Equitas Holdings Limited Report & Accounts

for the year ended 31 March 2007

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Review of the year

Equitas has been transformed following the reinsurance agreement completed with National Indemnity Company ('National Indemnity'), a member of the Berkshire Hathaway group of insurance companies, on 30 March 2007. Because of the significance of this agreement, the format of this report and accounts has been changed. We have not prepared a Chairman's statement or Executive Directors' reviews as we have in prior years. The intention is to produce a more concise report and accounts reflecting both the significantly reduced nature and scale of Equitas' operations and the risks associated with Equitas. A review of the transaction with National Indemnity is set out below. A summary of the Group's main activities, other than that reinsurance transaction, is included within the Business review section of the Directors' report.

The National Indemnity Reinsurance Agreement

Overview
There are two phases to the transaction. The first phase involving the purchase of a very significant additional reinsurance cover has now been completed and is outlined below. The second phase involves seeking the approval of the High Court to transfer Names' obligations to policyholders to another company. Further details of the second phase are set out on page 6.

Phase 1
With effect from 30 March 2007, National Indemnity reinsured all of Equitas' reinsurance obligations and provided an additional $5.7 billion of reinsurance cover over and above the existing Equitas reserves at 31 March 2006, less claims payments made and reinsurance recoveries received since 1 April 2006. The premium for this reinsurance consisted of all of Equitas' existing assets less £172 million and a contribution of £72 million from the Corporation of Lloyd's.

The total reinsurance cover available is set out in the table below:

	$m
Net undiscounted reserves at 31 March 2006	**8,686**
Net payments to 30 March 2007	**(574)**
	8,112
Additional reinsurance cover purchased	**5,700**
Reinsurance cover available at 31 March 2007	**13,812**

The net undiscounted reserves at 31 March 2006 in the table above do not include the operating expense reserve at 31 March 2006 since future operating expenses will be met by National Indemnity. As part of the transaction all the assets backing the existing liabilities, other than the Equitas retained assets explained below, were transferred to National Indemnity. The reinsurance cover available is first required to match the current estimate of the claim liabilities of the Group leaving an amount of cover not yet required but available to meet any future increases in the claim liabilities. Cover remaining that is not yet required is not shown in the financial statements but is quantified and explained on page 11.

The enhanced level of cover remaining to meet potential liabilities transforms the prospects for the Group and significantly strengthens the Group balance sheet. The risk that assets will not be sufficient to meet the liabilities as they fall due has been significantly reduced.

Equitas Retained Assets

Following the purchase of the reinsurance from National Indemnity, Equitas retained assets of £172 million which have been allocated as follows:

- £50 million will be available to be paid as a return premium and has been recognised in these financial statements.
- A bonus of £19.9 million, inclusive of employer's National Insurance contributions and other adjustments, was awarded to those who were Executive Directors or staff of Equitas at 30 March 2007. At 31 March 2007, £10.4 million of this bonus pool had been paid and the balance was paid in April 2007.
- The balance of £102 million will remain in Equitas. Of this amount, £22 million has been earmarked to purchase additional reinsurance cover at Phase 2 of the transaction. It is hoped that most of the balance of approximately £80 million will ultimately be payable to Reinsured Names, although future governance costs and the legal and transaction costs associated with Phase 2 must also be paid out of these retained funds.

How the run-off is managed

National Indemnity has taken on the staff and operations of the Group through the acquisition of the Group's management services company, Equitas Management Services Limited ('EMSL'). EMSL made staff, premises and other facilities available to Equitas. EMSL has now been renamed Resolute Management Services Limited ('RMSL').

RMSL manages the run-off as agent for Names. The costs of running RMSL will be met by National Indemnity, for as long as the total of claims paid (net of reinsurance recoveries) by National Indemnity is less than the total cover provided. RMSL is entitled to exercise wide powers to manage the retroceded business and is required to exercise those powers in the interests of Equitas and Names. Through this arrangement, the run-off continues to be managed by substantially the same people as in the past.

Role of Equitas

While the reinsurance agreement concluded on 30 March 2007 provides very significant additional reinsurance cover to Equitas, it does not disturb the existing chain of reinsurance established as part of Lloyd's Reconstruction and Renewal. Since Names remain ultimately responsible for their insurance liabilities before Phase 2 of the transaction, the agreement includes a number of provisions that allow continued monitoring of the run-off. Jane Barker, as Chief Executive, will carry out this monitoring function, reporting to the Board.

Protection

RMSL manages the claims adjusting process. National Indemnity will not be required to provide security for its reinsurance obligations for so long as National Indemnity's insurer financial strength rating, as measured by Standard & Poor's, remains at AA- or higher. If, however, National Indemnity's rating were to drop below this level, it must either provide a letter of credit or establish a trust fund, equal to 102 per cent of its net liabilities under the agreement (provided that this does not exceed the remaining reinsurance cover), plus estimated future operating expenses. If National Indemnity's rating falls below A- then the 102 per cent requirement increases to 125 per cent (provided that this does not exceed the remaining reinsurance cover).

The trust fund arrangements in North America that ring fence assets to match a large proportion of the liabilities that Equitas reinsures continue, thus providing additional protection to policyholders.

Implications for the financial statements

The transaction means that the current financial statements are much changed from prior years. For the first time in Equitas' history, the balance sheet at 31 March 2007 has been prepared on an undiscounted basis. In previous years the provisions for claims outstanding and related reinsurance recoveries were discounted as the liabilities were not expected to be fully settled for many years. The Companies Act 1985 permits discounting to take account of future investment income. As a result of the transaction with National Indemnity, Equitas does not have assets matching the provision for claims outstanding so it is no longer permitted to discount this provision and the related reinsurance recoveries. The unwinding of the discount has been reflected in the profit and loss account.

Accounting for the normal business transactions of the Group is unchanged from prior years. The transaction with National Indemnity was completed on the last working day of the financial year and the accounting entries relating to the transaction have been made as the last entries in the year to 31 March 2007, as reflected in the tables below.

All of the assets of the Group have been transferred to National Indemnity other than the £172 million retained funds. The transfer is accounted for as an outwards reinsurance premium in the profit and loss account (see note 4 on page 35). A new reinsurance asset recoverable from National Indemnity has been recorded in the balance sheet equal to the technical provision for claims outstanding.

Equitas retained assets of £172 million following the transaction. At the balance sheet date, £10.4 million of these assets had been paid as bonuses to Executive Directors and staff, hence the financial investments of £162 million shown in the balance sheet on page 26. A further £9.5 million is payable to HM Revenue and Customs in respect of the bonuses and £50 million is payable as a return premium. After deducting these amounts, the surplus remaining in the Group is £102 million.

The tables below explain how the retained surplus and claims and reinsurance reserves have moved from 1 April 2006. In line with the accounting approach described above, the tables initially show the movements due to transactions and reassessments made during the year followed by the impact of the reinsurance transaction with National Indemnity on the last business day of the year.

Retained surplus

	£m	£m
Retained surplus at 1 April 2006		**458**
Investment return in excess of the unwinding of the discount	85	
Reassessment of:		
Claims	(26)	
Reinsurances	(14)	
Exchange Losses	(17)	
Result for the year		28
		486
National Indemnity transaction		
Contribution received from Corporation of Lloyd's	72	
Premium Paid to National Indemnity in excess of liabilities reinsured	(386)	
		(314)
Assets retained		172
Return Premium payable		(50)
Deal bonuses		(20)
Retained surplus at 31 March 2007		**102**

For the period up to the point of the National Indemnity reinsurance, the investment return for the year amounted to £217 million and exceeded the unwinding of the discount by £85 million as shown in the table above. The liabilities were discounted to acknowledge the time value of money using a discount rate based on the prospective yield on the fixed income investments held prior to the National Indemnity reinsurance transaction. The unwinding of the discount is made up of two components as described below:

	£m
Reduction of one year in period over which net liabilities are discounted	132
Effect of change in discount rate	-
Unwinding of the discount	**132**

The discount rate for the year has remained unchanged at 4.30 per cent per annum reflecting market yields at 30 March 2007.

