Report & Accounts

for the year ended 31 March 2000

EQUITAS

Overview

Accumulated surplus after tax increased from £772 million to £784 million.

Solvency margin, being surplus expressed as a percentage of net claims outstanding, increased from 9.6 per cent to 11.2 per cent as surplus grew and liabilities decreased as claims were paid.

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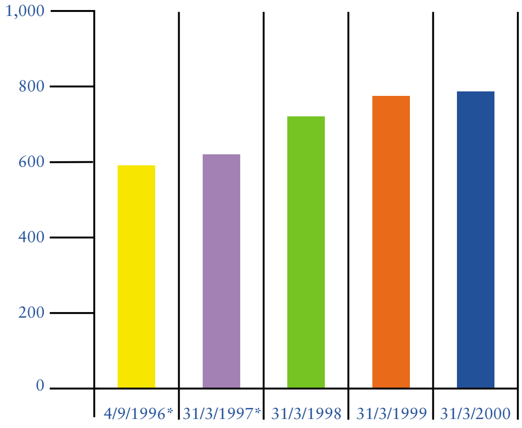
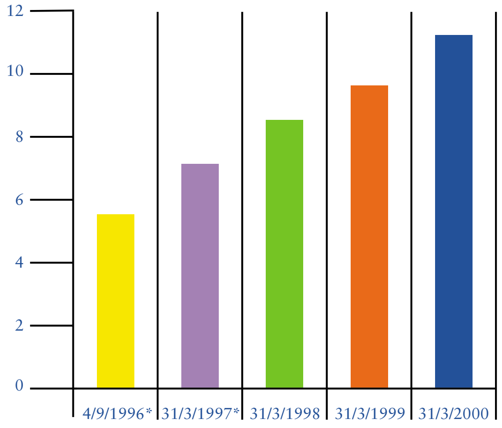
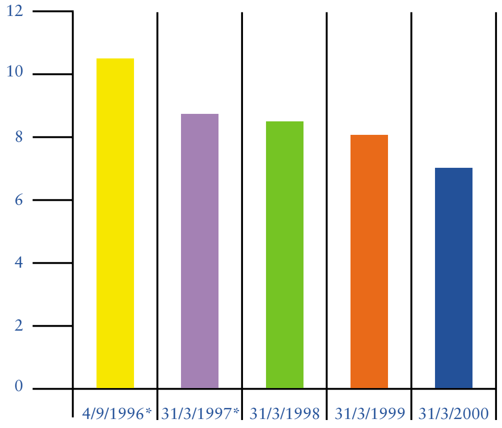
Accumulated surplus (£m)



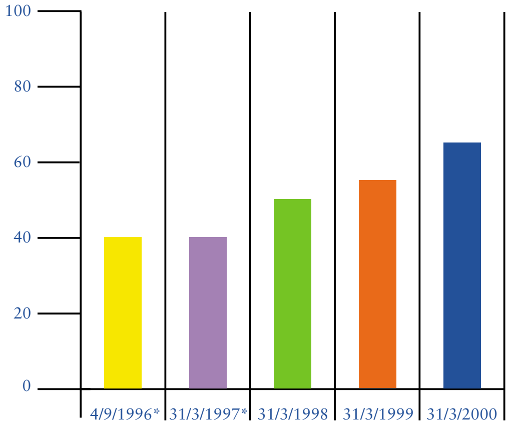
Solvency margin (%)



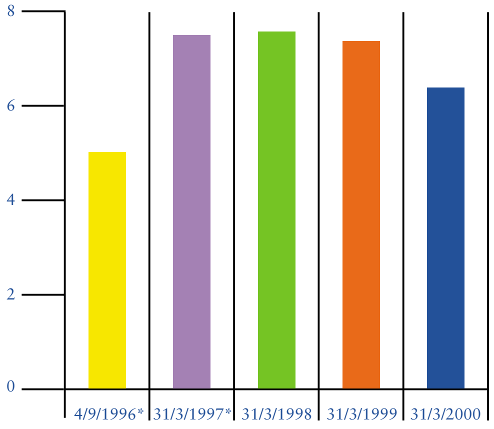
Net claims outstanding (£bn)[1]



APH claims as a percentage of net claims outstanding (%)[1]



Investments (£bn)



* Does not include Lioncover business

[1] Claims figures are shown net of discounting

Chairman's statement

Hugh Stevenson

In the financial year ended 31 March 2000:

- Accumulated surplus after tax increased from £772 million to £784 million; and
- The solvency margin, being accumulated surplus expressed as a percentage of net claims outstanding, increased from 9.6 per cent to 11.2 per cent.

The increase in accumulated surplus is smaller than in previous years. However, in the past year we did not benefit from any extraordinary credits, such as the £66 million payment which we received from Lloyd's during 1998-99 or the surplus of £70 million arising from the reinsurance of the liabilities of Lioncover during 1997-98. Excluding extraordinary credits, the contribution to surplus from our core activities was comparable to that achieved in previous years. Moreover, a relatively small increment to surplus should not be seen as a lack of progress, since it is also appropriate to take account of the reduction in net claims outstanding achieved during the year. Our solvency margin increased from 9.6 per cent to 11.2 per cent; had we merely maintained the solvency margin at last year's level, the accumulated surplus would have been over £100 million less than that disclosed in these accounts.

Our team of actuaries and, where appropriate, independent professionals have again carried out a comprehensive review of the outstanding claims liabilities as well as the reinsurance we expect to recover. As a result of this review, we have significantly strengthened our reserves for future asbestos claims, although we have also been able to release reserves in respect of other classes of business.

I am pleased to report that the Auditors have removed the qualification to the Group's accounts regarding the quality of data used to evaluate reserves. We have worked hard to improve the data with which we support our business decisions, and these efforts are continuing.
The Auditors have, however, once again qualified their report on the Group's accounts because of the uncertainty inherent to the business which Equitas has reinsured. The terms of this qualification are unchanged from previous years.

A description of each of the Group's three principal areas of activity – claims management, reinsurance recovery and the management of our investment portfolio – is provided by Michael Crall in his Chief Executive Officer's Review on pages 4 to 10. An analysis of the accounts is presented by Jane Barker in her Financial Review on pages 11 to 15.

As I have stated in the past, our prime objective is to reduce the financial uncertainties associated with Equitas to such an extent that Reinsured Names can disregard the risks which they still face from their underwriting at Lloyd's in respect of 1992 and prior years of account. A further objective is, in time, to create sufficient surplus to enable a return of premium to be made to Reinsured Names.

These objectives continue to present a great challenge, notwithstanding the progress reported by the Group thus far. The Auditors properly point to the uncertainties which are fundamental to the long tail nature of the asbestos, pollution and health hazard claims which now represent nearly two-thirds of our outstanding liabilities. We have little or no control over many important external factors such as legal developments, judicial decisions and social trends, especially in the United States, all of which could threaten our stability.

It is, however, within our control to ensure that the best possible people manage and carry on the business of Equitas and that they do it in a first class way. The results set out in these accounts reflect the further good progress which those who work for Equitas have achieved for Reinsured Names during the past year. I am deeply grateful to all of them.

Hugh Stevenson
Chairman
18 July 2000

Chief Executive Officer's review

Michael Crall

Equitas has concluded its fourth financial year with a modest increase in accumulated surplus and a significant improvement in solvency margin. Each of our core business areas – claims management, reinsurance management and investments – has made a positive contribution to our results.

Much of our early work was necessarily concentrated on building organisational capability. We now have in place an excellent team supported by tested systems and processes. With our infrastructure established, our efforts are fully focused on achieving the best possible results from each segment of the business.

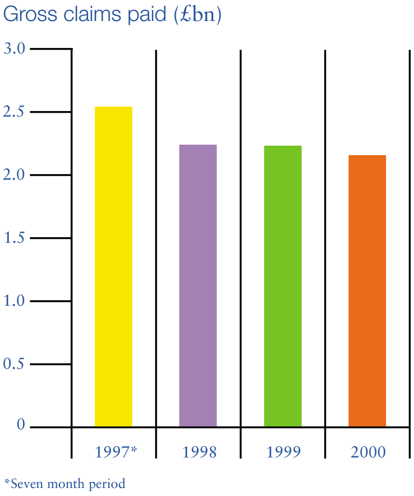
We have adopted a straightforward operating strategy for managing our business. The key elements of that strategy are to:

- resolve claims at values within our reserves at the earliest appropriate opportunity and to secure, where possible, releases which close off sources of future claims.
- commute syndicate reinsurance programmes whenever we can do so at an appropriate value, thereby converting current and future reinsurance recoverables into cash.
- produce a return on our investments in excess of the 'unwinding' of the discount applied to claims liabilities.
- keep costs below the levels assumed in our reserves. This requires reducing expenses each year by approximately 15 per cent.
- continue to enhance core skills – including claims management, deal making and portfolio evaluation – to enable us to deliver the other elements of our strategy.

Claims management

Gross claims paid, including operating costs, totalled £2.15 billion in the year ended 31 March 2000, a slight reduction from the £2.25 billion paid during the previous year.

It remains our policy to expedite the payment of valid claims, while resisting invalid claims with all proper means at our disposal. In a significant number of cases, especially those involving complex asbestos, pollution and health hazard (APH) claims, coverage and cost issues are not clear cut and are often subject to dispute. Although some cases inevitably involve a litigated outcome, our preferred approach is to negotiate directly with claimants in an attempt to achieve settlements more quickly and less expensively. When negotiating a settlement with a major claimant, we attempt to secure from the policyholder a release from further liability for both known and future claims.



Considerable progress continues to be made in settling environmental pollution claims. During the past year, we closed 128 – or 25 per cent – of the 509 open direct pollution claims pending at 1 April 1999. Furthermore, we settled 40 per cent of pollution claims with reserves in excess of £10 million at 1 April 1999. In most of these cases we received a broad release from future claims from the policyholder. After taking into account new claims, the number of open pollution claims decreased during the year by 20 per cent to 404.

