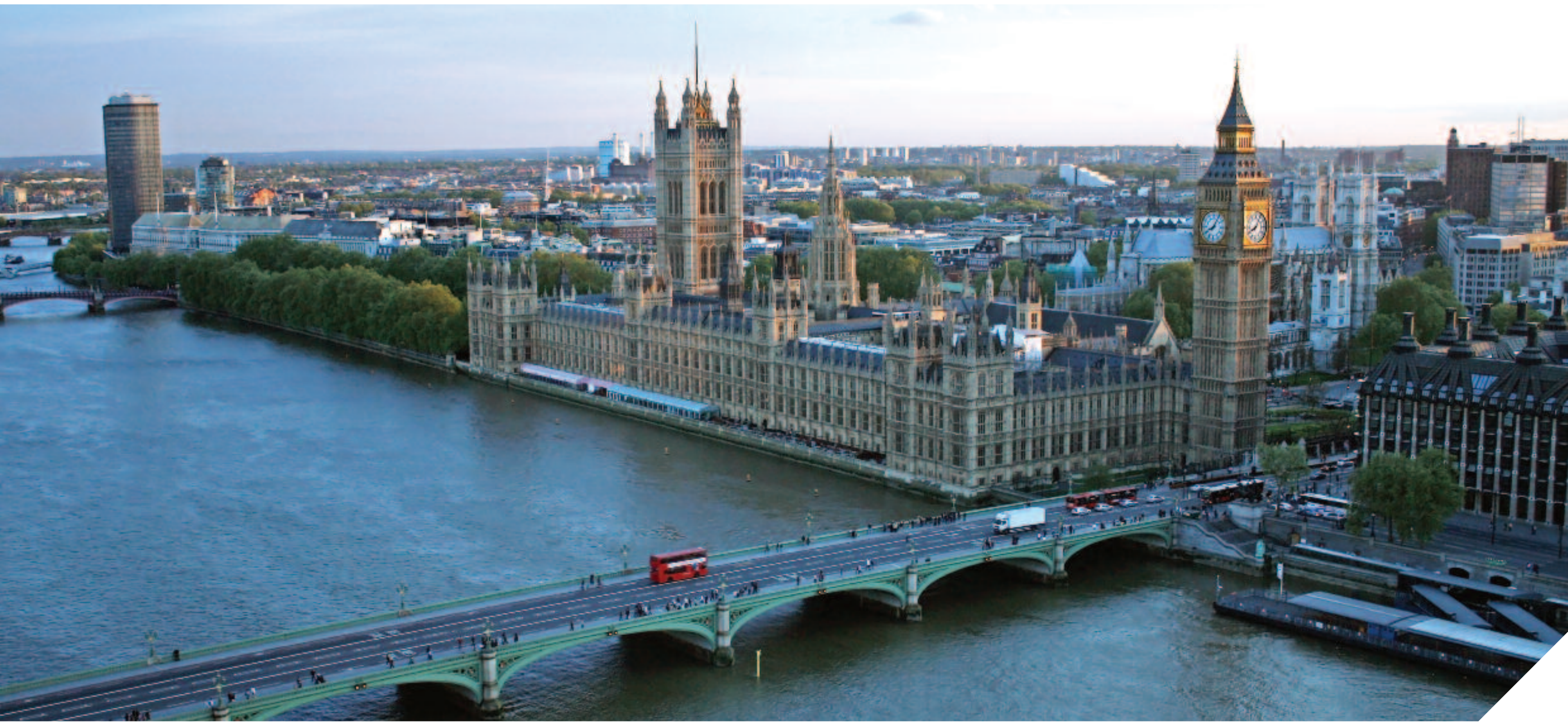

# ANNUAL REPORT 2012

## Great Lakes Reinsurance (UK) PLC

Risk Solutions

Munich RE

# CONTENTS

# DIRECTORY

### Directors

A. J. Medniuk (Chairman)
P. Göschl (Chief Executive Officer)
G. Guelfand (Chief Financial Officer)
G. Funke
A. A. Pröbstl
N. H. H. Smith
T. J. Carroll (appointed 3 January 2013)

### Secretary

S. G. Pendlebury

### Registered Office

Munich Re Group
Plantation Place
30 Fenchurch Street
London EC3M 3AJ

Telephone: +44 (0)20 3003 7000
Facsimile: +44 (0)20 3003 7010
Email: correspondence@greatlakes.co.uk

### Auditors

KPMG Audit Plc
15 Canada Square, London, E14 5GL

### Bankers

Barclays Bank PLC
The Bank of New York Mellon
HSBC Bank PLC
ANZ Banking Group Limited
Aargauische Kantonalbank
Zürcher Kantonalbank
CACEIS Bank Deutschland GmbH

### Registered Number

02189462

# REPORT OF THE DIRECTORS

The Directors present their annual report together with the audited financial statements of Great Lakes Reinsurance (UK) PLC ("the Company") for the year ended 31 December 2012 and the auditor's report thereon.

## Principal Activities and Business Review

### Principal Activities

The Company is authorised by the Financial Services Authority to transact all classes of non-life insurance and reinsurance in the United Kingdom and throughout the European Union via the Freedom of Services directive. The Company also conducts business via branches in Australia, New Zealand, Switzerland, Italy, and Ireland and is authorised to write surplus lines business in the USA. The Company is registered in England under registration number 02189462.

The Company is a wholly owned subsidiary of Münchener Rückversicherungs-Gesellschaft AG ("Munich Re"), a limited liability company incorporated in Germany and is therefore part of the Munich Re group. The Company acts as a specialist provider of insurance business for the group by using its licenses and relationship with other group members to develop insurance solutions for their customers.

### High Level Strategy

The Company's principal mission is to add value to the Munich Re group by being a leading provider of insurance solutions. This is done in collaboration with Munich Re to develop business opportunities, using our combined technical expertise and knowledge in insurance markets worldwide.

Strategy is formulated during the annual planning process when a business plan is developed and approved, and subsequent implementation is controlled and measured via regular monitoring. The necessary challenge and approval is provided by a quarterly Board review process. The strategy and resulting initiatives are communicated to staff and aligned with individual performance objectives. The Company is committed to empowering staff to make decisions in line with an appropriate level of authority.

