980.4

There were 19,935 shares (2009: 111,420) exercisable at the end of the year.

The weighted average exercise price of options exercisable at the end of the year was 1,275.4p (2009: 980.4p).

The weighted average share price at date of exercise during the year was 1040.7p (2009: n/a).

A summary of the range of exercise prices of the outstanding options and their remaining contractual lifetimes is presented below:

	31 December 2010		31 December 2009	
	Number of options	Weighted average remaining contractual life (years)	Number of options	Weighted average remaining contractual life (years)
Range of exercise prices for outstanding options				
906p (2009: 846p to 906p)	3,787	2.1	83,383	2.4
1362p (2009: 1362p to 1362p)	16,148	0.4	28,037	1.4
906p to 1362p (2009: 846p to 1362p)	19,935	0.8	111,420	2.1

Employee share trusts and award settlement

Awards under the ESOP are settled by the transfer of shares from an independent trust which acquires shares for this purpose by buying shares in the market. Distributions are payable on shares held in the Trust. As at 31 December 2010, the Trust held 114,166 (2009: 133,917) free shares, 70,944 (2009: 83,664) matching shares, 143,721 (2009: 169,676) partnership shares and 15,558 (2009: 3,080) unallocated shares with a total nominal value of €1.1m (2009: €1.5m) and a market value of £3.6m (2009: £3.1m), based on the mid-market value of the Group's shares at close of business on 31 December 2010, as shown in the Official List of the London Stock Exchange. This equates to 0.4% of the Group's issued share capital as at 31 December 2010 (2009: 0.5%).

Awards under the SRSOS, PSP, BSMP, ESOS and Executive Share Option Schemes are settled by the transfer of shares from the Group's Employee Share Participation Trust which acquires shares for this purpose by buying shares in the market. As at 31 December 2010, the Employee Share Participation Trust held 1,122,667 (2009: 1,017,196) ordinary shares which represented 1.4% (2009: 1.3%) of the issued share capital of the Group as at 31 December 2010. The shares had a total nominal value of €3.7m (2009: €4.1m) and a market value of £11.7m (2009: £8.0m), based on the mid-market value of the Group's shares at close of business on 31 December 2010, as shown in the Official List of the London Stock Exchange.

Notes to the Financial Statements continued

37 Subsidiary undertakings

The subsidiaries of Brit Insurance Holdings N.V. are as follows:

The Netherlands

Brit Group Holdings B.V.

Brit Services B.V.

United Kingdom

Brit Insurance Holdings Limited

Brit Insurance Limited

Brit Syndicates Limited

Brit UW Limited

Masthead Insurance Underwriting Limited

Brit Corporate Holdings Limited

Brit Investment Holdings Limited

Brit Underwriting Holdings Limited

Brit Group Finance Limited

Brit Capital Markets Limited

Brit Group Services Limited

Brit Insurance Australia Representative Limited

Brit Investment Company Limited

Brit Insurance Services Limited

Brit Pension Trustee Limited

Brit Corporate Secretaries Limited

Brit Corporate Services Limited

Brit Dormant One Limited

Brit Dormant Two Limited

Brit Dormant Three Limited

Brit Run-Off Services Limited

Brit Insurance (UK) Limited

Fuit One Limited

Fuit Two Limited

Fuit Three Limited

Fuit Four Limited

Fuit Five Limited

HCG Alpha Limited

HCG Bravo Limited

HCG Charlie Limited

HCG Delta Limited

HCG Echo Limited

HCG Foxtrot Limited

Masthead A Limited

Masthead B Limited

Masthead C Limited

Masthead D Limited

Masthead E Limited

Notes to the Financial Statements continued

37 Subsidiary undertakings continued

Luxembourg

Brit Overseas Holdings S.à.r.l.

United States of America

Brit Insurance Services USA Inc

Gibraltar

Brit Insurance (Gibraltar) PCC Ltd

38 Related party transactions

(i) Key management compensation

	Year ended 31 December 2010 £m	Year ended 31 December 2009 £m
Salaries and other short-term employee benefits	4.2	3.6
Post-employment benefits	0.5	0.5
Termination benefits	0.6	–
Share-based payments	2.9	2.6
	8.2	6.7

For the purposes of International Accounting Standard 24, 'Related Party Disclosures', key managers are defined as the Board of Directors and members of the Executive Management Committee which is the primary vehicle for implementing Board decisions in respect of UK-managed operations.

Further details concerning individual Directors' remuneration and interests is given in the Directors' remuneration report.