Achieving certainty with regard to asbestos related claims has proved to be more difficult. The legal and coverage issues fundamental to asbestos claims are very different from those pertaining to pollution claims and we have been less successful in sealing off asbestos liabilities and obtaining releases. Moreover, it is difficult to estimate with certainty the value and number of future asbestos claims. Thus the asbestos area, in spite of its maturity, is the most difficult segment of the claims portfolio. Based on the increase in new direct asbestos filings seen this year, our continued actuarial analysis resulted in a significant strengthening in our provisions in the balance sheet for future asbestos claims payments. These reserve increases have been offset by positive developments in other areas of the business.

We continue to track health hazard issues which could potentially lead to new claims, including tobacco liability, though we continue to believe that tobacco claims will not create a significant liability for Equitas. Furthermore, we have not identified any previously unknown health hazard which we believe could create a material liability.

Orphan syndicates

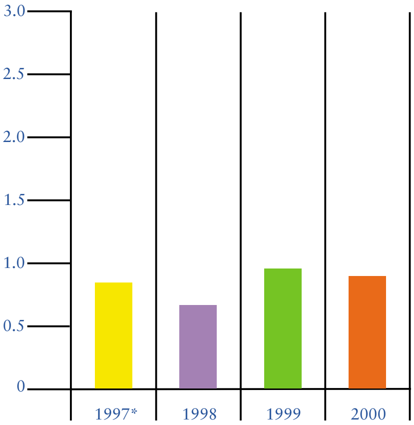
Equitas has been asked to provide indicative quotes to a handful of the 1993, 1994 and 1995 Orphan Syndicates. To date none of these quotes has been accepted. Most of the Orphan Syndicates have now been reinsured by the ongoing market, though problems still remain with several Orphan Syndicates, especially those which participated in the personal accident spiral. We recently issued an indicative quote to one of these syndicates which has resolved its pending disputes. We will honour our commitment to issue indicative quotes for the remaining syndicates, if requested, but we cannot offer a meaningful quote to a syndicate until all material disputes have been resolved.

Good progress is being made in the other major claims areas, particularly in those we refer to as 'balance of account' claims, a broad term encompassing most non-APH claims. Results in this segment are developing favourably. However, balance of account claims tend to be settled comparatively quickly with the inevitable result that APH claims make up an increasing share of our reserves each year. APH claims represent 65 per cent of net discounted liabilities at 31 March 2000 compared with 40 per cent when we began operations. As the proportion of APH claims in our total reserves increases, Equitas is exposed to potentially greater volatility and uncertainty in its financial position going forward.

Reinsurance management

Reinsurers' share of claims paid amounted to £892 million in the year ended 31 March 2000, compared with £952 million in the previous year.

Reinsurers' share of claims paid (£bn)



*Seven month period

During the year we completed negotiation of over 70 commutation agreements, including agreements with a number of our largest reinsurance counterparties. In addition, we have in process over a hundred commutation negotiations. In most cases commutations involve the settlement of all claims each party has against the other. Therefore commutations are a tool to extinguish liabilities for inwards reinsurance in addition to collecting outwards reinsurance proceeds.

Collecting reinsurance recoverables through traditional means has proved to be a slow and expensive process. Currently, more than half of our operating costs are connected with the reinsurance collection process. Collection of outstanding reinsurance debt has been severely hampered by market-wide disputes which affect all reinsurers, not only Equitas. Commuting reinsurance contracts reduces our costs, increases the certainty of the Group's balance sheet and, once the reinsurance asset is converted to cash, increases investable assets.

Several initiatives implemented in the past year support the commutation process. Responsibility for relationships with major counterparties has been assigned to individual managers. Assigning accountability in this way increases our understanding of each counterparty's key business objectives, reduces disputes and strengthens our ability to conclude commutation agreements on mutually acceptable terms. A cross-functional group of managers co-ordinates our approach to major counterparties and determines which companies receive priority attention.

We have also refined our strategy for collecting reinsurance debt by traditional means. Earlier this year, we adopted a syndicate specific approach to reinsurance collection, under which a designated manager will determine specific collection strategies and targets for each syndicate with material reinsurance assets. We believe this approach will expedite the collection of debt by more readily identifying problem areas and ensuring that all legitimate means are used to collect cash.

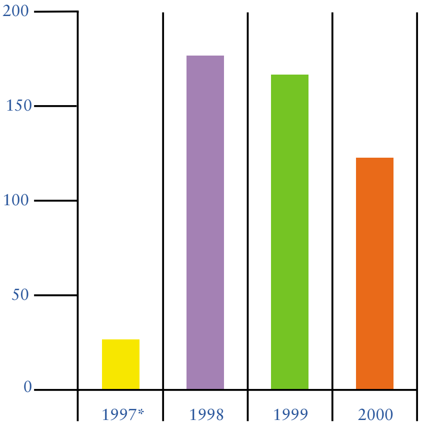
Supporting this strategy is a comprehensive tracking system which monitors each step of the reinsurance billing process from the time a bill leaves Equitas until cash collection is agreed. This system identifies delays in the reinsurance collection process, allowing us to act quickly to resolve the problem or take other measures, including the initiation of litigation or arbitration when warranted. The tracking system has also allowed us to monitor more accurately brokers' performance in the collection process. This has led to new operating procedures with major brokers that increase our control over their debt collection activities.

Investment management

Investment return amounted to £178 million in the year ended 31 March 2000, compared with £714 million in the previous year. Although this represents a substantial decrease in investment return, it was a satisfactory performance in the light of market conditions. Interest rates in both the United Kingdom and the United States rose during the past year, which caused the market value of bonds to fall. The consequent decline in investment income should be viewed in the context of the exceptional investment gains produced in the previous two years, during which interest rates fell and bond values rose.

Because Equitas discounts its liabilities to take account of the time value of money, a more meaningful indication of our investment performance is whether the investment return in a given year is sufficient to match the 'unwinding' of the discount applied to

Investment return in excess of unwinding of discount (£m)



*Seven month period

Syndicate level information

We have received a number of requests from Reinsured Names seeking a list of those syndicate years of account for which no claims have been paid in the past year. There are no such syndicates, as claims payments have been allocated in the past year against each reinsured syndicate year of account. It would be unwise for Reinsured Names to base any expectations on the amount of paid claims allocated in a given year to an individual syndicate as it is feasible that there could be no claims activity in one year but a substantial amount in a subsequent year. It is also conceivable that new claims could be filed against any syndicate at any given time.

Other Reinsured Names have requested a list of the syndicate years of account for which all liabilities have been exhausted. Again, there are as yet no such syndicates. Even if all known claims against a syndicate are exhausted in the future, we could not state that there would not be any incurred but not reported (IBNR) claims with any confidence.

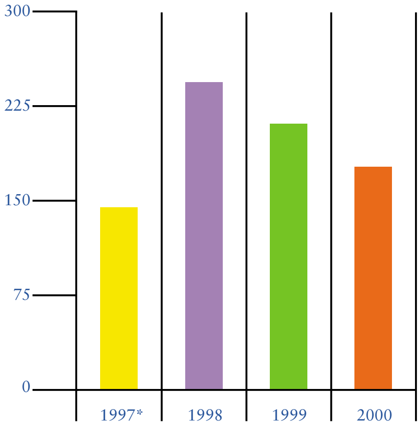
claims liabilities. In the year ended 31 March 2000, investment return exceeded the unwinding of the discount by £122 million, compared with an excess of £166 million in the previous year, not including the extraordinary credit received from Lloyd’s which was shown last year as investment return. The increase in bond yields caused us to raise the rate at which claims liabilities are discounted from 5 per cent per annum at 31 March 1999 to 5.75 per cent per annum at 31 March 2000, thereby reducing the present value of our liabilities by £263 million. The Financial Review on page 11 explains in greater detail the effects of discounting on the Group’s results.

The major portion of our investment portfolio is composed of high quality fixed income securities, though we continue to add to our equity position from time to time. Our intention remains to invest only a portion of our surplus in equities. Our equity and other investment strategies are formulated with the aid of our proprietary asset/liability modelling programme, the Equitas Financial Model, which has been broadened in the past year to analyse the credit risk associated with our fixed income portfolio and the maturity structure of our fixed income investments in relation to the expected payment patterns of claims liabilities.

Expense management

The Group’s operating expenses amounted to £176 million in the year ended 31 March 2000, 16 per cent lower than the £210 million spent in the previous year.

Operating costs (£m)



*Seven month period

Overlaying all of our activities is the requirement that we reduce operating expenses by 15 per cent per year to keep operating costs in line with the reserve established for future operating expenses. A commitment to expense management is firmly rooted in our culture, and managers are challenged to devise innovative ways of reducing costs without compromising effectiveness.

In the past year, we have brought in-house the claims and policy administration services that had previously been provided to Equitas by the Lloyd’s Claims Office and Lloyd’s Policy Signing Office. By re-engineering these processes, we are saving more than £15 million annually. We have also consolidated within Equitas the reinsurance ledger information previously managed by an external contractor. We believe that this will result in significant savings as well as improved control over this data.

Since its inception Equitas has had a remarkably stable employee force. Reduced claims and reinsurance volumes have been managed by reducing activities contracted out to third parties. In the future Equitas itself will have to reduce in size, but we will need to do so without sacrificing quality. With this in mind, we have begun to outsource non-core areas of the business. Agreements with outsourcing service providers are in place covering our Facilities

Management and Records Management functions, and we are currently negotiating an outsourcing contract relating to our Information Technology function. More than 180 employees in these business areas will be transferred to the employment of the selected outsourcing providers by the end of the current year. Outsourcing these non-core functions provides us with the ability to access high levels of skill and capability while converting significant fixed costs to variable costs. Additionally, we believe that outsourcing service providers can offer employees more attractive career paths.