While 1 January 2014 is still the official implementation date for Solvency II, during 2012 it became clear that due to the need for agreement on measures to address the Solvency II implications of products with long term guarantees, it is most unlikely that the Directive will be in place by that date. The revised implementation date remains unclear, but a one or two year delay is widely anticipated. Nevertheless the Company intends to maintain the momentum gained on its Solvency II project to date, and will use the additional time to further embed its models, enhance its risk management, governance framework and reporting processes and functionality.

### Business Review and Key Performance Indicators (KPIs)

The Company uses two distinct models for accessing insurance business – delegated acceptances via agency agreements and individual acceptances of large single risks. Overall, gross written premium in 2012 was 8.6% higher than in 2011, with positive gross underwriting performance. Agency sourced business continues to provide the dominant share of the Company's gross written premium, at approximately 82% and remained stable as a percentage of the total premium. The agency book is constantly monitored through a suite of quarterly KPIs to ensure the quality of the underlying business is not sacrificed for increased growth. The key focus remains on profitable underwriting and cycle management. Gross loss and combined ratios have decreased year on year, largely impacted by positive developments in Liability, Aviation and Marine lines of business. The 2012 year was largely benign in the way of large losses in comparison to 2011. The Company retains the business it underwrites through the Corporate Insurance Partner (CIP) division based in London. CIP offers a highly respected underwriting service to the world's 5000 largest companies and leading players in their industries as well as their captives. Standard and bespoke solutions in the classes of Property, Engineering, Energy, and Casualty, are developed through close cooperation with clients.

| KPIs | 2012 | 2011 | |
|---|---|---|---|
| Gross Written Premium £m | 2,077.4 | 1,913.7 | Gross premium written before outwards reinsurance |
| Gross Loss Ratio | 53.5% | 60.0% | Ratio of gross claims incurred to gross earned premiums |
| Gross Combined Ratio | 81.5% | 90.8% | Ratio of gross claims incurred, commissions and expenses to gross premium earned |
| Administrative Expense Ratio | 1.6% | 1.6% | Ratio of administrative expenses to gross premium earned |
| Profit Before Tax £m | 37.6 | 57.6 | Operating profit from ordinary activities before tax |
| Shareholder's Funds £m | 373.7 | 346.1 | Excess of assets over liabilities supporting business model |
| Solvency Margin | 209.8% | 210.5% | Ratio of the adjusted capital to minimum capital requirements |

Profit before tax of £37.6m for the year ended 31 December 2012 is £20.0m lower compared to the 2011 result. The main drivers of this lower result were the cost of reinsurance protections on the CIP London portfolio and the decrease in the investment result for 2012. The decrease in the investment return was primarily due to an increase in bond yields resulting in a reduction in unrealized gains. The Company invests in a conservative portfolio of fixed interest instruments. 90% of the total investment portfolio is invested in government bonds with approximate exposures by country as follows; United Kingdom 56%, United States 23%, Germany 5%, France 4%, Australia 5% and Others 7%. The Company's investment portfolio stands at £518.3m as at 31 December 2012 compared to £605.2m in 2011.

Shareholder's funds as at 31 December 2012 total £373.7m (2011 £346.1m). The Company's solvency margin remains very strong. The Company continually monitors its solvency adequacy and maintains a very satisfactory margin to ensure compliance with regulatory requirements and promote efficient capital management. The Company is rated A+ Superior by A M Best and AA- Strong by Standard and Poor's.

### Proposed Dividend

The directors have proposed a dividend of 184.2p per share equalling £21.0m in respect of the 2012 financial year. This dividend is subject to approval at the Board meeting on 26 March 2013.

### Management and Employees

The Company has a management agreement with Munich Re UK Services Limited, a wholly owned subsidiary of Munich Re. Munich Re UK Services Limited employs all the Company's UK personnel providing full administration management services. Accordingly the Company has no employees of its own.

### Risk Management

Risk management is a key part of the Company's corporate Management and company culture. Its purpose is not only to safeguard the Company's financial strength, enabling the Company to meet its obligations to clients and create sustained value, but also to protect the Company's reputation. This is achieved through risk management practices encompassing all areas of operation. The overall risk appetite of the Company is determined by the Board with support from Munich Re. The risk appetite laid down ensures an appropriate balance is maintained between business opportunities and risks taken against capital deployed. The risk appetite for each risk is reflected in business planning and integrated into the management of operations. The Board is accountable for risk topics for the Company as a whole and these are managed operationally through senior management and governed by the Audit, Risk and Capital and Investment Committees. The Remuneration Committee of the Board of Directors is responsible for ensuring that the structure of the remuneration arrangements for employees is aligned with the achievement of the Company's objectives and integrated with the application of its risk management principles.

### Principal Risks and Uncertainties

The Company's business involves the acceptance and management of risk. The Company has in place a risk management process, which is undertaken in accordance with both the Munich Re Group Risk Management framework and the Company's solvency capital calculations. This is used to manage capital requirements and to ensure the appropriate financial strength and capital adequacy support business growth, and meet the requirements of the shareholder, regulators, rating agencies, and the obligations to policyholders. A number of risk factors affect the Company's operating results and financial health. The financial risk factors affecting the Company include the effects of market risk, credit risk and liquidity risk on the financial instruments of the Company. The Company has a very low risk appetite for these risks, and manages them accordingly.

### Underwriting Risk Management

The Company has a medium appetite for insurance underwriting risk. Underwriting risk is defined as the risk of insured losses being higher than our expectations. Premium risk is the risk of future claims payments relating to insured losses that have not yet occurred being higher than expected. The reserve risk is the risk of technical provisions raised to cover losses that have already been incurred being insufficient. These risks are managed through underwriting authority management, reserve calculation assumptions/methods and a range of other internal processes/controls.

