

SC 2116

**AVIVA INSURANCE LIMITED**  
**ANNUAL REPORT AND FINANCIAL STATEMENTS**  
**2009**



**Aviva Insurance Limited**  
Annual Report and Financial Statements 2009

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## **Directors' report**

### **Directors**

The directors present their Annual Report and audited Financial Statements for Aviva Insurance Limited ("the Company") for the year ended 31 December 2009.

The current directors, and those in office during the year, are as follows:

M S Hodges  
I M Mayer (resigned 31 December 2009)  
A J Moss  
P Regan (appointed 22 March 2010)  
A Sahay (resigned 31 December 2009)  
P G Scott (resigned 26 January 2010)

### **Company secretary**

K A Cooper

### **Ultimate parent company**

The ultimate parent company is Aviva plc.

### **Auditor**

Ernst & Young LLP  
1 More London Place  
London SE1 2AF

### **Registered office**

Pitheavlis,  
Perth,  
Scotland PH2 0NH

### **Company number**

Registered in Scotland no. SC2116

### **Principal activities**

The Company transacts most classes of general insurance business. The Company also invests in securities, properties and loans. The Company is a member of the Association of British Insurers and is authorised and regulated by the Financial Services Authority.

### **Business review**

This business review is addressed to, and written for, the members of the Company with the aim of providing a fair review of the business development, performance during the financial period and position both at the end of the financial period and at the current time. In providing this review, the aim is to present a view that is both balanced and comprehensive and is consistent with the size and complexity of the business.

### **Objectives and future developments**

High level strategies are determined by Aviva plc and these are shown in its financial statements. The directors consider that the Company's principal activities will continue unchanged into the foreseeable future.

### **Financial key performance indicators**

The directors consider that the Company's key performance indicators ("KPIs") that communicate the financial performance are as follows:

- (Decrease)/increase in net written premiums; and
- Combined operating ratio ("COR") - this comprises the sum of the following ratios:
  - net incurred claims to net earned premiums ratio;
  - net written commissions to net written premiums ratio; and
  - net written expenses to net written premiums ratio

## Directors' report continued

A summary of the KPIs is set out below:

Measure	2009	2008
(Decrease)/increase in net written premiums	(21.1)%	2.5%
Combined operating ratio	104%	87%
Net incurred claims ratio	59.5%	40.9%
Net written commissions ratio	30.9%	34.2%
Net written expenses ratio	13.1%	11.8%

The net incurred claims ratio excludes costs of exceptional strengthening latent claims of £nil (2008: £166 million), net of discount and reinsurance.

The written expense ratio excludes corporate costs of £55 million (2008: £50 million), of which £40 million (2008: £48 million) relates to restructuring costs.

### Financial position and performance

The financial position of the Company at 31 December 2009 is shown in the statement of financial position on page 17, with the trading results shown in the income statement on page 15 and the statement of cash flows on page 19.

The Company's ultimate holding company, Aviva plc, has stated its intention to meet or beat a COR of 98% across the cycle. The Company is seeking to support Aviva plc in meeting this target.

Profit/loss before tax decreased from a £1,174 million profit in 2008 to £1,121 million loss in 2009. The loss in the current year is primarily due to an impairment of the Company's investment in its direct subsidiary, Aviva International Holdings Limited.

The net written premiums of the Company arise primarily from the sale of small to medium enterprise commercial lines insurance. The Company's underwriting result reflects continuing tough market conditions and a focus on sustainable profitability rather than on volume. Despite the action taken to exit unprofitable business, in the second half of 2009 the Company has seen some encouraging signs for business volumes.

In commercial lines, whilst the trend is for rates to continue to move up, achieving desired rate increases is difficult in a highly competitive market. The Company has achieved overall increases of 4% (2008: 3%) and continues to adopt a pricing policy that is sufficiently flexible to ensure that it retains attractive existing business.

Commission costs have decreased relative to net written premiums, reflecting the Company's work to reshape the book so that the business written through brokers and partners is on sustainably profitable terms, as well as a reduction in creditor business.

Investment income decreased in 2009 to £698 million (2008: £1,204 million) reflecting realised and unrealised losses on investments.

### Principal risks and uncertainties

A description of the principal risks and uncertainties facing the Company and the Company's risk management policies are set out in note 28 to the financial statements.

Risk factors beyond the Company's control, that could cause actual results to differ materially from those estimated include, but are not limited to:

- Frequency and severity of significant natural hazards
- UK domestic economic business conditions; and
- The impact of competition, inflation and deflation.

## **Directors' report continued**

### **Going concern**

The Company's business activities, together with the factors likely to affect its future development, performance and position including the Business review, are set out in this report. In addition, the financial statements include notes on the contingent liabilities and other risk factors (note 24); its capital structure (note 27); management of its major risks including market, credit and liquidity risk (note 28); and derivative financial instruments (note 29).

The Company and its ultimate holding company Aviva plc have considerable financial resources together with a diversified business model, with a spread of businesses and geographical reach. As a consequence, the directors believe that the Company is well placed to manage its business risks successfully despite the current uncertain economic outlook. After making enquiries, the directors have a reasonable expectation that the Company and its subsidiaries as a whole have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

The directors, having assessed the responses of the directors of the Company's parent, Aviva International Insurance Limited, have no reason to believe that a material uncertainty exists that may cast significant doubt about the ability to continue with the current banking arrangements.

### **Overseas branches**

The Company has branch offices outside the UK in Guernsey, Jersey, Hong Kong, Ireland, Malta, Bahamas, Cyprus and France.

### **Dividends**

The directors declared an interim dividend of £900 million (2008: £1,000 million) during the year. The directors do not recommend the payment of a final dividend (2008: £nil).

### **Financial instruments**

The business of the Company includes use of financial instruments. Details of the Company's risk management objectives and policies and exposure to risk relating to financial instruments are set out in note 28 to the financial statements.

### **Directors' interests**

None of the directors who held office at 31 December 2009 had any interest in the Company's shares.

### **Auditors and the disclosure of information to the auditor**

Each person who was a director of the Company on the date that this report was approved, confirms that so far as the director is aware, there is no relevant audit information of which the auditor is unaware. Each director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the auditor is aware of that information.

It is the intention of the directors to reappoint the auditor under the deemed appointment rules of Section 487 of the Companies Act 2006.

### **Directors' liabilities**

Aviva plc, the ultimate parent company, has granted an indemnity to the directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 1985. This indemnity was granted in 2004 and the provisions in the Company's Articles of Association constitute "qualifying third party indemnities" for the purposes of sections 309A to 309C of the Companies Act 1985. These qualifying third party indemnity provisions remain in force as at the date of approving the Directors' report by virtue of the transitional procedures of the Companies Act 2006.

## **Directors' report continued**

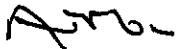
### **Statement of directors' responsibilities**

The directors are required to prepare the financial statements for each accounting period that comply with the relevant provisions of the Companies Act 2006 and International Financial Reporting Standards ("IFRS") as adopted by the European Union, and which present fairly the financial position, financial performance and cash flows of the Company at the end of the accounting period. A fair presentation of financial statements in accordance with IFRS requires the directors to:

- select suitable accounting policies and verify they are applied consistently in preparing the financial statements, on a going concern basis unless it is inappropriate to presume that the Company will continue in business;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance; and
- state that the Company has complied with applicable IFRS, subject to any material departures disclosed and explained in the annual report and audited financial statements.

The directors are responsible for maintaining proper accounting records which are intended to disclose with reasonable accuracy, at any time, the financial position of the Company. They are also ultimately responsible for the systems of internal control maintained for safeguarding the assets of the Company and for the prevention and detection of fraud and other irregularities.

By order of the Board



A J Moss

Director

25 March 2010  
Registered Office: Pitheavlis,  
Perth, Scotland PH2 0NH  
Registered in Scotland No. SC2116

## **Independent auditor's report**

### **To the members of Aviva Insurance Limited**

We have audited the Company's financial statements for the year ended 31 December 2009, which comprise the Accounting Policies, the Income Statement, the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows, and the related notes 1 to 30. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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

#### **Respective responsibilities of directors and auditors**

As explained more fully in the Statement of Directors' Responsibilities set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

#### **Opinion on financial statements**

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2009 and of its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

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

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

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

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

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



Michael Purrington (Senior Statutory Auditor)  
For and on behalf of Ernst & Young LLP (Statutory Auditor)  
London  
26 March 2010

## Accounting policies

The Company is a limited liability company incorporated and domiciled in the United Kingdom ("UK"). Its principal activity is the transaction of long-term and most classes of general insurance and health business through its subsidiaries, agencies and branches in the UK, Continental Europe, North America, Asia and other countries throughout the world. The Company also invests in securities, properties, mortgages and loans and carries on the business of trading in property.

The principal accounting policies adopted in the preparation of these financial statements are set out below.

### (A) Basis of presentation

The Company is exempt from preparing group financial statements by virtue of section 400 of the Companies Act 2006, as it is a subsidiary of an EEA parent. The Company is included in consolidated financial statements for the Aviva Group at the same date, as established under the law of an EEA state, and is therefore exempt from preparing consolidated financial statements. These financial statements therefore present information about the Company as an individual entity.

In 2009, the IASB issued IFRS 9, *Financial Instruments – Classification and Measurement*, the first part of a replacement standard for IAS 39, *Financial Instruments: Recognition and Measurement*. This is applicable prospectively for accounting periods commencing 1 January 2013 or later, and is therefore not applicable for the current accounting period. It has not yet been endorsed by the EU but, on adoption, will require us to review the classification of certain investments while allowing us to retain the fair value measurement option as we deem necessary.

During 2008 and 2009, the IASB also issued amendments to IFRS 1, *First Time Adoption of IFRS*, IAS 32, *Financial Instruments: Presentation*, IAS 39 and the results of its annual improvements project. Further amendments to IFRS 1, IFRS 2, *Share-Based Payment*, IAS 24, *Related Party Disclosures*, and the results of its second annual improvements project have been issued but have not yet been endorsed by the EU. These are applicable prospectively for accounting periods commencing 1 July 2009 or later, and are therefore not applicable for the current accounting period. On adoption, they will not have any material impact on the Company's financial reporting.

In accordance with IFRS 4, *Insurance Contracts*, the Company has applied existing accounting practices for insurance and participating investment contracts, modified as appropriate to comply with the IFRS framework and applicable standards. Further details are given in policy E below.

### (B) Critical accounting policies and the use of estimates

The preparation of financial statements requires the Company to select accounting policies and make estimates and assumptions that affect items reported in the income statement, statement of financial position, other primary statements and notes to the financial statements.

#### **Critical accounting policies**

The major areas of judgement on policy application are considered to be on product classification (set out in policy E), in insurance contract liabilities (set out in policy I) and in the classification of financial investments (set out in policy N).

#### **Use of estimates**

All estimates are based on management's knowledge of current facts and circumstances, assumptions based on that knowledge and their predictions of future events and actions. Actual results can always differ from those estimates, possibly significantly.

The table below sets out those items we consider particularly susceptible to changes in estimates and assumptions, and the relevant accounting policy.

Item	Accounting policy
Fair value of investments in subsidiaries	C
Insurance contract liabilities	I
Impairment of financial investments	N
Fair value of derivative financial instruments	O
Deferred acquisition costs	R
Provisions and contingent liabilities	U
Deferred income taxes	V

## **Accounting policies continued**

### **(C) Subsidiaries**

Subsidiaries are those entities (including special purpose entities) in which the Company, directly or indirectly, has power to exercise control over financial and operating policies in order to gain economic benefits.

In the statement of financial position, subsidiaries are stated at their fair values, estimated using applicable valuation models underpinned by Aviva plc's market capitalisation. These investments are classified as available for sale (AFS) financial assets, with changes in their fair value being recorded in a separate investment valuation reserve within equity.

Where the cumulative changes recognised in equity represent an unrealised loss, the investments are reviewed to test whether an impairment exists. Where there is objective evidence that such an asset is impaired, such as the financial difficulty of the entity or a prolonged decline in its fair value below cost, the unrealised loss recorded in equity is reclassified and charged to the income statement.

### **(D) Foreign currency transaction**

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions, and from the translation of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement.

Translation differences on debt securities and other monetary financial assets measured at fair value and designated as held at fair value through profit and loss (FV) (see policy N) are included in foreign exchange gains and losses in the income statement. Translation differences on non-monetary items, such as equities which are designated as FV, are reported as part of the fair value gain or loss, whereas such differences on AFS equities are included in the investment valuation reserve.

### **(E) Product classification**

Insurance or service contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause an insurer to make significant additional payments in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. Contracts can be reclassified as insurance contracts after inception if insurance risk becomes significant. Any contracts not considered to be insurance contracts under IFRS are classified as investment contracts.

Some insurance and investment contracts contain a discretionary participating feature, which is a contractual right to receive additional benefits as a supplement to guaranteed benefits. These are referred to as participating contracts.