Core skill enhancement

We initiated a number of programmes during the year designed to strengthen the individual and collective capabilities of the organisation. Some of these included:

Negotiation as a corporate capability

The claims unit and the commutations unit have developed processes which assure that negotiations are thoroughly prepared for, that individual negotiators are fully supported by the organisation, and that we systematically undertake post-negotiation de-briefings to learn everything we can from actual negotiating experiences. This is an important initiative, since negotiations are central to much of our work.

Attorney management

We have installed a comprehensive attorney management system, including annual and case budgeting, task-based billing analysis and qualitative assessment of attorney performance. These programmes allow us to manage our attorney selection and legal expense much more effectively and to pay for performance that gets results, while eliminating non-productive attorney activities.

Deal evaluation

In 1998 the claims unit developed a comprehensive claims valuation methodology and began employing it to value major claims. The methodology generates a case value based on objective, transparent criteria and, furthermore, serves as a guide through the key technical elements of a case negotiation. Over the past year the methodology has been extended to encompass all significant claims. Additionally, we have installed a similar process on the commutations side of the business which gives us clear targets when we enter a negotiation and an objective measure of our results.

Employee training

Equitas has from the outset committed itself to a high standard of employee education and training. During the past fiscal year over 50 per cent of our people were enrolled in one or more in-house training programmes. Additionally, over 250 Equitas employees received financial support for external professional education.

Programmes such as these not only improve our ability to execute our task effectively, but they also support the professional culture which we need to maintain to be successful.

Conclusion

In its brief existence Equitas has achieved a great deal and has built a capability that is approaching the 'world class' standard we aspire to. Our employees have approached their challenge creatively and with a high level of dedication. I thank them for their commitment and contribution.

Notwithstanding these accomplishments our task is far from complete. The external environment remains perilous. Not only are we exposed to adverse outcomes on major cases but small differences in outcomes over a large number of transactions can make large differences – positive or negative – in our results. We are confident – but far from complacent – as we face the future.

Michael Crall

Michael Crall
Chief Executive Officer
18 July 2000

Financial review

Jane Barker

The Group produced a surplus of £12 million after tax compared with £54 million in 1999.

Technical account

The Companies Act requires that we split the profit and loss account into the technical account and the non-technical account. Details of insurance business transactions are provided in the technical account; non-insurance transactions are detailed in the non-technical account.

Set out below is a description of some of the key items included in the technical account on page 30.

Investment return

Our investments produced a return of £178 million during the year. Management commentary on investment performance appears on page 7. Included in investment return for 1999 was £64 million of the £66 million received from Lloyd's in early settlement of an agreement to pay up to £100 million in February 2002 to protect the Group against a possible shortfall in certain deferred payments and changes in future interest rates.

Claims paid

The amount of gross claims paid of £2,149 million compares with £2,247 million in 1999. The reinsurers' share of the gross claims paid is £892 million (1999: £952 million).

Operating expenses of £176 million (1999: £210 million) have been included in the amount of gross claims. Payments or proceeds in respect of a commutation are treated as a claim or as part of the reinsurers' share.

The reinsurance recovery percentage of claims paid during the year was approximately the same as in the previous year, but it will vary over time as a result of commutation activity and the mix of claims paid.

Change in the provision for claims

The change in the provision for claims results from the reassessment of future insurance claims and reinsurance recoveries by major category and currency, including an adjustment for payments, receipts and accruals during the year.

Since we expect the liabilities to be settled over a long period of time, they have been discounted to acknowledge the time value of money. The return to be earned in the future on the investments that are held to meet these liabilities is anticipated through this process of discounting. As stated in the Group's accounting policies, the discount rate applied to the liabilities is determined having regard to current prospective yields on the asset portfolio. This rate is reviewed each year to ensure that it remains a prudent estimate of the average annual return expected to be achieved for the period for which these assets are likely to be held. For the year under review, we have revised the discount rate to 5.75 per cent per annum from 5 per cent per annum to reflect current market yields.

Two elements make up the discount adjustment, which is referred to as the 'unwinding' of the discount.

	£m
Reduction of one year in period over which net liabilities are discounted	319
Effect of change in the discount rate from 5% to 5.75% per annum	(263)
Unwinding of the discount	**56**

The last element in the change in provision for claims arises from our re-evaluation of the discounting effect of the likely timing of future payments and receipts.

Other technical charges

The other technical charges are made up of foreign exchange gains and losses. Liabilities are denominated in a number of currencies, and the Group's policy is to match our assets to the currencies of our liabilities as closely as possible. Thus the effect of exchange fluctuations on the provisions for claims was largely neutralised by exchange fluctuations in the value of assets. For the most significant foreign currency, the closing exchange rate used for translation of the balance sheet at 31 March 2000 was US$1.59 to £1 Sterling compared with US$1.61 at 31 March 1999.

The balance on the technical account is then carried forward to the non-technical account.

Surplus

The Group's surplus after tax increased to £784 million as at 31 March 2000. The movements were as follows:

	£m	*£m*
Retained surplus at 1 April 1999		**772**
Investment return in excess of unwinding of the discount		122
Reassessment of:		
Claims, including expenses (see below)	(711)	
Reinsurances (see below)	677	
Timing of net future payments	(73)	
		(107)
Exchange gains		3
Taxation		(6)
Retained surplus at 31 March 2000		**784**

Provision for claims outstanding

The provision for claims outstanding remains the most significant item on the Group's balance sheet. It should be considered together with the reinsurers' share of claims outstanding. Movements in these provisions from one year to the next comprise the following:

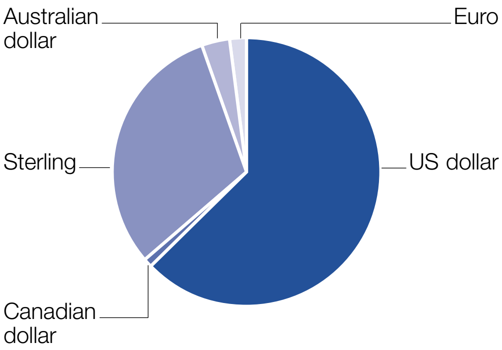
- payments, receipts and accruals in the year;
- adjustments in estimates of liabilities and associated reinsurances;
- changes in discount; and
- movements in exchange rates.

The reassessment of liabilities and reinsurances has been carried out this year with the help of better information. Following the annual actuarial review, we have strengthened our provisions, primarily in respect of asbestos claims. This has been balanced by the release of provisions for other classes of business and an increase in the reinsurers' share of outstanding claims.

	Claims £m	*Reinsurance £m*	*Net £m*
Provisions at 1 April 1999	**10,348**	**(2,312)**	**8,036**
Payments, receipts and accruals	(2,149)	892	(1,257)
Unwinding of the discount	98	(42)	56
Reassessment of:			
Liabilities and reinsurances	711	(677)	34
Timing of net future payments	(34)	107	73
Exchange and other movements	56	(14)	42
Provisions at 31 March 2000	**9,030**	**(2,046)**	**6,984**

Financial investments

Financial investments by currency



The Group's investment policy is to match its expected liabilities by duration and currency. The aims of the investment strategy are to:

- earn an investment return which matches or exceeds the unwinding of the discount. This return is credited to the technical account; and
- provide adequate funds as investments mature to pay claims.

The Group continues to increase its investment in equities. At 31 March 2000 equities represented just over 5 per cent of the market value of our investment portfolio and 36 per cent of our retained surplus. Our intention remains to invest only a portion of our surplus in equities, and the major part of the investment portfolio therefore remains largely invested in high quality fixed interest instruments.

The Group regularly assesses the performance of its fund managers against pre-determined benchmarks, which are established in the light of the overall investment strategy.

To enhance our investment earnings we began a programme of securities lending during the past year. This involves lending our securities to a third party, while retaining rights to all income from that security. The borrower is required to provide appropriate collateral, which must at all times exceed the value of the underlying security. We receive interest on this collateral, a portion of which we rebate to the borrower, keeping the difference for our own account.

During the year under review, the investment environment was less favourable than that of previous years. The return on our equity investment before dividend income was positive, taking into account realised and unrealised gains and losses. Bond markets, in which the majority of our assets are invested, suffered from rising short term interest rates and deteriorating inflation expectations, particularly in the United States. Inflation linked securities suffered less than fixed interest. Despite this, our investment return exceeded the unwind of the discount.

Bad debts

We have again reassessed our estimates of the amount to be provided for bad or doubtful reinsurance debts. After removing the amounts allocated to reinsurance debts which have since been commuted, the amount that was deducted from the reinsurance asset in the Group's opening accounts remains the best estimate of a prudent bad debt provision and accordingly no further adjustments have been made.

Data

Since the formation of Equitas, the Auditors have qualified the report on the Group's accounts because they considered the underlying reinsurance and non-APH claims data were neither complete nor sufficiently accurate to provide the audit evidence they required. Much of the problem stemmed from the large volume of unaudited data inherited by Equitas.

During the year we have taken a number of further steps which have considerably improved this position. Our reserving methodology for non-APH claims is now based on gross of reinsurance claims data rather than net of reinsurance data as in previous years. In addition we have continued to analyse and, where appropriate, correct the reinsurance data. A high proportion of the reinsurance and claims data is now processed within the Group, giving us greater confidence in the integrity of the data used to estimate both the claims liabilities and the related reinsurance assets. However, we do not believe, as a result of the work carried out in the past year, that material changes are required to figures reported in previous accounts.

This is a positive development for Equitas, particularly as the Auditors have been able to use this work to satisfy themselves that the data qualification may now be removed.

Risk management

The principal risk to the Group remains that it may not be able to settle its liabilities in full.