### Market Risk Management

Market risk is the risk that future changes in market prices may make a financial instrument less valuable. The primary market risks that the Company faces are interest rate and currency risk. Most of its assets are investments that are fixed interest securities and short term cash deposits, the value of which are subject to interest rate and currency risk. The Company maintains financial assets with similar duration, cash flow and currency characteristics as the underlying insurance liabilities in order to minimise these risks. Projected payment patterns of insurance liabilities are used to create a proposed benchmark investment portfolio in terms of asset liability matching. This benchmark investment portfolio is part of the mandate of the Company's investment manager, who reports on the comparison of the actual investment portfolio against the benchmark. The monitoring and performance of the investment portfolio is the responsibility of the Investment Committee, the results are reported to the Audit Committee and are monitored by the Board.

### Credit Risk Management

Credit risk is the risk that a counterparty or an issuer of securities, which the Company holds in its asset portfolio, defaults or another party fails to perform according to the terms of the contract. A mandate is in place that governs investment exposure to a very low risk in accordance with the Company risk appetite. The Company's investment manager reports on compliance with the mandate in respect of credit risk exposure in the investment portfolio. The results of this compliance are reported to the Audit and Investment Committees, and are monitored by the Board.

### Liquidity Risk Management

Liquidity risk is the risk that the Company may be unable to meet its payment obligations in a timely manner at a reasonable cost. Liquidity management in the Company seeks to ensure that, even under adverse conditions, the Company has access to the funds necessary to cover its claims obligations. Most of the Company's assets are highly marketable securities, which reduces the liquidity risk.

### Operational Risk Management

The Company has a very low appetite for operational risks with the exception of business obtained via delegated binding authorities where, subject to appropriate mitigation strategies, the Company has a medium risk appetite. The Company subscribes to Munich Re best practice standards for the operation of agency programme arrangements, and collectively these measures help to de-risk the operational aspects of the business to acceptable levels. The Company is committed to minimising risk for all transactions and has developed a risk based system for monitoring agency business, which includes a programme of regular on site reviews.

### Group Risk

Significant benefits are derived from being part of Munich Re group and group risk is primarily managed at the executive level through building strong relationships. We are exposed to group risk in a number of areas, as we utilise group resources for asset management, systems, reinsurance and capital support. The activities of the wider group could affect our strategy and reputation, in particular our regulatory, social and ethical standing and client perception. Business objectives are aligned to the Munich Re group strategy and, where appropriate, the Board adheres to the relevant group policies, guidelines and reporting requirements.

### Risk Monitoring and Control

The Company identifies, records and assesses all relevant risks and controls using the Internal Control System("ICS") that is part of a Munich Re group-wide harmonised control and monitoring system. This provides a uniform system for managing risks across all risk dimensions that both meets Group management needs and satisfies local legal and regulatory requirements. Risk owners at the operational level are charged with keeping the ICS current and relevant. A key risk report is produced quarterly and is provided to the Audit Committee who then report the key points to the Board. The report provides, for all risk categories, an updated view of the current risk position (including key events and quantitative changes) and compares the position with the Company risk appetite. In December 2012 the Risk and Capital Committee became a sub-committee of the Board and responsible for risk monitoring and control.

### Environment

The Company does not have a major direct environmental impact as it is essentially service based and operates in a nonmanufacturing industry. However, it is aware of its environmental responsibilities and actively strives to reduce its carbon footprint.

## Directors & Directors' Interests

The directors of the Company at the date of this report are set out on page 2. Changes in directors during 2012 and up to the date of this report are as follows:

| | Date of appointment |
|---|---|
| T.J. Carroll | 03 January 2013 |

None of the directors had a beneficial interest in the shares of the Company. Under the provisions of the Companies Disclosure of Directors' Interests (Exceptions) Regulations 2006, the directors of the Company are exempt from disclosing any interests in the shares of the ultimate holding company.

## Major Shareholdings

The Company is a wholly owned subsidiary of Munich Re, a company incorporated in Germany. Copies of the Munich Re group accounts are available from Königinstrasse 107, 80802, Munich, Germany.

## Creditors Payment Policy

All suppliers are paid via the Company's service company, Munich Re UK Services Limited. Creditors for the supply of goods and services not including insurance had an average payment period of 7 days (2011: 7 days).

## Disclosure of information to Auditors

The directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant information of which the Company's auditors are unaware; and that each director has taken all the steps that ought to have been taken as a director to be aware of any relevant audit information, and to establish that the Company's auditors are aware of that information.

## Auditors

Pursuant to section 487 of the Companies Act 2006, the auditors will be deemed to be reappointed and KPMG Audit Plc will therefore continue in office.

By order of the Board

**S. G. Pendlebury**
Company Secretary,
26 March 2013

# STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS

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

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

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

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included in the Company's website. Legislation in the United Kingdom governing the presentation and dissemination of financial statements may differ from the legislation in other jurisdictions.

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF GREAT LAKES REINSURANCE (UK) PLC

We have audited the financial statements of Great Lakes Reinsurance (UK) PLC for the year ended 31 December 2012 set out on pages 8 to 27. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

**Respective responsibilities of directors and auditor**

As explained more fully in the Directors' Responsibilities Statement set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

**Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

**Opinion on financial statements**

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2012 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

**Opinion on other matter prescribed by the Companies Act 2006**

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

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

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

**Mark Taylor (Senior Statutory Auditor)**
**for and on behalf of KPMG Audit Plc, Statutory Auditor**

Chartered Accountants
15 Canada Square
London E14 5GL

26 March 2013

# PROFIT AND LOSS ACCOUNT

## Technical Account - General Business
## for the year ended 31 December 2012

| | Notes | 2012 £'000 | 2011 £'000 |
|---|---|---|---|
| Gross premiums written | 3 | 2,077,422 | 1,913,734 |
| Outwards reinsurance premiums | | 1,920,446 | 1,789,544 |
| Net premiums written | | **156,976** | **124,190** |
| Change in the gross provision for unearned premiums | 14 | (84,794) | (47,325) |
| Change in the provision for unearned premiums - reinsurers' share | 14 | (56,494) | (43,318) |
| Change in the net provision for unearned premiums | | (28,300) | (4,007) |
| Earned premiums, net of reinsurance | | **128,676** | **120,183** |
| Investment return allocated from the non-technical account | | 12,433 | 24,360 |
| Other technical income, net of reinsurance | | 30,064 | 29,085 |
| **TECHNICAL INCOME** | | **171,173** | **173,628** |