As noted in policy A above, insurance contracts in general continue to be measured and accounted for under existing accounting practices at the later of the date of transition to IFRS or the date of the acquisition of the entity, in accordance with IFRS 4. Accounting for insurance contracts is determined in accordance with the Statement of Recommended Practice issued by the Association of British Insurers, the most recent version of which was issued in December 2005, and amended in December 2006. In certain businesses, the accounting policies or accounting estimates have been changed, as permitted by IFRS 4 and IAS 8 respectively, to remeasure designated insurance liabilities to reflect current market interest rates and changes to regulatory capital requirements. When accounting policies or accounting estimates have been changed and adjustments to the measurement basis have occurred then the financial statements of that year will have disclosed the impacts accordingly.

### **(F) Premiums earned**

Premiums written reflect business incepted during the year, and exclude any sales-based taxes or duties or levies. Written premiums include an estimate of pipeline premiums less a provision for anticipated lapses. Unearned premiums are those proportions of the premiums written in a year that relate to periods of risk after the statement of financial position date. Premiums collected by intermediaries, but not yet received, are assessed based on estimates from underwriting or past experience, and are included in premiums written.

### **(G) Fee and commission income**

Fee and commission income consists primarily of reinsurance commissions receivable, which are deferred in the same way as acquisition costs as described in policy R. All other fee and commission income is recognised as the services are provided.

## Accounting policies continued

### (H) Net investment income

Investment income consists of dividends, interest and rents receivable for the year, movements in amortised cost on debt securities, realised gains and losses, and unrealised gains and losses on FV investments (as defined in policy N). Dividends on equity securities are recorded as revenue on the ex-dividend date. Interest income is recognised as it accrues, taking into account the effective yield on the investment. Rental income is recognised on an accruals basis.

The realised gain or loss on disposal of an investment is the difference between the proceeds received, net of transaction costs, and its original cost or amortised cost as appropriate. Unrealised gains and losses, arising on investments which have not been derecognised as a result of disposal or transfer, represent the difference between the carrying value at the year end and the carrying value at the previous year end or purchase value during the year, less the reversal of previously recognised unrealised gains and losses in respect of disposals made during the year.

### (I) Insurance contract liabilities

#### *Claims*

General insurance and health claims incurred include all losses occurring during the year, whether reported or not, related handling costs, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years.

Claims handling costs include internal and external costs incurred in connection with the negotiation and settlement of claims. Internal costs include all direct expenses of the claims department and any part of the general administrative costs directly attributable to the claims function.

#### *Insurance provisions*

##### *(i) Outstanding claims provisions*

Insurance outstanding claims provisions are based on the estimated ultimate cost of all claims incurred but not settled at the statement of financial position date, whether reported or not, together with related claims handling costs. Significant delays are experienced in the notification and settlement of certain types of general insurance claims, particularly in respect of liability business, including environmental and pollution exposures, the ultimate cost of which cannot be known with certainty at the statement of financial position date. Any estimate represents a determination within a range of possible outcomes. Further details of estimation techniques are given in note 18.

Provisions for latent claims are discounted, using rates based on the relevant swap curve, in the relevant currency at the reporting date, having regard to the expected settlement dates of the claims. The discount rate is set at the start of the accounting period with any change in rates between the start and end of the accounting period being reflected as a change in insurance liabilities. The range of discount rates used is described in note 18.

Outstanding claims provisions are valued net of an allowance for expected future recoveries. Recoveries include non-insurance assets that have been acquired by exercising rights to salvage and subrogation under the terms of insurance contracts.

##### *(ii) Provision for unearned premiums*

The proportion of written premiums, gross of commission payable to intermediaries, attributable to subsequent periods is deferred as a provision for unearned premiums. The change in this provision is taken to the income statement as recognition of revenue over the period of risk.

##### *(iii) Liability adequacy*

At each reporting date, the Company reviews its unexpired risks and carries out a liability adequacy test for any overall excess of expected claims and deferred acquisition costs over unearned premiums, using the current estimates of future cash flows under its contracts after taking account of the investment return expected to arise on assets relating to the relevant general business provisions. If these estimates show that the carrying amount of its insurance liabilities (less related deferred acquisition costs) is insufficient in light of the estimated future cash flows, the deficiency is recognised in the income statement by setting up a provision in the statement of financial position.

#### *Other assessments and levies*

The Company is subject to various periodic insurance-related assessments or guarantee fund levies. Related provisions are established where there is a present obligation (legal or constructive) as a result of a past event. Such amounts are not included within insurance liabilities but are included under "Provisions" in the statement of financial position.

## **Accounting policies continued**

### **(J) Reinsurance**

The Company assumes and cedes reinsurance in the normal course of business, with retention limits varying by line of business. Premiums on reinsurance assumed are recognised as revenue in the same manner as they would be if the reinsurance were considered direct business, taking into account the product classification of the reinsured business. The cost of reinsurance related to long-duration contracts is accounted for over the life of the underlying reinsured policies, using assumptions consistent with those used to account for these policies.

Where general insurance liabilities are discounted, any corresponding reinsurance assets are also discounted using consistent assumptions.

Gains or losses on buying retroactive reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised. Premiums ceded and claims reimbursed are presented on a gross basis in the income statement and statement of financial position as appropriate.

Reinsurance assets primarily include balances due from reinsurance companies for ceded insurance liabilities. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provisions or settled claims associated with the reinsured policies and in accordance with the relevant reinsurance contract.

Reinsurance contracts that principally transfer financial risk are accounted for directly through the statement of financial position and are not included in reinsurance assets or liabilities. A deposit asset or liability is recognised, based on the consideration paid or received less any explicitly identified premiums or fees to be retained by the reinsured.

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

### **(K) Property and equipment**

Owner-occupied properties are carried at their revalued amounts, which are supported by market evidence, and movements are taken to a separate reserve within equity. When such properties are sold, the accumulated revaluation surpluses are transferred from this reserve to retained earnings. These properties are depreciated down to their estimated residual values over their useful lives. All other items classed as property and equipment within the statement of financial position are carried at historical cost less accumulated depreciation.

Depreciation is calculated on the straight-line method to write down the cost of other assets to their residual values over their estimated useful lives of three to five years. Land is not depreciated. The assets' residual values, useful lives and method of depreciation are reviewed regularly, and at least at each financial year end, and adjusted if appropriate.

Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal of property and equipment are determined by reference to their carrying amount.

Until 1 January 2009, borrowing costs directly attributable to the acquisition and construction of property and equipment were expensed as incurred. With effect from 1 January 2009, such costs are capitalised. All repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the most recently assessed standard of performance of existing asset will flow to the Company and the renovation replaces an identifiable part of the asset. Major renovations are depreciated over the remaining useful life of the related asset.

### **(L) Impairment of non-financial assets**

Property and equipment and other non-financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows.

## **Accounting policies continued**

### **(M) Derecognition and offset of financial assets and financial liabilities**

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- The rights to receive cash flows from the asset have expired;
- The Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- The Company has transferred its rights to receive cash flows from the asset and either transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

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

### **(N) Financial investments**

The Company classifies its investments as either financial assets at fair value through profit or loss (FV) or financial assets available for sale (AFS). The classification depends on the purpose for which the investments were acquired, and is determined by management at initial recognition. The FV category has two sub-categories – those that meet the definition as being held for trading and those the Company chooses to designate as FV (referred to in this accounting policy as "other than trading").

With the exception of investments in subsidiaries, the FV category is used as the Company's investment or risk management strategy is to manage its financial investments on a fair value basis. All securities in the FV category are classified as other than trading.

Purchases and sales of investments are recognised on the trade date, which is the date that the Company commits to purchase or sell the assets, at their fair values less transaction costs. Debt securities are initially recorded at their fair value which is taken to be amortised cost, with amortisation credited or charged to the income statement. Investments classified as other than trading are subsequently carried at fair value. Changes in the fair value of these investments are included in the income statement in the period in which they arise.

Fair value for listed equity securities are based on quoted bid prices or amounts derived from cash flow models. Fair values for unlisted equity securities are estimated using applicable price/earnings or price/cash flow ratios refined to reflect the specific circumstances of the issuer. Equity securities for which fair values cannot be measured reliably are recognised at cost less impairment.

Financial guarantees are recognised initially at their fair value and are subsequently amortised over the duration of the contract. A liability is recognised for amounts payable under the guarantee if it is more likely than not that the guarantee will be called upon.

#### ***Impairment***

The Company reviews the carrying value of its investments on a regular basis. If the carrying value of an investment is greater than the recoverable amount, the carrying value is reduced through a charge to the income statement in the period of impairment.

## Accounting policies continued

### (O) Derivative financial instruments and hedging

Derivative financial instruments are foreign exchange contracts that derive their value mainly from underlying foreign exchange rates. All derivatives are initially recognised in the statement of financial position at their fair value, which usually represents their cost. They are subsequently re-measured at their fair value, with the method of recognising movements in this value depending on whether they are designated as hedging instruments and, if so, the nature of the item being hedged. Fair values are obtained from quoted market prices or, if these are not available, by using valuation techniques such as discounted cash flow models or option pricing models. All derivatives are carried as assets when the fair values are positive and as liabilities when the fair values are negative. Premiums paid for derivatives are recorded as an asset on the statement of financial position at the date of purchase, representing their fair value at that date.

Derivative contracts may be traded on an exchange or over-the-counter ("OTC"). Exchange-traded derivatives are standardised and include certain futures and option contracts. OTC derivative contracts are individually negotiated between contracting parties and include forwards, swaps, caps and floors. Derivatives are subject to various risks including market, liquidity and credit risk, similar to those related to the underlying financial instruments.

The notional or contractual amounts associated with derivative financial instruments are not recorded as assets or liabilities on the statement of financial position as they do not represent the fair value of these transactions. These amounts are disclosed in note 29.

#### **Currency swaps**

Currency swaps, in their simplest form, are contractual agreements that involve the exchange of both periodic and final amounts in two different currencies. Exposure to gain or loss on both types of swap contracts will increase or decrease over their respective lives as a function of maturity dates, interest and foreign exchange rates, and the timing of payments.

#### **Foreign exchange contracts**

Foreign exchange contracts, which include spot, forward and futures contracts, represent agreements to exchange the currency of one country for the currency of another country at an agreed price and settlement date. Foreign exchange option contracts are similar to interest rate option contracts, except that they are based on currencies, rather than interest rates. Exposure to gain or loss on these contracts will increase or decrease over their respective lives as currency exchange and interest rates fluctuate.

For a variety of reasons, the above derivative transactions, while providing effective economic hedges under the Company's risk management positions, do not qualify for hedge accounting under the specific IFRS rules and are therefore treated as derivatives held for trading. Their fair value gains and losses are recognised immediately in other trading income.

### **(P) Loans**

Loans with fixed maturities, including mortgage loans on investment property and collateral loans, are recognised when cash is advanced to borrowers. The majority of these loans are carried at their unpaid principal balances and adjusted for amortisation of premium or discount, non-refundable loan fees and related direct costs. These amounts are deferred and amortised over the life of the loan as an adjustment to loan yield using the effective interest rate method.

To the extent that a loan is considered to be uncollectable, it is written off as impaired through the income statement. Any subsequent recoveries are credited to the income statement.

### **(Q) Collateral**

The Company receives and pledges collateral in the form of cash or non-cash assets in respect of stock lending transactions, as well as certain derivative contracts and loans in order to reduce the credit risk of these transactions. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty.

Collateral received in the form of cash, which is not legally segregated from the Company, is recognised as an asset on the statement of financial position with a corresponding liability for the repayment. Non-cash collateral received is not recognised on the statement of financial position unless the Company either sells or repledges these assets in the absence of default, at which point the obligation to return this collateral is recognised as a liability.

Collateral pledged in the form of cash, which is legally segregated from the Company, is derecognised from the statement of financial position with a corresponding receivable for its return. Non-cash collateral pledged is not derecognised from the statement of financial position unless the Company defaults on its obligations under the relevant agreement, and therefore continues to be recognised on the statement of financial position within the appropriate asset classification.

## **Accounting policies continued**

### **(R) Deferred acquisition costs**

The costs directly attributable to the acquisition of new business for insurance contracts are deferred to the extent that they are expected to be recoverable out of future margins in revenues on these contracts.

Where such business is reinsured, an appropriate proportion of the deferred acquisition costs is attributed to the reinsurer, and is treated as a separate liability.

Deferred acquisition costs are amortised over the period in which the related revenues are earned. The reinsurers' share of deferred acquisition costs is amortised in the same manner as the underlying asset.

Deferred acquisition costs are reviewed by category of business at the end of each reporting period and are written off where they are no longer considered to be recoverable.

### **(S) Statement of cash flows**

#### ***Cash and cash equivalents***

Cash and cash equivalents consist of cash at banks and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are those with less than three months' maturity from the date of acquisition, or which are redeemable on demand with only an insignificant change in their fair values.

For the purposes of the statement of cash flows, cash and cash equivalents also include bank overdrafts, which are included within payables and other financial liabilities on the statement of financial position.

#### ***Operating cash flows***

Purchases and sales of investment property, loans and financial investments are included within operating cash flows as the purchases are funded from cash flows associated with the origination of insurance and investment contracts, net of payments of related benefits and claims.

### **(T) Leases**

Leases, where a significant portion of the risks and rewards of ownership is retained by the lessor, are classified as operating leases. Assets held for use in such leases are included in property and equipment, and are depreciated to their residual values over their estimate useful lives. Rentals from such leases are credited to the income statement on a straight-line basis over the period of the relevant leases. Payments made as lessee under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the relevant leases.