(ii) Purchases of products and services and arising year-end balances

All of the following trading with associated undertakings is carried out on an arm's length basis and is settled in cash.

RI3K Limited

RI3K Limited has charged £0.3m (2009: £0.3m) for services to Group companies up to the date that it ceased to be a related party on 7 December 2010.

There were no fees outstanding as at 31 December 2010 or 31 December 2009.

Xbridge Limited

A Group company is a member of the panel to which Xbridge Limited introduces insurance business.

During the year, Xbridge Limited has received commission of £7.3m (2009: £6.4m) for introducing such business.

There were premiums net of commission outstanding from Xbridge Limited of £2.2m as at 31 December 2010 (2009: £2.0m).

Verex Limited

A Group company is the insurance provider to which Verex Limited introduces insurance business.

During the year, Verex Limited has received commission of £0.4m (2009: £0.1m) for introducing such business.

There were premiums net of commission outstanding from Verex Limited of £0.8m as at 31 December 2010 (2009: £0.4m).

(iii) Loans

Brit Insurance Holdings N.V. and its subsidiaries have the following loans with associated undertakings which are all on an arm's length basis.

Xbridge Limited

A Group company has granted Xbridge Limited a five year loan facility of up to £6.0m.

As at 31 December 2010, £5.2m of this amount had been drawn down (2009: £5.2m).

Verex Limited

A Group company has entered into a contract to subscribe for up to £6.0m of Verex Limited loan notes.

As at 31 December 2010, all of these loan notes had been subscribed for (2009: £4.0m).

Notes to the Financial Statements continued

39 Guarantees and contingent liabilities

(i) Lloyd's

The Group is a party to arrangements with Lloyd's as set out below:

If any of the corporate member subsidiaries fails to meet any of its Lloyd's obligations, then:

- (a) Lloyd's will be entitled to require the other corporate member subsidiaries to cease or reduce their underwriting; and/or
- (b) having regard to the fact that the Central Fund or the New Central Fund may be applied to discharge the obligations of the defaulting corporate member subsidiary, Lloyd's will be entitled to require each of the other corporate member subsidiaries to make contributions to the New Central Fund up to the amount of their respective net profits held from time to time in Premium Trust Funds, sufficient to reimburse the Central Fund or the New Central Fund in full for any payment made on behalf of the defaulting member.

At the date of signing these financial statements the Group is not aware of any corporate member subsidiary failing to meet its Lloyd's obligations.

Assets are required to be pledged, as Funds at Lloyd's, by way of deposits and fixed and floating charges for the corporate members of the Group, principally Brit UW Limited. As at 31 December 2010 these amounted to £455.7m (2009: £447.2m).

(ii) Letters of Credit

Brit Insurance Limited has a Letter of Credit (LOC) facility with Citibank Europe Plc for US\$ 250.0m (2009: US\$ 250.0m), of which US\$ 37.0m had been utilised at 31 December 2010 (2009: US\$ 92.1m).

During the year, Brit Insurance Limited cancelled a LOC facility for US\$ 30.0m (2009: US\$ 30.0m) with the Royal Bank of Scotland PLC of which US\$ 2.7m was utilised as at 31 December 2009.

These facilities provide security against liabilities arising from US reinsurance business and aviation excess of loss and are collateralised with cash and bonds.

(iii) Success fees

On 23 November 2010, a recommended cash offer was made by Achilles Netherlands Holdings B.V. for the entire share capital of the Group.

The Group has entered into contracts with certain advisors whereby those advisors would receive success fees amounting to £6.9m upon completion of the acquisition.

40 Post balance sheet events

On 23 November 2010, a recommended cash offer was made by Achilles Netherlands Holdings B.V. (Achilles) for the entire share capital of the Group. The offer was subject to a number of conditions including receiving valid acceptances in respect of not less than 95% of the diluted share capital (or a lesser number on which Achilles may decide) and certain regulatory approvals.

On 15 February 2011, Achilles announced that the FSA had given formal notice of its approval in respect of the acquisitions of control over the relevant members of the Brit Insurance Group which would result from the implementation of the offer. It was also announced that Lloyd's approval had been granted.

On 17 February 2011, Achilles announced that it had reduced the number of acceptances required to fulfil the acceptance condition from 95% of the diluted share capital to 80% of the existing share capital. Based on the number of valid acceptances received at that time, Achilles announced that it was treating the acceptance condition as satisfied.

As at 24 February 2011, certain other conditions remain outstanding.

