Sunderland Marine Mutual Insurance Company Limited

Registered Number: 16432

Directors' Report and Financial Statements

Year Ended 31st December 2010

CONTENTS **PAGE**

Sunderland Marine Mutual Insurance Company Limited
Company Information
Year Ended 31st December 2010

Registered Office	Salvus House Aykley Heads Durham DH1 5TS
Auditor	KPMG Audit Plc Quayside House 110 Quayside Newcastle upon Tyne NE1 3DX
Bankers	Barclays Bank Plc 1 Park Row Leeds LS1 5WU

The directors present their report and financial statements for the year ended 31st December 2010

Status

The company is a mutual company limited by guarantee without share capital

Principal activities

The company carries on the business of insurance against marine and war risks and risks incidental to marine insurance, including protection and indemnity risks, of vessels in which the members of the company are interested

The company also carries on the business of insurance against risks incidental to aquaculture

Inward reinsurance in respect of marine and aquaculture risks is also accepted

The principal activities of the company's subsidiaries are marine reinsurance and insurance broking

BUSINESS REVIEW

Forward looking statements

This business review contains statements on the company's outlook for the future By their nature such statements involve uncertainties as they relate to future events and these may be affected materially by a variety of existing factors, both economic and market based

Strategy

The company's objectives are to provide protection to policyholders where the scope of cover has been tailored to meet specific needs, and to achieve and maintain the highest standards of service

This requires cover to be provided at an economic premium which is fair and reasonable to cover both the attendant risks and other costs of the company as are relevant from time to time and to provide a timely and informed response in resolving the losses of policyholders

Stability and continuity are cornerstones of this strategy. Stability of financial strength to withstand market conditions and unforeseen events, and continuity of cover, membership, counterparty relationships and employees are all important elements in maintaining price and service stability in the company's niche markets

Markets

The company underwrites a variety of marine risks, including hull and machinery, protection and indemnity and personal accident as well as 'all risks' cover for the aquaculture industry

The portfolio of risks is well diversified within the marine portfolio in relation to size of vessel, fishery and service activity and within aquaculture by species

This diversification is further enhanced geographically The company's markets for marine are the UK (16 6%), North America (39 5%), Europe (14 2%), Australasia (19 5%), and others (10 2%), and for aquaculture they are UK (12 4%), North America (51 9%), Europe (11 2%), Australasia (10 3%), South America (13 7%) and others (0 5%)

Business environment

Competition has remained a key factor in many geographical areas during the year, primarily where price is focused on acquiring short-term market share Policyholder loyalty to the company and rates of renewal remain high

Over the course of the year Sterling weakened against the Canadian, Australian, New Zealand and United States Dollars whilst appreciating marginally against the Euro Changes in exchange rates affect the Sterling equivalent of underlying overseas figures reported within the financial statements The group, however, maintains assets in the currency of risk that are materially sufficient to meet its liabilities in that currency and therefore the net asset position is not significantly affected by alterations in currency conversion rates between Sterling and other currencies

Key performance indicators

The company's key financial performance indicators (KPIs) are those that communicate the financial performance and strength of the group as a whole to the company's members and counterparties These KPIs comprise -

- Written premium
- Combined ratio (net claims costs plus net operating expenses as a proportion of earned premium net of reinsurance)
- Loss ratio (net claims costs as a proportion of earned premium net of reinsurance)
- Expense ratio (net operating expenses as a proportion of earned premium net of reinsurance)
- Operating performance before investment return
- Investment return
- Solvency margin (free reserves as a proportion of earned premium net of reinsurance)

Group performance

The group's written premium of £73,747,000 reflects a reduction of 4 0% from £76,786,000 in 2009. Taking out the currency effect the reduction, in real terms, was 7.7%

Operating performance remained satisfactory under difficult trading conditions with a technical underwriting deficit of £360,000 (2009 £677,000) Positive investment return in the non-technical account of £3,336,000 (2009. £5,761,000) produced a surplus before tax of £2,976,000 (2009 £5,084,000) Net of tax the surplus was £2,555,000 (2009 £4,449,000)

Net operating expenses decreased but the expense ratio increased to 39 1% (2009 36 9%) reflective of lower net premium income The combined ratio was 104 2% (2009 104 5%).

Marine

The marine division accounted for 81 1% of written premiums in 2010 (2009. 85 2%)

The business is written worldwide Protection and indemnity business has a US and European bias and personal accident has a UK and Australian bias

Marine written premium reduced by £5,643,000 mainly due to the strategic withdrawal from French Polynesia and parts of South America

Retained written premium continued with moderate increases in a number of areas Hull rates were increased by 3-5% in the UK, Australia, New Zealand, Holland and parts of the USA even against a backdrop of domestic competition in the respective countries in question P&I premium increases of 5-10% were also achieved in the UK, Ireland and Australia along with smaller increments in the company's Spanish portfolio. Retention rates were again very high - with the global average exceeding 95%.

Sustainability is increasingly important as the fishing industry and governments strive to ensure there is a sustainable industry for future generations of fishermen The success of fisheries management is vital to protect stocks and ensure the viability of the industry For those that have adapted, many reported strong results in 2010 Working with key partners, our non-fishing vessel portfolio continues to grow and represents over 30% of direct vessels insured by the company

Direct marine business written in 2010 is protected by a quota share reinsurance contract The effects of this contract are to increase outward reinsurance premiums, reinsurance commissions and reinsurers' share of claims incurred in the income and expenditure account and to increase reinsurers' share of technical provisions in the consolidated balance sheet

Aquaculture

The aquaculture division accounted for 18 9% of gross written premium in 2010 (2009· 14 8%)

Written premiums increased by 14 8% in real terms A relatively static risk profile was retained for 2010, reflecting the company's wish to consolidate the portfolio following significant business movements, effected during 2009 in response to worsening experience in areas such as Chile Apart from a sudden and unexpected increase in claims due to sea lice, the underlying trend remained positive with lower seasonal losses from blooms, disease and storms The sea lice problem has been brought under control once again through timely intervention by the farm operators assisted by an increasing understanding of the need for support on the part of regulators

Stability has returned to the tuna market, allowing the company to tentatively and strategically increase its market share, but only to a modest extent until a market trend is firmly established

2010 was characterised in the industry by continuing capital investment, mergers and takeovers, but on this occasion from an unexpected direction, that of processors buying into the producer market It is a feature the company is following with great interest This has been a driver to further consolidation of the salmon industry which we expect to continue throughout 2011

Investment return

The company's investment portfolio structure has changed little during 2010 Underlying asset allocation remains heavily weighted toward bond investment

The board has maintained the cautious investment strategy initiated in 2009 with emphasis placed on capital preservation and stable income generation

The portfolio has generated a satisfactory investment return of £3,336,000 (2009 £5,761,000) This is above that anticipated and is reflective of the further compression of bond yields during the year

Investment risk is monitored closely to ensure it remains within the budget set by the board The risk budget is likely to remain at current low levels during 2011 It follows that a lower investment return should be expected given high bond investment weighting and the current level of bond yields

Capital structure and solvency

The company's markets and structure require it to meet regulatory capital requirements in eight jurisdictions and to report to fourteen different supervisory authorities around the world

The company's primary regulator is the UK's Financial Services Authority (FSA), under whose auspices the capital regime for regulated insurance businesses continues to evolve with Enhanced Capital Requirements (ECR), Individual Capital Assessments (ICA) and Individual Capital Guidance (ICG) The company has developed a framework using the Financial Services Authority's ICA principles to identify risks that business units and the company as a whole are exposed to and quantify their impact on economic capital The company continues to develop financial modelling and other tests to calculate and maintain capital required at a 99 5% confidence level

The company, its branches and subsidiaries all satisfy existing regulatory requirements The company's capital structure is considered appropriate to support the group's business needs for the foreseeable future

The company monitors capital adequacy across the group by reference to FSA requirements, and to the published solvency margin, being the ratio of its capital and reserves to earned premiums net of reinsurance

The solvency margin has strengthened this year from 71 9% in 2009 to 94 5% in 2010 The increase in the ratio during 2010 is due to the fall in net earned premium, as a result of new reinsurances taken out in the year

The total capital and reserves of the group are £46,030,000 compared with £43,664,000 at 31st December 2009 The reserve fund of the company is £26,007,000 (2009. £26,007,000) and the surplus retained in the income and expenditure account of the group is £19,823,000 (2009 £17,322,000)

The company is working towards Solvency II and has developed a timetable for review and development of its governance, risk management and capital systems to ensure that compliance is achieved by the implementation date

Mutuality and policy years

The company does not have investors to whom dividends are paid or from whom additional capital would be sought in the event that it is required Should additional capital be required the company could, as one of its options, seek contributions from its members on its current open policy years The company's policy is not to attract additional capital either from members or the financial markets, preferring to accumulate and deploy capital through its own business acumen

It is accordingly the company's policy to charge premiums that it is estimated will meet the net claims, reinsurance premiums, expenses and other costs and commitments of each year

Cash flow

Operations utilised £7,145,000 of cash (2009 £1,869,000)

Portfolio investments decreased by £1,687,000 (2009 increase £2,556,000) Deposit and short-term cash holdings were reduced by £7,639,000 (2009 decrease £10,811,000)

Employees

The company aims to attract, develop, retain and motivate high quality staff The growth and development of the company and the number of employees, including senior staff, with long service records is testament to the success of this objective

Risk management

The risks, related uncertainties and details on how the company mitigates these risks are summarised below and reported in more detail in note 1 to the financial statements

The primary objective of the company's risk management framework is to protect the group from events that hinder the achievement of service objectives and financial performance Details of the company's governance framework are given in the directors' report on corporate governance on pages 11 to 16

The principal risks and uncertainties facing the group are summarised below

Insurance contracts risk

Insurance contracts risk is the potential adverse financial impact if combined claims, acquisition and administrative costs exceed the amount of premium income earned

Market risk

Market risk is the potential adverse financial impact of changes to interest rates and equity prices

Credit risk

Credit risk is the potential adverse financial impact of loss in the value of financial assets due to counterparties (such as, but not limited to, insurance debtors, banks and reinsurers) failing to meet all or part of their obligations

Liquidity risk

Liquidity risk is the possibility that the company does not have sufficient available assets to meet obligations as they fall due

Operational risk

Operational risk arises as a result of inadequately controlled internal processes or systems, human error or from external events This definition is intended to include all other risks to which the company is exposed including, for example, information technology, information security, human resources, tax, legal, fraud, compliance risks, project management and outsourcing

Group risk

Group risk arises from the potential for adverse events in, or the failure of, one of the subsidiaries to affect the group as a whole

Directors

The directors of the company are shown below

In accordance with Article 38 of the Articles of Association the following directors retire by rotation

F J Mattera
C H D Venn*
W J J Crowe
P M Johnson
T F Hart

(* Not standing for re-election)

The table below shows the composition of the board and its committees at 31st December 2010

On the 30th June 2010 Mrs A J Alden, Mr T Rutter and Miss A C Vipond were appointed as directors On 22nd March 2011 Mr S W Taylor was appointed as a director In accordance with Article 41 of the Articles of Association, these four new directors will retire at the Annual General Meeting and offer themselves for re-election

A legend is shown in support of the table

* member of board or committee
c chairman of board or committee

Director	Board	Audit	Defence	Executive	Investment	Nomination	Remuneration	Risk	Security	Strategy
A J Alden (executive director - appointed 30 06 10)	*		*					*		
J Alford	*				*					
A D W Allan	*	c	*	*	*	*	*	*	*	*
P A Bobeff	*	*	*	*	*	c	*	*	*	*
J P Crichton	*		*					*		*
W J J Crowe	*	*								
T F Hart	c	*	c	*	*	*	c	c	c	c
C J Hilton	*		*					*		
P M Johnson	*	*			*					
A L Marr	*				c					
F J Mattera	*									
G C Parkinson (executive director)	*		*	c	*	*		*	*	*
T Rutter (executive director - appointed 30 06 10)	*									
P I Talley	*									
C H D Venn	*									
A C Vipond (executive director - appointed 30 06 10)	*		*					*		
D M Windmill	*	*								
S W Taylor (appointed 22nd March 2011)	*									

In addition to those persons shown above, Mr A S Blake (Corporate Treasurer) and Mr D McEuen are members of the investment committee

Directors' biographical details

Alison J. Alden (40)

Mrs Alden commenced employment with Sunderland Marine Mutual Insurance Company Limited in 2004 She was appointed to the board as an executive director on 30th June 2010. She is also a director of certain subsidiary companies She is a member of the Institute of Chartered Accountants in England and Wales She is the finance director of the company and is based in England

Jeremy D. Alford (48)

Mr Alford was appointed as a non-executive director of the company in 2009 He is also a director of the East Sussex Downs and Weald Primary Care Trust His involvement with the company began many years ago through his previous employment with Alliance Bernstein, London (of which he was senior vice president) and Whittingdale Holdings Ltd He is based in England