We have in place a system of controls over insurance transactions such as claims, reinsurance and commutations, investment transactions and operational transactions. These are reviewed and changed where necessary in the light of any new circumstances.

Insurance claims and associated reinsurance recoveries are periodically assessed by major category and currency against provisions held. New types of claims and any changes in settlement trends are examined carefully and their impact on provisions evaluated.

Other risks include counterparty risks such as amounts due from reinsurers, balances at banks and custodians, and obligations of specific insurers. These risks are managed by regular review and assessment of relevant balances against established criteria.

During the year we conducted a review of the effectiveness of internal control to verify that our control structure complied with that outlined in the Turnbull guidance issued by the Institute of Chartered Accountants in England and Wales. This review concluded that the control framework is adequate to comply with that guidance.

Jane Barker
Finance Director
18 July 2000

Board of Directors

Hugh Stevenson ‡§

Chairman; joined the Board in April 1998. He was formerly Chairman of Mercury Asset Management Group plc, a Managing Director of S G Warburg Group plc's investment banking business and with Linklaters & Paines. He is Chairman of The Merchants Trust PLC and a Director of The Standard Life Assurance Company and other companies. Age 57.

Michael Crall #Δ*

Chief Executive Officer; joined the Board in December 1995. He was formerly President and Chief Executive Officer of Argonaut Insurance Company in California and a senior executive at CIGNA Corporation. Age 56.

Dick Barfield †Δ

Non-Executive Director; joined the Board in April 1997. He is currently a Director of Baillie Gifford Japan Trust plc, Marshalls plc, The Merchants Trust PLC, New Look Group plc and Rio Tinto Pension Investments. He was formerly Chief Investment Manager of The Standard Life Assurance Company. Age 53.

Jane Barker Δ*

Finance Director; joined the Board in December 1995. She was formerly Chief Financial Officer and Chief Operating Officer of the London Stock Exchange and Chief Financial Officer of the insurance broking operations of Marsh & McLennan Inc outside the Americas. Age 50.

Stephen Catlin #‡

Lloyd's Appointed Non-Executive Director; joined the Board in October 1996. He is Chairman of Catlin Underwriting Agencies Limited and Catlin Holdings Limited and Underwriter of Lloyd's Syndicates 1003 and 2003. He is also Chairman of the Lloyd's Market Association. Age 46.

Michael Deeny #‡§

Trustees-nominated Non-Executive Director; joined the Board in October 1996. He is Chairman of MultiMedia Television plc, Chairman of the Association of Lloyd's Members and Deputy Chairman of The Equitas Trust. Age 55.

Paul Jardine *

Commutations Director and Chief Actuary; joined the Board in February 1999. He joined Equitas as Chief Actuary in December 1996. He was formerly a Partner in Coopers & Lybrand's Actuarial Insurance Services Group and an Actuary with Prudential Assurance Company Limited. He is a Fellow of the Institute of Actuaries and a Member of the American Academy of Actuaries. Age 39.

James Joll †§

Non-Executive Director; joined the Board in June 1996. He is Chairman of AIB Asset Management Holdings and Deputy Chairman of Jarvis Hotels plc. He was formerly Finance Director of Pearson plc. Age 63.

Scott Moser *

Claims Director; joined the Board in May 1997. He was formerly President of Envision Claims Management Corporation; Vice President of Environmental/Excess Claims at Aetna Casualty & Surety Company; and a Partner with the law firm Day, Berry & Howard. Age 49.

Sir Bryan Nicholson #‡

Non-Executive Director; joined the Board in October 1996. He is Chairman of the British United Provident Association (BUPA) and Cookson Group plc. He is also a Director of GKN plc. He was formerly President of the Confederation of British Industry; Chairman of the Manpower Services Commission; and Chairman and Chief Executive of the Post Office. Age 68.

Richard Spooner †Δ

Trustees-nominated Non-Executive Director; joined the Board in October 1996. He is Managing Director of Team User Systems Company Limited. He was formerly a member of the Names Committee and the Assistance and Recovery Committee of Lloyd's. Age 53.

† Member of Audit and Compliance Committee

Member of Claims and Commutations Committee

Δ Member of Investment Committee

‡ Member of Nominations Committee

§ Member of Remuneration Committee

* Executive office held with Equitas Limited

Directors' report

for the year ended 31 March 2000

The Directors present their report and the audited financial statements for the financial year ended 31 March 2000.

Principal activities

The Equitas Group was formed as part of the Lloyd's Reconstruction and Renewal Plan to reinsure the liabilities of Lloyd's of London syndicates allocated to the 1992 and prior years of account, other than life syndicates, and to perform the run-off of these liabilities. Equitas Reinsurance Limited completed the reinsurance of the 1992 and prior years' business, except business previously reinsured by Lioncover Insurance Company Limited ('Lioncover business'), with effect from 3 September 1996 and reinsured the Lioncover business with effect from 18 December 1997. It retroceded these businesses to Equitas Limited, which is the main operating company of the Group. Equitas Reinsurance Limited and Equitas Limited are regulated under the Insurance Companies Act 1982 by the Financial Services Authority (the body which has day to day responsibility for the regulation of insurance in the United Kingdom) on behalf of HM Treasury. Equitas Reinsurance Limited and Equitas Limited are only authorised to effect these reinsurances and related activities and to perform the run-off of the reinsured liabilities.

Business review and future developments

The Chairman's Statement, the Chief Executive Officer's Review and the Financial Review on pages 2 to 15 report on the progress of the business during the financial year and outline future developments.

Results

The Equitas Group made a surplus after tax of £12 million for the year ended 31 March 2000 (1999: £54 million) which is being retained in the business. The Company's Articles of Association do not permit the payment of a dividend.

Share capital

The share capital of the Company comprises two ordinary shares of £50 each, which were issued at par on incorporation and which are fully paid, and one deferred share of £1, which was allotted on 2 September 1996 and which is fully paid. The ordinary shares carry voting rights, but no dividends may be paid on these shares. The deferred share carries neither voting nor dividend rights.

Substantial shareholding

Ownership of the entire issued ordinary share capital of the Company was transferred on 3 September 1996 from the Corporation of Lloyd's to the seven Trustees of The Equitas Trust who hold these shares jointly.

The Corporation of Lloyd's owns the one deferred share in the capital of the Company, which carries the right to appoint one Director.

Directors

The names of the Directors at the date of this report, together with brief biographical details, are listed on pages 16 and 17.

Messrs ME McL Deeny and RB Spooner are the Trustees-nominated Directors. Mr SJO Catlin is the Lloyd's appointed Director.

Messrs MJ Crall and RB Spooner and Mrs JV Barker retire by rotation. They offer themselves for re-appointment at the forthcoming Annual General Meeting.

Mr AC Pollard and Sir Roger Neville, who also served as Directors during the year, stepped down as Directors on 17 September 1999. Mr Pollard continues to act as a consultant to the Group.

All Directors of the Company also hold office as Directors of Equitas Reinsurance Limited and Equitas Limited.

Directors' interests

Mr ME McL Deeny has an interest in the business of the Group as an underwriting member of Lloyd's who resumed underwriting in 1999 after having ceased to do so in 1994. Messrs SJO Catlin, JAB Joll and RB Spooner also have an interest in the business of the Group as former underwriting members of Lloyd's who ceased underwriting in 1997, 1991 and 1993, respectively. Mr Catlin has a continuing interest in Syndicate 2003 through his shareholding in Catlin Westgen Limited, the sole member of Syndicate 2003.

Directors appointed prior to September 1997 were provided with indemnities by the Company, Equitas Reinsurance Limited, Equitas Limited and the Corporation of Lloyd's in respect of liabilities arising out of or connected with the Lloyd's Reconstruction and Renewal Plan.

None of the Directors has an interest in shares in any Group company other than Messrs ME McL Deeny and RB Spooner who, since 3 September 1996, have held the two ordinary shares in the Company jointly with the other Trustees of The Equitas Trust.

Corporate governance

The Board supports the Combined Code published by the Committee on Corporate Governance chaired by Sir Ronald Hampel. The Group has in place a framework for sound corporate governance which incorporates many of the principles and provisions of the Code.

The Board

The Board comprises four Executive Directors and seven Non-Executive Directors, including two Trustees-nominated Directors and one Director appointed by the Corporation of Lloyd's. The Board meets regularly and receives detailed reports from management, including in those months in which no Board meeting is held. The roles of Chairman and Chief Executive Officer are split.

The Board is responsible for policy and strategy and for monitoring the performance of executive management. Certain matters are reserved to the Board for collective decision. In addition, there are matters which require the consent of the holders of the ordinary shares pursuant to the Company's Articles of Association. Day to day management is delegated to the Chief Executive Officer.

Non-Executive Directors are appointed for an initial three year term, which may be renewed, and all Directors, except the Lloyd's appointed Director, are subject to the re-election provisions of the Company's Articles of Association.

A procedure is in place for Directors to take independent professional advice, if necessary.

Company Secretary

The Board is supported in its work by the Company Secretary, who co-ordinates the supply of timely information and provides advice.

Board committees

The Board has established five committees with clearly defined terms of reference:

1 The Audit and Compliance Committee

JAB Joll (Chairman), RA Barfield, RB Spooner

The committee meets at least three times a year and reviews the annual financial statements, the interim financial information and the system of internal controls. The Chief Executive Officer, the Finance Director, the external Auditors and the Head of Internal Audit attend meetings as appropriate.

2 The Claims and Commutations Committee

Sir Bryan Nicholson (Chairman), SJO Catlin, MJ Crall, ME McL Deeny

The committee has certain decision making authorities delegated to it by the Board in respect of the adjustment and settlement of major claims, commutations, and the initiation of significant litigation or arbitration. It meets at approximately quarterly intervals.