### **(U) Provisions and contingent liabilities**

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Where the Company expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is more probable than not.

The Company recognises a provision for onerous contracts when the expected benefits to be derived from a contract are less than the unavoidable costs of meeting the obligations under the contract.

Contingent liabilities are disclosed if there is a possible future obligation as a result of a past event, or if there is a present obligation as a result of a past event but either a payment is not probable or the amount cannot be reasonably estimated.

### **(V) Income taxes**

The current tax expense is based on the taxable profits for the year, after any adjustments in respect of prior years. Tax, including tax relief for losses if applicable, is allocated over profits before taxation and amounts charged or credited to reserves as appropriate.

Provision is made for deferred tax liabilities, or credit taken for deferred tax assets, using the liability method, on all material temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements.

The principal temporary differences arise from the equalisation provision, and the trading and capital losses. The rates enacted or substantively enacted at the statement of financial position date are used to determine the deferred tax.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

## **Accounting policies continued**

### **(V) Income taxes continued**

Deferred tax is not provided on revaluations of investments in subsidiaries as under current tax legislation no tax is expected to arise on their disposal.

### **(W) Dividends**

Interim dividends on ordinary shares are recognised in equity in the period in which they are paid. Final dividends on these shares are recognised when they have been approved by shareholders.

### **(X) Equalisation provision**

Equalisation provisions are established in accordance with UK company law. These provisions are in addition to the provisions required to meet the anticipated ultimate cost of settlement of outstanding claims at the statement of financial position date. Under IFRS, the provisions are not reported in the statement of financial position as no liability exists but are presented within retained earnings, net of attributable tax relief.

**Income statement**  
**For the year ended 31 December 2009**

	Note	2009 £m	2008 £m
<b>Income</b>	2		
Gross written premiums		1,296	1,563
Premiums ceded to reinsurers		(142)	(101)
Premiums written net of reinsurance		1,154	1,462
Net change in provision for unearned premiums		131	38
Net earned premiums	F	1,285	1,500
Fee and commission income	G	8	(24)
Net investment income	H	698	1,204
Profit on the disposal of subsidiaries		88	-
		2,079	2,680
<b>Expenses</b>	3		
Claims paid, net of recoveries from reinsurers		(801)	(817)
Change in insurance liabilities, net of reinsurance		37	38
Fee and commission expense		(513)	(594)
Other expenses		(1,918)	(131)
Finance costs		(5)	(2)
		(3,200)	(1,506)
<b>(Loss)/profit before tax</b>		(1,121)	1,174
Tax credit/(expense)	V&6	65	(66)
<b>(Loss)/profit for the year</b>		(1,056)	1,108

The accounting policies (identified alphabetically) on pages 7 to 14 and notes (identified numerically) on pages 20 to 50 are an integral part of these financial statements.

**Statement of comprehensive income**  
For the year ended 31 December 2009

	Note	2009 £m	2008 £m
<b>(Loss)/profit for the year</b>		<b>(1,056)</b>	1,108
<b>Other comprehensive income</b>			
Subsidiaries			
Fair value gains transferred to profit on disposal	C&2	(88)	-
Fair value gains/(losses) on investments in subsidiaries	C,8(a)&15	171	(3,152)
Impairment losses on investments previously revalued through other comprehensive income, now taken to the income statement	C,3&15 V&6(b)	1,808	- 1
Aggregate tax effect		4	-
Foreign exchange rate movements on overseas branches			
Other comprehensive income, net of tax		1,895	(3,151)
<b>Total comprehensive income for the year</b>		<b>839</b>	(2,043)

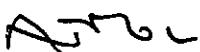
The accounting policies (identified alphabetically) on pages 7 to 14 and notes (identified numerically) on pages 20 to 50 are an integral part of these financial statements.

## **Statement of financial position**

### **As at 31 December 2009**

	Note	2009 £m	2008 £m
<b>Assets</b>			
Investments in subsidiaries	C&8	11,424	10,859
Property and equipment	K&9	3	3
Loans	P	-	12
Financial investments	M,N,O,Q &10	553	668
Reinsurance assets	J,17&19	242	340
Receivables and other financial assets	12	5,018	5,648
Deferred acquisition costs and other assets	R&13	365	492
Current tax asset	V&20	40	-
Group relief asset	V&20	-	170
Cash and cash equivalents	S&26	103	61
<b>Total assets</b>		<b>17,748</b>	<b>18,253</b>
<b>Equity</b>			
Capital			
Ordinary share capital	14	7,584	6,988
Capital reserves			
Share premium	14	3,049	3,049
Other reserves	15	65	(1,826)
Retained earnings	16	3,976	5,928
<b>Total equity</b>		<b>14,674</b>	<b>14,139</b>
<b>Liabilities</b>			
Gross insurance liabilities	I&18	2,468	2,731
Provisions	U&21	17	29
Deferred tax liabilities	V&20	-	17
Current tax liabilities	V&20	-	83
Group relief liability	V&20	58	-
Payables and other financial liabilities	M&22	329	981
Other liabilities	23	202	273
<b>Total liabilities</b>		<b>3,074</b>	<b>4,114</b>
<b>Total equity and liabilities</b>		<b>17,748</b>	<b>18,253</b>

Approved by the Board on 25 March 2010



**Andrew Moss**  
Director

The accounting policies (identified alphabetically) on pages 7 to 14 and notes (identified numerically) on pages 20 to 50 are an integral part of these financial statements.

**Statement of changes in equity**  
 For the year ended 31 December 2009

	Ordinary share capital	Share premium	Owner- occupied properties reserve	Investment valuation reserve	Special reserve	Retained earnings	Total equity
	£m	£m	£m	£m	£m	£m	£m
<b>Balance at 1 January 2008</b>	6,988	3,049	2	1,212	111	5,820	17,182
Profit for the year	-	-	-	-	-	1,108	1,108
Other comprehensive income	-	-	1	(3,152)	-	-	(3,151)
Total comprehensive income for the year	-	-	1	(3,152)	-	1,108	(2,043)
Dividends	-	-	-	-	-	(1,000)	(1,000)
<b>Balance at 31 December 2008</b>	6,988	3,049	3	(1,940)	111	5,928	14,139
Loss for the year	-	-	-	-	-	(1,056)	(1,056)
Other comprehensive income	-	-	-	1,891	-	4	1,895
Total comprehensive income for the year	-	-	-	1,891	-	(1,052)	839
Dividends	-	-	-	-	-	(900)	(900)
Shares issued	596	-	-	-	-	-	596
<b>Balance at 31 December 2009</b>	<b>7,584</b>	<b>3,049</b>	<b>3</b>	<b>(49)</b>	<b>111</b>	<b>3,976</b>	<b>14,674</b>

The accounting policies (identified alphabetically) on pages 7 to 14 and notes (identified numerically) on pages 20 to 50 are an integral part of these financial statements.

**Statement of cash flows**  
For the year ended 31 December 2009

	Note	2009 £m	2008 £m
<b>Cash flows from operating activities</b>			
Cash generated from/(used in) operations	26(a)	34	(169)
<b>Net cash generated from/(used in) operating activities</b>		<b>34</b>	<b>(169)</b>
<b>Cash flows from investing activities</b>			
Proceeds on sale of property and equipment		-	9
<b>Net cash from investing activities</b>		<b>-</b>	<b>9</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>34</b>	<b>(160)</b>
Cash and cash equivalents at 1 January		34	194
Effect of exchange rate changes on cash and cash equivalents		(1)	-
<b>Cash and cash equivalents at 31 December</b>	26(b)	<b>67</b>	<b>34</b>

The accounting policies (identified alphabetically) on pages 7 to 14 and notes (identified numerically) on pages 20 to 50 are an integral part of these financial statements.

## Notes to the financial statements

### 1. Presentation changes

(a) The Company has adopted IAS 1 (Revised), *Presentation of Financial Statements*, as at 1 January 2009. The principal effect of this has been in presentation of the financial statements, in the following areas:

(i) The titles of some of the prime statements have changed, so that the statement of recognised income and expense is now called the statement of comprehensive income; the reconciliation of movements in shareholder's equity is now called the statement of changes in equity; the balance sheet is now called the statement of financial position; and the cash flow statement is now called the statement of cash flows.

(ii) The standard requires the income tax effect of each component of comprehensive income to be disclosed. This information is given in note 6(b).

(iii) Changes in the year in each element of equity must now be shown on the face of the statement of changes in equity, rather than in the notes.

(b) The Company has also adopted Amendments to IFRS 7, *Improving Disclosures about Financial Instruments*, as of 1 January 2009. The principal impact of these amendments is to require the following additional disclosures:

(i) An analysis of financial assets and liabilities carried at fair value using a fair value hierarchy that reflects the significance of inputs used in making the fair value measurements;

(ii) An analysis of transfers of financial assets and liabilities between different levels of the fair value hierarchy;

(iii) A reconciliation from beginning to end of period of financial assets and liabilities whose fair value is based on unobservable inputs; and

(iv) An enhanced discussion and analysis of liquidity risk, including a maturity analysis of financial assets held for managing liquidity risk, if that information is necessary to enable users of its financial statements to evaluate the nature and extent of liquidity risk.

Comparative information for the disclosures required by the IFRS 7 amendments is not needed in the first year of application. However, the Company has provided comparatives for the analysis of financial assets according to a fair value hierarchy.

## Notes to the financial statements continued

### 2. Details of income

	Note	2009 £m	2008 £m
<b>Gross written premiums</b>		<b>1,296</b>	<b>1,563</b>
Less: premiums ceded to reinsurers		(142)	(101)
Gross change in provision for unearned premiums	18(d)	189	124
Reinsurers' share of change in provision for unearned premiums	19(c)(ii)	(58)	(86)
<b>Net change in provision for unearned premiums</b>		<b>131</b>	<b>38</b>
<b>Net earned premiums</b>		<b>1,285</b>	<b>1,500</b>
Fee and commission income			
Reinsurance commissions receivable		8	(23)
Net change in deferred revenue		-	(1)
		8	(24)
<b>Total revenue</b>		<b>1,293</b>	<b>1,476</b>
<b>Net investment income</b>			
Interest and similar income			
From investments designated as trading and other than trading		28	60
Dividend income		909	908
Other income from investments designated as trading			
Realised losses (note 29)		(227)	-
Unrealised losses (note 29)		(38)	-
		(265)	-
Other income from investments designated as other than trading			
Realised losses		(46)	(24)
Unrealised gains		75	261
		29	237
<b>Other investment expenses</b>		<b>(3)</b>	<b>(1)</b>
<b>Net investment income</b>		<b>698</b>	<b>1,204</b>
Profit on the disposal of subsidiaries	8(b)	88	-
<b>Total income</b>		<b>2,079</b>	<b>2,680</b>

## Notes to the financial statements continued

### 3. Details of expenses

	Note	2009 £m	2008 £m
<b>Claims and benefits paid</b>		<b>840</b>	<b>863</b>
Less: Claim recoveries from reinsurers		(39)	(46)
<b>Claims and benefits paid, net of recoveries from reinsurers</b>		<b>801</b>	<b>817</b>
<b>Change in insurance liabilities</b>	18(b)	<b>(81)</b>	<b>(36)</b>
Change in reinsurance asset for insurance provisions	19(c)(i)	<b>44</b>	<b>(2)</b>
Change in insurance liabilities, net of reinsurance		<b>(37)</b>	<b>(38)</b>
<b>Fee and commission expense, net of reinsurance</b>			
Acquisition costs			
Commission expenses		<b>365</b>	<b>477</b>
Change in deferred acquisition costs		<b>53</b>	<b>6</b>
Other acquisition costs		<b>95</b>	<b>111</b>
		<b>513</b>	<b>594</b>
<b>Other operating expenses</b>			
Impairment of investments in subsidiaries	15	<b>1,808</b>	<b>-</b>
Net foreign exchange (gains)/losses		<b>(1)</b>	<b>8</b>
Corporate costs		<b>15</b>	<b>2</b>
Restructuring costs		<b>40</b>	<b>48</b>
Other expenses		<b>56</b>	<b>73</b>
		<b>1,918</b>	<b>131</b>
<b>Finance costs</b>		<b>5</b>	<b>2</b>
<b>Total expenses</b>		<b>3,200</b>	<b>1,506</b>

### 4. Directors and employees

All directors are remunerated by Aviva Employment Services Limited, a fellow subsidiary of the ultimate parent company, Aviva plc. The emoluments of these directors are not recharged to the Company.

The Company has no employees.

### 5. Auditor's remuneration

The total remuneration payable by the Company, excluding VAT, to its principal auditor, Ernst & Young LLP, in respect of the audit of these financial statements is shown below.

	2009 £'000	2008 £'000
Fees payable to Ernst & Young LLP for the statutory audit of the Company	<b>79</b>	<b>79</b>

Fees payable to the Company's auditor, Ernst & Young LLP, and its associates for services other than the statutory audit of the Company are not disclosed in the Company's financial statements since the consolidated financial statements of the ultimate parent, Aviva plc, disclose non-audit fees on a consolidated basis.