Alistair D. W. Allan (66)

Mr Allan was appointed as a non-executive director in 1986 and is also a director of certain subsidiary companies and joint ventures He is also a director of The Shipowners Mutual Protection and Indemnity Association and a member of the Institute of Chartered Accountants of Scotland He was previously managing director of Denholm Seafoods Limited, retiring from that position in 2004, and is based in Scotland

Peter A. Bobeff (69) Vice chairman

Mr Bobeff was appointed as a non-executive director in 1985 and as vice-chairman in 2007 He is, ex officio, a member of all board committees He was previously Senior Vice President Commercial Affairs of Foster's Group Limited, retiring in 2005, a director of the Global Foundation Group, Chairman of International House Council, University of Melbourne and on the advisory board of Visy Industries Group, retiring in 2009 He is based in Australia

J. Peter Crichton (62)

Mr Crichton was appointed as a non-executive director in 2008 He was previously joint managing director of North of England P&I Association, retiring in 2006 He continues to act as a consultant to it He is also a trustee of the Edward Lloyd Trust He is based in England

William J. J. Crowe (63)

Mr Crowe was appointed as a non-executive director in 2000 He is a self-employed consultant specialising in fish farming and European governance He is based in Scotland

Trevor F. Hart (66) Chairman

Mr Hart was appointed as a non-executive director in 2001 and appointed chairman in 2007 He is also a director of certain subsidiary companies and its joint ventures He is, ex officio, a member of all board committees He was previously a marine underwriter with a Lloyds' syndicate and is based in England

Christopher J. Hilton (60)

Mr Hilton was appointed as a non-executive director in 2008 and is also a company nominated trustee and chairman of the trustees of the company's pension scheme He was a partner in Eversheds LLP, retiring in 2010, but continues to act on a consultancy basis. He was also a director of Newcastle Building Society, retiring in 2010 He is a director of Newcastle Strategic Solutions Ltd and Graig Shipping plc and is chairman of NEPIA Employees Benefit Trust He is based in England

Peter M. Johnson (62)

Mr Johnson was appointed as a non-executive director in 2000 He is a self-employed chartered accountant, and was previously a senior partner of KPMG, Newcastle He is a director of Bellway plc, Honorary Treasurer of both the University of Newcastle upon Tyne and of St John Ambulance, Northumbria He is a Trustee of the Newcastle University Development Trust and a fellow of the Institute of Chartered Accountants in England and Wales He is based in England

Andrew L. Marr (68)

Mr Marr was appointed as a non-executive director in 1981 He is Chairman of Andrew Marr International Limited and its subsidiaries He is based in England

Frederick J. Mattera (59)

Mr Mattera was appointed as a non-executive director in 1998 He is a commercial fisherman and President of the Point Club. He is actively involved in marine safety training as head of NESTCo and is a director of the Commercial Fishing Vessel Safety Advisory Committee, US Coast Guard He is based in the USA.

Geoffrey C. Parkinson (55)

Mr Parkinson commenced employment with the company in 1972 He was appointed to the board as an executive director in 1993 He is also a director of certain subsidiary companies and joint ventures He is the Chief Executive Officer of the company and is based in England

Thomas Rutter (50)

Mr Rutter commenced employment with the company in 1979 He was appointed to the board as an executive director on 30th June 2010 He is the Aquaculture Manager of the company and is based in England

Peter I. Talley (65)

Mr Talley was appointed as a non-executive director in 1990 He is the Managing Director of Talley's Fisheries Limited and is based in New Zealand

Silas W. Taylor (58)

Mr Taylor was appointed as a non-executive director on 22nd March 2011. He was a partner in law firm Andrew Jackson, retiring in 2008, but continues to act on a consultancy basis He is based in England

Christopher H. D. Venn (68)

Mr Venn was appointed as a non-executive director in 1999 He is a director of Ovenstone Limited and is based in South Africa

Angela C. Vipond (38)

Miss Vipond commenced employment with Sunderland Marine Mutual Insurance Company Limited in 1990 She was appointed to the board as an executive director on 30th June 2010 She is also a director of certain subsidiary companies and joint ventures She is the Corporate Risk Manager of the company and is based in England

David M. Windmill (61)

Mr Windmill was appointed as a non-executive director in 1996

He was previously the Managing Director of Marine Harvest Limited He was also the Chief Executive of The Royal Zoological Society of Scotland, retiring in February 2011 He is the Honorary Consul General of Norway in Scotland and a trustee of the Great Steward of Scotland Dumfries House Trust He is based in Scotland

Directors' interests

Other than contracts of employment between the executive directors and the company, no director had a material interest at any time during the year in any contract of significance with the company or any of its subsidiary undertakings No director has an interest in the equity of subsidiary undertakings

Directors' and officers' insurance and directors' indemnities

The company has purchased and maintained throughout the year directors' and officers' liability insurance in respect of the company and its directors The directors are also entitled under the Articles of Association to be indemnified by the company against costs, charges, losses, expenses and liability incurred in the discharge of their duties, unless prohibited by statute

All directors benefited from qualifying third party indemnity provisions in place during the financial year and at the date of this report

Political and charitable contributions

The group made charitable contributions during the year totalling £9,000 (2009 £26,000) No political contributions were made (2009 £nil)

Payment of suppliers

The group's policy is to pay all of its creditors promptly and within the terms of the agreement made at the time of supply The amount owed to trade creditors at 31st December 2010 represented eight days of average daily purchases from suppliers during the year ended on that date

Going concern

The directors are satisfied that the group has adequate resources to continue in operational existence for the foreseeable future The going concern basis therefore continues to be adopted in preparing the accounts

Disclosure of information to auditors

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the company's auditors are unaware and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information

Auditors

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

By order of the board

A S Rowland
Secretary
23rd March 2011

Company registration number 16432

The combined code

The board is committed to a high standard of corporate governance.

The board considers that, except where stated, throughout the year ended 31st December 2010, the company has applied the relevant principles and complied with the relevant provisions of the UK Corporate Governance Code published in June 2010

The board

Composition and balance

The board at 31st December 2010 comprised the non-executive chairman, twelve non-executive directors and four executive directors The non-executive directors bring to bear knowledge, experience and an objective viewpoint to board decisions The vice chairman fulfils the role of senior non-executive director All the non-executive directors are independent There are a number of board members with service periods exceeding nine years, however each has been individually considered and is believed to remain independent in both character and judgement and, having no relationships that are relevant to such independence, their circumstances are not such as to require that their independent status should be altered Biographies of all the directors appear on pages 8 to 9 Membership of the board committees is set out on page 7 The board is satisfied that this balance and range of expertise, experience and qualifications is appropriate for the current needs of the business

Role

The board determines the group's

- strategy and objectives, and monitors the group's performance in achieving them,
- risk appetite,
- organisational structure, and
- remuneration policies

The board

- reviews the most significant risks affecting the group and the action being taken to manage or mitigate them,
- appoints directors and approves senior appointments,
- determines the responsibilities of the group chief executive and approves any delegation of his responsibilities to heads of business units or support functions,
- monitors and reviews the group's risk management policies and systems,
- determines the company's risk appetite,
- approves the annual report and accounts and significant regulatory returns, and
- reserves to itself certain decisions

These reserved decisions include

- the acquisition or disposal of any business or major asset, the setting-up of a new business or joint venture or the merging of any part of the group's business with a third party,
- investment policy,
- approval of significant claims; and
- approval of reinsurance arrangements

Beneath the board there is in place clear and appropriate apportionment of responsibilities amongst the executive directors and senior managers

How the board operates

The board meets five times a year, or more frequently, and ahead of these meetings the group chief executive circulates a report on the performance of the group and on any other material matters, both internal and external This includes operational and financial information and reports on how the group has performed against key indicators Reports are also provided on risk management and compliance matters

Board committees

The board has established audit, defence advisory, executive, investment, nomination, remuneration, risk, security and strategy committees

Audit committee

The members of the audit committee are shown on page 7 The committee meets at least twice a year, or more frequently if required, and its responsibilities include

- monitoring the integrity of the financial statements of the group, including their compliance with applicable laws and accounting standards, and any formal announcement relating to the group's financial performance,
- reviewing significant financial reporting judgements,
- monitoring and reviewing the group's internal financial controls and internal control systems, including those relating to the prevention of financial crime,
- reviewing the external auditor's management letters and management's response to them,
- reviewing reports from the compliance function and internal audit,
- making recommendations to the board for it to put to the members for their approval in general meeting in relation to the appointment of the external auditors and their remuneration,
- approving non-audit work provided by the external auditors and the fees for such work,
- reviewing and monitoring the external auditor's independence and objectivity and the effectiveness of the audit process, and
- reviewing whistle-blowing arrangements

The external auditors, the company's senior financial management, the corporate risk manager, general counsel, the compliance officer and the external manager of internal audit attend meetings of the committee as required

In complying with the combined code the board is satisfied that at least one member of the audit committee has recent and relevant financial experience

The committee meets with the external auditors without the executive directors or representatives of senior management present

Defence advisory committee

The members of the defence advisory committee are shown on page 7 The committee meets once a year or more frequently if required It advises the board on the group's defensive strategy

Executive committee

The members of the executive committee are shown on page 7 Meetings are held as circumstances require. The duties of the committee are to be available to the chief executive and to advise on matters relating to the management of the group requiring attention between board meetings The committee also considers other matters relating to the group upon which senior management may need guidance with a view to making recommendations to the board

Investment committee

The members of the investment committee are shown on page 7 The committee meets five times a year, or more frequently if required, and its responsibilities include

- recommending the asset allocation benchmarks, the performance objectives and the performance benchmarks for the group's funds,
- making recommendations to the board regarding guidelines for the management of foreign exchange exposure, and
- monitoring the investment performance of the group's funds

Nomination committee

The members of the nomination committee are shown on page 7 The committee meets at least once a year, or more frequently if required, and its responsibilities include

- reviewing the structure, size and composition (including the skills, knowledge and experience) of the board and its committees and making recommendations to the board with regard to any changes,
- nominating for board approval candidates to fill vacancies on the board and board committees,
- approving senior management recommendations for appointments to senior positions,
- succession planning - taking into account the challenges and opportunities facing the group and skills and expertise needed on the board in the future, and
- keeping under review the leadership needs of the organisation, both executive and non-executive, with a view to ensuring the continued ability of the organisation to compete effectively in the marketplace

Remuneration committee

The members of the remuneration committee are shown on page 7 and are all non-executive directors. The committee meets at least once a year, or more frequently if required, and its responsibilities include determining, for board approval, the policy for remunerating executive directors and other senior executives Non-executive directors' remuneration is determined by the board The committee also ensures that there is a coherent approach to remuneration in respect of all employees

Risk committee

The members of the risk committee are shown on page 7 The committee was formed in August 2010 and met once in the year In future years it will meet at least four times a year or more frequently if required The committee considers all aspects of high level risk which may impact on the business of the group and ensures that appropriate policies and procedures are in place to mitigate the effect of such risk

Security committee

The members of the security committee are shown on page 7 The committee meets at least once a year or more frequently if required It evaluates reinsurers, reinsurance intermediaries and other significant counterparties, thus ensuring that the company's exposure to the failure of a reinsurer, intermediary or other counterparty is kept to a minimum

Strategy committee

The members of the strategy committee are shown on page 7 The committee meets four times a year or more frequently if required It assists the board in relation to setting the company's strategy, risk appetite and specific corporate objectives This includes regular review of detailed financial and business plans

The terms of reference of all board committees are available on request

Meetings and attendance

Forum	Number of members	Attendance at Meeting						
		Feb	Mar	Jun	Aug	Sep	Nov	Dec
Board	14 (17 after 30 06 10)	11	14	14	-	14	-	16
Audit	6	-	4	-	-	-	5	-
Defence	6	-	6	-	-	-	-	-
Executive	4	-	-	-	-	4	-	4
Investment	7	7	7	7	-	6	-	6
Nomination	4	4	4	4	-	-	-	4
Remuneration	3	3	3	3	-	-	-	-
Risk	8	-	-	-	5	-	-	-
Security	4	-	4	-	-	-	-	-
Strategy	5	-	5	5	-	4	-	5

"-" denotes no meeting

Performance evaluation

The board has established a formal evaluation of its own performance, and that of its committees, individual directors and the chairman, which takes place on an annual basis This includes completion of questionnaires and face to face interviews Questionnaires are completed in respect of the performance of the board, its committees and the chairman The chairman carries out interviews and reviews the responses to the questionnaires relating to board performance and reports through the nomination committee to the board The review of responses relating to the chairman is the responsibility of the vice chairman, who is also the chairman of the nomination committee

Directors have the opportunity to update their skills and knowledge, either through presentations on key issues and developments within the industry or by attendance at internal and external training courses

The chairman meets periodically with the non-executive directors in the absence of the executive directors. Further, the non-executive directors met once during the year in the absence of the chairman, to appraise the chairman's performance