Provision for claims outstanding

	Claims *£m*	*Reinsurance* *£m*	*Net* *£m*
Provisions at 1 April 2006	**4,176**	**(360)**	**3,816**
Payments, receipts and accruals	(388)	46	(342)
Unwinding of the discount	150	(18)	132
Reassessment of liabilities and reinsurances	26	14	40
Exchange movements	(378)	37	(341)
Year end prior to transaction	**3,586**	**(281)**	**3,305**
Reinsurance asset transferred to National Indemnity	-	281	281
Expense liability transferred to National Indemnity	(311)	-	(311)
Unwinding of the discount	1,482	-	1,482
Reinsurance cover from National Indemnity	-	(4,757)	(4,757)
Provisions at 31 March 2007	**4,757**	**(4,757)**	**-**

The responsibility for collecting the reinsurance asset has passed to RMSL. National Indemnity receives the economic benefit of any recoveries, similarly it bears the loss should the reinsurance be uncollectable. Therefore the economic benefit of the reinsurances all falls to National Indemnity and so no recoveries, other than the reinsurance due from National Indemnity under the reinsurance agreement, are shown in the Group's balance sheet.

Phase 2

The remaining important objective for the Group is to achieve a transfer of all the reinsured liabilities from Names if and when it becomes possible to do so – thus providing true finality under English law. This second phase (should it proceed) will involve the transfer of Names' obligations to policyholders to Equitas Limited, Equitas Reinsurance Limited or a new insurance company specially formed for the purpose. If completed, this Transfer of Business will achieve the Group's ultimate objective of complete finality for Names, assuming foreign courts recognise the transfer.

Equitas has the option to purchase further reinsurance from National Indemnity of up to $1.3 billion at a cost of up to £40 million, provided the transfer is completed by 31 December 2009. The Corporation of Lloyd's has committed to pay £18 million which will be used towards the cost of this additional reinsurance cover. The option to purchase the additional reinsurance cover is not available in the unlikely event that Equitas' net undiscounted reserves (inclusive of IBNR) have deteriorated by more than US$2 billion since 31 March 2006.

The Transfer of Business will be implemented under the provisions of the Financial Services and Markets Act 2000 ('FSMA 2000') which govern the transfer of insurance portfolios. This type of transfer is sometimes referred to as a "novation". Amendments are required to the FSMA 2000 provisions to permit those Names who ceased to be underwriting members of Lloyd's prior to December 1996 to participate in the transfer. It is hoped that the amendments will come into effect before the end of 2007. HM Treasury has consulted on the proposed changes.

FSMA 2000 requires the Transfer of Business to be approved by the High Court. It cannot be guaranteed that the High Court will give this approval. However, Equitas is optimistic that the High Court's approval will be obtained, particularly as the Transfer of Business would enable additional reinsurance cover of up to US$1.3 billion to be purchased for the ultimate benefit of policyholders.

Provided the Financial Services Authority ('FSA') agrees, a second return premium is contemplated following the Transfer of Business. The amount of this payment will, however, depend upon a number of factors that cannot be determined at this point, including any additional FSA capital requirements and costs incurred by Equitas and the Equitas Trustees during Phase 1.

If it is not possible to pay out all the remaining funds immediately following the Transfer of Business, then future payments will be paid as soon as funds can prudently be released, subject to FSA approval.

If the Transfer of Business does not occur by 31 December 2009, for whatever reason, the Corporation of Lloyd's will still make the additional payment of £18 million. Assuming that the run-off is proceeding as planned, it is hoped that a second payment to Reinsured Names will be made at that time. However, Equitas will need to retain sufficient funds to meet future governance costs and therefore the amount and timing of any additional further payments to Reinsured Names will depend upon a number of factors, including the future capital requirements of the Group.

Conclusion

As a result of the completion of this transaction, the Board of Equitas believes the prospect of the failure of Equitas now to be extremely remote. Equitas has achieved a great deal since its inception but the Board has always been conscious of the serious threats and uncertainties that remained. This transaction has transformed the level of resources available to the Group to meet those threats and uncertainties and leaves the Group substantially better placed to meet all of its liabilities in full.

Board of Directors

Hugh Stevenson
Chairman; joined the Board in 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. He is Chairman of The Merchants Trust PLC and a Non-Executive Director of the Financial Services Authority and Standard Life plc.

Jane Barker
Chief Executive Officer since 30 March 2007. Previously Finance Director since joining the Board in 1995. She is a Non-Executive Director of Alliance & Leicester plc. 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.

Ian Agnew
Lloyd's Appointed Non-Executive Director; joined the Board in 2002. He is Chairman of the Jubilee Group of Companies at Lloyd's, Chairman of Insurance Capital Partners Limited and a member of the Lloyd's Market Supervision and Review Committee. He was formerly Chairman of Wellington Underwriting plc; Chairman of I C Agnew Underwriting Limited; and underwriter of Lloyd's syndicate 672. He is a past Deputy Chairman of Lloyd's.

Michael Deeny
Trustees-nominated Non-Executive Director; joined the Board in 1996. He is Chairman of the Association of Lloyd's Members and Deputy Chairman of The Equitas Trust.

Richard Spooner
Trustees-nominated Non-Executive Director; joined the Board in 1996. He is Chairman of Euractiv.com plc and 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.

Directors' report
for the year ended 31 March 2007

The Directors present their report and the audited financial statements for the financial year ended 31 March 2007.

Principal activities

Background

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. Equitas Reinsurance Limited and Equitas Limited are authorised and regulated under the Financial Services and Markets Act 2000 by the Financial Services Authority.

The National Indemnity Transaction

During the year Equitas Limited entered into a major whole account retrocession agreement with National Indemnity, a member of the Berkshire Hathaway group of companies.

That transaction, and its implications for the Group, is outlined in the Review of the year on pages 2 to 7.

Business review

Results and performance

The Equitas Group incurred a deficit of £356 million in the year ended 31 March 2007 (2006: £18 million deficit). The deficit in the year is attributable to the transaction with National Indemnity, which represents the key development during the financial year. That transaction is outlined in the Review of the year on pages 2 to 7, which explains the position of the Group at the end of the year and is incorporated by reference in this report.

The Group has continued to pursue its strategy to run-off the liabilities reinsured in 1996. The operational results of the business, before the reassessment of reserves for claims and recoveries, were positive in each of the key operating areas: claims management; reinsurance collection and investment management.

As a result of the activity relating to the transaction with National Indemnity a comprehensive actuarial review was not completed for the year ended 31 March 2007. Instead, a high level review was undertaken that focused on those aspects of the reserves with the greatest potential for material change. The brought forward reserves were adjusted for any such changes, as well as net payments in the year and the unwinding of the discount.

The level of detail at which the actuarial analysis has been carried out is, in most cases, considerably less than has historically been the case. As a consequence, the accuracy of the estimated changes in liabilities is less reliable than in previous years, when a full actuarial exercise has been carried out. The Directors are satisfied as to the appropriateness of the level of the review that has been conducted because of the very significant additional reinsurance cover now available to the Group.

Principal risks and uncertainties

The principal risk facing the Group has always been the ability to meet the reinsured liabilities as they fall due in the light of the significant uncertainties as to the accuracy of the provision for claims outstanding shown in the balance sheet. This risk has been significantly reduced following the reinsurance transaction with National Indemnity, which provided an additional $5.7 billion of reinsurance cover above that needed to meet the reserves at 31 March 2006.