## Notes to the financial statements continued

### 6. Tax

#### (a) Tax credited/(charged) to the income statement

##### (i) The total tax credit/charge) comprises:

	2009 £m	2008 £m
<b>Current tax:</b>		
For the year	39	(77)
Adjustment in respect of prior years	9	149
<b>Total current tax</b>	<b>48</b>	<b>72</b>
<b>Deferred tax:</b>		
Origination and reversal of temporary differences	17	(138)
<b>Total deferred tax</b>	<b>17</b>	(138)
<b>Total tax credited/(charged) to income statement</b>	<b>65</b>	(66)

##### (ii) Deferred tax credited/(charged) to the income statement represents movements on the following items:

	2009 £m	2008 £m
Technical provisions and other insurance items	(4)	(7)
Unused losses and tax credits	17	(131)
Accelerated capital allowances	3	(2)
Provisions and other timing differences	1	-
Other temporary differences	-	2
<b>Total deferred tax credited/(charged) to income statement</b>	<b>17</b>	(138)

#### (b) Tax credited to other comprehensive income

##### The total tax credit comprises:

	2009 £m	2008 £m
<b>Deferred tax</b>	-	1
<b>Total tax credited to equity</b>	<b>-</b>	<b>1</b>

#### (c) Tax credited to equity

Other than the tax credited to other comprehensive income in 2008 of £1 million, there has been no tax credited to equity in 2009 or 2008.

## Notes to the financial statements continued

### 6. Tax continued

#### (d) Tax reconciliation

The tax on the Company's (loss)/profit before tax differs from the theoretical amount that would arise using the tax rate of the United Kingdom as follows:

	2009 £m	2008 £m
<b>(Loss)/profit before tax</b>	<b>(1,121)</b>	<b>1,174</b>
Tax calculated at standard UK corporation tax rate of 28% (2008: 28.5%)	314	(335)
Adjustment to tax charge in respect of prior years	(2)	28
Non-assessable dividends	254	258
Non-taxable profit on sale of subsidiaries	25	-
Disallowable expenses	-	(6)
Deferred tax assets not recognised	(20)	(10)
Impairment of investments in subsidiaries	(506)	-
Other	-	(1)
<b>Total tax credited/(charged) to income statement (note 6(a)(i))</b>	<b>65</b>	<b>(66)</b>

### 7. Dividends

	2009 £m	2008 £m
Ordinary dividends declared and charged to equity in the year		
Interim 2008	-	1,000
Interim 2009	900	-
	900	1,000

### 8. Investments in subsidiaries

#### (a) Movements in the Company's investments in its subsidiaries are as follows:

	2009 £m	2008 £m
Fair value as at 1 January	10,859	14,011
Acquisitions	521	-
Additions	652	-
Disposals	(687)	-
Liquidations	(4)	-
Fair value gains transferred to profit on disposal (note 2)	(88)	-
Movement in fair value (note 15)	171	(3,152)
<b>At 31 December</b>	<b>11,424</b>	<b>10,859</b>

All investments in subsidiaries are recorded as level 3 investments in the fair value hierarchy (see note 11(b)).

#### (b) Material movements

##### *Acquisitions*

On 27 August 2009, the Company acquired ownership of the Aviva Group's Polish subsidiaries, Aviva Towarzystwo Ubezpieczen Na Zycie S.A. and Aviva Towarzystwo Ubezpieczen Ogolnych S.A., from its direct parent, Aviva International Insurance Limited ("AI"). The Polish subsidiaries were transferred to the Company at their fair value on the date of transfer, £521 million. The consideration for the transfer was the issue of 52,110 ordinary shares of £10,000 each to AI.

##### *Additions*

On 4 December 2009, the Company subsequently transferred the ownership of these subsidiaries to its direct subsidiary, Aviva International Holdings Limited ("AIH"), at their fair value on date of transfer, £566 million. The consideration for the transfer was a capital contribution of 56,600 ordinary shares of £10,000 each into AIH. As a result, the Company recorded a £45 million profit at the time of transfer and its holding in Aviva International Holdings increased by £566 million.

## Notes to the financial statements continued

### 8. Investments in subsidiaries continued

The Company has also increased its shareholding in Aviva Insurance UK Limited by £86 million.

#### Disposals

As noted above, the Company disposed of its £521 million holding in the Aviva Group's Polish subsidiaries. The Company has also transferred two subsidiaries, CGU Bonus Limited and Scottish Boiler and General Insurance Company Limited, to Aviva International UK Limited in order to settle a quota share arrangement with that company and as part of the legal entity restructuring within the Aviva Group. The value of these entities on the date of transfer was £166 million and the Company recorded a £43 million profit on the transfer.

#### Liquidations

The Company's subsidiary, Timberlaine Properties Limited, was liquidated during the year.

#### (c) Principal subsidiaries

The principal subsidiaries at 31 December 2009 are Aviva International Holdings Limited, an intermediate parent undertaking, and Aviva Insurance UK Limited which is an insurance company. Aviva International Holdings Limited holds the Company's overseas subsidiaries. These subsidiaries are all directly wholly-owned and domiciled in the UK.

### 9. Property and equipment

	Owner-occupied properties £m	Other assets £m	Total £m
<b>Cost or valuation</b>			
At 1 January 2008	3	9	12
Disposals	-	(9)	(9)
<b>At 31 December 2008 and 31 December 2009</b>	<b>3</b>	<b>-</b>	<b>3</b>
<b>Depreciation</b>			
At 1 January 2008, 31 December 2008 and 31 December 2009	-	-	-
<b>Carrying amount</b>			
At 1 January 2008	3	-	3
At 31 December 2008	3	-	3
<b>At 31 December 2009</b>	<b>3</b>	<b>-</b>	<b>3</b>

Owner-occupied properties are stated at their revalued amounts, as assessed by qualified external valuers or by local qualified staff of the Aviva Group in overseas operations, all with recent relevant experience. These values are assessed in accordance with the relevant parts of the current RICS Appraisal and Valuation Standards in the UK, and with current local valuation practices in other countries. This assessment, on the basis of Existing Use Value and in accordance with UK Practice Statement 1.3, is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction, after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion, assuming that the buyer is granted vacant possession of all parts of the property required by the business and disregarding potential alternative uses. The valuation assessment adopts market-based evidence and is in line with guidance from the International Valuation Standards Committee and the requirements of IAS 16, *Property, Plant and Equipment*.

If owner-occupied properties were stated on a historical cost basis, the carrying amount would be £1 million (2008: £1 million).

The Company has no material finance leases for property and equipment.

## Notes to the financial statements continued

### 10. Financial investments

#### (a) Carrying amount

Financial investments comprise:	At fair value through profit or loss		
	Trading £m	Other than trading £m	Total £m
<b>Debt securities</b>			
UK government	-	137	137
Non-UK government	-	40	40
Corporate - Non-UK	-	361	361
	-	538	538
<b>Equity securities</b>	-		
Corporate - Non-UK	-	5	5
	-	5	5
<b>Other investments</b>			
Derivative financial instruments (note 29)	10	-	10
<b>Total financial investments</b>	<b>10</b>	<b>543</b>	<b>553</b>
	At fair value through profit or loss		
	Trading £m	Other than trading £m	Total £m
<b>Debt securities</b>			
UK government	-	98	98
Non-UK government	-	12	12
Corporate - Non-UK	-	411	411
Other	-	521	521
<b>Equity securities</b>	-	-	-
Corporate - UK	-	3	3
Corporate - Non-UK	-	3	3
<b>Other investments</b>			
Derivative financial instruments (note 29)	144	-	144
<b>Total financial investments</b>	<b>144</b>	<b>524</b>	<b>668</b>

Of the above total £500 million (2008: £458 million) is expected to be recovered more than one year after the statement of financial position date.

## Notes to the financial statements continued

### 10. Financial investments continued

#### (b) Cost, unrealised gains and fair value

The following is a summary of the cost/amortised cost, gross unrealised gains and losses and fair value of financial investments:

				2009
	Cost/ amortised cost £m	Unrealised gains £m	Unrealised losses £m	Fair Value £m
Debt securities	543	15	(20)	538
Equity securities	6	-	(1)	5
Other investments				
Unit trusts and specialised investment vehicles	1	-	(1)	-
Derivative financial instruments	76	-	(66)	10
Other	4	-	(4)	-
	<b>630</b>	<b>15</b>	<b>(92)</b>	<b>553</b>
<hr/>				
				2008
	Cost/ amortised cost £m	Unrealised gains £m	Unrealised losses £m	Fair Value £m
Debt securities	597	8	(84)	521
Equity securities	6	-	(3)	3
Other investments				
Unit trusts and specialised investment vehicles	1	-	(1)	-
Derivative financial instruments	144	-	-	144
Other	4	-	(4)	-
	<b>752</b>	<b>8</b>	<b>(92)</b>	<b>668</b>

All unrealised gains and losses and impairments on financial investments classified as fair value through profit or loss have been recognised in the income statement.

Unrealised gains and losses on financial investments classified as at fair value through profit or loss recognised in the income statement in the year were a net gain of £37 million (2008: £261 million net gain).

The movement in the unrealised gain/loss position reported in the statement of financial position during the year, shown in the table above, includes transfers due to the realisation of gains and losses on disposal and the recognition of impairment losses.

#### (c) Financial lending arrangements

##### *Stock lending arrangements*

The Company has entered into stock lending arrangements during the year in accordance with established market conventions. The majority of the Company's stock lending transactions occurs in the UK, where investments are lent to EEA-regulated, locally-domiciled counterparties and governed by agreements written under English law.

The Company receives collateral in order to reduce the credit risk of these arrangements. The level of collateral held is monitored regularly, with further collateral obtained where this is considered necessary to manage the Company's risk exposure.

In certain markets, the Company's appointed stock lending managers obtain legal ownership of the collateral received and can re-pledge it as collateral elsewhere or sell outright in the absence of default. Collateral must be in a ready realisable form such as listed securities and is held in segregated accounts. Transfer of title always occurs for the collateral received, although no market risk or economic benefit is taken. The carrying amounts of financial assets received and pledged in this manner at 31 December 2009 were £148 million and £138 million, respectively (2008: £120 million and £nil, respectively). No collateral was actually sold or re-pledged in the absence of default in either 2009 or 2008.

## Notes to the financial statements continued

### 11. Fair value

#### a) Fair value methodology

For financial instruments carried at fair value, the Company has categorised the measurement basis into a 'fair value hierarchy' as follows:

##### **Quoted market prices in active markets – ("Level 1")**

Inputs to Level 1 fair values are quoted prices (unadjusted) in active markets for identical assets. An active market is one in which transactions for the asset occur with sufficient frequency and volume to provide pricing information on an ongoing basis. Examples are listed equities in active markets, listed debt securities in active markets and quoted unit trusts in active markets.

##### **Modelled with significant observable market inputs – ("Level 2")**

Inputs to Level 2 fair values are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. If the asset has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset. Level 2 inputs include the following:

- quoted prices for similar (i.e. not identical) assets in active markets;
- quoted prices for identical or similar assets in markets that are not active, the prices are not current, or price quotations vary substantially either over time or among market makers, or in which little information is released publicly;
- inputs other than quoted prices that are observable for the asset (for example, interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks, and default rates); and
- inputs that are derived principally from, or corroborated by, observable market data by correlation or other means (market-corroborated inputs).

Examples of these are securities measured using discounted cash flow models based on market observable swap yields, listed debt or equity securities in a market that is inactive, and investments in subsidiaries valued using applicable models underpinned by Aviva plc's market capitalisation. Valuations, whether sourced from internal models or third parties, incorporate credit risk by adjusting the spread above the yield curve for government treasury securities for the appropriate amount of credit risk for each issuer, based on observed market transactions. To the extent observed market spreads are either not used in valuing a security, or do not fully reflect liquidity risk, our valuation methodology, whether sourced from internal models or third parties, reflects a liquidity premium.

Where we use broker quotes and no information as to the observability of inputs is provided by the broker, we generally validate the price quoted by the broker by using internal models with observable inputs. When the price obtained from the broker and internal model are similar, we look to the inputs used in our internal model to understand the observability of the inputs used by the broker. In circumstances where internal models are not used to validate broker prices, and the observability of inputs used by brokers is unavailable, the investment is classified as Level 3. Broker quotes are usually non-binding.

##### **Modelled with significant unobservable market inputs – ("Level 3")**

Inputs to Level 3 fair values are unobservable inputs for the asset. Unobservable inputs may have been used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset at the measurement date (or market information for the inputs to any valuation models). As such, unobservable inputs reflect the assumptions the Company considers that market participants would use in pricing the asset. Examples are certain private equity investments and private placements, and investments in subsidiaries valued at net asset value.