Internal control

The system of internal control

The group's internal control system encompasses policies, processes, behaviours and other aspects of the group that taken together

- facilitate the effective and efficient operation of the group by assisting it to respond appropriately to significant business, operational, financial, compliance and other risks that could impact upon the group's ability to meet its objectives, and

- are designed to ensure compliance with applicable laws, regulations and internal policies

The role of the board

The board is ultimately responsible for the group's system of internal control and for reviewing its effectiveness The system is designed to manage rather than eliminate the risks of failure to achieve business objectives and, inevitably, can provide only reasonable and not absolute assurance against material misstatement or loss The system has been in place throughout the period under review and accords with the Code

The board has conducted a review of the effectiveness of the group's system of internal control. This covered all material controls, including financial, operational and compliance controls, and risk management systems It was conducted in part on an ongoing basis, via the reports submitted (both routinely and on an ad hoc basis) to the board and the audit committee during the period under review, and also by reports prepared as part of the year-end process

The board has established a committee (the risk committee) to consider, monitor and review the ongoing process for identifying, evaluating and managing the significant risks faced by the group The management of each business unit and support function is responsible for identifying, evaluating, rating (in terms of probability of occurrence and likely impact), assigning responsibility for, reporting on, and managing and mitigating all risks relevant to its area of business, including the design and operation of suitable internal controls This is facilitated through the management risk committee, comprising key members of the senior executive management team and chaired by the corporate risk manager The committee meets monthly, or more frequently if required

Risk management

The group has a risk management function which, in conjunction with the board risk committee

- drafts risk policies and processes and develops the risk management framework,
- maintains and regularly updates a risk matrix that sets out all of the significant risks impacting on the group and scores them in terms of probability and impact;
- facilitates the risk management process by developing and monitoring the performance of risk tools and methodologies,
- reports and makes recommendations to the group chief executive and the board, via the Board Risk Committee, on, for example, the risk matrix and on the management of all categories of risk including whether adequate risk management systems are in place, key risks are being properly managed and whether changes should be made to the overall strategy for the management of risk, and
- assists with achieving the objective of embedding risk management throughout the group, and with managing risks impacting on the group and within the business units and support functions

Compliance

The group has a compliance department which

- monitors and enforces compliance with the requirements and rules of regulators,
- checks that systems and controls are in place to counter the risk that the group may be exposed to practices linked with financial crime,
- develops a compliance plan and undertakes work in accordance with the plan, and
- co-ordinates the group's relationships with its regulators

Internal audit

The group has an internal audit function, the management of which is outsourced, which.

- provides management and the audit committee with independent and objective assurance on, and evaluation of, the overall effectiveness of the group's internal systems and controls, and risk management and corporate governance processes,
- develops a three year strategic plan and an annual operating plan in conjunction with management and the audit committee,
- conducts audits in line with that plan or additionally where required, and
- includes recommendations within all audit reports and monitors the implementation of these recommendations

Further information on risk management is contained in the directors' report and note 1 to the financial statements

Relations with members

The company's website at www smmi co uk contains up to date information on the group The company pursues a policy of personal contact and wide dialogue with members Members can make contact in person, by writing to the Company Secretary, Sunderland Marine Mutual Insurance Company Limited, Salvus House, Aykley Heads, Durham, United Kingdom DH1 5TS or by email to mutual@smmi co uk

Members are encouraged to attend the Annual General Meeting, at which directors are present, and to ask questions Proxy voting is permitted at all general meetings of the company

By order of the board

A S Rowland
Secretary
23rd March 2011

This report has not been prepared in accordance with the provisions of the Companies Act 2006, section 421 and schedule 8 as the board feels that the structure and content of such a report is inappropriate to the company at the present time

Remuneration committee

The role of the remuneration committee is set out in the directors' report on corporate governance

External independent advice is provided as considered appropriate to the committee and the board on the remuneration of all directors and senior executives

Remuneration

Salaries and fees

The salaries and fees of all directors are determined by considering the individual's responsibility and the remuneration paid in companies of comparable size and nature

Fees are earned by directors in respect of their position and also in respect of their responsibilities as a member or as chairman of a board committee In the case of executive directors, a salary is paid in respect of day-to-day managerial and executive responsibilities.

Benefits

During the year benefits offered to the executive directors were private medical insurance and either a company car or a cash allowance

Pensions

The executive directors are all members of a defined benefit pension scheme Life assurance cover for death in service is provided for these directors and is four times pensionable earnings

Executive directors' service contracts

During the year the chief executive director had a contract of employment which provided for a year's notice from either party The chief executive director's contract does not include compensation for severance as a result of a change of control The employment contracts of the remaining three executive directors provided for notice periods of. Thomas Rutter - 12 months, Alison Alden - 6 months and Angela Vipond - 3 months

Non-executive directors

The letters of appointment for non-executive directors include provisions in respect of termination

The directors' remuneration is disclosed in note 6

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

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

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

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

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

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

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

Independent auditor's report to the members of Sunderland Marine Mutual Insurance Company Limited

We have audited the financial statements of Sunderland Marine Mutual Insurance Company Limited for the year ended 31 December 2010 set out on pages 20 to 67 The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice)

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

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 18, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www frc org uk/apb/scope/private.cfm

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31st December 2010 and of the group's surplus for the year then ended,
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or
- the parent company 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

Jonathan Holt (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
Quayside House
110 Quayside
Newcastle upon Tyne
NE1 3DX

23rd March 2011

Sunderland Marine Mutual Insurance Company Limited
Consolidated Income and Expenditure Account
Year Ended 31st December 2010

Technical account - general business

	Note		2010 £'000		2009 £'000
Earned premiums, net of reinsurance					
Gross premiums written			73,747		76,786
Outward reinsurance premiums			(32,947)		(16,538)
			40,800		60,248
Change in the gross provision for unearned premiums	25		1,826		272
Change in the provision for unearned premium, reinsurers' share	18		6,105		230
			7,931		502
			48,731		60,750
Claims incurred, net of reinsurance					
Claims paid					
Gross amount			(53,152)		(51,884)
Reinsurers' share			13,832		6,375
			(39,320)		(45,509)
Change in provision for claims					
Gross amount	25		5,936		(149)
Reinsurers' share	18		1,691		4,630
			7,627		4,481
			(31,693)		(41,028)
Net operating expenses before goodwill and purchase costs		(17,741)		(21,585)	
Goodwill and purchase costs		(1,335)		(854)	
Net operating expenses	5		(19,076)		(22,439)
Other operating income					
Brokerage income group and share of joint ventures		3,881		4,019	
Less share of joint ventures' brokerage income		(2,206)		(2,178)	
Group brokerage income			1,675		1,841
Share of joint venture operating profit			3		199
Balance on the technical account - general business			(360)		(677)

Sunderland Marine Mutual Insurance Company Limited
Consolidated Income and Expenditure Account (continued)
Year Ended 31st December 2010

Non-technical account – general business

	Note		2010 £'000		2009 £'000
Balance on the technical account - general business			(360)		(677)
Investment income	7		3,828		4,856
Unrealised (losses)/gains on investments	8		(31)		4,214
Investment expenses and charges	9		(461)		(3,309)
Operating surplus before goodwill and purchase costs		4,311		5,938	
Goodwill and purchase costs		(1,335)		(854)	
Operating surplus	10		2,976		5,084
Surplus on ordinary activities before tax	11		2,976		5,084
Tax on surplus on ordinary activities	13		(421)		(635)
Surplus on ordinary activities after tax			2,555		4,449
Minority interests			(107)		(103)
Surplus after taxation attributable to members of the parent company for the financial year			2,448		4,346

In accordance with the amendment to FRS 3 published in June 1999 no note of historical cost profits has been prepared as the group's only material gains and losses on assets relate to the holding and disposal of investments

The company has utilised the exemption within section 408 of the Companies Act 2006 and has therefore not published its own income and expenditure account

All results are derived from continuing operations

Sunderland Marine Mutual Insurance Company Limited
Consolidated Statement of Total Recognised Gains and Losses
Year Ended 31st December 2010

	Note	2010 £'000	2009 £'000
Group surplus for the financial year		2,448	4,346
Foreign exchange rate movements	24	58	(188)
Actuarial surplus/(deficit) on pension scheme	35	21	(1,471)
Property revaluation	15	(161)	-
Total gains recognised since the last annual report		2,366	2,687

Sunderland Marine Mutual Insurance Company Limited
Consolidated Balance Sheet
As at 31st December 2010

	Note		2010 £'000		2009 £'000
Assets					
Intangible assets					
Goodwill	14		5,234		6,759
Investments					
Land and buildings	15	8,583		8,791	
Investment in group undertakings and participating interests	16	714		776	
Financial assets					
- Equity securities at fair value through income	17	4,097		3,842	
- Debt securities at fair value through income	17	64,130		63,687	
- Derivatives at fair value through income	17	348		402	
- Deposits with credit institutions		9,521		11,862	
			87,393		89,360
Reinsurers' share of technical provisions					
Provision for unearned premiums	18	14,264		7,559	
Provision for unearned commission	18	(4,097)		(1,677)	
Claims outstanding	18	13,698		11,132	
			23,865		17,014
Debtors					
Debtors arising out of direct insurance operations	19	18,095		17,647	
Debtors arising out of reinsurance operations	20	5,914		2,334	
Other debtors	21	2,022		2,369	
			26,031		22,350
Other assets					
Tangible assets	22	1,366		611	
Cash and cash equivalents		2,637		5,912	
			4,003		6,523
Prepayments and accrued income					
Accrued interest and rent		812		940	
Deferred acquisition costs		4,079		4,514	
Other prepayments and accrued income		298		228	
			5,189		5,682
Total assets			151,715		147,688

Sunderland Marine Mutual Insurance Company Limited
Consolidated Balance Sheet (continued)
As at 31st December 2010

	Note		2010 £'000		2009 £'000
Liabilities					
Capital and reserves					
Reserves					
Revaluation reserve	23	200		335	
Other reserves: reserve fund	23	26,007		26,007	
Income and expenditure account accumulated surplus	23	19,823		17,322	
Total capital and reserves	24		46,030		43,664
Minority interest			301		305
Technical provisions					
Provision for unearned premiums. gross amount	25	32,110		31,879	
Claims outstanding. gross amount	25	50,945		54,438	
			83,055		86,317
Financial liabilities					
- Derivatives at fair value through income	27	227		343	
- Creditors arising out of direct insurance operations		1,984		1,915	
- Creditors arising out of reinsurance operations	28	8,350		2,786	
- Borrowings	29	6,755		6,365	
- Other creditors, including taxation and social security	30	2,831		2,623	
			20,147		14,032
Accruals and deferred income			1,288		2,107
			150,821		146,425
Pension liability	35		894		1,263
Total liabilities			151,715		147,688

These financial statements were approved by the board of directors on 23rd March 2011 and were signed on its behalf by

T F Hart

A J Alden

Company registration number 16432

Sunderland Marine Mutual Insurance Company Limited
Company Balance Sheet
As at 31st December 2010

	Note		2010 £'000		2009 £'000
Assets					
Investments					
Land and buildings	15	8,118		8,271	
Investments in group undertakings and participating interests	16	27,467		32,573	
Financial assets					
- Debt securities at fair value through income	17	21,529		14,103	
- Derivatives at fair value through income	17	88		39	
- Deposits with credit institutions		7,462		9,577	
			64,664		64,563
Reinsurers' share of technical provisions					
Provision for unearned premiums	18	29,388		26,576	
Provision for unearned commission	18	(8,889)		(6,535)	
Claims outstanding	18	46,321		49,067	
			66,820		69,108
Debtors					
Debtors arising out of direct insurance operations	19	17,942		17,431	
Debtors arising out of reinsurance operations	20	5,914		2,301	
Other debtors	21	1,130		1,048	
			24,986		20,780
Other assets					
Tangible assets	22	1,138		442	
Cash and cash equivalents		714		2,255	
			1,852		2,697
Prepayments and accrued income					
Accrued interest and rent		96		93	
Deferred acquisition costs		4,013		4,395	
Other prepayments and accrued income		272		214	
			4,381		4,702
Total assets			162,703		161,850

Sunderland Marine Mutual Insurance Company Limited
Company Balance Sheet (continued)
As at 31st December 2010

	Note		2010 £'000		2009 £'000
Liabilities					
Capital and reserves					
Revaluation reserve	23	20,201		17,402	
Other reserves reserve fund	23	26,007		26,007	
Income and expenditure account accumulated (deficit)/surplus	23	(210)		112	
Total capital and reserves	24		45,998		43,521
Technical provisions					
Provision for unearned premiums gross amount	25	31,339		31,189	
Claims outstanding: gross amount	25	50,717		54,259	
			82,056		85,448
Financial liabilities					
- Derivatives at fair value through income	27	182		306	
- Creditors arising out of direct insurance operations		2,072		1,925	
- Creditors arising out of reinsurance operations	28	22,948		17,412	
- Borrowings	29	6,148		5,216	
- Other creditors, including taxation and social security	30	1,380		5,419	
			32,730		30,278
Accruals and deferred income			1,025		1,340
			161,809		160,587
Pension liability	35		894		1,263
Total liabilities			162,703		161,850