Authorisation of Consolidated Financial Statements

Amsterdam 24 February 2011

Robert John Orr Barton

Dane Jonathan Douetil

Joseph Patrick MacHale

Peter Frank Hazell

Maarten Joannes Hulshoff

Cornelis Antonius Carolus Maria Schrauwers

Willem Frans Casimir Stevens

Independent auditor's report on the Consolidated Financial statements

To: The Meeting of Shareholders of Brit Insurance Holdings N.V.

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements 2010 which are part of the financial statements of Brit Insurance Holdings N.V., Amsterdam, and comprise the consolidated statement of financial position as at 31 December 2010, the consolidated income statement, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended and notes, comprising a summary of the significant accounting policies and other explanatory information.

Directors' responsibility

The Directors are responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Dutch Civil Code, and for the preparation of the Directors' board report in accordance with Part 9 of Book 2 of the Dutch Civil Code. Furthermore the Directors are responsible for such internal control as it determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. This requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error.

In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion with respect to the consolidated financial statements

In our opinion, the consolidated financial statements give a true and fair view of the financial position of Brit Insurance Holdings N.V. as at 31 December 2010, its result and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Dutch Civil Code.

Report on other legal and regulatory requirements

Pursuant to the legal requirement under Section 2:393 sub 5 at e and f of the Dutch Civil Code, we have no deficiencies to report as a result of our examination whether the management board report, to the extent we can assess, has been prepared in accordance with Part 9 of Book 2 of this Code, and whether the information as required under Section 2:392 sub 1 at b-h has been annexed. Further we report that the Directors' board report, to the extent we can assess, is consistent with the consolidated financial statements as required by Section 2:391 sub 4 of the Dutch Civil Code.

The Hague, 24 February 2011

Ernst & Young Accountants LLP

Signed by S.B. Spiessens

Parent Company Financial Statements

133 Balance Sheet of Brit Insurance Holdings N.V.

134 Income Statement of Brit Insurance Holdings N.V.

135 Statement of Changes in Equity of Brit Insurance Holdings N.V.

136 Notes to the Financial Statements of Brit Insurance Holdings N.V.

139 Other Information

140 Independent auditor's report on the Parent Company Financial Statements

Balance Sheet of Brit Insurance Holdings N.V.

at 31 December 2010 before appropriation of result

	Notes	31 December 2010 £m	31 December 2009 £m
Assets			
Investment in subsidiaries	3	1,018.6	894.6
Amounts owed from Group companies		141.4	133.3
Cash and cash equivalents		0.1	–
Total assets		1,160.1	1,027.9
Equity			
Called up share capital	4	221.9	277.9
Share premium account		615.9	612.0
Unappropriated results		110.5	3.9
Revaluation reserve		15.3	–
Retained earnings		8.0	0.8
Total equity		971.6	894.6
Liabilities			
Long-term borrowings	6	133.0	132.8
Current liabilities:			
Accruals and deferred income		1.1	0.5
Amounts owed to Group companies		54.3	–
Other creditors		0.1	–
		55.5	0.5
Total liabilities		188.5	133.3
Total liabilities and equity		1,160.1	1,027.9

Income Statement of Brit Insurance Holdings N.V.

for the year ended 31 December 2010

	Year ended 31 December 2010 £m	Period ended 31 December 2009 £m
Result of Group companies after taxation	115.7	3.9
Other results after taxation	(5.2)	—
Net profit	110.5	3.9

Statement of Changes in Equity of Brit Insurance Holdings N.V.

for the year ended 31 December 2010

	Note	Called up share capital £m	Share premium account £m	Unappropriated results	Revaluation reserve	Retained earnings £m	Total £m
At 1 January 2010		277.9	612.0	3.9	–	0.8	894.6
Exchange difference on retranslation of share capital		(10.3)	–	–	–	10.3	–
Actuarial gains on defined benefit pension scheme		–	–	–	–	8.1	8.1
Tax relating to actuarial gains on defined benefit pension scheme		–	–	–	–	(2.2)	(2.2)
Effect of associates' capital movements		–	–	–	–	0.3	0.3
Acquisition of own shares for share schemes		–	–	–	–	(6.4)	(6.4)
Vesting of own shares		–	–	–	–	0.1	0.1
Share-based payments		–	–	–	–	7.7	7.7
Amount recognised directly in equity		(10.3)	–	–	–	17.9	7.6
Transferred to retained earnings		–	–	(3.9)	–	3.9	–
Transferred to revaluation reserve		–	–	–	15.3	(15.3)	–
Capital distribution	5	(45.7)	3.9	–	–	0.7	(41.1)
Net profit		–	–	110.5	–	–	110.5
At 31 December 2010		221.9	615.9	110.5	15.3	8.0	971.6

	Note	Called up share capital £m	Share premium account £m	Unappropriated results	Revaluation reserve	Retained earnings £m	Total £m
On incorporation		–	–	–	–	–	–
Corporate reorganisation	3	278.7	612.0	–	–	–	890.7
Exchange difference on retranslation of share capital		(0.8)	–	–	–	0.8	–
Amount recognised directly in equity		277.9	612.0	–	–	0.8	890.7
Net profit		–	–	3.9	–	–	3.9
At 31 December 2009		277.9	612.0	3.9	–	0.8	894.6

Notes to the Financial Statements of Brit Insurance Holdings N.V.