# PROFIT AND LOSS ACCOUNT

## Technical Account - General Business
## for the year ended 31 December 2012

| | Notes | 2012 £'000 | 2011 £'000 |
|---|---|---|---|
| Gross claims paid | | 900,888 | 978,385 |
| Reinsurers' share | | 861,568 | 946,112 |
| Claims paid - net | | **39,320** | **32,273** |
| Change in the gross provision for claims | 14 | 165,518 | 142,152 |
| Reinsurers' share | 14 | 145,201 | 135,938 |
| Change in the provision for claims - net | | **20,317** | **6,214** |
| Claims incurred net of reinsurance | | 59,637 | 38,487 |
| Net operating expenses | 5 | 70,575 | 77,717 |
| **TECHNICAL EXPENSES** | | **130,212** | **116,204** |
| **BALANCE ON THE TECHNICAL ACCOUNT FOR GENERAL BUSINESS** | | **40,961** | **57,424** |

# PROFIT AND LOSS ACCOUNT

## Non-Technical Account
## for the year ended 31 December 2012

| | Notes | 2012 £'000 | 2011 £'000 |
|---|---|---|---|
| **BALANCE ON THE TECHNICAL ACCOUNT FOR GENERAL BUSINESS** | | **40,961** | **57,424** |
| **INVESTMENT RETURN** | | | |
| Investment income | 4 | 15,392 | 15,510 |
| Unrealised (losses) gains on investments | | (2,070) | 9,659 |
| Investment expenses and charges | | (889) | (809) |
| Total investment return | | 12,433 | 24,360 |
| Investment return allocated to the technical account | | (12,433) | (24,360) |
| | | **40,961** | **57,424** |
| Exchange (losses) gains | | (3,331) | 143 |
| **PROFIT ON ORDINARY ACTIVITIES BEFORE TAX** | 3, 6 | **37,630** | **57,567** |
| Tax on profit on ordinary activities | 8 | 8,997 | 16,255 |
| **PROFIT ON ORDINARY ACTIVITIES AFTER TAX** | | **28,633** | **41,312** |

All profits for the year and prior year relate to continuing activities. The notes on pages 14 to 27 form part of these financial statements.

# STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

## for the year ended 31 December 2012

| | Notes | 2012 £'000 | 2011 £'000 |
|---|---|---|---|
| **PROFIT FOR THE YEAR** | | **28,633** | **41,312** |
| Currency translation losses on foreign currency net investments | 13 | 983 | 75 |
| **TOTAL RECOGNISED GAINS FOR THE YEAR** | | **27,650** | **41,237** |

In accordance with the amandment to FRS 3 no note of historical cost profits has been prepared as the Company's only material gains and losses on assets relate to the holding and disposal of investments.

The notes on pages 14 to 27 form part of these financial statements.

# BALANCE SHEET

## Assets
## as at 31 December 2012

| | Notes | 2012 £'000 | 2011 £'000 |
|---|---|---|---|
| **INVESTMENTS** | | | |
| Financial investments | 9 | 518,327 | 605,213 |
| Deposit assets | | 77,334 | 95,112 |
| | | **595,661** | **700,325** |
| Investment in subsidiary | 18 | - | 50 |
| **REINSURERS' SHARE OF TECHNICAL PROVISIONS** | | | |
| Unearned premium | 14 | 889,286 | 844,761 |
| Claims outstanding | 14 | 2,194,678 | 2,092,067 |
| | | **3,083,964** | **2,936,828** |
| **DEBTORS** | | | |
| Arising out of direct insurance operations | 10 | 488,818 | 413,326 |
| Deferred tax | 8 | 9 | 1,152 |
| Other debtors | | 28,854 | 57,524 |
| | | **517,681** | **472,002** |
| **OTHER ASSETS** | | | |
| Cash at bank | 11 | **133,667** | **45,263** |
| **PREPAYMENTS AND ACCRUED INCOME** | | | |
| Accrued interest | | 5,018 | 5,888 |
| Deferred acquisition costs | 15 | 234,346 | 212,424 |
| | | **239,364** | **218,312** |
| **TOTAL ASSETS** | | **4,570,337** | **4,372,780** |

# BALANCE SHEET

## Liabilities
## as at 31 December 2012

| | Notes | 2012 £'000 | 2011 £'000 |
|---|---|---|---|
| **CAPITAL AND RESERVES** | | | |
| Called up share capital | 12 | 114,000 | 114,000 |
| Profit and loss account | 13 | 259,735 | 232,085 |
| Shareholder's funds | 3, 13 | **373,735** | **346,085** |
| **TECHNICAL PROVISIONS - GROSS** | | | |
| Unearned premium | 14 | 990,863 | 920,211 |
| Claims outstanding | 14 | 2,468,355 | 2,351,688 |
| | | **3,459,218** | **3,271,899** |
| **PROVISIONS FOR OTHER RISKS AND CHARGES** | 16 | **343** | **399** |
| **CREDITORS** | | | |
| Arising out of direct insurance operations | 17 | 389,303 | 369,545 |
| Deposit liabilities | | 112,003 | 130,464 |
| Taxation | | 6,148 | 12,355 |
| Deferred tax | 8 | - | 1,139 |
| Other creditors | | 16,365 | 43,604 |
| | | **523,819** | **557,107** |
| **ACCRUALS AND DEFERRED INCOME** | | | |
| Deferred reinsurance commissions | 15 | 213,222 | 197,290 |
| **TOTAL LIABILITIES** | | **4,570,337** | **4,372,780** |

The notes on pages 14 to 27 form part of these financial statements.

Approved by the board on 26 March 2013.