3 The Investment Committee

RA Barfield (Chairman), JV Barker, MJ Crall, RB Spooner

The committee formulates and decides the strategy for the management of the Equitas Group's investment assets within a broad framework agreed by the Board, develops policies for the management of investment risks, appoints external fund managers and custodians, and monitors their performance. It meets at approximately quarterly intervals. Sir Roger Neville also served as a member of the committee during the year.

4 The Nominations Committee

HA Stevenson (Chairman), SJO Catlin, ME McL Deeny, Sir Bryan Nicholson

The committee is responsible for making recommendations to the Board on the appointment of new Board members other than Directors nominated by the Trustees or appointed by the Corporation of Lloyd's. It meets as necessary.

5 The Remuneration Committee

HA Stevenson (Chairman), ME McL Deeny, JAB Joll

The committee decides on the remuneration and other terms of service of the Executive Directors within a framework agreed by the Board and operates the performance-related incentive arrangements. It also advises on remuneration policy for senior executives. It meets as necessary. Sir Roger Neville also served as a member of the committee during the year.

Internal controls

The Board has adopted the procedures necessary to implement the guidance issued by the Turnbull Committee with respect to the principles of the Combined Code relating to internal controls.

The Board has overall responsibility for the system of internal control and for reviewing its effectiveness. Executive management is responsible for implementation and maintenance of the internal control system, which incorporates a process for identifying, evaluating and managing significant business, operational, financial, compliance and other risks faced by the Group. This is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

The Audit and Compliance Committee, on behalf of the Board, monitors the effectiveness of the Group's system of internal control. The Group maintains an internal audit function that regularly provides reports to the Audit and Compliance Committee. The external Auditors also contribute an independent perspective on aspects of financial control and annually report their findings to the Audit and Compliance Committee and the Board.

Directors' responsibilities

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Group and of the profit or loss of the Group for that period.

In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on a going concern basis unless it is inappropriate to do so.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities. The Directors' responsibility for the accounting records in relation to the reinsured liabilities commenced on 3 September 1996 on execution of the Reinsurance and Run-off Contract. The accounting policies on page 35 set out the issues relevant to the going concern basis for the preparation of the financial statements.

Indemnification of Trustees

The Trust Deed constituting The Equitas Trust provides for indemnification of the Trustees against liabilities arising from or connected with the proper performance of their duties as Trustees. The Trustees have been granted a charge over a £10 million bank deposit as security for this indemnity.

Employees

The Group is committed to a pro-active programme for involving employees. This includes regular communication through briefings and consultation with staff at all levels. A computer-based internal communications system provides information to all employees on work related issues and on matters of general interest. Suggestion schemes are in operation, providing a regular flow of ideas for improving efficiency and performance.

The Group recognises its responsibilities towards disabled people, who receive full and fair consideration for job vacancies for which they are suitable applicants. Employees who become disabled during their working life will be retained in employment and given help with any necessary rehabilitation retraining.

As detailed in the Chief Executive Officer's review, since the year end the Group has begun to outsource selected segments of the business. Employees in relevant business areas will be transferred to the employment of the selected outsourced service providers.

Suppliers

It is the policy of the Group to establish terms of payment with suppliers when agreeing the terms of business transactions. The aim is to effect payment in accordance with agreed terms.

Charitable and political donations policy

The Group has not made any charitable or political donations in the year and will not make any political donations. The Directors do not intend to make any charitable donations, but will keep this under review.

Year 2000

The Group's business critical systems (including those maintained by key external service providers) did not suffer any material disruption as a result of the advent of the Year 2000.

The total cost of the Group's Year 2000 compliance efforts was £4 million, in line with estimates. These costs were written off to the profit and loss account as incurred. The cost incurred during the year ended 31 March 2000 was £1.6 million (1999: £1.9 million).

Auditors

A resolution to reappoint PricewaterhouseCoopers as Auditors to the Company will be put to the forthcoming Annual General Meeting.

As permitted by the Company's Articles of Association, indemnities have been given to PricewaterhouseCoopers against costs and liabilities incurred or arising out of their work as Auditors in circumstances where a court finds in their favour.

By Order of the Board
Stephen Britt
Company Secretary
18 July 2000

Board report on Directors' remuneration

for the year ended 31 March 2000

Policy on Executive Directors' remuneration

The Equitas Group operates in an international environment. In framing its policy on remuneration, the Group aims to:

- set reward structures which enable the Group to attract, retain and motivate executives with the appropriate skills, background and experience to operate effectively in a run-off environment;
- pay basic salaries approximately at the median of market rates for companies in the same industry and of similar size; and
- provide a significant bonus opportunity based on the achievement of measurable goals and an executive's personal contribution to the Group's overall performance.

The Remuneration Committee, which comprises Messrs HA Stevenson, ME McL Deeny and JAB Joll, is responsible for setting the remuneration and other terms of service of the Executive Directors. It consults with the Chief Executive Officer regarding executive remuneration and seeks independent external professional advice, as appropriate, regarding market comparisons and developments in remuneration practice.

Performance-related incentive arrangements

The Group has an annual cash bonus plan in which all permanent employees participate. Awards are subject to achievement of financial goals and personal performance criteria.

In addition, the Group operates a long-term incentive plan (LTIP) for senior executives. This provides for cash payments in recognition of the performance of the Group during a financial year. Payments are deferred for two additional years and are dependent on the continued performance of the Group during this period. The payment of an award is also conditional upon the participant continuing in the employment of the Group throughout the three year period, other than in certain circumstances in which case the entitlement may be pro-rated.

Details of provisional awards made to date under the LTIP in respect of the Executive Directors are shown on page 26.

The Remuneration Committee administers the annual cash bonus plan and the LTIP under its delegated powers and decides on participation and the amounts of incentive payments. The Board determines at its discretion the amount which is available to be awarded under the LTIP.

Payments under performance-related incentive arrangements are not pensionable.

Service agreements

Messrs MJ Crall, PA Jardine and SP Moser and Mrs JV Barker have service agreements with Equitas Management Services Limited which are subject to 12 months' notice on a rolling basis. Mr AC Pollard's service contract as a Director ended by agreement as from 31 July 1999 although he continued to serve as a Director until 17 September 1999. Mr Pollard entered into a contract as a consultant to the Group with effect from 1 August 1999. That contract can be terminated by either party on 90 days' notice.

Non-Executive Directors' fees

Non-Executive Directors, including the Chairman, do not have service agreements. They do not have bonus or pension arrangements. The Chairman's fee is £125,000 per annum, inclusive of the Director's fee. Non-Executive Directors receive a fee of £30,000 per annum, unchanged from the previous two years. Non-Executive Directors who chair Board committees receive an additional fee of £10,000 per annum for these services, which is also unchanged. Mr HA Stevenson did not receive an additional fee for chairing committees.

Directors' remuneration

Directors' remuneration in respect of the financial year ended 31 March 2000 was:

	Salary/ Fees £	*Bonus* £	*Benefits-in-kind* £	*Total emoluments* £	*Pension contribution* £	*Total for year ended 31 March 2000* £	*Total for year ended 31 March 1999* £
Chairman							
HA Stevenson[1]	125,000			125,000		125,000	69,583
DK Newbigging[2]						–	116,667
Executive Directors							
MJ Crall	343,750	200,000	5,610	549,360	85,937	635,297	555,594
JV Barker	230,000	130,000	1,262	361,262	57,500	418,762	365,272
PA Jardine[3]	225,000	150,000	1,319	376,319	56,250	432,569	60,585
SP Moser	278,750	175,000	2,558	456,308	69,688	525,996	445,807
AC Pollard[4]	92,778	23,194	189	116,161	16,667	132,828	328,988
Non-Executive Directors							
RA Barfield	40,000			40,000		40,000	40,000
SJO Catlin	30,000			30,000		30,000	30,000
ME McL Deeny	30,000			30,000		30,000	30,000
JAB Joll	40,000			40,000		40,000	40,000
Sir Roger Neville[5]	17,500			17,500		17,500	30,000
Sir Bryan Nicholson	40,000			40,000		40,000	40,000
RB Spooner	30,000			30,000		30,000	30,000
Total	1,522,778	678,194	10,938	2,211,910	286,042	2,497,952	2,182,496

[1] Mr HA Stevenson assumed the duties of Chairman on 1 November 1998.

[2] Mr DK Newbigging retired from the Board on 31 October 1998.

[3] Mr PA Jardine joined the Board on 1 February 1999.

[4] Mr AC Pollard retired from the Board on 17 September 1999.

[5] Sir Roger Neville retired from the Board on 17 September 1999.

Based on the results for the year ended 31 March 1999, a total amount of £632,100 has been provided as follows for awards under the LTIP to the current Executive Directors:

	Provisional awards outstanding in respect of year ended 31 March 1998 £	*Provisional awards made during the year in respect of year ended 31 March 1999* £	*Total provisional awards outstanding* £
MJ Crall	147,674	208,800	356,474
JV Barker	94,000	136,900	230,900
PA Jardine	94,000	122,000	216,000
SP Moser	128,874	164,400	293,274
Total	464,548	632,100	1,096,648

An amount of £123,300 (1999: £80,558) has been provisionally awarded during the year to Mr AC Pollard, who stepped down as an Executive Director during the year.

LTIP awards relating to the year ended 31 March 1998, for which provision was made in the year ended 31 March 1999, are expected to be paid in 2000. LTIP awards relating to the year ended 31 March 1999, for which provision was made in the year ended 31 March 2000, are not payable until 2001. Payments are subject to the Board's determination that all of the conditions governing the plan have been met.

No LTIP awards have yet been made in respect of the year ended 31 March 2000.

Messrs ME McL Deeny and RB Spooner also received fees for services as Trustees of The Equitas Trust. Details are shown on page 27.

No Director waived any emoluments during the period ended 31 March 2000.