The principal risks now facing the Group are the financial security of National Indemnity and the risk that liabilities are in excess of the reinsurance cover purchased. The financial strength of National Indemnity and the provisions in the contract to deal with any changes in that status are outlined on page 4. The Directors believe the potential for the reinsurance cover to be insufficient to cover liabilities to be extremely remote.

Future outlook

The Group will focus on monitoring the run-off, which is now managed by RMSL as agent for Names whose liabilities are reinsured by Equitas. In addition, the Group will work towards completion of the second phase of the transaction to transfer Names' obligations to policyholders to another company. For this to be achieved, changes to FSMA 2000 will be required and it is hoped that these changes will be made by the end of 2007. Once those changes have been implemented, the Transfer of Business will need to be approved by the High Court.

Performance measurement

Following the National Indemnity reinsurance, the key measures of the Group's performance have changed from those reported in the 2006 Report and Accounts. The revised key measures are shown in the table below.

Key measure	What does it show?
Reinsurance cover remaining	The amount of reinsurance cover remaining less the estimate of the current and future liabilities reinsured by the Group. It represents the margin available to cover future reserve deterioration
Surplus	The surplus available to fund the Group expenses in monitoring the run-off, preparing for phase 2 of the transaction and for further return of premium
Gross undiscounted claims outstanding	The expected total remaining liabilities before any deduction for reinsurance on an undiscounted basis

The Group's key performance measures as defined above for the year to 31 March 2007 are set out in the table below:

	2007	*2006*
	$m	*$m*
Reinsurance cover remaining	5,623	N/A
	£m	*£m*
Surplus	102	458
Gross undiscounted claims outstanding	4,757	6,132

The reduction in surplus reflects the purchase of additional reinsurance cover from National Indemnity, the return premium payable and the bonuses paid to those working for Equitas at 30 March 2007.

All measures of the reinsurance cover from National Indemnity are expressed in US dollars in accordance with the reinsurance contract. The exchange rates used to calculate the cover are fixed at the rates prevailing on 31 March 2006.

The steps taken to calculate the cover remaining are shown in the table below and are explained as follows:

- First, a deduction to the cover available is made for the gross technical provisions at 31 March 2007. It is an equivalent figure to that shown in the balance sheet.

- Secondly, the reinsurers' share of technical provisions arising from the reinsurance programmes held by the reinsured syndicates is added back. The benefits of this asset have been transferred to National Indemnity. Although this asset has not yet been collected full credit for the asset is taken in the cover remaining calculation.
- Finally, the amount collectable from other debtors is added back. Any risks or rewards associated with the collection of these balances fall to National Indemnity.

Reinsurance cover remaining

	$m
Reinsurance cover available	13,812
Gross technical provisions	(9,157)
	4,655
Reinsurers' share of technical provisions transferred	797
Other Debtors	171
Reinsurance cover remaining to cover any future reserve deterioration	5,623

As at 31 March 2007, $77 million (or 1.4%) of the $5.7 billion of reinsurance cover purchased from National Indemnity has been utilised to cover reserve deterioration since 1 April 2006.

Share capital and dividends

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.

The Company's Articles of Association do not permit the payment of a dividend.

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 then seven Trustees of The Equitas Trust jointly.

The current Trustees are Sir AN Ridley (Chairman), Mr ME McL Deeny (Deputy Chairman), and Messrs GD Gilchrist, RJR Keeling and RB Spooner. CHL Bathurst QC (Third Viscount Bledisloe) retired as a Trustee with effect from 24 June 2006. Mr RJR Keeling has served notice of resignation as a Trustee, with effect from 1 August 2007.

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 page 8. All held office throughout the year.

Messrs MJ Crall, SP Moser, GE Brace, JA Collins, JW Heap, RA Barfield and JAB Joll also served as Directors during the year. Mr MJ Crall retired from the Board with effect from 5 June 2006. The other Directors stepped down from the Board on 30 March 2007.

Mr M E McL Deeny retires by rotation at the forthcoming Annual General Meeting. He offers himself for reappointment.

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 Company as an underwriting member of Lloyd's who resumed underwriting in 1999 after having ceased to do so in 1994. Messrs IC Agnew and RB Spooner each has an interest in the business of the Company as a former underwriting member of Lloyd's who ceased underwriting in 1998 and 1993, respectively. Mr Agnew also has an interest in the business of the Company through his shareholding in Fortw Underwriting Limited, a corporate member of Lloyd's which is a member of a number of syndicates, through his shareholding in members of the Jubilee Group of Companies at Lloyd's and by the provision of capital to CBSICP Capital Limited which is a corporate member of Lloyd's with a spread portfolio. He is also a shareholder and Chairman of Insurance Capital Partners Limited, which owns and manages capacity provided to various Lloyd's syndicates.

During the year each Director had the benefit of a standard indemnity under the Articles of Association of the Company, Equitas Limited and Equitas Reinsurance Limited in respect of liabilities (including legal fees and expenses) incurred in defending proceedings, whether civil or criminal, in which he is acquitted, judgement is given in his favour or certain other relief is granted. These indemnities did not cover liability attaching to a Director in connection with any finding of negligence, default, breach of duty or breach of trust by him in relation to the Company, Equitas Limited or Equitas Reinsurance Limited. These companies also entered into contractual indemnities with the Directors in respect of liabilities (including legal fees and expenses) incurred to third parties relating to their position as a Director. These indemnities did not apply if a Court in the United Kingdom had determined that the Director did not act honestly nor did they cover criminal fines or regulatory penalties payable by the Director. These contractual indemnities and similar indemnities in favour of employees, which were secured by a charge over a £50 million bank deposit, were replaced by indemnities given by National Indemnity under the reinsurance agreement entered into with that Company. Those indemnities took effect on 30 March 2007. The £50 million security over the bank deposit was released subsequent to the year end.

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.

Financial instruments and risk management

Prior to the reinsurance transaction with National Indemnity, the Group's equity fund managers were permitted to use derivative financial instruments for efficient portfolio management purposes. Strict limits were placed on the type, value and term of such contracts. Following the transaction, the exposure to such instruments was £nil (2006: £2 million).

The Group remains exposed to financial risk through its reinsurance assets, financial assets and liabilities. The Group recognises the importance of having efficient and effective risk management systems in place to identify, manage and monitor those risks.

Credit risk

Following the reinsurance agreement with National Indemnity, responsibility for paying claims and collecting reinsurance falls to RMSL. As a result, the Group's key area of risk is the ability of National Indemnity to pay amounts as they fall due under the retrocession agreement. National Indemnity has been awarded the highest credit rating by Standard and Poor's. The Berkshire Hathaway Group, of which National Indemnity is a wholly owned subsidiary, also carries the highest credit rating of Fitch and AM Best. To manage the Group's risk in this area further, the Group is entitled to require National Indemnity to post a letter of credit or to establish a trust fund equal to 102% or 125% of its net liabilities under the agreement (providing that this does not exceed the reinsurance cover purchased) plus estimated operating expenses, if National Indemnity's rating drops below AA- or A-, respectively.

The risk is further mitigated by the continuing existence of the trust fund arrangements in North America. These trust funds ring fence assets to match a large proportion of the liabilities that Equitas reinsures.

Insurance risk

The insurance provisions in the Group's accounts are subject to significant uncertainty and are based on estimates of future events, which are not all within the Group's control. The additional reinsurance protection purchased by the Group over and above the current reserves mitigates this risk to a substantial degree.

Interest rate risk

Interest rate risk arises primarily from investments in fixed interest securities. In addition, to the extent that claims inflation is correlated to interest rates, liabilities to policyholders are subject to interest rate risk.