P. Göschl - Chief Executive Officer G. Guelfand - Chief Financial Officer

# NOTES TO THE ACCOUNTS

## 1. Basis of preparation of the Financial Statements

The financial statements of Great Lakes Reinsurance (UK) PLC ("the Company") have been prepared in accordance with the provisions of Sections 396 of the Companies Act 2006 including applying the requirements set out in Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 relating to insurance companies. The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules as modified to include the revaluation of investments and comply with the revised Statement of Recommended Practice (SORP) issued by the Association of British Insurers in December 2005 (as amended in December 2006).

Under FRS 1 the Company is exempt from the requirement to prepare a cash flow statement on the grounds that it is a wholly owned subsidiary of Münchener Rückversicherungs-Gesellschaft AG ("Munich Re"), which includes the Company in its own published consolidated financial statements.

As the Company is a wholly owned subsidiary of Munich Re the Company has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the group (or investees of the group qualifying as related parties). The consolidated financial statements of Munich Re, within which this Company is included, can be obtained from the Company's registered office at the address provided in the Report of the Directors on page 5.

Under section 400 of the Companies Act 2006 an exemption from preparing consolidated accounts is available, subject to certain conditions. Following an assessment of these conditions it is appropriate for the Company to take advantage of the exemption to prepare consolidated accounts and therefore these financial statements are for the Company only. Great Lakes Services Limited, a wholly owned subsidiary of the Company, has therefore not been consolidated in these accounts.

An overview of the Company's key sources of business, key performance indicators and high level strategy are set out in the Directors' Report. The Company has significant financial resources together with prudent investment policies, high quality of assets, robust underwriting procedures controls and mitigating processes including, but not limited to, reinsurance. Consequently the Directors believe that the Company is well placed to manage its business risks despite the current uncertain economic outlook. The Directors are confident that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

## 2. Accounting Policies

The following accounting policies have been applied consistently within the accounts and from one financial year to another, in dealing with items which are considered material in relation to the financial statements.

### Premiums

Written premiums comprise the amount receivable including an estimate of pipeline premiums during the financial year for the whole period the Company is on risk in respect of contracts of insurance entered into and incepting during that period, together with any further adjustments to premiums receivable for prior accounting periods that had not been fully recognised in previous financial statements. Pipeline premiums are those collected by intermediaries but not yet received, and are assessed based on estimates from underwriting or past experience. Premiums are stated before deduction of commissions but net of taxes and duties levied on premiums.

Premiums are earned over the term of the insurance policies to which they relate, in accordance with the risk coverage provided by the underlying insurance policies.

Outward reinsurance and retrocession premiums are accounted for in the same accounting period as the premiums for the underlying direct insurance or inwards reinsurance business.

### Unearned premiums

Premiums that relate to the unexpired terms of insurance policies in force at the balance sheet date are deferred as unearned premiums. These unearned premiums are taken to the Profit and Loss account so that premiums are recognised over the period of risk coverage provided by the underlying insurance policies.

### Acquisition costs

Acquisition costs comprise all direct and indirect costs arising from the conclusion of insurance and reinsurance contracts. The proportion of acquisition costs incurred in respect of unearned premiums is deferred at the balance sheet date and recognised in later periods when the related premium is earned.

### Claims incurred

Claims incurred comprise claims and claim settlement expenses (both internal and external) paid in the year and the movement in the provision for outstanding claims and settlement expenses, including an allowance for the costs of claims incurred by the balance sheet date but not reported until after the year end.

### Claims outstanding

Provision is made at the year end for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported ("IBNR") to the Company. The estimate of claims includes expenses to be incurred in settling claims and a deduction for the expected value of salvage and other recoveries.

The Company takes all reasonable steps to ensure that it has all appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, the final outcome may be different from the original liability established. The estimation of IBNR is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Company, where more information about the claim event is generally available. IBNR claims may often not emerge until many years after the underling event has happened. Classes of business where the IBNR proportion of the total reserve is high, such as liability business, will typically display greater variations between initial estimates and final outcomes because of the greater degree of uncertainty involved.

Classes of business where claims are typically reported relatively quickly after the claim event, such as property business, tend to display lower levels of volatility. In calculating the estimated cost of unpaid claims, management uses a variety of estimation techniques, generally based upon statistical analyses of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to vary when compared with the cost of previously settled claims. This includes:

- changes in processes which might accelerate or slow down the development and/or recording of paid or incurred claims compared with the statistics from previous periods;
- changes in the legal environment;
- the effects of inflation;
- changes in the mix of business (including the effect of currency fluctuations);
- the impact of large losses; and
- movements in industry benchmarks.

Specific information on individual claims are also taken into account, based for example on reports of loss adjusters. Furthermore, large claims are generally assessed separately, being measured on a case by case basis or projected separately in order to prevent distortions of the general claims development pattern.

A range of techniques are used to estimate the required level of provisions. This generates a deeper understanding of the trends inherent in the data and also assists in providing a range of possible outcomes. The most appropriate estimation technique is selected, taking into account the characteristics of the class of business and the extent of the development of each underwriting year.

Provisions are calculated gross of any reinsurance recoveries. A separate estimate is made of the reinsurers' share of provisions for claims based on calculated amounts for outstanding claims and projections for IBNR, net of estimated uncollectible amounts. Again, a range of statistical techniques are used in making these estimates.

The Directors consider that the provisions for gross claims and related reinsurance recoveries are fairly stated on the basis of the information currently available to them. However, ultimate liability will vary as a result of subsequent information and events and this may result in significant adjustments to the amounts provided. Adjustments to the amounts of claims provisions established in prior years are reflected in the financial statements for the period in which the adjustments are made.

### Unexpired risk provisions
Provision is made for claims emanating from unexpired risks in respect of the contracts concluded before the end of the financial year which continue in force after that date and where claims are expected to exceed the unearned premiums under these policies, after deduction of deferred acquisition costs. In calculating such a provision all business segments are considered individually and are stated after taking into account future investment income.

### Other technical income
Other technical income comprises overriding commissions receivable and is reflected in the technical account on the same basis as the underlying business to which it relates.

### Investments
Listed investments are stated at bid - value at the close of business on the balance sheet date or the last Stock Exchange dealing day before the balance sheet date. Investments in Group undertakings recorded in the Company's own balance sheet are stated at cost less provisions for any impairment.