1 General information

Brit Insurance Holdings N.V. (the Company) was incorporated and registered in the Netherlands on 22 June 2009 as a public company limited by shares with registered number 24464323. The address of the registered office is provided in the Shareholder and Depositary Interest Holder Information page. The nature of the Group's operations and its principal activities are included in the Report of the Directors.

Following a corporate reorganisation, Brit Insurance Holdings N.V. became the ultimate holding company of the Brit Insurance Group on 21 December 2009. For further information relating to the corporate reorganisation, see Note 2 to the consolidated financial statements.

2 Accounting policies

Basis of preparation

The parent company accounts are prepared in accordance with the financial reporting requirements included in Part 9 of Book 2, of the Dutch Civil Code. The accounting policies applicable to presentation and disclosures are in accordance with the financial reporting requirements included in Part 9 of Book 2, of the Dutch Civil Code. The principles of valuation and determination of results stated in connection with the consolidated balance sheet and income statement are also applicable to the parent company balance sheet and income statement with the exception of investments in Group companies which are initially recognised at cost and subsequently accounted for using the equity method of accounting.

The income statement of the holding company, Brit Insurance Holdings N.V., has been drawn up in accordance with Section 402, Book 2, of the Dutch Civil Code, allowing a simplified format.

Other accounting policies

(i) Investments

Subsidiaries are stated at their net asset value, determined on the basis of IFRS as applied in the consolidated financial statements of the Group. For details on the accounting policies applied for the subsidiaries refer to the consolidated financial statements.

(ii) Cash and cash equivalents

Cash comprises cash at banks and in-hand. Cash equivalents are short-term highly liquid investments that are readily convertible to known cash amounts, are subject to insignificant risks of changes in value and are held for the purpose of meeting short-term cash commitments.

(iii) Impairment of assets

An asset is impaired if the carrying amount exceeds the amount that would be recovered through its use or sale.

(iv) Subordinated borrowings

A financial instrument issued by the Company is classified as a liability if the contractual obligation must be settled in cash or another financial asset or through the exchange of financial assets and liabilities at potentially unfavourable conditions for the company. Subordinated borrowings are initially recognised at their fair value including directly attributable transaction costs and are subsequently carried at amortised cost using the effective interest rate method. Fair value is normally determined by reference to the fair value of the proceeds received.

(v) Foreign currency translation

The financial statements are presented in Sterling which is the Company's presentational and functional currency.

Foreign currency transactions are recorded using the exchange rates prevailing at the dates of the transactions or at the average rate for the period when this is a reasonable approximation.

Monetary assets and liabilities denominated in foreign currencies are translated at period end exchange rates. Non-monetary assets and liabilities that are measured at historical cost denominated in a foreign currency are not retranslated. The resulting exchange differences on translation are recorded in the income statement.

(vi) Recognition and derecognition of financial assets and financial liabilities

Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the contract.

A financial asset is derecognised when either the contractual rights to the asset's cash flows expire, or the asset is transferred and the transfer qualifies for derecognition under a combination of risks and rewards and control tests.

A financial liability is derecognised when it is extinguished which is when the obligation in the contract is discharged, cancelled or expired.

(vii) Offsetting of assets and liabilities

Financial assets and liabilities are offset in the balance sheet when the Company has a legally enforceable right to offset and has the intention to settle the assets and liabilities on a net basis or simultaneously.

(viii) Revaluation reserve

The revaluation reserve includes unrealised gains on financial investments that do not have a frequent market listing.

Notes to the Financial Statements of Brit Insurance Holdings N.V. continued

3 Investment in subsidiaries

	31 December 2010 £m	31 December 2009 £m
As at 1 January/on incorporation	894.6	–
Corporate reorganisation	–	890.7
Result of Group companies after taxation	115.7	3.9
Other movements	8.3	–
As at 31 December	1,018.6	894.6

For a list of the subsidiaries of the Company, refer to Note 37 of the consolidated financial statements.