#### (b) Fair value hierarchy

The majority of the Company's investments are valued based on quoted market information or observable market data. None of the total assets recorded at fair value, are based on estimates and recorded as Level 3 investments. Where estimates are used, these are based on a combination of independent third party evidence and internally developed models, calibrated to market observable data where possible. Whilst such valuations are sensitive to estimates, it is believed that changing one or more of the assumptions to reasonably possible alternative assumptions would not change the fair value significantly. An analysis of investments according to fair value hierarchy is given below:

## Notes to the financial statements continued

### 11. Fair Value continued

	Fair value hierarchy			Statement of financial position total £m	2009
	Level 1 £m	Level 2 £m	Level 3 £m		
Debt securities	538	-	-	538	
Equity securities	5	-	-	5	
Other investments	10	-	-	10	
	553	-	-	553	
					2008
	Fair value hierarchy			Statement of financial position total £m	
	Level 1 £m	Level 2 £m	Level 3 £m		
Debt securities	521	-	-	521	
Equity securities	3	-	-	3	
Other investments	144	-	-	144	
	668	-	-	668	

All investments in subsidiaries are considered to be Level 3 investments. The unobservable inputs to the fair value relate to assumptions made to individual subsidiary net assets or embedded values, all of which are underpinned by the market capitalisation of Aviva plc. Whilst such valuations are sensitive to estimates, it is believed that changing one or more of the assumptions to reasonably possible alternatives assumptions would not change the fair value significantly.

### 12. Receivables and other financial assets

	2009 £m	2008 £m
Amounts due from contract holders	30	11
Amounts due from intermediaries	252	227
Amounts due from reinsurers	66	78
Amounts due to immediate parent (Note 30(a)(i))	687	-
Amounts due from subsidiaries (Note 30(a)(ii))	3,917	5,219
Amounts due from other Aviva Group companies (Note 30(a)(i))	13	22
Other financial assets	53	91
<b>Total</b>	<b>5,018</b>	<b>5,648</b>
Expected to be recovered in less than one year	5,018	5,648
Expected to be recovered in more than one year	-	-
	<b>5,018</b>	<b>5,648</b>

Concentrations of credit risk with respect to receivables are limited due to the size and spread of the Company's trading base. No further credit risk provision is therefore required in excess of the normal provision for doubtful receivables.

### 13. Deferred acquisition costs and other assets

#### (a) The carrying amount comprises:

	2009 £m	2008 £m
Deferred acquisition costs in respect of insurance contracts	351	461
Prepayments and accrued income	14	31
<b>Total</b>	<b>365</b>	<b>492</b>

## Notes to the financial statements continued

### 13. Deferred acquisition costs and other assets continued

(b) The movements in deferred acquisition costs during the year are:

	2009 £m	2008 £m
Carrying amount at 1 January	461	469
Acquisition costs deferred during the year	460	582
Amortisation	(570)	(590)
Carrying amount at 31 December	351	461

Deferred acquisition costs are generally recoverable within one year of the statement of financial position date.

### 14. Ordinary share capital

(a) Details of the Company's ordinary share capital are as follows:

	2009 £m	2008 £m
<b>Authorised</b>		
900,000 (2008: 750,000) ordinary shares of £10,000 each	9,000	7,500
<b>Allotted, called up and fully paid</b>		
758,345 (2008: 698,775) ordinary shares of £10,000 each	7,584	6,988

The Company's authorised share capital was increased by 50,000 ordinary shares of £10,000 each on 24 August 2009 and by a further 100,000 ordinary shares of £10,000 each on 19 November 2009.

(b) Movements in the year comprise:

	Number of shares	Share capital £m	Share premium £m
At 1 January 2009	698,775	6,988	3,049
Shares issued	59,570	596	-
<b>At 31 December 2009</b>	<b>758,345</b>	<b>7,584</b>	<b>3,049</b>

As explained in note 8(b), the Company's parent, Aviva International Insurance Limited (AII), transferred two Polish subsidiaries to the Company on 24 August 2009 at their fair value of £521 million, satisfied by the issue of 52,110 ordinary shares of £10,000 each. The Company's share capital was increased by a further £75 million on 23 December 2009 after an allotment of 7,460 shares of £10,000 each to AII in consideration for the intra-group transfer of its shareholding in two subsidiaries.

### 15. Other reserves

	Owner – occupied properties reserve (see accounting policy K) £m	Investment valuation reserve (see accounting policy C) £m	Special reserve £m	Total £m
<b>Balance at 1 January 2008</b>	<b>2</b>	1,212	111	1,325
Arising in the year:				
Fair value losses on investments in subsidiaries (note 8(a))	-	(3,152)	-	(3,152)
Aggregate tax effect	1	-	-	1
<b>Balance at 31 December 2008</b>	<b>3</b>	<b>(1,940)</b>	<b>111</b>	<b>(1,826)</b>
Arising in the year:				
Fair value gains transferred to profit on disposal of subsidiaries (note 2)	-	(88)	-	(88)
Fair value gains on investments in subsidiaries (note 8(a))	-	171	-	171
Impairment charged to income statement (note 3)	-	1,808	-	1,808
<b>Balance at 31 December 2009</b>	<b>3</b>	<b>(49)</b>	<b>111</b>	<b>65</b>

## Notes to the financial statements continued

### 15. Other reserves continued

#### Special reserve

As part of the ongoing Aviva Group restructuring, the Company's immediate parent, Aviva International Insurance Limited (AII), transferred its entire shareholding in Aviva Insurance UK Limited at its fair value of £1,348 million to the Company on 31 December 2007. The consideration was satisfied by the issue of new shares in the Company with the nominal value of £1,237 million to AII, and the establishment of a special reserve of £111 million under the group reconstruction relief provisions of section 132 of the Companies Act 1985.

### 16. Retained earnings

	2009 £m	2008 £m
Balance at 1 January	5,928	5,820
(Loss) / profit for the year	(1,056)	1,108
Dividends (note 7)	(900)	(1,000)
Foreign exchange rate movements on overseas branches	4	-
<b>Balance at 31 December</b>	<b>3,976</b>	<b>5,928</b>
 Distributable	 88	 317
Non-distributable	3,888	5,611
<b>Balance at 31 December</b>	<b>3,976</b>	<b>5,928</b>

### 17. Insurance contract liabilities and associated reinsurance

The following is a summary of the contract provisions and related reinsurance assets as at 31 December:

	2009			2008		
	Gross insurance provisions £m	Reinsurance assets £m	Net £m	Gross insurance provisions £m	Reinsurance assets £m	Net £m
Outstanding claims provisions	(1,403)	79	(1,324)	(1,466)	144	(1,322)
Provisions for claims incurred but not reported	(274)	25	(249)	(285)	-	(285)
	<b>(1,677)</b>	<b>104</b>	<b>(1,573)</b>	<b>(1,751)</b>	<b>144</b>	<b>(1,607)</b>
Provision for unearned premiums	(791)	138	(653)	(980)	196	(784)
<b>Total</b>	<b>(2,468)</b>	<b>242</b>	<b>(2,226)</b>	<b>(2,731)</b>	<b>340</b>	<b>(2,391)</b>

### 18. Insurance liabilities

#### (a) Carrying amount

Insurance liabilities at 31 December comprise:

	2009 £m	2008 £m
Outstanding claims provisions	1,403	1,466
Provision for claims incurred but not reported	274	285
	<b>1,677</b>	<b>1,751</b>
Provision for unearned premiums	791	980
<b>Total</b>	<b>2,468</b>	<b>2,731</b>

#### (b) General insurance liabilities

##### Provisions for outstanding claims

Significant delays occur in the notification and settlement of claims and a substantial measure of experience and judgement is involved in assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the statement of financial position date. The reserves for general insurance are based on information currently available; however, it is inherent in the nature of the business written that the ultimate liabilities may vary as a result of subsequent developments.

## Notes to the financial statements continued

### 18. Insurance liabilities continued

#### (b) General insurance liabilities continued

Provisions for outstanding claims are established to cover the outstanding expected ultimate liability for losses and loss adjustment expenses ("LAE") in respect of all claims that have already occurred. The provisions established cover reported claims and associated LAE, as well as claims incurred but not yet reported and associated LAE.

Outstanding claims provisions are based on undiscounted estimates of future claim payments, except for the following classes of business for which discounted provisions are held:

Class	Discounting Rate		Mean term of liabilities	
	2009	2008	2009	2008
Latent claims	1.02% to 4.58%	2.61% to 3.68%	15 years	15 Years
Reinsured London Market business	4.0%	3.56%	10 years	8 years
Structured settlements	3.3%	2.5%	35 years	35 years

The gross outstanding claims provision before discounting was £1,760 million (2008: £1,825 million). The period of time which will elapse before the liabilities are settled has been estimated by modelling the settlement patterns of the underlying claims.

The discount rate that has been applied to latent claims reserve is based on the relevant swap curve having regard to the expected settlement dates of the claims. The range of discount rates used depends on the duration of the claims and is given in the section above. The duration of the claims span over 35 years, with the average duration estimated to be 15 years.

During 2009, across the UKGI group, we have experienced an increase in the number of bodily injury claims settled by periodic payment orders (PPOs) or structured settlements, which are reserved for on a discounted basis.

#### Assumptions

Claims provisions are estimated based on known facts at the date of estimation. Case estimates are generally set by skilled claims technicians, applying their experience and knowledge to the circumstances of individual claims, taking into account all available information and correspondence regarding the circumstances of the claim, such as medical reports, investigations and inspections. Claims technicians set case estimates according to documented claims department policies and specialise in setting estimates for certain lines of business or types of claim. Claims above certain limits are referred to senior claims handlers for authorisation. No adjustments are made to the claims technicians' case estimates included in booked claims provisions, except for rare occasions when the estimated ultimate cost of a large or unusual claim may be adjusted, subject to internal reserve committee approval, to allow for uncertainty regarding, for example, the outcome of a court case. The ultimate cost of outstanding claims is then estimated by using a range of standard actuarial claims projection techniques, such as the Chain Ladder and Bornhuetter-Ferguson methods. The main assumption underlying these techniques is that a company's past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios. Historical claims development is mainly analysed by accident period, although underwriting or notification period is also used where this is considered appropriate.

Claims development is separately analysed for each line of business. Certain lines of business are also further analysed by claim type or type of coverage. In addition, large claims are usually separately assessed, either by being reserved at the face value of loss adjuster estimates, or separately projected in order to reflect their future development.

The assumptions used in most non-life actuarial projection techniques, including future rates of claims inflation or loss ratio assumptions, are implicit in the historical claims development data on which the projections are based. Additional qualitative judgement is used to assess the extent to which past trends may not apply in the future, for example, to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy conditions and claims handling procedures in order to arrive at the estimated ultimate cost of claims that represents the most likely outcome, from the range of possible outcomes, taking account of all the uncertainties involved. The range of possible outcomes does not, however, result in the quantification of a reserve range.

## Notes to the financial statements continued

### 18. Insurance liabilities continued

#### (b) General insurance liabilities continued

##### Movements

The following changes have occurred in the claims provisions during the year:

	2009 £m	2008 £m
<b>Carrying amount at 1 January</b>	<b>1,751</b>	1,774
Impact of changes in assumptions	(10)	19
Claims losses and expenses incurred in the current year	865	925
Decrease in estimated claim losses and expenses incurred in prior years	(96)	(117)
Incurred claims losses and expenses	759	827
Less:		
Payments made on claims incurred in the current year	(302)	(299)
Payments made on claims incurred in prior years	(538)	(564)
Claims payments made in the year	(840)	(863)
Unwinding of discount	4	1
Changes in claims reserve recognised as an income	(77)	(35)
Foreign exchange rate movements	3	12
<b>Carrying amount at 31 December</b>	<b>1,677</b>	1,751

In 2008, the Institute of Actuaries' Asbestos Working Party report contributed to our view that experience variances, which we had previously perceived as normal short-term volatility, reflected a real worsening of expected ultimate claims experience. The market trend in mesothelioma claims was fully reflected as a one-off strengthening of gross latent claims reserves in 2008, reported through the prior year's experience line in the table above.

#### (c) Loss development tables

(i) The tables that follow present the development of claims payments and the estimated ultimate cost of claims for the accident years 2001 to 2009. The upper half of the tables shows the cumulative amounts paid during successive years related to each accident year. For example, with respect to the accident year 2002, by the end of 2009 £501 million had actually been paid in settlement of claims. In addition, as reflected in the lower section of the table, the original estimated ultimate cost of claims of £561 million was re-estimated to be £526 million at 31 December 2009. This decrease from the original estimate is due to the combination of a number of factors. The original estimates will also be increased or decreased, as more information becomes known about the individual claims and overall claim frequency and severity.

In 2005, the year of adoption of IFRS, only five years were required to be disclosed. This is being increased in each succeeding additional year, until ten years of information is included.

The Company aims to maintain strong reserves in respect of its general insurance business in order to protect against adverse future claims experience and development. As claims develop and the ultimate cost of claims become more certain, the absence of adverse claims experience will then result in a release of reserves from earlier accident years, as shown in the loss development tables below. However, in order to maintain overall reserve adequacy the Company establishes strong reserves in respect of the current accident year (2009), where the development of claims is less mature and there is much greater uncertainty attaching to the ultimate cost of claims.