### Investment return
Investment income comprises interest, dividends, and realised and unrealised investment gains and losses.

Realised gains and losses represent the difference between net sales proceeds and purchase price or market value at the previous year end. Unrealised gains and losses on investments represent the difference between the valuation of investments at the balance sheet date and their purchase price, adjusted for previously recognised unrealised gains and losses on investments disposed of in the accounting period.

All investment income and gains and losses, are initially accounted for in the non-technical account. An allocation is then made from the non-technical account to the general business technical account to reflect the return of those assets supporting underwriting activities.

### Taxation

The charge for taxation on general business is based on the profit for the year, and takes into account taxation deferred because of timing differences between certain items for taxation and accounting purposes. Provision is made for deferred tax only to the extent that it is probable that an actual liability will crystallise in the foreseeable future. Deferred tax assets are recognised to the extent that it is more likely than not that they will be recovered.

Deferred taxation is recognised without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19 "Deferred tax". No provision is made for taxation of permanent differences.

### Leases and hire purchase contracts

Payments made under operating leases are charged to the profit and loss account in the period in which they become payable.

### Foreign currencies

Foreign currency transactions are translated at the rates of exchange ruling at the dates of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rate of exchange ruling at the balance sheet date.

The results and balance sheets of overseas controlled entities ("branches") that have a functional currency different from sterling (the presentation currency) are translated into sterling (the presentation currency) as follows:

- assets and liabilities are translated into sterling at the rate ruling at the balance sheet date;
- income and expenses are translated at cumulative average rates of exchange; and
- all resulting exchange differences are recognised in the Statement of Recognised Gains and Losses.

Exchange adjustments arising from the translation of foreign currency net investments in the overseas branches are dealt with in the statement of total recognised gains and losses. All other foreign exchange differences are taken to the non-technical account.

## 3. Segmental Information

### (a) Analysis of gross premiums, profit before tax and net assets

| | Gross premiums written 2012 £'000 | Profit/(Loss) before tax 2012 £'000 | Net assets 2012 £'000 | Gross premiums written 2011 £'000 | Profit/(Loss) before tax 2011 £'000 | Net assets 2011 £'000 |
|---|---|---|---|---|---|---|
| **BY GEOGRAPHICAL SEGMENT** | | | | | | |
| United Kingdom | 1,769,636 | 30,602 | 339,129 | 1,622,898 | 59,111 | 321,030 |
| Switzerland | 23,957 | 886 | 3,583 | 39,750 | 600 | 2,918 |
| Italy | 12,760 | (29) | 77 | 17,684 | 182 | 704 |
| Australia | 257,851 | 6,041 | 30,512 | 220,951 | (2,405) | 21,113 |
| New Zealand | 7,159 | 91 | 394 | 12,451 | 79 | 320 |
| Ireland | 6,059 | 39 | 40 | - | - | - |
| | **2,077,422** | **37,630** | **373,735** | **1,913,734** | **57,567** | **346,085** |

The directors consider the Company to be involved in only one type of business, that is general insurance business.

### (b) Analysis of gross written premiums

| | 2012 £'000 | 2011 £'000 |
|---|---|---|
| Resulting from contracts concluded by the Company: | | |
| In the EU member state of its head office | 1,788,455 | 1,640,582 |
| Outside EU member states | 288,967 | 273,152 |
| | **2,077,422** | **1,913,734** |

(c) **Analysis of gross premiums written, gross premiums earned, gross claims incurred, gross operating expense and the reinsurance balance**

| 2012 | Direct marine & aviation £'000 | Direct property £'000 | Direct general liability & other £'000 | Direct motor £'000 | Total direct £'000 | Re-insurance accepted £'000 | Total £'000 |
|---|---|---|---|---|---|---|---|
| Gross premiums written | 290,131 | 450,546 | 585,682 | 745,077 | 2,071,436 | 5,986 | 2,077,422 |
| Gross premiums earned | 281,979 | 424,484 | 547,515 | 732,664 | 1,986,642 | 5,986 | 1,992,628 |
| Gross claims incurred | 104,369 | 227,669 | 198,166 | 536,289 | 1,066,493 | (87) | 1,066,406 |
| Gross operating expenses | 39,483 | 99,888 | 231,290 | 187,428 | 558,089 | - | 558,089 |
| Gross technical result | 138,127 | 96,927 | 118,059 | 8,947 | 362,060 | 6,073 | 368,133 |
| Reinsurance balance | 138,305 | 92,458 | 94,355 | 8,639 | 333,757 | 5,848 | 339,605 |
| **Net technical result** | **(178)** | **4,469** | **23,704** | **308** | **28,303** | **225** | **28,528** |
| **Net technical provisions** | **6,144** | **98,658** | **270,449** | **-** | **375,251** | **3** | **375,254** |

| 2011 | Direct marine & aviation £'000 | Direct property £'000 | Direct general liability & other £'000 | Direct motor £'000 | Total direct £'000 | Re-insurance accepted £'000 | Total £'000 |
|---|---|---|---|---|---|---|---|
| Gross premiums written | 254,623 | 377,494 | 518,622 | 760,625 | 1,911,364 | 2,370 | 1,913,734 |
| Gross premiums earned | 264,575 | 399,658 | 520,294 | 676,722 | 1,861,249 | 5,160 | 1,866,409 |
| Gross claims incurred | 154,223 | 246,618 | 232,236 | 491,443 | 1,124,520 | (3,983) | 1,120,537 |
| Gross operating expenses | 46,691 | 119,849 | 243,589 | 162,301 | 572,430 | 812 | 573,242 |
| Gross technical result | 63,661 | 33,191 | 44,469 | 22,978 | 164,299 | 8,331 | 172,630 |
| Reinsurance balance | 65,059 | 25,521 | 19,643 | 21,243 | 131,466 | 8,100 | 139,566 |
| **Net technical result** | **(1,398)** | **7,670** | **24,826** | **1,735** | **32,833** | **231** | **33,064** |
| **Net technical provisions** | **737** | **74,520** | **259,723** | **-** | **334,980** | **91** | **335,071** |