4 Share capital

	31 December 2010 £m	31 December 2009 £m	31 December 2010 £m	31 December 2009 £m	31 December 2010 Number in millions	31 December 2009 Number in millions (restated)
Authorised:						
Ordinary shares	700.9	885.0	820.0	1,000.0	250.0	250.0
Allotted, issued and fully paid:						
Ordinary shares	221.9	277.9	259.6	314.0	79.2	78.5

As at 31 December 2010, the nominal value per ordinary was €3.28 (2009: €4.00) (restated).

Share capital has been translated from Euros into Sterling using an exchange rate of 1.17 as at the end of the year (2009: 1.13).

	31 December 2010 Number in millions	31 December 2009 Number in millions (restated)
Ordinary shares in issue		
At 1 January/on incorporation	78.5	–
Issue of ordinary shares on corporate reorganisation	–	78.5
Issued in respect of capital distribution	0.7	–
At 31 December	79.2	78.5

On 25 February 2010, the Company undertook a consolidation of its share capital, such that the shareholders received one ordinary €4 share for every four ordinary €1 shares owned as at that date.

5 Capital distributions

At the time of the Group reorganisation in December 2009, it was announced that for an initial period the Company would make distributions to shareholders by way of reductions of the par value of Brit Insurance Holdings N.V. shares.

	Amount (pence per ordinary share)	Settled with cash 31 December 2010 £m	Settled with shares 31 December 2010 £m	Total 31 December 2010 £m	Total 31 December 2009 £m
Distribution paid					
Final 2009	30.1	17.4	5.9	23.3	–
Interim 2010	30.4	23.7	–	23.7	–
		41.1	5.9	47.0	–

A final distribution of 30.1p per ordinary share for the year ended 31 December 2009 was approved by the Annual General Meeting on 6 May 2010 and paid on 15 July 2010. This was satisfied in the form of 675,217 newly issued shares for shareholders who elected to take the distribution in the form of a scrip and £17.4m in cash for the remaining shareholders. As a result of the distribution, the nominal value of the share capital was reduced by 36 eurocents from €4.00 to €3.64 in respect of each registered share.

An interim distribution of 30.4p per ordinary share for the period ended 30 June 2010 was approved by the General Meeting on 23 September 2010 and paid on 7 December 2010. As a result of the distribution, the nominal value of the share capital was reduced by 36 eurocents from €3.64 to €3.28 in respect of each registered share.

No final distribution has been recommended for the year ended 31 December 2010.

Notes to the Financial Statements of Brit Insurance Holdings N.V. continued

6 Long-term borrowings

				31 December 2010			31 December 2009	
	Maturity	Call	Effective interest rate %	Coupon %	Amortised cost £m	Fair value £m	Amortised cost £m	Fair value £m
Amounts payable after five years								
Lower Tier Two subordinated debt	2030	2020	6.84	6.625	133.0	89.4	132.8	95.6
					133.0	89.4	132.8	95.6

The fair value represents trading market values on recognised exchanges at the balance sheet date.

Lower Tier Two subordinated debt

The Lower Tier Two subordinated debt is callable in whole by the Group on 9 December 2020. Following this date the interest rate resets to 3.4% above the 10-year gilt rate prevailing at the time. The effective interest rate method of accounting has been applied over the term up to the call date.

7 Auditors' remuneration

For information relating to auditors' remuneration, refer to Note 13 of the consolidated financial statements.

8 Guarantees and contingent liabilities

The Company has provided a guarantee to the lenders of a £175m revolving credit facility. This facility has been entered into by Brit Group Holdings B.V., a subsidiary of the Company.

For information relating to guarantees and contingent liabilities, refer to Note 39 of the consolidated financial statements.

9 Board remuneration

Detailed information on remuneration of active and retired members of the Board of Directors including their share-based incentives and their interests in the shares of the Company are included in the Directors' remuneration report.

10 Share-based payments

For information relating to share-based payments, refer to Note 36 of the consolidated financial statements.

11 Commitments

For further information relating to commitments, refer to Note 34 of the consolidated financial statements.

12 Post balance sheet events

For further information relating to post balance sheet events, refer to Note 40 of the consolidated financial statements.

Authorisation of Parent Company Financial Statements

Amsterdam 24 February 2011

Robert John Orr Barton
Dane Jonathan Douetil
Joseph Patrick MacHale
Peter Frank Hazell
Maarten Joannes Hulshoff
Cornelis Antonius Carolus Maria Schrauwers
Willem Frans Casimir Stevens

Other information

Statutory requirements for appropriation of results

The Company's Articles of Association contain the following requirements regarding appropriation of results:

The profit will be distributed pursuant to Articles 86 to 90 of the Articles of Association of Brit Insurance Holdings N.V.