## Notes to the financial statements continued

### 18. Insurance liabilities continued

#### (c) Loss development table continued

Before the effect of reinsurance, the loss development table is:

Accident year	All prior years	2001	2002	2003	2004	2005	2006	2007	2008	2009	Total
		£m									
<b>Gross cumulative claim payments</b>											
At end of accident year		(180)	(175)	(148)	(158)	(176)	(199)	(328)	(299)	(302)	
One year later		(376)	(314)	(329)	(302)	(384)	(448)	(640)	(568)		
Two years later		(478)	(385)	(383)	(344)	(465)	(512)	(761)			
Three years later		(536)	(418)	(428)	(379)	(520)	(569)				
Four years later		(575)	(450)	(473)	(401)	(547)					
Five years later		(577)	(478)	(514)	(408)						
Six years later		(583)	(497)	(526)							
Seven years later		(583)	(501)								
Eight years later		(584)									
<b>Estimate of gross ultimate claims</b>											
At end of accident year		541	561	608	622	704	755	1,006	925	865	
One year later		582	592	588	498	653	756	1,000	941		
Two years later		601	574	585	495	664	738	991			
Three years later		605	570	579	464	622	712				
Four years later		600	551	554	432	602					
Five years later		599	543	542	419						
Six years later		590	529	541							
Seven years later		583	526								
Eight years later		584									
<b>Estimate of gross ultimate claims</b>											
Cumulative payments		(584)	(501)	(526)	(408)	(547)	(569)	(761)	(568)	(302)	
		345	-	25	15	11	55	143	230	373	563
Effect of discounting		(81)	-	-	(2)	-	-	-	-	-	(83)
Present value in the statement of financial position		264	-	25	13	11	55	143	230	373	563
											1,677

## Notes to the financial statements continued

### 18. Insurance liabilities continued

#### (c) Loss development table continued

After the effect of reinsurance, the loss development table is:

Accident year	All prior years	2001	2002	2003	2004	2005	2006	2007	2008	2009	Total
		£m									
<b>Net cumulative claim payments</b>											
At end of accident year		(178)	(153)	(137)	(145)	(171)	(199)	(320)	(294)	(296)	
One year later		(371)	(280)	(300)	(276)	(357)	(428)	(611)	(556)		
Two years later		(441)	(348)	(349)	(316)	(423)	(486)	(716)			
Three years later		(487)	(392)	(390)	(328)	(479)	(541)				
Four years later		(522)	(420)	(434)	(348)	(514)					
Five years later		(525)	(447)	(473)	(351)						
Six years later		(531)	(462)	(485)							
Seven years later		(531)	(462)								
Eight years later		(531)									
<b>Estimate of net ultimate claims</b>											
At end of accident year		529	521	567	569	673	716	963	904	848	
One year later		546	487	555	444	606	700	948	922		
Two years later		563	535	548	437	614	686	935			
Three years later		554	532	539	403	571	668				
Four years later		547	512	514	371	568					
Five years later		547	506	501	359						
Six years later		536	493	496							
Seven years later		531	487								
Eight years later		531									
<b>Estimate of ultimate claims</b>											
<b>Cumulative payments</b>		531	487	496	359	568	668	935	922	848	
		(531)	(462)	(485)	(351)	(514)	(541)	(716)	(556)	(296)	
		277	-	25	11	8	54	127	219	366	1,639
Effect of discounting		(66)	-	-	-	-	-	-	-	-	(66)
Present value recognised in the statement of financial position		211	-	25	11	8	54	127	219	366	552
											1,573

In the loss development tables shown above, the cumulative claim payments and estimates of cumulative claims for each accident year are translated into sterling at the exchange rates that applied at the end of that accident year. Disposals are dealt with by treating all outstanding and IBNR claims of the disposed entity as "paid" at the date of disposal.

The loss development tables include information on asbestos and environmental pollution claim provisions from business written before 2001. The undiscounted claim provisions, net of reinsurance, in respect of this business were £137 million at 31 December 2009 (2008: £161 million).

#### (d) Provision for unearned premiums

The following changes have occurred in the provision for unearned premiums ("UPR") during the year:

	2009	2008
	£m	£m
<b>Carrying amount at 1 January</b>	980	1,104
Premiums written during the year	1,296	1,563
Less: Premiums earned during the year	(1,485)	(1,687)
Changes in UPR recognised as income	(189)	(124)
<b>Carrying amount at 31 December</b>	791	980

## Notes to the financial statements continued

### 19. Reinsurance assets

#### (a) The following is a summary of the reinsurance assets as at 31 December:

	2009 £m	2008 £m
Outstanding claims provisions	79	144
Provisions for claims incurred but not reported	25	-
Provisions for unearned premiums	138	196
	<b>242</b>	<b>340</b>

Of the above reinsurance assets, £126million (2008: £119 million), is expected to be recovered more than one year after the statement of financial position date.

#### (b) Assumptions

The assumptions, including discount rates, used for reinsurance contracts follow those used for insurance contracts. Reinsurance assets are valued net of an allowance for their recoverability.

#### (c) Movements

The following movements have occurred in the reinsurance asset during the year:

##### (i) Outstanding claims provisions and IBNR

	2009 £m	2008 £m
<b>Carrying amount at 1 January</b>	<b>144</b>	142
Impact of changes in assumptions	-	1
Reinsurers' share of claim losses and expenses incurred in current year	17	21
Reinsurers' share of claim losses and expenses incurred in prior years	(22)	26
Reinsurers' share of incurred claim losses and expenses	(5)	47
Less:		
Reinsurance recoveries received on claims incurred in current year	(6)	(5)
Reinsurance recoveries received on claims incurred in prior years	(33)	(41)
Reinsurance recoveries received in the year	(39)	(46)
Change in reinsurance asset recognised as (expense)/income	(44)	2
Foreign exchange rate and other movements	4	-
<b>Carrying amount at 31 December</b>	<b>104</b>	144

##### (ii) Reinsurers' share of the provision for unearned premiums ("UPR")

	2009 £m	2008 £m
<b>Carrying amount at 1 January</b>	<b>196</b>	282
Premiums ceded to reinsurers in the year	142	101
Less:		
Reinsurers' share of premiums earned during the year	(200)	(187)
Changes in reinsurance asset recognised as expense	(58)	(86)
<b>Carrying amount at 31 December</b>	<b>138</b>	196

## Notes to the financial statements continued

### 20. Tax assets and liabilities

#### (a) Current tax

	2009 £m	2008 £m
(i) Tax asset		
Expected to be recoverable in more than one year	40	-
Tax asset recognised in statement of financial position	40	-
(ii) Tax liability		
Expected to be payable in more than one year	-	83
Tax liability recognised in statement of financial position	-	83

Assets and liabilities for prior years tax settled by Group relief of £nil and £58 million (2008: £170 million and £nil) are included in the statement of financial position. The liability of £58 million is payable in less than one year.

#### (b) Deferred tax

	2009 £m	2008 £m
(i) The balance at the year end comprises:		
Deferred tax liabilities	-	(17)
Net deferred tax liability	-	(17)
(ii) The net deferred tax liability arises on the following items:		
Temporary differences arising on insurance items	(37)	(33)
Unused losses and tax credits	33	16
Accelerated capital allowances	3	
Provisions and other timing differences	1	-
Net deferred tax liability	-	(17)
(iii) The movement in the net deferred tax (liability) / asset was as follows:		
Net (liability) / asset at 1 January	(17)	121
Amounts charged to profit (note 6)	17	(138)
Net liability at 31 December	-	(17)

The Company has unrecognised temporary differences of £73 million (2008: £34 million) to carry forward indefinitely against future taxable income. In addition, the Company has an unrecognised capital tax loss of £251 million (2008: £193 million).

## Notes to the financial statements continued

### 21. Provisions

#### (a) Carrying amounts

	2009 £m	2008 £m
Restructuring provision	3	15
Other provisions	14	14
<b>Total</b>	<b>17</b>	<b>29</b>

Of the above total, £13 million (2008: £23 million) is expected to be settled more than one year after the statement of financial position date.

#### (b) Movements during the year on restructuring and other provisions:

	Restructuring provision £m	Other provisions £m	Total £m
<b>At 1 January 2008</b>	5	14	19
Additional provisions	48	-	48
Utilised during the year	(38)	-	(38)
<b>At 31 December 2008</b>	<b>15</b>	<b>14</b>	<b>29</b>
Additional provisions	40	-	40
Utilised during the year	(52)	-	(52)
<b>At 31 December 2009</b>	<b>3</b>	<b>14</b>	<b>17</b>

Other provisions comprised many small provisions for obligations such as costs of compensation, litigation and reorganisation.

### 22. Payables and other financial liabilities

	2009 £m	2008 £m
Payables arising out of direct insurance	59	50
Payables arising out of reinsurance operations	41	28
Amounts due to immediate parent (Note 30(a)(ii))	-	665
Amounts due to subsidiaries (Note 30(a)(ii))	36	21
Amounts due to other Aviva Group companies (Note 30(a)(ii))	157	143
Bank overdrafts (Note 26(b))	36	27
Derivative liabilities (note 29)	-	47
	<b>329</b>	<b>981</b>
Expected to be settled within one year	<b>329</b>	<b>802</b>
Expected to be settled in more than one year	-	179
	<b>329</b>	<b>981</b>

### 23. Other liabilities

	2009 £m	2008 £m
Reinsurers' share of deferred acquisition costs	106	163
Accruals	52	66
Other liabilities	44	44
	<b>202</b>	<b>273</b>

All the above liabilities are expected to be settled within one year.

## Notes to the financial statements continued

### 24. Contingent liabilities and other risk factors

#### (a) Uncertainty over claims provisions

Note 18 gives details of the estimation techniques used in determining the general business outstanding claims provisions, which are designed to allow for prudence. These are estimated to give a result within the normal range of outcomes. To the extent that the ultimate cost falls outside this range, for example where experience is worse than that assumed, or future general business claims inflation differs from that expected, there is uncertainty in respect of this liability.

#### (b) Asbestos, pollution and social environmental hazards

In the course of conducting insurance business, the Company receives general insurance liability claims, and becomes involved in actual or threatened litigation arising there from, including claims in respect of pollution and other environmental hazards. Amongst these are claims in respect of asbestos production and handling in the United Kingdom. Given the significant delays that are experienced in the notification of these claims, the potential number of incidents which they cover and the uncertainties associated with establishing liability and the availability of reinsurance, the ultimate cost cannot be determined with certainty. However, the Company's net exposure to such liabilities is not significant and, on the basis of current information and having regard to the level of provisions made for general insurance claims, the directors consider that any costs arising are not likely to have a material impact on the financial position of the Company.

#### (c) Regulatory

The Financial Services Authority (FSA) regulates the Company's UK business and in addition monitors the financial resources and organisation of the Company as a whole. The FSA has broad powers including the authority to grant, vary the terms of, or cancel a regulated firm's, authorisation, to investigate marketing and sales practices and to require the maintenance of adequate financial resources. The Company's regulators outside the UK typically have similar powers but in some cases they operate a system of "prior product approval" and hence place less emphasis than the FSA on regulating sales and marketing practices.

The directors believe that the Company dedicates appropriate resources to its compliance programme, endeavours to respond to regulatory enquiries in a constructive way, and takes corrective action when warranted. However, all regulated financial services companies face the risk that the regulator could find that they have failed to comply with applicable regulations or have not undertaken corrective action as required.

The impact of any such finding could have a negative impact on the Company's reported results or on its relations with current or potential customers. Regulatory action against the Company could result in adverse publicity for, or negative perceptions regarding, the Company, or could have a material adverse effect on the business of the Company, its results of operations and/or financial condition and divert management's attention from the day-to-day management of the business.

With the approval of the Financial Services Authority, the Company and certain of its United Kingdom insurance subsidiaries transacting general insurance business have mutually guaranteed to discharge all liabilities attaching to their respective insurance policies. The guarantee enables a participating company, if it is unable to pay policyholder claims, to seek financial support from one of the guarantors. The guarantors are not obliged to make the payment if they cannot do so without seeking recourse to their funds where applicable. If any payments are made under the guarantee, the guarantors are entitled to seek repayment from the company benefiting from the guarantee. The guarantee cannot be relied upon by any other person, including without limitation the holder of any contracts of insurance issued by a party to the guarantee. There is no maximum amount the Company would have to pay under the guarantee but, in the opinion of the directors, the fair value of the guarantee above is not material and no material loss is expected to arise therefrom.

#### (d) Other

In addition, in line with standard business practice, the Company has given guarantees, indemnities and warranties in connection with disposals in recent years of subsidiaries to parties outside the Aviva Group. In the opinion of the directors, no material loss will arise in respect of these guarantees, indemnities and warranties.

## Notes to the financial statements continued

### 25. Commitments

#### Operating lease commitments

Future contractual aggregate minimum lease payments under non-cancellable operating leases are as follows:

	2009 £m	2008 £m
Within one year	9	9
Later than one year and not later than five years	31	34
Later than five years	18	21
	<b>58</b>	<b>64</b>
The total of future minimum sublease payments expected to be received under non-cancellable subleases	6	4

The Company has no capital commitments which have not been recognised in the financial statements.