The Group no longer holds any fixed interest securities. The Group monitors claims inflation as part of its actuarial assessments. The additional reinsurance protection purchased by the Group over and above the current reserves mitigates this risk to a substantial degree.

Price risk

The Group has very limited exposure to price risk through its remaining investments. The Group's current investment policy is to invest in short term, liquid money market funds and bank deposits. The Board will keep this policy under review.

Liquidity risk

The Group manages its liquidity in order to maintain sufficient financial resources to meet obligations as they fall due. All of the Group's investments are held in readily realisable securities and thus liquidity risk is considered to be low.

Foreign currency exchange risk

The liabilities are denominated in a number of foreign currencies. The reinsurance contract with National Indemnity fixes the rates of exchange to be used to calculate the cover at those prevailing on 31 March 2006. Through this mechanism, National Indemnity bears substantially all of the currency risk that might arise on settlement of the insurance liabilities of the Group.

The other assets and liabilities of the Group are denominated in sterling and carry no currency risk.

Foreign currency risk is considered to be very low because of the high level of reinsurance cover remaining and the financial strength of National Indemnity.

Directors' responsibilities

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company and of the Group and of the profit or loss of the Group for that period.

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

- select suitable accounting policies and then apply them consistently, with the exception of changes arising on the adoption of new accounting standards in the year;
- 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 accounting policies on page 30 set out the issues relevant to the going concern basis for the preparation of the financial statements.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group and 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 Directors confirm they have complied with the above requirements when preparing the financial statements.

Employees

The Group recognises its responsibilities towards disabled people who, to the extent relevant, will receive full and fair consideration for job vacancies for which they are suitable applicants. The Group will take reasonable steps to help employees who become disabled during their working life to continue in employment.

The Group now employs only two employees. The process for involving and consulting employees is therefore informal and ad hoc.

Charitable and political donations

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.

Disclosure of information to Auditors

Each Director confirms that so far as he is aware there is no relevant audit information of which the Company's auditors are unaware. Each Director also confirms that he has taken all the steps that he ought to have taken as a Director in order to make himself aware of any such information and to establish whether the auditors are aware of that information.

Auditors

A resolution to reappoint PricewaterhouseCoopers LLP 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 LLP 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
7 June 2007

Board report on Directors' remuneration
for the year ended 31 March 2007

Following the completion of the National Indemnity retrocession contract the Board has changed significantly, both in terms of number and composition. The Board now includes only one Executive Director among its five members. Accordingly, the Board will now exercise all functions hitherto delegated to the Remuneration Committee.

In the light of the significant reduction in the nature and scale of the Group's operations, in particular as the Group has only two employees (including the Chief Executive Officer), the historic remuneration policies adopted throughout the Group have changed and it is not expected that future years' accounts will include a separate Remuneration Report.

Policy on Executive Directors' remuneration

The Remuneration Committee set the remuneration and other terms of service of the Executive Directors within a framework agreed by the Board and advised on remuneration policy for senior executives. It consulted with the Chief Executive Officer regarding executive remuneration and engaged outside consultants to provide information about market remuneration for executive and general staff.

The remuneration of the Non-Executive Directors is determined by the Board as a whole, having regard to the provisions of the Company's Articles of Association. No Director is involved in setting his own remuneration.

Performance related incentive arrangements

The Group operated an annual cash bonus plan in which all employees participated. Awards were subject to achievement of financial goals and personal performance criteria.

In addition, the Group operated a long-term incentive plan ('LTIP') for selected senior employees. This provided for cash payments in recognition of the performance of the Group during a financial year. Payments were deferred for two additional years and were dependent on the continued performance of the Group during this period. The payment of an award was also conditional upon the employee continuing in the employment of the Group throughout the three-year period.

Details of provisional awards made under the LTIP in respect of those Directors who held executive office during the year are shown on page 20.

The Remuneration Committee administered the annual cash bonus plan and the LTIP under its delegated powers and decided on participation and the amounts of incentive payments. The Board determined at its discretion the amount available to be awarded under the LTIP.

All outstanding LTIP awards were paid on the completion of the National Indemnity agreement.

Payments under performance related incentive arrangements were not pensionable.

Service agreements

The Group's policy is that Executive Directors' service agreements should generally be terminable on 12 months' notice on a rolling basis. Mrs JV Barker's service agreement with Equitas Holdings Limited reflects that policy.

It is not the Group's policy to make ex-contractual payments to Executive Directors on termination of their service agreements.

The Chairman and Non-Executive Directors, supported by the Trustees, approved payments to the Executive Directors of £10,400,000 on the completion of the transaction with National Indemnity in recognition of the extraordinary success achieved by Equitas. In addition a normal annual bonus for the year ended 31 March 2007 was awarded to the Executive Directors amounting to a further £1,005,000.

Non-Executive Directors' fees

Non-Executive Directors, including the Chairman, do not have service agreements but do have letters of appointment. They do not have bonus or pension arrangements. The Chairman's fee during the year was £175,000 per annum, inclusive of his Director's fee. Non-Executive Directors received a fee of £35,000 per annum. Non-Executive Directors who chaired Board committees received an additional fee of £10,000 per annum for these services. Mr HA Stevenson did not receive an additional fee for chairing committees.

Watson Wyatt has reviewed the level of the Chairman's and Non-Executive Directors' fees. Following this review all such fees have been reduced, reflecting the reduced scale of the Group's business.

Directors' remuneration

Directors' remuneration, excluding LTIP payments, was:

	Salary/ Fees £	Bonus £	Benefits-in-kind £	Total emoluments £	Pension costs £	Total for year ended 31 March 2007 £	Total for year ended 31 March 2006 £
Chairman							
HA Stevenson	175,000			175,000		175,000	175,000
Executive Directors							
SP Moser	450,000	3,300,000	1,602	3,751,602	112,500	3,864,102	844,707
JV Barker	341,250	2,185,000	630	2,526,880	85,313	2,612,193	596,298
GE Brace	376,250	2,020,000	1,602	2,397,852	94,063	2,491,915	672,807
JA Collins	286,250	1,950,000	1,602	2,237,852	71,562	2,309,414	491,121
JW Heap	286,250	1,950,000	1,602	2,237,852	71,562	2,309,414	488,430
Non-Executive Directors							
IC Agnew	35,000			35,000		35,000	35,000
RA Barfield	55,000			55,000		55,000	47,500
MJ Crall[1]	6,319			6,319		6,319	35,000
ME McL Deeny	45,000			45,000		45,000	37,500
JAB Joll	45,000			45,000		45,000	45,000
Sir Bryan Nicholson[2]	-			-		-	33,750
RB Spooner	35,000			35,000		35,000	35,000
Total	2,136,319	11,405,000	7,038	13,548,357	435,000	13,983,357	3,537,113

Mrs JV Barker was entitled to fees of £65,000 in respect of her services as a Non-Executive Director of Alliance & Leicester plc. In accordance with the terms of her service agreement, this amount was paid directly to a Group company.

Based on the results for the year ended 31 March 2006 and 31 March 2007, a total amount of £3,200,000 was awarded and paid as follows under the LTIP to the Executive Directors:

	Total provisional awards outstanding at 31 March 2006 £	Awarded during the year £	Paid during the year £	Total provisional awards outstanding £
SP Moser	800,000	800,000	1,600,000	-
JV Barker	600,000	600,000	1,200,000	-
GE Brace	600,000	600,000	1,200,000	-
JA Collins	550,000	600,000	1,150,000	-
JW Heap	550,000	600,000	1,150,000	-
Total	3,100,000	3,200,000	6,300,000	-

LTIP awards relating to the year ended 31 March 2005, 31 March 2006 and 31 March 2007 were paid on completion of the retrocession agreement with National Indemnity.

[1] Mr Crall retired as a Non-Executive Director on 5 June 2006.