The Group provides Executive Directors with benefits-in-kind including medical and death-in-service benefits, and contributes towards their pension arrangements which are based on defined contributions. A percentage of basic salary is paid into the Group's pension scheme or at the direction of the Executive Director concerned.

The Equitas Trustees

The Trust Deed constituting The Equitas Trust contains provisions entitling the Trustees to remuneration and the discharge of expenses properly incurred by them in acting as Trustees. These are met by the Group and are defined as related party transactions under Financial Reporting Standard 8.

The remuneration and expenses met by the Group in the year ended 31 March 2000 were in respect of the following:

	Year ended 31 March 2000 £	*Year ended 31 March 1999 £*
Trustees' fees	200,000	200,000
Trustees' legal, professional and other costs and expenses	321,150	441,964
Total	521,150	641,964

Messrs ME McL Deeny and RB Spooner, who are also Directors of the Company, received fees of £33,340 each for the year ended 31 March 2000 (1999: £33,340 each). They received expenses for secretarial, office and other overheads of £16,402 and £15,420, respectively (1999: £12,266 and £15,919, respectively).

Report of the Auditors

to the Members of Equitas Holdings Limited

1. We have audited the financial statements on pages 30 to 47 which have been prepared in accordance with the accounting policies set out in note 1 on page 35.

Respective responsibilities of directors and auditors

2. The directors are responsible for preparing the Annual Report. As described on page 21, this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and our profession's ethical guidance.

3. We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the United Kingdom Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Group has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

4. We read the other information contained in the Annual Report and consider the implications of our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of opinion

5. We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. In the light of the exceptional circumstances of the Group, our opinion is qualified in respect of the uncertainties described below. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Group, consistently applied and adequately disclosed.

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

Uncertainties in our audit of claims outstanding, reinsurers' share of claims outstanding and reinsurance recoveries

Uncertainties

7. In forming our opinion, we have considered the uncertainties, described in notes 1 and 15 to the financial statements, relating to the provision for claims outstanding of £9,030 million, reinsurers' share of claims outstanding of £2,046 million and reinsurance debtors of £1,596 million. Future experience may show material adjustments are required to these amounts particularly in respect of:

(a) assumptions made in estimating provisions and the reliability of the underlying data upon which estimates are based;

(b) the potential for unforeseen change in the legal, judicial, technological or social environment and the potential for new sources or types of claim to emerge;

(c) assumptions in relation to expected interest yields and the timing of settlement of claims and reinsurance recoveries which influence the discount calculation; and

(d) assumptions in relation to estimating the reinsurers' share of claims outstanding and the extent to which these and amounts due from reinsurers will be collected.

Consequences of uncertainties

8. The potential adjustments referred to in paragraph 7, if adverse in the aggregate, could be material enough to exceed the amount of the shareholders' funds at 31 March 2000 of £784 million. If at any time the directors determine that there are insufficient assets to meet liabilities in full as they fall due then, under the contract by which the Group reinsured the 1992 and prior years' liabilities, the directors may implement a proportionate cover plan under which the Group will then be entitled to pay claims at a reduced rate, and liabilities under the Reinsurance Contract will be restricted in aggregate to assets available such that shareholders' funds would not become negative though they may be reduced to nil.

Qualified opinion arising from uncertainties in our audit

9. Except for material adjustments in respect of the matters described in paragraph 7 above, which may ultimately be required to the provision for claims outstanding, reinsurers' share of claims outstanding, reinsurance recoveries and consequent adjustments to shareholders' funds and the surplus for the year, in our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 March 2000 and of the surplus and cashflows of the Group for the year then ended and have been properly prepared in accordance with the United Kingdom Companies Act 1985.

PricewaterhouseCoopers
Chartered Accountants and Registered Auditors
18 July 2000

Group profit and loss account

for the year ended 31 March 2000

Technical account – general business

			2000		1999
	Note	*£m*	*£m*	*£m*	*£m*
Investment return transferred from non-technical account			**178**		714
Claims paid					
Gross amount		**(2,149)**		(2,247)	
Reinsurers' share		**892**		952	
Net claims paid		**(1,257)**		(1,295)	
Change in the provision for claims					
Gross amount		**1,438**		2,304	
Reinsurers' share		**(215)**		(936)	
Unwinding of the discount		**(56)**		(484)	
Timing of net future payments		**(73)**		(217)	
Change in the net provision for claims	15	**1,094**		667	
Claims incurred, net of reinsurance			**(163)**		(628)
Other technical charges	3		**3**		(1)
Balance on the technical account for general business			**18**		85

The accounting policies and notes on pages 35 to 46 form an integral part of these financial statements.

Group profit and loss account

for the year ended 31 March 2000

Non-technical account – general business

	Note	£m	2000 £m	£m	1999 £m
Balance on the technical account for general business			**18**		85
Income from financial investments		**326**		349	
(Losses)/gains on realisation of investments		**(35)**		367	
Movement on unrealised investment gains and losses		**(126)**		(155)	
Return on financial reinsurances		**13**		89	
Other financial income	4	**–**		64	
Investment return		**178**		714	
Allocated investment return transferred to general business technical account		**(178)**		(714)	
Investment return retained			**–**		–
Surplus on ordinary activities before tax	5		**18**		85
Tax on surplus on ordinary activities	8		**(6)**		(31)
Retained surplus for the year	14		**12**		54

No gains and losses have been recognised other than through the profit and loss account and the Group has no discontinued activities.

The accounting policies and notes on pages 35 to 46 form an integral part of these financial statements.

Group balance sheet

as at 31 March 2000

Assets

	Note	*2000* *£m*	*1999* *£m*
Investments			
Financial investments	9	**5,342**	6,089
Financial reinsurances	10	**1,027**	1,262
		6,369	7,351
Reinsurers' share of technical provisions			
Claims outstanding	15	**2,046**	2,312
Debtors			
Debtors arising out of reinsurance operations	12	**1,663**	1,737
Other debtors		**149**	116
		1,812	1,853
Other assets			
Tangible assets		**13**	14
Cash at bank and in hand		**34**	40
		47	54
Prepayments and accrued income			
Accrued interest		**71**	83
Other prepayments and accrued income		**5**	7
		76	90
Total assets		**10,350**	11,660

The accounting policies and notes on pages 35 to 46 form an integral part of these financial statements. The Company's balance sheet is shown on page 47.

Group balance sheet

as at 31 March 2000

Liabilities

	Note	*2000* *£m*	*1999* *£m*
Capital and reserves			
Called up share capital	13	**–**	–
Retained surplus	14	**784**	772
Shareholders' funds – non-equity interests		**784**	772
Technical provisions			
Claims outstanding	15	**9,030**	10,348
Deposits received from reinsurers		**–**	15
Creditors			
Creditors arising out of reinsurance operations	16	**264**	343
Other creditors including taxation and social security	17	**272**	182
		536	525
Total liabilities		**10,350**	11,660

The financial statements on pages 30 to 46 were approved by the Board on 18 July 2000 and were signed on its behalf by:

HA Stevenson
MJ Crall
JV Barker

The accounting policies and notes on pages 35 to 46 form an integral part of these financial statements.

Group cashflow statement

for the year ended 31 March 2000

Reconciliation of surplus on ordinary activities before tax to net cash outflow from operating activities

	Note	£m	2000 £m	£m	1999 £m
Surplus on ordinary activities before tax			**18**		85
Depreciation of tangible fixed assets	5	**5**		4	
Exchange gains on retranslation of opening balances		**(1)**		(1)	
Movement on unrealised investment gains and losses		**126**		155	
Return on financial reinsurances		**(13)**		(89)	
Decrease in provision for claims outstanding		**(1,394)**		(1,522)	
Decrease in reinsurers' share of technical provisions – claims outstanding		**287**		838	
Decrease in debtors		**88**		136	
Increase in creditors		**10**		72	
			(892)		(407)
Net cash outflow from operating activities			**(874)**		(322)
Taxation paid			**(13)**		(33)
Capital expenditure			**(4)**		(6)
Net cash outflow for the year			**(891)**		(361)
Cashflows were invested/(realised) as follows:					
Increase/(decrease) in cash holdings	19		**4**		(25)
Net portfolio investment					
Deposits with credit institutions		**(205)**		284	
Financial reinsurances		**(248)**		(244)	
Shares and other variable yield securities and units in unit trusts		**181**		82	
Debt securities and other fixed-interest securities		**(623)**		(458)	
	19		**(895)**		(336)
Net realisation of cashflows	20		**(891)**		(361)

The accounting policies and notes on pages 35 to 46 form an integral part of these financial statements.

Notes to the financial statements

for the year ended 31 March 2000

1 Accounting policies

No material changes in respect of accounting policies have been made this year.

Going concern

Significant uncertainties exist as to the accuracy of the provision for claims outstanding established by Equitas Limited and recoveries due from reinsurers shown in the balance sheet, further details of which are set out in note 15 to the financial statements. The ultimate cost of claims and the amounts ultimately recovered from reinsurers could vary materially from the amounts established and could, therefore, have a materially adverse effect on the ability of Equitas Limited to meet the reinsured liabilities in full.

In addition, there is uncertainty as to whether actual investment yields and the actual timing of claims settlements and reinsurance recoveries will match those assumed in discounting the provision for claims outstanding and reinsurance recoveries. Further details of these uncertainties are set out in note 15 to the financial statements.

If at any time the Directors of Equitas Reinsurance Limited believe that the reinsured liabilities cannot be met in full, they may consider implementing a proportionate cover plan. At the date of this report, the Directors believe that the assets should be sufficient to meet all liabilities in full.

Basis of accounting

The financial statements of the Group have been prepared in accordance with applicable accounting standards in the United Kingdom, the Statement of Recommended Practice on accounting for insurance business issued by the Association of British Insurers in December 1998 and in accordance with Section 255A of, and Schedule 9A to, the Companies Act 1985. The balance sheet of the Parent Company has been prepared in accordance with Section 226 of, and Schedule 4 to, the Companies Act 1985. A summary of the more important accounting policies, which have been applied consistently, is set out below.