These financial statements were approved by the board of directors on 23rd March 2011 and were signed on its behalf by

T F Hart

A J Alden

Company registration number: 16432

Sunderland Marine Mutual Insurance Company Limited
Consolidated Cash Flow Statement
Year Ended 31st December 2010

Operating activities	Note	2010 £'000	2009 £'000
Net cash outflow from operating activities	32	(7,145)	(1,869)
Dividends received from joint venture		95	122
Interest paid			
Bank interest paid		(252)	(349)
Taxation			
UK corporation tax recovered		104	37
Capital expenditure			
Purchase of tangible fixed assets		(1,055)	(163)
Sale of tangible fixed assets		62	37
Acquisition			
Acquisition of undertakings		-	(2,127)
Contingent consideration adjustment to goodwill		173	-
Financing			
Repayment of loan		(555)	(5,151)
Dividend paid by subsidiary undertaking		(105)	(51)
(Expense)/proceeds from settlement of derivatives		(648)	1,259
		(9,326)	(8,255)
Cash flows were invested as follows:			
Decrease in cash holdings	33	(7,639)	(10,811)
Portfolio investments			
Purchase of property		-	538
Purchase of equity securities at fair value through income		-	193
Purchase of debt securities at fair value through income		94,885	69,442
Sale of equity securities at fair value through income		(29)	(17,136)
Sale of debt securities at fair value through income		(96,543)	(50,481)
Net investment of cash flows		(9,326)	(8,255)
Movement in opening and closing portfolio investments net of financing			
Net cash outflow for year		(7,639)	(10,811)
Cash flow - portfolio investments		(1,687)	2,556
- decrease in loans		555	5,151
Movement arising from cash flows	33	(8,771)	(3,104)
Changes in market values and exchange rate effects	33	3,255	1,603
Total movement in portfolio investments net of financing		(5,516)	(1,501)
Portfolio investments net of financing at 1st January		87,729	89,230
Portfolio investments net of financing at 31st December	33	82,213	87,729

1. Accounting policies

Basis of presentation

The following accounting policies have been applied consistently in dealing with items which are considered material to the group's financial statements, except as noted below

The financial statements have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice The financial statements have been prepared on the historical cost basis except that certain investments have been revalued Derivative financial instruments and financial assets at fair value through income are measured at fair value

The financial statements have been prepared in accordance with the provisions of Section 396 of Companies Act 2006 and with the Association of British Insurers' Statement of Recommended Practice on Accounting (ABI SORP) for Insurance Business dated December 2005 (as amended December 2006)

The group's business activities, performance and financial position are set out in the directors' report and financial statements The company's objectives, policies and processes for managing risk and capital are shown below

The company has considerable financial resources, a portfolio well diversified both by product and geographical area together with a robust reinsurance programme As a consequence, the directors believe that the company is well placed to manage its business risks successfully despite the current uncertain economic outlook

The directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future They thus continue to adopt the going concern basis of accounting in preparing the annual financial statements

Use of estimates and judgements

The preparation of the financial statements requires judgements and estimates to be made and assumptions to be used that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses Actual results may vary from the estimates

Estimates and the underlying assumptions are reviewed on an ongoing basis Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Certain critical accounting judgements in applying the company's accounting policies are described below

Claims made under insurance contracts

The group recognises that the process of estimation is based upon certain variables and assumptions which could differ when claims arise

The estimates for reported and unreported losses and the resulting provisions and related reinsurance recoveries are continually reviewed and updated and adjustments resulting from these reviews are reflected in the income and expenditure account in the period in which the estimate is revised and in any future periods affected

The process used to determine the assumptions is intended to result in neutral estimates of the most likely or expected outcome

There is more emphasis on current trends, and where in early years there is insufficient information to make a reliable best estimate of claims development, prudent assumptions are used

The nature of the business makes it very difficult to predict with certainty the likely outcome of any particular claim and the ultimate cost of notified claims Each notified claim is assessed on a separate basis with due regard to the claim circumstances, information available from loss adjusters and historical evidence of the size of similar claims Case estimates are reviewed regularly and are updated as and when new information arises

Useful economic life of goodwill

The group recognises that the process of estimating the useful economic life of goodwill is based on certain variables and assumptions that could change over time

The estimates of the useful economic life of goodwill are regularly reviewed and updated and any adjustments resulting from these reviews are reflected in the income and expenditure account in the period in which the estimate is revised and in any future periods affected

Basis of consolidation

The consolidated financial statements include the financial statements of the company and all subsidiaries, adjusted where appropriate to conform to group accounting policies Their financial statements are made up to 31st December The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases

Investments in group undertakings and associated undertakings are stated at current value in the company's own balance sheet Increases in valuation are recognised in the revaluation reserve. Decreases in valuation recognised in the revaluation reserve to the extent that they reverse previously recognised revaluation gains Any downwards revaluation in excess of an amount previously recognised in the revaluation reserve is recognised in the income and expenditure account

Associated undertakings and joint ventures

In the group financial statements, interests in associated undertakings and joint ventures are accounted for using the equity method of accounting The consolidated income and expenditure account includes the group's share of the operating results, interest, pre-tax results and taxation of such undertakings based on audited financial statements for the year In the consolidated balance sheet, the interests in associated undertakings and joint ventures are shown as the group's share of the net assets or liabilities, exclusive of any goodwill The premium paid on acquisition is amortised over its estimated useful economic life

Premiums

Premiums are charged at the amounts which it is estimated will meet claims, reinsurance premiums, expenses and other costs of the policy year to which they relate

Premiums written are accounted for in the year in which the risk commences Where applicable the unearned proportions of the premiums, relating to periods of risk extending beyond the end of the financial year, are carried forward to the next accounting period

All premiums are shown gross of commission payable to intermediaries and are exclusive of taxes and duties levied thereon

Unearned premiums are calculated on a time apportionment basis using the daily pro rata method

Accounting policies *(continued)*

Outward reinsurance premiums, related commissions and profit commissions are accounted for in the same accounting period as the premiums for the related direct insurance or inward reinsurance business

Acquisition costs

Acquisition costs comprise the expenses, both direct and indirect, of acquiring insurance policies written during the financial year Acquisition costs which relate to a subsequent financial year are deferred and charged to the accounting periods in which the related premiums are earned Deferred acquisition costs represent the proportion of acquisition costs incurred which corresponds to the proportion of gross premiums written which are unearned at the balance sheet date

Unexpired risks

Provision is made where the cost of claims and expenses arising after the end of the year from contracts concluded before that date is expected to exceed the provision for unearned premiums, net of deferred acquisition costs, and premiums receivable The assessment of whether a provision is necessary is made by reference to classes of business which are managed together

Management charges

Management charges were payable up to 30th June 2009 under the terms of a management agreement calculated on the basis of the costs incurred by Salvus Bain (Management) Limited and its subsidiary companies From the date of the group restructure no management charges were payable to Salvus Bain (Management) Limited and its subsidiary companies

Claims

Outstanding claims comprise provisions for the estimated cost of settling all claims incurred up to but not paid at the balance sheet date and are determined on an individual case basis after taking into account handling costs, salvage and other recoveries, anticipated inflation and trends in settlements Provision is also made in respect of claims incurred but not reported (IBNR claims) as at 31st December based on statistical methods Provision is also made for all claims handling expenses to cover the anticipated future costs of negotiating and settling claims which have been incurred, whether reported or not, up to the balance sheet date In determining the provision for claims handling expenses it has been assumed that the activity of the claims handling department will remain at its current level

The main statistical method used for review of reserve adequacy is the chain ladder triangulation method This method involves taking current and prior year premiums and claims developments and projecting potential ultimate outcomes for each class, year and currency The main assumption behind this method is that development patterns will remain relatively constant, although specific events and occurrences are taken into account

The reinsurers' share of provisions for claims is based on calculated amounts for outstanding claims and projections for IBNR, net of estimated irrecoverable amounts having regard to the reinsurance programme in place for the class of business, the claims experience for the year and the current security rating of the reinsurance companies involved

Although provisions for claims are based upon the information currently available to the directors, subsequent information and events may show that the ultimate liability is less than, or in excess of, the amount provided. The methods used, and estimates made, are continually reviewed and any resulting adjustments are reported in the technical account for general business in the financial year in which the claims are settled or re-appraised

Intra-group funding

All financial guarantees in respect of intra-group funding between the company and its subsidiaries are treated as insurance contracts in accordance with FRS 12 *'Provisions, contingent assets and liabilities'.*

Accounting policies *(continued)*

Financial instruments

Non-derivative financial investments are classified as financial assets at fair value through income Non-derivative financial investments are classified in this category if acquired principally for the purpose of selling in the short term or if so designated by the group The group has designated non-derivative financial investments at fair value through income where the group's strategy is to manage those financial investments on a fair value basis

Non-derivative financial investments classified at fair value through income are initially recognised and subsequently measured at fair value in the balance sheet with transaction costs taken directly to the income and expenditure account. All changes in fair value are recognised in income as described in the 'Investment income' accounting policy The bases for determining the fair value of all financial assets and of the derivative liabilities is as set out in notes 17 and 27

The group holds derivative financial instruments to hedge its foreign currency exposure and to support the equity investment return Derivatives are categorised as held for trading and are classified as financial assets or financial liabilities at fair value through income Derivative financial instruments are measured at initial recognition, and subsequently, at fair value and changes in fair value are recognised in the income and expenditure account. Transaction costs incurred in buying and selling derivative financial instruments are recognised in the income and expenditure account when incurred The fair value of a derivative financial instrument is determined by reference to published price quotations in an active market.

Note 17 sets out the amount of each class of financial asset that has been designated at fair value through income

Recognition and de-recognition of financial instruments

A financial instrument is recognised if the group becomes a party to the contractual provisions of the instrument Financial assets are de-recognised if the group's contractual rights to the cash flows from the financial assets expire or if the group transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset Financial liabilities are de-recognised if the group's obligations specified in the contract expire or are discharged or cancelled.

Investment income

Investment income comprises gains or losses arising from changes in the fair value of financial assets at fair value through income It also comprises interest receivable on short term and bank deposits accounted for on an accruals basis Dividends are included as investment income on the date that the shares become quoted ex-dividend, exclusive of any attributable tax credits Investment income also includes rental income.

Land and buildings

All freehold properties are being depreciated in accordance with FRS 15 '*Tangible fixed assets*' The freehold property is valued every three years by a qualified external valuer in accordance with the Appraisal and Valuation Manual of the Royal Institution of Chartered Surveyors

Increases in valuation are recognised in the revaluation reserve Decreases in valuation are recognised in the revaluation reserve to the extent that they reverse previously recognised revaluation gains Any downwards valuation in excess of an amount previously recognised in the revaluation reserve is recognised in the income and expenditure account

Freehold land is not depreciated

Fixed assets and depreciation

All fixed assets are initially recorded at cost

Accounting policies (continued)

Depreciation is calculated so as to write off the cost of an asset, less its estimated residual value, over the useful economic life of that asset as follows

Freehold buildings	-	2% straight line
Fixtures & fittings	-	12 5% - 33 3% straight line
Motor vehicles	-	20% - 33 3% reducing balance
Computers	-	20% - 33 3% straight line

Goodwill

Goodwill represents the excess of the fair value of the purchase consideration over the fair value of the underlying net assets of the subsidiaries and associated undertakings at the time of acquisition Goodwill is capitalised in the balance sheet and amortised on a straight line basis over its estimated useful economic life The methodology for amortising goodwill over its estimated useful economic life is disclosed in note 14

Loans and debtors

Loans and debtors are measured at amortised cost The company reviews the carrying value of its loans and debtors on a regular basis If the carrying value of a loan or debtor is greater than the recoverable amount, the carrying value is reduced through a charge to the income and expenditure account in the period of impairment

Deferred taxation

Where the different treatment of certain items for taxation and accounting purposes results in an obligation to pay more or a right to pay less tax in the future deferred tax is recognised in respect of such timing differences that have originated but not reversed at the balance sheet date with certain limited exceptions A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised Deferred taxation is calculated on an undiscounted basis at the tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws enacted or substantially enacted at the balance sheet date

Operating lease agreements

Rentals applicable to operating leases where substantially all of the benefits and risks of ownership remain with the lessor are charged to the income and expenditure account on a straight line basis over the period of the lease

Post-retirement benefits

The company operates a defined benefit pension scheme for employees The assets of the scheme are held separately from the assets of the company Pension scheme assets are measured using market values For quoted securities the current bid price is taken as market value Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability

The pension scheme surplus (to the extent that it is recoverable) or deficit is recognised in full The movement in the scheme surplus or deficit is allocated between operating charges, finance items and, in the statement of total recognised gains and losses, actuarial gains and losses

The group also operates a number of defined contribution pension schemes. The assets of the schemes are held separately from those of the company in independently administered funds The amounts charged to the income and expenditure account represent the contributions payable to the schemes in respect of the accounting period

Accounting policies *(continued)*

Foreign currency

The financial statements are presented in Sterling, which is the group's presentation currency

The functional currency of a group entity is the currency of the primary economic environment in which it operates

A group entity whose functional currency is not Sterling is a foreign operation The income and expenses of foreign operations are translated into Sterling at the exchange rate ruling at the date of the transactions The assets and liabilities of foreign operations are translated into Sterling at the rate of exchange prevailing at the reporting date and the resulting exchange differences are recognised in the statement of total recognised gains and losses

Foreign currency transactions are transactions undertaken by a group entity other than in its functional currency Foreign currency transactions during the year are translated into the functional currency at the exchange rate ruling at the date of the transactions

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange prevailing at the balance sheet date Foreign exchange differences arising on translation are recognised in the income and expenditure account

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rate ruling at the date of the transaction Foreign exchange differences arising on translation are recognised in the income and expenditure account

Realised exchange gains and losses arising from cross currency funding are dealt with in the non-technical account Other exchange gains and losses and translation differences are dealt with in the technical account

RISK MANAGEMENT

The group's management of insurance and financial risk is a critical aspect of the business The group has a number of procedures in place to manage these risks which are explained in detail below

Governance framework

The primary objective of the group's risk and financial management framework is to protect the group's members from events that hinder the achievement of financial performance objectives A group policy framework has been put in place that sets out the risk profiles for the group and the board and risk committee regularly approves the group risk management policies

Capital management framework

The group has an internal risk management framework for identifying risks to which the group is exposed and to quantify their impact on economic capital The internal framework indicates how much capital is needed to mitigate the risk of capital exhaustion to a confidence level of 99 5% over one year The group has a finance committee consisting of senior management which meets regularly to evaluate the capital allocations and adequacy within different jurisdictions in which the group operates

Regulatory framework

One of the objectives of the group's primary regulator is to protect the rights of the members The regulator monitors the group closely to ensure that it is satisfactorily managing affairs for the members' benefit At the same time the regulator is also interested in ensuring that the group maintains an appropriate solvency position to meet unforeseen liabilities

The operations of the group are also subject to regulatory requirements within jurisdictions where it operates Such regulations not only prescribe approval and monitoring of activities, but also impose certain requirements (e g capital adequacy) to minimise the risk of default and insolvency

Asset liability management framework

The group has exposure to risks arising from movements in interest rates, currencies and equity prices, all of which are exposed to general and specific market movements The principal technique used by the group is to match financial assets to liabilities in the same currency The group also ensures that there is sufficient cash flow available to meet liabilities as they fall due

Specific risks that the group is exposed to and how they are managed by the group are explained below

Insurance risk

The group issues contracts that transfer insurance risk

The principal risk the group faces under insurance contracts is that actual claims payments or the timing thereof, differ from expectations This is influenced by the frequency of claims, severity of claims and the subsequent development of long-tail claims

The objective of the group is to ensure that sufficient technical provisions are available to cover these liabilities

This risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas The variability of risks is also reduced by careful selection and implementation of underwriting strategy guidelines, as well as the use of reinsurance arrangements

The group reinsures a portion of the risks it underwrites in order to control its exposure to losses and protect capital resources The group buys a combination of proportional and non-proportional reinsurance to reduce the net exposure to the group Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts Although the group has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to ceded insurance, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements The group's placement of reinsurance is diversified such that it is not dependent on a single reinsurer

The group has also limited its exposure by the use of reinsurance arrangements in order to limit exposure to catastrophic events

Strict claim review policies to assess all new and ongoing claims, regular detailed review of claims handling procedures and frequent investigation of possible fraudulent claims are all policies and procedures put in place to reduce the risk exposure of the group

The group further enforces a policy of actively managing claims in order to reduce its exposure to unpredictable future developments that can adversely impact the group

The table below sets out the concentration of the group's technical provisions excluding reinsurance commission by type of contract.-

	2010			2009		
	Gross £'000	**Reinsurance £'000**	**Net £'000**	**Gross £'000**	**Reinsurance £'000**	**Net £'000**
Marine	70,324	17,679	52,645	72,351	8,050	64,301
Aquaculture	12,731	10,283	2,448	13,966	10,641	3,325
Total	83,055	27,962	55,093	86,317	18,691	67,626

The geographical concentration of the group's technical provisions excluding reinsurance commission is noted below The disclosure is based on the countries where the business is written

	2010			2009		
	Gross £'000	**Reinsurance £'000**	**Net £'000**	**Gross £'000**	**Reinsurance £'000**	**Net £'000**
Australasia	14,876	5,877	8,999	14,007	2,477	11,530
Europe	12,968	4,703	8,265	13,468	3,636	9,832
North America	34,348	14,361	19,987	33,681	8,953	24,728
United Kingdom	11,025	394	10,631	11,533	882	10,651
Others	9,838	2,627	7,211	13,628	2,743	10,885
Total	83,055	27,962	55,093	86,317	18,691	67,626

Claims development

The group aims to maintain strong technical provisions in respect of its insurance business in order to protect against adverse future claims experience and developments. As claims develop and the ultimate cost of claims becomes more certain, potential adverse claims experiences are reduced which can result in the release of technical provisions from these earlier accident years

The following table reflects the cumulative incurred claims including both claims notified and incurred but not reported (IBNR) for each successive accident year at the balance sheet dates

	Gross claims incurred				
	2006	**2007**	**2008**	**2009**	**2010**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Accident year at end of					
Accident year	43,628	59,646	46,381	54,648	47,426
One year later	43,542	56,077	45,207	55,514	
Two years later	42,947	56,345	44,369		
Three years later	42,206	56,269			
Four years later	41,867				

Financial instrument risk

The group also has exposure to the following risks from its financial instruments -

Credit risk
Liquidity risk
Market risk

Information is presented about the group's exposure to each of the above risks, the group's objectives, policies and processes for measuring and managing these risks and the group's management of capital

Credit risk

Credit risk is the risk that a customer or counter-party to a financial instrument fails to meet its contractual obligations resulting in a financial loss to the group This risk arises principally from the group's reinsurance debtors, premium debtors and financial assets. The following policies and procedures are in place to mitigate the group's exposure to credit risk

Reinsurance is placed with counterparties that have a good credit rating Management performs an assessment of credit-worthiness of reinsurers and updates the security committee on a regular basis to ensure all the reinsurers on the main reinsurance programmes are A rated or above

The group also employs reinsurance intermediaries that are subject to the regulation and approval of the Financial Services Authority in the UK and as such are required to operate client trust accounts to ring-fence the amounts held on their client's behalf

The group's exposure to credit risk from premium debtors is influenced mainly by the individual characteristics of each customer

The credit risk in respect of customer balances incurred on non-payment of premium will only persist during the payment period specified in the policy document If payment is still outstanding when the payment period expires the policy can be cancelled If a member has ceased to be insured by the company, the company will not be liable for any claims under the company's general conditions if the incident giving rise to such claim occurred after the cessation of insurance

Investment related credit risk is managed through the investment guidelines issued to the fixed income managers The guidelines impose strict diversification limits by credit rating, maturity and per issuer

The maximum exposure to credit risk amounts to £102,319,000 (2009 £103,811,000) This exposure includes all financial assets (with the exception of equities and derivatives) as detailed in note 31 The exposure to credit risk arising from cash and cash equivalents, deposits with credit institutions, inward reinsurance operations and direct insurance operations is not considered significant The following table summarises the group's exposure to credit risk by rating the debt securities and outward reinsurance debtors

Rating	2010 Debt securities £'000	2010 Outward reinsurance debtors £'000	2009 Debt securities £'000	2009 Outward reinsurance debtors £'000
AAA	42,666	-	32,826	-
AA	2,933	3,354	5,866	1,235
A	10,679	2,027	11,688	72
BBB	5,255	268	9,185	203
BB	1,761	-	1,667	-
B	572	-	2,284	-
CCC	220	-	118	-
Not rated	44	-	53	20
Total	64,130	5,649	63,687	1,530

Liquidity risk

Liquidity risk is the risk that the group will encounter difficulty in meeting its financial obligations as they fall due The group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due The group monitors its forecast liquidity position by estimating the cash outflows from its insurance contracts and purchasing investments with similar durations to meet these obligations

The following table summarises the contractual maturities of the group's financial liabilities.

At 31st December 2010	No contractual maturity £'000	Less than one year £'000	1-2 years £'000	Total £'000
Derivative financial liabilities	-	227	-	227
Creditors arising out of direct insurance operations	1,984	-	-	1,984
Creditors arising out of reinsurance operations	8,350	-	-	8,350
Borrowings	6,148	461	223	6,832
Other creditors, including taxation and social security	1,805	1,026	-	2,831
Total	18,287	1,714	223	20,224

At 31st December 2009	**No contractual maturity £'000**	**Less than one year £'000**	**1-2 years £'000**	**2-5 years £'000**	**Total £'000**
Derivative financial liabilities	-	343	-	-	343
Creditors arising out of direct insurance operations	1,915	-	-	-	1,915
Creditors arising out of reinsurance operations	2,786	-	-	-	2,786
Borrowings	5,216	486	474	232	6,408
Other creditors, including taxation and social security	2,086	537	-	-	2,623
Total	12,003	1,366	474	232	14,075

Fair value hierarchy

In May 2009 the Accounting Standards Board issued 'Amendments to FRS29 – *Improving Disclosures about Financial Instruments'* The amended FRS requires certain additional disclosures to be included in the financial statements These include, as is presented below, a table of financial instruments carried at fair value analysed by their level as defined by the fair value hierarchy in the FRS This hierarchy is based on the inputs to the fair value measurement and reflects the lowest level input that is significant to that measurement

The classification criteria and their application to the group can be summarised as follows

Level 1 – active quoted prices
Items in this category are valued using unadjusted quoted prices from active markets for identical assets and liabilities.

Level 1 principally includes exchange listed equities, exchange traded derivatives such as futures and options and government bonds and equivalents, unless there is evidence that trading in a given instrument is so infrequent that the market cannot be considered active

Level 2 – other observable market-derived inputs
Items in this category are valued using inputs other than quoted prices as included within level 1 that are observable either directly (i e as prices) or indirectly (i e derived from prices)

Level 2 principally includes corporate bonds and other non-national government debt securities and forward exchange contracts which are valued using observable inputs and non-quoted investment funds valued with observable inputs

Level 3 - unobservable inputs
Items in the category would be valued on a basis using significant inputs for the asset or liability that are not based on observable market data (unobservable inputs)

Level 3 principally includes commercial mortgage backed securities and non-investment grade corporate bonds

The group holds a significant portfolio of government and corporate bonds, structured securities and other debt securities. These assets are valued by independent investment managers and are subject to their monitoring controls

The table below summarises the fair value measurement basis used for assets and liabilities held at fair value

At 31st December 2010	**Level 1 Active quoted prices £'000**	**Level 2 Other observable inputs £'000**	**Level 3 Unobservable inputs £'000**	**Total £'000**
Financial assets				
Equity securities at fair value through income	4,097	-	-	4,097
Debt securities at fair value through income	19,407	43,665	1,058	64,130
Derivatives at fair value through income	129	219	-	348
Deposits with credit institutions	9,521	-	-	9,521
	33,154	43,884	1,058	78,096
Financial liabilities				
Derivatives at fair value through income	(182)	(45)	-	(227)

At 31st December 2009	**Level 1 Active quoted prices £'000**	**Restated Level 2 Other observable inputs £'000**	**Level 3 Unobservable inputs £'000**	**Total £'000**
Financial assets				
Equity securities at fair value through income	3,842	-	-	3,842
Debt securities at fair value through income	21,645	41,063	979	63,687
Derivatives at fair value through income	307	95	-	402
Deposits with credit institutions	10,577	1,285	-	11,862
	36,371	42,443	979	79,793
Financial liabilities				
Derivatives at fair value through income	(343)	-	-	(343)

Guidance on classification between the various levels continues to evolve Formerly certain debt securities whose fair value is determined using prices from brokers, dealers and/or pricing services were classified in Level 1 if the quoted prices indicated the market for those securities was actively trading Based upon recent guidance issued by the Committee of European Securities Regulators (CESR), the company now classifies these securities in Level 1 only if it can be demonstrated on an individual security basis that these are quoted in an active market, i e that the price quotes obtained are representative of actual trades in the market (through obtaining binding quotes or through corroboration to published market prices) Otherwise, these are classified in Level 2 Comparatives for 2009 have been similarly reclassified with the most significant movements from Level 1 to Level 2 at the end of 2009 being in respect of corporate bonds

The table below shows the reconciliation of movements in level 3 investments during the year

	Total £'000
Balance at 1st January 2010	979
Purchases	606
Sales	(268)
Realised loss	(48)
Unrealised loss	(211)
Balance at 31st December 2010	1,058

The realised losses are included within investment income in the income and expenditure account The unrealised losses are included within unrealised (losses)/gains on investments in the income and expenditure account

The majority of the group's investments are valued based on quoted market information or other observable market data A small percentage (1 4%) of 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 While 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

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices Market risk comprises three types of risk, foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (prices risk)

The objective of market risk management is to manage and control market risk exposures within acceptable parameters whilst optimising the return on risk

The group's exposure to changes in interest rates and market prices is concentrated in the investment portfolio

The group manages its investment portfolio in accordance with an investment framework that is approved by the directors The framework is used to determine both the investment policy and to establish the investment risk appetite. In this context the overall risk is reviewed on a regular basis and the asset allocation is adjusted to ensure it reflects the investment risk appetite.