## 4. Investment Income

| | 2012 £'000 | 2011 £'000 |
|---|---|---|
| Investment Income | 10,559 | 11,151 |
| Realised gains | 4,833 | 4,359 |
| | **15,392** | **15,510** |

## 5. Net Operating Expenses

| | 2012 £'000 | 2011 £'000 |
|---|---|---|
| Acquisition costs | 551,541 | 533,352 |
| Change in gross operating expense provision | (56) | (137) |
| Change in gross deferred acquisition costs (note 15) | (25,180) | 10,611 |
| | **526,305** | **543,826** |
| Administrative expenses | 31,784 | 29,416 |
| Gross operating expenses | 558,089 | 573,242 |
| Reinsurance commissions and profit participation | (506,175) | (486,312) |
| Change in ceded operating expense provision | 56 | 137 |
| Change in deferred reinsurance commission (note 15) | 18,605 | (9,350) |
| | **70,575** | **77,717** |

## 6. Profit on Ordinary Activities before Tax

Profit on ordinary activities before tax is stated after charging:

| | 2012<br>£'000 | 2011<br>£'000 |
|---|---|---|
| **AUDITORS' REMUNERATION** | | |
| Audit of these financial statements | 181 | 159 |
| Audit of subsidiary's financial statements | - | 18 |
| Other services pursuant to legislation | 99 | 102 |
| Other services relating to taxation | 65 | 118 |
| All other services | 25 | 30 |

The Company has no employees and does not pay any remuneration other than fees to its Directors. Any pension contributions to the multi employer pension scheme are disclosed in the accounts of the service company.

## 7. Remuneration of Directors

| | 2012<br>£'000 | 2011<br>£'000 |
|---|---|---|
| Directors' emoluments | 943 | 579 |
| Pension contributions | 18 | 17 |
| | **961** | **596** |

The directors' remuneration consists of the emoluments paid to the directors by the Company and Munich Re UK Services Limited. The emoluments of the highest paid director for the year were £552,427 (2011: £331,530) and pension contributions of £Nil (2011: £Nil). There was one director for whom retirement benefits are accruing in respect of qualifying services under a money purchase plan.

## 8. Taxation

| | 2012 £'000 | 2011 £'000 |
|---|---|---|
| UK Corporation tax at 24.5% (2011: 26.5%) | 8,960 | 14,991 |
| Change in prior year current tax | 33 | 1,260 |
| **Total Current Tax** | **8,993** | **16,251** |
| Change in current year net deferred tax | 3 | 3 |
| Impact of change in UK Tax rate | 1 | 1 |
| **Total Deferred Tax** | **4** | **4** |
| | **8,997** | **16,255** |

The 2012 current tax charge for the year is lower (2011: higher) than the standard rate of corporation tax in the UK at 24.5% (2011: 26.5%). The differences are explained below:

| | | |
|---|---|---|
| **Profit before tax** | **37,630** | **57,567** |
| Corporation tax at 24.5% (2011: 26.5%) | 9,219 | 15,255 |
| Excess capital allowances over depreciation | (3) | (3) |
| Tax effect of franked investment income | (291) | (265) |
| Tax effect of other permanent differences | 35 | 4 |
| Under provision relating to prior periods | 33 | 1,260 |
| | **8,993** | **16,251** |

**Deferred Tax Asset**

Under FRS 19 deferred tax is provided in full on certain timing differences.

| | | |
|---|---|---|
| Balance at start of year | 1,152 | 17 |
| Change in deferred tax | (1,142) | 1,136 |
| Impact of change in UK Tax rate | (1) | (1) |
| | **9** | **1,152** |

The deferred tax liability of £1,139,416 for 2011 related to the expected reduction in double tax relief available in the UK resulting from the utilisation of Australian branch losses to reduce the Australian tax paid. An equivalent amount of £1,139,416 is recognised as a deferred tax asset for available tax losses in the Australian branch. This deferred tax asset and corresponding deferred tax liability reversed in 2012.

The Autumn Statement on 5 December 2012 announced that the UK corporation tax rate will reduce to 21% by 2014. With the 2013 Budget Statement on 20 March 2013 it was announced that an additional 1% reduction to 20% is expected by 2015. A reduction in the rate from 26% to 25% (effective from 1 April 2012) was substantively enacted on 5 July 2011, and further reductions to 24% (effective from 1 April 2012) and 23% (effective from 1 April 2013) were substantively enacted on 26 March 2012 and 3 July 2012 respectively. This will reduce the company's future current tax charge accordingly. The deferred tax asset at 31 December 2012 has been calculated based on the rate of 23% substantively enacted at the balance sheet date.

## 9. Investments

| | Current Value | | Historical Value | |
|---|---|---|---|---|
| | 2012 £'000 | 2011 £'000 | 2012 £'000 | 2011 £'000 |
| **Financial Investments** | | | | |
| Government fixed interest securities | 465,452 | 536,669 | 456,280 | 517,856 |
| Other listed fixed interest securities | 52,844 | 44,245 | 52,874 | 43,315 |
| Deposits with credit institutions | 31 | 24,299 | 31 | 24,299 |
| | **518,327** | **605,213** | **509,185** | **585,470** |

Government fixed interest securities included gilts, treasury notes and other government backed securities. The Company has fully funded a US$100.0m United States Trust Fund obligation; a US$35.6m Swiss tied assets obligation; and a CAD$5.1m Canadian Trust Fund obligation. These comprise of investments in government fixed interest securities.

## 10. Debtors arising out of direct insurance operations

| | 2012 £'000 | 2011 £'000 |
|---|---|---|
| Amounts owed by intermediaries | 476,175 | 404,343 |
| Amounts owed by group companies | 12,643 | 8,983 |
| **Total** | **488,818** | **413,326** |

Amounts receivable by the Company for intermediaries and group companies are due within one year.

## 11. Cash at Bank

The cash at bank balance of £133.7m (2011: £45.3m) includes accounts totalling £18.1m (2011: £10.5m) which have been set aside to secure letters of credit and guarantees issued in the normal course of business, and in respect of other statutory requirements. As such these balances are restricted from general use.