The financial statements have been prepared in accordance with the historical cost convention modified by the revaluation of certain assets and liabilities. An annual basis of accounting has been adopted.

(a) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries from 1 April 1999 to 31 March 2000.

(b) Claims and related reinsurance recoveries

The provision for claims outstanding in the consolidated balance sheet is based upon the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related claims handling expenses. Provisions for claims outstanding are stated gross of recoveries to be made on reinsurance contracts purchased by the reinsured syndicates in recognition of the fact that they are separate liabilities and assets of the Group.

Claims incurred include all operational expenses relating to the run-off of the reinsured liabilities. Deductions are made for salvage and other recoveries. Additional premiums receivable and payable by syndicates in respect of risks accepted under the Reinsurance and Run-off Contract are included within the movement of claims incurred.

The adequacy of the provision for claims outstanding is assessed by reference to actuarial and other studies of the ultimate cost of liabilities, which use exposure based and statistical techniques. Significant delays occur in the notification and settlement of certain claims, and a substantial measure of experience and judgment is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the balance sheet date. The gross provision for claims outstanding and the related reinsurance recoveries are determined on the basis of information currently available; however, it is inherent in the nature of the business written that the estimates of the ultimate liabilities will vary as a result of subsequent developments.

(c) Discounting

As the reinsured liabilities will not be fully settled for many years, the provisions for claims outstanding and related reinsurance recoveries have been discounted (see note 15). The Group has structured its asset portfolio to match its expected liability stream. Accordingly the rate of discount applied to those liabilities is calculated having regard to the current prospective yields associated with its asset portfolio.

(d) Tangible assets

Tangible assets are stated at cost less accumulated depreciation. The cost of tangible assets is their purchase cost together with any incidental costs of acquisition. Depreciation is calculated so as to write off the cost of tangible assets, less their estimated residual values, on a straight line basis over the expected useful economic lives of the assets concerned.

(e) Deferred taxation

Provision is made for deferred taxation, using the liability method, on all material timing differences to the extent that it is probable that a liability or asset will crystallise in the foreseeable future.

(f) Investments

Listed investments are stated at mid-market value based on prices quoted by the relevant exchanges. Other investments are stated at prices quoted by various recognised sources. Securities lent are valued on the same basis. In the Company’s accounts, investments in Group undertakings are stated at cost.

(g) Financial reinsurances

In accordance with Financial Reporting Standard 5 – Reporting the Substance of Transactions, financial reinsurance policies are accounted for as investment assets. They are stated at the value of the expected receipts discounted at market yields to recognise the period until receipt. The change in the amount by which these assets are discounted from one period end to the next is recognised as investment return.

(h) Investment return

The return from investments, which is reported on an accruals basis and includes net income from securities lent, is transferred together with the related foreign withholding taxes to the technical account.

(i) Foreign exchange

Assets and liabilities are translated into Sterling at the rates of exchange ruling at the balance sheet date and the exchange differences taken to the profit and loss account. Transactions during the period are translated into Sterling using the rate of exchange prevailing at the time of the transaction, with the exchange differences taken to the profit and loss account.

(j) Pension costs

The Group operates a defined contribution pension scheme. Contributions payable to the scheme are charged in the period in which they are incurred.

The Group provides no other post-retirement benefits to its employees.

(k) Leases

Operating lease costs are charged in the period in which they are incurred.

2 Segmental information

The Group transacts only one class of business, being 100% proportional reinsurance written in the United Kingdom.

3 Other technical charges

Other technical charges relate to foreign exchange differences.

4 Other financial income

Other financial income in the prior year represents an early settlement by Lloyd’s of an obligation to make a payment to Equitas Limited of up to £100 million in February 2002 to protect it from adverse movements in interest rates and the possible shortfall in some deferred payments. Of the amount of £66 million received, £64 million represented other financial income, leaving £2 million to fund the possible shortfall in deferred payments.

5 Surplus on ordinary activities before tax

The surplus is stated after charging:

	Group 2000 £m	*Group 1999 £m*
Auditors' remuneration – audit fees	**2.4**	2.8
– non-audit fees	**0.5**	0.6
	2.9	3.4
Depreciation – tangible owned fixed assets	**4.9**	3.8
Operating lease rentals incurred – property	**3.1**	3.0
– other	**0.3**	0.4

The audit fees for the Company were borne by a subsidiary company.

Details of related party transactions, as defined by Financial Reporting Standard 8, are given on page 26.

6 Employees

The monthly average number of persons employed by the Group, including Directors, was 872 for the year ended 31 March 2000 (1999: 828), all of whom were engaged in run-off and related activities.

Total staff costs, including those for Directors, comprised the following:

	Group 2000 £m	*Group 1999 £m*
Wages and salaries	**39**	35
Social security costs	**4**	3
Pension contributions	**4**	4
	47	42

7 Directors' emoluments

The aggregate remuneration of the Directors was as follows:

	Group 2000 £000	*Group 1999 £000*
Executive Directors – remuneration	**1,859**	1,502
– pension contributions	**286**	254
Non-Executive Directors – fees	**353**	426
	2,498	2,182

In addition to the above amounts, conditional awards under the long term incentive plan were made to the Executive Directors as detailed on page 26. Full details of the remuneration of, and transactions with, Directors are given in the Board Report on Directors' Remuneration on page 24.

8 Tax on surplus on ordinary activities

	Group 2000 £m	Group 1999 £m
United Kingdom corporation tax at 30% (1999: 31%)		
Current	**9**	31
Overprovision in respect of prior years	**(3)**	–
	6	31

9 Investments: financial investments

	£m	Group 2000 £m	£m	Group 1999 £m
Listed				
Shares and other variable yield securities and units in unit trusts	**280**		100	
Debt securities and other fixed interest securities	**4,477**		5,203	
		4,757		5,303
Unlisted				
Deposits with credit institutions		**585**		786
Market value		**5,342**		6,089
Cost		**5,386**		6,006

These investments include Sterling denominated assets of US$410 million (1999: US$410 million) equivalent which are charged in favour of the New York Insurance Department and a charge over Sterling denominated assets of A$217 million (1999: A$325 million) equivalent in favour of Citibank NA to support obligations undertaken in Australia on the Group's behalf. This charge remained in place throughout the year. It was released on 4 July 2000 following the establishment of the Equitas Australian Trust Fund.

Included in the above table are lent securities with a market value of £54.7 million (1999: £nil), which were fully collateralised.

Certain investments are held in trust funds as described in note 11.

10 Investments: financial reinsurances

The average prospective rate of return on financial reinsurances is 7 per cent (1999: 6 per cent) per annum. The mean term is five (1999: five) years. The value of the expected receipts from financial reinsurances, before discounting at market yields to recognise the period until receipt, is £1,375 million (1999: £1,618 million).

11 Trust funds

Financial investments amounting to £2,847 million (1999: £3,116 million) and cash amounting to £0.4 million (1999: £nil) were held in trust funds in the United States and Canada. In addition, all proceeds of financial reinsurances are assigned to a trust fund in the United States. These trust funds were established under the laws of those countries for the settlement of claims relating to those jurisdictions. The amounts held in these trust funds cannot be used for any other purpose and can only be released with the appropriate regulatory consent if there is a surplus of assets over the liabilities they support.

The Equitas Australian Trust Fund, financed by a letter of credit of A$180 million, was established under a trust deed dated 7 June 2000 in anticipation of the release of the charge in favour of Citibank NA (see note 9).

12 Debtors arising out of reinsurance operations

	Group 2000 £m	*Group 1999 £m*
Unpaid premium	**30**	54
Reinsurance recoveries	**1,596**	1,627
Other	**37**	56
	1,663	1,737

The unpaid premium is being collected by the Corporation of Lloyd's on the Group's behalf and includes £6.6 million (1999: £10.3 million) receivable through a structured payment plan secured upon bank guarantees. The remaining amount consists mainly of brokers' contributions under deferred payment arrangements.

Reinsurance recoveries are stated after elimination of inter-syndicate transactions.

13 Called up share capital

	Company 2000 £	*Company 1999 £*
Authorised, allotted and called up		
1 deferred share of £1	**1**	1
2 ordinary shares of £50 each	**100**	100
	101	101

All of these shares were issued at par and are fully paid.

The deferred share carries the right to appoint and remove one Director of Equitas Holdings Limited (who will also serve as a Director of Equitas Reinsurance Limited and Equitas Limited) and is held by the Corporation of Lloyd's. On winding up, the deferred share carries no rights to any portion of surplus assets of the Company other than a return of the par value; it is accordingly a non-equity share.

The ordinary shares bear the right to appoint and remove the remaining Directors of the Company and to decide all matters reserved for decision by shareholders. The Articles of Association do not permit the payment of a dividend on the ordinary shares. Accordingly, these are non-equity shares.

14 Retained surplus

	Company £	*Group £m*
At 1 April 1999	**–**	772
Retained surplus for the year	**–**	12
At 31 March 2000	**–**	**784**

The retained surplus is not distributable.

15 Provision for claims outstanding

	Claims £m	*Reinsurance £m*	*Group 2000 Net £m*	*Claims £m*	*Reinsurance £m*	*Group 1999 Net £m*
Provisions before discounting	**13,212**	**2,910**	**10,302**	14,316	3,225	11,091
Discount	**(4,182)**	**(864)**	**(3,318)**	(3,968)	(913)	(3,055)
	9,030	**2,046**	**6,984**	10,348	2,312	8,036

Provision has been made for the estimated cost of all future claims liabilities including those incurred but not reported ('IBNR') at the balance sheet date and for the operational cost of handling and settling these liabilities. The provision for claims outstanding is based on actuarial and other assessments of ultimate claims costs including exposure based and statistical methods. While the Group has taken into account all available information within its assessment of future claims liabilities, there is nevertheless significant inherent uncertainty. The ultimate liability may vary as a result of subsequent information and events which may result in significant adjustments being made to the amounts provided.