The detailed consideration of group investment strategy is the responsibility of the investment committee, a committee of the board Investment management is outsourced and the performance of investment managers against their respective benchmarks is monitored on a monthly basis There is also a formal quarterly review of performance and measurement of portfolio risk by the investment committee and, through it, the board

The asset class allocation aims to ensure that the group's technical liabilities are matched against assets by currency and maturity In addition, the group ensures minimal risk is taken with the committed regulatory capital An overall investment risk budget is established annually by the board Asset allocation is determined by reference to the risk budget and strictly monitored and controlled Diversification is used where possible as a means of minimising volatility, whilst observing necessary risk constraints

Known claims liabilities of the group are matched by currency and maturity to fixed income assets providing appropriate security and liquidity to facilitate expeditious settlement of claims The remainder of the portfolio, being invested from free reserves, is allocated to a more diversified bond mandate with a small allocation to other higher yielding assets which are expected to produce higher absolute returns in the long-term

a) **Currency risk**

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates The company operates internationally and its exposures to foreign exchange risk arise primarily with respect to the US, Canadian, Australian, New Zealand, Euro and South African currencies

The group's financial assets are primarily denominated in the same currencies as its liabilities (including forward currency contracts) which mitigate the foreign exchange rate risk of the overseas operations Cross currency funding underpinning regional regulatory capital requirements is effectively managed by the group through derivative financial instruments as forward currency contracts are put in place to reduce the currency exposure

Forward currency contracts are used to reduce the group's exposure to fluctuations in currency conversion rates between Sterling and other currencies so that the group's net assets are not significantly affected

The table below summarises the group's exposure to foreign currency exchange rate risk by categorising the assets and liabilities by major currencies

At 31st December 2010	**Assets**	**Liabilities**	**Net assets/ (liabilities)**	**Forward contracts**	**Net assets/ (liabilities) after forward contracts**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Australian Dollars	20,515	13,146	7,369	(7,144)	225
Canadian Dollars	23,867	19,023	4,844	(6,949)	(2,105)
Euro	10,576	15,033	(4,457)	2,897	(1,560)
New Zealand Dollars	3,585	4,108	(523)	1,016	493
US Dollars	25,048	32,105	(7,057)	7,124	67
South African Rand	3,188	1,363	1,825	(975)	850
	86,779	84,778	2,001	(4,031)	(2,030)
Sterling	64,936	20,907	44,029	4,031	48,060
	151,715	105,685	46,030	-	46,030
At 31st December 2009					
Australian Dollars	15,837	10,369	5,468	(6,002)	(534)
Canadian Dollars	19,001	17,547	1,454	(1,783)	(329)
Euro	11,243	18,044	(6,801)	7,086	285
New Zealand Dollars	2,721	3,696	(975)	1,135	160
US Dollars	23,720	36,515	(12,795)	10,846	(1,949)
South African Rand	2,579	946	1,633	(845)	788
	75,101	87,117	(12,016)	10,437	(1,579)
Sterling	72,587	16,907	55,680	(10,437)	45,243
	147,688	104,024	43,664	-	43,664

b) **Interest rate risk**

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates Interest rate risk arises primarily from the nature and term of investments held and is managed through the buying and selling of appropriate fixed interest securities of different durations

The group uses a number of sensitivity management tools to understand the volatility of earnings The table below shows the effects of a 0 5% increase or decrease in interest rates on earnings from debt securities

	2010	**2009**
	£'000	**£'000**
0 5% increase in interest rates	(188)	(176)
0 5% decrease in interest rates	203	166

c) **Price risk**

Price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices The group is exposed to price risk as a result of its holdings in equity investments and debt securities

The group's price risk policy requires it to manage such risks by setting and monitoring objectives and constraints on investments, limits on investments in each country, sector and market and careful and planned use of derivative financial instruments

The table below shows the anticipated change in equity and alternative investment market values from a 10% increase or decrease in underlying prices·

	2010	**2009**
	£'000	**£'000**
10% increase in equity price	410	384
10% decrease in equity price	(410)	(384)

The table above demonstrates the effect of a change in a key assumption whilst other assumptions remain unchanged It should be noted that these sensitivities are non-linear, and larger or smaller impacts should not be extrapolated or interpolated from these results The sensitivity analyses do not take into consideration that the group's assets and liabilities are actively managed Management actions could include selling investments, changing investment portfolio allocation and taking other protective action In addition, the financial position of the group may vary at the time that any actual market movement occurs

Operational risks

Operational risk is the risk of loss arising from system failure, human error, fraud or external events When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications or can lead to financial loss The group cannot expect to eliminate all operational risks, but by initiating a rigorous control framework and by monitoring and responding to potential risks, the group is able to manage the risks. Controls include effective segregation of duties, access controls within the IT environment, authorisation and reconciliation procedures, staff education and assessment processes and internal audit

Group risks

Group risk is the potential for one of the subsidiaries to fail, or for adverse events in a subsidiary having a significant impact on the group These risks are mitigated by the use of procedures and controls, which aim to be as consistent as possible throughout the group Additionally, head office provides functionality and oversight to group companies providing additional control

Capital management

The required capital, as measured by the UK Financial Services Authority's (FSA's) Required Minimum Margin (RMM) is determined by the application of a formula that contains variables for premium and claims, expenses and reserves The company also submits to its domiciliary regulator an annual Enhanced Capital Requirement (ECR) calculation and an Individual Capital Assessment (ICA) as required

The company is required to maintain sufficient capital locally to provide solvency coverage for its operations in Australia, New Zealand, South Africa, the United States and Canada, in line with the applicable local regulations The company has capital management procedures in place to ensure that such overseas requirements are complied with at all times As part of this process the group has, where appropriate, developed its own more robust internal solvency calculations to ensure compliance with the regulatory minima The company met the requirements of the RMM and ECR throughout 2010

The group capital comprises the capital and reserves of £46,030,000 shown in the consolidated balance sheet The company manages capital on an adjusted solo solvency basis as prescribed by the FSA which includes the capital of SM Insurance (Bermuda) Limited This core tier one capital was £45,696,000 as at 31st December 2010 (2009 £43,423,000) of which a total of £20,400,000 (2009 £14,100,000) was held in local currency to support local solvency requirements in Australia, USA, Canada and New Zealand

At 31st December 2010, the insurance subsidiary Sunderland Marine (Africa) Limited held regulatory capital of £1,619,000 (2009 £1,261,000)

2. Analysis of premiums, result before taxation and net assets

On the grounds that the information is commercially sensitive the directors of the company have taken advantage of the exemption from disclosure that is available within SSAP 25 and therefore disclosure of the geographical analysis of gross premium income, result before taxation and net assets has not been provided

3. Analysis of gross direct written premiums

Gross direct written premiums resulting from contracts concluded

	2010 £'000	**2009 £'000**
In the United Kingdom	11,681	12,979
In other countries	60,883	61,254
	72,564	74,233

4. Prior years' claims provisions

Over/(under) provisions for claims at the beginning of the year compared to payments and provisions at the end of the year in respect of prior years' claims are as follows

	2010 £'000	**2009 £'000**
Direct	2,691	5,227
Inward reinsurance	(95)	(474)

5. Net operating expenses

	2010 £'000	2009 £'000
Acquisition costs	11,898	11,940
Change in deferred acquisition costs	435	499
Administration expenses	13,797	12,816
Reinsurance commissions and profit participation	(9,326)	(3,017)
Change in unearned reinsurance commission	2,272	201
	19,076	22,439

6. Particulars of employees

The average number of staff employed by the group during the financial year amounted to

	2010 No	2009 No
Number of staff - full time	111	113
Number of staff - part time	8	8
	119	121
Staff employed by joint venture companies	58	58
	177	179

The aggregate payroll costs of the staff employed by the group were

	2010 £'000	2009 £'000
Wages and salaries	6,133	5,861
Social security costs	424	411
Staff pension contributions	878	714
Directors' pension contributions	24	-
	7,459	6,986

The directors' aggregate emoluments, including pension contributions, in respect of qualifying services were.

	2010 £'000	2009 £'000
Emoluments receivable	1,258	826
Value of company pension contributions to defined benefit schemes	24	-
	1,282	826

Fees of £59,221 (2009 £51,325) payable to one director were paid, with the addition of VAT, to his company, Sandwood Services Limited Fees of £10,217 (2009 £21,312) for Mr C J Hilton were paid to Eversheds LLP, covering the period up to 30th April 2010 when he retired from Eversheds, with the balance of fees due paid directly to him

These disclosures include amounts relating to directors of the company in respect of their positions as directors of subsidiary companies where appropriate

The aggregate emoluments of the highest paid director were £509,417 (2009· £378,082) including pension contributions of £nil (2009 £nil) His accrued pension at the year-end was £146,618 (2009 £141,444) and his accrued lump sum was £450,000 (2009· £437,500) The aggregate emoluments include deferred bonuses relating to 2006 and 2007

Four directors accrued benefits under a company pension scheme (2009 1)

7. Investment income

	2010 £'000	2009 £'000
Interest income group and share of joint ventures	510	469
Less share of joint ventures' interest income	(2)	(5)
	508	464
Gains on the realisation of investments	976	-
Other investment income	3,017	2,923
Interest on defined benefit pension plan obligation	(1,060)	(884)
Expected return on defined benefit pension plan assets	1,050	854
Exchange and translation losses	(77)	(404)
Derivative (charge)/income	(586)	1,903
	3,828	4,856

Income from listed investments included in other investment income was £2,966,000 (2009 £2,889,000)

8. Unrealised (losses)/gains on investments

	2010 £'000	2009 £'000
Unrealised (losses)/gains on investments	(31)	4,214

9. Investment expenses and charges

	2010 £'000	2009 £'000
Investment management expenses, including interest	461	562
Losses on the realisation of investments	-	2,747
	461	3,309

10. Operating surplus

Of the group operating result, £3,000 surplus (2009 surplus of £199,000) is attributable to the share of operating results in joint ventures

11. Surplus on ordinary activities before tax

	2010 £'000	2009 £'000
Surplus on ordinary activities before tax is stated after charging/(crediting)		
Overdraft and loan interest	250	352
Depreciation on land and buildings	149	152
Depreciation on tangible fixed assets	254	262
(Profit)/loss on sale of fixed assets	(2)	3
Amortisation of goodwill	1,335	854
Exchange and translation losses	513	1,128
Derivative charge/(income)	586	(1,903)
Operating lease costs - land and buildings	172	114
- other items	215	191
Property revaluation through income & expenditure account	215	-
Auditors' remuneration.		
Audit of these financial statements	157	152
Amounts receivable by the auditors and their associates in respect of		
Audit of financial statements of subsidiaries pursuant to legislation	88	89
Other services pursuant to such legislation	158	154
Other services relating to tax	-	9
Audit of pension scheme	4	5
All other services (principally regulatory)	-	33

12. Surplus attributable to members of the parent company

The deficit in the accounts of the parent company was £260,000 (2009 £1,917,000)

13. Tax on surplus on ordinary activities

	2010 £'000	2009 £'000
The charge for taxation is computed as follows		
UK corporation tax on the taxable surplus for the year at 28% (2009 28%)	87	50
Adjustment in respect of previous periods	-	(89)
	87	(39)
Double taxation relief	(13)	(50)
	74	(89)
Overseas tax	417	420
Adjustment in respect of previous periods	47	10
	464	430
Share of joint ventures' current taxation	(4)	30
	(4)	30
Total current taxation	534	371
Deferred tax (note 26)		
Reversal of timing differences	(113)	(34)
Tax relief claimed in respect of contributions paid to the group defined benefit pension scheme	-	298
Total deferred taxation	(113)	264
Tax on surplus on ordinary activities	421	635