## 12. Share Capital

| | 2012 £'000 | 2011 £'000 |
|---|---|---|
| Allotted, called up and fully paid<br>11,400,000 (2011 - 11,400,000) Ordinary Shares of £10 each | 114,000 | 114,000 |

## 13. Reconciliation of movements in Shareholder's Funds

| | Ordinary Share Capital £'000 | Profit and Loss Account £'000 | Total £'000 |
|---|---|---|---|
| At 1 January 2012 | 114,000 | 232,085 | 346,085 |
| Profit for the year | - | 28,633 | 28,633 |
| Currency translation differences on foreign currency net investments | - | (983) | (983) |
| At 31 December 2012 | **114,000** | **259,735** | **373,735** |

## 14. Technical Provisions

| | Unearned premiums 2012 £'000 | Claims outstanding 2012 £'000 | Total 2012 £'000 | Unearned premiums 2011 £'000 | Claims outstanding 2011 £'000 | Total 2011 £'000 |
|---|---|---|---|---|---|---|
| **GROSS AMOUNT** | | | | | | |
| At beginning of the year | 920,211 | 2,351,688 | 3,271,899 | 871,592 | 2,210,648 | 3,082,240 |
| Currency translation differences | (14,142) | (48,851) | (62,993) | 1,294 | (1,112) | 182 |
| Movement in the provision | 84,794 | 165,518 | 250,312 | 47,325 | 142,152 | 189,477 |
| **At end of the year** | **990,863** | **2,468,355** | **3,459,218** | **920,211** | **2,351,688** | **3,271,899** |
| **REINSURANCE AMOUNT** | | | | | | |
| At beginning of the year | (844,761) | (2,092,067) | (2,936,828) | (800,496) | (1,957,249) | (2,757,745) |
| Currency translation differences | 11,969 | 42,590 | 54,559 | (947) | 1,120 | 173 |
| Movement in the provision | (56,494) | (145,201) | (201,695) | (43,318) | (135,938) | (179,256) |
| **At end of the year** | **(889,286)** | **(2,194,678)** | **(3,083,964)** | **(844,761)** | **(2,092,067)** | **(2,936,828)** |
| **NET TECHNICAL PROVISIONS** | | | | | | |
| **At beginning of the year** | **75,450** | **259,621** | **335,071** | **71,096** | **253,399** | **324,495** |
| **At end of the year** | **101,577** | **273,677** | **375,254** | **75,450** | **259,621** | **335,071** |

Provisions for net claims at the beginning of the year compared to payments and provisions at the end of the year in respect of prior underwriting years' liabilities amounted to an overprovision in 2012 of £34.7m (2011 of £65.2m overprovision).

The overprovision was in respect of direct general liability of £29.6m (2011: of £52.6m) and direct property and other of £5.1m (2011: of £12.6m).

## 15. Deferred Acquisition Costs

| | 2012<br>£'000 | 2011<br>£'000 |
|---|---|---|
| **GROSS AMOUNT** | | |
| At beginning of the year | 212,424 | 222,753 |
| Currency translation differences | (3,258) | 282 |
| Movement in the provision | 25,180 | (10,611) |
| **At end of the year** | **234,346** | **212,424** |
| **REINSURANCE AMOUNT** | | |
| At beginning of the year | (197,290) | (206,481) |
| Currency translation differences | 2,673 | (159) |
| Movement in the provision | (18,605) | 9,350 |
| **At end of the year** | **(213,222)** | **(197,290)** |
| **NET DEFERRED ACQUISITION COSTS** | | |
| **At beginning of the year** | **15,134** | **16,272** |
| **At end of the year** | **21,124** | **15,134** |

## 16. Provisions for other risks and charges

| | Expense provision<br>2012<br>£'000 | Expense provision<br>2011<br>£'000 |
|---|---|---|
| At beginning of the year | 399 | 536 |
| Movement in the year | (56) | (137) |
| **At end of the year** | **343** | **399** |

The provision for risks and other charges is for an expense provision in relation to the assumption of liabilities under a Part VII transfer that took place in 2008.

## 17. Creditors arising out of Direct Insurance Operations

| | 2012<br>£'000 | 2011<br>£'000 |
|---|---|---|
| Amounts owed to intermediaries | 28,867 | 161,789 |
| Amounts owed to group companies | 360,436 | 207,756 |
| | **389,303** | **369,545** |

Amounts due to intermediaries and group companies are payable within one year.

## 18. Group Companies

a) Parent Company
The Company is a wholly owned subsidiary of Munich Re which is the immediate and ultimate parent company, incorporated in Germany. The largest group in which the results of the Company are consolidated is that headed by Munich Re and no other group financial statements include the results of the Company.

b) Subsidiary Company
The 'Investment in subsidiary' is a 100% shareholding in Great Lakes Services Limited, an unlisted service company incorporated in the United Kingdom. As of 31 December 2011 all the liabilities and obligations of Great Lakes Services Limited and an equivalent portion of assets were transferred to Munich Re UK Services Limited, a wholly owned subsidiary of Munich Re incorporated in the United Kingdom. Effective 7 November 2012, Great Lakes Services Limited reduced its share capital to £1 by cancelling 49,999 ordinary shares of £1 each. Great Lakes Services Limited was liquidated on 5 March 2013.

## 19. Leases

| | Land and Buildings 2012 £'000 | 2011 £'000 |
|---|---|---|
| Annual commitments under non-cancellable operating leases are as follows: | | |
| Operating lease which expires in under five years | 170 | 170 |
| Operating lease payments made during the financial year | 170 | 170 |

## 20. Contingent Liabilities and Guarantees

During 2009 the Company entered into an agreement to guarantee payments to be made by Great Lakes Services Limited in respect of a pension scheme of which certain employees are members. Payments of £368,500 are to be made annually up to 2015. As of 31 December 2011 the liabilities and obligations of Great Lakes Services Limited were transferred to Munich Re UK Services Limited. Consequently, from 31 December 2011 the Company's guarantee is for the payments of Munich Re UK Services Limited instead of Great Lakes Services Limited.

Risk Solutions

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