[2] Sir Bryan Nicholson retired as a Non-Executive Director on 31 December 2005.

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

The Group provided Executive Directors with benefits-in-kind, including medical and death-in-service benefits, and contributed towards their pension arrangements, which are based on defined contributions.

The Group no longer provides Executive Directors with benefits-in-kind.

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 of the Trustees met by the Group in the year ended 31 March 2007 were in respect of the following:

	Year ended 31 March 2007 £	Year ended 31 March 2006 £
Trustees' fees	352,750	220,181
Trustees' legal, professional and other costs and expenses	1,655,384	797,426
Total	2,008,134	1,017,607

The Trustees have proposed that Sir Adam Ridley and Mr RB Spooner should receive fees for additional work in their capacity as Equitas Trustees in relation to the National Indemnity transaction.

Messrs ME McL Deeny and RB Spooner, who are also Directors of the Company, received Trustees' fees of £41,000 and £96,000 respectively for the year ended 31 March 2007 (2006: £41,000 each). They received expenses for secretarial, office and other overheads of £20,151 and £15,205, respectively (2006: £17,696 and £17,977, respectively).

Independent Auditors' report to the members of Equitas Holdings Limited

We have audited the group and parent company financial statements (the ''financial statements'') of Equitas Holdings Limited for the year ended 31 March 2007 which comprise the Group profit and loss account, the Group balance sheet, the Group cash flow statement, the Company balance sheet and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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 Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' report, the Review of the year and the Board report on Directors' remuneration is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the Annual Report, and consider whether it is consistent with the audited financial statements. The other information comprises only the Directors' report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board, except that the scope of our work was limited as explained 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 group's and company's circumstances, consistently applied and adequately disclosed.

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.

However, in respect of claims outstanding of £4,757 million and reinsurers' share of claims outstanding of £4,757 million, the evidence available to us was limited as described in note 1. A comprehensive actuarial review for the year ended 31 March 2007 was not completed as a result of the activity during the year in concluding, on 30 March 2007, a significant reinsurance arrangement with National Indemnity Company. Consequently we have been unable to obtain all the information and explanations which we have considered necessary for our audit regarding the valuation of claims outstanding and reinsurers' share of claims outstanding, nor were we able to carry out other audit procedures.

Claims outstanding and reinsurers' share of claims outstanding are, as discussed in note 2, subject to significant uncertainties. As described in note 1, because of the reinsurance with National Indemnity Company, movements in claims outstanding would only affect the result for the year or net assets if the remaining reinsurance cover becomes exhausted.

In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Qualified opinion arising from limitation of scope

Except for the financial effects of such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the valuation of claims outstanding and reinsurers' share of claims outstanding, in our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the group's and the parent company's affairs as at 31 March 2007 and of the group's deficit and cash flows for the year then ended; and

- the financial statements have been properly prepared in accordance with the Companies Act 1985.

In respect solely of the limitation on our work relating to claims outstanding and reinsurers' share of claims outstanding we have not obtained all the information and explanations that we considered necessary for the purpose of our audit.

In our opinion the information given in the Directors' report is consistent with the financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
7 June 2007

Group profit and loss account
for the year ended 31 March 2007

Technical account – general business

	Note	2007 £m	2007 £m	2006 £m	2006 £m
Gross premiums written	20		**(50)**		-
Outwards reinsurance premiums	4		**(3,661)**		-
Net premiums written			**(3,711)**		-
Investment return transferred from non-technical account			**217**		189
Claims paid					
Gross amount		**(408)**		(744)	
Reinsurers' share		**46**		190	
Net claims paid		**(362)**		(554)	
Change in the provision for claims					
Gross amount		**362**		630	
Reinsurers' share		**4,697**		(209)	
Unwinding of the discount		**(1,614)**		(101)	
Timing of net future payments		**-**		2	
Change in the net provision for claims		**3,445**		322	
Claims incurred, net of reinsurance			**3,083**		(232)
Other income	5		**72**		-
Other technical charges	6		**(17)**		25
Balance on the technical account for general business			**(356)**		(18)

The accounting policies and notes on pages 30 to 43 form an integral part of these financial statements.

Group profit and loss account

for the year ended 31 March 2007

Non-technical account	Note		*2007*		*2006*
	Note	*£m*	*£m*	*£m*	*£m*
Balance on the technical account for general business			**(356)**		**(18)**
Income from financial investments		**182**		194	
Gains on the realisation of investments		**35**		53	
Unrealised losses on investments		**-**		(58)	
Investment return		**217**		189	
Allocated investment return transferred to general business technical account		**(217)**		(189)	
Investment return retained			**-**		**-**
(Deficit) on ordinary activities before tax	*7*		**(356)**		**(18)**
Tax on (deficit) on ordinary activities	*11*		**-**		**-**
(Deficit) for the year	*18*		**(356)**		**(18)**

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 30 to 43 form an integral part of these financial statements.

Group balance sheet
as at 31 March 2007

Assets

	Note	2007 £m	2006 £m
Investments			
Financial investments	12	**162**	4,137
Financial reinsurances	13	**-**	28
		162	4,165
Reinsurers' share of technical provisions			
Claims outstanding	19	**4,757**	360
Debtors			
Debtors arising out of reinsurance operations	15	**-**	264
Other debtors		**-**	7
		-	271
Other assets			
Tangible assets		**-**	1
Cash at bank and in hand		**-**	17
		-	18
Prepayments and accrued income			
Accrued interest		**-**	32
Other prepayments and accrued income	16	**-**	20
		-	52
Total assets		**4,919**	4,866

The accounting policies and notes on pages 30 to 43 form an integral part of these financial statements. The Company's balance sheet is shown on page 28.

Group balance sheet
as at 31 March 2007

Liabilities

	Note	2007 £m	2006 £m
Capital and reserves			
Called up share capital	17	**-**	-
Retained surplus	18	**102**	458
Shareholders' funds – non-equity interests		**102**	458
Technical provisions			
Claims outstanding	19	**4,757**	4,176
Creditors			
Creditors arising out of reinsurance operations	20	**50**	202
Other creditors including taxation and social security		**10**	30
		60	232
Total liabilities		**4,919**	4,866

The financial statements on pages 24 to 43 were approved by the Board on 7 June 2007 and were signed on its behalf by:

HA Stevenson

JV Barker

The accounting policies and notes on pages 30 to 43 form an integral part of these financial statements.

Company balance sheet
as at 31 March 2007

	Note	*2007* £	*2006* £
Investments			
Investments in Group Undertakings	*25*	**200**	300
Financial Investments		**72,000,000**	-
		72,000,200	300
Current assets			
Amounts due from a Group undertaking		**-**	1
Total assets less current liabilities		**72,000,200**	301
Creditors – amounts falling due after more than one year			
Amounts owed to Group undertakings		**200**	200
Net assets		**72,000,000**	101
Capital and reserves			
Called up share capital	*17*	**101**	101
Profit and loss account	*18*	**71,999,899**	-
Shareholders' funds – non-equity interests		**72,000,000**	101

The financial statements on pages 24 to 43 were approved by the Board on 7 June 2007 and were signed on its behalf by:

HA Stevenson

JV Barker

The accounting policies and notes on pages 30 to 43 form an integral part of these financial statements.