The provisions can be summarised as follows:

Subject to the provisions of the Civil Code, the Board of Directors may from time to time and at any time declare and make distributions on shares other than dividends of such amounts and on such dates and in respect of such periods as it thinks fit.

The profits realised in a financial year are at the disposal of the General Meeting but no distributions declared by the General Meeting shall exceed the amount proposed by the Board of Directors.

No distribution shall be paid otherwise than out of profits available for distribution under the provisions of the Civil Code.

Subject to the provisions of the Civil Code, if and so far as in the opinion of the Board of Directors the profits of the Company justify such payments, the Board of Directors may from time to time declare and pay interim distributions on shares of such amounts and on such dates and in respect of such periods as it thinks fit.

Distributable reserves

Brit Insurance Holdings N.V. is subject to legal restrictions on the amount of distributions it can make to shareholders. Under Dutch law the amount that is available for distribution consists of total shareholders' equity less the issued and outstanding capital and less any legal reserves. The distributable reserves as at 31 December 2010 were £734.4m (2009: £616.7m).

Proposed appropriation of result

	£m
Net result	110.5
Distributions out of net result	—
Transferred to retained earnings	110.5

At the time of the Group reorganisation in December 2009, it was announced that for an initial period the Group would make distributions to shareholders by way of reductions of the par value of Brit Insurance Holdings N.V. shares (i.e. in the form of a capital distribution).

For information relating to capital distributions made during the year, refer to Note 5.

No final distribution has been recommended for the year ended 31 December 2010.

Independent auditor's report on the Parent Company Financial Statements

To: The Meeting of Shareholders of Brit Insurance Holdings N.V.

Report on the company financial statements

We have audited the accompanying Company financial statements 2010 which are part of the financial statements of Brit Insurance Holdings N.V., Amsterdam, and comprise the Company balance sheet as at 31 December 2010, the income statement and the statement of changes in equity for the year then ended and the notes, comprising a summary of the accounting policies and other explanatory information.

Directors' responsibility

The Directors are responsible for the preparation and fair presentation of these Company financial statements and for the preparation of the Directors' board report, both in accordance with Part 9 of Book 2 of the Dutch Civil Code. Furthermore the Directors are responsible for such internal control as it determines is necessary to enable the preparation of the Company financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these Company financial statements based on our audit. We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. This requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Company financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the company financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the company financial statements, whether due to fraud or error.

In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the company financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the company financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion with respect to the Company financial statements

In our opinion, the Company financial statements give a true and fair view of the financial position of Brit Insurance Holdings N.V. as at 31 December 2010 and of its result for the year then ended in accordance with Part 9 of Book 2 of the Dutch Civil Code.

Report on other legal and regulatory requirements

Pursuant to the legal requirement under Section 2:393 sub 5 at e and f of the Dutch Civil Code, we have no deficiencies to report as a result of our examination whether the Directors' board report, to the extent we can assess, has been prepared in accordance with Part 9 of Book 2 of this Code, and whether the information as required under Section 2:392 sub 1 at b-h has been annexed. Further we report that the Directors' board report, to the extent we can assess, is consistent with the Company financial statements as required by Section 2:391 sub 4 of the Dutch Civil Code.

The Hague, 24 February 2011

Ernst & Young Accountants LLP

Signed by S.B. Spiessens

Other Information

142 Glossary

145 Shareholder and Depositary
Interest Holder Information

Glossary

A

Aggregate exposure

The maximum total of claims that can be incurred by an insurer in respect of any event or series of similar events. It is usually related to a particular risk type, class of business and/or geographical area. Also see 'realistic disaster scenario'.

Asset allocation

The process of dividing our investments among different kinds of assets, such as stocks, bonds, property and cash, in order to achieve a balance between return and risk.

B

Bordereaux

A detailed list of financial information (e.g. premiums or claims) prepared by cedants or coverholders for periodic submission to underwriters to advise them of risks covered and claims incurred.

C

Capacity

The maximum premium income which an insurer is permitted to underwrite. For a Lloyd's syndicate, a capacity figure is assigned to each underwriting year and is defined as gross written premiums less commissions payable.

Cell

See 'Protected cell company'.

Casualty

A class of insurance, mainly comprising accident and liability business.

Claims

Demand by an insured for indemnity under an insurance contract.