13. Tax on surplus on ordinary activities (continued)

	2010 £'000	2009 £'000
Factors affecting the tax charge for the period		
Surplus on ordinary activities before tax	2,976	5,084
Current tax at 28% (2009 28%)	833	1,424
Effects of		
Non taxable income	(1,718)	8
Expenses not deductible for tax purposes	1,973	597
Lower rates of overseas tax	(644)	(1,206)
Capital allowances in excess of depreciation	310	(20)
Other short-term timing differences	(197)	54
Double taxation relief	(13)	(50)
Adjustments to tax charge in respect of previous periods	47	(79)
Foreign tax credits	-	(9)
Losses utilised	(51)	(44)
Tax relief claimed in respect of contributions paid to the group defined benefit pension scheme	-	(298)
Small companies relief	(6)	(6)
Total current tax charge (see above)	534	371

There is no UK deferred tax Overseas deferred tax is calculated at the relevant tax rates applicable in each jurisdiction

14. Goodwill

Group

	2010 £'000
Cost	
At 1st January 2010	9,193
Adjustment due to exchange rates	(10)
Adjustment due to contingent consideration	(173)
At 31st December 2010	9,010
Amortisation	
At 1st January 2010	2,434
Adjustment due to exchange rates	7
Charged in year	1,335
At 31st December 2010	3,776
Net book value	
At 31st December 2010	5,234
At 31st December 2009	6,759

14. Goodwill (continued)

Goodwill is being amortised over its useful economic life, which the directors estimate individually for each acquisition and is shown below

Goodwill in respect of the acquisition of Salvus Bain (Management) Limited is being amortised over five years Following the completion of the group restructure in 2009 the directors have reassessed the useful economic life of this goodwill and reduced the amortisation period from twenty to five years

Goodwill in respect of the acquisition of shares in Van Olst de Graaff & Co BV is being amortised over five years

On 1st January 2009 Salvus Bain (Management) USA LLC acquired the trade and net assets of Marine Underwriters Inc, a business trading in USA The carrying value of the identifiable assets and liabilities of the entity at the date of acquisition was also the fair value to the group

The fair value of the identifiable assets and liabilities of the entity at the date of acquisition were

	Carrying value and fair value to the group £'000
Assets	
Tangible assets	47
Net assets acquired	47
Goodwill arising on acquisition	809
Total consideration	856

The consideration was satisfied solely by cash

The acquisition has been accounted for by using the acquisition method of accounting

Goodwill is being amortised over five years

On 1st January 2009 Van Olst de Graaff & Co BV acquired the trade of Assurantiekantoor P M Arkesteijn an entity trading in the Netherlands No identifiable assets or liabilities were acquired at the date of acquisition The goodwill arising on the acquisition is the purchase price of £1,271,000

The goodwill adjustment relating to contingent consideration is in relation to the acquisition of Assurantiekantoor P M Arkesteijn

The consideration was satisfied solely by cash

The acquisition has been accounted for by using the acquisition method of accounting

Goodwill is being amortised over five years

15. Land and buildings

	Freehold land and buildings £'000
Group	
Valuation	
At 1st January 2010	8,968
Adjustment due to exchange rates	327
Revaluation through reserves	(432)
Revaluation through income and expenditure account	(233)
At 31st December 2010	8,630
Depreciation	
At 1st January 2010	177
Adjustment due to exchange rates	10
Charge for the year	149
Revaluation through reserves	(271)
Revaluation through income and expenditure account	(18)
At 31st December 2010	47
Net book value	
At 31st December 2010	8,583
At 31st December 2009	8,791
Company	
Valuation	
At 1st January 2010	8,437
Adjustment due to exchange rates	307
Revaluation through reserves	(432)
Revaluation through income and expenditure account	(150)
At 31st December 2010	8,162
Depreciation	
At 1st January 2010	166
Adjustment due to exchange rates	10
Charge for the year	139
Revaluation through reserves	(271)
Revaluation through income and expenditure account	-
At 31st December 2010	44
Net book value	
At 31st December 2010	8,118
At 31st December 2009	8,271

15. Land and buildings (continued)

The group's freehold property in the UK was re-valued to £6,250,000 at 24th September 2010 by external valuers Bradley Hall Chartered Surveyors Limited The property was valued on the basis of open market value for existing use The valuation is in accordance with the Appraisal and Valuation Manual of the Royal Institution of Chartered Surveyors

The group's overseas freehold properties were re-valued during August 2010 Freehold property amounting to £1,512,561 was valued by suitably qualified external valuers, Sutherland Farrelly, Licenced Property Valuers. Freehold property amounting to £399,798 was valued by suitably qualified external valuers, Duke & Cooke Limited, Valuers & Property Specialists Freehold property amounting to £467,806 was valued by suitably qualified external valuers CB Richard Ellis, Inc , Valuation and Advisory Services The properties were valued on the basis of open market value for existing use

The total cost of all land and buildings at 31st December 2010 was £8,578,000 (2009· £8,578,000).

16. Investments in group undertakings and participating interests

The principal subsidiaries at the end of the year included in the consolidation are

	Country of incorporation or registration	Proportion of equity shares held	Nature of business
Sunderland Marine (Africa) Limited	South Africa	100%	Marine insurance
SM Insurance (Bermuda) Limited	Bermuda	100%	Marine reinsurance
Salvus Bain Management (USA) LLC	U S A	100%	Brokerage
Van Olst de Graaff & Co BV	Netherlands	73%	Brokerage

The joint ventures included in the consolidation are

Joint ventures	Country of incorporation or registration	Proportion of equity shares held	Nature of business
Knighthood Corporate Assurance Services Plc	England	49%	Insurance Broker
Harlock Murray Underwriting Limited	Canada	50%	Broking & management Services

Knighthood has been accounted for as a joint venture by virtue of the joint control exercised over the financial and operating policies of the company.

16. Investments in group undertakings and participating interests (continued)

	Shares in group undertakings £'000
Group	
At 1st January 2010	776
Adjustment due to exchange movements	26
Share of profits of joint ventures	3
Share of joint venture current taxation	4
Dividend paid	(95)
At 31st December 2010	714
Company	
At 1st January 2010	32,573
Adjustment due to exchange movements	230
Increase in loans owed by subsidiary undertakings	130
Repayment of subsidiaries capital	(3,275)
Revaluation of subsidiaries through reserves	2,831
Revaluation of subsidiaries through income and expenditure account	(798)
Impairment on striking off subsidiaries	(4,224)
At 31st December 2010	27,467

Sunderland Pacific Management Pty Limited has been struck off following the group restructure in 2009

Sunderland Pacific Management (NZ) Limited paid a final dividend and then repaid its share capital to Salvus Bain (Management) Limited before being struck off

Salvus Bain (Management) Limited paid a final dividend and then repaid its share capital to the company before it was struck off The value of Salvus Bain (Management) Limited in the company balance sheet was then eliminated

Salvus Bain (Africa) Limited paid a final dividend to Sunderland Marine (Africa) Limited before becoming dormant

The repayment of subsidiaries capital to the company of £3,275,000 represents the repayment of Salvus Bain (Management) Limited's share capital and the repayment by SM Insurance (Bermuda) Limited of its contributed capital of £2,800,000

SM Insurance (Guernsey) Limited was struck off during the year

Sunderland Marine (Africa) Limited and SM Insurance (Bermuda) Limited have been valued at net asset value in the company balance sheet at 31st December 2010

Salvus Bain Management (USA) LLC and the company's share of Van Olst de Graaff & Co BV have been re-valued in the company balance sheet by suitably qualified external valuers at 31st December 2010

The company's share in its joint ventures, Knighthood Corporate Assurance Services Plc and Harlock Murray Underwriting Limited, have been re-valued in the company balance sheet by suitably qualified valuers at 31st December 2010

16. Investments in group undertakings and participating interests (continued)

	2010 £'000	2009 £'000
Share of joint ventures' assets	1,840	1,770
Share of joint ventures' liabilities	(1,126)	(994)
	714	776

At the year end, balances due to/(from) the group to its joint ventures were as follows -

	2010 £'000	2009 £'000
Knighthood Corporate Assurance Services Plc - trading balances	(2)	204
Harlock Murray Underwriting Limited - trading balances	397	306

The total cost of investments in group undertakings at 31st December 2010 is £8,342,000 (2009 £15,426,000)

17. Financial assets

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Equity securities at fair value through income				
Market value	4,097	3,842	-	-
Cost	4,386	4,409	-	-
Debt securities at fair value through income				
Market value	64,130	63,687	21,529	14,103
Cost	63,775	62,845	21,594	14,139
Derivatives at fair value through income	348	402	88	39

The fair value of listed equities and debt securities is determined by reference to their quoted bid price at the reporting date

The fair value of the derivative financial instruments is based on their listed market price

18. Reinsurers' share of technical provisions

	Provision for unearned premiums £'000	Provision for unearned commission £'000	Claims outstanding £'000	Total £'000
Group				
At 1st January 2010	7,559	(1,677)	11,132	17,014
Adjustment due to exchange movements	600	(148)	875	1,327
Movement during the year	6,105	(2,272)	1,691	5,524
At 31st December 2010	14,264	(4,097)	13,698	23,865
Company				
At 1st January 2010	26,576	(6,535)	49,067	69,108
Adjustment due to exchange movements	1,698	(139)	2,294	3,853
Movement during the year	1,114	(2,215)	(5,040)	(6,141)
At 31st December 2010	29,388	(8,889)	46,321	66,820

19. Debtors arising out of direct insurance operations

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Amounts owed by policyholders	17,903	17,510	17,750	17,294
Amounts owed by intermediaries	192	137	192	137
	18,095	17,647	17,942	17,431

20. Debtors arising out of reinsurance operations

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Debtors arising out of inward reinsurance operations	265	804	265	804
Debtors arising out of outward reinsurance operations	5,649	1,530	5,649	1,497
	5,914	2,334	5,914	2,301

21. Other debtors

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Corporation tax	-	102	-	102
Other taxation	198	101	89	81
Other debtors	1,304	1,860	584	610
Deferred taxation (note 26)	520	306	457	255
	2,022	2,369	1,130	1,048

22. Tangible fixed assets

	Fixtures & fittings £'000	Motor vehicles £'000	Computers £'000	Total £'000
Group				
Cost				
At 1st January 2010	823	332	740	1,895
Adjustment due to exchange movements	8	19	19	46
Additions	47	219	789	1,055
Disposals	-	(173)	(42)	(215)
At 31st December 2010	878	397	1,506	2,781
Depreciation				
At 1st January 2010	503	150	631	1,284
Adjustment due to exchange movements	7	9	16	32
Charge for the year	102	59	93	254
On disposals	-	(115)	(40)	(155)
At 31st December 2010	612	103	700	1,415
Net book value				
At 31st December 2010	266	294	806	1,366
At 31st December 2009	320	182	109	611

22. Tangible fixed assets (continued)

	Fixtures & fittings £'000	Motor vehicles £'000	Computers £'000	Total £'000
Company				
Cost				
At 1st January 2010	357	85	103	545
Adjustments due to exchange movements	(2)	22	(7)	13
Additions	40	100	766	906
Disposals	-	(42)	-	(42)
At 31st December 2010	395	165	862	1,422
Depreciation				
At 1st January 2010	70	2	31	103
Adjustments due to exchange movements	(3)	9	(9)	(3)
Charge for the year	94	29	71	194
Disposals	-	(10)	-	(10)
At 31st December 2010	161	30	93	284
Net book value				
At 31st December 2010	234	135	769	1,138
At 31st December 2009	287	83	72	442

23. Capital and reserves

			Income & expenditure account		
	Revaluation reserve £'000	Reserve fund £'000	Translation reserve £'000	I&E reserve £'000	Total £'000
Group					
At 1st January 2010	335	26,007	2	17,320	17,322
Surplus for year	-	-	-	2,448	2,448
Foreign exchange rate movements	26	-	32	-	32
Actuarial surplus recognised in pension scheme	-	-	-	21	21
Revaluation of property	(161)	-	-	-	-
At 31st December 2010	200	26,007	34	19,789	19,823

23. Capital and reserves (continued)

	Revaluation reserve £'000	Reserve fund £'000	Income & expenditure account Translation reserve £'000	I&E reserve £'000	Total £'000
Company					
At 1st January 2010	17,402	26,007	(535)	647	112
Deficit for year	-	-	-	(260)	(260)
Revaluation of subsidiaries	2,831	-	-	-	-
Revaluation of property	(161)	-	-	-	-
Foreign exchange rate movements	129	-	(83)	-	(83)
Actuarial surplus recognised in pension scheme	-	-	-	21	21
At 31st December 2010	20,201	26,007	(618)	408	(210)