Group cash flow statement
for the year ended 31 March 2007

Reconciliation of (deficit) on ordinary activities before tax to net cash outflow from operating activities

	Note	2007 £m	2007 £m	2006 £m	2006 £m
(Deficit) on ordinary activities before tax			**(356)**		(18)
Depreciation of tangible fixed assets	*7*	**1**		1	
(Gain) on disposal of tangible fixed assets	*7*	**-**		(1)	
Exchange losses / (gains), including losses on retranslation of opening balances*		**13**		(24)	
Unrealised losses on investments		**-**		58	
(Increase) / decrease in reinsurers' share of technical provisions - claims outstanding		**(4,435)**		194	
Increase / (decrease) in provision for claims outstanding		**968**		(529)	
Decrease in debtors		**291**		92	
(Decrease)/increase in creditors		**(147)**		77	
			(3,309)		(132)
Net cash outflow from operating activities			**(3,665)**		(150)
Proceeds from disposal of tangible fixed assets			**-**		2
Net cash outflow for the year			**(3,665)**		(148)
Cash flows were (realised)/invested as follows:					
(Decrease)/increase in cash holdings	*22*		**(14)**		11
Net portfolio investment					
Shares and other variable yield securities and units in unit trusts		**(270)**		(26)	
Debt securities and other fixed interest securities		**(3,216)**		25	
Deposits with credit institutions		**(140)**		(151)	
Financial reinsurances		**(25)**		(7)	
			(3,651)		(159)
Net realisation of cash flows	*23*		**(3,665)**		(148)

* The effect of the retranslation of opening balances has been eliminated from all the relevant cash flow categories and is included within these amounts.

The accounting policies and notes on pages 30 to 43 form an integral part of these financial statements.

Notes to the financial statements
for the year ended 31 March 2007

1. Accounting policies

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

Going concern
The financial statements have been prepared on a going concern basis.

Significant uncertainties exist as to the accuracy of the provision for claims outstanding established by Equitas Limited. Adjustments to claims outstanding due to the uncertainties highlighted in note 2 may be material. Because of the terms of the reinsurance agreement with National Indemnity, Equitas is not exposed to movements in claims outstanding provided these remain within the limits of the reinsurance cover purchased. As discussed on page 11 the unexhausted cover is currently substantial.

In view of the financial strength of National Indemnity and the size of the additional reinsurance cover available to the Group following the National Indemnity transaction, in overall terms and relative to the size of the provision for claims outstanding, the Directors have concluded that it continues to be appropriate to prepare the financial statements on a going concern basis.

Basis of presentation
As a result of the activity relating to the transaction with National Indemnity a comprehensive actuarial review was not completed at 31 March 2007. Instead a high level review was undertaken that focused on those aspects of the reserves with the greatest potential for material change. The brought forward reserves were adjusted for any such changes, as well as net payments in the year and the unwinding of the discount.

The level of detail at which the actuarial analysis has been carried out is, in most cases, less than has historically been the case. As a consequence, the accuracy of the estimated changes in liabilities is less reliable than in previous years, when a full actuarial exercise has been carried out. The Directors are satisfied as to the appropriateness of the level of the review that has been conducted because of the significant additional cover now available to the Group.

The financial statements of the Group have been prepared in accordance with the provisions of Section 255A of, and Schedule 9A to, the Companies Act 1985 and with the Statement of Recommended Practice on accounting for insurance business issued by the Association of British Insurers dated December 2005. The balance sheet of the Parent Company has been prepared in accordance with Section 226 of, and Schedule 4 to, the Companies Act 1985.

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards.

Basis of consolidation
The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries from 1 April 2006 to 31 March 2007.

Other important accounting policies

A summary of the more important accounting policies is set out below. The accounting policies have been applied consistently.

(a) Basis of accounting

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.

(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, including those incurred but not reported ('IBNR') at the balance sheet date, 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 and 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.

(c) *The reinsurance contract with National Indemnity*

Both the premium payable to and the corresponding reinsurance cover received from National Indemnity are reported through the technical account.

The transfer of the investment assets matching the liabilities and the loss of future investment income as a result of the reinsurance contract with National Indemnity mean that it is no longer permitted to discount the provision for claims outstanding and related reinsurance recoveries and therefore all remaining discount has been unwound at 31 March 2007. The unwinding of the discount is reported through the technical account and the provision for claims outstanding is reported on an undiscounted basis in the balance sheet.

Reinsurance recoveries on claims outstanding represent the amount recoverable under the reinsurance contract from National Indemnity and equate to the gross claims outstanding at 31 March 2007. The additional cover over and above these reserves provided by the reinsurance agreement is not reported in the balance sheet until such time as it is required.

(d) Discounting

As the reinsured liabilities are not expected to be fully settled for many years, the provisions for claims outstanding and related reinsurance recoveries have been discounted in previous years. The Group had structured its investment portfolio to match its expected net liability stream. Accordingly, the rate of discount applied to those liabilities had been calculated having regard to prospective yields associated with its investment portfolio. The majority of the Group's investments have been transferred to National Indemnity along with the benefit of the associated future investment income. As a result it is no longer permitted to discount the provisions for claims outstanding and related reinsurance recoveries.

(e) Deferred taxation
Provision is made for deferred taxation, using the liability method, on all material timing differences. Deferred tax, which is calculated at the rates at which it is expected that the tax will arise, is recognised in the profit and loss account for the period. Deferred tax balances are not discounted.

(f) Investments
Investments are classified at fair value through the profit and loss account as investments that are held for trading. Listed investments are stated at bid prices quoted by the relevant exchanges. Other investments are stated at bid prices provided by various recognised sources. For short term money market instruments, where market values are not available, fair values have been calculated by discounting expected cash flows at prevailing interest rates at the balance sheet date. The fair value of forward exchange contracts have been determined based on market forward exchange rates at the balance sheet date, where applicable. Purchases and sales of investments are accounted for on a trade date basis.

Securities lent, where substantially all the risks and rewards of ownership remain with the Group, are retained on the balance sheet. Collateral received in respect of securities lent is not recorded in the balance sheet.

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 is reported on an accruals basis and includes realised gains and losses, movements on unrealised gains and losses, net income from securities lent and dividends. Dividends are recorded on the date on which the shares are quoted ex-dividend. The investment return 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 prevailing 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 makes pension contributions on a defined contributions basis on behalf of employees at the direction of the employee concerned. Contributions are charged in the period in which they are incurred.

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

(k) Leases
Operating lease costs are charged in the period in which they are incurred.

2. Estimation techniques and uncertainties

Introduction
The last comprehensive actuarial review was undertaken for the 31 March 2006 report and accounts. These brought forward reserves were adjusted for changes arising from the high level review undertaken at 31 March 2007 as well as net payments in the year and the unwinding of the discount. The estimation techniques described in this section were those adopted for the review at 31 March 2006, with the same principles being applied when evaluating any material adjustments. The core estimation techniques described below are expected to be followed in future years, although the level and frequency of reviews in each area may be reduced in view of the much improved financial position of the Group following the National Indemnity transaction.

Because of the uncertainties inherent in the Group's liabilities, there are many assumptions and estimation techniques described below which individually could have a material impact on the amount of liabilities and the related reinsurance assets. Actual experience will often vary from these assumptions, and any consequential adjustments to amounts previously reported will be reflected in the results of the year in which they are identified. The provision for claims outstanding is based upon actuarial and other studies of the ultimate cost of liabilities including exposure based and statistical estimation techniques.

Significant delays occur in the notification and settlement of certain claims, and a substantial measure of experience and judgment is involved in making the assumptions for 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 related reinsurance recoveries is estimated on the basis of information currently available.

The provision for claims outstanding includes significant amounts in respect of notified and potential IBNR claims for long tail liabilities. The settlement of these claims is not expected to occur for many years, and there is considerable uncertainty as to the amounts at which they will be settled.

Where a claim is disputed, the validity of the claim is ultimately an issue that can only be determined by the courts. The provisions for disputed claims are based on the Group's view as to the expected outcomes of such court decisions.

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.

Asbestos claims
In estimating asbestos liabilities, the Group follows a highly developed actuarial framework. The majority of asbestos reserves is estimated by modelling the expected claims from policyholders of the reinsured syndicates.