Claims development triangles

Tabulations of claims development data. This data is set out with underwriting years along one axis and years of development. (e.g. calendar year end dates) along the other.

Claims incurred

Claims that have occurred, regardless of whether or not they have been reported to the insurer.

Claims ratio

Ratio, in per cent, of net claims incurred to net earned premiums.

Combined ratio

Ratio, in per cent, of net claims incurred, acquisition costs plus insurance related administrative expenses to net earned premiums. Also the sum of the claims ratio and the expense ratio.

Coverholder

See 'Delegated authority'.

D

Deferred acquisition costs (DAC)

Costs incurred for the acquisition or renewal of insurance policies (e.g. brokerage and underwriter related costs) which are capitalised and amortised over the term of those policies.

Delegated authority

An authority granted by an underwriter to an agent (known as a coverholder) whereby that agent is entitled to accept, within certain limits, insurance business on behalf of the underwriter. The coverholder deals with premium collection, the issue of certificates and the servicing of claims, and has full power to commit the underwriter within the terms of the authority.

E

Earned premium

That proportion of a premium which relates to the portion of a risk which has expired during the period.

Earnings per share (EPS)

Basic:

Ratio, in pence, calculated by dividing the consolidated profit after tax by the weighted average number of ordinary shares issued, excluding shares owned by the Group.

Diluted:

For calculating diluted earnings per share the number of shares and profit or loss for the year is adjusted for all dilutive potential ordinary shares such as share options granted to employees.

Expense ratio

Acquisition costs plus insurance related administrative expenses divided by net earned premiums.

G

Gearing ratio

Ratio, in per cent, of total borrowings to total capital resources.

Gross written premium (GWP)

Amounts payable by the insured, including any brokerage or commission deducted by intermediaries but excluding any taxes or duties levied on the premium.

Gross written premium represented by catastrophe exposed premium

Percentage of Group calendar year GWP with potential exposure to catastrophic events.

H

Hard market

An insurance market where prevalent prices are high, with more restrictive terms and conditions offered by insurers.

Glossary continued

I

IFRS

International Financial Reporting Standards. Standards formulated by the International Accounting Standards Board (IASB). UK listed entities have reported on an IFRS basis since 2005.

Incurred but not reported (IBNR)

Anticipated or likely claims that may result from an insured event although no claims have been reported so far.

Investment return

Investment return is calculated using the 'Dietz' method. This method calculates a return percentage for the average funds invested over a month. It assumes that all net contributions take place in the middle of the period. The annual return is calculated by geometrically adding the monthly returns figures.

L

Lead underwriter/lead

A lead underwriter (usually a specialist in the field of the insurance concerned) is the first underwriter to take a portion of a risk and quote an appropriate rate of premium.

LIBOR

London Interbank Offered Rate. An interest rate at which banks can borrow funds, in marketable size, from other banks in the London interbank market.

Line size

The proportion of an insurance or reinsurance risk that is accepted by an underwriter or which an underwriter is willing to accept.

Long-tail

The difference between the average claim payment and the average premium payment term. Long tail is over three years.

Long-term subordinated debt

Subordinated borrowings which have at least five years remaining to maturity or call and are of types which qualify as regulatory capital.

M

Medium-tail

The difference between the average claim payment and the average premium payment term. Medium tail is 1.5 to three years.

MMI scale

The Modified Mercalli Intensity (MMI) scale measures the shaking severity generated by an earthquake. The scale ranges from 'I' (not felt) to 'XII' (damage nearly total).

Monoline insurers

An insurer who has exposure to only one line of business.

N

Net tangible assets per share

Shareholder funds less intangible assets divided by the number of shares in issue at the balance sheet date less own shares.

Net written premiums

Gross written premiums less outwards reinsurance premiums.

O

Outstanding claims

Claims which have been notified at the balance sheet date but not settled.

P

Protected cell company (PCC)

A company that has been separated into legally distinct portions or cells. The revenue streams, assets and liabilities of each cell are kept separate from all other cells. Each cell has its own separate portion of the PCC's overall share capital, allowing shareholders to maintain sole ownership of an entire cell while owning only a small proportion of the PCC as a whole. PCCs can provide a means of entry into captive insurance markets to entities for which it was previously uneconomic.

R

Rating model

A formal, structured tool to assist an underwriter in setting a price for a risk.

Realistic disaster scenario (RDS)

A stress test for underwriting entities to show how they withstand accumulated exposure. Levels of claims are assessed in respect of a number of hypothetical disaster scenarios, using consistent and appropriate methods and assumptions. Also see 'aggregate exposure'.

Reserves

Outstanding claims and claims incurred but not reported (IBNR).