### 26. Statement of cash flows

#### (a) The reconciliation of profit before tax to the net cash inflow from operating activities is:

	2009 £m	2008 £m
(Loss)/profit before tax	(1,121)	1,174
<b>Adjustments for:</b>		
Loss/(profit) on sale of:		
Subsidiaries	(88)	-
Investments	273	24
	<b>185</b>	<b>24</b>
Impairment of:		
Investments in subsidiaries	1,808	-
Other intangibles	-	8
	<b>1,808</b>	<b>8</b>
Amortisation of:		
Premium or discount on debt securities	2	-
Intangibles	-	2
	<b>2</b>	<b>2</b>
Fair value gains on investments	(37)	(261)
Unwind of discount	4	(2)
Foreign currency exchange loss	(1)	8
<b>Changes in working capital:</b>		
Decrease in reinsurance assets	98	84
Decrease in deferred acquisition costs	53	8
Decrease in insurance liabilities	(263)	(147)
Increase in other assets and liabilities	(781)	(1,419)
	<b>(893)</b>	<b>(1,474)</b>
<b>Net purchases of operating assets</b>		
Proceeds from repayments received on loans	-	5
Financial investments	87	347
	<b>87</b>	<b>352</b>
<b>Cash used in operations</b>	<b>34</b>	<b>(169)</b>

Purchases and sales of investment property, loans and financial investments are included in operating cash flows as the purchases are funded from cash flows associated with the origination of insurance contracts, net of payments of related benefits and claims.

## Notes to the financial statements continued

### 26. Statement of cash flows continued

#### (b) Cash and cash equivalents in the cash flow statement at 31 December comprised

	2009 £m	2008 £m
Cash at bank and in hand	48	22
Cash equivalents	55	39
	103	61
Bank overdrafts	(36)	(27)
	67	34

### 27. Company capital structure

The Company maintains an efficient capital structure from equity shareholders' funds, consistent with the Company's overall risk profile and the regulatory and market requirements of the business. This note describes the way the Company manages capital and shows where this is employed.

#### (a) General

IFRS underpins the Company's capital structure and accordingly, the capital structure is analysed on this basis. Increasingly, the Company uses an ICA measure to assess its own internal economic capital requirements.

#### (b) Capital management

In managing its capital, the Company seeks to:

- (i) match the profile of its assets and liabilities, taking account of the risks inherent in each business;
- (ii) maintain financial strength to support new business growth and satisfy the requirements of its policyholders and regulators;
- (iii) retain financial flexibility by maintaining strong liquidity; and
- (iv) allocate capital efficiently to support growth and repatriate excess capital where appropriate.

The Company considers not only traditional sources of capital funding but alternative sources of capital including reinsurance, as appropriate, when assessing its deployment and usage of capital.

#### (c) Different measures of capital

The Company measures its capital on a number of different bases. These include measures which comply with the regulatory regime within which the Company operates and those which the directors consider appropriate for the management of the business. The measures which the Company uses are:

##### (i) Accounting basis

The Company is required to report its results on an IFRS basis.

##### (ii) Regulatory basis

Relevant capital and solvency regulations are used to measure and report the Company's financial strength. These measures are based on the FSA's regulatory requirements under Solvency I and the ICA regime. The regulatory capital tests verify that the Company retains an excess of solvency capital above the required minimum level calculated using a series of prudent assumptions about the type of business that is underwritten.

The Company fully complied with these regulatory requirements during the year.

##### (iii) Economic basis

Notwithstanding the required levels of capital laid out by the FSA, UKGI also measures its capital using various risk-based management tools that take into account a more realistic set of financial and non-financial assumptions. Note 28 Risk management, gives further details.

## Notes to the financial statements continued

### 27. Company capital structure continued

#### (d) Company capital structure

	2009 £m	2008 £m
<b>Total capital employed</b>	<b>14,674</b>	<b>14,139</b>
<b>Financed by</b> Equity shareholders' funds	<b>14,674</b>	<b>14,139</b>

### 28. Risk management

The ultimate parent company, Aviva plc, and its subsidiaries, joint ventures and associates (collectively known as "the Aviva Group"), have established a risk management framework with the primary objective of protecting the Aviva Group, including the Company, from events that hinder the sustainable achievement of performance objectives, including failing to exploit opportunities.

Risk is categorised as follows:

- Financial risks, which cover market, credit, general insurance and liquidity risks;
- Strategic risks, which include issues such as customer, products and markets as well as any risks to the Company's business model arising from changes in the market, and risks arising from mergers and acquisitions; and
- Operational risks, which arise from inadequately controlled processes or systems, human error or non-compliance as well as from external events. Operational risks include reputation and regulatory risks, such as compliance.

The Aviva Group monitors risk on an ongoing basis and prepares quarterly reports identifying all material risks, along with information on likelihood, severity and mitigating actions taken or planned. This enables the Aviva Group to assess its overall risk exposure against local and global risk appetites, identify any concentrations of risk that may exist, and to identify where risks lie outside risk appetite and mitigating action is required or risk appetite requires revision in light of changing market conditions.

The Aviva Group risk management framework is designed to measure, rather than eliminate, the risk of failure to achieve business objectives and can provide only reasonable assurance against material financial misstatement or loss. New risks or risks currently considered immaterial may also impair the future achievement of business objectives.

The Aviva Group recognises the critical importance of having an efficient and effective risk management framework in place. To this end, the Aviva Group has an established governance framework, which has the following key elements:

- Defined terms of reference for the legal entity Boards and the associated executive management and other committees within the Aviva Group;
- A clear organisational structure with documented delegated authorities and responsibilities from the legal entity Boards to executive management committees and senior management;
- Adoption of the Aviva Group policy framework that defines risk appetite measures and sets out risk management and control standards for the Group's worldwide operations. Each policy has a member of senior management who is charged with overseeing compliance with the policy throughout the Aviva Group. The policies also set out the roles and responsibilities of businesses, regions, policy owners and risk oversight committees; and
- A risk management function operating throughout the Aviva Group, from Aviva Group Centre, to regional support offices, to business units, with clear responsibilities and objectives.

## Notes to the financial statements continued

### 28. Risk management continued

The adoption of Aviva Group policies enables a consistent approach to management of risk at a business unit level. The Aviva Group operates a number of oversight committees that monitor aggregate risk data and take overall risk management decisions.

The Aviva Group has also developed a framework, using Individual Capital Assessment ("ICA") principles, for quantifying the impact of risks on economic capital. The ICA combines the results of financial and operational risk stress tests. The results of modelling are incorporated into key strategic planning and decision making processes. The FSA also requires the Aviva Group and the Company to assess its economic capital requirements to ensure that it adequately reflects the business and control risks.

#### (a) Market risk

Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments from fluctuations in interest rates, equity prices, property prices and foreign currency exchange rates. Market risk arises due to credit spread widening, and fluctuations in both the value of liabilities and the value of investments held.

Market risk is managed locally within the Aviva Group market risk framework, within local regulatory constraints and in line with established Aviva Group policy, including minimum principles for matching liabilities with appropriate assets.

The Aviva Group's insurance operations are subject to numerous local regulatory requirements that prescribe the type, quality, and concentration of investments, and the level of assets to be maintained in local currency in order to meet local insurance liabilities. These requirements help to maintain market risk at an acceptable level in each of the jurisdictions in which the Aviva Group operates.

For each of the major components of market risk, described in more detail below, additional policies and procedures are in place to set out how each risk should be managed and monitored, and the approach to setting an appropriate risk appetite.

Equity price risk	The Company is subject to equity price risk due to daily changes in the market values of its equity securities portfolio. Equity price risk is actively managed in order to mitigate potential unfavourable market movements and includes using a variety of derivative instruments, including futures and options.
Interest rate risk	Sensitivity to changes in equity prices is given in section (g) below. Interest rate risk arises primarily from the Company's investments, fixed income securities and other liabilities, which are exposed to fluctuations in interest rates. The Company maintains a close matching of assets and liabilities by duration, using derivative instruments if necessary, to minimise this risk.
Currency risk	Sensitivity to changes in interest rates is given in section (g) below. The Company has minimal exposure to currency risk, other than through the fair value of overseas subsidiaries.
Derivatives risk	Derivatives are used within policy guidelines agreed by the Aviva plc Board of Directors and in line with Group policy. Derivatives are only used for efficient investment management, asset and liability management or risk hedging purposes.

The fair values of investments in subsidiaries are estimated using applicable valuation models, underpinned by the Aviva Group's market capitalisation. This uses a three month rolling average of the Aviva Group's share price and is, therefore, sensitive to movements in that price.

## Notes to the financial statements continued

### 28. Risk management continued

#### (b) Credit risk

Credit risk is the risk of loss in the value of financial assets due to counterparties failing to meet all or part of their obligations.

The Company's management of credit risk is carried out in accordance with the Aviva Group credit risk processes, which include setting exposure limits and monitoring exposures in accordance with ratings set by credit ratings agencies such as Standard & Poor's.

Financial assets are graded according to current credit ratings issued. AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB ratings. Financial assets which fall outside this range are classified as speculative grade. Credit limits for each counterparty are set based on default probabilities that are in turn based on the rating of the counterparty and the type of exposure.

The Company has significant financial exposure to amounts due from its parent, Aviva plc, and fellow Aviva group companies. The credit risk arising from Aviva group counterparties failing to meet all or part of their obligations is considered remote. Due to the nature of the intra-group loans, and the fact that these loans are settled, and not traded, the Company is not exposed to the risk of changes to the market value caused by changing perceptions of the credit worthiness of such counterparties.

The following table provides information regarding the aggregated credit risk exposure for financial assets with external credit ratings. 'Non-rated' captures assets not rated by external ratings agencies.

As at 31 December 2009	Credit rating						Total
	AAA	AA	A	BBB	Speculative grade	Non-rated	
	%	%	%	%	%	%	£m
Debt securities	45.7%	16.9%	23.0%	8.6%	0.4%	5.4%	538
Reinsurance assets	22.7%	58.5%	2.9%	-	-	15.9%	242

As at 31 December 2008	Credit rating						Total
	AAA	AA	A	BBB	Speculative grade	Non-rated	
	%	%	%	%	%	%	£m
Debt securities	33.4%	25.1%	30.5%	10.2%	0.2%	0.6%	521
Reinsurance assets	24.1%	53.8%	18.2%	0.3%	-	3.6%	340
Loans	-	-	-	-	-	100%	12

The Company is not generally exposed to significant concentrations of credit risk due to compliance with the FSA's regulations limiting investments in individual assets and classes.

The Company manages exposure to reinsurance counterparties in accordance with Group policy. Exposure limits are set by the Group Approvals Committee which maintains a list of reinsurers that have acceptable credit standing. Reinsurer exposure and the impact of any reinsurer default are monitored regularly.

The company's largest reinsurance counterparty is HSBC Reinsurance Ltd. At 31 December 2009, the reinsurance asset recoverable from HSBC Reinsurance Ltd was £124 million. At 31 December 2008 the company's largest reinsurance counterparty was Munich Reinsurance Company (including subsidiaries). At 31 December 2008, the reinsurance asset recoverable from Munich Reinsurance Company was £157 million. This exposure is monitored on a regular basis with the forecast to completion monitored for any shortfall in the claims history to verify that the contract is progressing as expected and that no further exposure for the Group will arise.

The Company's maximum exposure to credit risk is equal to the carrying value of assets in the statement of financial position plus financial guarantees given to other group companies, outlined in note 24(d).

## Notes to the financial statements continued

### 28. Risk management continued

The credit quality of receivables and other financial assets is monitored by the Company, and provisions for impairment are made for irrecoverable amounts. The following table provides information regarding the carrying value of financial assets that have been impaired and the ageing of financial assets that are past due but not impaired:

31 December 2009	Neither past due nor impaired	Financial assets that are past due but not impaired				Carrying value of impaired financial assets	Total
		0 – 3 months	3 – 6 months	6 months – 1 year	Greater than 1 year		
		£m	£m	£m	£m		
Debt securities	535	-	-	-	-	3	538
Reinsurance assets	242	-	-	-	-	-	242
Loans	-	-	-	-	-	-	-
Receivables and other financial assets	5,018	-	-	-	-	-	5,018

31 December 2008	Neither past due nor impaired	Financial assets that are past due but not impaired				Carrying value of impaired financial assets	Total
		0 – 3 months	3 – 6 months	6 months – 1 year	Greater than 1 year		
		£m	£m	£m	£m		
Debt securities	518	-	-	-	-	3	521
Reinsurance assets	340	-	-	-	-	-	340
Loans	12	-	-	-	-	-	12
Receivables and other financial assets	5,645	-	-	-	-	3	5,648

Receivables and other financial assets include loans and amounts due from other group companies.

There were no material financial assets that would have been past due or impaired had the terms not been renegotiated.

#### (c) General insurance risk

The Company's insurance business is managed within a group of companies, "UKGI", undertaking insurance business and other non-insurance business in the UK. The Company considers insurance risk within its general insurance activity to comprise the following:

- Inaccurate pricing and selection of risks when underwritten;
- Fluctuations in the timing, frequency and severity of claims and claim settlements relative to expectations;
- Unexpected claims arising from a single source;
- Inadequate reinsurance protection or other risk transfer techniques; and
- Inadequate reserves.

The majority of the general insurance business underwritten by the Company is of a short-tail nature such as motor, household and commercial property insurances.