24. Reconciliation of movements on capital and reserves

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
At 1st January	43,664	40,977	43,521	41,939
Surplus/(deficit) for year	2,448	4,346	(260)	(1,917)
Revaluation of property	(161)	-	(161)	-
Revaluation of subsidiaries	-	-	2,831	4,921
Foreign exchange rate movements	58	(188)	46	(284)
Actuarial surplus/(deficit) recognised in pension scheme	21	(1,471)	21	(1,138)
At 31st December	46,030	43,664	45,998	43,521

25. Technical provisions – gross amounts

	Provision for unearned premiums £'000	Claims outstanding £'000	Total £'000
Group			
At 1st January 2010	31,879	54,438	86,317
Adjustment due to exchange movements	2,057	2,443	4,500
Movement during the year	(1,826)	(5,936)	(7,762)
At 31st December 2010	32,110	50,945	83,055
Company			
At 1st January 2010	31,189	54,259	85,448
Adjustment due to exchange movements	1,950	2,389	4,339
Movement during the year	(1,800)	(5,931)	(7,731)
At 31st December 2010	31,339	50,717	82,056

26. Provision for deferred tax assets

The provision for deferred tax assets has been made at the rate of tax relevant in each overseas jurisdiction as follows

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
At 1st January	306	215	255	(17)
Adjustment due to exchange movements	101	57	92	45
Adjusted provision at 1st January	407	272	347	28
Transfer on group restructure	-	-	-	29
Movement during year	113	34	110	198
At 31st December	520	306	457	255
Excess of taxation allowances over depreciation on fixed assets	(5)	(351)	(27)	(316)
Other timing differences	525	657	484	571
	520	306	457	255

27. Derivative liabilities

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Derivatives at fair value through income	227	343	182	306

The fair value of the derivative financial instruments is based on their listed market price

28. Creditors arising out of reinsurance operations

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Amounts owing to subsidiary undertakings	-	-	14,598	14,626
Other creditors arising out of reinsurance operations	8,350	2,786	8,350	2,786
	8,350	2,786	22,948	17,412

29. Creditors - borrowings

Creditors include finance capital which is due for repayment as follows

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Bank overdraft	6,148	5,216	6,148	5,216
Bank loans	607	1,149	-	-
	6,755	6,365	6,148	5,216
Amounts repayable:				
In one year or less or on demand	6,603	5,676	6,148	5,216
In more than one year but not more than five years	152	689	-	-
	6,755	6,365	6,148	5,216

Group borrowings are secured by guarantee provided by the company and a subsidiary undertaking Interest is charged at 2 1% above base rate on the overdraft and 2 25% above Libor on the loans Interest charged during the year on the loans was £36,000 (2009 £151,000) and on the overdraft £214,000 (2009 £201,000)

30. Other creditors including taxation and social security

	Group 2010 £'000	Group 2009 £'000	Company 2010 £'000	Company 2009 £'000
Corporation tax	76	-	76	-
Other taxes and social security	950	537	919	573
Other creditors	1,805	2,086	385	4,846
	2,831	2,623	1,380	5,419

31. Financial assets and liabilities

Group At 31st December 2010	Fair value through income £'000	Loans and receivables £'000	Amortised cost £'000	Total carrying value £'000	Total fair value £'000
Financial assets					
Equity securities at fair value through income	4,097	-	-	4,097	4,097
Debt securities at fair value through income	64,130	-	-	64,130	64,130
Derivatives	348	-	-	348	348
Deposits with credit institutions	-	9,521	-	9,521	9,521
Debtors arising out of direct insurance operations	-	18,095	-	18,095	18,095
Debtors arising out of reinsurance operations	-	5,914	-	5,914	5,914
Other debtors	-	2,022	-	2,022	2,022
Cash and cash equivalents	-	2,637	-	2,637	2,637
At 31st December 2010	68,575	38,189	-	106,764	106,764
Financial liabilities					
Derivatives	(227)	-	-	(227)	(227)
Creditors arising out of direct insurance operations	-	-	(1,984)	(1,984)	(1,984)
Creditors arising out of reinsurance operations	-	-	(8,350)	(8,350)	(8,350)
Borrowings	-	-	(6,755)	(6,755)	(6,755)
Other creditors, including taxation and social security	-	-	(2,831)	(2,831)	(2,831)
At 31st December 2010	(227)	-	(19,920)	(20,147)	(20,147)

31. Financial assets and liabilities (continued)

At 31st December 2009	Fair value through income £'000	Loans and receivables £'000	Amortised cost £'000	Total carrying value £'000	Total fair value £'000
Financial assets					
Equity securities at fair value through income	3,842	-	-	3,842	3,842
Debt securities at fair value through income	63,687	-	-	63,687	63,687
Derivatives	402	-	-	402	402
Deposits with credit institutions	-	11,862	-	11,862	11,862
Debtors arising out of direct insurance operations	-	17,647	-	17,647	17,647
Debtors arising out of reinsurance operations	-	2,334	-	2,334	2,334
Other debtors	-	2,369	-	2,369	2,369
Cash and cash equivalents	-	5,912	-	5,912	5,912
At 31st December 2009	67,931	40,124	-	108,055	108,055
Financial liabilities					
Derivatives	(343)	-	-	(343)	(343)
Creditors arising out of direct insurance operations	-	-	(1,915)	(1,915)	(1,915)
Creditors arising out of reinsurance operations	-	-	(2,786)	(2,786)	(2,786)
Borrowings	-	-	(6,365)	(6,365)	(6,365)
Other creditors, including taxation and social security	-	-	(2,623)	(2,623)	(2,623)
At 31st December 2009	(343)	-	(13,689)	(14,032)	(14,032)

32. Reconciliation of surplus on ordinary activities before taxation to net cash outflow from operating activities

	2010 £'000	2009 £'000
Surplus on ordinary activities before taxation	2,976	5,084
Share of profit of joint ventures	(3)	(199)
Amortisation of goodwill	1,335	854
Depreciation	403	414
(Profit)/loss on sale of fixed assets	(2)	3
Derivative charge/(income)	586	(1,903)
(Gain)/loss on sale of liquid investments	(976)	2,747
Adjustment to carrying value of liquid investments	31	(4,214)
Foreign exchange rate fluctuation	(2,907)	(576)
Tax suffered on investment income	(464)	(430)
Bank interest charge	250	352
Property revaluation through income and expenditure account	215	-
Pension contributions in excess of expense in income and expenditure account	(348)	(1,271)
Increase in reinsurers' share of technical provisions	(6,851)	(4,429)
(Increase)/decrease in debtors	(3,569)	3,174
Decrease in prepayments and accrued income	493	517
Decrease in technical provisions	(3,262)	(1,460)
Increase/(decrease) in creditors	5,765	(1,123)
(Decrease)/increase in accruals and deferred income	(817)	591
Net cash outflow from operating activities	(7,145)	(1,869)

33. Movement in cash, portfolio investments and financing

	Deposits & cash at bank net of overdraft £'000	Ordinary shares £'000	Fixed income securities £'000	Land and buildings £'000	Loans £'000	Total £'000
At 1st January 2010	12,558	3,842	63,687	8,791	(1,149)	87,729
Cash flow	(7,639)	(29)	(1,658)	-	555	(8,771)
Changes to market value and currencies	1,091	284	2,101	(208)	(13)	3,255
At 31st December 2010	6,010	4,097	64,130	8,583	(607)	82,213

34. Commitments under operating leases

At 31st December the group had annual commitments under non-cancellable operating leases as set out below

	2010 Land & buildings £'000	2010 Other items £'000	2009 Land & buildings £'000	2009 Other items £'000
Group				
Operating leases which expire				
Within one year	36	37	56	9
Within two to five years	123	133	69	160
Over five years	35	-	-	-
	194	170	125	169

35. Pension commitments

Group

Defined benefit pension scheme

Salvus Bain (Management) Limited operated a defined benefit pension scheme in the United Kingdom, the Salvus Bain (Management) Limited Pension Scheme until 30th June 2009 The scheme was transferred to Sunderland Marine Mutual Insurance Company Limited on this date. The information disclosed below is in respect of the only plan for which Sunderland Marine Mutual Company Limited is the sponsoring employer

	2010 £'000	2009 £'000
Present value of funded defined benefit obligations	(21,103)	(18,257)
Fair value of plan assets	20,209	16,994
Deficit	(894)	(1,263)

35. Pension commitments (continued)

Movements in present value of defined benefit obligation

	2010 £'000	2009 £'000
At 1st January	18,257	13,202
Current service cost	671	458
Interest cost	1,060	884
Actuarial losses	1,090	3,736
Benefits paid	(139)	(188)
Contributions by members	164	165
At 31st December	21,103	18,257

Movements in fair value of plan assets

	2010 £'000	2009 £'000
At 1st January	16,994	12,139
Expected return on plan assets	1,050	854
Actuarial gains	1,111	2,265
Contributions by employer	1,029	1,759
Contributions by members	164	165
Benefits paid	(139)	(188)
At 31st December	20,209	16,994

Expense recognised in the income and expenditure account

	2010 £'000	2009 £'000
Current service cost	671	458
Interest on defined benefit pension plan obligation	1,060	884
Expected return on defined benefit pension plan assets	(1,050)	(854)
Total	681	488

35. Pension commitments (continued)

The expense is recognised in the following line items in the income and expenditure account:

	2010 £'000	2009 £'000
Net operating expenses	671	458
Investment losses	10	30
	681	488

The total amount recognised in the statement of total recognised gains and losses in respect of actuarial gains is £21,000 (2009 losses £1,471,000)

The fair value of the plan assets and the return on those assets were as follows

	2010 Fair value £'000	2009 Fair value £'000
Equities	8,716	11,000
Bonds	9,783	4,625
Property	35	14
Hedge fund of funds	1,126	870
Cash	549	485
	20,209	16,994
Actual return on plan assets	2,206	2,520

The expected rates of return on plan assets are determined by considering the expected return on each individual asset class The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the plan's investment portfolio

35. Pension commitments (continued)

Principal actuarial assumptions (expressed as weighted averages) at the year end were as follows

	2010 %	2009 %
Discount rate	5 5	5 7
Expected rate of return on plan assets	6 0	6 0
Expected return on plan assets at beginning of the period	6 0	6 5
Future salary increases	3 75	3 6
Inflation	3 50	3 6
Mortality	PA92mc	PA92mc

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date are based on standard actuarial mortality tables and include an allowance for future improvements in longevity The assumptions are equivalent to expecting a current pensioner aged 63 years old to live for 24 years (male) and 27 years (female)

History of plan

The history of the plan for the current and prior periods is as follows The company has chosen not to restate the corresponding amounts for the first two of the previous four accounting periods for the effect of using the current bid-price rather than the mid-market price

Balance sheet	2010 £'000	2009 £'000	2008 £'000	2007 £'000	2006 £'000
Present value of scheme liabilities	(21,103)	(18,257)	(13,202)	(15,077)	(13,814)
Fair value of scheme assets	20,209	16,994	12,139	12,854	11,468
Deficit	(894)	(1,263)	(1,063)	(2,223)	(2,346)

	2010 %	2009 %	2008 %	2007 %	2006 %
Experience adjustments on scheme liabilities as a percentage of scheme liabilities	(5 2)	(20 7)	25 1	(1 8)	(10 0)
Experience adjustments on scheme assets as a percentage of scheme assets	5 5	13.4	(31 6)	4 4	5 6

The company expects to contribute approximately £953,000 to its defined benefit plan in the next financial year

35. Pension commitments (continued)

The company contributed £159,000 (2009 £180,000) to the pension scheme for administration fees, audit fees and members' life assurance premiums

Defined contribution pension schemes

The group also operates a number of defined contribution pension schemes. The total pension cost charge for the year represents contributions payable to the schemes and amounted to £170,000 (2009 £206,000) There were no outstanding or prepaid contributions at either the beginning or the end of the financial year Contributions of £61,000 (2009 £50,000) were also made to a government superannuation scheme

Company

On 30th June 2009 the defined benefit pension scheme was transferred from Salvus Bain (Management) Limited to Sunderland Marine Mutual Insurance Company Limited The scheme liability at this date was £535,000.

On 30th June 2009 the defined contribution pension scheme operated by Salvus Bain (Management) Limited was also transferred to Sunderland Marine Mutual Insurance Company Limited

36. Guarantees

SM Insurance (Bermuda) Limited has a guarantee in favour of Barclays Bank Plc to enable Sunderland Marine Mutual Insurance Company Limited to enter into commercial borrowing with Barclays Bank Plc for a sum of up to £25,000,000 At 31st December 2010 the amount owing on the facility was £6,148,000, representing the charge over the assets that Barclays Bank Plc has on SM Insurance (Bermuda) Limited

The company had a guarantee in favour of Barclays Bank Plc to enable its subsidiary undertakings to enter into commercial loans with the bank At 31st December the amount owing was £607,000

The company has a guarantee in favour of its subsidiary company Sunderland Marine (Africa) Limited The guarantee provides comfort to the policyholders of Sunderland Marine (Africa) Limited as the company will stand as a guarantor for the first South African R3,000,000 of any claim