(a) Claims

Claims are stated after elimination of inter-syndicate transactions.

The provision for claims outstanding includes significant amounts in respect of notified and potential IBNR claims relating to long tail liabilities. These claims are not expected to be settled for many years, and there is considerable uncertainty as to the amounts at which they will be settled. The principal components of long tail liabilities are asbestos, pollution and health hazard (APH) liabilities, which comprised approximately 65 per cent (1999: 55 per cent) of the net discounted provision for claims outstanding.

Potential APH liabilities have been estimated by means of exposure based analyses of the global losses and potential insurance claims arising from these causes and the Lloyd's market share of these claims. These analyses involved the use of many critical assumptions which have a significant effect on the quantification of claims liabilities. These assumptions included those in respect of numbers of and average costs per claim, the basis of liability, and insurance coverage issues. Uncertainty is further increased because of the potential for unforeseen changes in the legal, judicial, technological or social environment, which may increase or decrease the cost, frequency or reporting of claims, and because of the potential for new sources or types of claim to emerge.

Non-APH liabilities comprised approximately 35 per cent (1999: 45 per cent) of the net discounted provision for claims outstanding. The estimation of the majority of these liabilities involved the analysis of separate homogeneous sub-divisions of the underlying syndicate historical claims experience by underwriting year and currency. Notwithstanding the analytical nature of the methodologies adopted, significant judgment was required to determine the necessary level of provision for claims outstanding.

The provision for the cost of handling and settling the claims to extinction was based on an analysis of the expected costs to be incurred in run-off activities and adjusted to reflect savings expected to arise as a result of centralisation and reduction of transaction volumes over time. There are inherent uncertainties in projecting future costs which will be incurred over an extended period of time.

(b) Reinsurance recoveries

Reinsurance recoveries are stated after elimination of inter-syndicate transactions.

In determining the expected reinsurance recoveries on claims outstanding, assumptions have been made about the distribution of these claims based on a combination of historical claims experience and the reinsurance programmes of the Lloyd's syndicates which were reinsured. The reinsurance policies were purchased from approximately 3,000 reinsurers and 2,000 reinsurance 'pools', some of which are no longer paying claims or are subject to insolvency procedures. Provision has been made where companies are currently, or are considered to be at risk of being in the future, unable or unwilling to settle their liabilities in full when due. No single reinsurer accounts for more than 7 per cent (1999: 4 per cent) of the total expected recoveries before discounting.

If the actual experience differs from these assumptions, material adjustments may be required to the amount of reinsurance recoveries, including those amounts within debtors arising out of reinsurance operations.

(c) Discounting

The provision for claims outstanding and the cost of undertaking the run-off has been discounted at a rate of 5.75 per cent (1999: 5 per cent) per annum compound to reflect the time value of money. An adjustment for non-interest bearing assets has been made. The period of time which will elapse before the liabilities are settled has been modelled using the estimated settlement patterns of the underlying claims and associated reinsurance recoveries separately. The long tail liabilities are expected to be paid out over a period in excess of 40 years with the majority of the remaining liabilities expected to be settled in the next several years. As at 31 March 2000, the mean term of the liabilities, that is the weighted average period to settlement where the weights are the undiscounted expected cashflows in each future period, was approximately eight (1999: seven) years.

At each balance sheet date a portion of the increase in the liability for claims outstanding compared to those outstanding at the previous reporting date will relate to discounted claims not yet settled being one period closer to settlement. In effect, one year's interest at the previously assumed discount rate has to be credited to discounted claims which are still outstanding in order to revalue them to the balance sheet date. In addition, any change to the discount rate employed compared to the previous balance sheet date will, other things being equal, result in an increase or decrease to the discounted liability. The combination of these two features is referred to as the 'unwinding' of the discount.

The ability to settle the liabilities in full is also dependent upon the generation of sufficient investment income to match the increase in insurance liabilities that will result each year from the unwinding of the discount. There are uncertainties in forecasting the generation of such investment income, which may vary due to changes in interest rates, exchange rates, the ultimate cost of claims, and the timing of liability settlements and reinsurance recoveries. If there is insufficient investment income to offset the increase in the discounted liabilities arising from the unwinding of the discount, the resulting shortfall will be accounted for through the profit and loss account.

16 Creditors arising out of reinsurance operations

	Group 2000 £m	*Group 1999 £m*
Amounts due in less than one year	**264**	332
Amounts due in more than one year but less than five years	**–**	4
Amounts due in more than five years	**–**	7
	264	343

17 Other creditors including taxation and social security

These balances include corporation tax payable of £23 million (1999: £30 million), of which £18 million (1999: £21 million) is payable in more than one year.

18 Reconciliation of movements in shareholders' funds

	Group 2000 £m	*Group 1999 £m*
Opening shareholders' funds	**772**	718
Surplus for the year (see note 14)	**12**	54
Closing shareholders' funds	**784**	772

The Company made neither a profit nor a loss for the year. As permitted by Section 230 of the Companies Act 1985, the Company does not present its own profit and loss account.

19 Movement in opening and closing portfolio investments net of financing

	Group 2000 £m	*Group 1999 £m*
Net cash inflow/(outflow) for the year (see note 20)	**4**	(25)
Movement arising from cashflows of portfolio investments	**(895)**	(336)
Changes to market values and discount (see note 20)	**(113)**	(66)
Other changes, including exchange rate effects (see note 20)	**26**	200
Total movement in portfolio investments net of financing	**(978)**	(227)
Opening portfolio investments net of financing (see note 20)	**7,376**	7,603
Closing portfolio investments net of financing (see note 20)	**6,398**	7,376

20 Movement in cash, portfolio investments and financing

	At 31 Mar 1999 £m	*Cashflow £m*	*Changes to market values and discount £m*	*Other changes, including exchange rate effects £m*	*At 31 Mar 2000 £m*
Cash at bank and in hand	25	**4**	**–**	**–**	**29**
Deposits with credit institutions	786	**(205)**	**–**	**4**	**585**
Financial reinsurances	1,262	**(248)**	**13**	**–**	**1,027**
Shares and other variable yield securities and units in unit trusts	100	**181**	**(1)**	**–**	**280**
Debt securities and other fixed interest securities	5,203	**(623)**	**(125)**	**22**	**4,477**
	7,376	**(891)**	**(113)**	**26**	**6,398**

During the year shares and other variable yield securities and units in unit trusts of £248 million (1999: £82 million) were purchased and £67 million (1999: £nil) were sold. For the same period debt securities and other fixed interest securities of £5,107 million (1999: £12,190 million) were purchased and £5,730 million (1999: £12,648 million) were sold. Cash at bank and in hand as at 31 March 2000 shown above is stated net of £5 million (1999: £15 million) of overdrafts.

21 Contingent liabilities

The Group has granted certain indemnities to Trustees, Directors, Employees and the Auditors.

Apart from these indemnities, the Group had no contingent liabilities outside the normal course of business at the balance sheet date.

22 Investments in Group undertakings

Company Name	*Class and proportion of shares held*	*Country of incorporation*	*Business activities*
Equitas Reinsurance Limited	Ordinary 100%	England	Reinsurance
Equitas Limited*	Ordinary 100%	England	Reinsurance Run-off
Equitas Management Services Limited	Ordinary 100%	England	Provision of administrative services
Equitas Policyholders Trustee Limited	Ordinary 100%	England	Trustee

**Held via a subsidiary*

No dividends may be paid or capital distributions made by Equitas Reinsurance Limited or Equitas Limited. Any surplus assets would be applied by Equitas Reinsurance Limited towards the payment of a return premium to Reinsured Names. Such a payment would require the consent of the Financial Services Authority on behalf of HM Treasury.

23 Financial commitments

	Group 2000 £m	*Group 1999 £m*
Expiring within one year	**1**	–
Expiring between two and five years inclusive	**–**	1
Expiring in over five years	**3**	3
	4	4

Company balance sheet

as at 31 March 2000

	Note	2000 £	1999 £
Fixed assets			
Investments – investments in Group undertakings	22	**300**	300
Current assets			
Amounts due from a Group undertaking		**1**	1
Net current assets		**1**	1
Total assets less current liabilities		**301**	301
Creditors – amounts falling due after more than one year			
Amounts owed to Group undertakings		**200**	200
Net assets		**101**	101
Capital and reserves			
Called up share capital	13	**101**	101
Profit and loss account	14	**–**	–
Shareholders' funds – non-equity interests		**101**	101

The financial statements on pages 35 to 47 were approved by the Board on 18 July 2000 and were signed on its behalf by:

HA Stevenson
MJ Crall
JV Barker

The accounting policies and notes on pages 35 to 46 form an integral part of these financial statements.

Notices to Reinsured Names

The annual Open Meeting of Reinsured Names will be held at 10.30am on Friday 8 September 2000 at the Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1. All Reinsured Names are invited to attend. A card with complete details of the meeting accompanies this report. Reinsured Names who wish to attend the meeting are asked to return the reply-paid section of the card by 29 August 2000.

Reinsured Names should note that the Reinsurance and Run-off Contract dated 3 September 1996 requires them to notify Equitas Reinsurance Limited of a change of address or, if so required, to provide written confirmation of their addresses. Equitas Reinsurance Limited does not require written confirmation of a Reinsured Name's address at this time, but changes in address in the past 12 months (unless previously notified) should be sent to the Company Secretary, Equitas Reinsurance Limited, 33 St Mary Axe, London EC3A 8LL within 21 days from receipt of this report.

Designed and produced by Fishburn Hedges

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