The Aviva Group's underwriting strategy and appetite is agreed by the Aviva Group Executive Committee and communicated via specific policy statements and guidelines. The Company also sets its own underwriting strategy, consistent with the Group version. The vast majority of the Company's general insurance business is managed and priced in the same country as the domicile of the customer, predominantly in the UK.

The Company has developed mechanisms that identify, quantify and manage accumulated exposures to contain them within the limits of the appetite of the Company. The Company has in place various methodologies to manage effectively exposures arising from specific perils. The Company analyses accumulations of insurance risk under various headings, including type of business, location, profile of customers and type of claim and uses these analyses to inform underwriting and reserving.

## Notes to the financial statements continued

### 28. Risk management continued

Reinsurance purchases are reviewed to verify that the levels of protection being bought reflect any developments in exposure and the risk appetite of the Company. The basis of these purchases is underpinned by extensive financial and capital modelling and actuarial analysis to optimise the cost and capital efficiency benefits. This involves utilising externally sourced probabilistic models to verify the accumulations and loss probabilities based on the Company's specific portfolios of business. In addition to external models, scenarios are developed and tested using the Company's data to determine the potential losses and appropriate levels of reinsurance protection. Reinsurance covers single large exposures and concentrations of exposures. The Company has processes in place to manage catastrophe risk and purchases catastrophe reinsurance to protect against significant natural hazard events. For a single realistic catastrophic event, UKGI's maximum retention is approximately £235 million.

The adequacy of the Company's general insurance claims provisions is overseen by a Reserving Committee. Actuarial claims reserving is conducted by the Company's actuaries in compliance with the Group General Insurance Reserving policy. There are periodic external reviews by consultant actuaries.

Risk-based capital models are being used to support the quantification of risk under the ICA framework. The Company undertakes a quarterly review of insurance risks, the output from which is a key input into the ICA and risk-based capital assessments.

#### (d) Liquidity risk

The Company has set its investment strategy to ensure it has sufficient liquid funds to meet its expected obligations as they fall due. In extreme circumstances, the Company would approach the Aviva Group for additional short-term borrowing whilst the Company liquidated other assets. The Aviva Group maintains significant committed borrowing facilities from a range of highly-rated banks to mitigate this risk further.

The following table provides an analysis, by maturity date of the principal, of the carrying value of financial assets and reinsurers' share of unearned premium provisions, which are available to fund the repayment of liabilities as they crystallise:

	Total £m	On demand or within 1 year £m	1-5 years £m	Over 5 years £m	No fixed term (perpetual) £m
Debt securities	538	43	224	271	-
Equity securities	5	-	-	-	5
Other investments	10	10	-	-	-
Reinsurance assets	242	116	84	42	-
Receivables and other financial assets	5,018	5,018	-	-	-
Cash and cash equivalents	103	103	-	-	-
	5,916	5,290	308	313	5

The assets above are analysed in accordance with the earliest possible redemption date of the instrument at the initiation of the Company. Where an instrument is puttable back to the issuer on demand, such as a unit trust or similar type of investment vehicle, it is included in the "On demand or within 1 year" column. The Company's equity securities represent a strategic investment and, therefore, cannot be readily sold.

As explained in note 1(b), comparative information for the disclosures required by the IFRS 7 amendments is not needed in the first year of application and so no table for 2008 is presented above.

For insurance contracts, the analysis of liabilities below is based on the estimated timing of future cash flows.

The following table shows the Company's general insurance liabilities analysed by duration:

	Total £m	Within 1 year £m	1-5 years £m	5-15 years £m	Over 15 years £m
2009	2,468	1,223	1,020	131	94
2008	2,731	1,415	1,140	176	-

## Notes to the financial statements continued

### 28. Risk management continued

#### (e) Strategic risks.

The Company is exposed to a number of strategic risks. The Company's strategy needs to support its vision, purpose and objectives and be responsive to both the external and internal environment, for example changes in the competitive landscape arising from economic conditions, customer demands and competitor activity, regulatory changes, merger and acquisition opportunities and emerging trends (such as climate change, pandemic events and improving longevity).

Strategic risk is explicitly considered throughout the Company's strategic review and planning process. Developments are assessed during the quarterly performance management process where all aspects of the risk profile are considered.

The Company actively engages with external bodies to share the benefits of its expertise in supporting responses to emerging risks as well as challenging developments that could be damaging to the business and the industry as a whole.

#### (f) Operational risk

Operational risk is the risk of loss, resulting from inadequate or failed internal processes or systems or from external events. Operational risk includes reputation and regulatory risks, such as compliance. Only financial instrument risk requires quantification under IFRS and consequently no quantification of this risk is provided.

The Company is responsible for identifying and managing operational risks in line with minimum control standards set out in Group policies. Each operational risk is assessed by considering the potential impact and the probability of the event occurring. Impact assessments are considered against financial, operational and reputational criteria. Business management teams must be satisfied that all material risks falling outside the Group's risk appetite are being mitigated, monitored and reported to an acceptable level.

The Aviva Group risk management function is responsible for ensuring implementation of the Aviva Group risk management methodologies and frameworks to assist line management in this work. It also provides support and independent challenge on the completeness, accuracy and consistency of risk assessments and the adequacy of mitigating action plans.

As a consequence of the above, executive management satisfies itself that material risks are being mitigated and reported to an acceptable level.

#### (g) Risk and capital management

The Aviva Group uses a number of risk management tools to understand the volatility of earnings, the volatility of its capital requirements, and to manage its capital more efficiently. Primarily, risk-based capital models and scenario tests are used. Sensitivities to economic and operating experience are regularly produced on financial performance measurements to inform the Aviva Group's decision making and planning processes and quantifying the risks to which the Aviva Group is exposed.

General insurance claims liabilities are estimated by using standard actuarial claims projection techniques. These methods extrapolate the claims development for each accident year based on the observed development of earlier years. In most cases, no explicit assumptions are made as projections are based on assumptions implicit in the historic claims development on which the projections are based. As such, in the analysis below, the sensitivity of general insurance claims liabilities is primarily based on the financial impact of changes to the reported loss ratio.

Some results of sensitivity testing for the Company's business are set out below. For each sensitivity test the impact of a change in a single factor is shown, with other assumptions left unchanged.

<b>Sensitivity factor</b>	<b>Description of sensitivity factor applied</b>
Interest rate and investment return	The impact of a change in market interest rates by $\pm 1\%$ (e.g. if a current interest rate is 5%, the impact of an immediate change to 4% and 6%). The test allows consistently for similar changes to investment returns and movements in the market value of fixed interest securities.
Equity / property market values	The impact of a change in equity/property market values by $\pm 10\%$ .
Expenses	The impact of an increase in expenses by 10%.
Gross loss ratios	The impact of an increase in gross loss ratios for general insurance business by 5%.

## Notes to the financial statements continued

### 28. Risk management continued

The above sensitivity factors are applied using actuarial and statistical models. The impacts are shown in the tables below.

Pre-tax impacts on profit and shareholder's equity at 31 December 2009:

#### Impact on profit before tax (£m)

	Interest rates +1%	Interest rates -1%	Equity / Property +10%	Equity / Property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	(5)	5	-	-	(25)	(40)
Net of reinsurance	(10)	10	-	-	(25)	(40)

#### Impact before tax on shareholder's equity (£m)

	Interest rates +1%	Interest rates -1%	Equity / Property +10%	Equity / Property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	(5)	5	-	-	(5)	(40)
Net of reinsurance	(10)	10	-	-	(5)	(40)

Pre-tax impacts on profit and shareholder's equity at 31 December 2008:

#### Impact on profit before tax (£m)

	Interest rates +1%	Interest rates -1%	Equity / Property +10%	Equity / Property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	-	-	-	-	(35)	(40)
Net of reinsurance	(5)	5	-	-	(35)	(40)

#### Impact before tax on shareholder's equity (£m)

	Interest rates +1%	Interest rates -1%	Equity / Property +10%	Equity / Property -10%	Expenses +10%	Gross loss ratios +5%
Gross of reinsurance	-	-	-	-	(5)	(40)
Net of reinsurance	(5)	5	-	-	(5)	(40)

Due to the importance of reinsurance, the impact of sensitivities on profit and equity is shown gross and net of reinsurance. For general insurance, the impact of the expense sensitivity on profit also includes the increase in ongoing administration expenses, in addition to the increase in the claims handling expense provision.

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Company's assets and liabilities are actively managed. Additionally, the financial position of the Company may vary at the time that any actual market movement occurs. For example, the Company's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action.

## Notes to the financial statements continued

### 28. Risk management continued

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Aviva Group's view of possible near-term market changes that cannot be predicted with any certainty, and the assumption that all interest rates, equity prices and property values move in an identical fashion.

Assets are held at fair value in accordance with the relevant accounting policy. The majority of such assets are valued based on quoted market information or observable market data. A small percentage of total assets recorded at fair value are based on estimates. Where estimates are used, these are based on a combination of independent third party evidence and internally developed models, calibrated to market observable data where possible. Whilst such valuations are sensitive to estimates, it is believed that changing one or more of the assumptions to reasonably possible alternative assumptions would not significantly change the fair value.

### 29. Derivative financial instruments

The Company uses a variety of derivative financial instruments, including both exchange traded and over-the-counter instruments, in line with our overall risk management strategy. The objectives include managing exposure to price, foreign currency and/or interest rate risk on existing assets or liabilities, as well as planned or anticipated investment purchases.

In the table below, figures are given for both the notional amounts and fair values of these instruments. The notional amounts reflect the aggregate of individual derivative positions on a gross basis and so give an indication of the overall scale of the derivative transaction. They do not reflect current market values of the open positions. The fair values represent the gross carrying values at the year end for each class of derivative contract held (or issued) by the Company.

The fair values do not provide an indication of credit risk, as many over-the-counter transactions are contracted and documented under ISDA (International Swaps and Derivatives Association Inc) master agreements or their equivalent. Such agreements are designed to provide a legally enforceable set-off in the event of default, which reduces credit exposure. In addition, the Company has in place collateral agreements between the Company and relevant counterparties.

The Company had no cash flow or fair value hedges at 31 December 2009 (2008: nil).

The Company's non-hedge derivative activity at 31 December 2009 was as follows:

	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m	Contract/ notional amount £m	Fair value asset £m	Fair value liability £m
<b>Equity/Index contracts</b>						
OTC						
Options	1,470	10	-	1,315	144	(47)
<b>Totals at 31 December</b>	<b>1,470</b>	<b>10</b>	<b>-</b>	<b>1,315</b>	<b>144</b>	<b>(47)</b>

The fair value of the Company's derivatives was £144 million as at 31 December 2008. During the year, the Company purchased and sold a number of equity options in order to hedge market exposure. The realised losses incurred on these options was £227 million, due to the expiration of the options, and the unrealised losses for the year on those options that remained open at 31 December 2009 was £38 million.

Fair value assets are recognised as 'Derivative financial instruments' in note 10. Fair value liabilities are recognised as 'Other financial liabilities' in note 22.

The contractual undiscounted cash flows in relation to non-hedge derivative liabilities have the following maturities:

	2009 £m	2008 £m
Within one year	-	47
<b>Total</b>	<b>-</b>	<b>47</b>

## Notes to the financial statements continued

### 30. Related party transactions

#### (a) The Company had the following related party transactions in 2009 and 2008:

The Company receives dividend and interest income from, and pays dividends and interest to parent companies, subsidiaries and fellow subsidiaries in the normal course of business. These activities are reflected in the tables below.

##### (i) Services provided to related parties

		2009		2008
	Income earned in year £m	Receivable at year end £m	Income earned in year £m	Receivable at year end £m
Immediate parent	-	687	-	-
Subsidiaries	909	3,917	908	5,219
Other Aviva Group companies	-	13	-	22
	909	4,617	908	5,241

The related parties' receivables are not secured and no guarantees were received in respect thereof. The receivables will be settled in accordance with normal credit terms.

Income earned includes £909 million (2008: £908 million) relating to dividends received.

##### (ii) Services provided and expenses recharged by related parties

		2009		2008
	Services provided/ expenses recharged in year £m	Payable at year end £m	Services provided/ expenses recharged in year £m	Payable at year end £m
Immediate parent	-	-	-	665
Subsidiaries	194	36	233	21
Other Aviva Group companies	2	157	1	143
	196	193	234	829

Services provided include £2 million (2008: £1 million) investment management fees payable to fellow subsidiaries.

Expenses recharged represent £194 million (2008: £233 million) management charges payable to Aviva Insurance UK Limited, a subsidiary of the Company.

The related parties' payables are not secured and no guarantees were received in respect thereof. The payables will be settled in accordance with normal credit terms.

##### (b) Key management compensation

The Company bears costs of £1 million (2008: £1 million) in relation to key management compensation as the majority of such costs are borne by Aviva plc and Aviva Insurance UK Limited and are not recharged to the Company. Please refer to the financial statements of Aviva plc and Aviva Insurance UK Limited for the IAS24 disclosures in relation to management compensation.

##### (c) Parent entity

The immediate parent undertaking is Aviva International Insurance Limited, registered in the UK.

##### (d) Ultimate controlling entity

The Ultimate controlling entity is Aviva plc. Its Group Financial Statements are available on application to the Group Company Secretary, Aviva plc, St Helen's, 1 Undershaft, London EC3P 3DQ.