The number of future claims is projected for direct policyholders based on past claims experience combined with the results of epidemiological and other relevant studies that predict the incidence of asbestos related diseases into the future. This is then combined with estimates of the average cost of settling different types of claims for each policyholder to give a total value of claims to the relevant underlying policyholders. The results of these projections are then applied to the insurance coverage available for those policyholders, resulting in an estimation of the Group's liabilities arising from claims against those policyholders. The results are then adjusted to take into account liabilities in respect of policyholders that are not modelled explicitly, including an amount for those liabilities of which the Group may be currently unaware.

A similar modelling process is used to estimate asbestos liabilities for the largest inwards reinsurance accounts ceded to the reinsured syndicates, but with the additional step of applying the ceding companies' expected liabilities to the reinsurance cover available. The ceded liabilities that cannot be explicitly modelled are estimated by reference to the current and historical claims experience of the cedants, taking into account cedant specific characteristics where appropriate.

The techniques described above include a number of important assumptions, including:

- the projected level of future valid claims filings for each policyholder by disease type;
- future levels of claims settlement values;
- the impact of bankruptcy of policyholders on the amount and timing of claims payments;
- the legal interpretation of insurance policies and the outcome of litigation, based upon legal advice received; and
- the period between the filing and payment of claims.

The assumptions on the proportion of claims filings that will ultimately lead to claims payments reflect an assessment that the claims management strategies adopted by the Group will reduce claims payments below the level that they would otherwise have been.

Pollution and health hazard claims
Pollution liabilities are estimated for policyholders of the reinsured syndicates by evaluating the expected costs to be incurred by the policyholders in cleaning up polluted sites and then applying these costs to the insurance coverage available. The pollution liabilities expected by means of inwards reinsurance are evaluated in a similar manner, but with the additional step of applying the ceding companies' expected liabilities to the reinsurance cover available.

Allowance is then made for liabilities in respect of policyholders for which either sufficient information is unavailable to carry out the above analysis or which have not yet been identified.

Health hazard liabilities are estimated using similar principles to the above, in that the liabilities of the policyholder are estimated for the majority of reserves and then applied to the insurance coverage.

These evaluation techniques involve a number of important assumptions, including:

- the validity and quantum of the claims potentially faced by the policyholder;
- the legal interpretation of insurance policies and the outcome of litigation, based upon legal advice received; and
- the degree to which potential or unforeseen health hazards may have an effect on the liabilities.

Other claims
The estimation of the majority of other liabilities involves a projection, based upon historical claims experience, of separate homogeneous sub-divisions by underwriting year. The techniques used include calendar year and development year projections, as well as curve-fitting.

Operating expenses
The provision for operating expenses has been transferred to National Indemnity, which is now responsible for current and future operating expenses for as long as the net claims paid by National Indemnity are less than the total cover available.

Reinsurance recoveries
Reinsurance recoveries on claims outstanding represent the reinsurance cover purchased from National Indemnity. The reinsurance agreement with National Indemnity provides cover for all of Equitas Limited's claims liabilities, provided those liabilities are less than the total cover provided and therefore equates to the provision for claims outstanding. Reinsurance recoveries are considered recoverable in full.

3. Segmental information

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

4. Outwards reinsurance premiums

The outwards reinsurance premium relates entirely to the reinsurance agreement completed with National Indemnity. All of the assets of the Group, other than the retained amount of £172 million, have been transferred to National Indemnity and are shown as an outwards reinsurance premium in the Group profit and loss account. In return, National Indemnity has provided reinsurance cover amounting to $13.8 billion at the balance sheet date.

The premium paid can be analysed as follows:

	Group 2007 £m	*Group 2006 £m*
Financial investments and cash	**3,562**	-
Reinsurers' share of technical provisions	**281**	-
Other net debtors	**129**	-
Operating expense reserve	**(311)**	-
	3,661	-

National Indemnity, as part of the transaction, has taken on the staff and operations of Equitas through the acquisition of Equitas Management Services Limited, now re-named Resolute Management Services Limited ('RMSL'). The premium, therefore, includes the transfer of the operating expense liability and the financial investments backing this reserve, to National Indemnity.

The future operating costs of RMSL will be met by National Indemnity for as long as the total claims paid, net of reinsurance recoveries, by National Indemnity is less than the total cover provided.

5. Other Income

The Group received £72 million from the Corporation of Lloyd's as part of the reinsurance transaction with National Indemnity.

6. Other technical charges

Other technical charges relate to foreign exchange movements.

7. Deficit on ordinary activities before tax

The deficit is stated after charging/(crediting):

		Group 2007 £000	*Group 2006 £000*
Depreciation - tangible owned fixed assets		**526**	567
Profit on disposal of tangible fixed assets		**(53)**	(933)
Operating lease rentals incurred	- property	**5,389**	5,784
	- other	**14**	13
Operating lease rentals receivable	- property	**(998)**	(1,185)

Details of related party transactions, as defined by Financial Reporting Standard 8, are given on page 21.

8. Auditors' remuneration

During the year the Group obtained the following services from the Group's auditor at costs as detailed below:

	Group 2007 £000	*Group 2006 £000*
Audit services		
Fees payable to the Company's auditor of the Parent Company and consolidated accounts	**25**	35
Non Audit Services		
Fees payable to the Company's auditor for other services:		
The audit of the Company's subsidiaries, pursuant to legislation	**340**	768
Other services pursuant to legislation, including the audit of the regulatory return,	**35**	45
Other services not covered above	**32**	28
	432	876
Fees in respect of the Equitas Group pension scheme:		
Audit	**12**	11

9. Employees

The monthly average number of persons employed by the Group, including Directors, was 274 for the year ended 31 March 2007 (2006: 347), all of whom were engaged in run-off and related activities.

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

	Group 2007 £000	*Group 2006 £000*
Wages and salaries	**43,129**	28,641
Social security costs	**4,813**	3,096
Other pension costs	**2,956**	4,460
	50,898	36,197

The Group makes pension contributions on a defined contribution basis on behalf of employees at the direction of the employee concerned.

No amount was included in creditors in respect of pension costs (2006: £2 million).

Included within staff costs for the year ended 31 March 2007 is £19.9 million in respect of bonuses awarded on the completion of the reinsurance transaction with National Indemnity.

10. Directors' emoluments

The aggregate remuneration of the Directors was as follows:

		Group 2007 £000	*Group 2006 £000*
Executive Directors	- remuneration	**13,152**	2,679
	- LTIP awards paid	**6,300**	1,245
	- pension costs	**435**	414
Non-Executive Directors	- fees	**396**	444
		20,283	4,782

Full details of the remuneration of, and transactions with, Directors are given in the Board report on Directors' remuneration on page 18.

11. Tax on deficit on ordinary activities

Analysis of charge/(credit) in the year

	Group 2007 £m	*Group 2006 £m*
United Kingdom corporation tax at 30% (2006: 30%)		
Current tax	**-**	-
Deferred tax – origination and reversal of timing differences	**-**	-
	-	-

Factors affecting the tax charge/(credit) for the year

The tax assessed for the year differs from the standard rate of corporation tax in the UK. The differences are explained below:

	Group 2007 £m	*Group 2006 £m*
Deficit on ordinary activities before tax	**(356)**	(18)
Deficit on ordinary activities multiplied by the standard rate of corporation tax in the UK of 30% (2006: 30%)	**(107)**	(5)
Effects of:		
Unrealised losses on revaluation of equity investments	**(1)**	(1)
Unutilised tax losses carried forward	**128**	3
Non taxable income	**(24)**	-
Other permanent differences	**4**	3
Current tax charge/(credit) for the year	**-**	-

There is an unrecognised deferred tax asset of £312 million (2006: £157 million) arising on losses carried forward within the Group, which is not expected to be utilised in the foreseeable future.