Retention ratio

Ratio, in per cent, of the value of premiums written in one year renewed in the following year.

Retrocession/retrocessional

Reinsurance of the reinsurance account.

Return on equity (RoE)

Profit after tax achieved by the Group adjusted for movements charged to the income statement in respect of intangible assets, divided by opening net tangible assets adjusted on a weighted average basis for share issues or buy-backs during the period.

Glossary continued

S

Short-tail

The difference between the average claim payment and the average premium payment term. Short tail is under 1.5 years.

Soft market

An insurance market where prevalent prices are low, and terms and conditions offered by insurers are less restrictive.

Solvency II

Initiative launched by the European Commission to revise current EU insurance solvency rules. Solvency II focuses on capital requirements, risk modelling, prudential rules, supervisory control, market discipline and disclosure and is currently forecast to apply from 2012.

Specialised investment funds

Investments in assets with low correlation to interest rate and equity price movements.

SS scale

The Saffir-Simpson (SS) scale is used to classify hurricanes from category 1 (wind speed 74 to 95 mph) to category 5 (wind speed 156+ mph). The SS scale evaluates winds and storm surge generated by the hurricane over open water pre-landfall.

Strategic Business Unit (SBU)

Underwriting division of Brit Insurance. Brit Insurance underwrites through three SBUs: Global Markets, Reinsurance and UK.

T

Tail

See 'short-tail', 'medium-tail' and 'long-tail'.

Technical price

The price for the risk which is expected to produce the long-term required return on capital for the Group.

Total capital resources

Net tangible assets plus long-term subordinated debt.

Total invested assets

The sum of 'financial investments', 'assets held for sale' and 'cash and cash equivalents'.

U

Ultimate loss ratio (ULR)

The ratio of the sum of paid claims, outstanding claims and IBNR to premiums, all of which can be expressed either gross or net of reinsurance recoveries and reinsurance premiums.

Underlying premium growth

Increase in Gross Written Premium between two calendar years where the earlier year is restated using the exchange rates applicable to the latter year.

Underwriting profit

Profit before tax arising from each SBU less investment return.

Unearned premium reserve (UPR)

The portion of premium income written in the calendar year that is attributable to periods after the balance sheet date. It is accounted for as unearned premiums in the underwriting provisions.

Shareholder and Depositary Interest Holder Information

Annual General Meeting

Details of the 2011 Annual General Meeting (AGM) will be contained in the AGM notice of meeting.

Publication

The sections in this document titled Report of the Directors and Financial Statements and Other Information together form the 2010 annual report, the 2010 financial statements and other information of Brit Insurance Holdings N.V. as required by Dutch law.

Filing

After they have been adopted, the 2010 annual report, the 2010 financial statements and other information will be filed at the offices of Trade Registry of the Chamber of Commerce and Industries under number 24464323.

Website

Our website, www.britinsurance.com, contains

- ▶ The Company's latest results, and key dates and announcements
- ▶ Current and past Annual Reports
- ▶ Current and historic Brit insurance share price information and distribution history
- ▶ Presentations and webcasts of financial results
- ▶ Announcements

Registered address

The Company's Head Office is located at: SOM II, Claude Debussylaan 11, 1082 MC Amsterdam, The Netherlands.

All correspondence to the Company should be conveyed to the following address.

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T: +44 (0)20 7098 6626

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T: +44 (0)20 7417 8989

Managing your shareholding or Depositary Interest holding

Computershare Investment Services Plc maintains the Company's register of members and in respect of the holders of Depositary Interests.

Computershare can be contacted for any queries regarding your holdings at:

The Pavilions, Bridgwater Road, Bristol
BS13 8AE, United Kingdom

Tel: +44 (0)871 495 0102

Fax: +44 (0)870 703 6116

Website: www.computershare.com

(at the date of this document calls to this number are charged at 8p per minute from a BT landline, other telephone providers' costs may vary)

Unsolicited phone calls or mail

Shareholders and Depositary Interest holders are advised to be very wary of any unsolicited advice, offers to buy shares at a discount or offers for free company reports. These are typically from 'brokers' who target shareholders offering to sell them what often turns out to be worthless or high risk shares in US or UK investments.

If you receive any unsolicited investment advice:

- ▶ Make sure you get the correct name of the person and organisation; and
- ▶ Check that they are properly authorised by the FSA before getting involved. You can check at www.fsa.gov.uk/register.

For further information on avoiding fraud please see the FSA website at www.moneymadeclear.fsa.gov.uk/news/scams/share_scams.html

Auditor

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