12. Investments: financial investments

	Group 2007		Group 2006	
	Market Value £m	Cost £m	Market Value £m	Cost £m
Listed				
Shares and other variable yield securities and units in unit trusts	-	-	283	249
Debt securities and other fixed interest securities	-	-	3,529	3,535
	-	-	3,812	3,784
Unlisted				
Deposits with credit institutions	**162**	**162**	325	325
	162	**162**	4,137	4,109

Further disclosures relating to financial instruments and financial risk management are included in the Directors' report on pages 14 to 15.

The Group received collateral for all securities lent as a condition of the transaction. Included in the above table are lent securities with a market value of £nil (2006: £1,155 million), which were collateralised at over 100 per cent of their value. A further £nil (2006: £10 million) of accrued interest on lent securities, also collateralised at over 100 per cent of their value, was included under other debtors. The total market value of the collateral received was £nil (2006:£1,189 million). A proportion of this collateral was sold and reinvested. The market value of the reinvested collateral was £nil (2006: £936 million). The value of the retained collateral was £nil (2006: £256 million).

Deposits with credit institutions include £70 million (2006: £70 million) that were subject to charge on 31 March 2007.

13. Investments: financial reinsurances

There are no financial reinsurances in the balance sheet at 31 March 2007. In respect of the year ended 31 March 2006 the average prospective rate of return on financial reinsurances was 4.88 per cent per annum, the mean term was four years and the value of the expected receipts from financial reinsurances, before discounting at market yields to recognise the period until receipt, was £35 million.

14. Trust funds

The majority of the Group's liabilities in the United States and Canada were backed by assets held in trust funds. Following the transaction with National Indemnity, the Group no longer has an economic interest in the assets within those trust funds and therefore they are no longer recorded in the Group's balance sheet.

At 31 March 2006 financial investments and cash amounting to £2,078 million were held in trust funds in the United States and Canada. These trust funds were established under the laws of those countries for the settlement of claims relating to those jurisdictions.

The Equitas Australian Trust Fund supports obligations undertaken in Australia. It was financed by a letter of credit, which was secured by a charge over certain sterling denominated financial investments. The Group no longer has an economic interest in the assets supporting the letter of credit. As at 31 March 2006 the value of the letter of credit was A$170 million.

15. Debtors arising out of reinsurance operations

	Group 2007 £m	*Group 2006 £m*
Reinsurance recoveries	**-**	193
Other	**-**	71
	-	264

16. Other prepayments and accrued income

Other prepayments and accrued income do not include any amount due after more than one year (2006: £15 million).

17. Called up share capital

	Company 2007 £	*Company 2006 £*
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 the Company (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. Accordingly, it is 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.

18. Retained surplus

	Company	*Group*
	£m	*£m*
At 1 April 2006	**-**	458
Surplus / (deficit) for the year	**72**	(356)
At 31 March 2007	**72**	**102**

The retained surplus is not distributable by way of dividend.

As permitted by section 230 of the Companies Act 1985, the Company's profit and loss account has not been included in these financial statements. The Company's profit for the financial year was £72 million (2006:£nil).

19. Provision for claims outstanding

	Claims	*Reinsurance*	*Group 2007 Net*	*Claims*	*Reinsurance*	*Group 2006 Net*
	£m	*£m*	*£m*	*£m*	*£m*	*£m*
Provision before discounting	**4,757**	**4,757**	**-**	6,132	533	5,599
Discount	**-**	**-**	**-**	(1,956)	(173)	(1,783)
	4,757	**4,757**	**-**	4,176	360	3,816

(a) Claims and reinsurance recoveries
Claims and reinsurance recoveries are stated after elimination of inter-syndicate transactions.

(b) Discounting
For the year ended 31 March 2007 the balance sheet has been prepared on an undiscounted basis. As a result of the transaction with National Indemnity, the financial investments matching the provision for claims outstanding have been transferred to National Indemnity. The Group will not therefore receive the benefit of the investment income on those assets and so it is no longer permitted to discount the balance sheet.

At 31 March 2006 the provision for claims outstanding, related reinsurance recoveries and the cost of undertaking the run-off were discounted at a rate of 4.30 per cent per annum compound to reflect the time value of money.

(c) Estimation techniques and uncertainties
Details of the estimation techniques employed in the setting of the provision for claims outstanding and the associated uncertainties appear in note 2 on page 33.

20. Creditors arising out of reinsurance operations

Following completion of the reinsurance agreement with National Indemnity, the Group intends to pay an aggregate return premium of £50 million during the year. This is shown as negative gross premiums written in the Technical Account on page 24. The first payments in respect of this amount were made in June 2007. No such provisions existed at 31 March 2006.

The proposal to pay this return premium, subject to completion of the reinsurance agreement and the satisfaction of certain conditions, including the approval of the Board, was communicated to Reinsured Names in December 2006.

All creditors arising out of reinsurance operations are payable within one year.

21. Reconciliation of movements in Group shareholders' funds

	Group 2007 £m	*Group 2006 £m*
Opening shareholders' funds	**458**	476
Deficit for the year (see note 18)	**(356)**	(18)
Closing shareholders' funds	**102**	458

22. Movement in portfolio investments net of financing

	Group 2007 £m	*Group 2006 £m*
(Decrease) / increase in cash holdings	**(14)**	11
Cash transferred to National Indemnity	**145**	-
Net cash inflow for the year (see note 23)	**131**	11
Movement arising from cash flows of portfolio investments	**(234)**	(159)
Changes to market values and discount	**-**	(58)
Cash and investments transferred to National Indemnity	**(3,562)**	-
Other changes, including exchange rate effects (see note 23)	**(354)**	264
Total movement in portfolio investments net of financing	**(4,019)**	58
Opening portfolio investments net of financing (see note 23)	**4,181**	4,123
Closing portfolio investments net of financing (see note 23)	**162**	4,181

23. Movement in cash, portfolio investments and financing

	At 31 March 2006 £m	*Cash flow £m*	*Transfer to National Indemnity £m*	*Other changes, including exchange rate effects £m*	*At 31 March 2007 £m*
Cash at bank and in hand	16	**131**	**(145)**	**(2)**	**-**
Shares and other variable yield securities and units in unit trusts	283	**(4)**	**(266)**	**(13)**	**-**
Debt securities and other fixed interest securities	3,529	**(170)**	**(3,046)**	**(313)**	**-**
Deposits with credit institutions	325	**(59)**	**(81)**	**(23)**	**162**
Financial reinsurances	28	**(1)**	**(24)**	**(3)**	**-**
	4,181	**(103)**	**(3,562)**	**(354)**	**162**

During the year shares and other variable yield securities and units in unit trusts of £13 million (2006: £337 million) were purchased and £17 million (2006: £363 million) were sold. For the same period debt securities and other fixed interest securities of £2,593 million (2006: £4,801 million) were purchased and £2,763 million (2006: £4,776 million) were sold. Cash at bank and in hand as at 31 March 2007 shown above is stated net of £nil (2006: £1 million) of overdrafts.

24. Contingent liabilities and assets

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

The Group had no other contingent liabilities or assets outside the normal course of business at the balance sheet date.

25. 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 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. A return premium of £50 million is payable by Equitas Reinsurance Limited following the completion of the transaction with National Indemnity. The Financial Services Authority has confirmed that it has no objection to this payment.

As part of the reinsurance transaction agreed with National Indemnity, Equitas Management Services Limited was sold to National Indemnity on 30 March 2007 for nominal consideration.

26. Financial commitments

The Group had annual commitments under non-cancellable operating leases in respect of land and buildings, expiring in one year of £nil (2006: £2 million) and expiring in over five years, of £nil (2006: £3 million).

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